What Makes a Great Boss...page 70 A Hidden Brain Drain...page 43

Harvard Business Review

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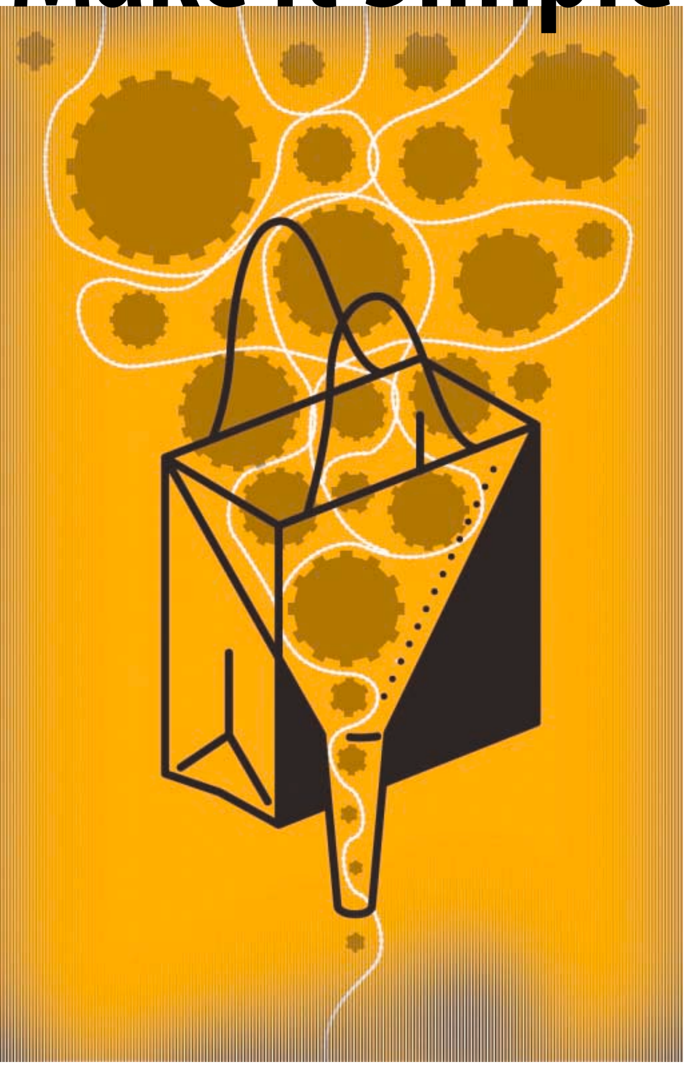
March 2005

Make It Simple



...page 58

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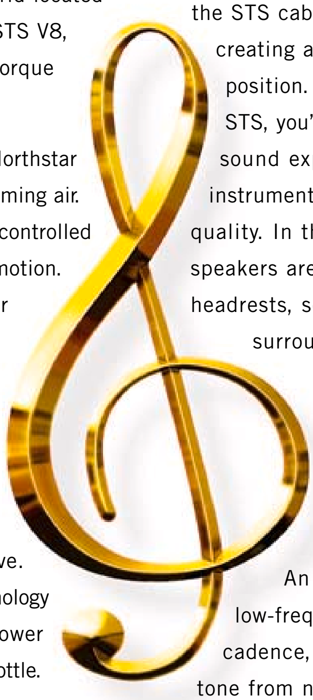

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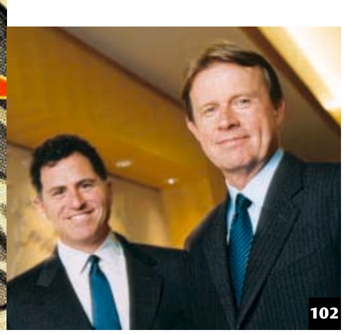
FEATURES

March 2005

continued on page 6



COVER ART: JOHN HERSEY

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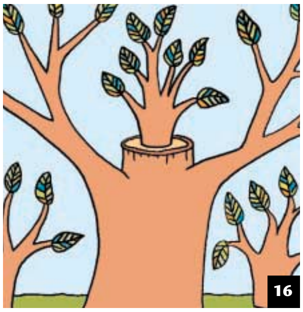
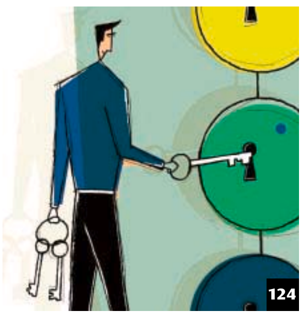
HBR

Departments

March 2005



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The Ideas of March

ALMOST EVERY BUSINESS is like a woven fabric, its people the weavers. They begin by setting up a vertical warp of functions – procurement, manufacturing, distribution, sales, finance, and so on. Across them they weave processes, such as product development, order generation and fulfillment, and supply chain management.

Much of the progress in management in the last two decades has come from paying attention to the weft of processes. In that field, no one has had more to say than James Womack and Daniel Jones. Their 1990 book *The Machine That Changed the World* (cowritten with Daniel Roos) described the process-oriented principles of lean manufacturing that undergird Toyota's production system. Since then, the work of their Lean Enterprise Institute has deepened their understanding of lean production and extended its influence in business.

Get ready for the lean revolution, part deux.

"Consumption is a process, too," Womack said to me one evening at the Charles Hotel in Cambridge. As we consumed drinks, he and Jones outlined the thinking behind this month's lead article: The brainpower that businesses bring to bear to eliminate wasted assets, materials, and time in *production* should equally be deployed to improve the processes of *consumption* that customers follow. Like their earlier work, this is both a landmark synthesis of ideas whose implications haven't been fully understood and a breakthrough to new territory. Telling what lean consumption means, then showing the results at the handful of companies that have grasped its significance, Womack and Jones offer HBR readers an exclusive first look at an idea whose impact is likely to be enormous.

And what of the weavers, the people? I'd like to highlight a pair of important articles in this issue. One is Marcus Buckingham's "What Great Managers Do." Just as every one of us had a great teacher in school, so we've all had – or I hope will have – a great boss. Maybe she wasn't a great strategist, maybe he wasn't the most technically skilled – but he or she got better performance out of you than anyone ever had. You remember a boss like that with an emotion not unlike love. But how do great managers do it?

There's an enormous literature on managerial tasks like hiring, motivating, developing, and rewarding – and much discussion of the difference between management and leadership. But Buckingham – the former Gallup Organization researcher who is coauthor of *First, Break All the Rules* – takes a different tack, looking deeply into how great bosses interact with their direct reports. What he found is fascinating. Effective leaders, for the most part, capitalize on the dreams and fears that people hold in common; many human resource policies similarly seek to establish common practices in the laudable pursuit of fairness. Great managers, though, seek out uniqueness. They figure out what *you* do well and what makes *you* tick. Rather than obscure differences, they develop them. It's a powerful insight; understanding it will make you better at both managing and leading.

"Off-Ramps and On-Ramps" by Sylvia Ann Hewlett and Carolyn Buck Luce shines the light of research onto a frustratingly intractable problem. Too many highly qualified women drop out of mainstream careers. If they take a break – to bear children, for example – they often find they cannot get back into the workforce even if they want to. ("It's the pause that represses," senior editor Julia Kirby says.) This article is the first fruit of a multiyear investigation of why talented women and minorities don't fully use the skills they have learned. (A longer research report is available at www.womenscareersreport.hbr.org.) The problem is no longer sexism among male executives – though that persists, of course. Working with survey data and detailed case studies of companies and industries, Hewlett and Buck Luce have identified structures and mechanisms that keep the hidden brain drain operating despite everyone's best intentions. They have also found companies that have made tremendous progress – and profited immensely – from fixing the problem.

Thomas A. Stewart

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VOLUME 83, NUMBER 3
MARCH 2005
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forethought

A survey of ideas, trends, people, and practices on the business horizon.

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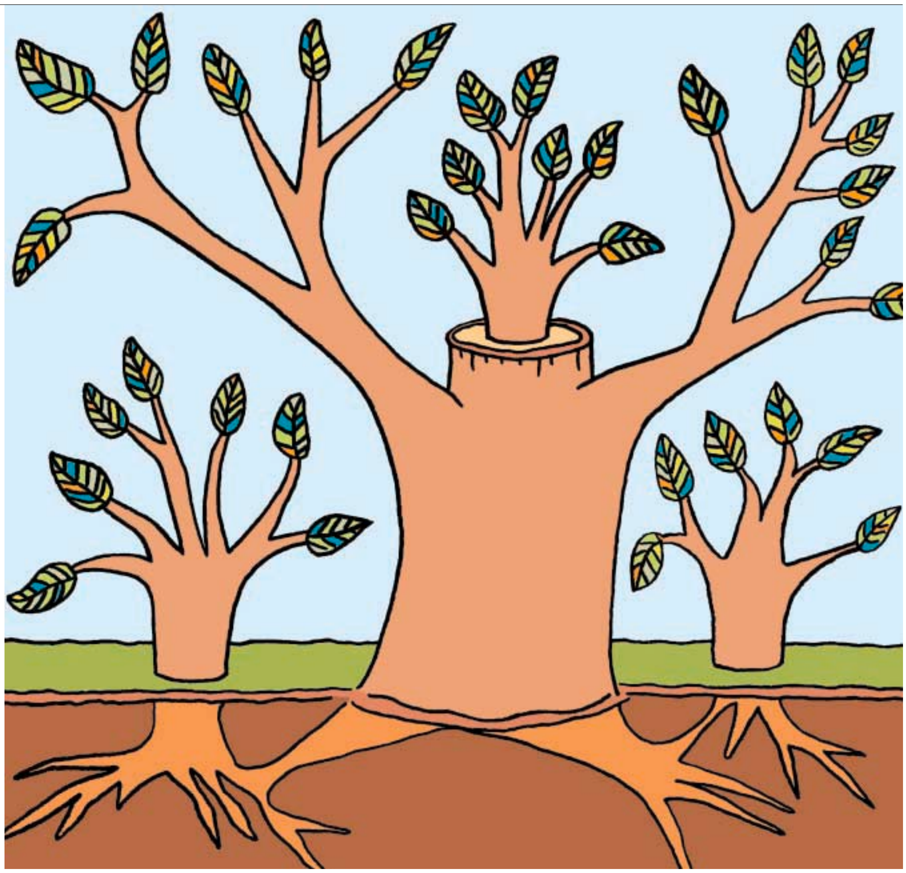


FRANKLIN HAMMOND

GRIST

Sorting Data to Suit Yourself

by DAVID WEINBERGER

The Bettmann Archive of 11 million photographs is kept secure in a limestone quarry 220 feet below the earth. The front room – a painted cavern – holds a couple of offices, scanning equipment, and, most important, the card catalog. In the back room, filing cabinets filled with photos stretch to the vanishing point.

The Bettmann's layout embodies the two basic orders of organization that have dominated our thinking for thousands of years. The back room represents *first-order* organization: the sorting and arrangement of objects themselves. The front room represents *second-order* organization: information about information (metadata), which is sorted in a different way. We encounter this dual structure in libraries, warehouses – even when catalog shopping. In the physical realm, it works. But as we digitize the world's information, a third order of organization is emerging that's undoing many of our old assumptions.

In the digital age, we are coming to realize how much of what we do is shaped by the limitations of the physical world. No physical object can be in two places at once – so we classify and file documents based on the assumption that objects can go into one bucket only, with exceptions for the occasional cross-reference. But we can file each electronic object into dozens, or even hundreds, of buckets. That means traditional tree structures – organization charts, the Dewey decimal system, some knowledge management concept trees – are ill suited to the task of organizing digital information.

Not only do traditional tree structures assume that objects hang from just one branch, they also value neatness and include exceptions only when they have to, flagging them with dotted lines. By contrast, lots of messy links enhances the value of digital information, providing context and guiding people to unexpected destinations. While the Dewey decimal system places books on related topics near one another, helping you find additional relevant volumes, messy webs of information awaken you to the far-flung, serendipitous connections made by bright (and not so bright) minds before you, spurring your own innovation.

The biggest change wrought by the third order, however, is that owners of information (such as companies) no longer own the organization of that information. Users (such as employees and customers) can sort and organize information in any way that suits their needs. All over the Web, customers are getting used to sorting through long lists of products based on criteria that are important to them rather than browsing along a tree that some marketing person thought would be right for everyone.

Accordingly, the rise of third-order organization changes the jobs of corporate information architects and knowledge managers. Their role is no longer to build trees that define the relationship of every bit of data in a company but to build enriched pools of data objects whose relationships to one another change constantly, depending on who is looking at them. For example, the uBio project, sponsored by the Woods Hole Oceanographic Institution, is creating a pool of information objects related to species. A marine biologist may assemble these classifications based on physical characteristics or gene sequence information. A restaurateur could sort fish and shellfish according to seasonal location and price. The same data pool allows for both.

Within companies, employees are using third-order schemes to manage information about complex products that are frequently reused or recombined into new offerings. The British Broadcasting Corporation, for example, packages and distributes television and radio programs, movies, music, and Web sites created by producers all over the world, often combining them into new products. Each media type is described by different metadata;

ECONOMICS

Both Sides Now *by* STEVE HANNAFORD

You've heard the term *oligopoly* – a market with a small number of sellers. An *oligopsony* may be less familiar – that's a market with few buyers. For example, if you raise cocoa beans anywhere in the world, you can sell to Cargill or ADM, and that's about it. To get your movie into the cineplexes, you must talk to the four or five companies that own almost all the screens in North America. And if you make aircraft parts, your salespeople had better get into Boeing, Lockheed Martin, and just a handful of other companies that assemble planes.

But what happens when a company is in both an oligopoly and an oligopsony? It's an increasingly common situation, and one for which I've coined the term *oligonomy.* Oligonomies have unique power in both retail and B2B markets. The most notorious oligonomy player is Wal-Mart.

Economists have traditionally focused on the power of oligopolies to set high prices, whether through collusion or silent agreement. But Wal-Mart uses its market power to set low prices. Suppliers are so dependent on oligonomies that they have to eat their own margins to stay in business. There's always another supplier – whether a Nebraska-based service center, a Chinese furniture maker, or a Brazilian farmer – that can lower prices further.

Most M&As of the past decade have aimed at building oligonomies, which are well protected from the extremes of business cycles since they can adjust costs as well as prices. Not so for the small and midsize businesses that supply and service these behemoths. Those companies have just three options. They can get bigger themselves, either by acquiring or by being acquired. They can become indispensable by means of patents, copyrights, or unique expertise. Or they can try to bypass the oligonomies entirely by selling directly to customers over the Web.

As industries from steel to hotels to toys concentrate further, most businesses will at some point feel the hot breath of an oligonomy on their necks. How they deal with that threat will determine whether they survive. Reprint F0503B television programs, for example, might be broken down by scenes, articles by sections. The BBC is turning this vast assemblage of content into a pool of objects that users can sort, classify, and combine differently for each new project. That should greatly reduce the cost and labor of creating and delivering complex, integrated products.

The third order is not without dangers. Companies lose yet another instrument of control over their customers. And if everyone creates organizational structures that reflect their immediate needs and individual ways of thinking, integrating information from dueling structures could get tough. But the benefits of letting users order their own data are compelling. Enabling customers to organize *your* information the way that works for *them* is a cool benefit today but will be a necessity tomorrow. Reprint F0503A

HEADQUARTERS

Rotate the Core

by GEORGE STALK, JR.

Unit managers tend to regard headquarters as a nuisance:

"What does Corporate want now?"
"The center is where dinosaurs go to die."
"Look out when you hear, 'We're from Corporate, and we're here to help.'"

Indeed, since the 1980s, the trend has been toward reducing headquarters, both in size and influence over the business units. The driving logic of this *minimalist center* is cost containment. Push as much cost into the businesses as possible. Then get rid of all remaining costs except those needed for corporate governance and a few essential shared services, set the right objectives, measures, and rewards – and get out of the way.

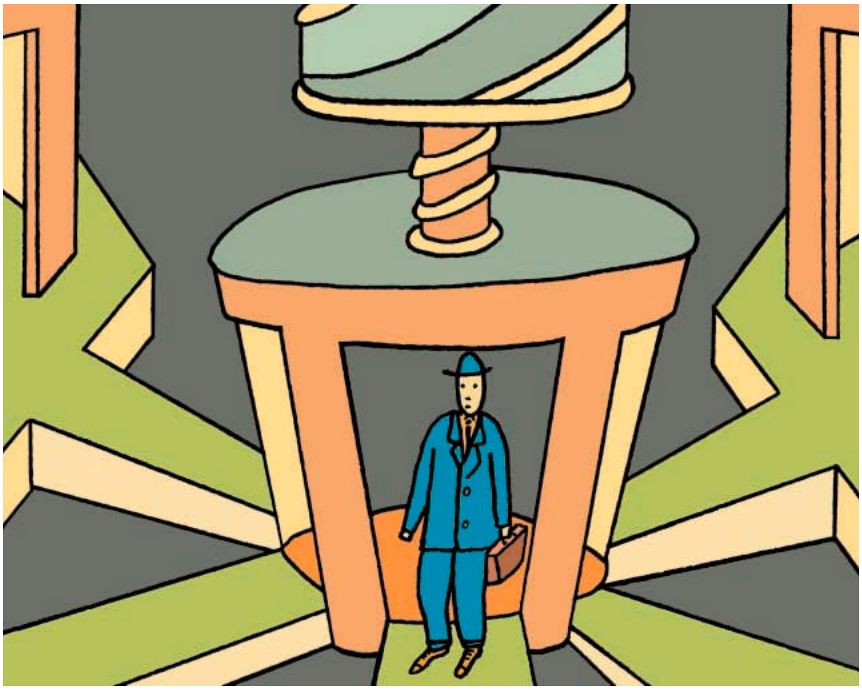
Engineering a minimalist center may be an effective cost-cutting strategy, but it's an overreaction to the once-predominant *imperialist center,* where hordes of staffers peer over the shoulders of line managers. Done wrong – as it often is – the minimalist center eliminates opportunities for headquarters to actually enhance the units' performance by ensuring that they make needed investments in talent and in their own businesses.

What's the alternative? A lean, *activist center.* Some of today's most respected organizations – companies like General Electric, PepsiCo, and Hitachi – make lean but influential centers a keystone of their managerial practice. The very trends that seem to call for a hands-off center – fragmenting markets, rapidly changing technologies, faster innovation cycles – sometimes require the opposite: a corporate center that engages the reflexively autonomous business units. Naturally, the units tend to focus on their own industry, on their traditional competitors, and on meeting their numbers. As a result, they can miss and may even ignore broader market trends, new competitive threats, or game-changing opportunities. The activist center encourages, cajoles, and sometimes pushes line managers to take off the blinders, look outside established business unit boundaries, and preempt competitors.

Activist centers gain their clout by rotating executives with specific skills from the units into teams in headquarters, generally for two-year assignments. These teams comprise the company's most talented up-and-coming (or sometimes nearing-retirement) business unit executives. Only accomplished managers with extensive line experience have enough credibility to command the respect of senior line executives and, ultimately, persuade them to treat the center as a resource.

Instead of having a defined role, these teams focus their energies on a few key corporate priorities at a time. And rather than impose a process and an agenda on the units, the teams engage unit managers in a dialogue and in mutual efforts to effect change. At GE, Jeffrey Immelt uses the center, as Jack Welch did before him, to identify and drive major themes throughout the corporation, including "Be Number One or Number Two," "Six Sigma Quality," and, currently, "Growth." The themes, once they're endorsed by the business unit leaders, are executed within the businesses with the help of the small teams from headquarters, together with outsiders hired expressly for the purpose. Help can take many forms, such as assistance in accelerating product development or training Six Sigma black belts.

Team members are expected to achieve success during their brief tenure in a way that leads to their next assignments within the businesses. By actively managing the careers of these superior executives, headquarters ensures that the corporation develops leaders with



a breadth of experience and that business capabilities are transferred across the units.

Routinely cycling a few of your top people through headquarters may seem risky: Will the units suffer when you extract talent? Will these transplanted line executives become effective consultants to the businesses? Will there be a job for them when it's time to return to the businesses? But the costs of running a lean but less-engaged center – timid strategies, underleveraged capabilities, and underdeveloped talent – are riskier still.

Reprint F0503C

GLOBAL STRATEGY

Expanding in China

by ANN CHEN AND VIJAY VISHWANATH

You'd think that Danone, one of the globe's biggest makers of milk products, should have had an easy time entering the world's fastest-growing dairy market. But the French food conglomerate, which has been successfully selling biscuits and mineral water in China, flopped with its dairy offerings. In 2002, after a decade of effort and an investment of more than $10 million, it withdrew its dairy products from the Chinese market and sold its facilities to domestic competitors.

Danone is not the only foreign company whose efforts have gone sour in China. Major multinationals – from Unilever to Carlsberg to Quaker Oats – have also struggled to make headway there. The problem isn't their products. Nor is it a Chinese aversion to foreign brands. And it's certainly not the companies' starting point; almost all foreign brands aim first at the premium segment. Rather, it's their approach to broadening market share.

A handful of multinationals – Colgate, Coca-Cola, and Anheuser-Busch among them – point to a better path. Through a careful combination of pricing, positioning, distribution, and acquisition, they've managed to turn a toehold in China's premium segments into a rapidly expanding market. They use three key strategies.

Close the cost gap. The first step is to manage costs. Chinese consumers no

Opinion

No More Metaphors

A few years ago, I set out to compile an A-to-Z roster of business metaphors. In less than two weeks, I had all 26 entries, starting with "Antarctica" (*Shackleton's Way: Leadership Lessons from the Great Antarctic Explorer*) and ending with "Zeus" (*Gods of Management: The Changing Work of Organizations*). In between came books or articles comparing business to, among other subjects, *Star Trek,* organized crime, *The Wizard of Oz,* yachting, fairy tales, and – my favorite – geese. (I largely eschewed the many, many works on war and sports. Fish in a barrel, I figured.) A few of the books were pretty good. More seemed to exist not because the author had something genuinely different to say but because he or she had found a slightly different way of saying something.

Now, I'm actually pretty fond of metaphors. I recognize their role in education and – as the good people at the Boston Consulting Group persuasively argue – in innovation. But I wonder whether the obsession with metaphors devalues management as a field. After all, the more something is like other things (and the more other things it is like), the less it is distinctly itself. In addition, metaphors are never better than approximations. Are jazz combos really the best models for spontaneous collaboration in engineering teams, considering how dramatically different their personalities, time frames, and deliverables are?

Other fields thrive within their own frames of reference. This is, in part, a triumph of language. The sciences have their own highly specific vocabularies, which are coupled to highly specific sets of ideas. (Physics is particularly plummy: think antimatter, entropy, quarks.) The same is true of cooking. Scan the first hundred cookbooks on Amazon, and you won't stumble across a single metaphor-themed entry. (I don't count *The Cake Mix Doctor* or *The Wine Bible,* which beyond their titles make no reference to medicine or religion, respectively.) A similar tour of business books turns up management lessons from dog training, Renaissance art patronage, the U.S. Navy, fish markets, and – not surprisingly – physics.

One – admittedly nontraditional – indication of a discipline's conceptual fertility is its ability to spawn new language. New words emerge where there are new ideas, and where there are new ideas *something is happening.* Internet culture and commerce rapidly produced a large, distinctive vocabulary for their many distinctive concepts. Some of that language is coinage: spot-on terms like "dot-com" and "click stream" sprang up without antecedents. And some of that language ("portal," "surfing") is metaphor – but metaphor that draws more power from the new meaning than from the old. (When was the last time you said "spam" and meant lunch meat?) Creative language, almost as much as creative technology, keeps the Internet revolution alive in the public mind.

The best books about business management are about business management, and there is plenty of smart, original work in that area. But the vocabulary has grown stale, the imagery dull. That is no invitation to concoct words for novelty's sake. Management authors should seek to express their ideas in language that is inventive, precise, and organic to the subject. Managers, meanwhile, should spend less time peering through the scrim of others' disciplines and more time pioneering those practices that will confer a unique identity on their own. – Leigh Buchanan

Reprint F0503E

longer will shell out 70% to 100% premiums for foreign products. At most, they may pay 20% to 30% more for world-class brands. Parmalat (which has been in the news for other reasons) discovered this when it tried to sell fruit-flavored yogurt for 24 cents a cup; consumers stuck with local brands at half the price.

But companies using local suppliers can close the cost gap. Colgate became China's top oral care company, in large part by cutting production costs and passing those savings on to consumers. After arriving in 1991, it began manufacturing its toothpaste in China, eventually sourcing the ingredients locally. The result: The price of a 65-gram tube of toothpaste dropped almost 63% from 4.8 renminbi in 1996 to 1.8 renminbi in 2003 (or from about 59 cents to 22 cents). The price differential between Colgate and local brands fell even more dramatically – from 270% to just 44%.

Add products and channels. It makes sense for most foreign brands, because of their cost structures, to start at the top, as Colgate did. But it's crucial to break into the mass market quickly. Quaker Oats

learned this the hard way when, before it became part of PepsiCo, it introduced Gatorade to China in 1995. The sports drink didn't catch on. Though Quaker Oats lowered the price by 10% to 15% in the late 1990s, Gatorade was still expensive by local standards. Worse, it was sold in only a few large cities.

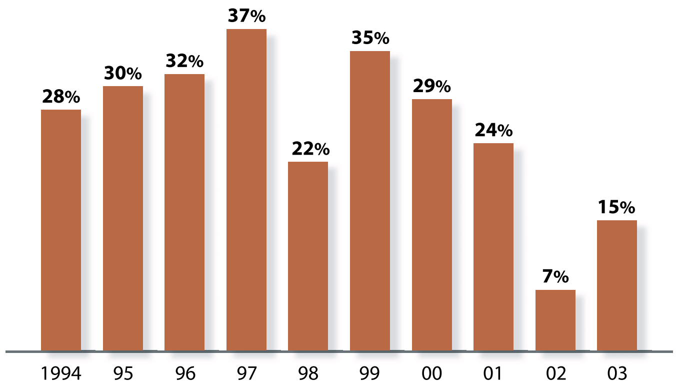
Back in 1979, Coca-Cola also began by offering its high-profile (and pricey) soft drink. Like Gatorade, Coke captured just

Data Point

Global Manufacturers at a Crossroads

by PETER KOUDAL

Fact The percentage of foreign direct investment by U.S. global manufacturers into fast-growing, low-wage economies decreased 57% between 1999 and 2003.



Conventional wisdom holds that multinationals increase their foreign direct investment as opportunities arise in low-cost, emerging markets. But a Deloitte Research study of global investment by U.S. manufacturers finds the opposite: In industries ranging from chemicals to computers to transportation equipment, U.S. manufacturing FDI *decreased* from $12 billion in 1999 to $4 billion in 2003. Today, such investments capture less than 15% of total U.S. FDI, compared with nearly 30% in 1994.

This trend has troubling implications for the competitiveness of U.S. manufacturing multinationals. Rather than establishing or acquiring their own assets, including plants, equipment, distribution facilities, and office buildings, companies increasingly appear to be using arm's-length contractual means – such as through outsourcing – to engineer, manufacture, and sell in these markets. However, as the hub of global manufacturing activity moves toward low-wage nations such as China and India, innovation in technology, products, and processes will move as well.

An asset-light investment strategy for low-wage economies may seem attractive to manufacturers seeking to increase their short-term return on assets, minimize fixed costs, and increase flexibility. But holding back on direct investment may extract a high cost over the long term: It could diminish multinationals' ability to compete against the expanding number of manufacturers rooted in the dynamic low-cost markets where new technologies, consumption patterns, and business models emerge. By failing to take more direct control over a greater share of their sourcing, engineering, manufacturing, and marketing in low-wage, fast-growing economies, multinational manufacturers are, in effect, creating competitors on a massive scale.

Send Data Point chart proposals to **Edward E. Leamer** *(Leamer.HBRgraph@anderson.ucla.edu). Leamer is a professor of management, economics, and statistics at the University of California, Los Angeles, and the director of the UCLA Anderson Forecast.*

Reprint F0503F

a sliver of the market at first. But Coca-Cola reduced expenses by manufacturing locally, setting up 34 bottling plants and forming partnerships with three bottling groups to create a low-cost, efficient distribution network. With a bottling system that now covered 28 cities across the country, Coke was able to harness system economics to cut production, marketing, and distribution costs. Coca-Cola then added products, selling everything from Modern Tea Workshop herbal tea drinks to Coke Light. It now sells more than 20 different drinks for about 25 cents a can and 12 cents a returnable glass bottle, only slightly more than local brands. Even its marquee Coke brand sells for only 10% to 15% more than the most popular local brands. As a result, Coke sells more than half of all carbonated soft drinks in China and generated more than $2 billion in revenue in 2003.

Bring local brands on board. Perhaps the biggest barrier for most foreign companies is entrenched local competition. Beer makers are up against well-known and inexpensive local brands, as Australia's Foster's, Britain's Bass, and Denmark's Carlsberg learned the hard way. Ditto for dairy producers. China's "big six" dairy companies control well over half the local milk market.

The most successful multinationals are tackling China through a mix of global and local brands. In 2000, Colgate snapped up Jiangsu Sanxiao Group, the leading local player, to control the category. Anheuser-Busch, which leads the market for premium beer with its Budweiser brand, recently purchased a controlling stake in Harbin Brewery, China's fourth-largest brewer. The Harbin acquisition allows Anheuser-Busch to reach the masses, and – along with Anheuser-Busch's minority position in Tsingtao, China's number one brewery – consolidate its position in the market. Similarly, Gillette not only sells premium Duracell batteries but also Nanfu, a local brand it has acquired.

After failing to penetrate the Chinese market on its first try, Danone is now taking a cue from companies like Colgate and Gillette. It recently purchased a stake in Bright Dairy & Food, one of China's largest dairies. The move should improve Danone's cost structure and competitive position, giving it yet another chance to milk the world's fastest-growing dairy market.

Reprint F0503D

DEMOGRAPHICS

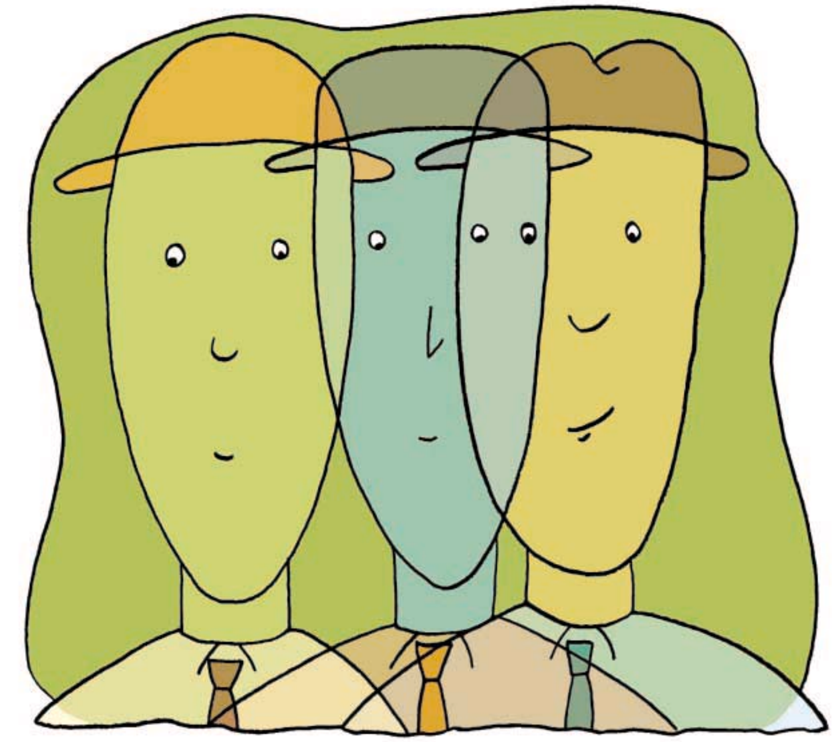
Vanishing Jobs? Blame the Boomers

by PHILLIP LONGMAN

To all the brouhaha over offshoring in America, one rejoinder is that any unemployment is temporary. When the mass of baby boomers starts retiring in the next few years, the argument goes, there will be plenty of work for anyone in the baby bust generation whose job went overseas. That may be a comforting thought for U.S. baby busters, but it's probably wrong. Despite their small numbers, the busters may paradoxically see unemployment get worse, not better.

Without a crystal ball, we can't say definitely what will happen as baby boomers start retiring. But we can find clues in two places. Japan's birthrate fell below replacement levels long before that of any other industrialized nation. As a result, workers have been a shrinking proportion of the country's population since 1989. Yet the jobless rate has actually gone up. Similarly, in the United States, the number of people between the ages of 15 and 24 has been declining in relative terms since 1990. But the smaller supply has not made younger workers more valuable; their unemployment rate has increased relative to that of their older counterparts. The situation is even worse for young men: Their median inflation-adjusted income in the booming economy of the late 1990s was actually below what the legions of young baby boomer men earned when they hit the workforce during the stagflation of the late 1970s. A similar story can be told about young workers in most European economies.

Why doesn't a declining labor supply bring more opportunities for those seeking jobs? First, an aging population often increases the cost of hiring. All those elder baby boomers are already helping to drive up the cost of employer-provided health care, and as they start to retire, payroll taxes will be likely to rise to make up for shortfalls in public health and pension



systems. Such a jump in taxes could discourage hiring in the United States, as it has in nations that have already experienced large jumps in their elderly populations, like Germany. Payroll taxes there exceed 40%.

Second, as their populations age, societies become more risk averse and resistant to change. One reason Japan is still struggling to fix its sclerotic banking system and France can barely raise its absurdly low retirement age is that older voters have nothing to gain, and much to lose, from fundamental changes that pay off only in the long term. The U.S. population may not be as old as those of other rich countries, but just look at how hard it is for Americans to face up to obvious threats to their country's long-term prosperity, such as the unsustainable cost of entitlement programs, looming future deficits, and overdependence on foreign energy sources. Studies worldwide also show that older populations are less likely to be entrepreneurial and so may create fewer new jobs.

Finally, businesses have other, potentially less costly, options besides replacing retirees with the next generation. They can move even more work offshore, and for those jobs that can't be sent overseas, they can lobby the government to allow more immigration. Or, as some hard-nosed firms are already doing, they can reduce their operations, either directly or by cutting plans for future investment. A shrinking workforce could give us merely a shrinking economy.

Reprint F0503G

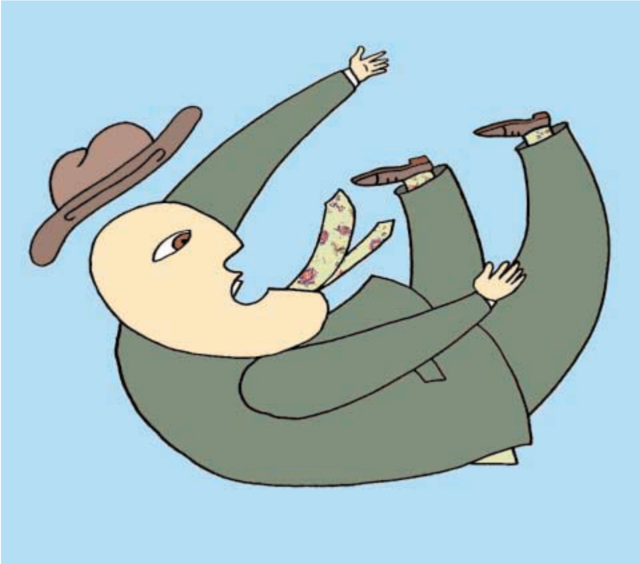
COMPETITION

The Faster They Fall

by S. PATRICK VIGUERIE AND CAROLINE THOMPSON

As the economy strengthens, industry leadership is more contestable and fleeting than ever. Globalization, changes in technology, and deregulation not only drive strong supply-side growth in the broader economy but also create new sources of supply, new competitors, a flood of new innovations (and knockoffs), and dramatically higher productivity.

Today's industry leaders will face increasing risk as growth emboldens attackers – many of whom will have lower costs, lower return requirements, or both.



We have powerful evidence that attackers have gained greater traction in recent decades. We analyzed industry leaders in 1,300 companies from 35 industries over some 30 years. The results were stark when we tracked the "topple rate" for the entire group of companies. That's the probability that a top company (a firm with revenues in the top 20% of its industry) will lose its revenue leadership position in the ensuing five years. Our data show that the rate doubled between 1972 and 2002.

Our analysis does not count companies that are acquired as topples. When these are taken into account, the rate has actually tripled. And the loss in revenue leadership is accompanied by an average 30% decline in profitability. Perhaps more important, toppled leaders are far more likely to exit their industry through acquisition or bankruptcy than those that sustain their position (no matter what quintile they're in); more than one-third of toppled companies no longer existed as independent companies after five years. That exit rate is twice as high as it is for leaders that are not toppled and a third higher than for the average company in the data sample.

Strikingly, many of the successful attackers that topple incumbents come abruptly (and unexpectedly) from far behind. Companies are traveling through the ranks about 40% faster than they did in the 1970s or 1980s, and the average new leader was in the middle of the pack just five years before ascending to the top quintile.

Why do companies topple? Each case is unique, but three factors figure most often: First, shifts in demand or superior offerings from competitors undercut the leader's value proposition. Second, competitors come along with acceptable substitutes or prices so much lower that the leader's productivity or cost position is undermined. Third, the leader makes some radically mistimed or otherwise unsuccessful big bets. Growth only exacerbates these strategic risks.

Growth, and the three supply-side forces that will help drive it over the next five to ten years, will almost certainly create a new generation of industry leaders. How well companies manage this risk – or capitalize on this opportunity – will determine which ones topple and which rise to the top.

Reprint F0503H

MARKETING

Outsourcing Marketing

by GAIL McGOVERN AND JOHN QUELCH

Companies have long outsourced creative, right-brain marketing activities, such as advertising and promotion campaigns. But a fundamental change is under way: Increasingly, firms are farming out marketing operations and analytics as well. A Forrester Research survey of 650 B2B marketing executives found that 53% aimed to outsource more than half their marketing activities in 2004. Forrester projects that CRM outsourcing in the United States will quadruple to $4.6 billion by 2008. And the British firm Astron Group forecasts that customer

continued on page 26

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Traditionally, supply chains have been viewed as a necessary evil. A cost to be contained. Which is why so many logistics managers have been given orders to just make them leaner and cheaper.
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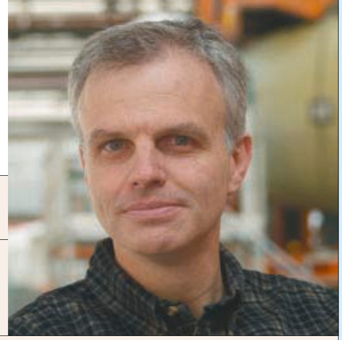
forethought

Conversation

DAVID NEELEMAN ON THE ORIGINS OF JETBLUE'S CULTURE

Lessons from the Slums of Brazil



JETBLUE AIRWAYS

In an industry plagued by bankruptcy, JetBlue Airways has grown revenues threefold during the four years since its launch. Smart cost containment is part of the story, but perhaps just as important is its down-to-earth culture, which inspires unusual customer and employee loyalty. Here JetBlue CEO and founder David Neeleman talks about the inspiration for the airline's culture and how it plays out day-to-day.

Where does JetBlue's egalitarian culture come from?
The way I live my life and run this company are colored by a couple of realizations I had more than 20 years ago. Throughout high school, I was an undistinguished student. So, after a year at the University of Utah, I decided to go on a mission for my church and ended up living and working in the favelas, or slums, of Brazil. My dad was a journalist. We lived in Brazil until I was five, and we visited during summers after that. Brazil was divided between haves and have-nots, and as I was growing up I saw only the rich part of the country – the part with the big houses and the country clubs. On my mission, though, I suddenly found myself on the other side of the barbed wire fence, with people who were desperately poor. It was the kind of place where, after you'd been out walking around all day, your shoes smelled like human feces.

Living in the favelas, a few things struck me. The first was that most wealthy people had a huge sense of entitlement. They thought they were better than the people in the slums – and this rubbed me the wrong way. The second was that the poor people I met seemed happier than the rich, and they were also incredibly generous in sharing what little they had. And the third – and most striking – thing was that I was actually much happier, too. Objectively, this made no sense. I was a young guy, far away from my family, only allowed to write letters home once a week and call home twice a year. In that situation, I should've been miserable. But I wasn't because I got enormous pleasure and satisfaction from my work.

When my time in Brazil was up, I went for my exit interview, and the interviewer said something I've never forgotten. "David," he told me, "when you go back to your life in the U.S., everything you do will be for you. You'll be in school for yourself, earning money for yourself, and so on. And you're never going to be as content as you were here unless you feel like you're serving – like you're helping other people." That nugget of wisdom was incredibly powerful: It resonated with me then, and it continues to resonate with me today.

How do you translate this worldview into action?
Two insights from that experience drive how I manage JetBlue: For myself and for the people I work with, I try to eliminate obvious differences in wealth and status, and I try to provide opportunities to serve others.

Let's say I go on a business trip. Lincoln Town Car? No, thanks – just give me the standard midsize rental. At JetBlue, we have no reserved parking, and the coffee in the kitchen down the hall from my work space is the same kind we have in the employee lounge out at Kennedy. We have only one class on our planes, and the seats that have more legroom are at the back, so the people who get off the plane last actually have nicer seats in-flight. The desk and chair I've got in my office are the same kinds as the ones used by everyone else in this office. As I tell my pilots: There are people who make more money at this company than others, but that doesn't mean you should flaunt it.

What about serving others?
This week, I'm flying to Florida for work, and on the way down and back I'll serve drinks and snacks along with the crew and take out the garbage when we're done. It's a chance to serve the customer directly. On a much larger scale, we run what we call the JetBlue Crewmember Crisis Fund; everyone gives money to it, and it's used to help employees in crisis. If someone at JetBlue gets cancer, they have health benefits, sure, but they might need money to pay for a babysitter while Mom's at chemotherapy.

When employees know they're coming to a great job where they get full benefits – and that if something terrible happens to them the other employees will help them out – they do their best work, and they serve their customers well.

– Daisy Wademan

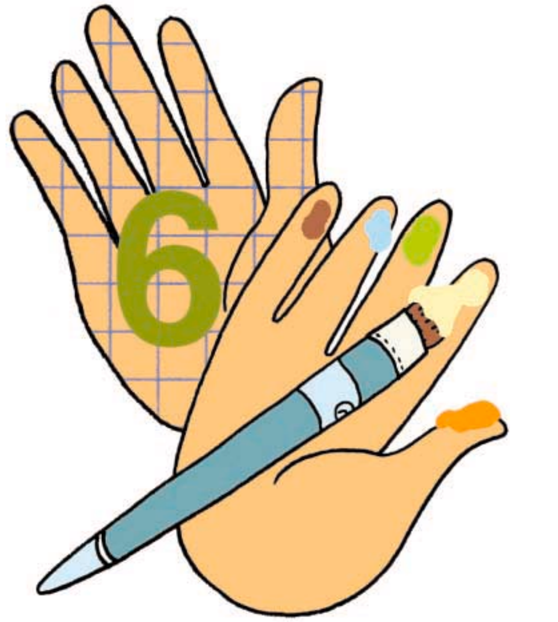
Reprint F0503K

database and lead management outsourcing is growing 10% annually. What's going on?

We believe there are two key reasons for this trend: First, outsourcing can save money and improve quality. American Express's consolidation of customer service call center operations in India, for example, cut service costs per customer by 20% to 30% while improving response time and boosting the percentage of satisfied customers by 20 points.

Second, outsourcing can provide increasingly critical left-brain marketing expertise that many companies lack, such as customer database management and analysis. When Sony, a legendary marketer, wanted to build a customer database, sell services, and market new, high-end products through its online store, Sony Style, it outsourced the program, recognizing that it didn't have the required skills in-house. Allstate has outsourced lead management, which has doubled the leads each agent gets. Ericsson has outsourced the management of its extranet, which provides the sales force with up-to-date customer information and allows direct communication with selected customers.

American Express now outsources its data mining to specialist third-party firms that can process millions of transactions a day to reveal purchasing patterns and other aspects of consumer behavior. And



Best Buy, the electronics retailer, is outsourcing not just database management but also marketing analyses and the complete execution of the marketing programs for two of its six segments – business and high-end customers.

The need for left-brain marketing expertise, we think, will only grow. A discipline that was once principally creative has become increasingly analytic, as the old workhorses – print and television advertising, and direct mail – become less and less effective. Marketing managers tend to be right-brain creatives with a fondness for mass-marketing campaigns when what's needed are left-brain number crunchers who zero in on the "market of one." Today, computer models optimize the allocation of pharmaceutical sales representatives' time, determining which customers to address and which products to promote to achieve the greatest return. Dynamic pricing models allow airlines to change ticket prices in real time based on the number of seats sold on a given flight. And IT-intensive database management now lets companies precisely target just the right messages to just the right customers in just the right terms.

While many things, from customer call centers to pricing-elasticity studies and sales force deployment models, can be outsourced, some aspects of marketing can't: those that directly drive marketing strategy. The CEO and top management team must regularly spend face time with customers and end consumers and drive this customer-focused culture throughout the organization. A chief marketing officer should be appointed to lead the marketing strategy, inject the customer perspective into new product development, and ensure that the company's intangible brand assets are carefully stewarded. Major accounts must be served by sales and service teams that have been given the right incentives so that they can integrate themselves into those customer organizations and ensure the "stickiness" necessary for long-term relationships.

To create the most value from outsourcing, marketing managers must become expert ringmasters who cherry-pick, develop, and monitor an integrated network of outside suppliers that brings new capabilities to the marketing effort. Above all, management must start seeing its marketing suppliers not as contractors that need to be controlled but as partners that can create shared value over the long term.

Reprint F0503J

What Are They Outsourcing?

MARKETING ACTIVITY	Operations	Program development and execution	Data analytics	Customer experience integration
COMMONLY OUTSOURCED FUNCTIONS	Call center operation Web site management Direct mail and e-mail program management Database management	Program design Campaign creative development Campaign management Lead management	Analysis of: Program performance Customer behavior Brand health	Design and implementation of uniform customer experience across many contact points or communication channels.
COMPANY EXAMPLES (function outsourced)	**General Motors** (data warehousing) **Ericsson** (development of sales tool for tracking interactions with customers)	**Sony** (Sony Style's Web-marketing program) **Allstate** (lead management)	**American Express** (identification of high-potential customers)	**Best Buy** (program integration for high-value customer segment)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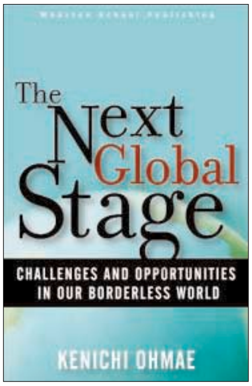
Reviews

The Next Global Stage

Challenges and Opportunities in our Borderless World
Kenichi Ohmae
(Wharton School Publishing, 2005)

In the early 1900s, German physicist Werner Heisenberg laid the foundations for quantum mechanics, a set of rules showing that at the subatomic level Newtonian physics was irrelevant. Just as quantum mechanics upstaged Newton, says strategist Kenichi Ohmae, a radical new model is upending old notions about the global economy. In this sprawling book, Ohmae warns that governments, businesses, and leaders that cling to their Newtonian approaches will become irrelevant themselves.



The heart of Ohmae's thesis will be familiar to readers of his previous books, including *The Borderless World* (1990) and *The Invisible Continent* (2000): In the new global economy, the nation-state, and the protectionist economic thinking that goes with it, is obsolete. Nation-states have borders, armies, flags, currencies, and a development-stifling instinct to protect their economies from the outside world. As global economic players, they're being displaced by "region states" – borderless centers of vibrant economic activity that welcome global trade and investment, like the Shutoken metropolitan area of Japan and Guangzhou in China.

If the rules of the old economy no longer apply, Ohmae ventures, then neither do the old rules of business. Fair enough. The problem is, he says, no one knows, or can know, what the new rules are: "By the time any rule book or user's manual appears…the 'new rules' will already be obsolete." What business leaders can be sure of, Ohmae argues, is that massive change without requires massive change within. That means wall-to-wall rethinking of corporate mission, strategy, and organization. Companies must cut loose from their "ancestry" and, for instance, compete by selling the very products that threaten them. Clinging to the core, as Kodak did in the face of predation by digital-camera makers, is a recipe for failure in this new age.

Companies must cast off their sentimental attachment to the nation-states where they're headquartered and jettison their hierarchies and old approaches to markets. Their leaders must become visionary facilitators without preconceived attitudes about their roles – ready to embrace even the idea that the best leader may be a team, not an individual. There can be no half measures in this radical transformation, Ohmae says, no testing the waters before taking the plunge.

It's a strong prescription. Unfortunately, this lively book can't, by its own admission, give business readers what they want most: practical advice for competing in the global economy. But it does remind executives to pry their gaze from the present and set it firmly on the future. As Heisenberg well understood, the more doggedly you map where a moving target is, the less you know about where it's headed.

– Gardiner Morse

The Bottomless Well: The Twilight of Fuel, the Virtue of Waste, and Why We Will Never Run Out of Energy

Peter Huber and Mark P. Mills
(Basic Books, 2005)

The spike in oil and gas prices has revived fears of an energy crisis, but regulatory scholar Huber and venture capitalist Mills aren't worried. Raw fuel, they explain, has surprisingly little effect on power costs, and technological advances in mining, engineering, lighting, and other processes, as well as alternative fuels, will make up for dwindling supplies. The authors are reassuring about every major issue except global warming, about which they warn that "going back to nature" through biomass and other such fuels will actually make things worse.

The Embedded Corporation: Corporate Governance and Employment Relations in Japan and the United States

Sanford M. Jacoby
(Princeton University Press, 2005)

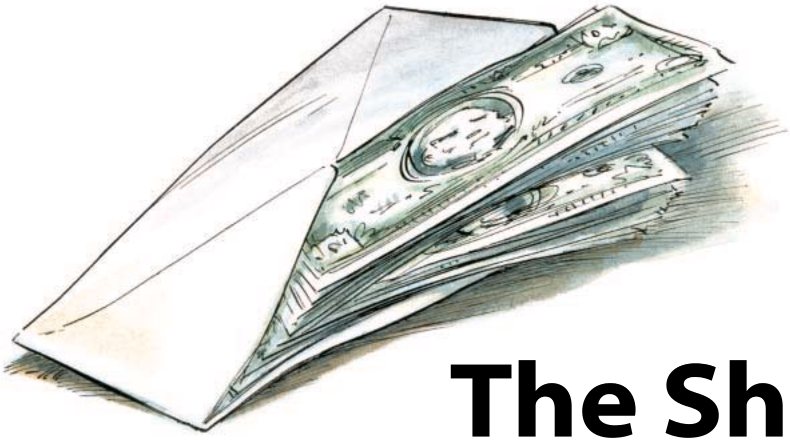
Human resource managers get no respect in the United States. By contrast, their Japanese counterparts wield so much power that critics blame them for the seniority system that's undermining the country's competitiveness. Jacoby, a historian, persuasively argues that the divergent American and Japanese attitudes toward employment arose from deep social and economic pressures and aren't likely to change much.

Pay Without Performance: The Unfulfilled Promise of Executive Compensation

Lucian Bebchuk and Jesse Fried
(Harvard University Press, 2004)

Here's a book for anyone who thinks Sarbanes-Oxley will finally force American executive compensation in line with investors' interests. Bebchuk and Fried, both law professors, show that even independent directors inevitably end up serving CEOs. The solution, they insist, is to give shareholders the power to nominate their own slates of directors. Perhaps, but that won't happen until investors get fed up and start selling in droves, as the authors would probably concede.

– John T. Landry



A young American businessman in a developing country discovers that nothing gets done unless palms are greased. Should he play the game by his personal ethics – or the local rules?

The Shakedown

by Phil Bodrock

"How many of them were there? Were they armed? Did they confiscate any papers or disks?"

Pavlo Zhuk suddenly realized he was shouting, though for once the telephone line to Kiev was crystal clear. Zhuk was in a state. The grandfather clock in his sprawling farmhouse in Redwoods, California, had struck 6 AM, and the young software entrepreneur had just come down to the kitchen when the telephone startled him. His friend Kostya Hnatyuk, who headed Zhuk's software development center in Kiev, was calling to say that the center had had visitors that day – and not very welcome ones.

Hnatyuk patiently repeated what he had said a moment earlier. "I'm on my way to the office, Pavlo, so I don't have all the details. Taras Borovetz called me 15 minutes ago as I was getting off the plane and said that three or four UTA agents showed up this afternoon. That's Ukraine Tax Authority. Only one of them, a woman, entered the office. I suppose the men could have been armed, but Taras didn't say so – "

"What did the woman say, exactly?" Zhuk interrupted.

"She said that her name was Laryssa Ossipivna Simonenko. She claimed to be a UTA special agent. She told Taras that she and her boss, who heads something called the Special Audits Department, want to meet with us soon," Hnatyuk replied. "She says that we haven't filed five of the 17 schedules we were supposed to last quarter and we owe the government tax arrears of 86,954 hryvnia." Zhuk quickly converted the figure in his head: close to $16,000. "It's a shakedown," Hnatyuk concluded.

"I can't believe it!" Zhuk cried. Had his life somehow turned into a B movie? "Why are they picking on us? We did everything by the book. How much time did she give us?"

"She said next week. Don't worry, Pavlo. Our accountant can dig out all the tax papers, and I'll keep the lawyer on call in case Simonenko drops in again. Meantime, I'll figure out who she is and whether she's really conducting an official inquiry. She could be running an extortion racket on the side…" Hnatyuk's voice trailed off; then he added: "I'll get our security guy to post two guards outside the office 24/7, starting tonight. No one else gets in unchallenged."

Zhuk was rattled by the thought of the Ukraine Tax Authority laying siege to his company's office. Standing barefoot in his kitchen, he felt powerless to

DANIEL VASCONCELLOS

HBR's cases, which are fictional, present common managerial dilemmas and offer concrete solutions from experts.

deal with the situation. "Look. I'll try to get on that Lufthansa flight out of LAX this afternoon. I should be there before the weekend. Maybe it's just a misunderstanding, but if we're in the tax authority's crosshairs, this could be big trouble. I'll call you again before I head out. Tell Taras and the other guys not to panic."

Because of the current backlog of orders, Mylofienko informed them, it would take some time to install the lines in their office on Predslavynska Street – about three years, in fact.

After putting the telephone back in its cradle, Zhuk took a deep breath. He stared out the window toward the woods, hoping to spot the family of foxes he'd seen playing there a few days earlier. Waiting for his coffee to brew, he went out for the newspaper and scanned the headlines. He stopped again to take in the countryside. It dawned on him that for the first time in memory, he wasn't looking forward to packing his bags and heading for Kiev.

Back in the USSR

Six months earlier, Zhuk could hardly wait to land in Kiev. When the plane descended through a thin layer of clouds, he saw the setting sun reflecting off the Dnieper River and Kiev's golden domes. Without a doubt, this 1,000-year-old city was the most beautiful sight he had ever seen from the air. Sacked by the Mongols in the thirteenth century and virtually destroyed by the Nazis and the Red Army in the twentieth century, it had still clung to much of its magnificent Renaissance and Baroque architecture.

Zhuk had his own connection with Kiev's past. His parents had fled the city at the end of World War II and by 1951 had found their way to the United States. The family first settled in Cleveland but moved in 1973 when Zhuk, Sr., an engineer, accepted a job in California. Pavlo, the last of six children, was born the same year and grew up speaking English and Ukrainian at home. He was the academic star of the family. After graduating with top honors from an engineering school on the East Coast, he worked for three years in Silicon Valley as a systems analyst and then entered an MBA program at a premier West Coast school. He hadn't even graduated when he decided to set up his company, Customer Strategy Solutions, to develop software for order-fulfillment systems. That proved to be a lucrative niche. After five years, the start-up employed 35 people, generated annual revenues of $40 million, and reported profits.

Then, with the help of his friend Hnatyuk, Zhuk drew up a plan to create a software development center in Kiev. Hnatyuk, a British national of Ukrainian descent, had graduated from a Newcastle polytechnic as an electronics engineer. The two had met years before while Zhuk was summering in the UK as an exchange student. Their Ukrainian roots – and love for soccer – had kept them in touch.

Before joining Customer Strategy Solutions, Hnatyuk had been based in Kiev as the vice president of a German company that sold seeds, pesticides, and fertilizers in the Commonwealth of Independent States. His company had been doing business in Ukraine for more than six years but hadn't turned a profit there until recently. When Zhuk had called a year ago to chat about his desire to set up a software development center, Hnatyuk immediately volunteered to quit his job and help set it up.

Without discussing it much, the men both knew they were motivated by a feeling that this wasn't just about business; something more basic was at stake. Ukraine was a land where, due to two world wars, an ideology-created famine, the Holocaust, and political purges too numerous to list, 17 million people had lost their lives during the twentieth century. A tenth of Western Ukraine's population, including one of Zhuk's uncles and many of Hnatyuk's relatives, had been deported to Siberia. Zhuk and Hnatyuk's return was an assertion of resilience. They were driven by a desire to create opportunity, to bring hope, and to help build a modern society in Ukraine.

Zhuk thought he was well on his way to proving the naysayers – those who had pointed out the political turmoil and corruption in Ukraine and told him he should think twice about setting up shop there – wrong. He appreciated their concern but thought it was overblown. As he'd told his 80-year-old father at Thanksgiving, he felt quite at home in the country of his ancestors.

Don't Know How Lucky You Are

As Zhuk disembarked from the aircraft at Borispol Airport, he felt less at home in Kiev than ever before. Hnatyuk picked him up in his beat-up Land Rover and seemed to think that despite the extortion threat, it was business as usual. "Check it out," Hnatyuk said as he drove toward the city apartment they shared whenever Zhuk was in town. "Another McDonald's, and a new Wimpy's is going in across the plaza." He knew that Zhuk would be heartened by the sight: While most Western companies were reluctant to invest in Ukraine, fast-food restaurants were opening all over Kiev.

When he got only a weary grunt of acknowledgment from Zhuk, Hnatyuk piped up again: "By the way, I haven't had a chance to tell you about that USDA meeting." The Ukrainian Software Developers Association had held its annual meeting the week before, and Zhuk had asked Hnatyuk to check it out. "I was quite impressed," said Hnatyuk. "Do you know there are over 25 medium-sized IT companies here – not just in Kiev, but also in Lviv, Kharkiv, and Dnepropetrovsk? We're still the only development center for a multina-

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tional. Everyone there was talking about how two Ukrainian firms had beaten an Indian rival and won a contract to develop embedded systems for a big American corporation. The Association forecasts that Ukraine's exports of IT-related services will double over the next two years."

Zhuk perked up momentarily. "There's no question, we're here at the right time," he said. His business model was simple. Like India and Ireland, Ukraine offered a virtually unlimited supply of highly skilled and, by American standards, reasonably priced programmers. The country had a tradition of excellence in scientific and technical education that dated back to the formation of the Soviet Union. But most engineers and programmers had lost their jobs since the Soviet Union's demise and were looking for new openings. Meanwhile, Ukraine's schools produced 50,000 fresh technical graduates every year.

That was great for Customer Strategy Solutions because, despite an economic downturn in the U.S., the company had more work than it could handle. It had started out installing off-the-shelf order-fulfillment systems, but its professionals increasingly consulted with clients on custom solutions and, more broadly, on innovative digital strategies. With Zhuk's top talent being pulled into strategy-related work, he needed more programmers to engineer systems.

On his previous visit, Zhuk had helped Hnatyuk recruit a core group of programmers, mostly through Hnatyuk's personal network. Later, as they made the rounds at Ukraine's universities and polytechnics, they found other institutions, such as the Institute of Cybernetics in Kiev, that were great sources of talent. "I feel like a kid in a candy store," Zhuk had said at the time. In a week, they hired 12 top-notch programmers, all in their twenties and with an average of three years' experience.

Zhuk wanted the best talent and was willing to pay top dollar for it. That was another point the two men had agreed on before hiring anyone: They would pay a wage that would afford their employees a level of comfort that most Ukrainians didn't have. The typical programmer's salary in Ukraine, at $500 a month, accounted for only 40% to 60% of his or her family's budget. Zhuk wanted his programmers to be able to afford three meals a day without having to barter, stand in queues for hours, or moonlight. He wanted their families

to have good medical care when they needed it. At the end of the day, he thought, the best way to make a difference in Ukraine was to enable people to buy homes, cars, and consumer durables. Customer Strategy Solutions therefore paid its programmers a salary of 66,000 hryvnia, or $12,000 – twice as much as a programmer could normally expect to earn in Ukraine but well below the $75,000 to $85,000 that his American counterpart would command or the $24,000 that a Russian programmer would earn.

"But that just isn't enough for some Ukrainians," Zhuk thought darkly, his mind returning to the reason for his current visit.

The Costs of Doing Business

It wasn't as though Zhuk's eyes were entirely shut to the difficulties of doing business in a developing economy. If they had been, they opened pretty quickly in the process of getting the development center up and running. The first lesson came the day Hnatyuk took Zhuk to Dnipro Telecom, the state-owned telecommunications utility, to get the telephone lines they would need. Hnatyuk had already explained that the company didn't offer dedicated high-speed lines, and getting Dnipro Telecom to sanction even plain-vanilla telephone lines wouldn't be easy.

At precisely 9 AM, Zhuk and Hnatyuk were ushered into the office of Vasyl Feodorovych Mylofienko, a senior business manager at Dnipro Telecom. The meeting had been arranged by a former colleague of Hnatyuk's. They sat respectfully while Mylofienko detailed the costs of telephone line rentals, at ten hryvnia ($1.85) per month, and usage rates, at 0.5 hryvnia (9 cents) per minute. The onetime installation fee that Dnipro Telecom would charge the company, 100 hryvnia ($18.50) per line, was reasonable.

But then came an unpleasant surprise. Because of the current backlog of orders, Mylofienko informed them, it would take some time to install the lines in their office on Predslavynska Street – about three years, in fact. If Zhuk couldn't connect the center to the firm's headquarters in Silicon Valley via the Internet, the project would be dead in the water. Hnatyuk had seemed calm, though. He turned to Zhuk and remarked that they would have to approach one of the other telephone companies in the city. A smaller firm would be more expensive but would probably be able to provide the center with lines in months, not years.

Zhuk was puzzled. Why were they discussing their options out loud in Mylofienko's office? He got his answer when Mylofienko cleared his throat. "Of course," he said, "we could expedite your application."

Hnatyuk jumped on the remark. "*Tse duzhe tsikavo* [That's very interesting]," he purred. "Please tell us more, Vasyl Feodorovych. What is it that you have in mind?"

"For a onetime fee of $300 per line" – Zhuk noted the shift to U.S. currency – "I could install the ten telephone lines in your office next month. For $500 per line, I would be pleased to offer you service beginning next week. That would require rearranging our installation schedules in Old Kiev, but I'm sure it can be done."

For $3,000, Zhuk's software center could be up and running next month; for $5,000, next week. He was sorely tempted to take his business to another telecom company, where the installation charges would be more reasonable. The downside was that Hnatyuk would have to set up fresh appointments, they'd have to visit more people, and they'd spend more time getting wired than training their programmers or scouting for customers. Zhuk felt a trifle uncomfortable but made the call: "We would like to have the lines as soon as possible," he said, as much to Hnatyuk as to Mylofienko.

That was the cue Hnatyuk had been waiting for. He asked Mylofienko to draw up a contract for ten telephone lines, then excused himself and went to the men's room, where he extracted 50 hundred-dollar bills from his security belt, placed them in an envelope, and put the envelope in his breast pocket. When Hnatyuk returned, he took his seat, carefully read the contract, and signed both copies. He ceremoniously handed one copy to Zhuk. He folded Mylofienko's copy in half. Zhuk saw Hnatyuk take the envelope filled with cash out of his pocket, discreetly insert it into the crease of the contract, and hand it to the manager. Hnatyuk wrote a check drawn on a Kiev bank for 1,000 hryvnia and handed it to Mylofienko.

Hnatyuk got up to leave.

Following Hnatyuk's lead, Zhuk got up and bid the telecom manager good day. Mylofienko smiled and assured Zhuk that his telephone lines would be installed early the following week.

The kicker came at the very end. As Mylofienko shook hands with Hnatyuk, he presented him with two receipts: one for $5,000, the other for 1,000 hryvnia. Zhuk was no longer sure what was going on. Had they or had they not just bribed Mylofienko?

As Zhuk and Hnatyuk walked down the steps of the Dnipro Telecom building, Hnatyuk burst out laughing at the expression on his friend's face. He explained that so many people had complained about the demands for extra charges in hard currency that the telephone company had taken to issuing receipts. Paying extra in U.S. dollars or euros for a service had become standard practice in Ukraine. In fact, Hnatyuk warned Zhuk, bureaucrats in most offices followed the same procedure. When they registered the company, got the fire inspector to visit the premises, and listed with the tax authorities, they might have to pay official fees in local currency and quasi-official charges in dollars or euros.

"Crazy as that sounds, I'm relieved," said Zhuk. "I knew that because of different laws, European firms could pay bribes more easily than American firms, but I'd never have guessed that paying bribes could be official." He asked Hnatyuk to check, in any case, with the firm's CFO in California about how to account for such payments on the company's books. "I realize you have a local accountant," he added, "but let's just make sure there won't be any trouble with the IRS."

By the end of the week, Zhuk was convinced that incorporating a business in Kiev was no more burdensome than setting up a company in California. They had to register with only six bureaucracies: the Kiev city administration, an ecology office, a statistics bureau, the local social security office, the local police, and the Ukraine Tax Authority. Zhuk and Hnatyuk had to visit the police twice – first to obtain a permit to open a business, then again to get the permit stamped, since the part of the office that stamped permits was open only two days a week. But all that was hardly insurmountable. In the end, Zhuk got back to the United States just two days later than he had originally planned, secure in the knowledge that the Kiev software development center would be up and running the very next week.

A Matter of Principle

Hnatyuk's Land Rover pulled into the parking area behind the apartment building. Zhuk sneezed and said he might be catching a cold. As they entered the apartment, they discussed what they should attempt to accomplish – and be prepared to accept – in the days to come.

"So we don't know anything more, do we?" asked Zhuk. "We only know that Simonenko told Taras that if payment was not forthcoming within a week, there could be some serious consequences."

Hnatyuk nodded. "She also said that in such cases, it was not uncommon for the parties to reach an agreement," he said. "That sounded like an invitation to me."

"Look, Kostya, I'm way outside my comfort zone on this." Zhuk massaged his forehead. "I was willing to go along with all those so-called facilitation payments to get bureaucrats to do their jobs, especially if that's what everyone else does. But let's assume this is really an extortion racket. What happens when word gets out that we're a soft target? I don't have the stomach or the capital to pay off every thug in town. Also, we're doing something good for this country. We shouldn't have to put up with this."

"No question," Hnatyuk said. "We shouldn't pay them too much." Zhuk could tell his colleague was trying to hold him to a pragmatic line of thought. Why waste time wishing reality were other than what it is?

But reality was different where Zhuk came from, and it could be different here. Strike that "could," Zhuk thought. It *will* be different here. It's only a matter of time. And Ukraine was where he wanted his company to be. A couple of days ago, he had gone to lunch with a merchant banker who felt that Zhuk should take Customer Strategy Solutions public. "You'll get a bigger premium for your shares because you have a development center in Kiev," the banker had said. "People are crazy nowadays over firms that outsource."

Maybe it wasn't a comfortable time to be doing business here. But which was better: to pack up and go home with one's personal ethics unsullied or to live to fight another day and commit to being part of the solution? Perhaps he could lead a double life, abiding by the local rules of the game while investing in initiatives led by local NGOs that wanted to battle corruption in the country.

Zhuk glanced at Hnatyuk and realized it wasn't that straightforward. What about his friend's well-being? Hnatyuk would never leave Kiev, and hadn't Zhuk encouraged him to quit his job and work for Customer Strategy Solutions? For that matter, what about the programmers they'd hired? He knew each of them by name and knew how grateful they were for the opportunity he'd given them. How could he let them down at the first sign of trouble?

In his heart, Zhuk knew he wasn't ready to pull out of Ukraine; he would have to bargain with the bullies. But what actions would constitute the high ground?

Should Customer Strategy Solutions pay off the tax officials? • Four commentators offer expert advice.

(see next page)

***Alan L. Boeckmann** is the chairman and CEO of Southern California–based Fluor Corporation, an engineering and construction services company with annual revenues of $9 billion.*

Had Zhuk created clear internal policies and controls within his firm, he might have found ways to operate effectively in Ukraine.

Despite Kostya Hnatyuk's years of doing business in Ukraine, Pavlo Zhuk took a seat-of-the-pants approach to starting the software development center in Kiev. They should have spent more time and effort up front trying to understand the challenges, practices, and business culture they were walking into.

Zhuk could have learned a lot from two U.S. government Web sites. First, the U.S. State Department's (www.state.gov) background note on Ukraine would have told him that the country is burdened by corruption, excessive government regulation, and lack of law enforcement. Second, the CIA's World Factbook (www.cia.gov/cia/publications/factbook/) would have revealed that Ukraine's telephone system is antiquated and in disrepair and that there are 3.5 million pending telephone applications. Since Zhuk needed a modern telephone system for his development center, he would have immediately realized that he faced a problem.

From the State Department note, Zhuk could have obtained contact information for key U.S. officials in Kiev. He should have consulted them before deciding to invest in Ukraine. Zhuk should also have asked his accountant and his attorney in the U.S. for references in Kiev. Ukrainian accountants and attorneys would have alerted him to the difficulties lying ahead. Moreover, before setting up his foreign operation, Zhuk should have familiarized himself with the U.S. Foreign Corrupt Practices Act (FCPA). He should have developed a company policy against bribery and made a plan for how to deal with corruption.

Encounters with corrupt officials are, regrettably, common in many parts of the world. An understanding of the local business culture and appropriate policies for addressing demands for bribes are basic tools for succeeding in unfamiliar settings. Last year, companies in my industry, with the support of Transparency International and the Basel Institute, created a set of global anticorruption principles. The point was to create a level playing field and to eradicate the effects of bribery in an industry where corruption has too often determined who wins contracts. Companies that agree to the principles commit to implementing a zero-tolerance policy against bribery and to developing internal programs to persuade employees not to pay bribes.

By having Hnatyuk pay a bribe to Vasyl Feodorovych Mylofienko, Zhuk signaled that he would pay local bureaucrats whatever was necessary to do business in Kiev. In fact, by making that $5,000 payment, he may have violated the FCPA. The act permits facilitation payments as long as they are small. Hnatyuk clearly violated the Anti-Terrorism, Crime, and Security Act of 2001 by paying a bribe. He would therefore be subject to prosecution in Great Britain because English law, unlike the FCPA, does not make exceptions for facilitation payments.

Companies pay bribes for three reasons. First, multinationals operate in countries where bribery has become systemic due to weak institutions and poor rule of law. Second, most countries do a bad job of enforcing their anticorruption laws. Third, managers often have to meet tough business goals. Those factors can place managers in circumstances where paying bribes may seem like the best choice. Only clear internal policies and controls can ensure that managers do the right thing. Had Zhuk created those policies and controls within his own firm, he might have found ways to operate effectively in Ukraine.

In the present circumstances, Zhuk will face a series of requests for bribes. Since he cannot ethically operate in that environment, disengagement is his best course of action. Breaking the law – in this case, the FCPA – would be unthinkable.

WENDY WRAY

Motorola's Chairman and CEO, Ed Zander, does business everywhere. France is no exception.

Some people might say, "Who needs the French?" What about you?

I'm color-blind. If I'm sitting in a lab in France discussing products that are part of our overall R&D strategy, I don't see French people. I just see smart people who are creating value and innovation.

Motorola has been expanding its French operations. How come?

We can't design products for the European or the French market here in the US. We have to tap into the local expertise that's out there where we sell our products. I'll go anywhere in the world where I can find education, a talent pool and a favorable climate for investing which the government supports. You find all those things in France today. The people work hard, they're educated and they understand the whole global picture.

Has your investment in France been a smart move?

The answer is unequivocally yes. My background is in companies with a long heritage of investing in France. At Sun Microsystems, we had a big R&D center in Grenoble. Before that, at Data General, our European headquarters was in Paris. Today, at Motorola, we have over 3,000 people working for us in France. We like to go where the smart people are. France fits the bill.

How do French workers measure up to the competition?

I don't see any difference between a great French engineer and a great US or Chinese engineer. I look at output. France is a place that produces lots of smart people. We wouldn't be investing in France if we didn't have great people there delivering great products and great technology. They've got great schools, good scientists and engineers. It's a good place to be.

Motorola in France:

- Established the first semi-conductor site outside the US in France in 1967
- 3000 employees in the broadband, telecommunications, semiconductor and personal communications sectors.
- Partnership with ST Microelectronics and Philips has produced one of the most advanced nanotechnology R&D centers in the world at Crolles 2 France

Can France cut it in the 21st century?

Everyone's running around talking about globalization and the outsourcing of jobs. To win in today's world, businesses and countries have got to seize the moment by investing in programs to keep the best people in their countries. We need the education systems, we need innovation, we need all that stuff. I've got to say, I'm impressed with what I've seen in France.

Is this the best time for a US company to be doing business in France?

I think most of us in the business world are smart enough to be able to separate business from politics. The French and the Americans have been together for a long, long time. I've always found the people great.

Do you get what you want from the French government?

We're urging not only the French government but the US and all the governments around the world to keep investing in education, in innovation and in technologies. We need research to be encouraged. In fact, I'm pushing hard in the US for business and government to work together more closely on education and technology – like they do in France. We need to save jobs and retain core skills here too.

"I'm color-blind… I don't see French people. I just see smart people who are creating value and innovation."

Is France a popular posting for your US personnel?

You bet it is! Great food, great wine! If you had to pick a country to go and live in, France has got to be up there at the top, right? I wouldn't mind doing a stint there myself.

There has never been a better time to invest in France. To find out what the new France can do for your business, visit www.thenewfrance.com

THE NEW FRANCE. WHERE THE SMART MONEY GOES.

Rafael Di Tella is a professor at Harvard Business School in Boston.

As any businessperson would do in this situation, Zhuk will pay off the UTA officials. After all, he wouldn't be breaking the law if he did so. The situation clearly suggests that Zhuk is a victim of extortion. According to most nations' laws, succumbing to extortion isn't a crime. So Zhuk will pay off Simonenko. He will consider the bribes an additional tax he has to pay for doing business in Ukraine and carry on with his pet project. Make no mistake: That's how the situation would play out in real life. If a businessperson doesn't pay officials when he is a victim of extortion, he doesn't have the stomach to do business in developing countries.

But should Zhuk pay off the officials? That's tougher to answer. I know what Zhuk will do; I don't know what he *should* do, because that's a moral issue, and we don't know from the case what Zhuk's morality dictates.

Let's think of a framework that might help us. Start by imagining a continuum of corruption cases. At one end, there is extortion of the Simonenko kind. At the other, there are money-laundering schemes that allow businesspeople in cahoots with local politicians to enrich themselves without having to invest in a company. Businessmen like Zhuk usually tell themselves that while they may have to pay off politicians and officials, they would never get involved in rackets of the second kind. Fair enough.

When companies are corrupt, they lose legitimacy. As a result, people demand more regulation.

What's interesting is what companies do when they are in the middle of the continuum. Let's say you are a businessperson who wants to do business without bribing officials. One day, you find that a rival company is bribing bureaucrats for favors that are giving it an unbeatable advantage. You realize that if you don't get the preferential treatment your rival is buying, you're going to have to leave the country. In an economic sense, your choices are identical to those Zhuk faces: pay – or quit.

Under those circumstances, the end result will also be the same: Like Zhuk, you will pay a bribe. You'll talk to the corrupt bureaucrat and demand to be treated the same as your rival. When the official says he can extend favors to you only if you agree to do him favors in return, you'll agree. You'll find it easy to justify these favors to yourself by saying that you were the victim of an extortion demand by the bureaucrat. Thus, companies that start paying bribes are actually on a slippery slope. They justify extortion payments, and they justify bribes by saying they're doing only what their rivals are doing. And then…I'm not sure where they will stop on the continuum.

That worries me, because first, it means companies' moral standards are going downhill. Second – and this is something most firms don't realize – companies create a bad business environment by indulging corrupt politicians. When organizations are corrupt, they lose legitimacy. As a result, people demand more regulation, more taxes on companies, and more harassment of firms. That sets off a vicious cycle of policy intervention – and more corruption. It is up to Zhuk to decide what he wants to do: create one software center in Ukraine and risk damning his business in people's eyes, or work to increase the legitimacy of Ukrainian business, even if that means pulling out.

A word of caution. Talking about corruption in emerging countries has become too fashionable. It has few direct benefits and many indirect costs. Since the judicial systems in most developing countries are highly politicized, real – as opposed to rhetorical – progress is unlikely. Real change requires judicial reform, which is hard and takes time. No amount of talking about corruption and bribery is going to change that. This is why I recently proposed the creation of a Harvard-Yale Judicial Observatory. It will consist of a group of law academics and practitioners who can pass judgment on high-profile legal rulings that people suspect are politically motivated. That will change the incentives facing politicized judges and reduce idle corruption talk, and it may even improve the quality of politicians in emerging countries.

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Once Zhuk is safely out of Ukraine, he must publicly state why he had to leave and provide all the information he has gathered on Simonenko and her friends.

IF SIMONENKO HAS ASKED ZHUK for a coarse bribe rather than a facilitation payment, Zhuk's only ethical recourse is to resist. If he is unable to fight her demands successfully, Zhuk must publicly pull out of his Ukrainian venture. Although he may want to focus on a pragmatic or a legal solution to the problem, doing so would be a moral mistake. Any concession to Simonenko and those she represents will serve only to sustain corruption in Ukraine–a grave consequence for that country's people.

Zhuk may be tempted to pay off Simonenko because that may help his Ukrainian employees. The urge to do so may be particularly great because of his desire to create opportunity and bring hope to Ukraine. But the good Zhuk can achieve by maintaining a continued presence in Kiev isn't a sufficient counterweight to the harm caused by corruption. Paying bribes to stay in business doesn't achieve the greatest good for the greatest number of people; it contributes to the cycle of corruption and harms many.

Ukraine has failed to live up to its economic promise for years, and the primary reason is pervasive corruption. In Transparency International's 2004 Corruption Perception Index, Ukraine tied for 122nd (first is least corrupt). The cost to Ukrainians is enormous. Corruption often involves human rights violations because bribes are extorted from those who provide essential medical supplies and food for the starving. Ukrainians will be truly free only when they reach a tipping point against corruption. That will happen when Ukrainians have the information, power, and will to counter extortionists like Simonenko.

How can Zhuk help create a tipping point against corruption? Simonenko appears to be demanding a coarse bribe, which involves payment of a benefit to a public official to breach a duty pertaining to a significant community interest. It would therefore be a mistake for Zhuk to assume that Simonenko and her compatriots care in the slightest about the long-term impact of their actions on either Ukrainians or on Customer Strategy Solutions. Even if Zhuk makes only a small payment, he gives Simonenko the leverage to exert ever greater pressure on him.

Zhuk must act very quickly to see if he can counter the threat from Simonenko. He could contact other software firms or non-Ukrainian companies doing business in the country to determine if there are strategies they can collectively use to thwart such solicitations. After all, transnational fast-food companies have been successful in Ukraine. If that quest doesn't produce results, Zhuk could contact NGOs like Transparency International to see if there is another reasonable option. If there isn't, Zhuk should leave Ukraine. Once he is safely out, he must publicly state why it became necessary for him to leave and provide all the information he has gathered on Simonenko and her friends.

This case study demonstrates the pervasive and insidious nature of corruption. It is extremely difficult to uproot. David Hess and I argued in 2000 in the *Cornell International Law Journal* that business can be an important part of the solution. We suggested that companies adopt antibribery principles, similar to the Sullivan Principles, when they do business. The Sullivan Principles were used in the 1970s as a strategy to fight apartheid in South Africa, and firms that adopted them committed themselves to equality in hiring and wages, nonsegregation in the workplace, and the training and promotion of blacks. In the same vein, Hess and I proposed the C2 Principles (see www.c2principles.org) for combating corruption in the hope that they might encourage firms to resist solicitations for bribes. Adopting the C2 Principles can, together with other pressures, move companies closer to the day when an anticorruption tipping point is reached in every developing country.

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By accepting Simonenko's seemingly limited offer, Zhuk will be flagging himself and his firm for bigger trouble.

SHOULD ZHUK ACCEPT the protection-for-money deal offered to him by organized criminals under the guise of UTA Special Agent Simonenko?

The answer is simply and emphatically no.

Much can be said about the need to understand the situation in Ukraine and to accept that there's a fine line between legitimate activity and bribery, as Zhuk found out at Dnipro Telecom's office. But by putting things too much "into perspective," Westerners in emerging markets end up accepting and doing things they would never accept or do in their own countries. Few of them recognize that by behaving that way, they go down a path along which they cannot return.

Zhuk has probably done a cost/benefit analysis of his possible courses of action. Although he finds paying bribes morally reprehensible, doing so is the only way he can save a promising operation that employs so many young people. Zhuk, a patriot, might find some moral comfort in that thought.

But Zhuk needs to realize that by accepting Simonenko's seemingly limited offer, he will be flagging himself for bigger trouble. Once you join that dance, the music never stops. The same seedy group will soon be back, asking for bigger benefits to protect Zhuk's firm on other fronts: land rights, contracts with business partners, you name it. Rival underworld groups might also fight to extend their turf to Customer Strategy Solutions.

Over time, Zhuk will hear through the Kiev business grapevine that Simonenko and her associates have been bragging about their successful relationship with him. That will lead some people to stay away from Zhuk's company in order to avoid trouble. Finally, the entrepreneur might one day find himself answering questions on the matter from local media or from the public prosecutor's office. The noise around Zhuk in Kiev might even be heard in Silicon Valley. No matter what he says at that stage, the fact that he illegally gave money to a public official will stick to his reputation.

Zhuk should therefore immediately implement the following five steps:

1. He should hire a professional security firm to avoid unnecessary provocation from the thugs and to reassure his staff. That's part of the cost of doing business in less-structured environments.

2. He should get his staff's buy-in for the tough stance he plans to take. Most of those young professionals will admire Zhuk for his courage and will tell other people about it. All of Kiev will hear of his standards and ethics.

3. He should write about the extortion demand to Ukrainian authorities at the highest level: the minister of finance, the minister of the economy, the Foreign Investment Protection Agency, and the head of the UTA as well as the U.S. ambassador to Ukraine. Zhuk should also request meetings with them. Like all developing countries, Ukraine needs inflows, not outflows, of foreign investment. I can vouch from personal experience that Zhuk will get a patient hearing from the people at the top.

4. If the threats don't subside, he should hold a press conference to draw public attention to his problems. Zhuk will be able to explain his patriotic motives and state that he wants to help improve business standards in his homeland. He will emerge as a principled and ethical business leader, and no one will dare ask him for a bribe again.

5. If none of these actions produce results, he should pack up and leave Ukraine.

Having lived and worked for years in similar environments, I doubt that Zhuk will have to shut down his software development center. Quite the contrary: He and his firm will eventually be celebrated in Ukraine as proof that things are changing for the better.

Reprint R0503A
To order, see page 151.

***Bozidar Djelic** (bdjelic@altiscapital.net), founder of Altis, a professional services group focusing on Southeast Europe, was the finance and economy minister of Serbia from January 2001 to March 2004. Prior to that, he was a partner at McKinsey & Company and based in Paris and Silicon Valley.*

Stepping off the career fast track is easy. What's hard is getting back on. Careers, companies, and economies suffer when highly skilled women cannot get back where they belong.

MARIA RENDON

Off-Ramps and On-Ramps

Keeping Talented Women on the Road to Success

by Sylvia Ann Hewlett and Carolyn Buck Luce

THROUGHOUT THE PAST YEAR, a noisy debate has erupted in the media over the meaning of what Lisa Belkin of the *New York Times* has called the "opt-out revolution." Recent articles in the *Wall Street Journal,* the *New York Times, Time,* and *Fast Company* all point to a disturbing trend–large numbers of highly qualified women dropping out of mainstream careers. These articles also speculate on what might be behind this new brain drain. Are the complex demands of modern child rearing the nub of the problem? Or should one blame the trend on a failure of female ambition?

The facts and figures in these articles are eye-catching: a survey of the class of 1981 at Stanford University showing that 57% of women graduates leave the work force; a survey of three graduating classes at Harvard Business School demonstrating that only 38% of women graduates end up in full-time careers; and a broader-gauged study of MBAs showing that one in three white women holding an MBA is not working full-time, compared with one in 20 for men with the same degree.

The stories that enliven these articles are also powerful: Brenda Barnes, the former CEO of PepsiCo, who gave up her megawatt career to spend more time with her three children; Karen Hughes, who resigned from her enormously influential job in the Bush White House to go home to Texas to better look after a needy teenage son; and a raft of less prominent women who also said goodbye to their careers. Lisa Beattie Frelinghuysen, for example–featured in a recent *60 Minutes* segment – was building a very successful career as a lawyer. She'd been president of the law review at Stanford and went to work for a prestigious law firm. She quit after she had her first baby three years later.

These stories certainly resonate, but scratch the surface and it quickly becomes clear that there is very little in the way of systematic, rigorous data about the seeming exodus. A sector here, a graduating class there, and a flood of anecdotes: No one seems to know the basic facts. Across professions and across sectors, what is the scope of this opt-out phenomenon? What proportion of professional women take off-ramps rather than continue on their chosen career paths? Are they pushed off or pulled? Which sectors of the economy are most severely affected when women leave the workforce? How many years do women tend to spend out of the workforce? When women decide to reenter, what are they looking for? How easy is it to find on-ramps? What policies and practices help women return to work?

Early in 2004, the Center for Work-Life Policy formed a private sector, multiyear task force entitled "The Hidden Brain Drain: Women and Minorities as Unrealized Assets" to answer these and other questions. In the summer of 2004, three member companies of the task force (Ernst & Young, Goldman Sachs, and Lehman Brothers) sponsored a survey specifically designed to investigate the role of off-ramps and on-ramps in the lives of highly qualified women. The survey, conducted by Harris Interactive, comprised a nationally representative group of highly qualified women, defined as those with a graduate degree, a professional degree, or a high-honors undergraduate degree. The sample size was 2,443 women. The survey focused on two age groups: older women aged 41 to 55 and younger women aged 28 to 40. We also surveyed a smaller group of highly qualified men (653) to allow us to draw comparisons.

Using the data from the survey, we've created a more comprehensive and nuanced portrait of women's career paths than has been available to date. Even more important, these data suggest actions that companies can take to ensure that female potential does not go unrealized. Given current demographic and labor market trends, it's imperative that employers learn to reverse this brain drain. Indeed, companies that can develop policies and practices to tap into the female talent pool over the long haul will enjoy a substantial competitive advantage.

Women Do Leave

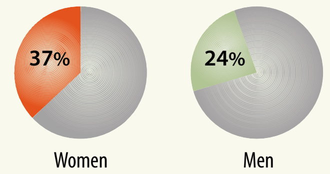
Many women take an off-ramp at some point on their career highway. Nearly four in ten highly qualified women (37%) report that they have left work voluntarily at some point in their careers. Among women who have children, that statistic rises to 43%.

Factors other than having children that pull women away from their jobs include the demands of caring for elderly parents or other family members (reported by 24%) and personal health issues (9%). Not surprisingly, the pull of elder care responsibilities is particularly strong for women in the 41 to 55 age group – often called the "sandwich" generation, positioned as it is between growing children and aging parents. One in three women in that bracket have left work for some period to spend time caring for family members who are not children. And lurking behind all this is the pervasiveness of a highly traditional division of labor on the home front. In a 2001 survey conducted by the Center for Work-Life Policy, fully 40% of highly qualified women with spouses felt that their husbands create more work around the house than they perform.

Alongside these "pull" factors are a series of "push" factors – that is, features of the job or workplace that make women head for the door. Seventeen percent of women say they took an off-ramp, at least in part, because their jobs were not satisfying or meaningful. Overall, understimulation and lack of opportunity seem to be larger problems than overwork. Only 6% of women stopped working because the work itself was too demanding. In business sectors, the survey results suggest that push factors are particularly powerful – indeed, in these sectors, unlike, say, in medicine or teaching, they outweigh pull factors. Of course, in the hurly-burly world of everyday life, most women are dealing with a combination of push and pull factors – and one often serves to intensify the other. When women feel hemmed in by rigid policies or a glass ceiling, for example, they are much more likely to respond to the pull of family.

It's important to note that, however pulled or pushed, only a relatively privileged group of women have the option of not working. Most women cannot quit their careers unless their spouses

How Many Opt Out?



In our survey of highly qualified professionals, we asked the question, "Since you first began working, has there ever been a period where you took a voluntary time out from work?" Nearly four in ten women reported that they had – and that statistic rises to 43% among women who have children. By contrast, only 24% of highly qualified men have taken off-ramps (with no statistical difference between those who are fathers and those who are not).

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earn considerable incomes. Fully 32% of the women surveyed cite the fact that their spouses' income "was sufficient for our family to live on one income" as a reason contributing to their decision to off-ramp.

Contrast this with the experience of highly qualified men, only 24% of whom have taken off-ramps (with no statistical difference between those who are fathers and those who are not). When men leave the workforce, they do it for different reasons. Child-care and elder-care responsibilities are much less important; only 12% of men cite these factors as compared with 44% of women. Instead, on the pull side, they cite switching careers (29%), obtaining additional training (25%), or starting a business (12%) as important reasons for taking time out. For highly qualified men, off-ramping seems to be about strategic repositioning in their careers – a far cry from the dominant concerns of their female peers.

For many women in our study, the decision to off-ramp is a tough one. These women have invested heavily in their education and training. They have spent years accumulating the skills and credentials necessary for successful careers. Most are not eager to toss that painstaking effort aside.

Lost on Reentry

Among women who take off-ramps, the overwhelming majority have every intention of returning to the workforce – and seemingly little idea of just how difficult that will prove. Women, like lawyer Lisa Beattie Frelinghuysen from the *60 Minutes* segment, who happily give up their careers to have children are the exception rather than the rule. In our research, we find that most highly qualified women who are currently off-ramped (93%) want to return to their careers.

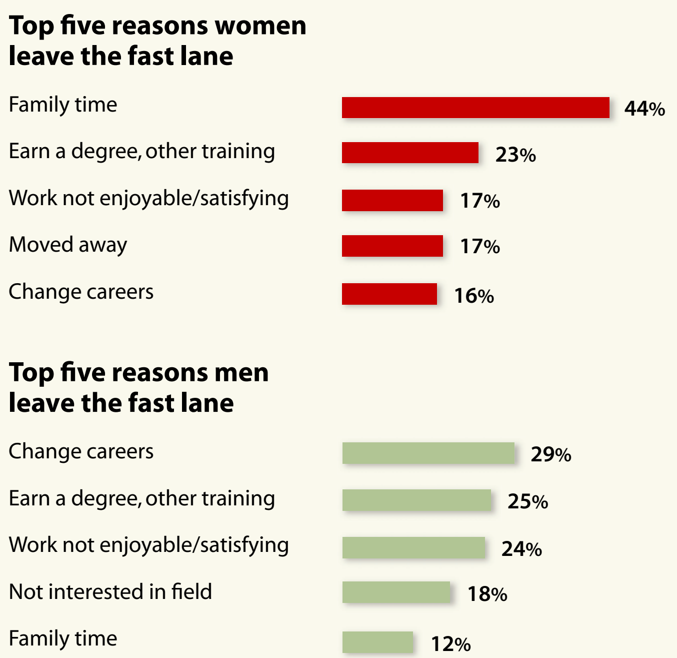
Many of these women have financial reasons for wanting to get back to work. Nearly half (46%) cite "having their own independent source of income" as an important propelling factor. Women who participated in focus groups conducted as part of our research talked about their discomfort with "dependence." However good their marriages, many disliked needing to ask for money. Not being able to splurge on some small extravagance or make their own philanthropic choices without clearing it with their husbands did not sit well with them. It's also true that a significant proportion of women currently seeking on-ramps are facing troubling shortfalls in family income: 38% cite "household income no longer sufficient for family needs" and 24% cite "partner's income no longer sufficient for family needs." Given what has happened to the cost of homes (up 38% over the past five years), the cost of college education (up 40% over the past decade), and the cost of health insurance (up 49% since 2000), it's easy to see why many professional families find it hard to manage on one income.

But financial pressure does not tell the whole story. Many of these women find deep pleasure in their chosen careers and want to reconnect with something they love. Forty-three percent cite the "enjoyment and satisfaction" they derive from their careers as an important reason to return – among teachers this figure rises to 54% and among doctors it rises to 70%. A further 16% want to "regain power and status in their profession." In our focus groups, women talked eloquently about how work gives shape and structure to their lives, boosts confidence and self-esteem, and confers status and standing in their communities. For many off-rampers, their professional identities remain their primary identities, despite the fact that they have taken time out.

Perhaps most interesting, 24% of the women currently looking for on-ramps are motivated by "a desire to give something back to society" and are seeking jobs that allow them to contribute to

Why Do They Leave the Fast Lane?

Our survey data show that women and men take off-ramps for dramatically different reasons. While men leave the workforce mainly to reposition themselves for a career change, the majority of women off-ramp to attend to responsibilities at home.



their communities in some way. In our focus groups, off-ramped women talked about how their time at home had changed their aspirations. Whether they had gotten involved in protecting the wetlands, supporting the local library, or rebuilding a playground, they felt newly connected to the importance of what one woman called "the work of care."

Unfortunately, only 74% of off-ramped women who want to rejoin the ranks of the employed manage to do so, according to our survey. And among these, only 40% return to full-time, professional jobs. Many (24%) take part-time jobs, and some (9%) become self-employed. The implication is clear: Off-ramps are around every curve in the road, but once a woman has taken one, on-ramps are few and far between – and extremely costly.

The Penalties of Time Out

Women off-ramp for surprisingly short periods of time – on average, 2.2 years. In business sectors, off-rampers average even shorter periods of time out (1.2 years). However, even these relatively short career interruptions entail heavy financial penalties. Our data show that women lose an average of 18% of their earning power when they take an off-ramp. In business sectors, penalties are particularly draconian: In these fields, women's earning power dips an average of 28% when they take time out. The longer you spend out, the more severe the penalty becomes. Across sectors, women lose a staggering 37% of their earning power when they spend three or more years out of the workforce.

Naomi, 34, is a case in point. In an interview, this part-time working mother was open about her anxieties: "Every day, I think about what I am going to do when I want to return to work full-time. I worry about whether I will be employable – will anyone even look at my résumé?" This is despite an MBA and substantial work experience.

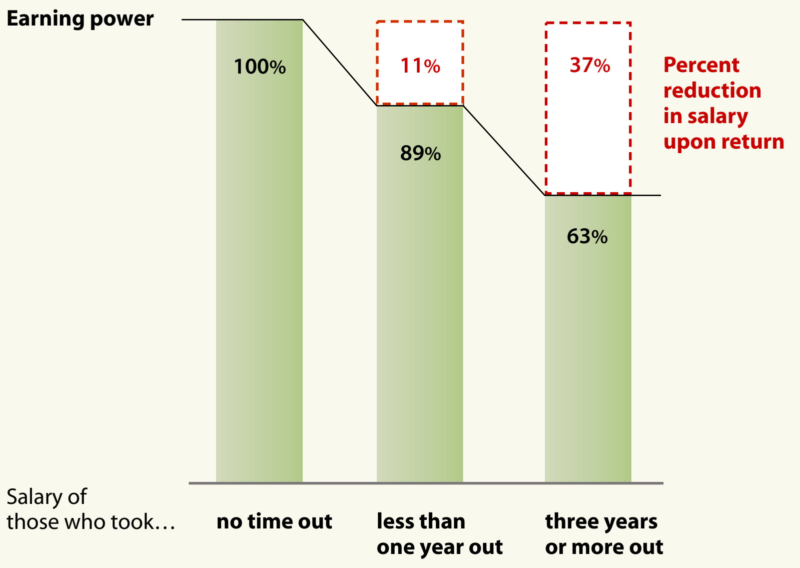
Three years ago, Naomi felt she had no choice but to quit her lucrative position in market research. She had just had a child, and returning to full-time work after the standard maternity leave proved to be well-nigh impossible. Her 55-hour week combined with her husband's 80-hour week didn't leave enough time to raise a healthy child – let alone care for a child who was prone to illness, as theirs was. When her employer denied her request to work reduced hours, Naomi quit.

After nine months at home, Naomi did find some flexible work – but it came at a high price. Her new freelance job as a consultant to an advertising agency barely covered the cost of her son's day care. She now earns a third of what she did three years ago. What plagues Naomi the most about her situation is her anxiety about the future. "Will my skills become obsolete? Will I be able to support myself and my son if something should happen to my husband?"

The scholarly literature shows that Naomi's experience is not unusual. Economist Jane Waldfogel has analyzed the pattern of earnings over the life span. When women enter the workforce in their early and mid twenties they earn nearly as much as men do. For a few years, they almost keep pace. For example, at ages 25 to 29, they earn 87% of the male wage. However, when women start having children, their earnings fall way behind those of men. By the time they reach the 40-to-44 age group, women earn a mere 71% of the male wage. In the words of MIT economist Lester Thurow, "These are the prime years for establishing a successful career. These are the years when hard work has the maximum payoff. They are also the prime years for launching a family. Women who leave the job market during those years may find that they never catch up."

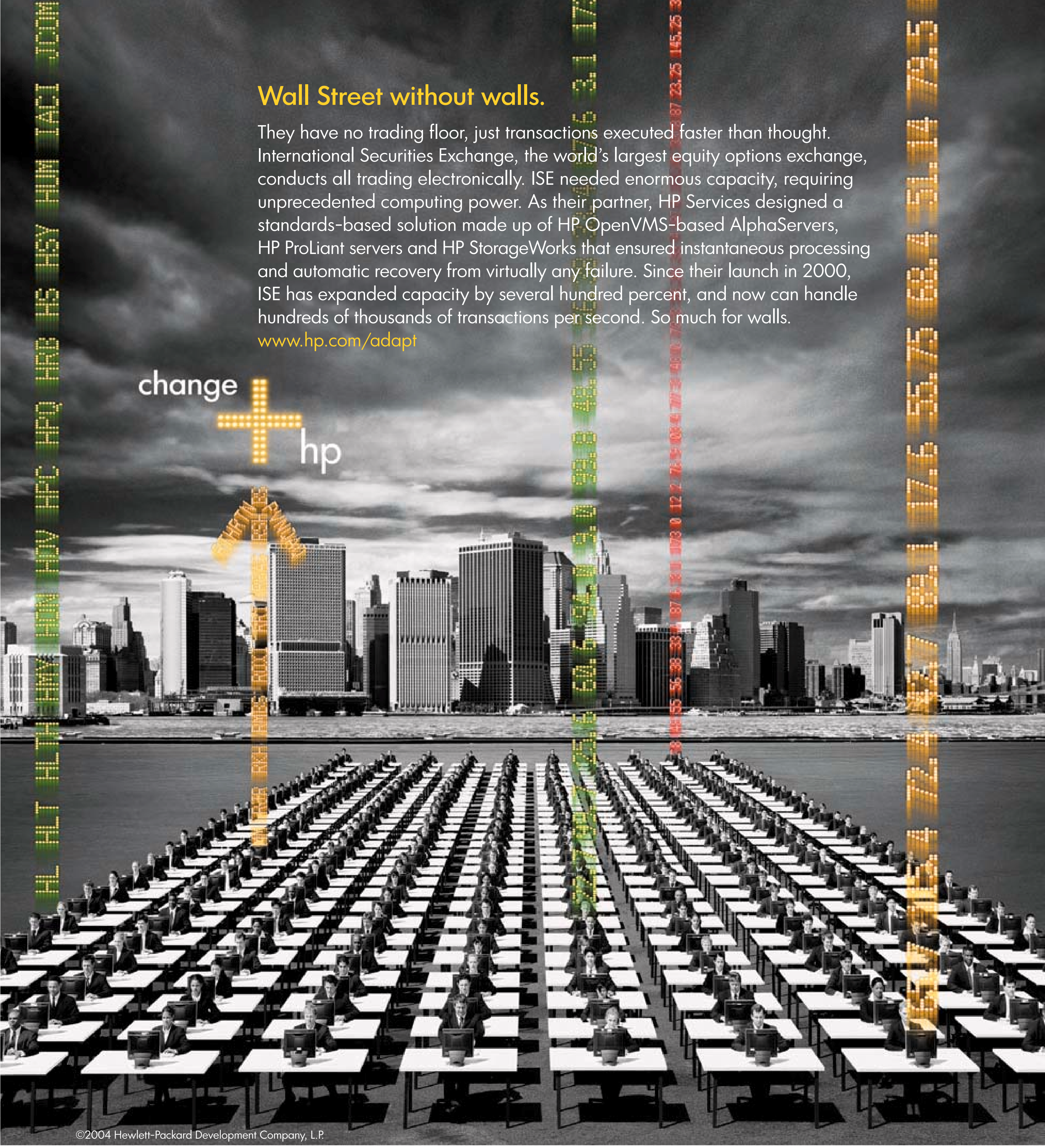
The High Cost of Time Out

Though the average amount of time that women take off from their careers is surprisingly short (less than three years), the salary penalty for doing so is severe. Women who return to the workforce after time out earn significantly less than their peers who remained in their jobs.



Taking the Scenic Route

A majority (58%) of highly qualified women describe their careers as "nonlinear" – which is to say, they do not follow the conventional trajectory long established by successful men. That ladder of success features a steep gradient in one's 30s and steady progress thereafter. In contrast, these women report that


Wall Street without walls.
They have no trading floor, just transactions executed faster than thought. International Securities Exchange, the world's largest equity options exchange, conducts all trading electronically. ISE needed enormous capacity, requiring unprecedented computing power. As their partner, HP Services designed a standards-based solution made up of HP OpenVMS-based AlphaServers, HP ProLiant servers and HP StorageWorks that ensured instantaneous processing and automatic recovery from virtually any failure. Since their launch in 2000, ISE has expanded capacity by several hundred percent, and now can handle hundreds of thousands of transactions per second. So much for walls.
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their "career paths have not followed a progression through the hierarchy of an industry."

Some of this nonlinearity is the result of taking off-ramps. But there are many other ways in which women ease out of the professional fast lane. Our survey reveals that 16% of highly qualified women work part-time. Such arrangements are more prevalent in the legal and medical professions, where 23% and 20% of female professionals work less than full-time, than in the business sector, where only 8% of women work part-time. Another common work-life strategy is telecommuting; 8% of highly qualified women work exclusively from home, and another 25% work partly from home.

Looking back over their careers, 36% of highly qualified women say they have worked part-time for some period of time as part of a strategy to balance work and personal life. Twenty-five percent say they have reduced the number of work hours within a full-time job, and 16% say they have declined a promotion. A significant proportion (38%) say they have deliberately chosen a position with fewer responsibilities and lower compensation than they were qualified for, in order to fulfill responsibilities at home.

Downsizing Ambition

Given the tour of women's careers we've just taken, is it any surprise that women find it difficult to claim or sustain ambition? The survey shows that while almost half of the men consider themselves extremely or very ambitious, only about a third of the women do. (The proportion rises among women in business and the professions of law and medicine; there, 43% and 51%, respectively, consider themselves very ambitious.) In a similar vein, only 15% of highly qualified women (and 27% in the business sector) single out "a powerful position" as an important career goal; in fact, this goal ranked lowest in women's priorities in every sector we surveyed.

Far more important to these women are other items on the workplace wish list: the ability to associate with people they respect (82%); the freedom to "be themselves" at work (79%); and the opportunity to be flexible with their schedules (64%). Fully 61% of women consider it extremely or very important to have the opportunity to collaborate with others and work as part of a team. A majority (56%) believe it is very important for them to be able to give back to the community through their work. And 51% find "recognition from my company" either extremely or very important.

These top priorities constitute a departure from the traditional male take on ambition. Moreover, further analysis points to a disturbing age gap. In the business sector, 53% of younger women (ages 28 to 40) own up to being very ambitious, as contrasted with only 37% of older women. This makes sense in light of Anna Fels's groundbreaking work on women and ambition. In a 2004 HBR article, Fels argues convincingly that ambition stands on two legs – mastery and recognition. To hold onto their dreams, not only must women attain the necessary skills and experience, they must also have their achievements appropriately recognized. To the extent the latter is missing in female careers, ambition is undermined. A vicious cycle emerges: As women's ambitions stall, they are perceived as less committed, they no longer get the best assignments, and this lowers their ambitions further.

In our focus groups, we heard the disappointment – and discouragement – of

women who had reached senior levels in corporations only to find the glass ceiling still in place, despite years of diversity initiatives. These women feel that they are languishing and have not been given either the opportunities or the recognition that would allow them to realize their full potential. Many feel handicapped in the attainment of their goals. The result is the vicious cycle that Fels describes: a "downsizing" of women's ambition that becomes a self-fulfilling prophecy. And the discrepancy in ambition levels between men and women has an insidious side effect in that it results in insufficient role models for younger women.

Reversing the Brain Drain

These, then, are the hard facts. With them in hand, we move from anecdotes to data – and, more important, to a different, richer analytical understanding of the problem. In the structural issue of off-ramps and on-ramps, we see the mechanism derailing the careers of highly qualified women and also the focal point for making positive change. What are the implications for corporate America? One thing at least seems clear: Employers can no longer pretend that treating women as "men in skirts" will fix their retention problems. Like it or not, large numbers of highly qualified, committed women need to take time out. The trick is to help them maintain connections that will allow them to come back from that time without being marginalized for the rest of their careers.

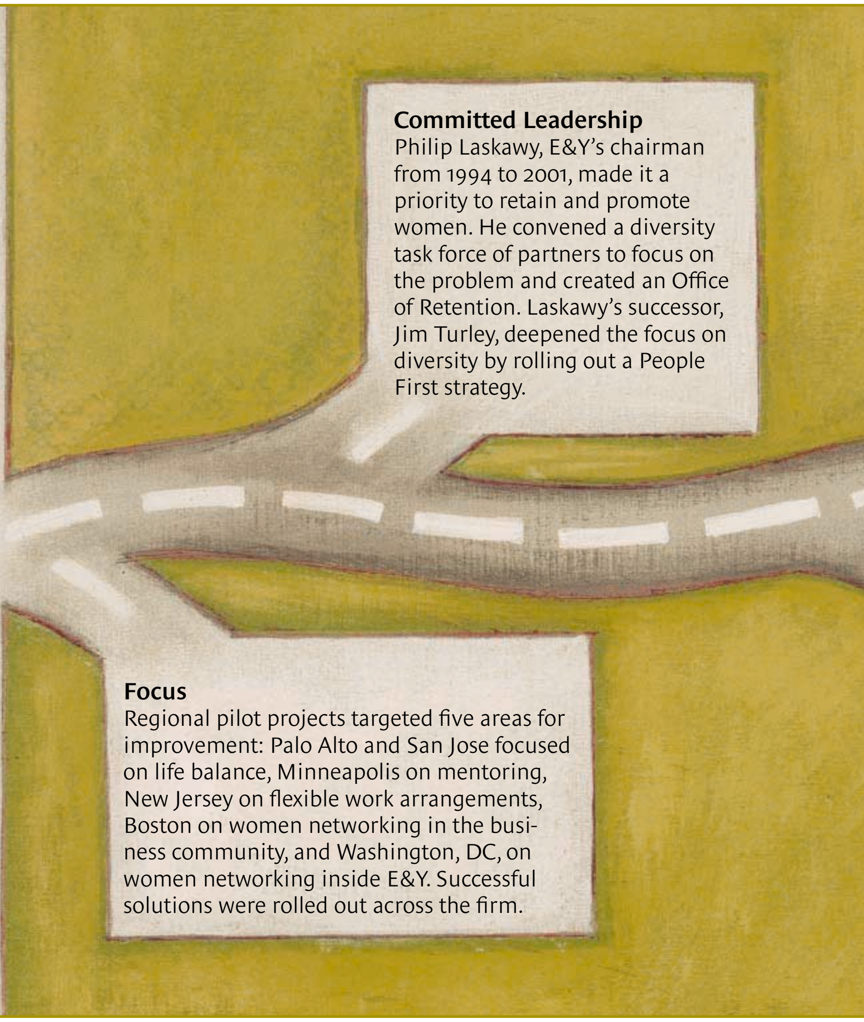
Create reduced-hour jobs. The most obvious way to stay connected is to offer women with demanding lives a way to keep a hand in their chosen field, short of full-time involvement. Our survey found that, in business sectors, fully 89% of women believe that access to reduced-hour jobs is important. Across all sectors, the figure is 82%.

The Johnson & Johnson family of companies has seen the increased loyalty and productivity that can result from such arrangements. We recently held a focus group with 12 part-time managers at these companies and found a level of commitment that was palpable. The women had logged histories with J&J that ranged from eight to 19 years and spoke of the corporation with great affection. All had a focus on productivity and pushed themselves to deliver at the same level they had achieved before switching to part-time. One woman, a 15-year J&J veteran, was particularly eloquent in her gratitude to the corporation. She had had her first child at age 40 and, like so many new mothers, felt

How Ernst & Young Keeps Women on the Path to Partnership

In the mid-1990s, turnover among female employees at Ernst & Young was much higher than it was among male peers. Company leaders knew something was seriously wrong; for many years, its entering classes of young auditors had been made up of nearly equal numbers of men and women – yet it was still the case that only a tiny percentage of its partnership was female. This was a major problem. Turnover in client-serving roles meant lost continuity on work assignments. And on top of losing talent that the firm had invested in training, E&Y was incurring costs averaging 150% of a departing employee's annual salary just to fill the vacant position.

E&Y set a new course, marked by several important features outlined here. Since E&Y began this work, the percentage of women partners has more than tripled to 12% and the downward trend in retention of women at every level has been reversed. E&Y now has four women on the management board, and many more women are in key operating and client serving roles. Among its women partners, 10% work on a flexible schedule and more than 20 have been promoted to partner while working a reduced schedule. In 2004, 22% of new partners were women.



Committed Leadership
Philip Laskawy, E&Y's chairman from 1994 to 2001, made it a priority to retain and promote women. He convened a diversity task force of partners to focus on the problem and created an Office of Retention. Laskawy's successor, Jim Turley, deepened the focus on diversity by rolling out a People First strategy.

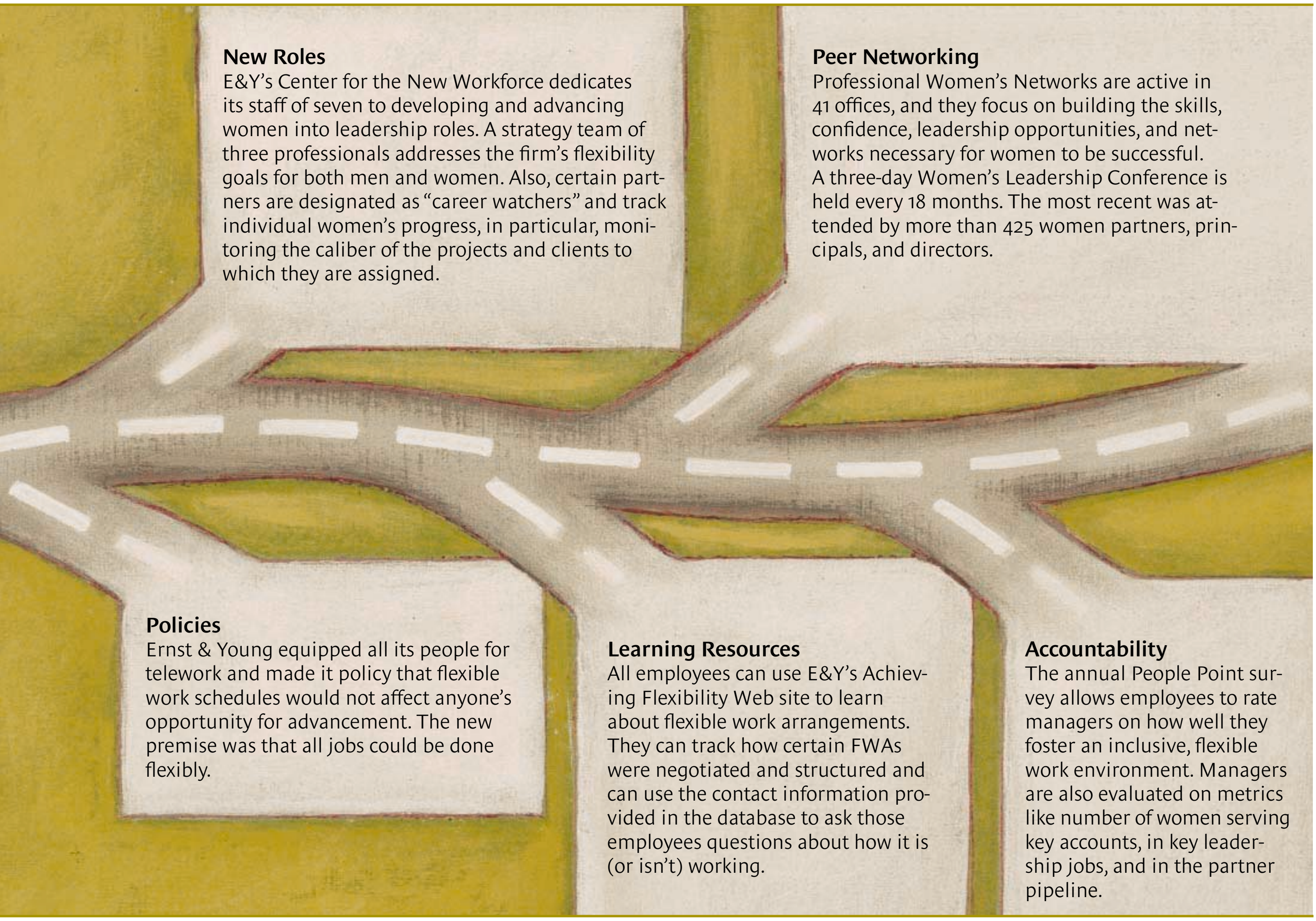
Focus
Regional pilot projects targeted five areas for improvement: Palo Alto and San Jose focused on life balance, Minneapolis on mentoring, New Jersey on flexible work arrangements, Boston on women networking in the business community, and Washington, DC, on women networking inside E&Y. Successful solutions were rolled out across the firm.

torn apart by the conflicting demands of home and work. In her words, "I thought I only had two choices – work full-time or leave – and I didn't want either. J&J's reduced-hour option has been a savior." All the women in the room were clear on one point: They would have quit had part-time jobs not been available.

At Pfizer, the deal is sweetened further for part-time workers; field sales professionals in the company's Vista Rx division are given access to the same benefits and training as full-time employees but work 60% of the hours (with a corresponding difference in base pay). Many opt for a three-day workweek; others structure their working day around children's school hours. These 230 employees – 93% of whom are working mothers – remain eligible for promotion and may return to full-time status at their discretion.

Provide flexibility in the day. Some women don't require reduced work hours; they merely need flexibility in when, where, and how they do their work. Even parents who employ nannies or have children in day care, for example, must make time for teacher conferences, medical appointments, volunteering, child-related errands – not to mention the days the nanny calls in sick or the day care center is closed. Someone caring for an invalid or a fragile elderly person may likewise have many hours of potentially productive time in a day yet not be able to stray far from home.

For these and other reasons, almost two-thirds (64%) of the women we surveyed cite flexible work arrangements as being either extremely or very important to them. In fact, by a considerable margin, highly qualified women find flexibility more important than compensation; only 42% say that "earning a lot of money" is an important motivator. In our focus groups, we heard women use terms like "nirvana" and "the golden ring" to describe employment arrangements that allow them to flex their workdays, their workweeks, and their careers. A senior employee who recently joined Lehman Brothers' equity division is an example. She had been working at another financial services company when a Lehman recruiter called. "The person who had been in the job previously was working one day a week from home, so they offered that opportunity to me. Though I was content in my current job," she told us, "that intriguing possibility made me reevaluate. In the end, I took the job at Lehman. Working from home one day a week was a huge lure."



Provide flexibility in the arc of a career. Booz Allen Hamilton, the management and technology consulting firm, recognized that it isn't simply a workday, or a workweek, that needs to be made more flexible. It's the entire arc of a career.

Management consulting as a profession loses twice as many women as men in the middle reaches of career ladders. A big part of the problem is that, perhaps more than in any other business sector, it is driven by an up-or-out ethos; client-serving professionals must progress steadily or fall by the wayside. The strongest contenders make partner through a relentless winnowing process. While many firms take care to make the separations as painless as possible (the chaff, after all, tends to land in organizations that might employ their services), there are clear limits to their patience. Typically, if a valued professional is unable to keep pace with the road warrior lifestyle, the best she can hope for is reassignment to a staff job.

Over the past year, Booz Allen has initiated a "ramp up, ramp down" flexible program to allow professionals to balance work and life and still do the client work they find most interesting. The key to the program is Booz Allen's effort to "unbundle" standard consulting projects and identify chunks that can be done by telecommuting or shorts stints in the office. Participating professionals are either regular employees or alumni that sign standard employment contracts and are activated as needed. For the professional, it's a way to take on a manageable amount of the kind of work they do best. For Booz Allen, it's a way to maintain ties to consultants who have already proved their merit in a challenging profession. Since many of these talented women will eventually return to full-time consulting employment, Booz Allen wants to be their employer of choice – and to keep their skills sharp in the meantime.

When asked how the program is being received, DeAnne Aguirre, a vice president at Booz Allen who was involved in its design (and who is also a member of our task force), had an instant reaction: "I think it's instilled new hope – a lot of young women I work with no longer feel that they will have to sacrifice some precious part of themselves." Aguirre explains that trade-offs are inevitable, but at Booz Allen an off-ramping decision doesn't have to be a devastating one anymore. "Flex careers are bound to be slower than conventional ones, but in ten years' time you probably won't remember the precise year you made partner. The point here is to remain on track and vitally connected."

Remove the stigma. Making flexible arrangements succeed over the long term is hard work. It means crafting an imaginative set of policies, but even more important, it means eliminating the stigma that is often attached to such nonstandard work arrangements. As many as 35% of the women we surveyed report various aspects of their organizations' cultures that effectively penalize people who take advantage of work-life policies. Telecommuting appears to be most stigmatized, with 39% of women reporting some form of tacit resistance to it, followed by job sharing and part-time work. Of flexible work arrangements in general, 21% report that "there is an unspoken rule at my workplace that people who use these options will not be promoted." Parental leave policies get more respect – though even here, 19% of women report cultural or attitudinal barriers to taking the time off that they are entitled to. In environments where flexible work arrangements are tacitly deemed illegitimate, many women would rather resign than request them.

Only 5% of highly qualified women looking for on-ramps are interested in rejoining the companies they left. In business sectors, that percentage is zero.

Interestingly, when it comes to taking advantage of work-life policies, men encounter even more stigma. For example, 48% of the men we surveyed perceived job sharing as illegitimate in their workplace culture – even when it's part of official policy.

Transformation of the corporate culture seems to be a prerequisite for success on the work-life front. Those people at or near the top of an organization need to have that "eureka" moment, when they not only understand the business imperative for imaginative work-life policies but are prepared to embrace them, and in so doing remove the stigma. In the words of Dessa Bokides, treasurer at Pitney Bowes, "Only a leader's devotion to these issues will give others permission to transform conventional career paths."

Stop burning bridges. One particularly dramatic finding of our survey deserves special mention: Only 5% of highly qualified women looking for on-ramps are interested in rejoining the companies they left. In business sectors, that percentage is zero. If ever there was a danger signal for corporations, this is it.

The finding implies that the vast majority of off-ramped women, at the moment they left their careers, felt ill-used – or at least underutilized and unappreciated – by their employers. We can only speculate as to why this was. In some cases, perhaps, the situation ended badly; a woman, attempting impossible juggling feats, started dropping balls. Or an employer, embittered by the loss of too many "star" women, lets this one go much too easily.

It's understandable for managers to assume that women leave mainly for "pull" reasons and that there's no point in trying to keep them. Indeed, when family overload and the traditional division of labor place unmanageable demands on a working woman, it does appear that quitting has much more to do with what's going on at home than what's going on at work. However, it is important to realize that even when pull factors seem to be dominant, push factors are also in play. Most off-ramping decisions are conditioned by policies, practices, and attitudes at work. Recognition, flexibility, and the opportunity to telecommute – especially when endorsed by the corporate culture – can make a huge difference.

The point is, managers will not stay in a departing employee's good graces unless they take the time to explore the reasons for off-ramping and are able and willing to offer options short of total severance. If a company wants future access to this talent, it will need to go beyond the perfunctory exit interview and, at the very least, impart the message that the door is open. Better still, it will maintain a connection with off-ramped employees through a formal alumni program.

Provide outlets for altruism. Imaginative attachment policies notwithstanding, some women have no interest in returning to their old organizations because their desire to work in their former field has waned. Recall the focus group participants who spoke of a deepened desire to give back to the community after taking a hiatus from work. Remember, too, that women in business sectors are pushed off track more by dissatisfaction with work than pulled by external demands. Our data suggest that fully 52% of women with MBAs in the business sector cite the fact that they do not find their careers "either satisfying or enjoyable" as an important reason for why they left work. Perhaps not surprisingly, then, a majority (54%) of the women looking for on-ramps want to change their profession or field. And in most of those cases, it's a woman who formerly worked in the corporate sphere hoping to move into the not-for-profit sector.

Employers would be well advised to recognize and harness the altruism of these women. Supporting female professionals in their advocacy and public service efforts serves to win their energy and loyalty. Companies may also be able to redirect women's desire to give back to the community by asking them to become involved in mentoring and formal women's networks within the company.

Nurture ambition. Finally, if women are to sustain their passion for work and their competitive edge – whether or not they take formal time out – they must keep ambition alive. Our findings point to an urgent need to implement mentoring and networking programs that help women expand and sustain their professional aspirations. Companies like American Express, GE, Goldman Sachs, Johnson & Johnson, Lehman Brothers, and Time Warner are developing "old girls networks" that build skills, contacts, and confidence. They link women to inside power brokers and to outside business players and effectively inculcate those precious rainmaking skills.

Networks (with fund-raising and friend-raising functions) can enhance client connections. But they also play another, critical role. They provide the infrastructure within which women can earn recognition, as well as a safe platform from which to blow one's own horn without being perceived as too pushy. In the words of Patricia Fili-Krushel, executive vice president of Time Warner, "Company-sponsored women's networks encourage women to cultivate both sides of the power equation. Women hone their own leadership abilities but also learn to use power on behalf of others. Both skill sets help us increase our pipeline of talented women."

Adopt an On-Ramp

As we write this, market and economic factors, both cyclical and structural, are aligned in ways guaranteed to make talent constraints and skill shortages huge issues again. Unemployment is down and labor markets are beginning to tighten, just as the baby-bust generation is about to hit "prime time" and the number of workers between the ages of 35 to 45 is shrinking. Immigration levels are stable, so there's little chance of relief there. Likewise, productivity improvements are flattening. The phenomenon that bailed us out of our last big labor crunch – the entry for the first time of millions of women into the labor force – is not available to us again. Add it all up, and CEOs are back to wondering how they will find enough high-caliber talent to drive growth.

There is a winning strategy. It revolves around the retention and reattachment of highly qualified women. America these days has a large and impressive pool of female talent. Fifty-eight percent of college graduates are now women, and nearly half of all professional and graduate degrees are earned by women. Even more important, the incremental additions to the talent pool will be disproportionately female, according to figures released by the U.S. Department of Education. The number of women with graduate and professional degrees is projected to grow by 16% over the next decade, while the number of men with these degrees is projected to grow by a mere 1.3%. Companies are beginning to pay attention to these figures. As Melinda Wolfe, head of global leadership and diversity at Goldman Sachs, recently pointed out, "A large part of the potential talent pool consists of females and historically underrepresented groups. With the professional labor market tightening, it is in our direct interest to give serious attention to these matters of retention and reattachment."

In short, the talent is there; the challenge is to create the circumstances that allow businesses to take advantage of it over the long run. To tap this all-important resource, companies must understand the complexities of women's nonlinear careers and be prepared to support rather than punish those who take alternate routes.

The complete statistical findings from this research project, and additional commentary and company examples, are available in an HBR research report entitled "The Hidden Brain Drain: Off-Ramps and On-Ramps in Women's Careers" (see www.womenscareersreport.hbr.org).

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"Not to worry. It's the good kind of stress."

MARK LITZLER

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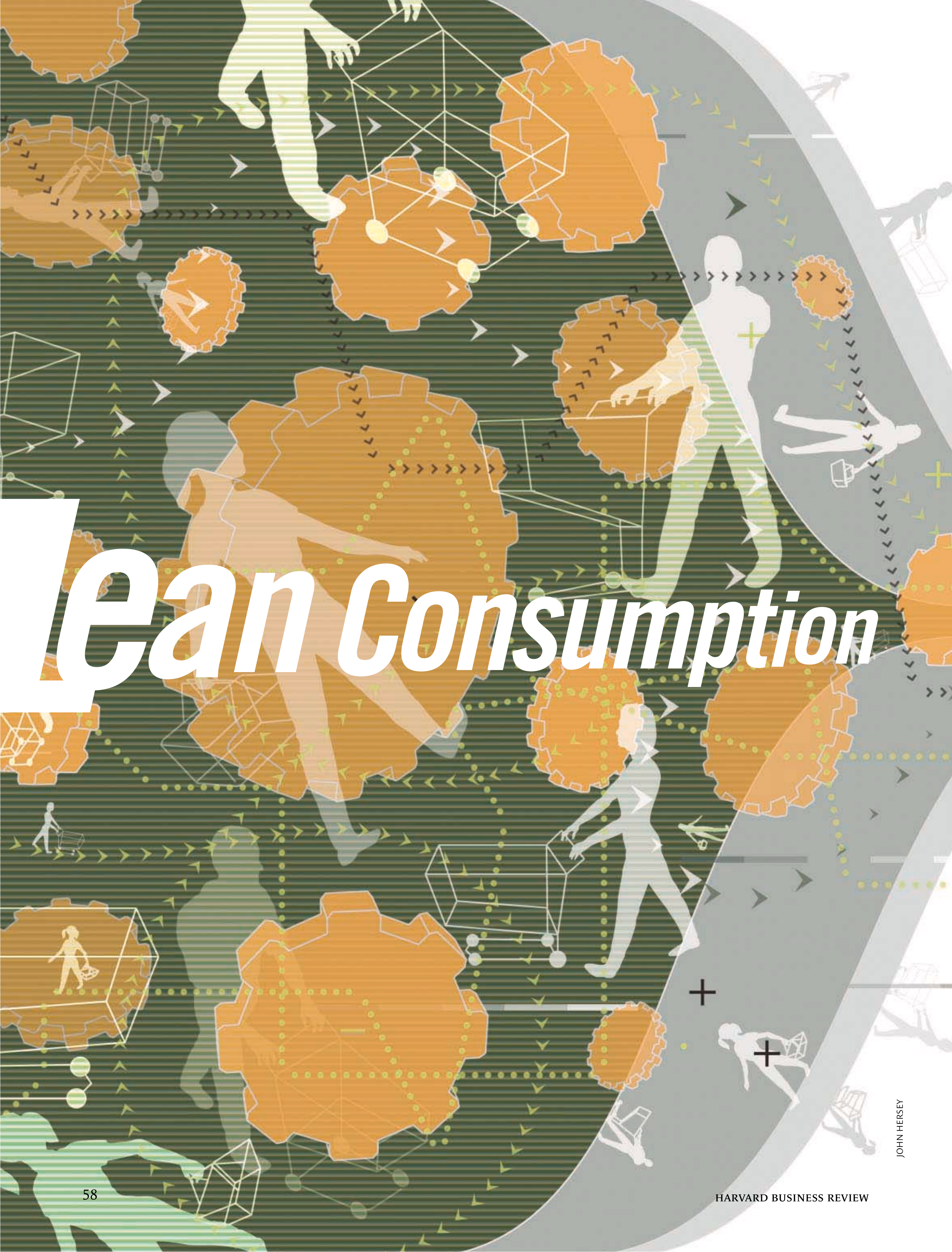
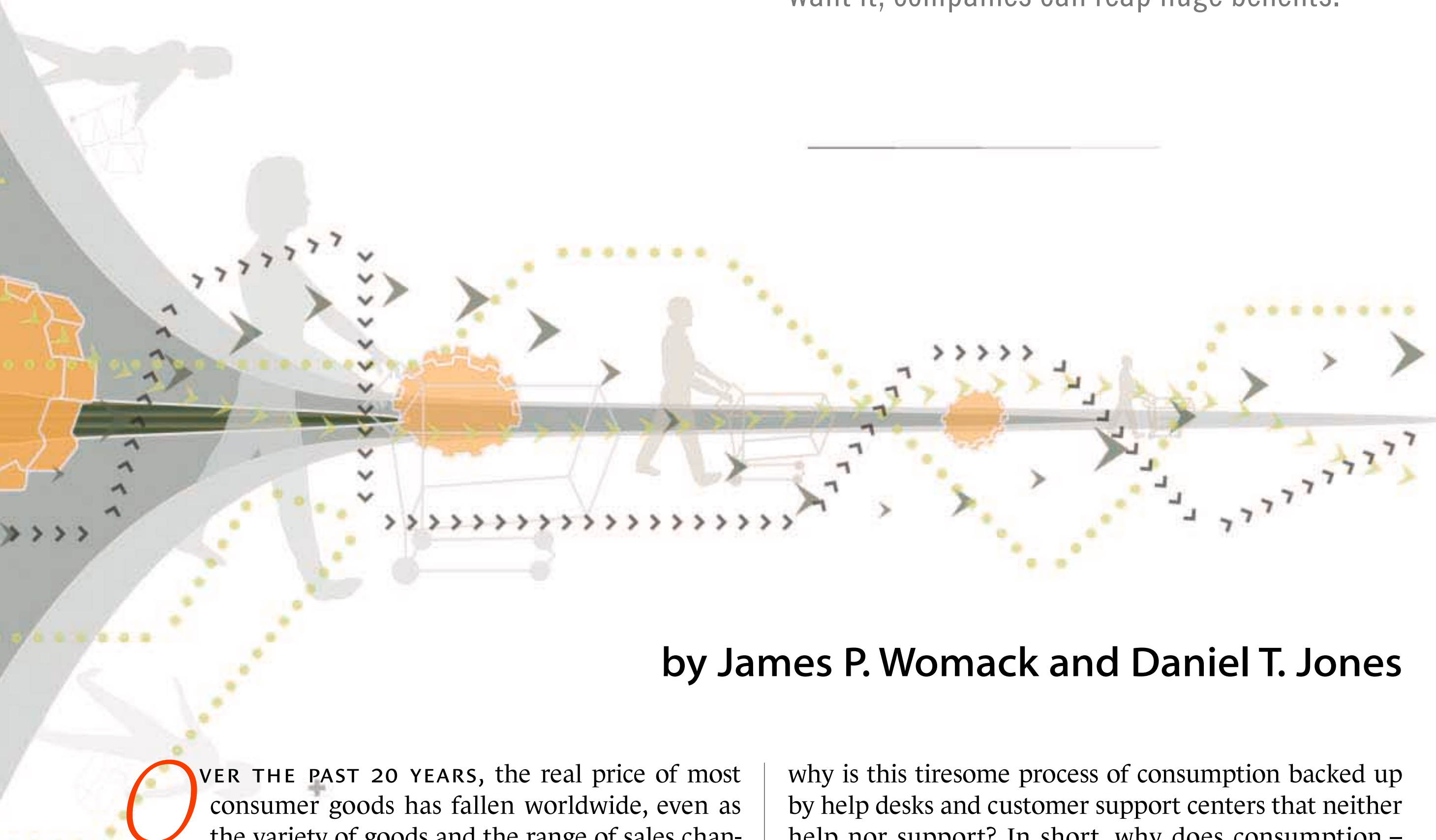


Lean Consumption

JOHN HERSEY

Lean production transformed manufacturing. **Now it's time to apply lean thinking to the processes of consumption.** By minimizing customers' time and effort and delivering exactly what they want when and where they want it, companies can reap huge benefits.



by James P. Womack and Daniel T. Jones

OVER THE PAST 20 YEARS, the real price of most consumer goods has fallen worldwide, even as the variety of goods and the range of sales channels offering them have continued to grow. Meanwhile, product quality – in the sense of durability and number of delivered defects – has steadily improved.

So, if consumers have access to an ever-growing range of products at lower prices, with fewer lemons, and from more formats, why is consumption often so frustrating? Why do we routinely encounter the custom-built computer that refuses to work with the printer, the other computers in the house, and the network software? Why does the simple process of getting the car fixed require countless loops of miscommunication, travel, waiting, and defective repairs? Why does the diligent shopper frequently return from a store stocking thousands of items without having found the one item that was wanted? And why is this tiresome process of consumption backed up by help desks and customer support centers that neither help nor support? In short, why does consumption – which should be easy and satisfying – require so much time and hassle?

It doesn't have to – and shouldn't. Companies may think that they save time and money by off-loading work to customers, making it the customer's problem to get the computer up and running, and wasting the customer's time. In fact, however, the opposite is true. By streamlining the systems for providing goods and services, and making it easier for customers to buy and use them, a growing number of companies are actually lowering costs while saving everyone's time. In the process, these businesses are learning more about their customers, strengthening consumer loyalty, and attracting new customers who defect from less user-friendly competitors.

What these companies are doing has a familiar feel: Just as businesses around the world have embraced the principles of lean production to squeeze inefficiency out of manufacturing processes, these innovative companies are streamlining the processes of consuming. In the early 1990s we popularized the term *lean production* to describe the ultra-efficient process management of our exemplar firm, Toyota. We believe it is now time to recognize *lean consumption* as its necessary and inevitable complement.

"But surely," you say, "when it comes to consumption, less can't be more." Actually it can be, for both consumer and provider. Lean consumption isn't about reducing the amount customers buy or the business they bring. Rather, it's about providing the full value that consumers desire from their goods and services, with the greatest efficiency and least pain.

The key word here is "process." Think about consumption not as an isolated moment of decision about purchasing a specific product, but as a continuing process linking many goods and services to solve consumer problems. When a person buys a home computer, for example, this is not a onetime transaction. The individual has embarked on the arduous process of researching, obtaining, integrating, maintaining, upgrading, and, finally, disposing of this purchase. For producers and providers (whether employees, managers, or entrepreneurs), developing lean consumption processes requires determining how to configure linked business activities, especially across firms, to meet customer needs without squandering their own – or the consumer's – time, effort, and resources.

The way to do this is to tightly integrate and streamline the processes of provision and consumption. The challenge is not simply logistical: Lean consumption requires a fundamental shift in the way retailers, service providers, manufacturers, and suppliers think about the relationship between provision and consumption, and the role their customers play in these processes. It also requires consumers to change the nature of their relationships with the companies they patronize. Customers and providers must start collaborating to minimize total cost and wasted time and to create new value.

That may seem like a doubtful proposition. But some companies – along with their customers – have started the culture shift that will make lean consumption possible. And they're finding that everybody wins.

Some companies – along with their customers – **have started the culture shift that will make lean consumption possible.** And they're finding that everybody wins.

Why Lean Consumption Now?

While lean consumption would be a sensible idea in any era, we see several convergent trends that we think make it inevitable and, indeed, a competitive necessity now.

With the regulated economy steadily contracting, consumers have a broader range of decisions to make, from how to invest retirement funds, to what telecommunications provider to use, to what airline to fly at what price. At the same time, they must cope with a growing profusion of choices as producers relentlessly customize their offerings, pursue product niches, and increase their sales channels.

In this demanding environment, information technology is steadily blurring the distinction between consumption and production. Consumers are doing increasing amounts of unpaid work on behalf of providers, such as entering data into Web-based order forms and tracking the progress of their own orders. And these consumers are spending more and more time and energy to obtain and maintain the computers, printers, PDAs, and other technological tools needed to solve routine problems – for themselves *and* for providers.

This growing burden on consumers might be sustainable if not for the changes consumers themselves are undergoing. Household configurations in every advanced economy are transforming in ways that create additional time pressures and energy drains. Two-wage-earner and single-parent households, where no one has time to manage consumption, are increasingly common; and aging populations are confronted with an expanding array of choices but have declining energy to address them.

Collectively, these trends give rise to the consumer's emerging dilemma of more choices to make and products to manage with decreasing time and energy. Yet the situation also creates a major opportunity for providers.

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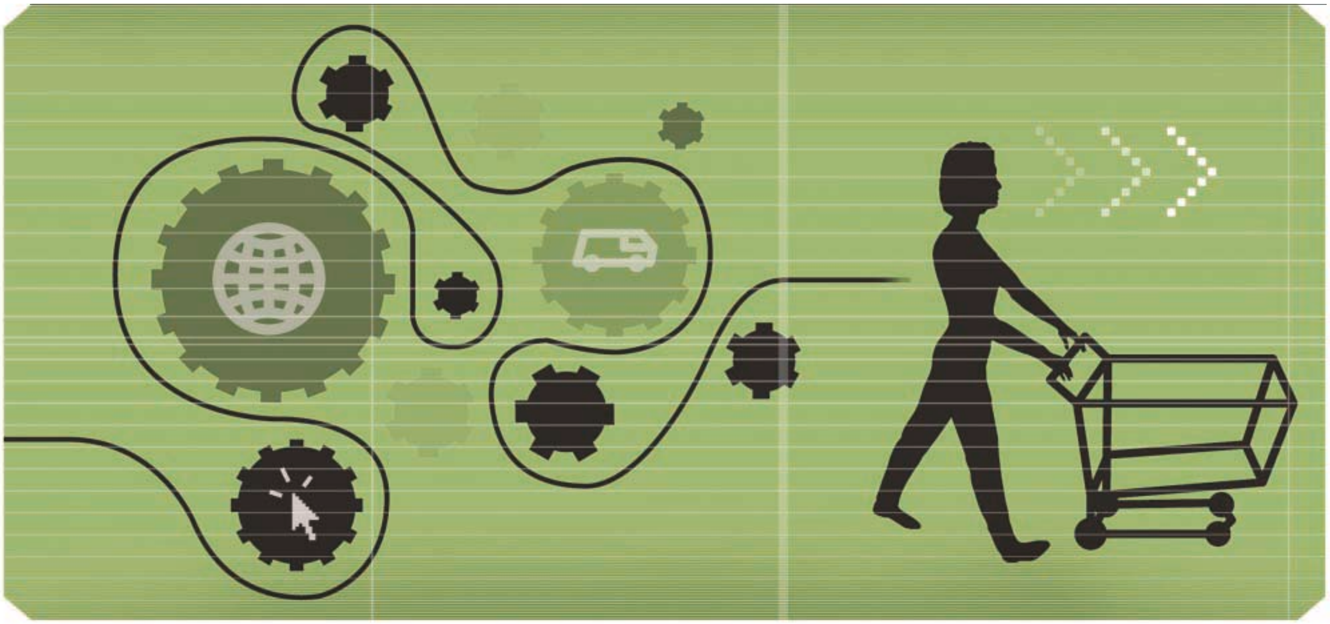


The Principles of Lean Consumption

The concepts underlying lean consumption boil down to six simple principles that correspond closely with those of lean production. (For more on these principles, see our book *Lean Thinking.*)

1. Solve the customer's problem completely by insuring that all the goods and services work, and work together.
2. Don't waste the customer's time.
3. Provide exactly *what* the customer wants.
4. Provide what's wanted exactly *where* it's wanted.
5. Provide what's wanted where it's wanted exactly *when* it's wanted.
6. Continually aggregate solutions to reduce the customer's time and hassle.

Let's examine these principles one at a time.

Solve the customer's problem completely by insuring that all the goods and services work, and work together. Customers obtain goods and services to solve problems in their lives. But they don't acquire them in a single transaction. Instead they search for, obtain, install, integrate, maintain, and dispose of them over an extended period – which is a lot more complicated. We don't just buy a car or a home in an hour to solve our mobility and shelter problems. Rather, we search at length, find the right item, purchase it, and begin immediately to maintain, repair, and upgrade it over an extended period as our needs change.

This complex process rarely goes smoothly. Consider personal computing, which now involves your camera, your PDA, and your phones. Most of us are less interested in the specific features of all these items than providers seem to think. What we really want is for everything (hardware, software, and support services) to work together reliably and seamlessly with minimal drain on our time and emotions. Yet we struggle endlessly with multiple providers of goods and services for our information and communication problems, all of which require our continuous unpaid management.

Why is this? Because providers, instead of working together to perfect the entire consumption process, have created an enormous "failure industry" of help lines and service desks to deal with their individual piece of the solution. Their objective has been ever-greater efficiency (in terms of their own resources) at patching recurring customer problems. Their management goal has been to minimize the time needed to get the customer off the line while avoiding the hard work of getting to the root cause of the problem.

Lean consumption principles suggest a radically different approach. Rather than assigning the least knowledgeable personnel to deal repetitively (but "efficiently") with the same customer problems, a lean provider deploys highly trained personnel who not only solve the customer's specific problem but also identify its systemic source. Management can then put permanent fixes in place, integrating the various elements of the solution, so that consumers no longer need to complain.

This approach has been pursued brilliantly by Fujitsu Services, a leading global provider of outsourced customer service. Companies that contract with Fujitsu to manage their in-house IT help desks find that the number of calls their desks receive about a recurring problem inside the company – say malfunctioning printers – often falls to near zero. What Fujitsu does is identify and fix the *source* of the problem – for example, replace the flawed printers with new ones fit for the particular purpose. By seeking the root cause of the problem somewhere up the value stream (often involving multiple companies), Fujitsu has pioneered a way to eliminate it. (See the sidebar "Solving Problems at the Source.")

Don't waste the customer's time. Providers typically send a very clear message to customers: "Your time has no value." Just think of when you last had your car repaired. You called to make an appointment, took your vehicle to a dealer, went through numerous queues to explain the problem, arranged for a loaner vehicle or a ride to your destination, and then waited for the dreaded call with the diagnosis and cost of the repair. When you went to pick up the vehicle, you may have found that it wasn't ready. Or you may have waited in several queues (again) to pay for and collect the car, only to discover later that the repair had not been done right. (Surveys show that car repairs are done correctly and on time only six times out of ten.) The dealer squandered your valuable time – and goodwill.

The lean provider takes a different approach by looking at the problem from the standpoint of the customer and drawing a "consumption map" of all the steps in the repair process. Then, in each instance where the customer is forced to expend time for no return in value, the provider asks how the system can be reconfigured to eliminate wasted time.

Most managers instinctively assume that this will raise their costs, but the reality is just the opposite. Purging inefficiency from the "provision stream" – the steps needed to create and deliver goods or services – solves providers' problems even as it helps customers. All those endless queues entail needless work for staff, and reworking jobs done wrong is even more expensive. By marrying a lean provision stream to a lean consumption stream (all the actions that must be taken by the consumer to acquire goods or services), providers can usually reduce their costs – and lower prices to consumers.

Skeptical? Take at look at Grupo Fernando Simão (GFS), a family-owned automobile dealer group based in Oporto, Portugal. GFS is the third-largest dealer group in Portugal, with 900 employees and group sales now more than $400 million. Since 1999, the company has introduced lean provision and consumption practices throughout its entire business. By prediagnosing every

Solving Problems at the Source

Fujitsu Services is one of the largest providers of IT services in Europe, the Middle East, and Africa, with 15,400 employees in 30 countries and sales of $4.2 billion in 2004. After providing technical support for its own products for many years, Fujitsu began to offer services to companies that were outsourcing their customer service and technical support activities. Here Fujitsu has often found itself playing the difficult role of mediating between hardware and software vendors and users about the problems the latter encountered. Typically, firms like Fujitsu are paid to respond to user complaints at the lowest cost per complaint handled. This call center model gives firms no reason to reduce the number of complaints received and, indeed, creates a disincentive: If the call volume falls, so does the service company's revenue. Fujitsu approached the problem with a completely different mind-set. It decided to eliminate the root causes of callers' complaints.

When Fujitsu took over the help desk contract in 2001 for BMI (an airline formerly known as BMI British Midland), Fujitsu immediately analyzed the different types of calls coming in from BMI employees. Then it set to work to understand the problems that gave rise to the calls; to track the time and effort required to fix them; and, most important, to measure the impact on the business of failures or delays in doing so. (Note that in this example, the users being helped are BMI employees, such as the check-in staff. Operationally, this works the same way as help lines serving customers at, say, Dell or Microsoft.)

Fujitsu found that more than half the calls to help desks were repeat complaints about recurring problems or repair delays. One of the most common reasons for calls – accounting for 26% of the total – was malfunctioning printers: Ticketing agents kept finding that they couldn't print boarding passes and baggage tags for passengers at check-in. It was immediately apparent that solving the printer problem was critical to the airline's business. Given tight airport security, the inability to print boarding passes and baggage tags that could be scanned at a number of points could cause flights to miss their takeoff slots.

Under BMI's previous contractor, the help desk had struggled to get service technicians to respond more quickly so check-in staff wouldn't keep calling with complaints. Fujitsu's response was to find the most cost-effective way to eliminate the root cause of the printer problem. The answer was to convince BMI senior management to spend money up front to install better printers. As a result, the number of calls about malfunctioning printers was cut by more than 80% within 18 months. This action translated into major savings in flight operations far exceeding the cost of the new printers. In addition, Fujitsu improved the technician-response process so that the average time needed to fix printers that still failed fell from ten hours to three.

Fujitsu coupled this problem-solving approach with a different business proposition for BMI. Instead of being paid for each call handled, Fujitsu asked to be paid a set car repair whenever possible, scheduling to eliminate queues, standardizing repair processes, and introducing other lean practices, GFS has removed many wasteful steps, increased the speed at which customers and vehicles move through the system, and reduced the total cost to the company of the typical repair by 30%.

This approach yields more than just a cost savings for GFS: It's a boon for customers. The prices customers pay for repairs have fallen – especially in terms of wasted time – and most jobs are now fixed right the first time. Before these changes, a customer could expect to spend about two hours searching for a repair shop, making an appointment, getting the car to the dealer, negotiating the repair, and collecting the vehicle at the end of the process. GFS's lean repair process has cut customers' time commitments almost by half – to an average of 69 minutes. As a result, GFS has climbed from near the bottom of the car manufacturers' customer-service rankings to the top and has dramatically increased its share of the service business for vehicles it sells. (See the sidebar "Drawing a Lean Consumption Map.")

fee based on the number of *potential* callers to the BMI system. This allowed Fujitsu to profitably offer BMI a lower bid than its current vendor.

By addressing root causes, Fujitsu reduced total calls to the help desk by 40% within 18 months and improved customer satisfaction. As the company has progressively applied this problem-solving approach to all of its customers, it has moved beyond its original role as a mediator between vendors and frustrated consumers to become an analyst and optimizer of entire IT response systems. Fujitsu is solving the customer's problem completely – and then some.

While discussing a customer's current problem, for example, Fujitsu personnel pass on new information about the user's computing systems, including how to prevent problems the customer hasn't yet encountered but will, if not warned. At the same time, Fujitsu can learn more about what problems the customer is trying to solve with the system, which can lead to ideas for new products. Instead of simply fixing defects so that customers get the value originally promised, Fujitsu creates *new* value by offering them additional information and services they might want. What starts as a negative customer interaction can turn into an opportunity for information sharing that builds loyalty, generates fresh market intelligence, and saves Fujitsu money. As a result, satisfied clients have rewarded Fujitsu with extra work previously divided among competing subcontractors – a win-win for both parties.

Provide exactly *what* the customer wants. You may think that if current consumption systems do anything well it is to get customers the exact items they want. Not true. For example, the average item in a typical grocery store is in stock at the right location on the shelf only 92% of the time (this is called the "level of service"). Given that the average shopper has 40 items on a list, multiply the probabilities of finding each of the 40 items together and it's apparent that obtaining all of the items in the same shopping trip will happen only one time in 20. You can buy substitutes, or make additional trips, or change what you plan to eat, but the store is not giving you exactly what you want.

Shoe stores don't do any better. By relocating most production for North America and Europe to Southeast Asia and putting retailers on 150-day order windows, the shoe industry has created a marvel of low cost at the factory gate in combination with an extraordinary array of styles (about half of which only endure for one three-month selling season). But suppose you want the size nine "Wonder Wings" in gray? The chances are only 80% (an industry average) that they will be in stock; and there is a good possibility (because of the long order window) that they will never be in stock again. Not to worry, though. There are millions of size nine Wonder Wings in pink available and many more on the way because the order flow, once turned on, cannot be turned off and the replenishment cycle is so long. As a result, the shoe industry fails to get one customer in five the product he or she actually wants, while it remainders 40% of total production (pink Wonder Wings, for example) through secondary channels at much lower revenues.

There will certainly be differences among industries in the difficulty of implementing lean consumption. But even in those where lean provision seems impractical, there are likely to be practical, if counterintuitive, solutions. Consider that Nike can now profitably deliver even customized bags overnight anywhere in North America. How? By – of all things – locating manufacturing in California. (See the sidebar "Locating for Lean Provision.")

Whatever the industry, the lean provider's approach has a common theme: pull. Rather than infrequently ordering large numbers of items based on very sophisticated centralized forecasts (which are almost always wrong), the lean provider puts in place rapid replenishment systems that quickly restock exactly what a customer has just pulled from the shelf. This is not just a warehousing problem. It's a total-system issue of multiple replenishment loops running all the way back to raw materials. These loops permit a business to quickly restock at every level what the next downstream customer actually wants, as shown by what a previous customer just used.

Tesco, a UK-based retailer, is the world leader in applying these principles and is now approaching a level of service of more than 96%. That's still not good enough to get

Drawing a Lean Consumption Map

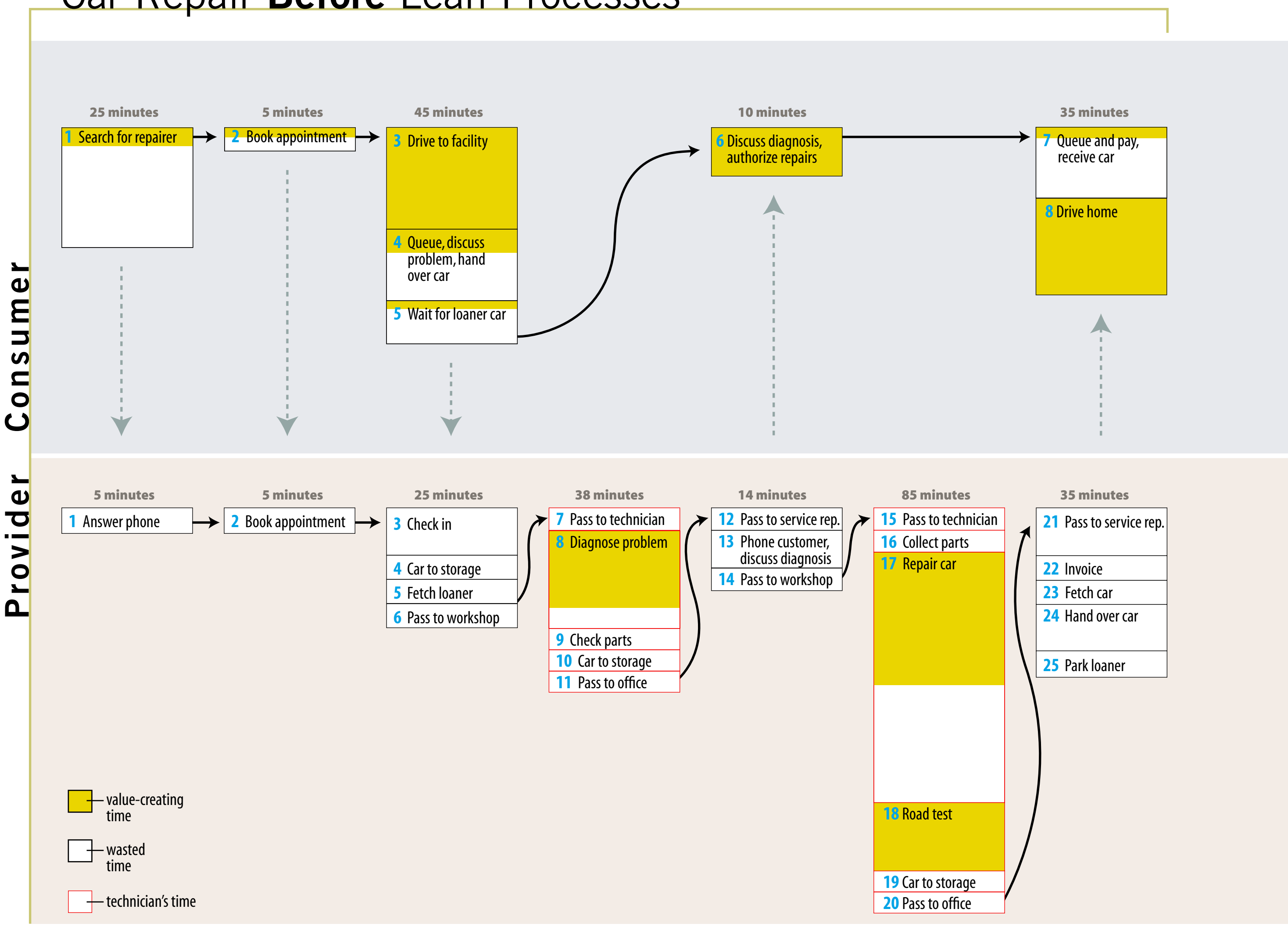
Mapping the steps in a production and consumption process is the best way to see opportunities for improvement. A map can reveal how broken processes waste providers' and consumers' time and money.

Here's how Grupo Fernando Simão (GFS), a Portuguese automobile dealer group, discovered the inefficiencies in its processes. First, the company looked at consumption. It listed the steps a typical consumer takes to get a car fixed – from searching for a repair shop to arriving home with the vehicle repaired – and the time required for each. Then GFS drew boxes representing the eight steps it identified, sized each box in proportion to the time needed to complete the corresponding task, and shaded in the value-creating time. The company also collected data on the percentage of jobs done right the first time and on time.

GFS found that these consumption steps took the average consumer a total of 120 minutes. And, because dealers often couldn't do repairs on the day they received the car – either because they didn't have time after diagnosing the problem or because they lacked necessary parts, tools, or knowledge – almost half of the customers' time was wasted. What's more, only 60% of the jobs were completed on time.

Next, GFS mapped the 25 steps in its provision process, adding arrows to show where these provision steps interacted with the steps in the consumption process. The group discovered that the provision steps took 207 minutes of paid time, only 27% of which created any value for the customer. A closer look revealed that technicians, the sole creators of customer value, were creating value during only 45% of their paid work time. Not impressive. (See the exhibit "Car Repair Before Lean Processes.")

Car Repair **Before** Lean Processes

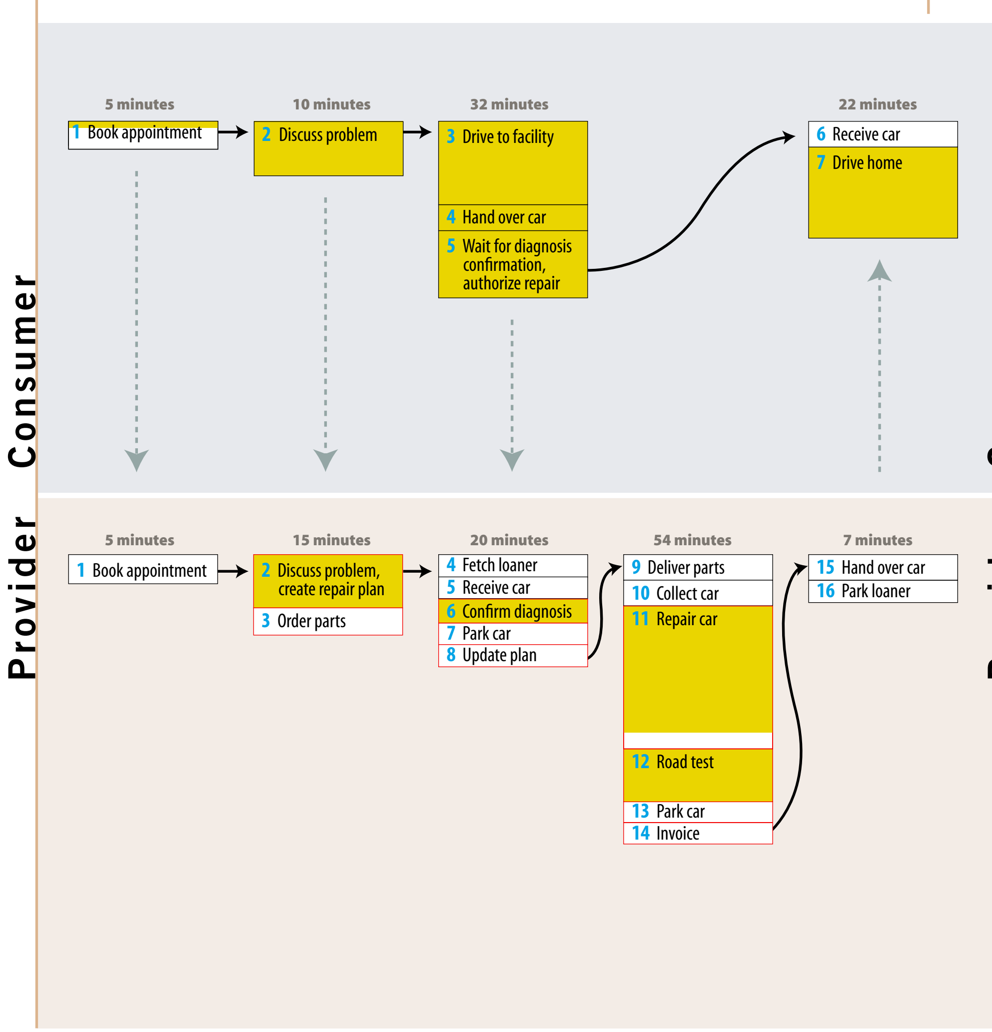


Using this map, GFS eliminated unnecessary steps in both the provision and consumption processes. The gains for GFS and its customers become clearly visible when we look at how the process works today (see the exhibit "Car Repair After Lean Processes").

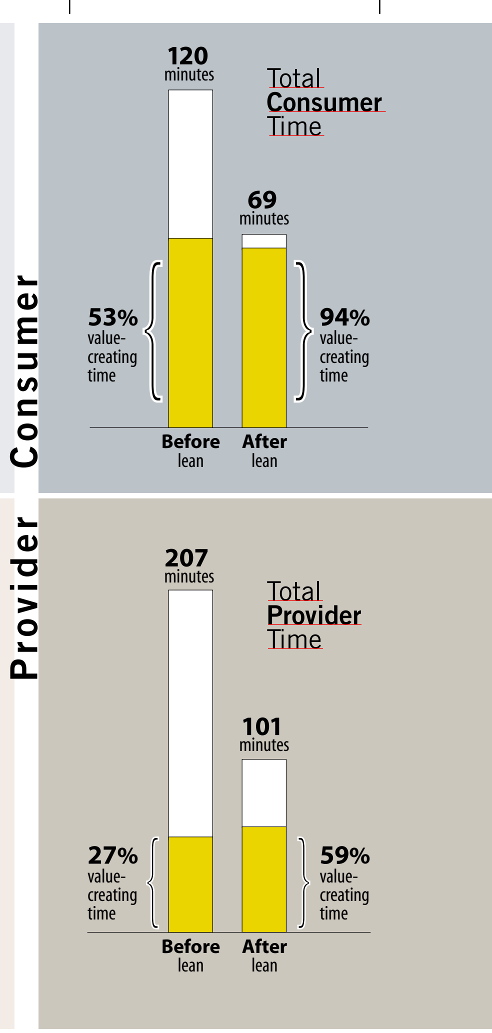
Here, GFS leverages its ongoing relationship with customers, eliminating the need for them to search for a new repair shop because of dissatisfaction with a previous repair. GFS prediagnoses the problem by phone whenever possible and confirms the diagnosis as soon as the car arrives. If customers can wait a few moments, they can authorize the repair work right then and avoid the extra phone call. The dealers have also smoothed the work flow by carefully scheduling arrivals to eliminate queues and passing work directly to the technician, with no handoffs. In addition, they have minimized the technician's time by leveling work flow and separating jobs according to their complexity and the time required to complete them. Parts and tools are prekitted and delivered to the technician in the service bay just as needed. And common repair tasks are standardized to reduce time spent as well as to increase the chance of getting the work done correctly and on time.

These gains create a win-win situation. Customers' time is no longer wasted and GFS can handle a greater volume of business. GFS's technicians are now creating value during 78% of their work time and they complete nearly twice as many jobs per day. More jobs are done right the first time, so fewer cars are brought back for a second visit. As a result, GFS requires a smaller support staff and needs only one-quarter the number of loaner cars.

Car Repair **After** Lean Processes



Time Saved



all customers exactly what they want, but it's a big leap–and proof that lean production principles can support lean consumption.

How does Tesco do it? By replenishing every store continuously, over a 24-hour day, to eliminate the need to hold stock either at the back of the store (as does Wal-Mart) or in high-bay storage (like Home Depot). Tesco reorders from key suppliers that produce – in a matter of hours–items that have just been purchased. What's more, Tesco picks up directly from suppliers' shipping docks at precise times and takes the goods to regional distribution centers where fresh products and fast-moving items are cross docked onto vehicles delivering to stores. In a further lean innovation, Tesco satisfies Web-shopping orders by having store personnel fulfill orders from the shelves during lulls. This process has reduced personnel costs, avoided the cost of separate warehouses for Web orders, and made Tesco the world's largest Internet grocer.

Lean techniques have helped Tesco to grow its share rapidly and become the UK's market leader in groceries, fueling its global expansion in Eastern Europe and East Asia as well. They have also allowed the grocer to increase customer satisfaction and loyalty by giving shoppers what they want (and, as we shall see, by providing it where and when they want it)–without wasting their time.

Provide what's wanted exactly *where* it's wanted. Conventional wisdom holds that customers usually obtain needed items from a single format (the price-conscious suburban shopper goes to Costco or Sam's Club; the time-pressed urban professional goes to Trader Joe's). But the conventional wisdom is wrong. Balancing many considerations, chief among them price and convenience, most of us use a variety of formats to get what we want as our circumstances change. We make the occasional trip to Costco for bulk items, the weekly trip to the standard supermarket for its wide selection of groceries, and several stops at the convenience store for the little things we missed, and we order out for home delivery when time's especially tight or we're just exhausted. By using different formats depending on circumstances, we minimize our total cost of consumption: the sum of prices we pay for products plus the time and effort expended to obtain them. In this equation, typically, price goes up as time and hassle decrease; we pay–sometimes a lot–for convenience.

Imagine, though, a provision process that maximizes convenience while keeping prices nearly uniform across

Locating for Lean Provision

From the lean perspective, the stampede to outsource manufacturing to China in order to serve North American and European customers is questionable, but not for the reasons usually cited. The real challenge for lean providers is the inability of remote production facilities to respond instantly to changing customer demands, such as a surge in requests for size nine gray "Wonder Wings."

Most manufacturers and their retail partners seem to have no method for calculating total costs of the entire provision stream for their products. These include costs for parts, actual logistics (not just the cheap container shipping probably called for in the business plan), stock-outs, remaindering, and carrying inventory over extended supply lines. In our experience, when all these costs are added up to accurately calculate total product costs, the lowest-cost location for labor-intensive products with unpredictable demand is often at the lowest wage point within the region of sale. That means Mexico for North America, Romania and Turkey for Western Europe, and, yes, China for Japan, because rapid replenishment at reasonable cost is possible from these locations.

For lean thinkers, the general rule is that shipping by boat is cheap but slow and, when forecasts are wrong, must be replaced by airfreight that is fast but expensive. By contrast, trucks are much faster than boats and much cheaper than planes. They permit overnight replenishment through each of the loops in a typical provision stream, provided that production is within the geographic region of sale. If you can't eliminate costly activities within production processes, you may still need to relocate to low-wage countries – but do it in a way that minimizes total costs.

In the case of products that are made to order, it might make sense to move manufacturing closer still to the customer, even when that's not the lowest wage point in the region. Consider Nike's surprising approach to the low-cost manufacture of customized goods. On Nike's Web site, you can customize a bag or backpack, choosing from a variety of fabrics and colors for the bag's panels, and even have Nike embroider a monogram or personal message on the item you order. And your customized bag will cost only $10 more (including express shipping) than a standard version in a retail store.

What you wouldn't have known is that your bag will be manufactured to your precise order at NuSewCo, a small contractor in the San Francisco area. At $15 per hour, NuSewCo's labor costs are 20 times higher than the fully loaded labor costs of the contractors in China that make Nike's other products. But Nike calculates that the total expense of obtaining its customized bags using high-priced American labor and offering express delivery is lower than the total cost of sourcing its standard bags for formats and preserving retailers' margins. In fact, this is possible if one fulfillment channel can supply every format. That's because the cost to the provider of the products entering its channel from suppliers depends predominantly on the buying power of the channel operator rather than on scale economies in larger bulk orders or scale advantages in larger stores.

For instance, the reason Wal-Mart sells hammers more cheaply than the corner hardware store isn't that the scale of Wal-Mart's order reduces hammer production costs or that the store's size significantly reduces its costs. It's because the scale of Wal-Mart's order causes the hammer maker to accept a low selling price in return for volume, and Wal-Mart passes on this savings to its customers.

The opportunity is ripe for large retailers using lean logistics techniques to offer a complete range of formats with uniform pricing to serve every customer need. Tesco is already doing this. It has created a full complement of formats ranging from local convenience stores (Tesco Express), to midsize stores in town centers (Tesco Metro), to standard-size supermarkets in the suburbs (Tesco Superstore), to hypermarkets on the periphery (Tesco Extra), to Web-based shopping (Tesco.com). By integrating the fulfillment channel behind all these formats, Tesco is answering an expanded array of consumption needs.

One result of this efficient channel sharing is that Tesco seems to be the only grocer making money on Web-based grocery shopping while continually increasing sales volume. Another, more provocative consequence is that all of the goods entering this unified fulfillment channel benefit from the same purchasing power: The tube of toothpaste going to the tiny Tesco Express outlet costs Tesco the same amount to buy from the supplier as the tube going to the vast Tesco Extra store, and the fulfillment cost is very nearly the same as well. This strongly suggests that the age of mass consumption retailing, in which the industry keeps heading toward ever larger formats, is coming to an end. Why drive miles to a "big box" if the items you want are available nearby from a smaller format at the same prices?

Perhaps the biggest benefit Tesco gains from this approach is that its customers are no longer strangers. By offering loyalty cards that are accepted at all formats, Tesco has begun to harvest invaluable data about the entire purchasing pattern of the 12 million UK customers in its loyalty program, who account for 80% of Tesco's sales revenue. This information is now being used to put the right items in the right stores and to target the right customers with the right promotional offers.

With Tesco's multiple-format model, customers can get what they want where they want it, and at a nearly uniform price; and the retailer captures additional consumer spending – and loyalty.

Provide what's wanted where it's wanted exactly *when* it's wanted. Most consumers have been trained to believe that goods and services are purchased on impulse. And for small items – the latest DVD release, for example – this may be true. *When* we want them is right now. However, for most items – and in particular for major durable goods, which account for the bulk of our spending – most of us continually plan ahead. We still want the goods when we want them, but that date is often some ways off.

Think about your household vehicles. Do you suddenly decide to buy a new car while driving past a dealer? Probably not. But you probably are contemplating a future purchase even as you read this: You know that you can trade your boring van for a two-door roadster as soon as you haul the youngest child to college next fall, and the SUV will reach a point of questionable reliability by the end of next summer.

Imagine that you could get a customized product for a reduced price simply by sharing your plans with a producer and ordering in advance. This purchasing model already works well for services such as vacation cruises, where advance ticket purchases are not only cheaper but can guarantee a preferred (in a sense, "customized") room. And it could work for consumer goods and a broad range of services – if producers would only listen to you.

American customers from Southeast Asia and selling them through retail.

How can this be? It's possible because sourcing locally and manufacturing only to order permits Nike to leave out a large number of steps in the logistics and sales processes: The storage of items at the plant in Southeast Asia until there is a full container to take to the port. The further storage of the container at the port while shipping awaits a full load for the container ship. The customs processes on both ends. The storage of the items in the distribution center on the U.S. West Coast and the assembly into containers to send to the stores. The *entire cost* of the store. The cost of the inevitable overstocks. The cost of lost sales due to stock-outs. And the cost of remaindering (which sometimes simply means discarding) the items produced on forecast for those customers who never materialized.

As Nike's cost analysis shows, the touch labor is actually a small portion of the total cost of producing and delivering these products, despite their labor intensity. Most of the costs reside in the various overheads at Nike, the management of the many handoffs from production sources on the other side of the world, the large inventories at many points, the retail dealers' overheads, the lost sales from too few goods, and the lost pricing power from too many.

But most current interactions actually penalize the customer for planning ahead. For example, if you ask to special order a specific vehicle for delivery sometime in the future, the dealer will be frustrated that you don't want one of the vehicles already in inventory and will try to steer you to available stock through price discounts. And if you insist on ordering ahead, you will pay a penalty when the dealer refuses to budge on price. This situation is bad for both consumers and producers. It thwarts customers' desire to get exactly what they want when they want it, and it increases the producers' production and distribution costs. Producers incur these extra expenses because they can't accurately predict the total volume of products that will be wanted at a specific time or the mix of features each customer will seek. As a result, they must keep extra production capacity available, keep large inventories of finished units and parts on hand, or both.

Most of us do plan ahead for large, durable purchases and would be willing to share our plans with the producer in return for getting exactly what we want at a future date with a discount. And those who absolutely must have a specific product (standard shift, purple paint) right now are usually willing to pay a premium for it. If producers can find a way to share the gains with their retailers, it should be possible to presell a large fraction of products to customers' specifications (at a lower cost and price) while keeping the capability to build customized products (at a higher cost and price) right away for the "got to have it now" customer.

A major challenge to "when it's wanted" consumption is that in complex, multifirm provision streams, the interests of the customer, the retailer, the producer, and the suppliers must be aligned. This brings us to the final principle of lean consumption.

Continually aggregate solutions to reduce the customer's time and hassle. With our background in lean production, we are repeatedly struck by a phenomenon most business analysts seem to miss: Consumers are using more and more suppliers – frequently strangers reached through impersonal markets–to solve smaller and smaller problems, often on a onetime basis. By contrast, lean producers, following Toyota's example, are steadily reducing their supply base for each item and asking fewer suppliers with deeper knowledge of their needs to solve bigger problems on a continuing basis.

This same concept can be applied to the process of consumption. For example, why can't a single provider solve your computation and communication problems by evaluating your specific needs and then determining the best equipment, software, and services? The provider could then obtain, install, maintain, upgrade, and replace the required items for a standard fee, with no unpaid work or hassle for you. And why can't another solution provider put the vehicles in your driveway, then maintain, repair, and dispose of them as appropriate, for a simple usage fee, without consuming any of your time or attention?

Few such solutions are currently being offered cost effectively for consumers' small number of really big problems: mobility, communication, shelter, health care, financial management, and shopping. (Concierge services and consumer advocates may be available, but are actually a step backward into a world where the well-to-do hire staff to cure their consumption headaches, which are caused by broken processes.)

However, advances in information technology – for managing providers' logistics and connecting consumers and providers – will lift the technical barriers to solving these problems and make solutions cost effective. And transparent pricing of bundled goods and services, along with clear rules governing how providers use consumers' information, will be essential. Finally, providers and consumers will have to truly open lines of communication and learn how to plan together over the long term.

The age of mass consumption retailing, in which the industry keeps heading toward ever larger formats, **is coming to an end.**

Making Lean Consumption Work

We believe that consumers will be quick to learn their role in lean consumption. Most of us would surely embrace the opportunity to solve our consumption problems completely, getting just what we want, when we want it, where we want it, at an attractive price from a small number of stable providers, with no waste of our time, and with no unpaid work.

The real challenge lies with the retailers, service providers, manufacturers, and suppliers that are not used to looking at total cost from the standpoint of the consumer and are even less accustomed to working with customers to optimize the process of consuming. Lean production has clearly triumphed over similar obstacles in recent years to become the dominant global model. Can lean consumption, its logical companion, be far behind?

Reprint R0503C; HBR OnPoint 9432
To order, see page 151.

What Great Managers Do

by Marcus Buckingham

Great leaders tap into the needs and fears we all share. Great managers, by contrast, perform their magic by discovering, developing, and celebrating what's different about each person who works for them. Here's how they do it.

"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

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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.

And a good manager would have left it at that. But Michelle knew she could get more out 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.

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

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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 11:30 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,

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.

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."

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.

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 anothers' 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

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.

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.

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 trigger-

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.

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?

ing 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.

Differences of trait and talent are like blood types: They cut across the superficial variations of race, sex, and age and capture each person's uniqueness.

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.

Reprint R0503D
To order, see page 151.

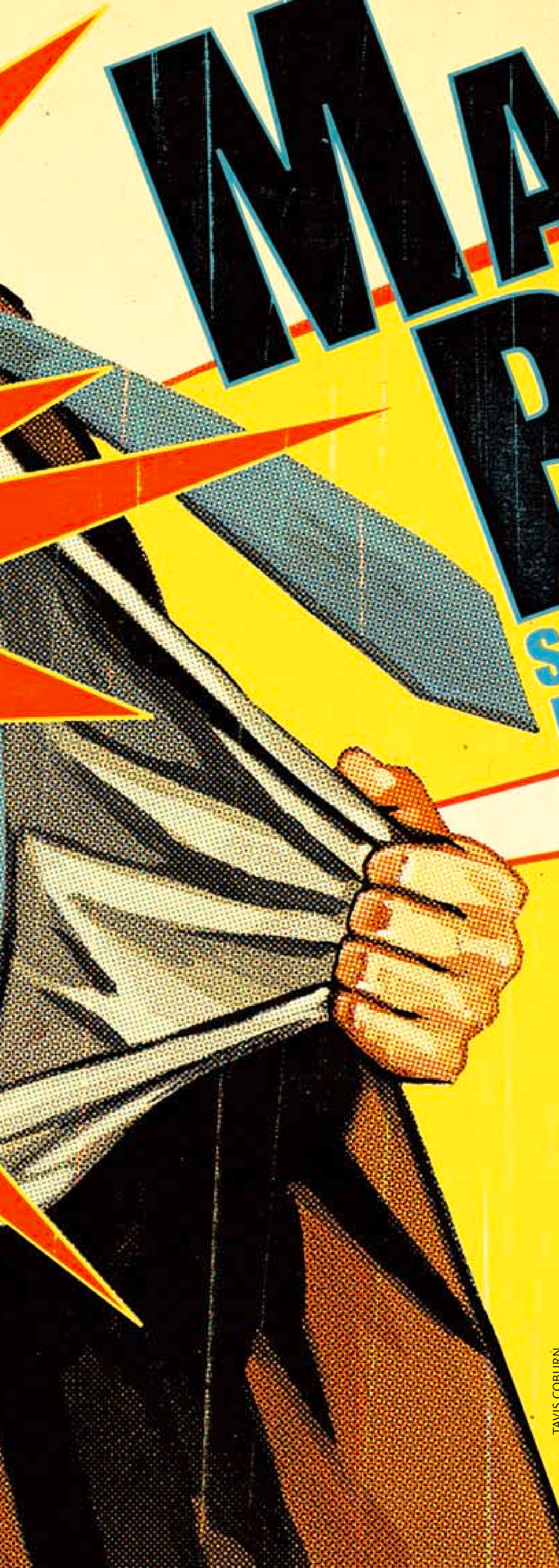
"Of course I'm a team player, but why am I always stuck with the extra innings?"

DAVE CARPENTER

Market Busting

Strategies for Exceptional Business Growth

by Rita Gunther McGrath and Ian C. MacMillan



TAVIS COBURN

A company can't outperform its rivals if it competes the same way they do. Reconceive your business's profit drivers, and you can change from copycat to king of the jungle.

If company leaders were granted a single wish, their most frequent request would surely be for a reliable way to create new growth businesses. Business practitioners' overwhelming interest in this subject, which we as academics share, prompted us to undertake a major study of successful growth moves initiated by established companies in several industries. We looked at a wide range of strategic approaches to growth–everything from low-risk, incremental changes to high-risk, disruptive ones. In the course of our three-year study, we became intrigued by an approach that lay somewhere between those two extremes. At a high level, this strategy is about redefining profit drivers. At a practical level, it involves making several deceptively simple moves: Some companies reconfigured their *unit of business*–what they bill customers for–to more closely match the customers' needs. Some companies focused on different *key metrics* than their competitors did, and, in doing so, created a better business design. Still other companies helped customers change their own unit of business or key metrics. Once we started to look at new growth through this lens, we found success stories in industries that had been written off as hopelessly commoditized or strategically unattractive. In a few cases, the companies we studied succeeded so well at redefining their profit drivers that they had transformed their industries.

Building a Better Model

It's hard to imagine two businesses more mature than ready-mix concrete and reinsurance. Both industries have been around for more than 100 years, and competition in both has devolved: The companies offer standardized products and play by well-established rules. Yet in both industries, we identified companies that were enjoying sustained and impressive growth because they had redefined their profit drivers or changed their unit of business and key metrics.

Let's start with concrete. The problem with ready-mix concrete is that it's highly perishable; it begins to set when a truck is loaded, and the producer has only limited time to get it to its destination. In Mexico – as in many other rapidly urbanizing countries – traffic, weather, and unpredictable construction labor make it incredibly hard to plan deliveries accurately. So a construction contractor might have concrete ready for delivery when the site isn't ready or, worse, expensive work crews at a standstill because the concrete hasn't arrived.

Lorenzo Zambrano, who became CEO of the Mexican company Cemex in 1985, decided that there had to be a better way to run this business. Cemex, like all traditional cement companies, sold concrete by the cubic yard. But Zambrano's customers didn't particularly value cubic yards of concrete. They rightly considered concrete a commodity product. What they did value (and what Zambrano had the good sense to start selling) were deliveries–in other words, the right amount of concrete delivered just when it was needed. To figure out how to accomplish this goal, Cemex staffers studied how FedEx, pizza delivery companies, and ambulance squads worked. Eventually, they developed digital systems that allowed Cemex to adjust, in real time, where trucks were bound. They learned to optimize delivery patterns across a whole region; customers who unexpectedly needed concrete could be served, often by shipments that had unexpectedly been postponed by other customers.

Cemex can now deliver concrete within hours – sometimes even minutes. It can accept unlimited change orders. It can help customers anticipate demand and cash-flow requirements. Cemex, once a regional company operating in Mexico, is now the third-largest ready-mix concrete business in the world, with plans to capture the number two spot. In 2003, it generated $7.17 billion in revenues from about 30 countries, primarily because of its aggressive acquisition and transformation of firms in emerging economies.

Now let's consider the world of reinsurance providers. They sell backup policies to insurance companies so the latter can then cover customers they might otherwise have needed to decline. Many of the reinsurance companies' customers share a problem. Some types of primary insurance–life insurance, for example–can remain active for decades. And even after they stop selling a particular product, insurance companies need to support existing policies. As a result, they're often forced to maintain out-of-date legacy computer systems as well as control and accounting procedures. This maintenance responsibility ties up capital and hampers competitive effectiveness.

Swiss Reinsurance Company (Swiss Re) recognized an opportunity to help insurance companies solve this problem. The solution was in a product called "administrative reinsurance," or Admin Re. With this offering, Swiss Re changed its unit of business. It now handles the administration of the life insurance and health insurance policies no longer sold by its clients. Swiss Re administers the policies using proprietary business processes, sometimes with help from administrative partners.

This new service has freed up capital and human resources for Swiss Re's clients, while also allowing them to eliminate legacy computer systems. These benefits show up in the insurers' key metrics – the numbers that analysts use to judge the insurers' performance. The benefits flow back, in turn, to Swiss Re. In the seven years since it started to offer Admin Re, the company has taken on 4.5 million policies, making this service one of its fastest-growing business lines.

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The Language of Growth

Before we get into the *how* of reexamining your unit of business and the associated key metrics–or those of your customers–let's make sure we're clear on *what* we're talking about. As industries emerge and evolve, most players eventually settle on a common unit of offering. Lawyers sell units of time (billable hours), consumer-goods producers sell bars of soap and boxes of cereal, airlines sell passenger trips, and so on. These are all units of business – the fundamental basis for transactions between buyers and sellers.

Associated with each is a set of measures–we call them key metrics–that can be used to assess how well a firm is doing with respect to its profitability drivers. Thus, key metrics for law firms involve the percentage of total billable hours actually billed, average hourly charges per employee, and administrative costs per unit of revenue. Key

MARKET BUSTING Strategies

When we did research on organizational growth, we wanted to understand a range of strategies that would support organic, profitable growth. We decided to call these strategies MarketBusters. In order to qualify as an exemplar of MarketBusting, a business needed:

- a 2% change in market share within a year;
- 10% or more annual growth in sales or shipments over at least two years;
- or annual sales or shipment growth 5% greater than the growth in the overall market.

We identified five MarketBusting strategies. This article looks in-depth at one of them–redefining profit drivers by reconfiguring a unit of business or refocusing on distinctive **key metrics** that drive growth. All five strategies are described briefly below.

Lens	Strategy	Description	Example
Customers	Transform the customer's experience.	Dramatically change how customers meet their needs.	Coinstar ($176 million in revenues) converts loose change for customers–conveniently. It has placed about 10,000 change-conversion machines in easy-to-find locations, such as supermarkets.
Products and services	Transform your offerings.	Compare your product and service attributes with those of your competitors. Sort attributes into three categories: basic, discriminating, and energizing. Figure out how changes would give you leverage over rivals.	Procter & Gamble's battery-powered SpinBrush offers consumers the experience of using an electric toothbrush–for the price of a high-end manual brush.
Key metrics	**Redefine your business's profit drivers.**	**Identify the fundamental thing you charge customers for–your unit of business–and the key metrics used to measure how profitably you're selling it. Change one or both to better meet customers' needs.**	**Air Products installs industrial gas generators on customers' sites rather than shipping liquefied gas in tankers.**
Industry dynamics	Anticipate and exploit industry changes.	If a major industrywide shift is in the works, you can: provoke disruptive change; capitalize by being first to implement change or by seeing its implications more clearly than competitors can; or exploit second-order effects.	As Internet usage took off, Sealed Air Corporation anticipated demand for new packaging solutions. The company captured substantial advantages by being quick to respond.
Tectonic opportunities	Create a radically new offering.	These opportunities are major shifts, not just product or market extensions. And they're notoriously difficult to identify if you're an established company. Watch what entrepreneurs in your space are doing in regard to creating new products and services, and see if you can leapfrog or acquire them or their technologies.	Subway noted consumers' competing desires for low-calorie meals and fast-food convenience. In response, it has created the "healthy fast food" concept, helping to drive its 2003 revenues to $468 million.

metrics for consumer-goods producers include asset and inventory turnover, working capital ratios, average margins, and product utilization. Key metrics for airlines include costs per passenger mile flown and seat yield. You get the idea.

It's often possible to grow a business by doing one of two things for your company (or for your customers):

Change your unit of business so it more closely reflects the value created for customers. You will probably also want to change how you measure the effectiveness of your performance.

Dramatically change your performance on existing key metrics in a way that uniquely favors your company.

To go back to our examples, Cemex's strategy was so powerful because the company changed its focus from the sale of a commodity to the sale of something customers really cared about. In short, the unit of business shifted from cubic yards to the delivery window. This was a simple change in one sense. But Cemex then oriented its information, logistics, and delivery infrastructure around the delivery-window concept, creating far-reaching changes in the company and eventually throughout the industry. Swiss Re also added a new unit of business to the traditional product portfolio of the reinsurance industry – creating services to free up clients' capital and resources. (For an overview of all the approaches to growth we observed in our research, see the sidebar "MarketBusting Strategies.")

A Profitable Alignment

Changing your unit of business, or radically changing your key metrics, can be a powerful engine for growth, particularly for early movers. If you can figure out quickly how to help improve a customer's core performance – as both Cemex and Swiss Re did – the constraints that tied you down in the past can melt away. You can begin to price your products based on their value to your customers, not according to low-margin commodity pricing. You can be more proactive; your business and your incentives will be aligned with what your customers care about. In the best case, you can create new shareholder value for your company because you are expanding the pool of problems that your company can address.

From a competitive point of view, a change in the unit of business can be difficult for rivals to respond to because it often comes as a surprise. Consider the medical-imaging-equipment industry. Let's say a maker of imaging equipment figures out that customers, such as hospitals, don't really care about the machines themselves; customers care more about the creation and interpretation of the images the equipment produces. Now consider the advantage the equipment maker can gain if it can figure out how to move from selling machines to selling imaging and interpretation services. If the company can execute this move effectively, customers will pay for what they value – the image and what it means to them. The equipment maker can also improve customers' key metrics by eliminating the costs associated with owning and maintaining the machines. The company can implement value-based pricing, not commodity pricing, and the customer will realize improved performance. Competitors still operating under the old model won't even *see* the threat – how can they when their competitive analysis is likely to involve only equipment sales? The new business doesn't even register with them.

Even if competitors do figure out what you're up to, it takes them time to respond. Everything about an established business – its power structure, incentive system, sales force, and so on – is built around the old unit of business. Change the unit and the company capabilities that go with it, and you can create a barrier to entry that lasts for a long while, though not indefinitely. In one study, we found that even easily imitated banking products were not actually copied for 12 to 18 months, even though their competitive threat was clearly visible to all the players in the industry.

Eight Moves for Growth

We've identified eight moves companies can make to redefine their profit drivers and realize low-risk growth.

Change your unit of business. We've already seen how rethinking the unit of business helped Cemex spark an upheaval in the global ready-mix concrete industry. Similar thinking is taking place in a host of other industries. More often than not, companies are moving away from selling a pure product and toward selling a product–service mix or even a pure service.

> Easily imitated banking products weren't copied for 12 to 18 months – even though their **threat was visible** to all the industry players.

Privately held Madden Communications, once a conventional printing house, used to make its money by printing promotional materials for companies. In 1988, then-salesman Jim Donahugh visited a target supermarket to see his company's materials on display. Madden's displays were nowhere to be seen, nor could Donahugh find them at several other supermarkets he subsequently visited. Eventually, Donahugh and his bosses discovered that this was not at all unusual. Operating on thin margins, the supermarkets often didn't or couldn't take the time to display promotional materials properly. Donahugh also found that Madden's customers, primarily packaged-goods companies, often over-ordered promotional materials as a hedge against running short. Money was being wasted on printed materials that were displayed badly or not at all.

Today, Madden's customers no longer buy individual print jobs. Instead, they hire the company to print promotional materials *and* manage the distribution and installation of those materials on-site. Madden now focuses on a few large customers who are happy to pay more for the enhanced service. Conventional printing companies have found it difficult to respond to Madden's move, because the new business depended on new capabilities, including the capacity to connect with customers at a senior level. Madden's revenues grew from $10 million in 1990 to $133 million in 2004, in an industry that many had come to regard as hopelessly mature.

Retain your unit of business, but radically improve your key metrics, particularly productivity. You don't always need to do something as radical as overturn the way your industry does business. Sometimes you can create dramatic growth by doing what you do right now – but much more productively. Digitization has helped many companies do this.

Lamons Gasket Company is a good example. An $80 million subsidiary of MetalDyne, Lamons manufactures and distributes static sealing solutions for the petrochemical, refining, nuclear, OEM, and pulp and paper industries. It sells more than 100,000 standard and special-order products, including gaskets, packings, nuts, bolts, and screws. Until recently, simply figuring out what customers wanted to buy and getting the right items to them was a horribly inefficient process at Lamons. Customers would phone or fax in an order, and a customer service representative would have to translate the information into Lamons's part numbers and format. The average order cost less than $500 but took 30 to 60 minutes to get into the system. This level of inefficiency was devastating to Lamons's profits and costly to customers as well, since they were spending the same 30 to 60 minutes to get the order right.

Then Lamons built an e-commerce Web site, and customers' ability to find, order, and pay for goods improved radically. The company's productivity improvements added to its bottom line considerably. Customers were so pleased by their own productivity gains that they drove up Lamons's market share. Customer retention rates also went up – which is particularly vital to a business whose strategy depends on serving large numbers of small repeat customers.

Improve your cash-flow velocity. In some industries, companies can create powerful growth engines by figuring out how to work faster – much faster. Improving cash-flow velocity is akin to a Monopoly player passing "Go" more frequently – thereby collecting his or her $200 more often. The higher your cash-flow velocity, the less working capital you need, and the more effectively you can use your assets. If you can also improve customers' cash-flow velocity, so much the better.

In recent years, it has become extremely popular for U.S. home owners to refinance their mortgages as interest rates have dropped and real estate values have risen. American Home Mortgage Holdings (AHMH) figured out a way to take advantage of this boom. It focused intensely on speeding up the refinancing process, building systems that made it one of the most rapid service providers in the industry. The company works closely with large refinancing companies, such as Fannie Mae and the government-owned Freddie Mac. Because AHMH's systems interact with those of the other providers, it can guarantee credit compliance, place deals, and move cash quickly. The more deals it closes in shorter time, the higher its cash-flow velocity. AHMH works fast by using automated systems and by doing a lot of its customer-related business electronically. It originates and sells mortgage loans through its Web site, which gives customers 24-hour access to product terms and interest rates. Customers can lock in interest rates, check the status of pending applications, obtain credit reports, calculate financing affordability, and prescreen their own qualifications.

AHMH didn't reinvent the financing business. It simply recognized an opportunity and aggressively focused on one way to benefit from it. As a result, the company is forecasted to grow at 28% a year and is expected to continue to produce above-average operational results.

Dramatically improve your asset utilization. For a lot of companies, the most important key metric is return on assets. The idea is that you should be adding economic value (often expressed in terms of EVA) or, at a minimum, providing a return on the funds tied up in capital (often expressed in terms of ROA). If you can reduce the assets tied up in your operations, your key metrics around asset utilization will improve. Do this for yourself, and you'll make shareholders happy. Do this for your customers, and they'll be happy; they'll reward you, and ultimately your shareholders will reap the benefits.

Consider the two ways in which Quanta Computer (a Taiwanese company founded in 1988 by entrepreneur Barry Lam) reduced asset intensity both for itself and its customers. First, it serves many notebook-producing customers (Apple, Dell, Gateway, Fujitsu Siemens) as a contract manufacturer and design partner, which means it spreads its assets invested in manufacturing more effectively than any one company could do in-house. Second, Quanta helps its customers reduce their asset intensity because they're using Quanta to manufacture some, preferably all, of the components they need. In this way, Quanta has effectively played a two-way game of reducing asset intensity. Its sales in 2002 exceeded $4 billion.

Improve your customers' performance. As we showed in the Swiss Re example, another powerful application of key-metrics analysis is to focus on your customers. Helping your customers improve their performance generates a more robust, profitable, loyal base of clients who are more willing and able to buy from you. To the extent that your system is critical to or embedded in the way customers do business, you can also achieve a certain amount of competitive sustainability.

For instance, package-delivery firm UPS has begun to branch out from its core business into an array of services designed to help customers improve their key metrics. Under the rubric "synchronizing commerce," UPS performs a variety of services that go well beyond picking up and delivering packages. Last spring, certified UPS technicians started doing repair work on Toshiba laptops. (Most of them have eight to ten years experience repairing notebooks, Toshiba officials have said.) As Mark Simons, a general manager of Toshiba's digital products division, told one trade publication: "Moving a unit around and getting replacement parts consumes most of the time…The actual service only takes about an hour." By taking over both the shipping and the repair aspects of PC servicing, UPS eliminates steps in the process, removes the need for PC makers to employ a maintenance staff, integrates the repair and shipping activity, and, most important, reduces the time that a broken PC is not in the hands of its owner.

Not only does the process outsource a tedious chore for the notebook makers (thus improving their productivity, asset utilization, and so on), it also increases end-user customer satisfaction, thereby creating value for all three parties.

Improve your customers' personal productivity. What asset productivity is to a commercial customer, convenience and time-savings are to a consumer. Whenever a company sees a way to make a complex process more convenient, it may be able to grow the business. Most people can readily recite the things that even well-intentioned companies do that drive them crazy. Banks and insurance companies force you to get information from third parties before they will do business with you; service desks run you through the "press 1, press 2" voice-mail gauntlet; retail establishments subject you to the same checkout delays whether you are buying a truck full of stuff or just a single item; and so on. Solve the irritations, and customers will gratefully reciprocate by increasing your sales volumes or paying you more.

Just as AHMH figured out how to accelerate refinancing, mortgage broker LendingTree figured out how to make the process less onerous for consumers. In contrast to the AHMH model, in which the company itself is a mortgage broker, LendingTree uses Web-based technology to link networks of mortgage providers in order to give consumers more choices and improve the competitiveness of offers. It sends requests to its network of lenders, who return bids. Consumers can also use the service to choose from a list of mortgages, credit cards, and home-equity, auto, and personal loans. LendingTree's model empowers borrowers by making lenders apply to them, rather than making the borrowers apply to the lenders.

Participating lenders pay transaction fees to LendingTree. Consumers do not pay a service fee. From 1998 through 2001, LendingTree processed more than five million credit requests and generated $10 billion in transaction volume. In 2003, it was acquired by InterActive

Prospecting Questions

The following queries can help you determine how best to change your unit of business or key metrics in the pursuit of sustainable, low-risk growth.

Change your unit of business.

- Can you charge for what you offer in a different way?
- Can you incur costs and make payments in a different way?
- Can you charge customers for what they might value rather than for what you traditionally provide?
- Can you create better incentives for your people by changing the unit of business?
- Would some other way of charging for what you sell be easier for you or easier to explain to your customers?

Improve your productivity metrics.

- Can you use the five REs (remove, replace, reduce, redesign, redistribute) to dramatically enhance your productivity?
- Can you dramatically enhance your productivity by deploying new technology?
- Can you leapfrog your competition in productivity? Look especially for situations in which the competition's resources are already committed to something else, such as integrating a large merger.
- Can you eliminate time-wasting, repetitive activities to enhance your productivity? Can you figure out how to eliminate transaction costs (such as internal reviews and approvals) by automating some of your internal control practices?

Improve your cash-flow velocity.

- Could you eliminate or reduce inventory?
- Might you delay payments to others?
- Can you speed up receipts from your customers?
- Can you generate cash before you have to incur costs?
- Can you speed up your customers' ordering cycles?
- Can you get paid more frequently over the lifetime of a contract?
- Can you automate the payment stream so that manual delays don't hold up cash coming in?
- Can you make sure that your invoicing mechanisms are easy for your customers to respond to, so you don't create additional payment delays?
- Could you offer customers electronic-payment options to speed them up?
- Have you explored technologies such as direct deposit or lockboxes to speed payments?

Improve your asset utilization.

- Can you reduce the asset intensity of your business by outsourcing some activities to specialists?
- Can you eliminate the need to own certain assets?
- Can you utilize assets owned by someone else, as needed?
- Can you use assets more effectively – for instance, by extending the time of day in which they are used or by using remote electronics to operate them?
- Can you pool your assets with those of other firms and reduce the asset intensity for the whole group?
- Can you change fixed assets to variable assets by, for instance, establishing utilization contracts with suppliers for certain services?

Improve your customers' key metrics.

- What numbers are your customers seeking to achieve? (Be explicit.)
- What outcomes are your customers measuring?
- What are your customers' key ratios?
- Can you think of ways to help customers improve their financial, operating, and investment ratios?
- Can you help your customers hit their desired market-share, cash-flow, EBITDA, revenue-growth, and profit numbers?
- Can you help your customers better understand what really drives success in their businesses?

Improve your customers' personal productivity.

- Can you find ways to help customers' staffers improve their productivity on the job…
- …and in their private lives?

Help improve your customers' cash flow.

- Can you help customers get cash earlier and pay out cash later?
- Can you help customers get better margins from *their* customers?

Improve your customers' asset utilization.

- Can you reduce customers' assets?
- Can you help customers use assets more productively?
- Can you help customers reduce their fixed-asset burden by taking on their assets and charging them for usage?

Corporation – an acquisition inspired no doubt by LendingTree's 74% sales increase from 2001 to 2002.

Help improve your customers' cash flow. As we've seen, if you can help your customers become more profitable and efficient, it only makes sense for them to do more business with you. The software company SAS Institute grew rapidly because it was able to help customers make better decisions faster, ultimately improving their cash-flow velocity. SAS adjusted many of its decision-support applications in response to customers' needs for improved operations, and that responsiveness has turned it into a strategic partner for many of its customers.

> Improving cash-flow velocity is akin to a **Monopoly player passing "Go"** more frequently – thereby collecting his or her $200 more often.

SAS has one of the lowest employee turnover rates in its industry, so long-standing employees really know, and know how to help, their customers. The company boasts a 98% customer retention rate, and SAS has enjoyed a long track record of solid profits. It has a balance sheet free of debt and a projected annual growth rate of more than 20%.

Reduce your customers' asset intensity. We often say to businesspeople, "You should know your customers' balance sheets better than they do." If you can find ways to reduce or improve customers' utilization of their assets, you may profit from their increased loyalty to your firm. For instance, GE's locomotive division decided to change its unit of business and sell haulage contracts, not locomotives, to railroads. This allowed the railroads that signed up for contracts to take their locomotives off their balance sheets – much to the delight of their CFOs.

Putting These Ideas to Good Use

As we said at the outset, redefining your company by changing your unit of business or your key metrics can be among the lowest-risk routes to growth. Why? Because you already have a lot of the necessary information – you don't need to invent whole new markets, and you have interactions with customers that can give you the data you need. The sidebar "Prospecting Questions" provides detailed questions to think about for each of the eight moves described above. But before you drill down with that level of specificity, you will need to carefully consider what your unit of business is, what it could become, which key metrics offer the most leverage, and so forth. To assist in that process, we suggest an approach that we've used with clients. (If you happen to have a few underutilized MBAs hanging around, they can do some of the analytical work.)

Identify your unit of business and associated key metrics. It should be easy to determine what your current unit of business is. What do you charge for? When you send customers invoices, what do you bill for? Try to spell it out in the simplest terms possible: "We make money by billing our customers or clients for ________."

Next, be critical. Does what you sell really reflect the value you create for customers? If you sell a product, could you redefine it to reflect the benefits or services yielded by that product? If you sell a unit of time, could you instead sell the outcome that the customer wants? A good general guideline is to try to align your unit of business with some performance outcome that is relevant to your customer.

Getting at current key metrics is usually very straightforward. If you don't already outline them in your annual report, the analysts who cover your industry will be able to tell you what they are. It's often useful to create a table with the basic financial performance parameters of your business and, if you have the data, those of the top competitors in your industry.

Identify obstacles to change. What's keeping you from changing to a new unit of business or from achieving higher performance on the key metrics associated with an existing unit of business? In this part of the process, you want to remove the blinders that exist when you've been competing in the same way for a long time. A number of devices can help you gain a fresh perspective. Three have proven particularly useful in our work.

First is a well-known technique from the quality movement, popularized in Japan as the Five Whys exercise. For every metric, ask yourself, "Why can't we improve?" for five levels of answers. If you can get to a root cause, you can often conceive of ways to overcome it. If one root cause is affecting several key metrics, you can dramatically improve your effectiveness by addressing it. To illustrate how this works, let's simulate how Cemex might have derived the core capabilities it needed by using the five whys. Let's assume that the company has compared its key metrics with those of top U.S. firms and is unhappy with its truck utilization, a key metric for delivery businesses.

- Why are our truck-utilization ratios so low compared with those of ready-mix cement firms in the United States? *Because we have much wider delivery windows.*
- Why do we have wider delivery windows? *Because the trucks often get stuck in traffic, and the clients are often not ready for the pour.*

• Why can't we send a second truck when the first truck is stuck in traffic or send the first truck to another destination when the client isn't ready? *Because we have no way to tell the two truck drivers to change their destinations. Besides, the second truck could get stuck in the same traffic.*

• Why can't we set up mobile communications between plants and trucks, so that more than one plant can dispatch trucks to avoid traffic jams? *This still wouldn't handle cases where the customer is not ready to pour.*

• Why can't we have a communications center that plants, trucks, and customers can call if they are delayed? This center could coordinate all deliveries, redirecting trucks to sites that are ready for a pour. *Hmmm–let's think about that.*

The second technique is our variation of the five whys, which we call the Five REs exercise. The idea is to look at all the key metrics that represent costs and assets and probe them ruthlessly. The five REs are:

• **Remove.** Why incur a cost at all? Why not remove it entirely from your cost base? Toshiba, mentioned earlier in this article, has handed off expensive repair costs to UPS. Everyone wins.

• **Replace.** If you can't remove a cost, can you lower it by substituting a less-expensive product or service? For instance, companies have sometimes used voice-recognition systems in place of expensive human operators, and manufacturers of sodas and candies have used corn syrup in place of sucrose.

• **Reduce.** If you can't replace the cost, can you reduce it instead? Lamons Gasket reduced the labor intensity of its ordering system by switching to an interactive online system. Alternatively, can you reduce the price you are paying?

• **Redesign.** If you can't reduce the amount you need to spend on a scarce resource, can you redesign your business to use it more efficiently? There are many ways companies can economize on technical or service resources. For instance, law firms may complement services from their expensive lawyers with services from less costly paralegals; hospitals may replace some physicians with nurse practitioners; software companies may encourage customers to use self-help Web sites or phone services rather than rely on costly help-desk technicians.

• **Redistribute.** If you can't redesign, can you redistribute costs over more units? Quanta, for instance, has built a formidable advantage by spreading its production and design costs over many notebook manufacturers.

Once you have attacked major cost ratios in this way, ask the same questions about assets. Can you remove, replace, reduce, redesign, or redistribute assets? People tend to resist these types of questions, so our rule is that there has to be strong, highly substantiated reasons to say no to any of these questions. Persevere–you may be thrilled by the creativity that persistence provokes.

A third way to gain perspective is to do some benchmarking – but not necessarily against your direct competitors. It's useful to benchmark against firms that have successfully transformed a particular metric through better business practices. Thus, we saw Cemex benchmark its delivery function against FedEx. Groups like the Conference Board and the Corporate Executive Board can help you identify best-in-class performers for the metrics you want to explore.

Review the key customer segments you serve. The next challenge is to apply the techniques described above to your customers. The questions you want to consider are whether you might benefit by developing a different unit of business for a particular set of customers, whether those customers might benefit if *they* developed a different unit of business, or whether you can help them with their key metrics.

Assess the need for new capabilities and the potential for internal resistance. Typically, a significant shift in your business design also implies major shifts in your capabilities. Cemex, for instance, had to add new skills in telecommunications, programming, and system administration. As you go through this assessment, you're bound to run into resistance from senior managers; they aren't likely to embrace a change that will require the company to develop totally different skill sets. So it's worth thinking about how to deal with the politics of changing a business before you find yourself stalled by internal opposition.

Decide on a marketing and communications plan. How can you convey the value of your new approach to your customers and your internal constituencies? And who needs to be part of the communications process? Make sure you consider which audiences are important, in which sequence, and with what types of communication. The idea is not to spend endless hours agonizing but to make sure that when you do make a move, it is decisive and clearly conveyed to critical constituencies. Remember, too, that analysts who are used to looking at your company one way may need to be educated on a more appropriate set of metrics to use.

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The approach we've described can be an easy path to substantial, quick, profitable, low-risk growth. The beauty of it is that your people already know the business, the customers, and the products. Indeed, after we've employed this methodology with clients, we often hear them say, "Well, that should have been obvious." Sure–except that some firms see the obvious first and move aggressively to take advantage of it, and others simply don't. Use this strategy to spark creative changes in your unit of business or your metrics, and you, too, will find seeds of quick, low-risk growth.

Reprint R0503E; HBR OnPoint 9408
To order, see page 151.

Time-Out

"We have to provide 24/7 service 365 days a year, and every single day is just as important as any other.... Managers who have an attitude of 'I'll get to it on Monday' don't last long in our industry."

Bill Munck
"Changing a Culture of Face Time"
Harvard Business Review
November 2001

"Bernice, when you get around to it, bring me everything we've got on procrastination."

"If we could afford to take another vacation this year, I'd really get some work done."

JOHN CALDWELL, DON CRESCI, HARLEY L. SCHWADRON, MIKE SHAPIRO, AND P.C. VEY

"Can I call back? I'm sending you an e-mail right now."

"After considering the pros and cons of commuting, I've decided the only sane thing to do is live in my office."

PLUNKERT

WANT COLLABORATION?

ACCEPT—AND ACTIVELY MANAGE—CONFLICT

The quest for harmony and common goals can actually obstruct teamwork. Managers get truly effective collaboration only when they realize that conflict is natural and necessary.

by Jeff Weiss and Jonathan Hughes

THE CHALLENGE is a long-standing one for senior managers: How do you get people in your organization to work together across internal boundaries? But the question has taken on urgency in today's global and fast-changing business environment. To service multinational accounts, you increasingly need seamless collaboration across geographic boundaries. To improve customer satisfaction, you increasingly need collaboration among functions ranging from R&D to distribution. To offer solutions tailored to customers' needs, you increasingly need collaboration between product and service groups.

Meanwhile, as competitive pressures continually force companies to find ways to do more with less, few managers have the luxury of relying on their own dedicated staffs to accomplish their objectives. Instead, most must work with and through people across the organization, many of whom have different priorities, incentives, and ways of doing things.

Getting collaboration right promises tremendous benefits: a unified face to customers, faster internal decision making, reduced costs through shared resources, and the development of more innovative products. But despite the billions of dollars spent on initiatives to improve collaboration, few companies are happy with the results. Time and again we have seen management teams employ the same few strategies to boost internal cooperation. They restructure their organizations and reengineer their business processes. They create cross-unit incentives. They offer teamwork training. While such initiatives yield the occasional success story, most of them have only limited impact in dismantling organizational silos and fostering collaboration – and many are total failures. (See the sidebar "The Three Myths of Collaboration.")

So what's the problem? Most companies respond to the challenge of improving collaboration in entirely the wrong way. They focus on the symptoms ("Sales and delivery do not work together as closely as they should") rather than on the root cause of failures in cooperation: conflict. The fact is, you can't improve collaboration until you've addressed the issue of conflict.

This can come as a surprise to even the most experienced executives, who generally don't fully appreciate the inevitability of conflict in complex organizations. And even if they do recognize this, many mistakenly assume that efforts to increase collaboration will significantly reduce that conflict, when in fact some of these efforts – for example, restructuring initiatives – actually produce more of it.

Executives underestimate not only the inevitability of conflict but also – and this is key – its importance to the organization. The disagreements sparked by differences in perspective, competencies, access to information, and strategic focus within a company actually generate much of the value that can come from collaboration across organizational boundaries. Clashes between parties are the crucibles in which creative solutions are developed and wise trade-offs among competing objectives are made. So instead of trying simply to

DAVID PLUNKERT

reduce disagreements, senior executives need to embrace conflict and, just as important, institutionalize mechanisms for managing it.

Even though most people lack an innate understanding of how to deal with conflict effectively, there are a number of straightforward ways that executives can help their people–and their organizations–constructively manage it. These can be divided into two main areas: strategies for managing disagreements at the point of conflict and strategies for managing conflict upon escalation up the management chain. These methods can help a company move through the conflict that is a necessary precursor to truly effective collaboration and, more important, extract the value that often lies latent in intra-organizational differences. When companies are able to do both, conflict is transformed from a major liability into a significant asset.

Strategies for Managing Disagreements at the Point of Conflict

Conflict management works best when the parties involved in a disagreement are equipped to manage it themselves. The aim is to get people to resolve issues on their own through a process that improves – or at least does not damage – their relationships. The following strategies help produce decisions that are better informed and more likely to be implemented.

Devise and implement a common method for resolving conflict. Consider for a moment the hypothetical Matrix Corporation, a composite of many organizations we've worked with whose challenges will likely be familiar to managers. Over the past few years, salespeople from nearly a dozen of Matrix's product and service groups have been called on to design and sell integrated solutions to their customers. For any given sale, five or more lead salespeople and their teams have to agree on issues of resource allocation, solution design, pricing, and sales strategy. Not surprisingly, the teams are finding this difficult. Who should contribute the most resources to a particular customer's offering? Who should reduce the scope of their participation or discount their pricing to meet a customer's budget? Who should defer when disagreements arise about account strategy? Who should manage key relationships within the customer account? Indeed, given these thorny questions, Matrix is finding that a single large sale typically generates far more conflict inside the company than it does with the customer. The resulting wasted time and damaged relationships among sales teams are making it increasingly difficult to close sales.

Most companies face similar sorts of problems. And, like Matrix, they leave employees to find their own ways of resolving them. But without a structured method for dealing with these issues, people get bogged down not only in what the right result should be but also in how to arrive at it. Often, they will avoid or work around conflict, thereby forgoing important opportunities to collaborate. And when people do decide to confront their differences, they usually default to the approach they know best: debating about who's right and who's wrong or haggling over small concessions. Among the negative consequences of such approaches are suboptimal, "split-the-difference" resolutions–if not outright deadlock.

Establishing a companywide process for resolving disagreements can alter this familiar scenario. At the very least, a well-defined, well-designed conflict resolution method will reduce transaction costs, such as wasted time and the accumulation of ill will, that often come with the struggle to work though differences. At best, it will yield the innovative outcomes that are likely to emerge from discussions that draw on a multitude of objectives and perspectives. There is an array of conflict resolution methods a company can use. But to be effective, they should offer a clear, step-by-step process for parties to follow. They should also be made an integral part of existing business activities–account planning, sourcing, R&D budgeting, and the like. If conflict resolution is set up as a separate, exception-based process – a kind of organizational appeals court–it will likely wither away once initial managerial enthusiasm wanes.

At Intel, new employees learn a common method and language for decision making and conflict resolution. The company puts them through training in which they learn to use a variety of tools for handling discord. Not only does the training show that top management sees disagreements as an inevitable aspect of doing business, it also provides a common framework that expedites conflict resolution. Little time is wasted in figuring out the best way to handle a disagreement or trading accusations about "not being a team player"; guided by this clearly defined process, people can devote their time and energy to exploring and constructively evaluating a variety of options for how to move forward. Intel's systematic method for working through differences has helped sustain some of the company's hallmark qualities: innovation, operational efficiency, and the ability to make and implement hard decisions in the face of complex strategic choices.

Provide people with criteria for making trade-offs. At our hypothetical Matrix Corporation, senior managers overseeing cross-unit sales teams often admonish

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THE THREE MYTHS OF COLLABORATION

Companies attempt to foster collaboration among different parts of their organizations through a variety of methods, many based on a number of seemingly sensible but ultimately misguided assumptions:

Effective collaboration means "teaming."

Many companies think that teamwork training is the way to promote collaboration across an organization. So they'll get the HR department to run hundreds of managers and their subordinates through intensive two- or three-day training programs. Workshops will offer techniques for getting groups aligned around common goals, for clarifying roles and responsibilities, for operating according to a shared set of behavioral norms, and so on.

Unfortunately, such workshops are usually the right solution to the wrong problems. First, the most critical breakdowns in collaboration typically occur not on actual teams but in the rapid and unstructured interactions between different groups within the organization. For example, someone from R&D will spend weeks unsuccessfully trying to get help from manufacturing to run a few tests on a new prototype. Meanwhile, people in manufacturing begin to complain about arrogant engineers from R&D expecting them to drop everything to help with another one of R&D's pet projects. Clearly, the need for collaboration extends to areas other than a formal team.

The second problem is that breakdowns in collaboration almost always result from fundamental differences among business functions and divisions. Teamwork training offers little guidance on how to work together in the context of competing objectives and limited resources. Indeed, the frequent emphasis on common goals further stigmatizes the idea of conflict in organizations where an emphasis on "polite" behavior regularly prevents effective problem solving. People who need to collaborate more effectively usually don't need to align around and work toward a common goal. They need to quickly and creatively solve problems by managing the inevitable conflict so that it works in their favor.

An effective incentive system will ensure collaboration.

It's a tantalizing proposition: You can hardwire collaboration into your organization by rewarding collaborative behavior. Salespeople receive bonuses not only for hitting targets for their own division's products but also for hitting cross-selling targets. Staff in corporate support functions like IT and procurement have part of their bonuses determined by positive feedback from their internal clients.

Unfortunately, the results of such programs are usually disappointing. Despite greater financial incentives, for example, salespeople continue to focus on the sales of their own products to the detriment of selling integrated solutions. Employees continue to perceive the IT and procurement departments as difficult to work with, too focused on their own priorities. Why such poor results? To some extent, it's because individuals think – for the most part correctly – that if they perform well in their own operation they will be "taken care of" by their bosses. In addition, many people find that the costs of working with individuals in other parts of the organization – the extra time required, the aggravation – greatly outweigh the rewards for doing so.

Certainly, misaligned incentives can be a tremendous obstacle to cross-boundary collaboration. But even the most carefully constructed incentives won't eliminate tensions between people with competing business objectives. An incentive is too blunt an instrument to enable optimal resolution of the hundreds of different trade-offs that need to be made in a complex organization. What's more, overemphasis on incentives can create a culture in which people say, "If the company wanted me to do that, they would build it into my comp plan." Ironically, focusing on incentives as a means to encourage collaboration can end up undermining it.

Organizations can be structured for collaboration.

Many managers look for structural and procedural solutions – cross-functional task forces, collaborative "groupware," complex webs of dotted reporting lines on the organization chart – to create greater internal collaboration. But bringing people together is very different from getting them to collaborate.

Consider the following scenario. Individual information technology departments have been stripped out of a company's business units and moved to a corporatewide, shared-services IT organization. Senior managers rightly recognize that this kind of change is a recipe for conflict because various groups will now essentially compete with one another for scarce IT resources. So managers try mightily to design conflict out of, and collaboration into, the new organization. For example, to enable collaborative decision making within IT and between IT and the business units, business units are required to enter requests for IT support into a computerized tracking system. The system is designed to enable managers within the IT organization to prioritize projects and optimally deploy resources to meet the various requests.

Despite painstaking process design, results are disappointing. To avoid the inevitable conflicts between business units and IT over project prioritization, managers in the business units quickly learn to bring their requests to those they know in the IT organization rather than entering the requests into the new system. Consequently, IT professionals assume that any project in the system is a lower priority – further discouraging use of the system. People's inability to deal effectively with conflict has undermined a new process specifically designed to foster organizational collaboration.

those teams to "do what's right for the customer." Unfortunately, this exhortation isn't much help when conflict arises. Given Matrix's ability to offer numerous combinations of products and services, company managers – each with different training and experience and access to different information, not to mention different unit priorities – have, not surprisingly, different opinions about how best to meet customers' needs. Similar clashes in perspective result when exasperated senior managers tell squabbling team members to set aside their differences and "put Matrix's interests first." That's because it isn't always clear what's best for the company given the complex interplay among Matrix's objectives for revenue, profitability, market share, and long-term growth.

Even when companies equip people with a common method for resolving conflict, employees often will still need to make zero-sum trade-offs between competing priorities. That task is made much easier and less contentious when top management can clearly articulate the criteria for making such choices. Obviously, it's not easy to reduce a company's strategy to clearly defined trade-offs, but it's worth trying. For example, salespeople who know that five points of market share are more important than a ten point increase on a customer satisfaction scale are much better equipped to make strategic concessions when the needs and priorities of different parts of the business conflict. And even when the criteria do not lead to a straightforward answer, the guidelines can at least

Blue Cross and Blue Shield: Build, Buy, or Ally?

One of the most effective ways senior managers can help resolve cross-unit conflict is by giving people the criteria for making trade-offs when the needs of different parts of the business are at odds with one another. At Blue Cross and Blue Shield of Florida, there are often conflicting perspectives over whether to build new capabilities (for example, a new claims-processing system, as in the hypothetical example below), acquire them, or gain access to them through an alliance. The company uses a grid-like poster (a simplified version of which is shown here) that helps multiple parties analyze the trade-offs associated with these three options. By checking various boxes in the grid using personalized markers, participants indicate how they assess a particular option against a variety of criteria: for example, the date by which the new capability needs to be implemented; the availability of internal resources such as capital and staff needed to develop the capability; and the degree of integration required with existing products and processes. The table format makes criteria and trade-offs easy to compare. The visual depiction of people's "votes" and the ensuing discussion help individuals see how their differences often arise from such factors as access to different data or different prioritizing of objectives. As debate unfolds – and as people move their markers in response to new information – they can see where they are aligned and where and why they separate into significant factions of disagreement. Eventually, the criteria-based dialogue tends to produce a preponderance of markers in one of the three rows, thus yielding operational consensus around a decision.

New Claims-Processing System

Required Implementation Time Frame	Organizational Experience Level	Availability of Internal Resources	Volatility of Environment	Complexity of Solution	Availability of External Resources	Required Degree of Integration	Required Control	
>12 months	High	High	Low	Low	Low	High	High	**BUILD**
<6 months	Low	High to moderate	Medium	High	High	Medium	Medium	**BUY**
6–12 months	Medium	Moderate to low	High	Moderate	Moderate	Low	Low	**ALLY**

Participant 1 = Participant 2 = Participant 3 = Participant 4 = Participant 5 =

Source: Blue Cross and Blue Shield of Florida

CLASHES BETWEEN PARTIES are the crucibles in which creative solutions are developed and wise trade-offs among competing objectives are made.

foster productive conversations by providing an objective focus. Establishing such criteria also sends a clear signal from management that it views conflict as an inevitable result of managing a complex business.

At Blue Cross and Blue Shield of Florida, the strategic decision to rely more and more on alliances with other organizations has significantly increased the potential for disagreement in an organization long accustomed to developing capabilities in-house. Decisions about whether to build new capabilities, buy them outright, or gain access to them through alliances are natural flashpoints for conflict among internal groups. The health insurer might have tried to minimize such conflict through a structural solution, giving a particular group the authority to make decisions concerning whether, for instance, to develop a new claims-processing system in-house, to do so jointly with an alliance partner, or to license or acquire an existing system from a third party. Instead, the company established a set of criteria designed to help various groups within the organization – for example, the enterprise alliance group, IT, and marketing – to collectively make such decisions.

The criteria are embodied in a spreadsheet-type tool that guides people in assessing the trade-offs involved – say, between speed in getting a new process up and running versus ensuring its seamless integration with existing ones – when deciding whether to build, buy, or ally. People no longer debate back and forth across a table, advocating their preferred outcomes. Instead, they sit around the table and together apply a common set of trade-off criteria to the decision at hand. The resulting insights into the pros and cons of each approach enable more effective execution, no matter which path is chosen. (For a simplified version of the trade-off tool, see the exhibit "Blue Cross and Blue Shield: Build, Buy, or Ally?")

Use the escalation of conflict as an opportunity for coaching. Managers at Matrix spend much of their time playing the organizational equivalent of hot potato. Even people who are new to the company learn within weeks that the best thing to do with cross-unit conflict is to toss it up the management chain. Immediate supervisors take a quick pass at resolving the dispute but, being busy themselves, usually pass it up to *their* supervisors. Those supervisors do the same, and before long the problem lands in the lap of a senior-level manager, who then spends much of his time resolving disagreements. Clearly, this isn't ideal. Because the senior managers are a number of steps removed from the source of the controversy, they rarely have a good understanding of the situation. Furthermore, the more time they spend resolving internal clashes, the less time they spend engaged in the business, and the more isolated they are from the very information they need to resolve the disputes dumped in their laps. Meanwhile, Matrix employees get so little opportunity to learn about how to deal with conflict that it becomes not only expedient but almost necessary for them to quickly bump conflict up the management chain.

While Matrix's story may sound extreme, we can hardly count the number of companies we've seen that operate this way. And even in the best of situations – for example, where a companywide conflict-management process is in place and where trade-off criteria are well understood – there is still a natural tendency for people to let their bosses sort out disputes. Senior managers contribute to this tendency by quickly resolving the problems presented to them. While this may be the fastest and easiest way to fix the problems, it encourages people to punt issues upstairs at the first sign of difficulty. Instead, managers should treat escalations as opportunities to help employees become better at resolving conflict. (For an example of how managers can help their employees improve their conflict resolution skills, see the exhibit "IBM: Coaching for Conflict.")

At KLA-Tencor, a major manufacturer of semiconductor production equipment, a materials executive in each division oversees a number of buyers who procure the materials and component parts for machines that the division makes. When negotiating a companywide contract with a supplier, a buyer often must work with the company commodity manager, as well as with buyers from other divisions who deal with the same supplier. There is often conflict, for example, over the delivery terms for components supplied to two or more divisions under the contract. In such cases, the commodity manager and the division materials executive will push the division buyer to consider the needs of the other divisions, alternatives that might best address the collective needs of the different divisions, and the standards to be applied in assessing the trade-offs between alternatives. The aim is to help the buyer see solutions that haven't yet been considered and to resolve the conflict with the buyer in the other division.

Initially, this approach required more time from managers than if they had simply made the decisions themselves. But it has paid off in fewer disputes that senior managers need to resolve, speedier contract negotiation, and improved contract terms both for the company as a whole and for multiple divisions. For example, the buyers from three KLA-Tencor product divisions recently locked horns over a global contract with a key supplier. At issue was the trade-off between two variables: one, the supplier's level of liability for materials it needs to purchase in order to fulfill orders and, two, the flexibility granted the KLA-Tencor divisions in modifying the size of the orders and their required lead times. Each division demanded a different balance between these two factors, and the buyers took the conflict to their managers, wondering if they should try to negotiate each of the different trade-offs into the contract or pick among them. After being coached to consider how each division's business model shaped its preference – and using this understanding to jointly brainstorm alternatives – the buyers and commodity manager arrived at a creative solution that worked for everyone: They would request a clause in the contract that allowed them to increase and decrease flexibility in order volume and lead time, with corresponding changes in supplier liability, as required by changing market conditions.

IBM: Coaching for Conflict

Managers can reduce the repeated escalation of conflict up the management chain by helping employees learn how to resolve disputes themselves. At IBM, executives get training in conflict management and are offered online resources to help them coach others. One tool on the corporate intranet (an edited excerpt of which is shown here) walks managers through a variety of conversations they might have with a direct report who is struggling to resolve a dispute with people from one or more groups in the company – some of whom, by design, will be consulted to get their views but won't be involved in negotiating the final decision.

If you hear from someone reporting to you that …	The problem could be that …	And you could help your report by saying something like…
"Everyone still insists on being a decision maker."	The people your report is dealing with remain concerned that unless they have a formal voice in making the decision – or a key piece of the decision – their needs and interests won't be taken into account.	"You might want to explain why people are being consulted and how this information will be used." "Are there ways to break this decision apart into a series of subissues and assign decision-making roles around those subissues?" "Consider talking to the group about the costs of having everyone involved in the final decision."
"If I consult with this person up front, he might try to force an answer on me or create roadblocks to my efforts to move forward."	The person you are coaching may be overlooking the risks of not asking for input – mainly, that any decision arrived at without input could be sabotaged later on.	"How would you ask someone for input? What would you tell her about your purpose in seeking it? What questions would you ask? What would you say if she put forth a solution and resisted discussing other options?" "Is there a way to manage the risk that she will try to block your efforts other than by not consulting her at all? If you consult with her now, might that in fact lower the risk that she will try to derail your efforts later?"
"I have consulted with all the right parties and have crafted, by all accounts, a good plan. But the decision makers cannot settle on a final decision."	The right people were included in the negotiating group, but the process for negotiating a final decision was not determined.	"What are the ground rules for how decisions will be made? Do all those in the group need to agree? Must the majority agree? Or just those with the greatest competence?" "What interests underlie the objective of having everyone agree? Is there another decision-making process that would meet those interests?"

Strategies for Managing Conflict upon Escalation

Equipped with common conflict resolution methods and trade-off criteria, and supported by systematic coaching, people are better able to resolve conflict on their own. But certain complex disputes will inevitably need to be decided by superiors. Consequently, managers must ensure that, upon escalation, conflict is resolved constructively and efficiently–and in ways that model desired behaviors.

Establish and enforce a requirement of joint escalation. Let's again consider the situation at Matrix. In a typical conflict, three salespeople from different divisions become involved in a dispute over pricing. Frustrated, one of them decides to hand the problem up to his boss, explaining the situation in a short voice-mail message. The message offers little more than bare acknowledgment of the other salespeoples' viewpoints. The manager then determines, on the basis of what he knows about the situation, the solution to the problem. The salesperson, armed with his boss's decision, returns to his counterparts and shares with them the verdict–which, given the process, is simply a stronger version of the solution the salesperson had put forward in the first place. But wait! The other two salespeople have also gone to *their* managers and carried back stronger versions of *their* solutions. At this point, each salesperson is locked into what is now "my manager's view" of the right pricing scheme. The problem, already thorny, has become even more intractable.

The best way to avoid this kind of debilitating deadlock is for people to present a disagreement jointly to their boss or bosses. This will reduce or even eliminate the suspicion, surprises, and damaged personal relationships ordinarily associated with unilateral escalation. It will also guarantee that the ultimate decision maker has access to a wide array of perspectives on the conflict, its causes, and the various ways it might be resolved. Furthermore, companies that require people to share responsibility for the escalation of a conflict often see a decrease in the number of problems that are pushed up the management chain. Joint escalation helps create the kind of accountability that is lacking when people know they can provide their side of an issue to their own manager and blame others when things don't work out.

A few years ago, after a merger that resulted in a much larger and more complex organization, senior managers at the Canadian telecommunications company Telus found themselves virtually paralyzed by a daily barrage of unilateral escalations. Just determining who was dealing with what and who should be talking to whom took up huge amounts of senior management's time. So the company made joint escalation a central tenet of its new organizationwide protocols for conflict resolution–a requirement given teeth by managers' refusal to respond to unilateral escalation. When a conflict occurred among managers in different departments concerning, say, the allocation of resources among the departments, the managers were required to jointly describe the problem, what had been done so far to resolve it, and its possible solutions. Then they had to send a joint write-up of the situation to each of their bosses and stand ready to appear together and answer questions when those bosses met to work through a solution. In many cases, the requirement of systematically documenting the conflict and efforts to resolve it–because it forced people to make such efforts – led to a problem being resolved on the spot, without having to be kicked upstairs. Within weeks, this process resulted in the resolution of hundreds of issues that had been stalled for months in the newly merged organization.

Ensure that managers resolve escalated conflicts directly with *their* counterparts. Let's return to the three salespeople at Matrix who took their dispute over pricing to their respective bosses and then met again, only to find themselves further from agreement than before. So what did they do at that point? They sent the problem *back* to their bosses. These three bosses, each of whom thought he'd already resolved the issue, decided the easiest thing to do would be to escalate it themselves. This would save them time and put the conflict before senior managers with the broad view seemingly needed to make a decision. Unfortunately, by doing this, the three bosses simply perpetuated the situation their salespeople had created, putting forward a biased viewpoint and leaving it to their own managers to come up with an answer. In the end, the decision was made unilaterally by the senior manager with the most organizational clout. This result bred resentment back down the management chain. A sense of "we'll win next time" took hold, ensuring that future conflict would be even more difficult to resolve.

It's not unusual to see managers react to escalations from their employees by simply passing conflicts up their own functional or divisional chains until they reach a senior executive involved with all the affected functions or divisions. Besides providing a poor example for others in the organization, this can be disastrous for a company that needs to move quickly. To avoid wasting time, a manager somewhere along the chain might try to resolve the problem swiftly and decisively by herself. But this, too, has its costs. In a complex organization, where many issues have significant implications for numerous parts of the business, unilateral responses to unilateral escalations are a recipe for inefficiency, bad decisions, and ill feelings.

The solution to these problems is a commitment by managers – a commitment codified in a formal policy – to deal with escalated conflict directly with their counterparts. Of course, doing this can feel cumbersome, especially when an issue is time-sensitive. But resolving the problem early on is ultimately more efficient than trying to sort it out later, after a decision becomes known because it has negatively affected some part of the business.

In the 1990s, IBM's sales and delivery organization became increasingly complex as the company reintegrated previously independent divisions and reorganized itself to provide customers with full solutions of bundled products and services. Senior executives soon recognized that managers were not dealing with escalated conflicts and that relationships among them were strained because they failed to consult and coordinate around cross-unit issues. This led to the creation of a forum called the Market Growth Workshop (a name carefully chosen to send a message throughout the company that getting cross-unit conflict resolved was critical to meeting customer needs and, in turn, growing market share). These monthly conference calls brought together managers, salespeople, and frontline product specialists from across the company to discuss and resolve cross-unit conflicts that were hindering important sales – for example, the difficulty salespeople faced in getting needed technical resources from overstretched product groups.

The Market Growth Workshops weren't successful right away. In the beginning, busy senior managers, reluctant to spend time on issues that often hadn't been carefully thought through, began sending their subordinates to the meetings – which made it even more difficult to resolve the problems discussed. So the company developed a simple preparation template that forced people to document and analyze disputes before the conference calls. Senior managers, realizing the problems created by their absence, recommitted themselves to attending the meetings. Over time, as complex conflicts were resolved during these sessions and significant sales were closed, attendees began to see these meetings as an opportunity to be involved in the resolution of high-stakes, high-visibility issues.

Make the process for escalated conflict resolution transparent. When a sales conflict is resolved by a Matrix senior manager, the word comes down the management chain in the form of an action item: Put together an offering with this particular mix of products and services at these prices. The only elaboration may be an admonishment to "get the sales team together, work up a proposal, and get back to the customer as quickly as possible." The problem is solved, at least for the time being. But the salespeople – unless they have been able to divine themes from the patterns of decisions made over time – are left with little guidance on how to resolve similar issues in the future. They may justifiably wonder: How was the decision made? Based on what kinds of assumptions? With what kinds of trade-offs? How might the reasoning change if the situation were different?

In most companies, once managers have resolved a conflict, they announce the decision and move on. The resolution process and rationale behind the decision are left inside a managerial black box. While it's rarely helpful for managers to share all the gory details of their deliberations around contentious issues, failing to take the time to explain how a decision was reached and the factors that went into it squanders a major opportunity. A frank discussion of the trade-offs involved in decisions would provide guidance to people trying to resolve conflicts in the future and would help nip in the bud the kind of speculation – who won and who lost, which managers or units have the most power – that breeds mistrust, sparks turf battles, and otherwise impedes cross-organizational collaboration. In general, clear communication about the resolution of the conflict can increase people's willingness and ability to implement decisions.

During the past two years, IBM's Market Growth Workshops have evolved into a more structured approach to managing escalated conflict, known as Cross-Team Workouts. Designed to make conflict resolution more transparent, the workouts are weekly meetings of people across the organization who work together on sales and delivery issues for specific accounts. The meetings provide a public forum for resolving conflicts over account strategy, solution configuration, pricing, and delivery. Those issues that cannot be resolved at the local level are escalated to regional workout sessions attended by managers from product groups, services, sales, and finance. Attendees then communicate and explain meeting resolutions to their reports. Issues that cannot be resolved at the regional level are escalated to an even higher-level workout meeting attended by cross-unit executives from a larger geographic region – like the Americas or Asia Pacific – and chaired by the general manager of the region presenting the issue. The most complex and strategic issues reach this global forum. The overlapping attendance at these sessions – in which the managers who chair one level of meeting attend sessions at the next level up, thereby observing the decision-making process at that stage – further enhances the transparency of the system among different levels of the company. IBM has further formalized the process for the direct resolution of conflicts between services and product sales on large accounts by designating a managing director in sales and a global relationship partner in IBM global services as the ultimate point of resolution for escalated conflicts. By explicitly making the resolution of complex conflicts part of the job descriptions for both managing director and global relationship partner – and by making that clear to others in the organization – IBM has reduced ambiguity, increased transparency, and increased the efficiency with which conflicts are resolved.

Tapping the Learning Latent in Conflict

The six strategies we have discussed constitute a framework for effectively managing organizational discord, one that integrates conflict resolution into day-to-day decision-making processes, thereby removing a critical barrier to cross-organizational collaboration. But the strategies also hint at something else: that conflict can be more than a necessary antecedent to collaboration.

Let's return briefly to Matrix. More than three-quarters of all cross-unit sales at the company trigger disputes about pricing. Roughly half of the sales lead to clashes over account control. A substantial number of sales also produce disagreements over the design of customer solutions, with the conflict often rooted in divisions' incompatible measurement systems and the concerns of some people about the quality of the solutions being assembled. But managers are so busy trying to resolve these almost daily disputes that they don't see the patterns or sources of conflict. Interestingly, if they ever wanted to identify patterns like these, Matrix managers might find few signs of them. That's because salespeople, who regularly hear their bosses complain about all the disagreements in the organization, have concluded that they'd better start shielding their superiors from discord.

The situation at Matrix is not unusual – most companies view conflict as an unnecessary nuisance – but that view is unfortunate. When a company begins to see conflict as a valuable resource that should be managed and exploited, it is likely to gain insight into problems that senior managers may not have known existed. Because internal friction is often caused by unaddressed strains within an organization or between an organization and its environment, setting up methods to track conflict and examine its causes can provide an interesting new perspective on a variety of issues. In the case of Matrix, taking the time to aggregate the experiences of individual salespeople involved in recurring disputes would likely lead to better approaches to setting prices, establishing incentives for salespeople, and monitoring the company's quality control process.

At Johnson & Johnson, an organization that has a highly decentralized structure, conflict is recognized as a positive aspect of cross-company collaboration. For example, a small internal group charged with facilitating sourcing collaboration among J&J's independent operating companies – particularly their outsourcing of clinical research services – actively works to extract lessons from conflicts. The group tracks and analyzes disagreements about issues such as what to outsource, whether and how to shift spending among suppliers, and what supplier capabilities to invest in. It hosts a council, comprising representatives from the various operating companies, that meets regularly to discuss these differences and explore their strategic implications. As a result, trends in clinical research outsourcing are spotted and information about them is disseminated throughout J&J more quickly. The operating companies benefit from insights about new offshoring opportunities, technologies, and ways of structuring collaboration with suppliers. And J&J, which can now piece together an accurate and global view of its suppliers, is better able to partner with them. Furthermore, the company realizes more value from its relationship with suppliers – yet another example of how the effective management of conflict can ultimately lead to fruitful collaboration.

J&J's approach is unusual but not unique. The benefits it offers provide further evidence that conflict – so often viewed as a liability to be avoided whenever possible – can be valuable to a company that knows how to manage it.

Reprint R0503F
To order, see page 151.

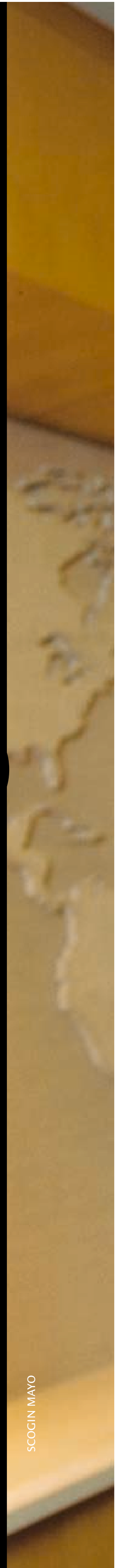
Dell's sustained competitive advantage is due to more than its famous business model. Consistent execution requires real-time P&L management, an emphasis on ingenuity rather than on investment, and a culture of accountability.

Execution Without Excuses

Interviewed by Thomas A. Stewart and Louise O'Brien

MICHAEL DELL FOUNDED the computer company that bears his name in 1984. Eight years later, at the age of 27, Dell became the youngest CEO in the *Fortune* 500. Soon the business world was abuzz with talk about the Dell business model, which allows the company to bypass middlemen, sell directly to customers, and achieve superior management of information and working capital. "The Power of Virtual Integration," HBR called it in a 1998 interview with Michael Dell. Since then, the company has continued to gain market share while delivering better shareholder returns than any of its competitors. Initially capitalized with $1,000, Dell is now worth more than $100 billion.

The secret of Dell's success goes beyond its famous business model. High expectations and disciplined, consistent execution are embedded in the company's DNA. Dell is more than an efficient factory – it's an organization that can turn on a dime and that has demonstrated impeccable timing in entering new markets. The company now employs 53,000 people and operates in more than 80 countries. Last month, its founder and chairman reached the ripe old age of 40. Kevin Rollins, a former Bain & Company consultant who began working with Dell back in 1993 and joined the company in 1996, was appointed CEO last



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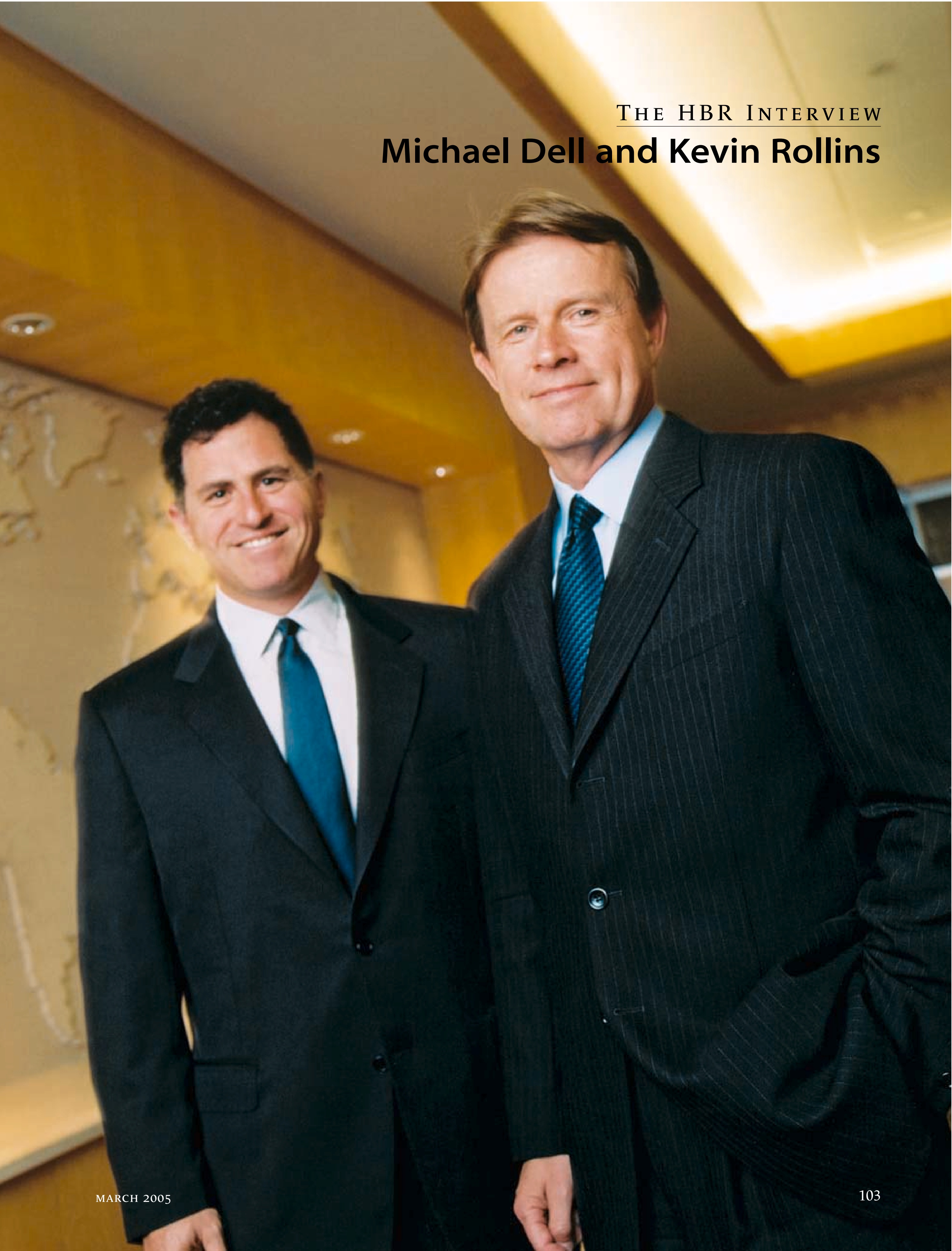
The HBR Interview

Michael Dell and Kevin Rollins



year. Chairman and CEO work in adjoining offices. The wall between them is glass, and it has a large door in the middle that is never closed.

While providing extraordinary rewards to its shareholders, Dell has created a culture that expects great performance from its people. In order to double its revenues over a five-year period, the company has had to adapt its execution-obsessed culture to new demands, as Rollins and Dell reveal. To discuss how the company has sustained its advantage over two decades, Thomas A. Stewart, the editor of HBR, and Louise O'Brien, an HBR consulting editor who served as Dell's VP of strategy from 1999 to 2002, met with Rollins and Dell at the company's headquarters in Round Rock, Texas. In this edited interview, the two describe how they've worked together to refine Dell's business model, management-development structure, and culture.

The elements of the Dell business model are no secret: going direct, information over inventory, world-class manufacturing, and superior customer information. Everybody knows these, so why haven't other companies been able to copy your model or beat you at your own game?

Rollins: The same reason why Kmart can't imitate Wal-Mart. What Wal-Mart does isn't rocket science – it's retailing. Why can't everybody be Wal-Mart or JetBlue or Samsung or whatever the best company in their industry is? Because it takes more than strategy. It takes years of consistent execution for a company to achieve sustainable competitive advantage. So while Dell does have a superior business model, the key to our success is years and years of DNA development within our teams that is not replicable outside the company. Other companies just can't execute as well as we do.

Dell: Culture plays a huge role. As our industry transitioned to a standards-based model from a proprietary model, with its 40% gross margins, protected franchises, and tiered distribution, a whole new set of business disciplines became important. Things like customer-centricity, supply chain logistics, and cash flow management had been completely off the industry's radar screen. Dell changed the game.

Rollins: We started talking about return on invested capital (ROIC), which focuses you on high returns at very low asset intensity. Before that, the market believed heavier asset intensity was better because you could charge huge margins for a proprietary product. We said, "No, that's not the way the world works." Asset reduction, inventory reduction, speed and time consolidation – these became more important than how much you spend on R&D. High R&D spending, when you do it to create proprietary products, leads you into a niche strategy, not a broad-based strategy. Yet many companies continue to argue that the winner will be the biggest R&D spender.

Dell: That paradigm belongs in the Smithsonian with the dinosaurs.

Rollins: Dell changed the strategic success factor for our industry from R&D spending to being the lowest-cost producer of standard technology. No company in the history of mankind that's been a low-cost provider has been a loser. But staying low cost is tough, especially when you have to keep improving your product.

Dell: Proprietary, vertically oriented technology companies believe that you're not a real company if you don't make your own chips and disk drives. Although we've proven our virtual model time and time again, we still see the same skepticism every time we enter new businesses. We're in the printer business now, and people are saying Dell won't get access to printer technology. Well, it turns out there's an abundance of technology available.

Rollins: Our competitors can't beat Dell while also spending a ton of money on R&D and trying to be "invent" companies. Those two goals are mutually exclusive.

So Dell is not an "invent" company?

Dell: We invent quite a bit but have a different approach. Our business model reflects what customers truly believe is important. We were the first in our industry to really embrace the Internet and to identify the role that standards would play in the server and storage markets. We leverage partners where it makes sense, rather than trying to reinvent things that have already been invented. But we've undersold our R&D model. In fact, if you look at the products that still represent most of the industry's revenues – PCs and Intel servers – we're actually doing more R&D than our competitors. We have 4,000 people and we spend $600 million a year on R&D. That's a significant investment, and we've figured out where R&D spending will generate the best return.

For every dollar we put into R&D, we get about six dollars back in profit. When Samsung puts in a dollar, it gets three or four dollars back. Those are both pretty healthy ratios. Microsoft earns about $18 billion in operating income on about $7.7 billion in R&D spending. But Sony invests $1 billion and gets back only $200 million in profits. Sony is overinventing. They invest in things that might be exciting but that aren't valued by customers. So they can't generate good returns.

Rollins: The true test of a company's innovation is whether the customer is willing to pay for it. Struggling companies have a ratio of R&D profits to R&D spending that's less than 1:1. OK companies are about 1:1, and successful companies exceed 1:1.

Dell: Our R&D strategy is shareholder focused. We don't reinvent and we don't do defensive R&D. A lot of the spending by proprietary companies is really to defend against attacks by other companies. They put features in

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their products so that the customer can't use them with other companies' products. For example, we have a competitor that's investing a lot of money to make sure customers can't save money by refilling used-up ink cartridges. Inventions like this might benefit shareholders in the short term, but they certainly don't benefit customers.

We don't waste money building moats and walls. We tell potential component suppliers which product features are important to our customers. If the suppliers' designs include those features, they'll have a better chance of getting our business. And, by the way, we hope they're successful in selling their components to as many companies as possible, because that drives costs down for everyone and we know we'll win our fair share of the market. This is how Dell defines standards. We think standards should be set in the marketplace, not in the patent office. Given our customer relationships and worldwide market share, it's pretty hard to set a standard without Dell's involvement.

> **While Dell does have** a superior business model, the key to our success is years and years of DNA development within our teams that is not replicable outside the company. [Rollins]

How did Dell's DNA become so different from others' in your industry?

Dell: I founded the company over 20 years ago with $1,000 in starting capital. By contrast, Compaq had been launched two years earlier in Texas with $100 million in capital. That's an unbelievable difference. Dell bubbled up through a kind of Darwinian evolution, finding holes in the way the industry was working. We didn't become asset-light just because it was a brilliant strategy. We didn't have any choice.

Rollins: History was the starting point for our culture. But by the mid-1990s, we had plenty of money. The issue was no longer necessity; we'd just found a better way to run a business. But we needed to articulate the strategic principles of our business model for customers, employees, and investors.

So we defined a complete set of management principles, with metrics, to the nth degree. Things that had been necessities at Dell became virtues. Although we didn't have much in the way of assets, we decided we should have even less. We knew that poor quality costs money. We knew that too much time in the cycle from order to delivery costs money. No inventory is better than any. With the steep depreciation curve for components in our business – they're like fish or vegetables – the value goes away the minute you buy them. Everyone at Dell came to understand these principles. We began to rigorously measure DSI (days of sales in inventory) and stamp it on the forehead of anybody who had anything to do with development, purchasing, or manufacturing.

Dell: In our industry, with all the permutations, combinations, and transitions, it's impossible to forecast. By getting rid of inventory, we created a pull rather than a push system and eliminated the need for a crystal ball.

How did you implant the Dell DNA throughout the company?

Rollins: We drummed into our people's heads, through presentation after presentation, what's good performance and what's bad performance. They saw data on inventory every day. They got rewarded when inventory came down and punished when inventory went up.

Dell: By the way, the reward and punishment didn't come from us, it came from our people seeing for themselves how much better their businesses worked when they didn't have inventory.

Rollins: Another lesson we implanted was how to contain operating expenses while increasing margins and growth. That sounds pretty basic, but most companies can't do both. Many companies like to talk about investing for the future. We say the future is today and tonight. Good execution requires a sense of urgency. The notion of investing for the future can become a trap.

Dell: Of course, there are times when we have to make investments that take a few years to fully pay back. But to Kevin's point, we don't tolerate businesses that don't make money. We used to hear all sorts of excuses for why a business didn't make money, but to us they all sounded like "The dog ate my homework." We just don't accept that. Our shareholders don't pay us to sit around and lose money.

If you're a Dell manager and your product or sales region falls off track and starts losing money, what happens to you?

Rollins: You become a pariah.

Dell: It hasn't happened recently.

Rollins: We've had a no-excuses culture from the beginning. Whenever we hear that a business might have to lose money for a while, we challenge the GM to figure out how to run the business better than anyone ever has and not lose money.

Dell: If you start accepting the idea that a business doesn't have to make money–for reasons that you might convince yourself are real–then that's what happens. The opposite is also true. If you say, "No, we're going to make this business profitable," good things happen. Of course, the first kind of culture is easier to live in than the second.

Rollins: I'm not saying we're the only real men in the world, but we set expectations very high.

Isn't there more to creating a high-performance culture than setting high expectations?

Rollins: It requires discipline and consistency. We know, down to our toenails, that our model works. When Dell fails to execute, it's either because the GM is applying the model wrong or he's not the right GM. In either case, Michael and I are to blame.

Over time, we've steadily improved the managerial talent at Dell. Our team of general managers is now very strong. They've learned the discipline, they have what it takes, they understand the model. So when they miss, it's just a failure to execute. And we're pretty hard on people who miss–not just the two of us but the whole company. When you fail to execute, our culture says, "Fix it. Find what's wrong, and fix it. Or ask for help."

Dell: We all make mistakes. It's not as though at any given time, Dell doesn't have some part of the business that's not working for us as it should. But we have a culture of continuous improvement. We train employees to constantly ask themselves: "How do we grow faster? How do we lower our cost structure? How do we improve service for customers?"

Is it as tough as it sounds to be a general manager at Dell?

Rollins: It's really tough. To succeed as a GM here, you have to be smart and you have to be tough. You have to be a team player, and you have to understand the P&L. You're in trouble if you don't understand the P&L.

Sometimes our managers think that what we've asked them to do is irrational. But the fact of the matter is our general managers have succeeded time and time again. When we hold somewhat irrational expectations and convince them they can do it, they come up with fantastic breakthroughs. We challenge our people to substitute ingenuity for investment.

Dell: In the late 1990s, we were growing really fast and bringing lots of new talent on board. We used to just throw people in the deep end and see if they'd sink or swim. If they couldn't swim, we'd get someone else.

Rollins: Now we believe we owe our managers more than that. Part of the problem was we were hiring the wrong people – people who weren't going to be able to swim at Dell. I think we've gotten better at picking people. We've also gotten better at developing them.

Five years ago, we weren't spending much senior-manager time on people development. That has changed dramatically. Our promotions to VP and director have shifted from about 75% outside hires and 25% promotes from within to about 30% outside and 70% within. We now understand this yields better results. There's less risk than in hiring random executives from outside. You've seen your own people. You know what they can do. And you know they've already got the DNA.

So we now give lots of swimming lessons. But if you still can't swim after the lessons, then this is going to feel like a tough place to work.

> "Dell bubbled up through a kind of Darwinian evolution, finding holes in the way the industry was working. We didn't become asset-light just because it was a brilliant strategy. **We didn't have any choice.**" [Dell]

Are you managing by fear? Or by truth telling?

Rollins: We've tried to create a culture where openness and honesty are encouraged.

I think there was a time when people were afraid, but even then, the fear of not telling the bad news was greater than the fear of telling.

Dell: The worst thing you can do as a leader at Dell is to be in denial–to try to convince people that a problem's not there or play charades. A manager is far better off coming forward and saying, "Hey, things aren't working, here's what we think is wrong, here's what we're going to do about it." Or, even, "Hey, I need some help. Will you help me?" That manager won't have a problem. The manager who covers up and says it's really not as bad as it looks–he'll have a big problem.

Rollins: Our culture has evolved from a fear of the consequences of not telling, to where you just know you have to tell. It's the way we all operate. Everybody sees everybody else's numbers and gets to help with suggestions about their businesses. Here you can't tell your boss or your peers, "Stay out of my business." Openness and sharing are part of success at Dell.

Dell: We also have a huge number of people inside the company with incredibly accurate and detailed information about a whole range of things. That level of transparency makes it difficult to hide a problem.

Rollins: Like many companies, we're organized in a matrix of sales regions and product groups. Then we break each of those groups down to a pretty fine level of subproducts and sales subsegments. Dell has more P&L managers, and smaller business units, than most companies its size. This not only increases accountability to the customer, it helps train general managers by moving them from smaller to larger businesses as their skills develop.

Our matrix organization has a third level – our business councils. For example, we have a small-business sales group in each country, along with product development people who become very familiar with what small-business customers buy. In addition, we have a worldwide small-business council made up of all our small-business GMs and product managers. Everyone in these councils sees everyone else's P&L, so it provides another set of checks and balances.

Dell: Our performance metrics are the same around the world, which allows us to identify the best practices on any given dimension: generating leads, increasing margins, capturing new customers. If a council sees that Japan has figured out a great strategy for selling more servers, its job is to learn how Japan is doing that and transfer the lessons to other countries.

Information is our most important management tool. Our salespeople know the margin on a sale while they're on the phone with the customer. This financial data is in real time, so our people know if there's a problem. If the folks in our consumer business notice it's 10 AM and they're not getting enough phone calls, they know they have to do something: run a promotion on the Web, starting at 10:15, or change their pricing or run more ads. They can't wait until 30 days after the end of the quarter to figure it out.

Rollins: And they don't need to call us for permission. If they don't change something now, they can't come to us at the end of the quarter and say, "I guess we should have taken action in the middle of the quarter when we knew something was wrong."

Dell operates with a lot of data, and analyzing data takes certain skills. Is there a Dell decision-making model?

Rollins: There is, but it's not perfectly articulated. The first rule is: Make your decision fast – even if you don't have complete data. Get the best data you can, because making a decision with no data is a sin. But delaying a decision while you overanalyze the data is not good.

Dell: We don't have a lot of layers. Extra layers, approvals, and meetings just slow things down. Our organization is flat so that information can flow freely and quickly.

Rollins: We have a strong bias toward action and a strong bias toward data.

Dell: Any Dell presentation – it doesn't matter what part of the company it's from – will have lots of data. That's just the way we manage. Our number-to-word ratio is really high.

Rollins: Many companies believe in massive delegation – which has some advantages but also a lot of negatives. Michael and I like to roll up our sleeves. Our years of experience with the model allow us to spot trends that others in the organization might miss. Michael and I probably know a lot more and make more decisions than many CEOs do, but we also have a lot more people involved in decision making at Dell than you might find at other companies, because a lot of people here own P&Ls.

How do your decision-making styles differ?

Dell: We're pretty complementary. We've learned over time that each of us is right about 80% of the time, but if you put us together, our hit rate is much, much higher. We each think about a slightly different set of things, but there's a lot of overlap.

Rollins: We're both opinionated, but we also realize that listening to one another is a good thing. We have a lot of trust in each other's judgment.

Dell: Leaders have to show that they know the *way,* even if they have no idea what to *do.* The truth is that we probably have a lot more fear than we're displaying. We think about failure all the time. I think about failure all the time. We've been able to simulate failure in our minds –

Rollins: – before it happens –

Dell: – and avoid extinction or disastrous consequences because we've thought through all the bad things that could happen.

You two have been a team for many years. Now Kevin is CEO and Michael is chairman – how does that relationship work?

Dell: We're very collaborative. We share all the issues and opportunities. It's not at all a typical hierarchy, and this transition was not at all a typical CEO-to-chairman transition. The traditional distribution of labor doesn't really apply. Everybody likes to try to stereotype us, put us in boxes. "OK, now I get it, you do technology and you do operations." They're all wrong.

Rollins: The nuance is not what we each do, but where our expertise lies. Michael's expertise lies more in technology. My expertise lies more in the institutionalization of running a big company. But we both do strategy, we both meet with customers, we both manage the P&L.

Dell: In any given week, you could take my entire schedule and give it to Kevin, and he could do what I do. Quite well. And I could take his entire schedule and do those things pretty well, too. To some extent there's a divide-and-conquer element. You can't be in all places at all times. It's a myth that one person can really run a company.

Rollins: Either he doesn't actually run it, or he dies trying. Michael and I can see twice as many customers as a CEO alone would be able to see. We can meet with twice as many employees. The two of us *can* be all over the map.

Dell: Ultimately, we make much better decisions because each of us comes up with ideas that aren't fully developed, we work through them together, and we end up with better decisions. For example, we both recognized the strategic importance of printers, but we debated the fine points between ourselves, and this led to a better decision process and rollout.

Rollins: From the beginning, Michael was enthusiastic about getting into printers, whereas I was a little risk averse. With regard to our storage partnership with EMC, our positions were reversed. So it's not as though one of us always plays the optimist and one the pessimist. In both cases, we each talked a lot about the issues and our concerns and got the other comfortable. Then we proceeded as a team.

Does Dell make fewer bad decisions than most companies because of your joint leadership?

Dell: Absolutely. In our business, it's easy to get caught up in the excitement of the latest technology development, so Kevin and I ask a lot of questions. When someone runs into our offices saying, "We've got to do tablet computers," because Microsoft says we should, or because everyone else is doing them, we ask, "How's this going to work? How big's the market? What's it going to cost us? And do we have the organizational bandwidth to handle it?" Because you can't do everything at one time and expect to succeed across the board.

Rollins: Few things clear all the hurdles. At one time, printers didn't quite fit – that's why I was a little nervous about going into the business. But Michael felt we had to go after printers because of the ridiculous margins one of our competitors was using to subsidize its fight against us in PCs and servers. So we kept messing with it, and before long we found a way to make it fit.

Is there an innate conservatism in Dell's decision making?

Rollins: We're very risk averse. Occasionally our managers develop emotional connections to businesses that they really want to drive. But we make them prove the opportunity to us, and if we're not convinced, we don't move forward. We avoid areas where it's not clear we can be successful.

Dell: In our industry, many promising new ideas become short, dead-end roads. We have a pretty good record of not going down them. That's why our competitors accuse us of not being innovative – because we're not investing in tablet computers or artificial intelligence.

But are we innovative? Show me another company that's 21 years old, has $50 billion in revenue, and hasn't done acquisitions. We've achieved massive organic growth, despite our caution about entering new businesses. We've led the market in the areas of innovation we believe will be important to customers – like the Internet, the commoditization of servers and storage, and converting from CRT monitors to LCDs. In our industry, there's always a better alternative to getting into or staying in a bad business. We're not looking for the most challenging problems, we're looking for the easiest problems that have the most opportunity.

You've had to adjust your business model as the company has grown. How have you needed to change the culture?

Rollins: In 2000, our industry went through a major downturn, and the company's growth flattened out for a couple of years. Our people started asking questions like: "Is it over? Why am I here? Am I developing as a professional?" We learned about these concerns through our Tell Dell employee survey. It helped us realize that we were in sort of a crisis. We had to address the gaps in our culture or we wouldn't be able to keep growing.

Historically, working at Dell was about money – becoming a Dellionaire – not about working for the best company. The Tell Dell survey indicated that 50% of our people would have been willing to leave the company for a comparable job elsewhere. That's a terrible number. We had a very visible group of employees who'd gotten rich from stock options and considered themselves volunteers–meaning they'd check out any time they wanted.

Dell: The mind-set was "What are you going to do for me?" as opposed to "What can I do for the company?" Some of this was the result of the larger bubble in the economy. Expectations everywhere had grown to the sky. Getting rich was way too easy.

Then the market crashed. Dell's crash was not nearly as severe as our peer group's, but in a perverse way, this kept expectations higher here. Our punishment for doing well during challenging times was that our people thought they could leave any time they wanted.

Rollins: Our culture was becoming the culture of the stock price. Everybody at Dell, down to the shop-floor person, followed the stock price. You can't build a great company based on employees who say, "If you pay me enough, I'll stay. If you don't, I'm leaving." We had to reignite the spirit of the company, and we couldn't do it with the stock price, because the stock had busted.

Dell: We knew we couldn't get to $60 billion in revenue without changing the culture. But it's not like you just flip the switch and it's done. First, we implemented Tell Dell to measure how good a job we were doing of managing people. The survey is voluntary, and 92% of our employees participate. Based on what we learned from Tell Dell, Kevin created the Winning Culture initiative, which has become a top operating priority at Dell.

Rollins: We asked, "What's the social contract we offer at Dell?" That led us to define the Soul of Dell: Focus on the customer, be open and direct in communications, be a good global citizen, have fun in winning. These were all elements of our traditional culture that had just never been articulated.

Dell: How were all the new people we were adding in Asia and Europe going to understand what we were trying to do? It was imperative to articulate the Soul of Dell. And it turned out to be a huge motivator for our teams.

You'd gotten to the top of your industry and were still highly successful financially – what convinced you two data-driven guys that this was a crisis?

Dell: Here's the data-driven answer: We did the math.

Rollins: We looked at how many people we'd have to hire if we wanted to double our revenue – how much new talent we'd have to find if 50% of our people left the company. We couldn't do it.

Dell: And when we talked to our people, we could just sense their desire for more professional development. Throughout the first 18 years of our history, we had very specific and measurable financial objectives. The people stuff was there, but we didn't emphasize it the way we did the financial goals. The surveys told us that we had to get more serious about developing managers. This was also what the company needed in order to grow. So we launched the Leadership Imperative.

> "It's a myth that one person can really run a company." [Dell]
>
> **"Either he doesn't actually run it, or he dies trying."** [Rollins]

Rollins: Michael and I also each went through a 360-degree feedback process. Our executive team told me that I sometimes acted as though I had all the answers and that I could come across as arrogant and aloof.

Dell: They told me I didn't give enough positive feedback. That was because I've never required a lot of personal recognition myself. I've already gotten way more than I need. I'm actually suspicious when I get positive feedback.

Rollins: This was a blind spot for both of us, because personally we've never needed a lot of outside validation. And we created a management team that didn't need it because we never gave it to them. We thought, "If you need to have someone tell you you're good, you probably don't belong at Dell. You're obviously not strong enough to be here."

Dell: I also learned from the 360-degree reviews that I needed to do a better job of connecting with people – relating to people as human beings who wanted connection and recognition, not mere abstract objects doing work. I've always really enjoyed business problems and didn't feel as much need for connection as our team clearly wanted. It took me a while to see how important this quality of relationships is in building loyalty to the company.

Rollins: We just didn't get it. That was a mistake, because obviously everybody needs positive feedback, even though some of our team tried to pretend they didn't.

Dell: In 2001, we took an important step in making Winning Culture one of four strategic initiatives for the corporation. For the past decade, we've identified three major objectives every year – the same initiatives, supported by the same metrics, everywhere in the world. They help the entire organization stay focused on what we're trying to accomplish, typically in customer experience, product leadership, and globalization. We calculate performance bonuses based on strategic initiatives, as well as on growth and profitability.

A lot of our success is due to the fact that we've been able to pick the right things at the right time and align the entire worldwide organization around them. So placing Winning Culture on this list was a big statement inside the company. Of course, there was some skepticism in the first year or two.

Rollins: Initially, people didn't believe we were serious about leadership development because we hadn't yet put any meat on the bones. So we began to develop a set of management tools, and we told managers if they didn't perform on the Tell Dell metrics, it would affect their pay.

Just as we shared our feedback with our team, we insist that all managers share their Tell Dell results with all of their people. We said, "If Michael and I can improve, then everyone can improve." Tell Dell has become a referendum on the executives, including us. We have to share the results with our board. So now we all have someone looking over our shoulders.

How does your leadership development work?

Rollins: The structure is similar to GE's. They have three levels in their Session C program. So far, we have only one, but we'll probably add another next year. We'd like it to be a graduated program that tracks our high-potential employees throughout their Dell careers.

Our own executives teach, and we use our own material and facilities. Rather than bringing employees to a central location, as GE does, we travel to them. Either Michael or I meet with the top 10% of Dell managers around the world every quarter and give them a short training dose. We also have an intense ten-day leadership training program, which our people tell us is the best session they've ever attended.

It's been a huge retention tool among our high potential employees. We were surprised at how well they responded to the time and attention from us and other senior executives. Our future leaders get lots of benefits from participating in the program, but knowing we value them as our next generation is the most important.

Dell: Kevin and I each spend three full days teaching. We review individual development plans, compensation, and career paths for all these people. We now consider them the corporate talent, and they're "owned" by the office of the CEO, not by their immediate supervisors.

Rollins: Developing people is now part of the GM job at Dell. Our senior managers are measured and compensated on it. If we'd put in place a program without metrics, no one would have taken it seriously.

> **Michael and I aspire to great things.** We want a culture that makes people stick around for reasons other than money. [Rollins]

In five years, will Dell be known as a great place to have worked? Will other companies be trying to poach your people?

Rollins: They already are. They think hiring a Dell manager will allow them to replicate our operational and financial success. But it's not that easy. If you hire a Dell-trained GM, you'll get a smart, tough P&L manager. But a single manager cannot create Dell. That's why Michael and I don't take as much credit for the success as people might like to give us. It's taken a team of a lot of people to create Dell.

A Dell GM couldn't be as successful without the tools he gets at Dell. At another company he'd find himself asking, "Where's my dashboard? Where's all the talent?"

It would be much harder to start over at another company, hoping for an uncertain return, than to stay here in this winning environment and get a predictable return. I think that's why none of our guys have left.

Are you satisfied with the results?

Rollins: For the first couple of years after we introduced Tell Dell, the scores were flat. We needed to make sure our executive team wanted to stay, in order for them to get their teams to want to stay. It had to start with us and move down through the organization.

After two years of flatlining, we're now seeing very encouraging results. On the first survey after implementing our Leadership Imperative, we saw a nice bump in scores. The second time, they bumped again. The third time, another bump.

Dell: Our employees now know we're serious about our Winning Culture and people development. If a manager's Tell Dell scores are in the lower quartile and not improving, he's got a big problem. You can't get promoted if you're not taking Tell Dell metrics seriously and embracing the notion of a Winning Culture.

Has all of this focus on people made Dell a kinder, gentler company?

Rollins: I'm not sure that was the intention, but I suppose it has. We've changed as individuals and as an organization – and it wasn't just about feedback or the fear of not reaching our goals. Both Michael and I aspire to great things. We've already created the best supply chain management model and one of the most financially successful companies ever. Everybody acknowledges that. We want the world to see not just a great financial record and operational performance, but a great company. We want to have leaders that other companies covet. We want a culture that makes people stick around for reasons other than money. We want Dell to be such a great place to work that no one wants to leave.

Dell: Of course, adding people development to our top initiatives doesn't take the pressure off driving for financial results. A key component of the Soul of Dell is winning. We care about our people, but we don't exist to make people feel good. We want to win and have fun at the same time.

Rollins: You don't find companies that have great winning cultures and terrible financial results. If a company with great financials and a great culture sees results start to slide, the culture will die real fast. So we've told our people that we're building a winning culture on top of great financial results. If we stop delivering results, the culture will slide into the ditch. We have to keep them both going.

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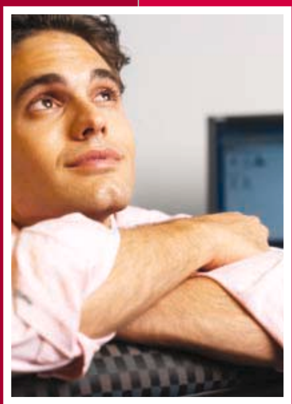
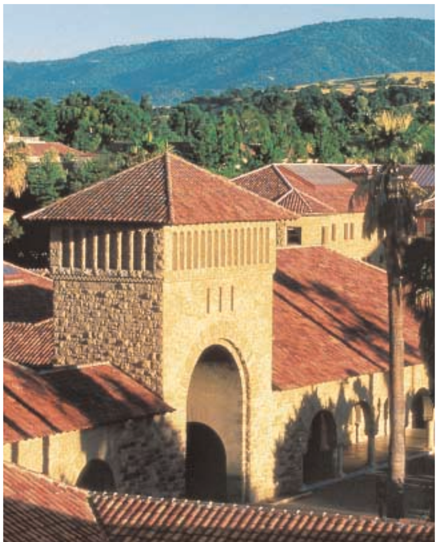
To order, see page 151.

DAVE CARPENTER

"Ms. Harris, will you please put this somewhere where I won't run across it again?"





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Diversity:
The Performance Factor

Illustrated by Chris Murray

by Michael L. Wheeler

Once written off by some as the latest corporate fad, diversity may, in fact, prove to be the single most important performance factor of the 21st century. Diversity's emergence as a critical performance factor is evidenced in new research; the growing number of corporate success stories; the increasing commitment of corporations, including the introduction of a CDO (Chief Diversity Officer) or similarly titled senior executive charged with overseeing diversity efforts; greater accountability measures; and new performance models. The reason is simple: The diversity of our global population affects every facet of business and society.

By linking diversity initiatives to core strategy, many business leaders are able to dramatically improve their companies' productivity, negotiating power, and problem solving; increase sales and profits; foster innovation; reduce costs; sustain competitiveness; and ultimately improve shareholder value.

What *Is* Diversity?

The term *diversity* describes the global economic village of myriad cultures, languages, races, ethnicities, and world views. For business, diversity represents the inexorably intertwined global marketplace, talent pool, vendors, and suppliers; the countries in which we operate; the governments with which we negotiate; and the communities in which we live. It is reflected in our laws and our values.

Corporate diversity initiatives are the proactive (and sometimes reactive) strategies and tactics developed to meet the challenges, address the issues, and, ideally, leverage diversity as a competitive advantage and opportunity.

Over the last 40 years, history has played a large role in helping corporations recognize and leverage diversity. The civil rights movement

and key legislative acts such as Equal Employment Opportunity, Affirmative Action, and, more recently, Sarbanes-Oxley, have continually raised the bar for accountability. In best practice companies, though, diversity is a move from mere compliance to proactive engagement of the world's greatest natural resource: people. Drivers may change, but the basic premise remains the same—the full engagement of talent and respect for all.

Business Opportunity, Not Business Case

In his MIT Sloan School of Management research report, *The Effects of Diversity on Business Performance: Report of the Diversity Research Network*, Thomas Kochen concludes: "There is little point in continuing to ask whether diversity's impact is naturally good or bad. Instead, managers and researchers alike should recognize that diversity has become an inescapable social fact and figure out how to maximize its benefits while minimizing its negative effects."

Diversity is creating a sheer force of inescapable change for corporations. A company's ability to align, integrate, and leverage diversity initiatives will determine its success in the 21st century. Kochen explains: "Organizations that invest their resources in taking advantage of the opportunities that diversity offers should outperform those that fail to make such investments.... The literature suggests that diversity, if unattended, is likely to have an adverse effect on group processes, such as communications, conflict, and cohesion.... To be successful in working with and gaining value from this diversity requires a sustained, systemic approach and long-term commitment." A company's overall market performance is directly linked to its ability or inability to create strategies and tactics that leverage the Diversity Performance Factor.

The Diversity Performance Factor: The "Soft Stuff" Is the Hard Stuff

The Diversity Performance Factor is the nexus, the convergence, the intersection, at which diversity can be an enabler or inhibitor—an advantage or disadvantage—to achieving business success (see exhibit).

The Diversity Performance Factor includes many variables: race, gender, ethnicity, culture, language, religion, sexual orientation, and class, socioeconomic, and even functional differences within an organization. It comes in the form of systemic racism, sexism, xenophobia, and homophobia, and systems that are misaligned with current business reality. It also includes issues that arise due to differences and systemic bias, such as adverse effect on group processes, breakdowns in communication, conflict, and poor morale. It encompasses different world views, new ideas, different ways of doing things, unique perspectives and skills, talents, and abilities. It occurs at any point where exclusion or inclusion is based upon some typically subjective factor.

DIVERSITY AND TALENT

"From our work globally, we have observed the wide range of strategies that organizations have been using to competitively market their employer brands and to recruit diverse talent. We have also witnessed the diligent ways that employees are now researching potential employers. Market leaders will be organizations that will competitively harness where diverse populations will want to work, spend, and invest."

Dr Glenda Stone, CEO, **Aurora**

Intersections and Convergence: When differences converge, or create what Frans Johansson, author of *The Medici Effect* (HBS Press, 2004) calls an "intersection," it potentially creates "a place where ideas from different fields and cultures meet and collide, ultimately igniting an explosion of extraordinary new discoveries." Johansson explains: "Innovators change the world by stepping into the intersection."

Some people thrive in the intersection, but for many, intersections are frightening and disconcerting—more like stepping into the great unknown. Without awareness, skills, openness, and a real competence for maximizing opportunities, these intersections become culture clashes, breakdowns in communication, and misunderstandings. The result: missed opportunities, lower productivity, turnover, and direct and indirect costs. The costs can be devastating: a failed marketing campaign, a lost contract, class-action lawsuits, or a tarnished public image. More often than not, it is the intangibles—what some call the "soft stuff"—that have the greatest impact on business performance. Instituting a comprehensive diversity strategy helps create a process that allows for these intersections to be effective—and in the organizational sense, be the point of opportunity.

The Diversity Performance Factor model demonstrates how these factors come into play and how specific interventions can turn a challenge into an opportunity for performance enhancement. In his September 2004 HBR article, "Diversity as Strategy," David Thomas writes about IBM's ability to expand minority markets dramatically by promoting diversity in its own workforce: "The result: a virtuous circle of growth and progress."

Diversity as Strategy

According to a 2001 Conference Board research report, *The Diversity Executive*, there are three key drivers behind diversity as strategy: the marketplace, talent, and organizational effectiveness. These three components are interdependent. IBM's Ted Childs captures the logic: "Diversity is the bridge between the workplace and the marketplace." Diversity as strategy involves the creation, retention, and development of a globally diverse workforce and then using this diversity as a strategic advantage in the marketplace.

Organizations like IBM, Safeco, Haynes and Boone LLP, and Texas Instruments understand how viewing diversity as strategy makes a difference.

- At Safeco, "valuing diversity" is a universal competency for success. Safeco's Kevin Carter, leader, corporate diversity initiatives, explains: "Safeco wants to sell insurance to as many people as possible, and we know America is becoming increasingly diverse. We're better off considering differing ideas and perspectives because inclusion of others often leads to better ideas and business results."
- When Haynes and Boone bid for a contract with Shell Oil, diversity was one of the requirements that helped them win the bid. Robert Wilson, managing partner at Haynes and Boone, explains: "We would not be a successful law firm without having recognized long ago that diversity is one of the key differentiators between a good firm and a great firm. Diversity at Haynes and Boone goes well beyond any coordinated effort; it's part of our culture."
- In 2004, the Texas Instruments Diversity Network (TIDN) asked a cross-section of diverse TI employees to join in an unusual and particularly daunting pilot project: to apply their unique knowledge and abilities to a significant problem-solving effort involving crucial cross-cultural communications. The effort galvanized this very diverse group and yielded an excellent business outcome. TI began to envision contributions TIDN might bring to other operations, such as TI's worldwide purchasing group, its sales and marketing operations, and its quality teams.

DIVERSITY AS STRATEGY

"Diversity is a key corporate strategy and a guiding principle behind the way we do business. New York Life continually strives to build a diverse workforce, and to ensure that all employees are given equal and ample opportunities to maximize their potential and establish successful careers. Diversity enables us to better serve our customers. It strengthens the workforce by broadening the pool of talent, which results in more innovative products and services."

Angela Coleman, vice president, human resources
New York Life Insurance Company

These companies apply both strategic and tactical approaches to enhance their business success and to realize the full potential of their diversity initiatives.

Next Practices for Performance Enhancement and Unleashing Potential

There are four critical steps to building competence and unleashing the potential of a diverse workforce: 1) understanding and overcoming barriers; 2) establishing a strong foundation; 3) recognizing universal themes about human and organizational behavior; and 4) creating real intersections to leverage diversity and enhance performance.

Overcoming the Barriers: Several barriers exist that prevent companies from fully engaging diversity as a way to maximize performance. Systemic barriers include racism, sexism, xenophobia, and homophobia. Issues facing women and people of color and other marginalized groups are not validated or seen as significant. The diversity executive may not have the real power or influence needed to do his job. Programmatic barriers include initiatives where diversity is retrofitted into current or archaic business processes and practices. White males are often left out of the diversity equation. At times, the implications of race, gender, and ethnicity are oversimplified, reinforcing stereotypes. People in charge of diversity initiatives may not have the skills and qualifications to be effective. Political correctness, too, is a barrier: Prejudice and bias go underground and are not seen as blatant discrimination. The biggest barrier is the failure to address issues honestly and with a real commitment to change and inclusion.

Building a Strong Foundation: The diversity executive plays a critical role in integrating diversity as a performance factor for success. Their objectives are:

- *Strategic direction*—aligning diversity with business goals and objectives.
- *Integration of diversity into key business and human resources practices, initiatives, and objectives*—ensuring that diversity is a consideration in every business initiative and policy; building a diverse workforce top down; ensuring an inclusive work environment; and leveraging diversity.
- *External relations*—providing a link between the corporation and communities, educational institutions, advocacy organizations, and the government.
- *Communication*—keeping the organization informed, and making sure that issues and progress are constantly on managers' and employees' radar screens.
- *Consulting and executive coaching*—helping leaders understand diversity issues and offering guidance on how to effectively handle them.
- *Relationship building*—as a catalyst, the diversity leader depends upon others to reach the entire organization and to drive change.
- *Metrics and accountability*—maintaining workforce balance, work environment, and instilling performance and leadership accountability measures as integrated performance measures. The CEO and top management team must lead the charge.

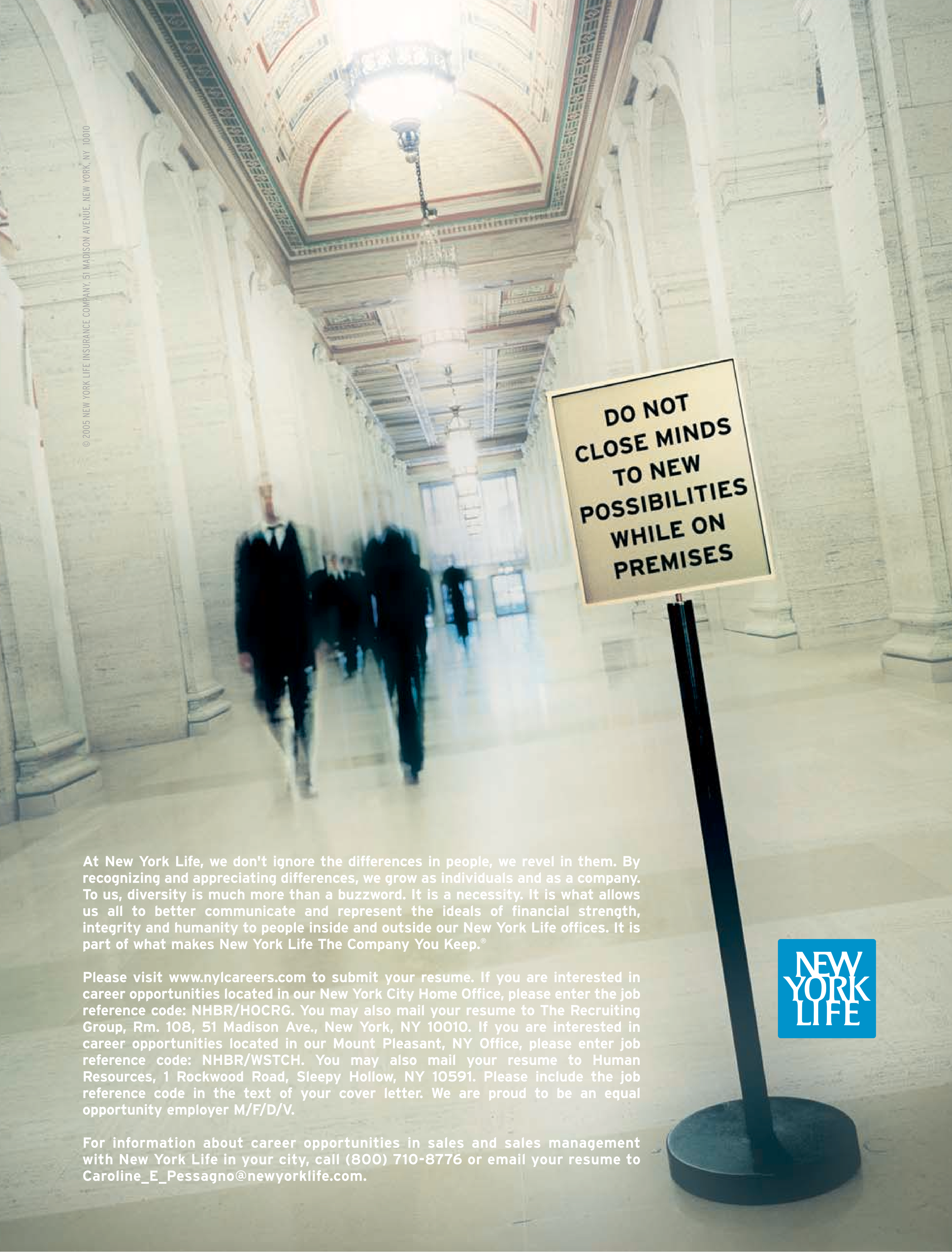
DIVERSITY AND INNOVATION

"Agilent stands at the edge of a global business era in which our ability to innovate and commit to excellent results are key to our success. Every step we take to leverage our global diversity as a competitive advantage is a step toward this goal. Our current global diversity and inclusion strategy ensures that global leaders are confident working across cultures and are inspiring breakthrough innovation within their teams."

Alma Vigo-Morales, director, global diversity
Agilent Technologies

Universal Themes: Understanding the psychosocial implications of change and differences and recognizing commonalities among those differences will greatly enhance a company's ability to leverage diversity as a driver of performance. Here are critical and universal factors to consider:

1. We all crave respect.
2. People want to be heard and validated for who they are.
3. We all have a world view.
4. People like to be with people who are like themselves but can learn to value differences.
5. It is as important to consider the majority as it is the minority.
6. The workplace is unique. Corporations have a tremendous opportunity to be learning labs that can positively influence society by providing examples of behavior that supports inclusion.
7. Exposure to difference is critical.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DO NOT CLOSE MINDS TO NEW POSSIBILITIES WHILE ON PREMISES
At New York Life, we don't ignore the differences in people, we revel in them. By recognizing and appreciating differences, we grow as individuals and as a company. To us, diversity is much more than a buzzword. It is a necessity. It is what allows us all to better communicate and represent the ideals of financial strength, integrity and humanity to people inside and outside our New York Life offices. It is part of what makes New York Life The Company You Keep.®
Please visit www.nylcareers.com to submit your resume. If you are interested in career opportunities located in our New York City Home Office, please enter the job reference code: NHBR/HOCRG. You may also mail your resume to The Recruiting Group, Rm. 108, 51 Madison Ave., New York, NY 10010. If you are interested in career opportunities located in our Mount Pleasant, NY Office, please enter job reference code: NHBR/WSTCH. You may also mail your resume to Human Resources, 1 Rockwood Road, Sleepy Hollow, NY 10591. Please include the job reference code in the text of your cover letter. We are proud to be an equal opportunity employer M/F/D/V.
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8 We all need to be a voice for any marginalized group.

9 We all have much more in common than we realize.

10 There are some things we can never understand because we are not someone else.

11 Just because something is not measured does not mean it is not important.

12 Discrimination can come from anyone.

13 The best ideas might come from the least expected place.

Creating Intersections: The intersection, according to Johansson, is "unknown territory where past knowledge and experiences are poor guides.... [it] is a place where we must leave many of our preconceived notions behind." He concludes: "The advantage goes to those with an open mind and the willingness to reach beyond their field of expertise. It goes to people who can break down barriers and stay motivated through failures."

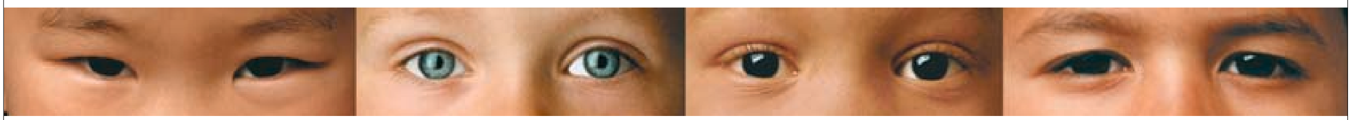
Breaking down barriers "requires authentic, honest, and candid dialogue about the issues that get in the way of our ability to be great," says Karen DeCuir-DiNicola, manager of diversity, General Motors. It starts with meeting people who are different, who have different skills and perspectives, continues with conversation, and grows through relationship and teamwork. Terry Howard III, diversity director for Texas Instruments, adds: "It's important to understand that the benefit isn't 'just' the specific solutions developed. These efforts can spark full engagement among the diverse employees who participate. The individuals are valued precisely because they are being *themselves*... identifying with their constituent groups; and also, in the process, they are building personal relationships across other groups."

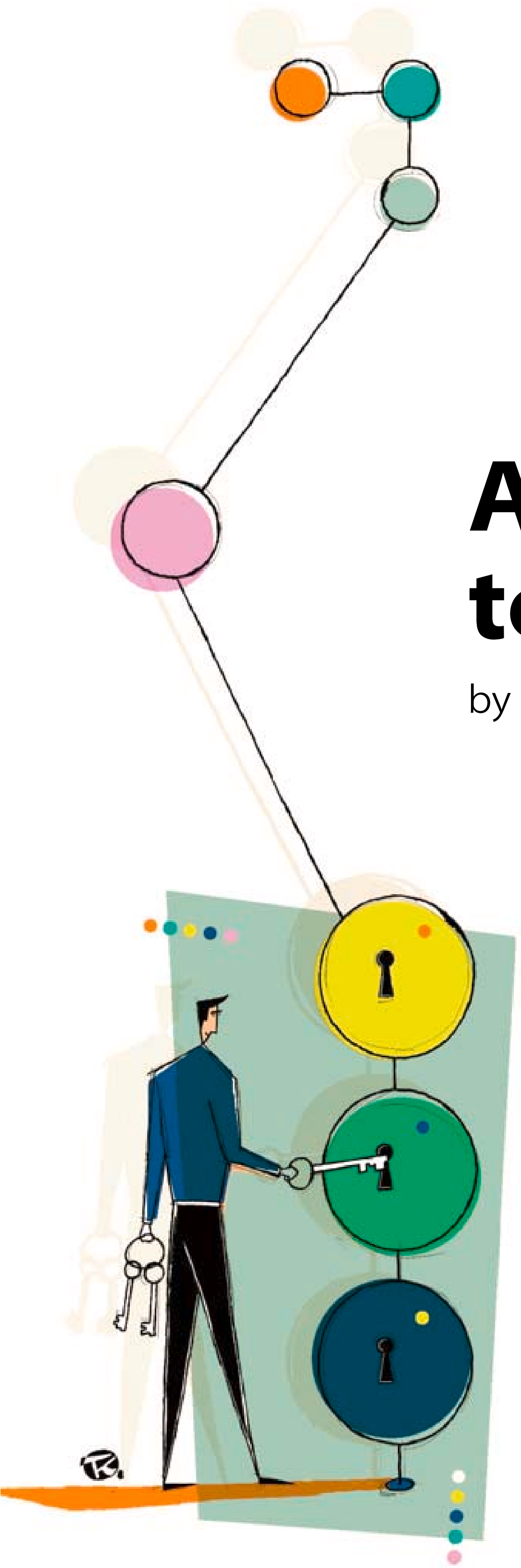
The late Santiago Rodriguez, former diversity executive for Microsoft, posed the question: "How does difference or absence of difference affect our design of products, our marketing of services, and our customer satisfaction?" Take this question, get a diverse group of people together, and begin the conversation!

Michael Wheeler *is a strategic management consultant and author specializing in workforce diversity. He is also a program director at The Conference Board, where he was instrumental in establishing their diversity councils, conference, and research. Wheeler has worked extensively with Fortune 500 companies and has published numerous research reports and articles for more than a decade. He can be reached at: michael.wheeler@oestrategiesinc.com.*

The Diversity Performance Factor

Business Objectives X +	The Diversity Performance Factor Y +	Diversity Initiatives as Catalysts Δ	Results =
• Expand market share • Foster innovation • Improve productivity • Reduce costs • Employee engagement • More diverse workforce • Expand global presence	• Primary dimensions of diversity (e.g., race, gender, etc.) • Systemic barriers (e.g., racism, sexism, xenophobia, and homophobia) • Exclusion • Breakdown in communication • Conflict • Complaints • Low morale • Fresh ideas • Different point of view • Different way of doing things • Different world view • Unique skills • Special talents • Inclusion	• Utilization of affinity and networking groups • Cross-cultural competency development • Accountability for diversity • Inclusive work environments • Diversity-related metrics • Integration of diversity into business processes • CEO commitment • Vendor-supplier relationships • Recruitment and retention initiatives	• Greater market share • Innovation • Improved productivity • Greater problem-solving • Cost savings • More efficient processes • Fewer lawsuits • Better teamwork • Less turnover • Fewer complaints





You know your company depends on informal networks, but what can you do about them? Decide which of three different types of networks will deliver the results you want, and then set up frameworks to help them flourish.

A Practical Guide to Social Networks

by Rob Cross, Jeanne Liedtka, and Leigh Weiss

When is a company greater than the sum of its parts? When its once-siloed business units find a way to harvest innovations in the white space between them. That's exactly what happened at heavy-equipment manufacturer United Technologies Corporation.

Each of UTC's five dominant business units–Pratt & Whitney, Sikorsky Aircraft, and Hamilton Sundstrand in aerospace; and Otis Elevator and Carrier on the commercial side–had a long history of pioneering products in its own industry. But because UTC's culture placed a high value on decentralized decision making, each unit operated almost entirely independently of the others.

That approach troubled UTC senior vice president John Cassidy and Carl Nett, director of the company's corporate research center, UTRC. They believed that enormous potential for organic growth existed in the junctures between the business units. But given the history, work practices, control systems, and cultural norms at UTC, integrating various kinds of expertise across those units was, in Cassidy's terms, an "unnatural act."

To change that, three years ago the two executives invited top technical talent from each division to several two-day brainstorming sessions with the intention of bringing together far-flung expertise to create new products and service new markets. The intersection of cooling, heating, and power emerged early on as a potential winner. In one session, engineers from Carrier, Pratt & Whitney, and UTRC realized that using cooling and heating equipment could transform an innovative power gener-

MARK TELLOK

ation concept into a revolutionary product. Called PureCycle, the product contained virtually no major new components, but offered a breakthrough value proposition: Customers could convert waste heat to electricity at rates substantially below those of utilities.

PureCycle coupled a compressor that was converted to run as a turbine with two types of standard heat exchangers used on big commercial air-conditioning units. Instead of taking in electricity and producing chilled air, PureCycle took in waste heat and produced electricity. The product held great promise, since U.S. industrial plants emit roughly as much waste heat as a 50-gigawatt power plant generates (enough to run most major U.S. cities).

Today, engineers involved with PureCycle can't believe that no one thought of the idea earlier. Thierry Jomard, a former Carrier engineer who transferred to UTRC to lead the PureCycle development effort, explains: "Carrier people are trained to think in terms of using heat exchange to produce cold air – that's the output that counts; the compressor is just there to move the fluid. Pratt & Whitney engineers, on the other hand, are power people. The outcome they care about is power, and they use turbines to get it." It wasn't until they started talking together that anyone recognized the opportunity before them.

Of course, saying that networks are important is stating the obvious. In all but the most rote manufacturing and service environments, work has become a collaborative endeavor accomplished less through standardized processes and formal structures than through informal networks of relationships. But harnessing the power of these seemingly invisible groups to achieve organizational goals is a murky and elusive undertaking. For every success story like PureCycle, there are many more failures. The problem is, efforts to promote collaboration are often haphazard and built on the implicit philosophy that more connectivity is better.

Many executives are quick to introduce new technologies to promote collaboration, for instance. In fact, according to a 2002 report by International Data Corporation, collaborative applications account for nearly one-fifth of corporate spending on software; and Collaborative Strategies, a San Francisco-based management services company, has estimated that the market for real-time collaboration tools will reach almost $6 billion this year. Yet most executives admit that they don't know if these investments are truly improving either collaboration or the quality of work. And if you ask them if they want another collaborative tool in their own work, the majority cringe at the idea of managing more contacts.

Rather than think about collaboration from a more-is-better perspective, executives need to take a clear-eyed, strategic view. They need to determine exactly what they want to accomplish through informal networks and, concurrently, what pattern and level of connectivity would best help them achieve their goals. Initiatives that create network connections indiscriminately – whether through technical applications or organizational efforts such as communities of practice – can take a toll on employees. Unproductive relational demands sap people's time and energy and can bog down entire organizations. Decision makers can become so consumed by managing contacts that their coworkers often cannot get to them in time to take action on opportunities. Many of us struggle to keep up with e-mail, phone calls, and meetings – often with substantial implications for both performance and quality of work life. That's why it's crucial for executives to learn how to promote connectivity only where it benefits an organization or individual – as well as learn how to decrease connectivity that isn't needed.

Three Types of Social Networks

Though all informal networks help organizations do two things – recognize opportunities or challenges and coordinate appropriate responses – effective networks look very different depending on strategic objectives and the nature of work within a given organization. Through our assessments of more than 60 networks across a wide range of industries, we have seen three network archetypes consistently deliver unique value propositions.

Customized Response. These networks exist in settings where both problems and solutions are ambiguous. New product–development companies, high-end investment banks, early-stage drug-development teams, and strategy consulting firms require networks that can rapidly define a problem or an opportunity and coordinate relevant expertise in response. Here, value is delivered by quickly framing and solving a problem in an innovative way.

Modular Response. These networks thrive in settings where components of a problem and solution are known but the combination or sequence of those components is not yet known.

Surgical teams, law firms, business-to-business sales, and midstage drug development teams require networks to identify problem components and address them with modularized expertise. Here, value derives from delivering a unique response depending on the constellation of expertise required by the problem (such as a surgical procedure or a lawsuit).

Routine Response. These networks are commonly found in environments where work is standardized. Problems and their solutions are well defined and predictable. Call centers, insurance claims–processing departments, and late-stage drug development teams require the reliable coordination of relevant expertise to solve common issues. Value is delivered through efficient and consistent response to a set of established problems.

These three value propositions demand different network configurations and require executives to craft contexts in which appropriate patterns of collaboration are more likely to occur. Executives can't – and shouldn't – force collaboration onto all employees. But they can do a tremendous amount to create an environment that allows networks and collaboration to emerge in a productive fashion. This is a holistic challenge. Simply introducing a collaborative technology, tweaking incentives, or advocating cultural programs to promote collaboration is usually insufficient. Rather, leaders must also align work management practices, technology, and human resource practices. And beyond organizational architecture, specific cultural values and leadership behavior can have a striking effect on patterns of collaboration. (For an overview of network characteristics and underlying strategies, see the exhibit "Social Networks at a Glance.")

Customized Response at Novartis

Some networks provide value by connecting a wide range of experts who sense (usually novel) market or customer needs, frame the problem, and then rapidly coordinate expertise to meet those needs. Professional services firms, for example, enjoy productive client relationships for years because of their ability to use customized response networks effectively.

For a closer look at how this type of network functions, consider Novartis, the Swiss pharmaceutical company. In May 2001, Novartis won U.S. Food and Drug Administration approval for Gleevec, a breakthrough medication that arrests a life-threatening form of cancer called chronic myeloid leukemia, or CML. Gleevec enjoyed the fastest approval ever granted by the FDA for a cancer drug and is considered revolutionary because of the way it treats CML. With his colleagues, Alex Matter, Novartis's former head of oncology research, redefined cancer treatment by looking at an old problem in a new way. Traditional cancer therapies can leave patients extremely weak because they attack both cancerous and healthy cells. Gleevec, by contrast, specifically targets cancer-producing molecules and fixes the genetic malfunction without harming normal cells.

Development of the tiny orange capsule would not have been possible without help from diverse external connections. Before Novartis even existed (the company resulted from the merger of Sandoz and Ciba-Geigy in 1996), Matter worked at Ciba-Geigy in Switzerland and had been considering the ways that some enzymes, called kinases, might affect cancer growth. At the time, most scientists thought it would be impossible to develop a compound that could cross a cell membrane to reach the kinases. But Matter was persistent, and his external contacts helped show him the way. Brian Druker, a medical oncologist who began working on this problem at the Dana Farber Cancer Institute in Boston, for instance, was instrumental in the early research because he told Matter that the cancer most likely to respond to his approach was CML. Of more than 100 kinds of cancer, it was the only one whose genetic cause had been scientifically established. Later, once the drug had been developed, Matter and his team relied on other external connections to identify potential hospitals for patient trials.

Work has become a collaborative endeavor. But harnessing the power of seemingly invisible groups for organizational goals is a murky and elusive undertaking.

Internal connections at Novartis were also crucial at each stage of the process. In drug development, these dense networks allowed for frequent brainstorming sessions and included members from distinct scientific disciplines, such as chemistry and biology. Manufacturing success was built on healthy internal connections between members of the global development team in Switzerland and the manufacturing team in Ireland. For example, to meet demand, the company devised a creative way to produce Gleevec in large quantities in Ireland immediately, instead of manufacturing the drug in smaller quantities first in Switzerland, as was customary. That change shaved a year off the normal production schedule. But it wouldn't have been possible without

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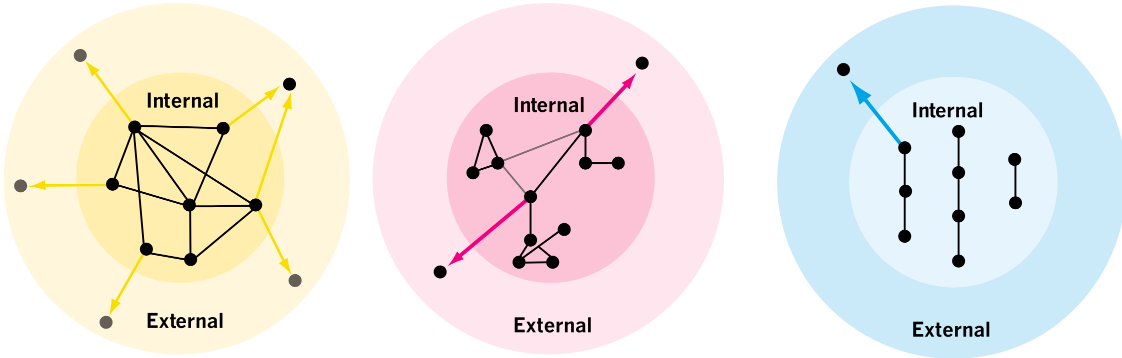
Social Networks at a Glance

Customized Response	Modular Response	Routine Response



	Customized Response	Modular Response	Routine Response
Best for:	Solving ambiguous problems that need innovative solutions	Solving complex problems where components of the problems are known but the sequence of the solutions is not	Solving familiar problems with known responses
Value is delivered:	In the problem's rapid framing and innovative resolution	In establishing and delivering the correct constellation or sequence of expertise	Through efficient, consistent responses to a set of established problems
Network connections:	Are dense and redundant, both internally and externally	Are focused on roles through which different parties can rotate; external connections are targeted to inform aspects of response	Are focused on process flow; external connections are limited
Trust:	Is placed in others' expertise	Is placed in role occupant	Is placed in process execution
Pricing:	Premium pricing for reinvestment in social capital	Moderate pricing for reinvestment in technology	Commodity pricing
Structure:	Permeable boundaries (inside and outside); decentralized decision rights and information access	Semipermeable boundaries (specific cross-functional junctures and liaisons); role-based decision rights and information access	Defined boundaries; embedded decision rights and information
Work management:	Planning focuses on general markets and expertise; controls focus on output, not coordination	Planning focuses on constellations of expertise; controls focus on integration at point of delivery	Planning focuses on offerings; controls focus on efficiency and reliable delivery
HR practices:	Develop and reward collaborative behavior	Hire, develop, and reward for functional depth; focus training on integration points	Hire, develop, and reward for specific task execution
Technology:	Expertise locators and portals	Role-based content systems and collaborative environments	Work management systems and artificial intelligence
Culture and leadership:	Collaborative within and across organizational lines, norms of generalized reciprocity	Shifting leadership, depending on domain; decision rights embedded in roles	Centralized decision making focused on standardization and task accountability
Example:	High-end investment banks, consulting firms, corporate R&D departments, early-stage drug development teams	Law firms, commercial banks, surgical teams, midstage drug development teams	Insurance claims processing – departments, call centers, late-stage drug development teams

trusted networks across geographic boundaries.

Of course, these network characteristics – devising a novel approach to a complex problem and assembling the right expertise to solve it – did not arise on their own. Management made strategic decisions that encouraged such a network to develop. First, Novartis's organizational structure was deliberately designed to have permeable boundaries. The global oncology business unit, for instance, comprises marketing, sales, and research functions in different geographies. As Matter explains, "We bring together different disciplines, functions, and geographies to try to break up silos."

Second, while many organizations' planning processes unwittingly compel functional- or business-unit heads to focus on their own objectives, Novartis takes a different approach. The company pushes executives to consider ways that unique packaging of expertise – both within and outside the organization – could create new market opportunities to which they could respond. For example, the company routinely forms strategic alliances with industry partners and academic institutions to develop new products, acquire platform technologies, and access untapped markets. For instance, scientists in the company's disease area strategy group, which focuses on alliances and acquisitions for disease areas that are expected to drive growth, work closely together across boundaries that would separate them in most other companies. Using their extensive networks, they share insights into the fundamental mechanisms of disease as well as any potential overlaps in the causes of illnesses that appear clinically unrelated. This approach lets them quickly refocus on new opportunities as they arise.

Third, Novartis maintains a delicate balance between stringent productivity criteria and protection of individual employees' abilities to experiment and be innovative. For instance, when internal critics argued that the population of CML patients was too small to warrant such a high-risk investment, Novartis's CEO, Daniel Vasella, vocally and financially supported the team's efforts. He also rearranged organizational priorities to help Matter's team. When the company needed to reduce the time it took to manufacture Gleevec to meet demand, for example, Vasella supported the decision to move production immediately to Ireland to meet that goal. More broadly, Novartis's managers are encouraged to help junior colleagues connect to wider networks, both within and outside the company, and to protect their younger colleagues over long stretches of lower productivity.

The approach seems to be working. Novartis's pharmaceutical products pipeline is one of the broadest in the industry, currently comprising 78 projects in clinical development or registration. The company also received seven major approvals for drugs during 2003 and has launched 11 new medicines in the United States since 2000. Productivity like that is the result of a great deal of collaboration within and across organizational boundaries.

Finally, Novartis invests in technology to help manage the vast sea of knowledge, creating a privileged knowledge environment for its scientists. Comprehensive databases help researchers assimilate volumes of external data, and various collaborative tools facilitate knowledge sharing among high-end experts. In keeping with its commitment to create an atmosphere for effective collaboration that will produce innovative drugs, Novartis recently announced plans to convert its headquarters in Basel, Switzerland, from an industrial complex to a campus with plenty of meeting areas to encourage the spontaneous exchange of ideas.

In January 2004, Novartis was voted one of the ten best European companies to work for by *Fortune*. It was the only health care company to make the list, and one reason employees cited was the collaborative nature of the organization and the many networks that run across hierarchical, geographic, and other organizational boundaries. In other words, Novartis excels at creating rich, customized response networks that produce innovative ideas and solutions.

Modular Response at the FAA

Rather than framing a problem in a new way (as a customized response network does), modular response networks address problems and opportunities by identifying the individual components of a problem and coordinating expertise to address each one. Financial transactions, for example, though unique to a given customer, typically require consistent kinds of expertise packaged to address a specific capital requirement. Similarly, systems-development consulting firms don't re-create the same system for different clients, but they do reuse components and apply consistent knowledge from one project to the next. In cases like these, when dimensions of the problem to be solved are more readily understood, it's not as important to have dense internal connections or links to external leading-edge thinking. Problems can be better solved by coordinating defined roles that any qualified party can step into.

Think about the coordination challenge confronting the U.S. Federal Aviation Administration. Air traffic control is divided into nine regions that hand off planes from one facility to another as they make their way to their final destinations. To get an idea of the complexity involved, consider that the southern region alone encompasses eight states and the Caribbean, and has approximately 1,600 facilities – ranging from major airports to unmanned devices operating on isolated mountaintops.

When things go wrong, a great deal of information is needed quickly, as is a coordinating body that can decide which problems to address and in what sequence. Because the FAA has vast internal systems expertise, it needs only a few external network ties that can deliver specific information, such as weather reports. Internally, however, employee expertise is highly specialized and dispersed across many locations. And responding to disruptions in service often involves approvals and decision making from a wide range of supporting organizations, such as headquarters, hazardous materials teams, and the Occupational Safety and Health Administration. Without a specific coordination mechanism, information overload could quickly occur, and critical decisions could be delayed while people try to determine who is in charge of what. To deliver value, the FAA's network cannot be free-form like the customized response networks. Neither can it be overly prescribed, however, because each problem demands a different constellation of expertise and decision-making authority.

That's why the FAA adopted a role-based approach. When an event such as a hurricane occurs, the necessary roles are identified and mobilized by a team leader. Management roles include the information point of contact, who captures, sorts, analyzes, and communicates data to ensure everyone receives information from one consistent source; the technical plans and programs coordinator, who provides response plans and makes staffing and equipment decisions; and the incident commander, who acts as the liaison with other divisions, conducts financial assessments of solutions, and is the overall team leader.

Anyone with the requisite expertise can step into a specific role. Depending on the nature and duration of the event, people can rotate through a given role as well. Because each team member knows what to expect from a particular position through training and well-defined processes, trust is easily established, enabling swift coordination among relative strangers. Further, because the modules of response are generally the same (only their packaging is unique to a given event), the FAA can adapt innovative solutions from one region to another to improve performance throughout the whole organization.

When the first plane struck the World Trade Center in the September 11 terrorist attacks, for example, the Southern Region rapid response system kicked into gear. Within approximately 15 minutes, emergency operations centers at seven locations were up and running. Although no FAA facilities were physically damaged, steps had to be taken to secure them and to protect employees.

The situation was very different from a weather disaster such as a hurricane, for which the agency typically would have days to prepare. All information would flow "up" from the areas affected by the storm, be verified and validated by the information point of contact, and then disseminated. On September 11, however, the agency's approach was reversed: Instead of gathering data from the field, the emergency operations centers had to gather information from the national program offices, regional security, and management – and then rapidly communicate that information to employees. Relying on established roles and customized software applications helped keep everyone informed, acting on consistent information, and coordinating work and activities rapidly in the face of an entirely new crisis.

Of course, a modular response network requires more than just technology and a set of well-conceived roles. Employees must not dogmatically adhere to formal hierarchy but, instead, be ready to follow those individuals with the necessary expertise who step into a specific role at a given time. Formal leaders must be willing to give up decision-making authority when others, who are better informed, are performing a particular role. And followers must not be afraid to take risks. Because of this, the FAA has changed the way it educates and supports its employees, driving decision making to the lowest level possible. The investment has been worth it. Without this role-based network, the FAA would need to keep teams out in the field to respond to incidents, at a cost of $15,000 to $25,000 per day.

The modular response also influences the FAA's training philosophy: valuing technical depth over generalist skills. Most technicians do not need to work together to do their jobs. Therefore, training on a broad set of response systems is less effective than developing depth in specific areas and then making sure everyone understands each role and how to use the technology to stay connected during a crisis.

To be sure, this coordination challenge is not unique to the FAA. Large corporations like IBM and BP are trying to become more nimble through modular response networks in areas such as software development and drilling. By reallocating information access and decision-making authority from hierarchies to roles, these organizations can be more responsive to the opportunities and challenges they face. Coordinating work in a modular way lessens the investment a company must make to ensure that the right people talk to the right people; at the same time, it allows for some customization in the delivery of products and services.

Routine Response at Sallie Mae

The third type of network creates value by coordinating expertise to provide reliable responses to recurring problems. Call centers and claims-processing departments at insurance companies become more efficient and better serve their customers when work is taken out of the network and embedded instead in systems, processes, and procedures. For example, to make responding to customer queries more efficient, an organization can prescribe patterns of interaction, minimize unnecessary relationships within and outside an organization, and employ a formal structure that focuses collaboration on inputs and outputs.

Executives can't simply hope that collaboration will spontaneously occur in the right places at the right times in their organizations.

Call centers are prominent in four main industries: financial services, telecom, high-tech, and airline. Most of us have dealt with a call center at some point, and many of us have been frustrated. We get put on hold or transferred to one person after another – none of whom can answer our questions. But companies with call centers have a very strong incentive to improve customers' experiences, since unhappy callers are likely to vote with their wallets the next time they buy a computer, choose a bank, or the like.

Deborah Bragg is the vice president of Texas servicing and call center operations at Sallie Mae, the largest private provider of educational loans in the United States. The company owns or manages approximately $100 billion in student loans for more than 7 million borrowers, and Bragg oversees customer service. "Our goal is to resolve a customer's question on the first contact while minimizing service expense to the company," she explains. That's no small task: The center receives nearly 20,000 calls per day.

A specific set of network characteristics helps Bragg and her team make sense of a jumble of customers' questions. Internal connections are focused on the process flow of different categories of requests, such as customer questions about a new product. What's more, these connections are intentionally designed and circumscribed – they're not ad hoc, as in a customized network – to make the processes more effective and efficient. And unlike a modular network, which centers on distinct roles, the routine response network at Sallie Mae follows defined process flows. For example, interactions typically occur among supervisors reviewing calls and then between call center agents and their supervisors, who give feedback and coaching. A horizontal communication network that directly connected call center agents would be inefficient and would reduce the consistency of customers' experiences.

The call center management and staff have very limited external connections. Those that exist serve highly specific purposes, such as bringing in an expert to redesign a Web site. For the most part, the nature of the inquiries at the call center are such that developing, nurturing, and maintaining external relationships are unnecessary costs.

The way a routine response network is structured allows collaboration to be focused on specific inputs and outputs. For example, Sallie Mae analyzes repeat call trends at least once per month to identify reasons for higher volume. When another part of the company is the cause, the center provides internal feedback to that department. So if customers don't understand a new loan product, the call center manager quickly contacts the group responsible for the new product to let the team know what consumers are saying. "Focused collaboration allows us to deliver clearer information to our customers and, in turn, reduces repeat and additional calls, improves our customer service, and contains cost," Bragg says.

Process flow also defines the way that agents locate experts. The center has an interdepartmental referral process to help agents find the right person for the call. For example, even though the call center doesn't process applications for new loans, it keeps tabs on new loan products. That way, if a parent whose loan Sallie Mae services calls the center because she needs to borrow money for another child, the representative can direct the call to a person who handles new loan approvals. For agents, the need to locate experts is filled by the call escalation process, in which a call is passed up a hierarchy of specialists with ever more decision-making authority.

Of course, the knowledge that agents need is constantly changing as new products are introduced and customer queries change. So the center must be able to do what Bragg calls "nimble servicing": reacting in real time to a dynamic environment. In part, this means identifying new trends and embedding learning in work processes so that the network doesn't take over or become more ad hoc.

One way Sallie Mae uncovers new trends is through a process called "hot topics." When agents notice a trend, they write a summary of it with examples and send an e-mail to management so that the issue can be reviewed. Once a resolution is determined, a Knowledge Tool is created – a user-friendly online resource that agents can access for real-time information. The online system is a repository for the expertise of the entire call center. So by typing in a keyword from a caller's question, an inexperienced agent can retrieve all the information he or she will need to answer it.

Bragg and her colleague Debra Walsh, Sallie Mae's director of training and quality assurance, have made strategic decisions about work management processes, human resource practices, and technology to support the efficient coordination of expertise and reduce the need for expensive, unproductive interactions. The operation's structure is designed to incorporate proficiency in processes, tools, and technologies, as well as to keep internal and external boundaries well defined.

Sallie Mae uses additional work management processes to emphasize the reliable delivery of quality service. Calibration exercises, for instance, are performed weekly. Supervisors, trainers, and quality assurance staff review and score agents' calls. They discuss variances, identify gray areas, and develop best practices, which are then entered into the online knowledge system. Management also evaluates each agent's call escalation process to see which agents might need more training and whether the specialists are able to respond. All these actions help to keep the informal network functioning as efficiently as possible.

Human resource protocols emphasize hiring, training, and rewarding call center agents individually for superior call center service. As Bragg explains, "One of the age-old problems in a call center is the hours of operation and who gets to work which shift. A couple of years ago, we moved to performance-based scheduling. An agent's performance-based score is determined by the quality of his or her work, attendance, and productivity. Those with higher performance-based scores have the option to work the more desirable shifts." Compensation and career advancement are also tied to the score. This approach works because, unlike in a customized environment, more of an individual's performance can be assessed independently of a group of collaborators.

During the training period at Sallie Mae, agents spend their first six weeks in a classroom learning basic tools and technologies, and the quality-assurance review process. Then the agents go on to develop different skill sets related to the type of calls they will handle. They might, for instance, focus on a private-loan education program, which is customized by school, or on different student-loan repayment options. To help agents learn new skills at their own pace, computer-based training is also available. Training in modular and customized environments, by contrast, focuses more on collaborative skill development and on creating connections across boundaries.

Sallie Mae's management relies on several technologies to embed information and knowledge into work processes. The online Knowledge Tool system is one example. Another is a quality-monitoring system that randomly captures calls (voice and screen), which supervisors can then score and review with agents. A third example is the center's use of self-service Web sites. In 2002, the hot topics forum revealed that the service on the Web-payment site was not sufficiently user-friendly. Call center managers worked with a cross-functional group responsible for the site to deploy a more robust product by the end of the year. Within three months, call volume for issues related to bill payment fell by more than 75%–from more than 20,000 calls to fewer than 5,000 calls per month. This reduction in volume translated into cost savings of more than $56,000 in that short time.

Embedding information in processes when work can be standardized has significant advantages. In the first half of 2003, 88% of Sallie Mae customers were satisfied with their most recent call to the center, according to an independent research firm. The same firm benchmarks the financial-services industry's average score at just 74%.

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In many ways, the natural unit of work has migrated from the responsibility of the individual to networks of employees. But although collaboration can have wonderful outcomes–think of PureCycle or the cancer-fighting drug Gleevec – it can also have darker consequences. Countless meetings drain employees' time and energy, and unclear leadership roles can delay decision making. Executives can't simply assume that more connectivity is always better, nor can they just hope that collaboration will spontaneously occur in the right places at the right times in their organizations. They need to develop a strategic, sophisticated view of collaboration, and they must take steps to ensure their company establishes the types of social networks that best fit their goals. The frameworks presented here give executives the tools they need to determine which network will deliver the best results for their organizations and which strategic investments will nurture the right degree of connectivity.

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"I've always been an advocate of the 'team player' concept, but in O'Brien's case, I'm going to make an exception."

DAVE CARPENTER

Inventory affects costs in more ways than you may realize. Understanding and managing inventory-driven costs can have a significant impact on margins.

NICK CRONIN

Inventory-Driven Costs

by Gianpaolo Callioni, Xavier de Montgros, Regine Slagmulder, Luk N. Van Wassenhove, and Linda Wright

The 1990s were hard for the PC business. Although demand grew fivefold between 1990 and 1997, the products had become household staples, and it was difficult for companies to differentiate their offerings.

Hewlett-Packard came out better than many. The computer hardware giant slashed prices on all of its PCs: 10% in 1991, another 26% in 1992, and yet another 22% in 1993. At the same time, it revamped its design, planning, and production processes to shorten cycle times, respond quickly to changes in demand, and move inventory to the right location as it was needed. By late 1999, HP had displaced IBM as the world's third-largest PC manufacturer in terms of revenue, behind Dell and Compaq.

But for all its success in maintaining market share, HP was struggling to turn a dollar. By 1997, margins on its PCs were as thin as a silicon wafer, and some product lines had not turned a profit since 1993. Price cuts made formerly insignificant costs critical – computer manufacturers simply could not stock up on components or any other inventory. Any excess at the end of a product's short life had to be written off, further eroding margins. Adding to the pressure, constant technology advances made new products obsolete in as few as six months. A common rule of thumb was that the value of a fully assembled PC decreased at the rate of 1% a week. Although HP's supply chains were flexible and responsive enough to deliver the PCs when and where customers wanted them, they were not economically sustainable.

Compounding the problem, company executives realized, was the fact that HP's management-accounting metrics had failed to keep pace with the evolution of its supply chains. HP now oversaw a complex, multitiered manufacturing network made up of many disparate entities. But the company's current approach to cost measurement allowed individual players in the chain to see only their piece of the puzzle, making it impossible for them to assess the overall dollar impact of their local decisions. They could not see the effects of operational decisions like setting the size of buffer inventory between two sections of the production process. Nor could they assess the impact of such strategic decisions as choosing to locate a final assembly plant close to a particular supplier. If the company wanted to design sustainable supply chains, it needed to give all its managers a direct line of sight to the overall bottom line.

The Hidden Cost of Inventory

To make the PC business more cost competitive, HP's Strategic Planning and Modeling (SPaM) group, led by Corey Billington, undertook an exhaustive review of the PC business's overall cost structure in 1997. It soon became clear that mismatches between demand and supply leading to excess inventory were *the* main drivers of PC costs; in 1995, for example, costs related to inventory had equaled the PC business's total operating margin. It was just as clear that the division's existing cost metrics did not track all of HP's inventory-driven costs (IDC), pieces of which were often mixed in with other cost items, scattered over different functions and geographic locations, and recorded at different times using different accounting conventions.

The most readily identifiable component of inventory-driven costs is the traditional inventory cost item, usually defined as the "holding cost of inventory," which covers both the capital cost of money tied up in inventory and the physical costs of having inventory (warehouse space costs, storage taxes, insurance, rework, breakage, spoilage). At HP, however, the holding cost accounted for less than 10% of total inventory-driven costs. SPaM's investigation revealed four other inventory-driven cost items at HP's PC business. And each of them needed to be managed in a distinct way.

Component Devaluation Costs. According to SPaM's calculations, these accounted for the lion's share of HP's inventory costs. Key components such as microprocessor chips and memory typically drop in price quickly and steeply. The price of a CPU, for instance, might fall as much as 40% during its nine-month life cycle, and the penalties for holding excess parts when a price drop occurred could be enormous. Back in 1997, however, few electronic hardware makers had realized just how perishable their goods had become, and HP, in common with many others, maintained inventory in several places – in factories and distribution centers, in merge centers, in transit. Every time the component prices fell, HP was hit with another devaluation cost at each of these points in the value chain.

HP had no control over component prices, but it could control how much inventory it was holding. That meant reducing the number of nodes in the supply chain, consolidating manufacturing facilities, taking possession of components on a just-in-time basis, paying the going price at that time, and working with suppliers to minimize inventory when a price drop was anticipated.

Price Protection Costs. If HP dropped the market price of a product after units had already been shipped to a sales channel, it had to reimburse its channel partners for the difference for any units that had not yet sold, so the channel partner didn't have to sell at a loss. Given how quickly value decayed, this mismatched inventory exposed HP to big price protection risks. A channel partner might buy a product from HP when the prevailing market price was $1,000. But if the item sold five weeks later at a new price of $950, HP had to reimburse the $50 difference. To limit this cost, HP had to be certain that channel partners' inventory never exceeded the minimum number of days required to ensure the desired availability, so that no excess inventory had to be protected. This meant that Hewlett-Packard had to keep its manufacturing turnaround times short and replenishment cycles frequent. HP also offered its channel partners incentives to carry the lower levels of inventory. Analysis showed that the cost of these incentives was almost always lower than the cost of reimbursing channel partners after price breaks.

Product Return Costs. In a sense, product return costs are simply 100% price protection costs; distributors can simply return unsold goods to the manufacturer for a full refund. In some cases, product returns constituted more than 10% of the product's revenue, not because of product failures but because resellers were returning excess inventory. Apart from incurring the operational costs (shipping, handling, product retesting, and the like), returns lengthened the time a product spent in the supply chain before reaching an end user, increasing HP's exposure to additional devaluation risks and inventory finance costs. To manage this type of inventory-driven cost, HP had to work closely with channel partners to optimize the whole supply chain. By agreeing with its channel partners on specific inventory levels and delivery expectations, HP reduced inefficient inventory in the channel and increased its overall quality of service both to partners and end customers.

Obsolescence Costs. End-of-life write-offs were initially the most obvious portion of this cost. PC life cycles being so short, even a small miscalculation in

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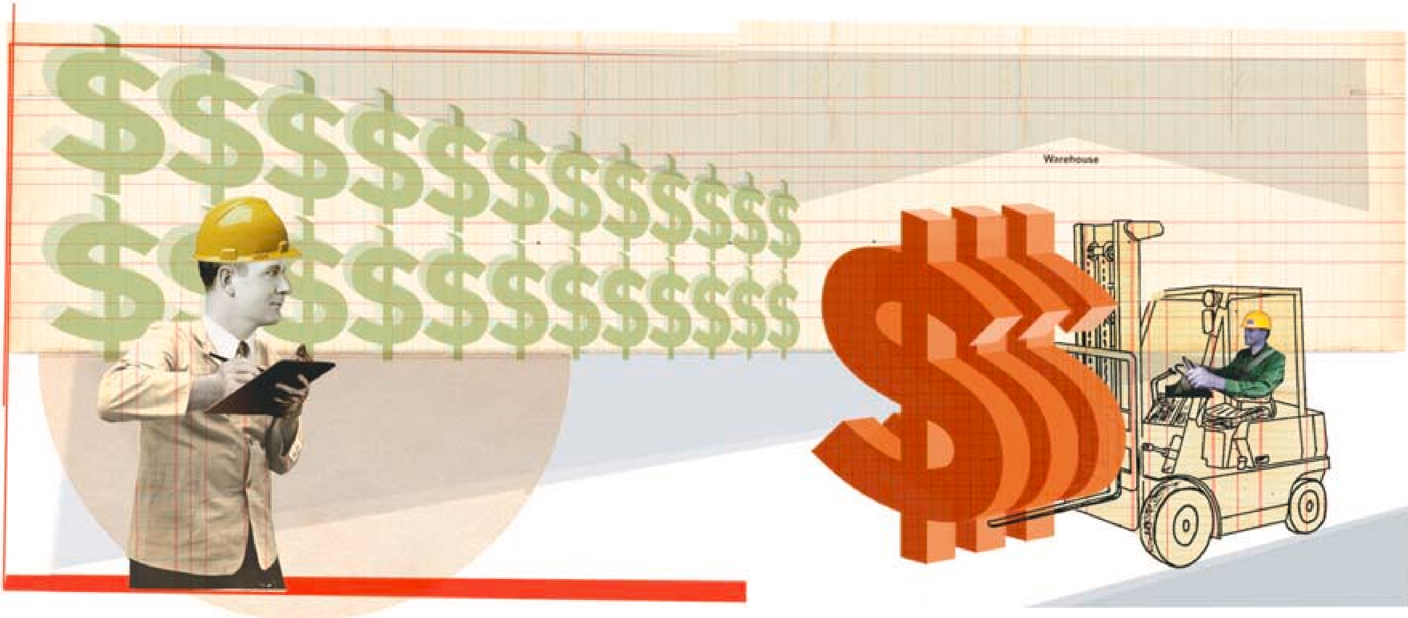


anticipated demand could leave the company holding stacks of worthless goods that had to be written off. The other related but sometimes less obvious components of obsolescence costs were discounts on about-to-be-discontinued products and the associated marketing effort required to accelerate their sale. These costs are typically not included in a company's cost of goods sold and, although HP executives took these discounts and marketing costs into account when making decisions about discontinuing product lines, they seldom considered them when determining the real cost of inventory. To avoid obsolescence costs, HP had to be very efficient in managing product introductions, so that new models were launched just as the last remaining units of the old models sold out.

On the whole, calculating these components of inventory costs is fairly straightforward. The simplest to determine is devaluation, which can be figured by multiplying the inventory level of the product or component in question by the proper devaluation rate. Suppose that a hypothetical company sells a consumer electronic item that devalues at a yearly rate of 60%. Average annual inventory related to the product is worth $200 million, and annual revenues from selling the product are $1 billion. Then, the yearly inventory-related cost due to product devaluation is the average annual inventory multiplied by the devaluation rate, or $120 million. Dividing that figure by revenues gives us the cost as a margin, in this case 12%. Clearly, at any given devaluation rate, inventory costs will increase directly as inventory increases. The faster prices fall, the more the inventory-driven costs rise as inventory increases. Since in most cases the devaluation rate is outside managerial control, the only way to reduce the impact of devaluation on profits is to do a better job of matching demand and supply, thereby shrinking inventories.

Price protection and return costs are calculated in a similar way, but the actual sums are somewhat more complicated because they depend on the contractual agreements set up between manufacturers and distributors. In its simplest case, if a manufacturer has agreed to reimburse its distributors 100% whenever it lowers its list price, the formula for determining price protection costs is the price drop times the number of units of the product in distributors' inventory. Similarly, return costs would be the number of items returned of a particular product times the wholesale price paid by the retailer in the first place. But those sums need to be adjusted by the contract terms, which might, for example, not allow all inventory to be returned if the retailer deliberately overstocks. (The more generous the price-protection and return terms, the less the distributor will lose by doing so.) What's more, contract enforcement may depend on specific circumstances. For example, even if the contract constrains the return options of the channel partner, HP may still agree to take products back to maintain good relations and secure future sales.

Devaluation, price protection, and return costs are essentially continuous costs; they occur all the time and can be calculated at any point. Obsolescence costs, however, are discrete, arising only when a company decides to retire a particular product and therefore cannot be estimated until that moment. The amount of obsolescence costs is determined by several factors. First, the company needs to write off 100% of the value of finished goods in its inventories (less any recycling or scrap benefits). Then it must write down the value of any components in the pipeline. If components are product specific, they will have to be written off 100%; those that can be used elsewhere will be subject to devaluation costs depending on how quickly they can be transferred to other products. Finally, the company has to add in the related marketing and discounting costs of selling off about-to-be discontinued products in fire sales.

As important as identifying the various hidden components of inventory costs was to HP, even more powerful was understanding how the impact of each IDC component differed for different products. That had profound implications for the way HP managed its product portfolio. This insight is illustrated in the table "Tracing Costs to the Source," which compares three unnamed HP products. Total IDC is relatively high for product A, at 14.25% of product revenues, and fully half of this total comes from price protection costs. Total IDC for product C, by contrast, is only 4.80% of revenues, and the largest share of that is component devaluation.

These figures suggest how the supply chains of the three products need to be managed. Since the inventories of channel partners represent the largest component of inventory costs for product A, what managers need to do is improve supply chain management downstream: They must do a better job of forecasting demand. They need to encourage vendor-managed inventory (VMI) and collaborative planning, forecasting, and replenishment (CPFR) initiatives. By contrast, products B and C probably need better upstream management with suppliers or with product designers to reduce component devaluation risks.

The four cost items that SPaM identified are not the only kinds of potential inventory-driven costs. Companies that maintain high stocks of raw materials, for instance, may well find that the write-down in the value of their inventory, stemming from reductions in raw material prices, can in any one year outweigh the benefits of the lower input prices. Another common source of IDC are price discounts, which typically arise when errors in forecasting demand lead to excess inventory that the company is forced to sell at below-market prices, resulting in lower margins on the products in question.

Excess inventory was *the* main driver of Hewlett-Packard's PC costs; one year, in fact, inventory-driven costs equaled the PC business's total operating margin.

The Turnaround

The Mobile Computing Division (MCD) was the first of Hewlett-Packard's PC units to take inventory-driven costs into account when formulating strategy. In 1998, before redesigning its supply chain, MCD was taping dollars to every machine it shipped. Year after year, its managers tried different initiatives to improve profits, including reducing the cost of materials, controlling operating expenses, and generating revenue growth through new product development. Nothing worked until the notebook division began to look at the impact of its supply chain decisions on IDC.

Intuitively, MCD's managers believed that the unit could not become profitable until it consolidated all worldwide manufacturing at a single location and shipped the finished products directly to customers. This would, however, represent a major strategic change, and the division's executives worried that centralized manufacturing would affect the unit's ability to give customers the service they wanted, resulting in the loss of both market share and revenue. To build a compelling case for making the move, they needed to quantify the risk – and the opportunity – involved in making such a radical change.

Collaborating with SPaM, the MCD team considered many different supply chain scenarios. The exhibit "Finding the Lowest-Cost Option" compares five of these. For reasons of confidentiality, the actual numbers have been disguised, but the exhibit truthfully reveals the relative cost differences. Scenario 1 represents the original configuration, a two-step supply chain with a central manufacturing facility and a certain amount of local product configuration carried out at regional facilities. It turns out that about 40% of the true total supply chain cost in this scenario is linked to inventory. The company had never taken inventory costs such as devaluation and

Tracing Costs to the Source

When the components of inventory costs are broken out, it becomes easy to see how the supply chains of different products need to be adjusted in different ways to lower costs at their source. In this example of three of Hewlett-Packard's products, the highest costs for product A are coming from goods whose prices have dropped after they've been shipped to retailers. But the greatest problem for products B and C are drops in component prices before the products ever get out of the factory.

Inventory-Driven Cost	IDC as a Percentage of Revenues		
	Product A	Product B	Product C
Component Devaluation	2.10	4.20	2.20
Price Protection	7.15	2.30	0.80
Product Return	1.15	0.60	0.60
Obsolescence	2.55	0.65	0.40
Holding Cost of Inventory	1.30	1.10	0.80
Total	14.25%	8.85%	4.80%

obsolescence fully into account before, so the exercise revealed just how expensive its past supply chain decisions had actually been.

Scenarios 2 and 3 essentially retain the basic two-step supply chain configuration of scenario 1 but assume that the company will limit inventory costs by putting more-efficient manufacturing processes in place and by passing on to supply chain partners as much responsibility as possible for inventories. As the exhibit shows, these nonstrategic changes would suffice to reduce total costs (including IDC) by as much as 24%. In scenarios 4 and 5, the unit considered radically restructuring its supply chain, and either approach would involve major strategic changes to implement. Both are essentially one-step supply chains, but there the similarities end. Scenario 4 assumes that HP would have several regional factories doing both manufacturing and localized configurations. In scenario 5, however, everything would be done in a single central factory and airfreighted directly to customers worldwide. What this means is that scenario 4 has higher manufacturing costs than scenario 5 but lower freight costs.

How should the Mobile Computing Division choose between the scenarios? In terms of manufacturing costs only, scenario 5, which MCD called International Direct Ship, is the best option, suggesting that the company should consider making the radical change to a one-step supply chain. Factoring in freight, the one-step model remains the theoretically optimal supply chain, although scenario 4, with regional factories, now appears to be the best option. But the case for switching to a one-step model is considerably undermined because scenario 3, the best-case two-step option, is now only one percentage point more expensive than scenario 4 and actually cheaper than scenario 5. The one percentage point difference is not enough to make up for the organizational and financial changes that switching to a one-step supply chain would involve, despite the tight margins on the PC business.

Finding the Lowest-Cost Option

Breaking out inventory-driven costs gave HP's Mobile Computing Division a far more comprehensive understanding of the various supply chain options it was considering. Scenario 1 represents the existing cost structure of the unit's business in 1998, in which products were manufactured centrally and configured to conform to local needs in regional markets. Scenario 5 is the centralized one-step manufacturing model that HP eventually adopted. Its merits do not become apparent until inventory-driven costs are taken into account.

Costs Relative to Scenario 1

TRADITIONAL COSTS	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
Manufacturing	100%	no change	–15.6%	–11.1%	–21.0%
Distribution	100%	no change	no change	no change	no change
Freight	100%	no change	+7.4%	–28.4%	+56.8%
Total costs w/o IDC	**100%**	**no change**	**–9.2%**	**–10.2%**	**–6.7%**
IDC COSTS					
Inventory finance	100%	–18.5%	–29.6%	–44.4%	–51.9%
Inventory devaluation	100%	–51.6%	–55.7%	–58.0%	–63.5%
Inventory obsolescence	100%	–24.0%	–34.9%	–52.7%	–58.1%
IDC total	**100%**	**–19.2%**	**–29.3%**	**–43.6%**	**–51.2%**
Total costs w/ IDC	**100%**	**–15.5%**	**–24.0%**	**–28.1%**	**–28.3%**

But what a different picture emerges when IDCs such as inventory devaluation and obsolescence costs are fully quantified and included in the analysis. Then, the case for switching to a one-step supply chain looks much stronger. Even if the company were to exploit all the possible opportunities for reducing IDC in the current supply chain structure, as scenario 3 rather unrealistically assumes, both one-step scenarios come out about four percentage points cheaper, which is enough to justify management's case for switching to a one-step supply chain. A full assessment of IDC, therefore, not only revealed the limitations of MCD's current supply chain but also provided strong evidence that the only way the division could turn its business around was by refashioning its entire supply chain strategy.

IDC considerations also drove the choice between the unit's two very different one-step supply chain alternatives. As the exhibit shows, the total cost difference between them, when IDCs were taken into account, was minimal (0.2 percentage points). But managers felt that scenario 4 offered many opportunities for losing control of inventory-driven costs, and it was not clear that MCD would always be able to contain those risks. Managing a multitude of regional factories with separate pools of materials and products is harder than managing just the one. More factories would mean greater chances that capacity would fall idle; several plants would certainly require higher levels of capital investment than a single one. And when MCD introduced new products, several factories would have to ramp up their production processes, not just one. So, although scenarios 4 and 5 seemed to be very similar in terms of base-case total costs, the Mobile Computing Division eventually plumped for scenario 5.

MCD started reaping the benefits almost at once. Inventory-driven costs dropped from 18.7% of total revenue in

1997 to 12.2% in 1998. In 1999, the division saw an even more dramatic improvement, as IDC dropped to a mere 3.8% of revenue. These reductions translated directly into savings for the notebook division's bottom line, which in 1998 broke even and in 1999 turned profitable. The IDC metrics enabled the Mobile Computing Division to clearly identify exactly where changes to its supply chain were needed and to justify changes that, according to more traditional thinking, would not have made sense.

Other PC units, notably the commercial desktop business, started to follow MCD's approach to costing in their supply chain decisions, with similarly impressive results. Inspired by these successes, HP decided to officially implement the new metrics in all of its PC operations. In the first stage of the rollout, the focus was on tracking IDC across all divisions. In some cases, the information had to be assembled manually; in others, it was possible to automate the data gathering. In the next stage, goals for each IDC line item were set for each region and product line, based on projects that were known to be in the works and estimates of future market conditions. A consistent presentation of the data was almost as important as the actual data. HP's regional units, product divisions, and finance groups worked closely together to develop a standard template for supply chain metrics, making sure that the data could be collected in the requested format for each line item in a timely manner. So everyone uses the same line items on their spreadsheets, each with the same definition, the same source of information, and the same method of calculation. As a result, all users can look at a line item and know exactly where the data came from and what they really mean.

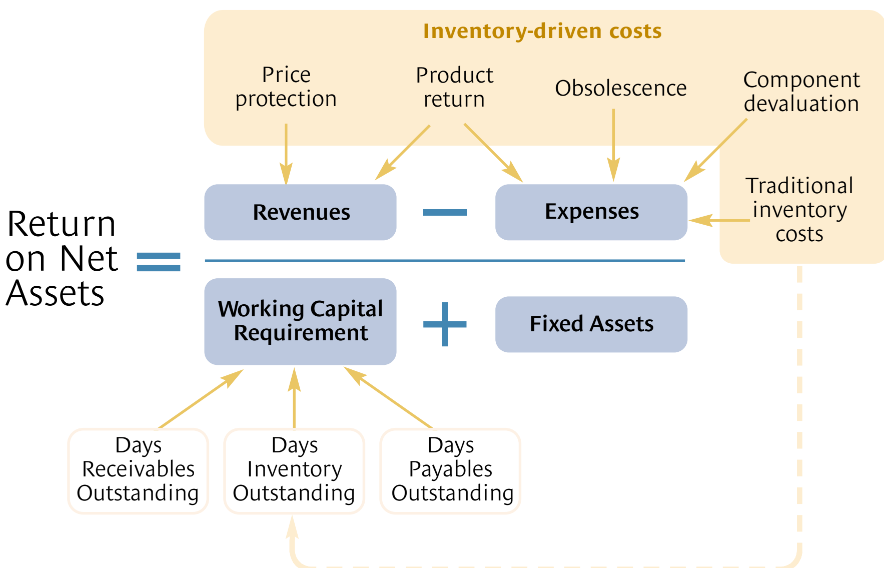
The Payoff

HP can now manage the profitability of its value chain in a much more sophisticated way. Gone are the days of across-the-board measures like "Everyone must cut inventories by 20% by the end of the year," which would usually result in a sometimes counterproductive flurry of cookie-cutter lean production and just-in-time initiatives. Now each product group is free to choose the supply chain configuration that best suits its needs as long as it meets the global IDC target. Product group managers may well have known before, on an intuitive level, what they needed to do, but the IDC metrics have made it easier for them to convince senior managers that their particular situations require particular solutions.

Incorporating the IDC metrics into decision making has also saved managers from moves that make perfect sense for their own unit but add to overall costs. Previously, for example, a manager might have decided against shipping goods by air because the extra transportation costs would have exceeded the identifiable cost of financing and warehousing local inventory. But that decision would have imposed costs elsewhere in the supply chain, which might well have exceeded the extra transportation costs. Without measuring total IDC, there was no way to know that, and even if the manager made the right decision, he would probably have been penalized for it. Now, however, he would be rewarded for incurring extra local cost in the interests of reducing total costs.

Linking Inventory Costs to Financial Performance

Hewlett-Packard is finding that return on net assets (RONA) is a more accurate measure of shareholder value than market share, because in such price-sensitive industries, the key to financial health is not revenue growth but sound asset management. To measure RONA accurately, companies need to track more than just traditional inventory costs. Those costs affect expenses only, but the price protection and product return costs that inventory-driven cost metrics track can also erode revenues. What's more, lowering inventory-driven costs can not only decrease total costs and raise revenues but also lower working capital requirements by reducing the number of days of inventory outstanding.



The IDC metrics are valuable in a whole range of R&D and marketing decisions. Many downstream supply chain costs arise because of choices managers make upstream in the product design phase. The IDC discipline has made HP's product designers much more aware of the consequences of their decisions, which makes them more responsible and accountable. Before, someone who had specified a hard drive that took three months to obtain would probably not have realized that during those months HP was liable for excess inventory, devaluation, and obsolescence costs. Now, such a designer no longer has that excuse. The IDC metrics also help managers decide how much flexibility to build into new products. In the past, HP often underestimated the related supply chain costs of offering lots of product features. Being able to quantify the real inventory-driven cost of adding, say, Lithuanian language customization to a product helps in determining whether or not to offer customers that option.

But perhaps the greatest benefit of the IDC metrics is that they link operational decisions to corporate goals for creating shareholder value. In the new profit-focused climate, HP has been abandoning its traditional financial-performance metric of return on sales in favor of return on net assets (RONA). This reflects the competitive reality that, for companies like HP, advantage derives less from market share than from how efficiently the firm manages its assets – in other words, its supply chain. As the exhibit "Linking Inventory Costs to Financial Performance" shows, the relationship between inventory-driven costs and return on net assets is direct, simple, and powerful, which makes it far easier to align the interests and decisions of managers up and down the hierarchy.

The financial benefits have come quickly. HP's Personal Systems Group, for example, saw worldwide inventory decline by 50% between 2000 and 2002, and it has maintained that level ever since. Costs associated with inventory have dropped even further, by some 70%. Since HP's merger with Compaq in May 2002, the push to adopt IDC companywide has moved forward. At this point, all of HP has adopted a standard set of inventory-driven cost metrics.

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Hewlett-Packard isn't the only company, of course, that operates in a dynamic, highly price-competitive industry. Consumer electronics, fashion producers, and fresh-goods retailers all face similar challenges. Any company with low margins, short life cycles, highly perishable or seasonal products, and unpredictable demand needs to track the various components of its inventory-driven costs. Without appropriate performance metrics to help visualize the magnitude of their supply chain problems and to prompt people to take action, these firms will simply not know if they are leaving hefty piles of money on the table.

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Presenteeism: At Work – But Out of It

In light of the business community's drive to reduce health care costs, we were intrigued by Paul Hemp's contention in "Presenteeism: At Work – But Out of It" (October 2004) that "presentee" employees – those who go to work with untreated illnesses instead of staying home – may be costing U.S. companies billions of dollars annually. We are

HBR AT LARGE

Presenteeism:
At Work – But Out of It

by Paul Hemp

As companies struggle to rein in health care costs, most overlook what may be a $150 billion problem: the nearly invisible drain on worker productivity caused by such common ailments as hay fever, headaches, and even heartburn.

For years, Amy Farler, who designs transmission components for International Truck and Engine, suffered in silence. Once in a while, when an allergy-related sinus headache escalated into a full-blown migraine, she missed a day of work. But most of the time, she went to the office and quietly lived with the congestion and discomfort of her seasonal allergies. "Sometimes, it's like you wouldn't mind if your head rolled off your body," says the 31-year-old engineer, who spends most of her day working with 3-D models on a computer screen. "You feel clogged up and hazy. The pressure makes you want to close your eyes. It's hard to focus. You end up just muddling through."

Woody Allen once said that 80% of success in life can be attributed to simply showing up. But a growing body of research indicates that – in the workplace, at least – this wry estimate may be somewhat optimistic. Researchers say that *presenteeism* – the problem of workers' being on the job but, because of illness or other medical conditions, not fully functioning – can cut individual productivity by one-third or more. In fact, presenteeism appears to be a much costlier problem than its productivity-reducing counterpart, absenteeism. And, unlike absenteeism, presenteeism isn't always apparent: You know when someone doesn't show up for work, but you often can't tell when – or how much – illness or a medical condition is hindering someone's performance. "Outwardly you look fine," says Farler, who over the years tried numerous prescription and nonprescription medications for her allergies, with little success. "People don't see how you feel."

However, a handful of companies – including International Truck and Engine, Bank One (recently acquired by

DANIEL CHANG

OCTOBER 2004 49

primary care physicians who have collectively worked for more than a half century in a city that boasts one of the most aggressive managed-competition markets in the United States. We've seen that the managed-care revolution and other recent cost control efforts have been moderately successful, at least in blunting the rate of increase. But the article seems to support critics who say these systems throw up roadblocks to appropriate care, depriving patients of needed services and drugs, and it implies that such roadblocks result in increased presenteeism.

We presume corporate leaders will be intrigued by this issue, too – American employers pay a greater proportion of health insurance than companies in any other Western nation. But before the business community can be convinced to invest money to combat presenteeism, more work must be done to characterize the nature and size of the problem. For instance, researchers must establish a baseline for decreased productivity due to illness. Imagine a person who is 100% healthy and productive. (Quick! Send him to work for us!) Does that person represent the baseline? Would any deviation from 100% health and 100% productivity be considered presenteeism? We think not. The 100% ideal is just that, an ideal.

An equally vexing problem is how to remedy the situation. Should clinical guidelines be applied more rigorously? Should employees be screened for the most costly diseases? Should employers pay closer attention to "report cards" for physicians and medical groups? Should workplace health care systems be enhanced? We are grateful to the author for stimulating thought along these lines.

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First, Empower All the Lawyers

As a lawyer who has worked both in-house and at major law firms, I was annoyed by Larry Downes's opinion piece "First, Empower All the Lawyers" (Forethought, December 2004). It reflects the typical managerial attitude that lawyers should be encouraged "to use law as a strategic weapon." I'd like to make three points:

First, anyone suggesting that law be used as a weapon in business loses all rights to complain about the legal, regulatory, and insurance burdens that have been brought down on business by companies that have attempted to use law as a weapon.

Second, it is all very well to complain about in-house lawyers who don't know enough about intellectual property, antitrust, or the other complex and highly specialized areas of law Downes lists. But the simple fact is that most corporate legal departments are understaffed (precisely because they are viewed as expensive overhead) with lawyers who are expected by management to magically answer questions about every area of the law – an impossible task.

Third, it is certainly the mark of the mediocre lawyer to just say "No" or "Don't do that" without proposing alternative solutions to the problems at hand or providing a reasoned assessment of the company's legal risk. But lawyers add the most value to an organization by preventing it from engaging in conduct that will ultimately destroy value. Lawyers are often seen as "roadblocks to innovation" – but an ounce of prevention…

While there is a certain schadenfreude in seeing predicted disasters occur when management charges ahead despite warnings, it would be more gratifying to in-house counsel if companies would "fix" their supposedly "broken" legal departments by focusing less on weaponizing them and more on listening to them.

Colin P.A. Jones
Founder
Lexdox Japan
Tokyo

The Wild West of Executive Coaching

It's clear that there's a need for executive coaching – the technically brilliant leader who leaves a wake of bitter coworkers is all too common. It's equally clear, as Stratford Sherman and Alyssa Freas point out in "The Wild West of

Executive Coaching" (November 2004), that organizations looking to improve their leaders' behavior face major obstacles. There are no accepted standards for executive coaching, there are no agreed-upon criteria for what makes a coach qualified, and there's no well-understood way to know whether coaching is working.

But my colleagues and I see a glimmer of a solution where the authors don't. We worked with executive coach Marshall Goldsmith to study proprietary data from leadership development initiatives conducted for nearly 12,000 leaders at eight large companies. What a leader should want to know is whether peers and direct reports notice a behavioral improvement that makes a difference to them. So the data included 86,000 responses by colleagues to surveys on perceived changes in the leaders' behavior. We found that the more the leaders involved their colleagues in the behavior-improvement process (for example, by asking for suggestions), the more likely the colleagues were to report amelioration in the leaders' behavior. (Some 94% of leaders who were thorough about dialogue and follow-up with colleagues were perceived as having made a positive behavior change.) Leaders who made the least effort at dialogue and follow-up were perceived as having achieved the least amount of positive behavior change (some 60% of their colleagues perceived them as unchanged or even worse than before).

This research reaffirms the coaching approach we advocate. We put the leaders at the center of an ongoing dialogue with their colleagues, who serve as partners in the effort. Rather than being the star, the coach is the facilitator; the leader and his or her colleagues are the main players.

On the matter of quantifying results, which Sherman and Freas say is nearly impossible, my colleagues have developed – and have been using for some time – metrics that enable clients to systematically track leaders' progress toward behavioral change. The metrics are based on the leaders' colleagues' perceptions. We've teamed up with Marshall Goldsmith to form an executive coaching firm that gets paid only if the intervention leads to a positive change in executive behavior. I hope we're bringing some order to the Wild West of coaching.

Niko Canner
Managing Partner
Katzenbach Partners
Cofounder, Marshall Goldsmith Partners, a subsidiary of Katzenbach Partners
New York

It's bad enough that the authors present executive coaching as a panacea. But I'm more disappointed that HBR would publish an article that is so blatantly a commercial for a consulting organization – it's full of comments such as "We are deeply committed to helping our coachees lead better lives." I would have expected HBR to insist that such an article be written from the standpoint of objective experts.

James F. Bolt
Chairman
Executive Development Associates
San Francisco

Sherman and Freas respond: Thanks to Niko Canner for highlighting the facilitative nature of coaching. We know and admire Marshall Goldsmith, whose insights and energy have significantly influenced us both. Our independent experience strongly supports Goldsmith's conclusions about the benefit of engaging a coachee's business colleagues in the coaching process. That said, measuring colleagues' perceptions of behavioral change isn't new, and the relationship of those measurements to business outcomes is obscure. Human nature – the context in which all coaching metrics must be evaluated – remains immeasurable. As for James Bolt's view that coaching is not a panacea, we agree.

Erratum: Due to a transcription error, the company name Alstom was misspelled on page 119 of the February 2005 issue (in the HBR Interview entitled "Transforming an Industrial Giant"). HBR regrets the error.

March 2005

COMING IN APRIL 2005

How Strategists Really Think: Tapping the Power of Analogy
Giovanni Gavetti and Jan W. Rivkin

Countering the Biggest Risk of All
Adrian J. Slywotzky and John Drzik

The Quest for Customer Focus
Ranjay Gulati and James B. Oldroyd

Page 16

FORETHOUGHT

Sorting Data to Suit Yourself Letting customers organize *your* information the way *they* want is a cool benefit today but will be a necessity tomorrow, says Harvard Law School Internet scholar David Weinberger. **Reprint F0503A**

Both Sides Now What's an oligonomy? A market with few sellers *and* few buyers, says market watchdog Steve Hannaford, and Wal-Mart controls the most notorious one. **Reprint F0503B**

Rotate the Core By rotating key executives through headquarters, companies can keep corporate lean but still hold sway over the units, says BCG senior VP George Stalk, Jr. **Reprint F0503C**

Expanding in China Bain consultants Ann Chen and Vijay Vishwanath offer three key strategies multinationals can use to expand from China's premium segment into the broader market. **Reprint F0503D**

No More Metaphors Truly new ideas spawn original language, but where new management ideas should be, there are too many clichés borrowed from other fields. We deserve better, argues HBR senior editor Leigh Buchanan. **Reprint F0503E**

Global Manufacturers at a Crossroads As multinationals decrease their direct investment in low-wage markets, they're opening the door to dangerous competitors, says Deloitte consultant Peter Koudal. **Reprint F0503F**

Vanishing Jobs? Blame the Boomers Baby busters won't get the jobs the boomers leave behind, warns demographer Phillip Longman. **Reprint F0503G**

The Faster They Fall The likelihood that an industry leader will lose its top position within five years has doubled since 1972, say McKinsey consultants S. Patrick Viguerie and Caroline Thompson. **Reprint F0503H**

Outsourcing Marketing Marketing is becoming more analytic and less creative. That's why, HBS professors Gail McGovern and John Quelch assert, more companies are finding it makes sense to outsource many marketing functions. **Reprint F0503J**

Lessons from the Slums of Brazil JetBlue's David Neeleman talks about how his unexpected lessons from working with the poor have informed his company's egalitarian culture. **Reprint F0503K**

Book Reviews HBR reviews four books.

Page 31

HBR CASE STUDY

The Shakedown

Phil Bodrock

Customer Strategy Solutions, a California-based developer of order-fulfillment systems, is facing a shakedown. Six months after the firm's CEO, Pavlo Zhuk, set up a software development center in Kiev, local bureaucrats say the company hasn't filed all the tax schedules it should have. Moreover, Ukrainian tax officials claim that the company owes the government tax arrears. Zhuk is shocked; he and his colleagues have done everything by the book.

This isn't the first time Zhuk has encountered trouble in Ukraine. In the process of getting the development center up and running, a state-owned telecommunications utility had made it difficult for Zhuk to get the phone lines his company needed. Senior telecom manager Vasyl Feodorovych Mylofienko had told Zhuk it would take three years to install the lines in his office – but for a certain price, Mylofienko had added, the lines could be functioning the following week.

Even as the picture of rampant bribery and corruption in Ukraine becomes clear, Zhuk still doesn't want to pull out of the country. Of Ukrainian descent, he has dreams of helping to modernize the country. By paying his programmers more than they could make at any local company, he hopes to raise their standard of living so they can afford three meals a day without having to barter, stand in queues for hours, or moonlight. And yet, he isn't sure he can keep compromising his principles for the sake of the greater good.

Should Customer Strategy Solutions pay off the Ukrainian tax officials? Commenting on this fictional case study are Alan L. Boeckmann, the chairman and CEO of Fluor Corporation; Rafael Di Tella, a professor at Harvard Business School; Thomas W. Dunfee, the Kolodny Professor of Social Responsibility and a professor of legal studies at Wharton; and Bozidar Djelic, the former finance and economy minister of Serbia.

Reprint R0503A

Page 43

BIG PICTURE

Off-Ramps and On-Ramps: Keeping Talented Women on the Road to Success

Sylvia Ann Hewlett and Carolyn Buck Luce

Most professional women step off the career fast track at some point. With children to raise, elderly parents to care for, and other pulls on their time, these women are confronted with one off-ramp after another. When they feel pushed at the same time by long hours and unsatisfying work, the decision to leave becomes even easier. But woe to the woman who intends for that exit to be temporary. The on-ramps for professional women to get back on track are few and far between, the authors confirm. Their new survey research reveals for the first time the extent of the problem – what percentage of highly qualified women leave work and for how long, what obstacles they face coming back, and what price they pay for their time-outs.

And what are the implications for corporate America? One thing at least seems clear: As market and economic factors align in ways guaranteed to make talent constraints and skill shortages huge issues again, employers must learn to reverse this brain drain. Like it or not, large numbers of highly qualified, committed women need to take time out of the workplace. The trick is to help them maintain connections that will allow them to reenter the workforce without being marginalized for the rest of their lives.

Strategies for building such connections include creating reduced-hour jobs, providing flexibility in the workday and in the arc of a career, removing the stigma of taking time off, refusing to burn bridges, offering outlets for altruism, and nurturing women's ambition. An HBR Special Report, available online at www.womenscareersreport.hbr.org, presents detailed findings of the survey.

Reprint R0503B; HBR OnPoint 9416; OnPoint collection "Required Reading for Executive Women – and the Companies Who Need Them" 9394

Page 58

Lean Consumption

James P. Womack and Daniel T. Jones

During the past 20 years, the real price of most consumer goods has fallen worldwide, the variety of goods and the range of sales channels offering them have continued to grow, and product quality has steadily improved. So why is consumption often so frustrating? It doesn't have to be – and shouldn't be – the authors say. They argue that it's time to apply lean thinking to the processes of consumption – to give consumers the full value they want from goods and services with the greatest efficiency and the least pain.

Companies may think they save time and money by off-loading work to the consumer but, in fact, the opposite is true. By streamlining their systems for providing goods and services, and by making it easier for customers to buy and use those products and services, a growing number of companies are actually lowering costs while saving everyone time. In the process, these businesses are learning more about their customers, strengthening consumer loyalty, and attracting new customers who are defecting from less user-friendly competitors.

The challenge lies with the retailers, service providers, manufacturers, and suppliers that are not used to looking at total cost from the standpoint of the consumer and even less accustomed to working with customers to optimize the consumption process.

Lean consumption requires a fundamental shift in the way companies think about the relationship between provision and consumption, and the role their customers play in these processes. It also requires consumers to change the nature of their relationships with the companies they patronize.

Lean production has clearly triumphed over similar obstacles in recent years to become the dominant global manufacturing model. Lean consumption, its logical companion, can't be far behind.

Reprint R0503C; HBR OnPoint 9432

Page 70

What Great Managers Do

Marcus Buckingham

Much has been written about the qualities that make a great manager, but most of the literature overlooks a fundamental question: What does a great manager actually *do?* While there are countless management styles, one thing underpins the behavior of all great managers. Above all, an exceptional manager comes to know and value the particular quirks and abilities of her employees. She figures out how to capitalize on her staffers' strengths and tweaks her environment to meet her larger goals.

Such a specialized approach may seem like a lot of work. But in fact, capitalizing on each person's uniqueness can save time. Rather than encourage employees to conform to strict job descriptions that may include tasks they don't enjoy and aren't good at, a manager who develops positions for his staff members based on their unique abilities will be rewarded with behaviors that are far more efficient and effective than they would be otherwise.

This focus on individuals also makes employees more accountable. Because staffers are evaluated on their particular strengths and weaknesses, they are challenged to take responsibility for their abilities and to hone them.

Capitalizing on a person's uniqueness also builds a stronger sense of team. By taking the time to understand what makes each employee tick, a great manager shows that he sees his people for who they are. This personal investment not only motivates individuals but also galvanizes the entire team.

Finally, this approach shakes up existing hierarchies, which leads to more creative thinking.

To take great managing from theory to practice, the author says, you must know three things about a person: her strengths, the triggers that activate those strengths, and how she learns. By asking the right questions, squeezing the right triggers, and becoming aware of your employees' learning styles, you will discover what motivates each person to excel.

Reprint R0503D

Page 80

MarketBusting: Strategies for Exceptional Business Growth

Rita Gunther McGrath and Ian C. MacMillan

If company leaders were granted a single wish, it would surely be for a reliable way to create new growth businesses. Business practitioners' overwhelming interest in this subject prompted the authors to conduct a three-year study of organizational growth – specifically, to find out which growth strategies were most successful.

They discovered, somewhat to their surprise, that even companies in mature industries found rich new sources of growth when they reconfigured their *unit of business* (what they bill customers for) or their *key metrics* (how they measure success). In this article, the authors outline these and other moves companies can make to redefine their profit drivers and realize low-risk growth. They offer plenty of real-world examples. For instance:

Changing Your Unit of Business. Once a conventional printing house, Madden Communications not only prints promotional materials for customers but also manages the distribution and installation of those materials on-site. Its revenues grew from $10 million in 1990 to $133 million in 2004, in an industry that many had come to regard as hopelessly mature.

Improving Your Key Metrics – Particularly Productivity. Lamons Gasket, with $80 million in revenues, built a Web site that radically improved its customers' ability to find, order, and pay for goods. The firm's market share rose along with its customer retention rate.

The authors also suggest ways to identify your unit of business and associated key metrics and recognize the obstacles to changing them; review the key customer segments you serve; assess the need for new capabilities and the potential for internal resistance to change; and communicate to internal and external constituencies the changes you wish to make in your unit of business or key metrics.

Reprint R0503E; HBR OnPoint 9408; OnPoint collection "Spur Market-Busting Growth" 9386

Page 92

Want Collaboration? Accept – and Actively Manage – Conflict

Jeff Weiss and Jonathan Hughes

Companies try all kinds of ways to improve collaboration among different parts of the organization: cross-unit incentive systems, organizational restructuring, teamwork training. While these initiatives produce occasional success stories, most have only limited impact in dismantling organizational silos and fostering collaboration.

The problem? Most companies focus on the symptoms ("Sales and delivery do not work together as closely as they should") rather than on the root cause of failures in cooperation: conflict. The fact is, you can't improve collaboration until you've addressed the issue of conflict. The authors offer six strategies for effectively managing conflict:

- Devise and implement a common method for resolving conflict.
- Provide people with criteria for making trade-offs.
- Use the escalation of conflict as an opportunity for coaching.
- Establish and enforce a requirement of joint escalation.
- Ensure that managers resolve escalated conflicts directly with their counterparts.
- Make the process for escalated conflict-resolution transparent.

The first three strategies focus on the point of conflict; the second three focus on escalation of conflict up the management chain. Together they constitute a framework for effectively managing discord, one that integrates conflict resolution into day-to-day decision-making processes, thereby removing a barrier to cross-organizational collaboration.

Reprint R0503F

Page 102

THE HBR INTERVIEW

Execution Without Excuses

Michael Dell and Kevin Rollins Interviewed by Thomas A. Stewart and Louise O'Brien

The success of Dell – it provides extraordinary rewards to shareholders, it can turn on a dime, and it has demonstrated impeccable timing in entering new markets – is based on more than its famous business model. High expectations and disciplined, consistent execution are embedded in the company's DNA.

"We don't tolerate businesses that don't make money," founder Michael Dell tells HBR. "We used to hear all sorts of excuses for why a business didn't make money, but to us they all sounded like 'The dog ate my homework.' We just don't accept that."

In order to double its revenues in a five-year period, the company had to adapt its execution-obsessed culture to new demands. In fact, Michael Dell and CEO Kevin Rollins realized they had a crisis on their hands. "We had a very visible group of employees who'd gotten rich from stock options," Rollins says. "You can't build a great company on employees who say, 'If you pay me enough, I'll stay.'" Dell and Rollins knew they had to reignite the spirit of the company.

They implemented an employee survey, whose results led to the creation of the Winning Culture initiative, now a top operating priority at Dell. They also defined the Soul of Dell: Focus on the customer, be open and direct in communications, be a good global citizen, have fun in winning. It turned out to be a huge motivator. And they increased the focus on developing people within the company.

"We've changed as individuals and as an organization," Rollins says. "We want the world to see not just a great financial record and operational performance but a great company. We want to have leaders that other companies covet. We want a culture that makes people stick around for reasons other than money."

Reprint R0503G

Page 124

BEST PRACTICE

A Practical Guide to Social Networks

Rob Cross, Jeanne Liedtka, and Leigh Weiss

Saying that networks are important is stating the obvious. But harnessing the power of these seemingly invisible groups to achieve organizational goals is an elusive undertaking. Most efforts to promote collaboration are haphazard and built on the implicit philosophy that more connectivity is better. In truth, networks create relational demands that sap people's time and energy and can bog down entire organizations. It's crucial for executives to learn how to promote connectivity only where it benefits an organization or individual and to decrease unnecessary connections.

In this article, the authors introduce three types of social networks, each of which delivers unique value. The *customized response network* excels at framing the ambiguous problems involved in innovation. Strategy consulting firms and new-product development groups rely on this format. By contrast, surgical teams and law firms rely mostly on the *modular response network,* which works best when components of the problem are known but the sequence of those components in the solution is unknown. And the *routine response network* is best suited for organizations like call centers, where the problems and solutions are fairly predictable but collaboration is still needed.

Executives shouldn't simply hope that collaboration will spontaneously occur in the right places at the right times in their organization. They need to develop a strategic, nuanced view of collaboration, and they must take steps to ensure that their companies support the types of social networks that best fit their goals.

Drawing on examples from Novartis, the FAA, and Sallie Mae, the authors offer managers the tools they need to determine which network will deliver the best results for their organizations and which strategic investments will nurture the right degree of connectivity.

Reprint R0503H

Page 135

TOOL KIT

Inventory-Driven Costs

Gianpaolo Callioni, Xavier de Montgros, Regine Slagmulder, Luk N. Van Wassenhove, and Linda Wright

In the 1990s, Hewlett-Packard's PC business was struggling to turn a dollar, despite the company's success in winning market share. By 1997, margins on its PCs were as thin as a silicon wafer, and some product lines hadn't turned a profit since 1993.

The problem had everything to do with the PC industry's notoriously short product cycles and brutal product and component price deflation. A common rule of thumb was that the value of a fully assembled PC decreased 1% a week. In such an environment, inventory costs become critical. But not just the inventory costs companies traditionally track, HP found, after a thorough review of the problem. The standard "holding cost of inventory" – the capital and physical costs of inventory – accounted for only about 10% of HP's inventory costs. The greater risks, it turned out, resided in four other, essentially hidden costs, which stemmed from mismatches between demand and supply:

Component devaluation costs for components still held in production;

Price protection costs incurred when product prices drop on the goods distributors still have on their shelves;

Product return costs that have to be absorbed when distributors return and receive refunds on overstock items, and;

Obsolescence costs for products still unsold when new models are introduced.

By developing metrics to track those costs in a consistent way throughout the PC division, HP has found it can manage its supply chains with much more sophistication. Gone are the days of across-the-board measures such as, "Everyone must cut inventories by 20% by the end of the year," which usually resulted in a flurry of cookie-cutter lean production and just-in-time initiatives. Now, each product group is free to choose the supply chain configuration that best suits its needs. Other companies can follow HP's example.

Reprint R0503J

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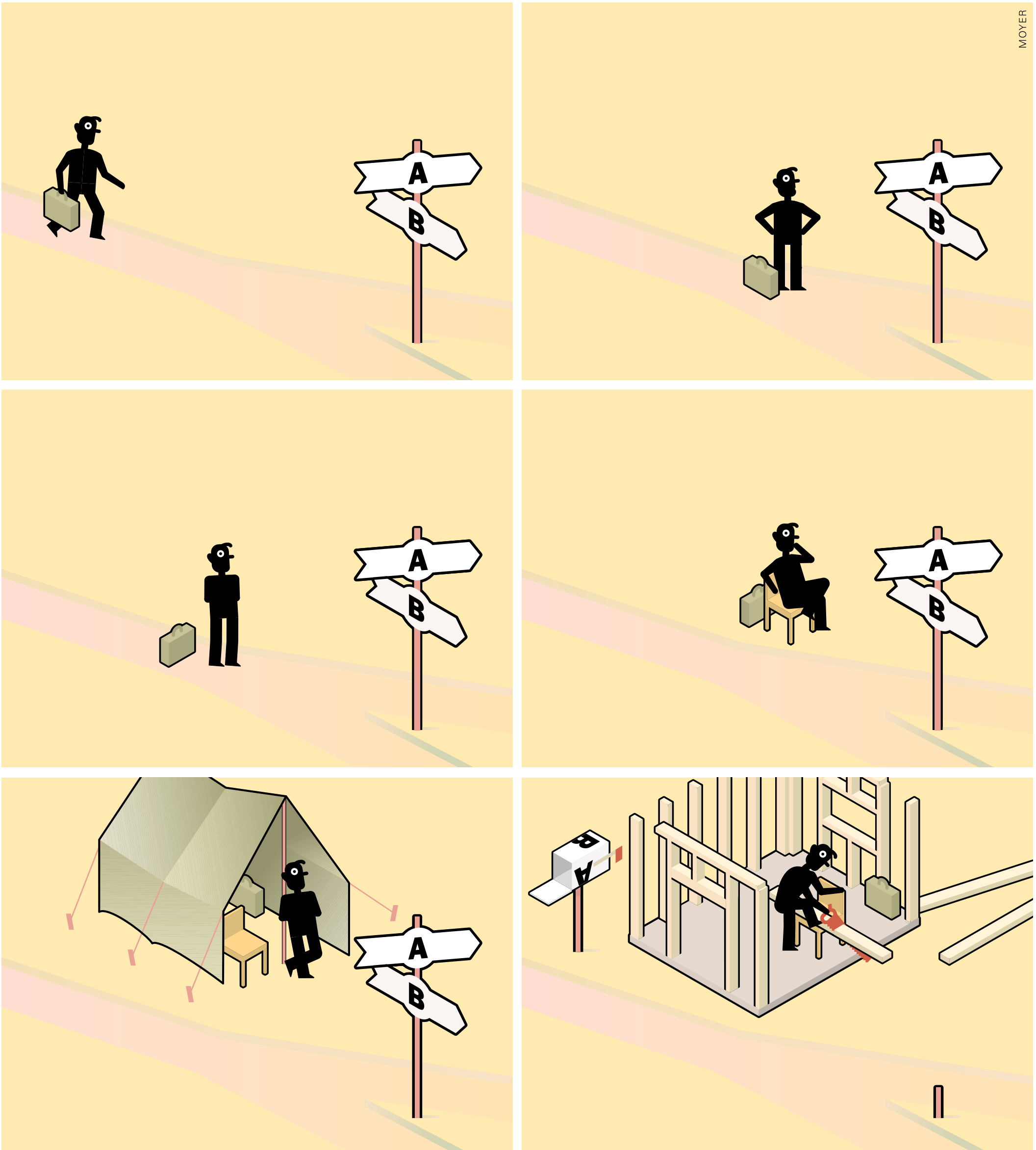
Volume 83, Number 3

by Don Moyer



The Snap Trap

Decisiveness is the leadership trait that brooks no compromise. Great leaders, we are told, assess their options and choose a course with supercomputer-like speed. Rat-a-tat-tat: Triple production! Rat-a-tat-tat: Fire the bastard!

What's the hurry? A few problems – defective products, dodgy financial reports – require immediate action. But as Joseph Badaracco points out in his article, "We Don't Need Another Hero" (HBR, September 2001), "the drama of do-or-die situations can lead us to exaggerate the frequency with which they arise." Time exists to be taken. A slower, more deliberative approach lets you collect facts, analyze subtleties, and challenge assumptions.

You may also come up with some new possibilities, which is good. In a comparison of two things, according to the rules of grammar, it can be said only that one is better than the other. In a comparison of more things, one will be the best.

Don Moyer can be reached at don@amsite.com.

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