Re-inventing Management

Through the years, I have watched with a kind of morbid fascination the number of once powerful companies that are no longer around. It would appear that Darwinian principles apply to companies as much as to organisms. There seems to be a kind of life cycle to a business, and beyond a certain number of years, *the invisible hand* of the marketplace lets you know that your time is up. And every so often, a kind of *near-mass-extinction* event seems to afflict a whole industry, such as is currently happening in the financial sector around the world.

How I came to my fatalistic view of business is not hard to understand. IBM's near-death experience in the 1990s was very painful for me personally and for all us in the company. Even though we managed to survive, as well as to recover and regain a position of leadership in the IT industry, the traumatic experience has definitely left its imprint and colors my views of the world.

Then there are the facts. In her book *Let Go to Grow*, my IBM colleague Linda Sanford cites a number of ominous statistics. For example, of more than 1,000 companies tracked by the Fortune 500 since 1960, less than one sixth of them are still around.

Over the years, I have personally seen many mighty companies in the IT industry disappear altogether, such as Digital, Compaq and Wang, while others like Cray, Fujitsu and SGI are but shadows of their former selves. Just before sitting down to write this post, I was reading about Sun Microsystems, one of the most successful computer companies in the last 20 years, at the top of the world during the dot-com days, being pushed to the brink by the present economic downturn.

While the carnage might arguably be more pronounced in the IT industry due to the fast-changing nature of information technologies, no industry is immune. As we know, the banking industry is going through the worst global financial crisis since the Great Depression. Digital technologies and the Internet are transforming the music industry right in front of our eyes. Similar transformations are occurring in just about all mass media industries, from newspapers to television. The list goes on. Indeed, “immunity” is probably the wrong metaphor. There is no industry or area of human activity any longer that remains "uninfected".

There is little question that we are truly undergoing a technology-driven transition of historic proportions, from the industrial to the knowledge economy. If you examine similar past major transitions, the revolutionary technology in question - IT in our case - acts as an engine of growth, rejuvenating and transforming whole industries and the whole economy, as well as re-shaping social behavior and the institutions of society. For one reason or another, many companies will not be able to adapt to the new environments. When that is the case, their fate is sealed.

What can a business do to maximize its chances of survival? Foremost is to embrace a *culture of innovation*. If the environment is going to change, you want to be among the first to anticipate the changes and start preparing for them. A commitment to innovation may not always help your business stay out of serious trouble, but having a good strategy and understanding of your options will help you transform the business and survive.

What is the role of senior management in all this? We know that the management of all companies is subject to all kinds of short-term pressures, - improving the competitiveness of the operating units, achieving solid financial results, attracting and retaining customers, and so on. But isn't the key responsibility of the senior management team - including the CEO and top executives, as well as the board of directors - to manage strategic uncertainty and create strategic options for the business?

You would expect that in today's environment, with such an uncertain future, this would be how the senior management of a company spends a significant portion of its time. But, we know that is not the case. Executives typically rise up in the organization by being very good operational managers. These management jobs are very tough and getting tougher. Being a good manager takes very hard work, attention to detail and organizational discipline.

People who do well in such operational jobs will tend to be the ones promoted to senior management positions. But as executives rise up in the organization, other skills become increasingly important. In particular, executives have to make the transition from managing the present to managing both the present and the future - that is, they now have to be good at both operations and strategy. They also have to make the transition from being good at delivering business results and running processes to being both good managers and good leaders.

This transition represents a kind of phase shift for the individual. The criteria for success early in a person's career are always going to be more operational than strategic – if only because lower-level employees don't get the opportunity to make large strategic decisions. Nonetheless, even if they are not primarily getting rewarded for having a vision of the future of the company or the ability to inspire people to buy into the vision and help make it a reality, they had better develop those skills along the way, because they will need them if and when they reach senior positions in their organization.

Of course, when skies are blue, a company might be able to cruise along with top operational managers who are indifferent strategists and leaders. But once the skies begin to darken, as they inevitably do, such managers will get into deep trouble, and often end up taking the business down with them. They have no one to rely on, because in all likelihood their most talented innovators and strategists, those whose skills are now badly needed to help set the business on the proper course, have either long departed or become so disenchanted that they have nothing left to give.

Most top managers hold advanced degrees from very good universities. So, it is reasonable to ask the question whether the business, management and engineering schools at such universities are doing a good job of preparing their students for the kind of market environment they will face once they graduate. Just about all indications are that universities, even the very top ones, are not properly preparing their students for the brave new world out there, especially as those students rise up in their companies and become senior executives.

Universities do an excellent job in teaching hard, quantitative, discrete skills - engineering methods, analytical tools, finance, marketing, etc. But they fall behind when it comes to preparing the students with so-called *soft skills*, which are more people-oriented and systemic in nature - human capital, decision making, strategy and innovation. Everyone is aware of the need to re-invent engineering and management education, and emphasize *soft* as well as *hard* skills. But changes come slowly, especially in academia.

We are living in a fast-changing, complex, fiercely competitive global world. Many companies have not yet adjusted to these market realities, and continue to promote and rely on executives who grew up and became successful in a kinder, gentler world. Universities are not helping enough, as they seemingly continue to prepare students for the industrial economy of the past, not the knowledge-based, global economy we are entering.

Re-inventing management is one of the most important responsibilities any company needs to undertake to maximize its chances of survival into this future. Re-inventing management education is one of the most important responsibilities of universities to help better prepare future managers for the kind of world they will encounter. These tough challenges will require us to open our minds to new ways of thinking. In the end, that is what innovation is all about.

Lou Gerstner at MIT

Leadership was the overriding objective of the graduate seminar I taught at MIT last Fall, - *Technology-based Business Transformation*, - which I will be teaching again in the Fall of 2008. I told the students at our first meeting that I hoped the course would help them develop or enhance their leadership skills, so they can better deal with the complex systems, complex markets and complex organizations they will likely encounter throughout their careers.

In the course, we used Lou Gerstner's book "Who Says Elephants Can't Dance", which all students read and we discussed extensively in class. Given my professional relationship with Lou, with whom I worked closely in his nine years at IBM, I invited him to come lecture to the class. He accepted, but due to health problems we had to postpone his visit.

Lou's visit to MIT took place on March 12. While my class was not in session this semester, we scheduled a breakfast meeting with all students in Systems and Design Management (SDM), the program that most of my students belong to, a public lecture as part of the Dean's Innovative Leader Series at the Sloan School of Management, and a few smaller meetings.

SDM is an interdisciplinary program between the School of Engineering and the Sloan School of Management, whose graduates receive a master of science in engineering and management. To kick off our discussion, I read a paragraph from Lou's book, which I had used in the section on organizational culture in the class:

"I came to see, in my time at IBM, that culture isn't just one aspect of the game – it is the game. In the end, an organization is nothing more than the collective capacity of its people to create value. Vision, strategy, marketing, financial management – can set you on the right path and can carry you for a while. But no enterprise – whether in business, government, education, health care, or any area of human endeavor - will succeed over the long haul if those elements aren't part of its DNA."

Lou asked the students to reflect on how many companies had not been able to turn themselves around when a new technology disrupted their business model, not because they did not know what to do, but because the culture of the institution did not embrace the change. He reminded us that while most companies say that their culture is about the pursuit of lofty goals like outstanding customer service, teamwork, excellence, and shareholder value, most of the really important rules of culture are not written down anywhere. Successful institutions almost always develop strong cultures that reinforce those elements that make the institution great. But, when the environment shifts, it is very hard and painful for the culture to change. The culture then becomes the key impediment to the institution's ability to adapt.

He told the story that early in his IBM tenure he made the decision that IBM was more valuable as an integrated company that could help solve complex problems and build solutions for clients. He then realized that he needed to make sure that people in IBM worked well together as a team. You could not integrate the company in front of the customer if it was not integrated internally.

But IBM was famous for its internal contention system, where units generally did not cooperate with each other. He realized that to change the culture, he had to change the compensation incentives that had given rise to that culture. Previously, IBM executives had been paid mostly on their own unit's performance, and thus had little financial incentive to work together across divisions. Without changing the compensation system, difficult as that was, he could not address the impediments to effective teamwork.

So now, his director reports, the general managers who led the various divisions, would be paid 90% on IBM's overall performance and 10% on their unit's performance. One or two levels down in the organization, the pay would now be based 60% on IBM's results and 40% on those of the unit. When people saw the change, they realized that the new CEO meant it when he said that teamwork and cooperation were absolutely necessary across the whole company.

Later in the day, Lou gave his public lecture - *Leadership is a Lifetime Journey* - to an overflow audience. He said that in his opinion, the concepts of line and staff management were outmoded. A good organization needs good business line managers - responsible for the revenue and profits of their units, as well as good process managers. The job of the process manager is to make sure that the individual processes of the organization - finance, HR, customer service, fulfillment, manufacturing, supply chain, IT and so on, were as efficient and high quality as possible.

Many companies do not pay serious attention to process management, and in fact allow different unit to each design and run their own processes. The results are almost always bad. Not only do the costs go up, because of redundant efforts across the company that could have been done globally for everyone, but different implementations of the same process make it difficult to integrate the company and share information and talent. Moreover, when key processes are part of individual units, it will be harder to attract top talent, pay them accordingly, and give them the necessary scope of responsibility needed to achieve world class processes.

Lou focused most of his remarks on leadership. The key quality you need for good leadership is passion - the urgency to attack and solve the complex problems that all organizations face. You cannot delegate leadership and passion the way you can delegate management tasks. It is critical that leaders roll up their sleeves and work closely with the teams addressing these complex problems - not as the manager presiding over the work, but as a trusted and respected colleague.

He illustrated his point with an example. When launching a new effort, the people doing the work will often schedule periodic reviews with their manager at fixed intervals - say every three months. That is all wrong he said. Most the major decisions in a new initiative will get made in the first few months. If the manager is a true leader - he or she will work closely with the team during that critical period, and do so - to whatever extent is possible, - as a peer of the members of the group, going to their offices and conference rooms where the real work is getting done.

I can attest that Lou practiced what he talks about. In 1996, in the first twelve months of the IBM Internet Division, we made a number of critical decisions. We decided not to get involved in the browser wars then raging between Netscape and Microsoft. We embraced Java, even though the technology had been developed by Sun Microsystems, one of our fiercest system competitors. We shut down a number of the efforts aiming to position IBM as an Internet content provider. We started to develop what became our successful e-business market strategy. Throughout that period, I had lots of informal, working meetings with Lou and others in IBM's senior management team, debating back and forth the pros and cons of the different decisions we were making.

Lou Gerstner's visit to MIT was very stimulating and educational for all of us. As Sloan Dean David Schmittlein said, we had just had a master's class in leadership from one of the very best business leaders in the world.