MEMO TO THE CEO

Winning in Turbulence

Strengthen the Organization

BY

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PREVIEWS THE FORTHCOMING BOOK

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Strengthen the Organization

WHO'S GOT TIME to worry about building a stronger organization in an acute downturn? Surely executives can't focus on internal issues when so many other pressing matters are crowding in on them.

In fact, this is exactly the time when leaders need to ensure their organizations are performing well, so that important decisions get made and executed quickly and effectively. Turbulence creates exceptional opportunities for some organizations and extraordinary urgency for others. None should be satisfied with the status quo.

It's clear enough how a company that is relatively strong can gain by strengthening its organization. Turbulence offers a rare chance to bring in new talent and improve the way that organizations function. But while skepticism from executives under stress is natural, companies in dire straits have everything to gain from investing in their organizations. They often lack the organizational capabilities to take on the challenges they face. Some rush to snap judgments and ill-considered decisions. Others stall, unable to make key decisions. Some of these companies badly need new people and the perspectives they bring to help the business survive. They may need to overhaul dysfunctional cultures—the kind, for instance, that supported excessive risk and reward without accountability. They certainly need to revisit the questionable decision processes that landed them in so much trouble.

The fact is, strengthening the organization is one of the most powerful levers any company can pull to improve its performance in a downturn. As we've said throughout this series, industries are affected differently by different recessions. Individual companies occupy stronger or weaker competitive positions. Some have adequate financial resources; others are strapped for cash. These differences determine a company's action plan in turbulence.

But even though the situations and necessary actions vary widely, the questions that companies must ask to strengthen their organizations are largely the same. What are the critical decisions we must address in this downturn? Do we need to adjust our organizational structure to address them effectively? How should our roles and processes change? Will our most experienced people be able to make and execute the key decisions, or are new skills and perspectives required? Which aspects of our culture reinforce decision effectiveness, and which should be thrown out?

Adopting this "decision lens"—by identifying the critical decisions and then determining what needs to change in order to help the organization make and execute those decisions effectively—is the single most important step a company can take to improve the performance of its organization. It helps leaders focus their efforts where they will have the most impact during a downturn. And it positions the company to accelerate when the economy turns around (figure 1).

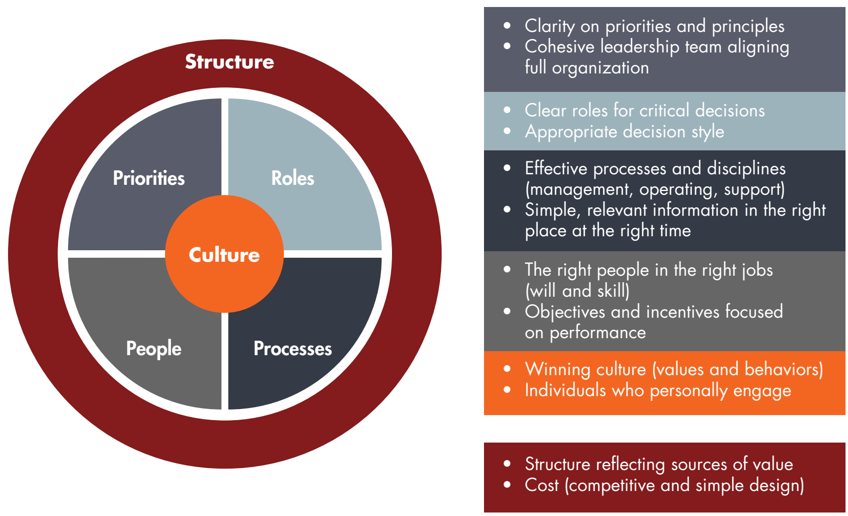
Identifying the Critical Decisions

Every company has its own set of critical decisions. If your business is in relatively good shape, those decisions may not have changed much. Some will be the big choices made by the senior team and the board, such as whether to acquire a competitor or invest in a new product. Others may be decisions made every day on the front line. Toyota, for example, achieved its leading position partly through its reputation for top-of-the-line manufacturing quality. To maintain that quality, Toyota had to ensure that workers in every plant (and in suppliers' plants) knew how to make and execute the right quality-related decisions during the production process. These decisions are no less important now than when Toyota was growing rapidly.

If you're in survival mode, the list of critical decisions will be different. The most important decisions bear on your ability to stay in business, like

FIGURE 1

Strengthen the organization and accelerate the decisions that really matter



whether to sell a stake in the company or overhaul the business model. Everyday decisions relating to cost reduction, cash management, and pricing take on critical importance. So do some of the key decisions made in the past—decisions that may have been right at the time but are now hurting the business. A once-promising acquisition may need to be sold. Compensation systems may need to be revamped and major contracts renegotiated. When survival is at stake, no company can take past decisions for granted.

Once you've identified your critical decisions, you need effective systems for making and executing them. Strong companies make sure that their structure isn't getting in the way. They define clear decision roles and ensure that people with the necessary skills and capabilities are in the roles where they can have the greatest impact.

Testing the Structure

Downturns force many companies to restructure their organizations, by centralizing decision making, for example, or consolidating divisions. Structural change can be distracting and cause upheaval at a time when companies need to be externally focused, so there should be a high bar for such changes. But sometimes structure is a serious obstacle to making and executing a business's critical decisions. In that case, structure has to change.

At Hewlett-Packard, for example, the company's salesforce used to be organized by customer while its manufacturing units were organized by product. It was a classic structural bottleneck: decisions stalled, people worked at cross-purposes, and H-P's performance suffered. The company's leaders responded by shifting to a product-based structure across the entire company, with accountabilities for decisions clearly defined. That created the conditions for better decision making and execution, which in turn generated higher profitability.

A downturn can magnify the need for this kind of structural change. Companies may need to improve accountability and break through decision bottlenecks. Financial pressures can also be a catalyst for adjusting a company's detailed structure. For example, many companies take this opportunity to simplify their organizations, adjusting management layers and spans of control with the goal of increasing both efficiency and effectiveness. Under pressure to improve performance, Intel restructured in 2006, removing two layers of the organization and increasing the span of control for each manager by two or three people. The resulting decrease in cost and complexity was one important factor contributing to improved operating income: Intel's operating income rose 45 percent between 2006 and 2007.

Clarifying Roles and Processes

Whatever a company's structure, decision roles need to be clear and unambiguous. Unless people know who's responsible for making and executing critical decisions, the stress on the organization will only increase. A tool we call RAPID® clarifies accountabilities for each part of these decisions.

RAPID is a loose acronym for the key roles in any major decision. The individual or team responsible for a *recommendation* gathers relevant information and comes up with a proposed course of action. People with *input* responsibilities are consulted about the recommendation. They help shape a recommendation so that it is operationally practical, financially feasible, and so on. An executive who must *agree* is anyone who needs to sign off on the proposal—often a legal or regulatory compliance officer.

Eventually, one person will *decide*. We say that person "has the D." The decision maker needs good business judgment, a grasp of the relevant tradeoffs, and a keen awareness of the organization that will execute the decision. Assigning the D to one individual ensures single-point accountability. The final role in the process involves the people who will *perform* or execute the decision. This is a crucial role to assign, since people with "P" responsibility are not always involved in making the decision.

Clear decision roles are essential in turbulent times: they can boost performance by unclogging bottlenecks and cutting the organization's cycle time. In the last downturn, for instance, the European division of a U.S. telecommunications company was always behind its competitors in submitting bids to customers. The reason: every bid had to be routed through U.S. headquarters for approval. A RAPID analysis helped U.S. executives see that European sales managers could have the D for submissions, enabling the organization to operate faster. In our experience, companies that implement RAPIDs start to use a powerful new vocabulary that reinforces the new way of thinking about decisions. ("Who has the D here?") That, too, helps the organization work faster and more effectively.

For clear decision roles to have their full impact, they must be supported by rigorous decision processes. The people participating in a decision need to be involved at the right time, gather all the facts necessary to evaluate alternatives against well-defined criteria, and commit the resources to follow through.

Putting the Right People in the Right Roles

When times are good, companies tend to focus on how to manage their growing organizations. In a downturn, the logic changes. Companies have to cut costs. Many do so by letting people go, difficult though it may be. But layoffs and attrition create problems of their own. The people who leave are not always the poorest performers. Those who stay may not have the skills and capabilities to make and execute the decisions required by the current environment. And because companies are in cost-reduction mode, they often fail to consider who they might *hire* to bolster their capabilities. Ultimately, individuals must make and execute every critical decision. And no company in a recession can afford to have the wrong people in key decision roles.

Here, too, a downturn is an opportunity to improve the caliber of the organization. Veteran managers, for instance, are sometimes prisoners of their experience and unable to cope with the requirements of a new situation. People coming in from other companies or even other industries can shed new light on strategic and operational challenges. Even without new blood from the outside, companies often can strengthen an organization by moving people to roles where they have the most impact. At one technology company, we found that more than 40 percent of managers identified as high performers were in positions deemed non-critical. Meanwhile, fewer than 40 percent of the company's mission-critical roles were occupied by top performers. The senior team acted quickly to correct the mismatch, and the performance of the business started to improve immediately.

The key to making the best possible use of people is a robust, effective performance-management system. Most companies already have the elements of performance management in place, and some parts of the process may be first-rate. But many suffer from problems such as grade inflation. One mining company, for instance, rated fully 80 percent of its people as above average, even though the company had been underperforming for years. The system also needs to carry real consequences. If differences in evaluation actually lead to differences in outcomes such as career opportunities, mentoring and coaching, compensation, retention efforts, then line managers (and everyone else) will take the evaluations seriously. At the mining company, senior executives tightened up the rating process and made the consequences of ratings more explicit. High performers received increases in pay along with better career development and training opportunities and better retention packages. Those with lower ratings received coaching and eventual outplacement if necessary. The system finally had teeth—and leaders throughout the organization could accurately gauge the quality of the people available and put their top talent in positions that mattered most to the success of the business.

Actively Managing the Culture

Culture underpins the decisions an organization makes and executes. It defines "the way we do things around here." As one observer said, it determines how people act when no one is looking. But cultures can change over time and are particularly susceptible to change when the organization is in crisis. In an acute downturn, leaders need to take deliberate action to keep a strong culture from deteriorating—or to transform a culture that gets in the way of good decisions.

Understanding that its culture is a competitive advantage, Southwest Airlines makes a point of reinforcing its culture in hard times. The airline is committed to the highest quality of customer service and to providing employees with a stable working environment. In the early stages of the 2008 recession, it made decisions consistent with these principles, investing in upgrading its customer service (for example, its Business Select fare for frequent travelers) and in maintaining staff loyalty (through no involuntary job cuts). Committed to these priorities and aided by a shrewd fuel-hedging strategy, Southwest had the highest net income of all U.S. carriers in the first half of 2008.

No company can avoid difficult choices in a recession, but its leaders can handle those choices in ways that are consistent with the culture. In this vein, it's not only what decisions are made but how they are made and communicated that matters. Zappos, the Internet shoe retailer known for its people-oriented culture, recently laid off some of its employees—but it provided them with generous severance packages and six months' worth of health insurance. The CEO explained the rationale behind the layoffs to employees and customers in his blog. "While layoffs are difficult for all parties," one commenter wrote, "I totally respect how you are treating your employees and how you are being transparent about the process."

Changing a dysfunctional culture may be harder, but it is even more urgent. If Detroit's auto companies and some of the big financial services firms are to emerge from the recession as healthy organizations, they will need to develop new values, norms, and behaviors. Any turnaround team jumping into these organizations would focus as much on culture and other organizational matters as on "hard" issues like finance and strategy.

Making the Most of the Crisis

A strong organization isn't optional, something to worry about when the crisis is over. The strength of your organization will greatly affect how well your company can weather the storm. It will greatly affect your chances for growth when the storm passes. Strong organizations identify and focus on their critical decisions—the ones they must make and execute well if they are to succeed. They ensure that their structure and decision roles and processes are set up to facilitate those decisions. They have measures and incentives that make sure people are working toward the right goals. They put the people who can best make and execute those decisions in the right place—even if they have to go out and hire those people.

They also take a good, hard look at their culture, reinforcing the strengths and addressing the weaknesses. And they know that the downturn provides opportunities for change that won't last forever. As somebody in Washington said recently, "A crisis is a terrible thing to waste."