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Putting people first for organizational success*

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Executive Overview

There's a disturbing disconnect in organizational management. Research, experience, and common sense all increasingly point to a direct relationship between a company's financial success and its commitment to management practices that treat people as assets. Yet trends in management practice are actually moving away from these very principles. Why is common sense so remarkably uncommon when it comes to managing people? Why do organizations habitually overlook readily available opportunities to boost their financial performance? Drawing on extensive empirical research, an irrefutable business case can be made that the culture and capabilities of an organization—derived from the way it manages its people—are the real and enduring sources of competitive advantage. Managers today must begin to take seriously the often heard, yet frequently ignored, adage that "people are our most important asset."

Over the past decade or so, numerous rigorous studies conducted both within specific industries and in samples of organizations that cross industries have demonstrated the enormous economic returns obtained through the implementation of what are variously called high involvement, high performance, or high commitment management practices. Furthermore, much of this research serves to validate earlier writing on participative management and employee involvement. But even as these research results pile up, trends in actual management practice are, in many instances, moving in a direction exactly opposite to what this growing body of evidence prescribes. Moreover, this disjuncture between knowledge and management practice is occurring at the same time that organizations, confronted with a very competitive environment, are frantically looking for some magic elixir that will provide sustained success, at least over some reasonable period of time.

Rather than putting their people first, numerous firms have sought solutions to competitive challenges in places and means that have not been very productive—treating their businesses as portfolios of assets to be bought and sold in an effort to find the right competitive niche, downsizing and outsourcing in a futile attempt to shrink or transact their way to profit, and doing a myriad other things that weaken or destroy their organizational culture in efforts to minimize labor costs.

Show Me the Evidence

Though we could go on at length about a company like Apple as a case in point (see "The Apple Story"), executives frequently say, "don't just give me anecdotes specifically selected to make some point. Show me the evidence!" Fortunately, there is a substantial and rapidly expanding body of evidence, some of it quite methodologically sophisticated, that speaks to the strong connection between how firms manage their people and the economic results achieved. This evidence is drawn from studies of the five-year survival rates of initial public offerings; studies of profitability and stock price in large samples of companies from multiple industries; and detailed research on the automobile, apparel, semiconductor, steel manufacturing, oil refining, and service industries. It shows that substantial gains, on the order of 40 percent, can be obtained by implementing high performance management practices.[1]

According to an award-winning study of the high performance work practices of 968 firms representing all major industries, "a one standard deviation increase in use of such practices is associated with

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The Apple Story

Most accounts of Apple Computer's history have stressed either strategic mistakes, such as not licensing the Macintosh operating system, or leadership issues, such as the succession to CEO by John Sculley and others. However, the Apple story also illustrates rather poignantly the negative case of what happens when a firm whose success derives fundamentally from its people fails to put people first.

Apple was founded in 1976 by Stephen Wozniak and Stephen Jobs in Jobs's garage. Their vision was to bring the power of the computer to the individual user. The Macintosh operating system, introduced in 1984, was (and many would maintain, still is) a leading technology in terms of ease of use. Apple launched the desktop publishing movement, and the company's emphasis on networks and connectivity among machines was also ahead of its time.

Apple was a company largely built on a unique culture. The Macintosh design team worked in a separate building with a pirate flag flying over it. The company built a cult-like commitment among its employees. People were recruited to Apple with the idea that they would be helping to change the world. Apple was more than a company; it was a cause. Its strategy of being an innovator in designing user-friendly personal computers that would make people more productive required a highly talented, creative, and innovative work force. When it took actions that resulted in the loss of that work force, its ability to implement its business strategy and to regain market leadership was irreparably harmed.

Not all of Apple's problems can be traced to how it handled its people. Even though its competitive advantage lay in its operating system, employing a mouse and a graphical user interface, the company consistently failed to license the operating system to other manufacturers, thereby limiting its share of the personal computer market. Because its culture emphasized technological innovation, Apple would occasionally introduce products, such as the Newton personal digital assistant that were either far ahead of their time or had some remaining hardware or software bugs, or both, thus occasionally suffering commercial flops. But, a case can be made that its handling of its people made both its technical and market problems and its recovery from them much worse.

In the beginning, the *Apple Employee Handbook* espoused the importance of people to the firm's success and spelled out many of the company's cherished cultural traditions, such as management accessibility and open communication, mementos of significant company events, celebrations of important life events of employees, and bagels and cream cheese on Friday mornings. After John Sculley laid off 20 percent of its work force to cut costs when sales did not meet expectations in 1985, Apple maintained that its responsibility to its employees was not to give them any security or a career with a progression of jobs, but rather simply to provide a series of challenging job assignments that would permit them to learn and develop so as to be readily employable. In a booming local job market, this encouraged people to develop talent and skills at Apple and then to use them elsewhere. Apple's shift in emphasis to an individualistic culture could also be seen in the language used to talk about employees, who were characterized as A, B, or C players. Apple wanted to attract and retain more As and get rid of the Cs.

In 1991, about 10 percent of the work force was laid off. In 1993, Michael Spindler replaced Sculley and continued the cost cutting by laying off 2,500 people, about 14 percent of the work force. In 1997, another round of layoffs affected almost a third of the remaining people. More damaging than the layoffs themselves was the way they occurred in waves over time, making people unsure of their futures and tempting the best people to leave. Salaries, which had been excellent to attract the best people, were cut, as were many of the amenities that had made working at the company special. Because they feared losing jobs when a project was over, many people slowed their progress substantially. The loss of key technical and marketing personnel made the firm's prospects even worse.

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The pathologies of Apple Computer are all too common. A company initially having problems with its profits, costs, or share price, takes quick action to raise profits and lower costs. Since employee costs are typically the most quickly and easily changed, the following actions are common: training is curtailed; pay may be frozen or cut; promotions are held up; the use of part-time or temporary help increases; and people are laid off or forced to work reduced hours. These measures logically and inevitably reduce motivation, satisfaction, and loyalty to the company. Rather than focus on their jobs, employees spend time discussing rumors and sharing complaints with coworkers. Cutting training cuts skill and knowledge development and dissemination. Attention focused on unhappiness at work can create a climate in which accidents and poor customer service flourish. Poor service, high accident rates, and increased turnover and absenteeism adversely affect sales, profits, and costs. So the cycle continues.

In the short run, some firms may be able to cut costs and thereby increase profits. In some cases, cuts can be made in ways that do not damage the viability of the organization. And, of course, Apple's obituary has yet to be written. While employees admit that Apple was in a death spiral, the recent return of Stephen Jobs and Apple's introduction of the iMac suggest to some that a rebirth is possible.

Indeed, as Stephen Jobs told *Fortune*,[a] "Innovation has nothing to do with how many R&D dollars you have . . . . It's not about money. It's about the people you have, how you're led, and how much you get it."

[a]Kirkpatrick, D. 1998. The second coming of Apple. *Fortune*, 138:90.

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a . . . 7.05 percent decrease in turnover and, on a per employee basis, $27,044 more in sales and $18,641 and $3,814 more in market value and profits, respectively."[2] Yes, you read those results correctly. That's an $18,000 increase in stock market value *per employee*! A subsequent study conducted on 702 firms in 1996 found even larger economic benefits: "A one standard deviation improvement in the human resources system was associated with an increase in shareholder wealth of $41,000 per employee"[3]—about a 14 percent market value premium.

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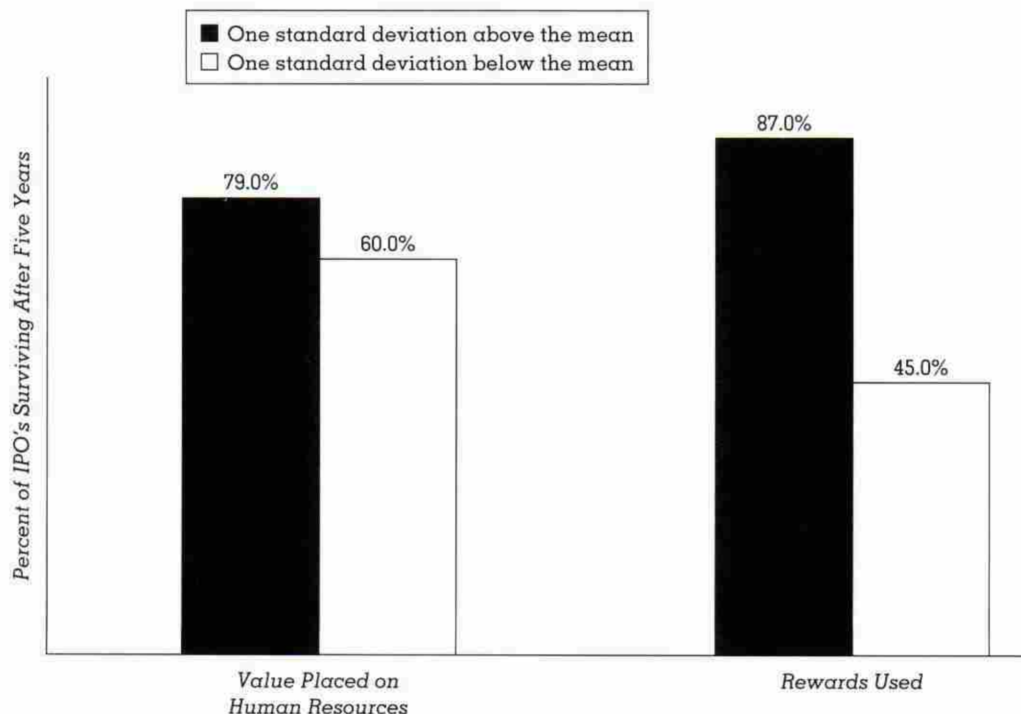
Are these results unique to firms operating in the United States? No. Similar results were obtained in a study of more than one hundred German companies operating in ten industrial sectors. The study found "a strong link between investing in employees and stock market performance. Companies which place workers at the core of their strategies produce higher long-term returns to shareholders than their industry peers."[4]

One of the clearest demonstrations of the causal effect of management practices on performance comes from a study of the five-year survival rate of 136 non-financial companies that initiated their public offering in the U.S. stock market in 1988.[5] By 1993, some five years later, only 60 percent of these companies were still in existence. The empirical analysis demonstrated that with other factors such as size, industry, and even profits statistically controlled, both the value the firm placed on human resources—such as whether the company cited employees as a source of competitive advantage—and how the organization rewarded people—such as stock options for all employees and profit sharing—were significantly related to the probability of survival. Moreover, the results were substantively important. As shown in Figure 1, the difference in survival probability for firms one standard deviation above and one standard deviation below the mean (in the upper 16 percent and the lower 16 percent of all firms in the sample) on valuing human resource was almost 20 percent. The difference in survival depending on where the firm scored on rewards was even more dramatic, with a difference in five-year survival probability of 42



Source: Based on information from Theresa Welbourne and Alice Andrews, 1996, "Predicting Performance of Initial Public Offering Firms: Should HRM Be in the Equation?" *Academy of Management Journal*, 39: 910–911.

FIGURE 1
Probability of an Initial Public Offering Firm's Surviving Five Years

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percent between firms in the upper and lower tails of the distribution.

How can such substantial benefits in profits, quality, and productivity occur? Essentially, these tremendous gains come about because high performance management practices provide a number of important sources for enhanced organizational performance. Simply put, people work harder because of the increased involvement and commitment that comes from having more control and say in their work; people work smarter because they are encouraged to build skills and competence; and people work more responsibly because more responsibility is placed in hands of employees farther down in the organization. These practices work not because of some mystical process, but because they are grounded in sound social science principles that have been shown to be effective by a great deal of evidence. And, they make sense.

Seven Practices of Successful Organizations

Based on these various studies, related literature, and personal observation and experience, a set of seven dimensions emerge that seem to characterize most, if not all, of the systems producing profits through people emerge. Let's take a look at each one briefly.

Employment Security

Most research on the effects of high performance management systems has incorporated employment security as an important dimension. Indeed, "one of the most widely accepted propositions . . . is that innovations in work practices or other forms of worker-management cooperation or productivity improvement are not likely to be sustained over time when workers fear that by increasing productivity they will work themselves out of their jobs."[6]

The idea of providing employment security in today's competitive world seems somehow anachronistic or impossible and very much at odds with what most firms seem to be doing. But employment security is fundamental to the implementation of most other high performance management practices. For example, when General Motors wanted to implement new work arrangements in its innovative Saturn plant in the 1990s, it guaranteed its people job security except in the most extreme circumstances. When New United Motors Manufacturing, Inc. (NUMMI) was formed to operate the Fremont automobile assembly plant, it offered its people job security. How else could it ask for flexibility and cooperation in becoming more efficient and productive?

Many additional benefits follow from employment assurances besides workers' free contribution of knowledge and their efforts to enhance productivity. One advantage to firms is the decreased likelihood that they will lay off employees during downturns. How is this a benefit to the firm? In the absence of some way of building commitment to retaining the work force—either through pledges about employment security or through employment obligations contractually negotiated with a union—firms may lay off employees too quickly and too readily at the first sign of financial difficulty. This constitutes a cost for firms that have done a good job selecting, training, and developing their work force, because layoffs put important strategic assets on the street for the competition to employ. Herb Kelleher, the CEO of Southwest Airlines, summarized this argument best when he wrote:

> Our most important tools for building employee partnership are job security and a stimulating work environment . . . Certainly there were times when we could have made substantially more profits in the short-term if we had furloughed people, but we didn't. We were looking at our employees' and our company's longer-term interests . . . [A]s it turns out, providing job security imposes additional discipline, because if your goal is to avoid layoffs, then you hire very sparingly. So our commitment to job security has actually helped us keep our labor force smaller and more productive than our competitors'.[7]

Selective Hiring

Companies serious about obtaining profits through people will expend the effort needed to ensure that they recruit the right people in the first place. This requires several things. First, the organization needs to have a large applicant pool from which to select. In 1993, for example, Southwest Airlines received about 98,000 job applications, interviewed 16,000 people, and hired 2,700. In 1994, applications increased to more than 125,000 for 4,000 hires. Some organizations see processing this many job inquiries as an unnecessary expense. Southwest sees it as a necessary first step.

Second, the organization needs to be clear about what are the most critical skills and attributes needed in its applicant pool. At Southwest, applicants for flight attendant positions are evaluated on the basis of initiative, judgment, adaptability,

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and their ability to learn. These attributes are assessed in part from interview questions that evoke specific instances of these attributes. For instance, to assess adaptability, interviewers ask, "Give an example of working with a difficult co-worker. How did you handle it?"[8] To measure initiative, one question asks, "Describe a time when a co-worker failed to pull their weight and what you did about it."

Third, the skills and abilities sought need to be carefully considered and consistent with the particular job requirements and the organization's approach to its market. Enterprise Rent-A-Car is today the largest car rental company in the United States, and it has expanded at a rate of between 25 and 30 percent a year for the past 11 years. It has grown by pursuing a high customer service strategy and emphasizing sales of rental car services to repair garage customers. In a low-wage, often unionized, and seemingly low-employee-skill industry, virtually all of Enterprise's people are college graduates. But these people are hired primarily for their sales skills and personality and for their willingness to provide good service, not for their academic performance. Brian O'Reilly interpolates Enterprise's reasoning:

> The social directors make good sales people, able to chat up service managers and calm down someone who has just been in a car wreck . . . The Enterprise employees hired from the caboose end of the class have something else going for them . . . a chilling realization of how unforgiving the job market can be.[9]

Fourth, organizations should screen primarily on important attributes that are difficult to change through training and should emphasize qualities that actually differentiate among those in the applicant pool. Southwest rejected a top pilot from another airline who did stunt work for movie studios because he was rude to a receptionist. Southwest believes that technical skills are easier to acquire than a teamwork and service attitude. Ironically, many firms select for specific, job-relevant skills that, while important, are easily acquired. Meanwhile, they fail to find people with the right attitudes, values, and cultural fit—attributes that are harder to train or change and that are quite predictive of turnover and performance.

One MBA job applicant reported that interviewers at PeopleSoft, a producer of human resource management software, asked very little about personal or academic background, except about learning experiences from school and work. Rather, the interviews focused mostly on whether she saw herself as team-oriented or as an individual achiever, what she liked to do outside school and work, and her philosophy on life. The specific question was "Do you have a personal mission statement? If you don't, what would it be if you were to write it today?" Moreover, the people interviewing the applicant presented a consistent picture of the values that were shared among employees at PeopleSoft. Such a selection process is more likely to produce cultural fit. A great deal of research evidence shows that the degree of cultural fit and value congruence between job applicants and their organizations significantly predicts both subsequent turnover and job performance.[10]

Self-Managed Teams and Decentralization as Basic Elements of Organizational Design

Numerous articles and case examples, as well as rigorous, systematic studies, attest to the effectiveness of teams as a principle of organization design. For example, Honeywell's defense avionics plant credits improved on-time delivery—reaching 99 percent in the first quarter of 1996 as compared with below 40 percent in the late 1980s—to the implementation of teams.[11] Perhaps one of the greatest payoffs from team-based organizations is that teams substitute peer-based control for hierarchical control of work. Team-based organizations also are largely successful in having all of the people in the firm feel accountable and responsible for the operation and success of the enterprise, not just a few people in senior management positions. This increased sense of responsibility stimulates more initiative and effort on the part of everyone involved. In addition, and perhaps most importantly, by substituting peer for hierarchical control, teams permit removal of layers of hierarchy and absorption of administrative tasks previously performed by specialists, avoiding the enormous costs of having people whose sole job it is to watch people who watch other people do the work.

Perhaps one of the greatest payoffs from team-based organizations is that teams substitute peer-based control for hierarchical control of work.

The tremendously successful natural foods grocery store chain, Whole Foods Markets, organized on the basis of teams, attributes much of its success to that arrangement. Between 1991 and 1996,

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the company enjoyed sales growth of 864 percent and net income growth of 438 percent as it expanded, in part through acquisitions as well as through internal growth, from 10 to 68 stores. In its 1995 annual report, the company's team-oriented philosophy is clearly stated.

> Our growing information systems capability is fully aligned with our goal of creating a more intelligent organization—one which is less bureaucratic, elitist, hierarchical, and authoritarian and more communicative, participatory, and empowered. The ultimate goal is to have all team members contributing their full intelligence, creativity, and skills to continuously improving the company . . . Everyone who works at Whole Foods Market is a team member. This reflects our philosophy that we are all partners in the shared mission of giving our customers the very best in products and services. We invest in and believe in the collective wisdom of our team members. The stores are organized into self-managing work teams that are responsible and accountable for their own performance.[12]

Teams also permit employees to pool their ideas to come up with better and more creative solutions to problems. Teams at Saturn and at the Chrysler Corporation's Jefferson North plant, for example, "provide a framework in which workers more readily help one another and more freely share their production knowledge—the innumerable 'tricks of the trade' that are vital in any manufacturing process."[13]

Team-based organizations are not simply a made-only-in-America phenomenon. Consider, for example, Vancom Zuid-Limburg, a joint venture in the Netherlands that operates a public bus company. This company has enjoyed very rapid growth in ridership and has been able to win transport concessions by offering more services at the same price as its competitors. The key to this success lies in its use of self-managed teams and the consequent savings in management overhead.

> Vancom is able to [win transport contracts] mainly because of its very low overhead costs . . . [O]ne manager supervises around forty bus drivers . . . This management-driver ratio of 1 in 40 substantially differs from the norm in this sector. At best, competitors achieve a ratio of 1 in 8. Most of this difference can be attributed to the self-managed teams. Vancom . . . has two teams of around twenty drivers. Each team has its own bus lines and budgeting responsibilities . . . Vancom also expects each individual driver to assume more responsibilities when on the road. This includes customer service (e.g., helping elderly persons board the bus), identifying problems (e.g., reporting damage to a bus stop), and active contributions (e.g., making suggestions for improvement of the services).[14]

Comparatively High Compensation Contingent on Organizational Performance

It is often argued that high compensation is a consequence of organizational success, rather than its progenitor, and that high compensation (compared with the average) is possible only in certain industries that either face less competition or have particularly highly educated employees. But neither of these statements is correct. Obviously, successful firms can afford to pay more, and frequently do so, but high pay can also produce economic success.

When John Whitney assumed the leadership of Pathmark, a large grocery store chain in the eastern United States in 1972, the company had about 90 days to live, according to its banks, and was in desperate financial shape. Whitney looked at the situation and discovered that 120 store managers in the chain were paid terribly. Many of them made less than the butchers, who were unionized. He decided that the store managers were vital to the chain's success and its ability to accomplish a turnaround. Consequently, he gave the store managers a substantial raise—about 40 to 50 percent. Whitney attributes the subsequent success of the chain to the store managers' focusing on improving performance instead of worrying and complaining about their pay.

The idea that only certain jobs or industries can or should pay high wages is belied by the example of many firms. Home Depot has been successful and profitable, and its stock price has shown exceptional returns. Even though the chain emphasizes everyday low pricing as an important part of its business strategy and operates in a highly competitive environment, it pays its staff comparatively well for the retail industry, hires more experienced people with building industry experience, and expects its sales associates to provide a higher level of individual customer service.

Contingent compensation also figures importantly in most high performance work systems. Such compensation can take a number of different forms, including gain sharing, profit sharing, stock ownership, pay for skill, or various forms of individual or team incentives. Wal-Mart, AES Corporation, Southwest Airlines, Whole Foods Markets, Mi-

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crosoft, and many other successful organizations encourage share ownership. When employees are owners, they act and think like owners. However, little evidence suggests that employee ownership, by itself, affects organizational performance. Rather, employee ownership works best as part of a broader philosophy or culture that incorporates other practices. Merely putting in ownership schemes without providing training, information sharing, and delegation of responsibility will have little effect on performance. Even if people are more motivated by their share ownership, they don't necessarily have the skills, information, or power to do anything with that motivation.

Extensive Training

Training is often seen as a frill in many U.S. organizations, something to be reduced to make profit goals in times of economic stringency. Studies of firms in the United States and the United Kingdom consistently provide evidence of inadequate levels of training and training focused on the wrong things: specialist skills rather than generalist competence and organizational culture. This is the case in a world in which we are constantly told that knowledge and intellectual capital are critical for success. Knowledge and skill *are* critical—and too few organizations act on this insight. Training is an essential component of high performance work systems because these systems rely on frontline employee skill and initiative to identify and resolve problems, to initiate changes in work methods, and to take responsibility for quality. All of this requires a skilled and motivated work force that has the knowledge and capability to perform the requisite tasks.

Training is an essential component of high performance work systems because these systems rely on frontline employee skill and initiative to identify and resolve problems, to initiate changes in work methods, and to take responsibility for quality.

Training can be a source of competitive advantage in numerous industries for firms with the wisdom to use it. The Men's Wearhouse, an off-price specialty retailer of men's tailored business attire and accessories, went public in 1991. Its 1995 annual report noted that it had achieved compounded annual growth rates in revenues and net earnings of 32 and 41 percent, respectively, and that the value of its stock had increased by approximately 400 percent. The company attributes its success to how it treats its people and particularly to the emphasis it has placed on training, an approach that separates it from many of its competitors. The company built a 35,000 square foot training center in Fremont, California, its headquarters. In 1994, some 600 "clothing consultants" went through Suits University, and that year the company added Suits High and Selling Accessories U.[15] During the winter, experienced store personnel come back to headquarters in groups of about 30 for a three- or four-day retraining program.

While training is an investment in the organization's staff, in the current business milieu it virtually begs for some sort of return-on-investment calculations. But such analyses are difficult, if not impossible, to carry out. Successful firms that emphasize training do so almost as a matter of faith and because of their belief in the connection between people and profits. Even Motorola does a poor job of measuring its return on training. Although the company has been mentioned as reporting a $3 return for every $1 invested in training, an official from Motorola's training group said that she did not know where these numbers came from and that the company is notoriously poor at evaluating its $170 million investment in training. The firm mandates forty hours of training per employee per year, and believes that the effects of training are both difficult to measure and expensive to evaluate. Training is part and parcel of an overall management process and is evaluated in that light.

Reduction of Status Differences

The fundamental premise of high performance management systems is that organizations perform at a higher level when they are able to tap the ideas, skill, and effort of all of their people. In order to help make all organizational members feel important and committed, most high commitment management systems attempt to reduce the status distinctions that separate individuals and groups and cause some to feel less valued. This is accomplished in two principle ways—symbolically, through the use of language and labels, physical space, and dress, and substantively, in the reduction of the organization's degree of wage inequality, particularly across levels.

At NUMMI, everyone wears the same colored smock; executive dining rooms and reserved parking don't exist. At Kingston Technology, a private firm manufacturing add-on memory modules for personal computers, the two cofounders sit in open

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cubicles and do not have private secretaries.[16] Status differences are also reduced, and a sense of common fate developed, by limiting the difference in compensation between senior management and other employees. Herb Kelleher, who earns about $500,000 per year as the CEO of Southwest, including base and bonus, has been on the cover of *Fortune* magazine with the headline, "Is he America's best CEO?" In 1995, when Southwest negotiated a five-year wage freeze with its pilots in exchange for stock options and occasional profitability bonuses, Kelleher agreed to freeze his base salary at $395,000 for four years. Sam Walton, the founder and chairman of Wal-Mart, was one of the most underpaid CEOs in the U.S. Kelleher and Walton weren't poor; each owned stock in his company. But stock ownership was also encouraged for their employees. Having an executive's fortune rise and fall together with those of the other employees differs dramatically from providing large bonuses and substantial salaries for executives even as the stock price languishes and people are being laid off.

Sharing Information

Information sharing is an essential component of high performance work systems. The sharing of information on such things as financial performance, strategy, and operational measures conveys to the organization's people that they are trusted. John Mackey, the chief executive of Whole Foods Markets, states, "If you're trying to create a high-trust organization, . . . an organization where people are all-for-one and one-for-all, you can't have secrets."[17] Whole Foods shares detailed financial and performance information with every employee, including individual salary information. Every Whole Foods store has a book that lists the previous year's salary and bonus of all 6,500 employees.[18]

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Even motivated and trained people cannot contribute to enhancing organizational performance if they don't have information on important dimensions of performance and training on how to use and interpret that information. The now famous case of Springfield ReManufacturing Corporation (SRC) illustrates this point. On February 1, 1983, SRC was created when the plant's management and employees purchased an old International Harvester plant in a financial transaction that consisted of about $100,000 in equity and $8.9 million in debt, an 89-1 debt to equity ratio that has to make this one of the most leveraged of all buyouts. Jack Stack, the former plant manager and now chief executive, knew that if the plant was to succeed, all employees had to do their best, and had to share all their wisdom and ideas for enhancing the plant's performance. Stack came up with a system called "open-book management," that has become so popular that SRC now makes money by running seminars on it. When General Motors canceled an order in 1986 that represented about 40 percent of Springfield's business for the coming year, the firm averted a layoff by providing its people with information on what had happened and letting them figure out how to grow the company and achieve the productivity improvements that would obviate layoffs. SRC has since enjoyed tremendous financial success. In 1983, its first year of operation, sales were about $13 million. By 1992, sales had increased to $70 million and the number of employees had grown from 119 to 700. The original equity investment of $100,000 was worth more than $23 million by 1993. No one who knows the company, and certainly not Jack Stack or the other managers, believes this economic performance could have been achieved without a set of practices that enlisted the cooperation and ingenuity of all of the firm's people. The system and philosophy of open-book management took a failing International Harvester plant and transformed it into a highly successful, growing business.

It All Seems So Easy

How difficult can it be to increase the level of training, to share information and plans with people, to reorganize work into teams, to upgrade hiring practices, and to do all the other things described above? It is easy to form the ideas that are the foundation for people-centered management. But, if it were actually easy to implement those ideas, other airlines would have been able to copy Southwest, other grocery stores would be as successful as Whole Foods Markets, other power producers would be as profitable and efficient as AES, other retailers would have achieved the same record of growth and profitability as the Men's Wearhouse. Implementing these ideas in a systematic, consistent fashion remains rare enough to be an important source of competitive advantage for firms in a number of industries. Why is this so?

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Managers Are Enslaved By Short-Term Pressures

Because achieving profits through people takes time to accomplish, an emphasis on short-term financial results will not be helpful in getting organizations to do the right thing. Short-term financial pressures and measurements abound. Many organizations provide raises and bonuses based on annual results. Ask senior managers how long it takes to change an organization's culture, and it's extremely unlikely that you will hear, "a year or less." But that is the time horizon of the evaluation process. Taking actions with payoffs that will occur beyond the time for which you will be measured on your performance is difficult and risky.

A second pressure occurs when organizations seek to create shareholder value by increasing stock price. The time horizon for evaluating stock market returns is again often quite short, often a year or less. Mutual fund and other institutional money managers are themselves frequently evaluated on a quarterly or at most an annual basis; they often invest in stocks for only a short time and have high portfolio turnover, so it is little surprise that they, in turn, put pressure on organizations for short-term, quick results.

A third pressure is that the immediate drives out the long-term. Today's pressing problems make it difficult to focus on actions aimed at building a better organization for the future. Managerial career processes contribute to this short-term pressure. When and where managers are hired for an indefinite period and careers are embedded in a single organization, it makes sense for those individuals to take a long-term view. But movements by managers across organizations have increased dramatically at nearly all organizational levels. Individuals trying to build a track record that will look good on the external labor market aren't likely to take a longer-term view of building organizational competence and capabilities. Stephen Smith has argued that the typical career system facing managers today encourages "managerial opportunism." He suggests that "managers are rewarded . . . for appropriating the ideas of their subordinates or for improving the bottom line in the short run and then moving on to other positions before the long-term implications of the strategies they have adopted make themselves felt."[19]

Organizations Tend to Destroy Competence

Organizations often inadvertently destroy wisdom and competence or make it impossible for wisdom, knowledge, and experience to benefit the firm. Management practices that require programs and ideas to be explained and reviewed in groups are a major culprit.

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That formal planning and evaluation, and particularly the use of financial criteria, destroy competence is consistent with the results of research on innovation. Experts on organizational management have acquired the ability to see and understand things that are not evident to novices. An expert advertising executive moves quickly and creatively to come up with a good advertising campaign; an expert in production management understands the dynamics of both the human and mechanical elements of the production system and can accurately and quickly diagnose problems and figure out appropriate action; an expert in management or leadership has a good grasp of the principles of human motivation, great intuition, and the ability to read people and situations. But in any domain of expertise, by definition, some portion of the expert's knowledge and competence must be tacit, not readily articulated or explainable, irreducible to a formula or recipe. If that were not the case, then the expert knowledge would be codified and novices could do about as well as experts at the task in question, given access to the same formulas or insights.

But if expert knowledge has a substantial component of tacit knowledge, it will be impossible for experts to present the real basis of their judgments and decisions. Experts are more likely to rely on those factors and evidence that are available and accessible to all. In so doing, they lose virtually all the benefits of their expertise. Forced to explain decisions to a wider audience, the experts will have to rely on the same data and decision processes as anyone else. Thus, the organization will have created a decision process in which its experts behave like novices, and will have lost the benefits of the experts' wisdom and competence.

Consider the following example. Bob Scott, associate director of the Center for Advanced Study in the Behavioral Sciences at Stanford, had to give a talk about the Center's management to an outside group interested in establishing an interdisciplinary, social-science research center. As he was giving the talk, he recalled thinking, "If we

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actually managed the center this way, it would be a disaster." It was not possible for him to articulate his expertise, to explain his tacit knowledge. Suppose that instead of a group of curious outsiders, his audience had been a governing board or oversight body that would hold Scott and his colleagues accountable for following and implementing the ideas he expressed? They might have been forced to manage in ways that could seriously degrade the organization's operations.

Managers Don't Delegate Enough

Relying on the tacit knowledge and expertise of others requires trust and the willingness to let them do what they know how to do. Using self-managing teams as an organizing principle requires permitting the teams to actually manage themselves. At NUMMI, teams were given real responsibility and were listened to, while at the General Motors Van Nuys, California, plant, a culture of hierarchical control meant that team members were frequently told to be quiet and supervisors exercised the same control they had before the institution of teams.

Even though employee participation is associated with enhanced economic performance, organizations frequently fail to introduce it, and it remains fragile even when it is implemented. At least some of this resistance derives from two social psychological processes: first, belief in the efficacy of leadership, that is, the "faith in supervision" effect; and second, a self-enhancement bias. The faith in supervision effect means that observers tend to believe that the greater the degree of supervisor involvement and control, the better the work produced. In one study, for instance, identical company performance was evaluated more positively when the leadership factors accounting for the performance were made more apparent.[20] The self-enhancement bias is a pervasive social psychological phenomenon. Researchers have found that "one of the most widely documented effects in social psychology is the preference of most people to see themselves in a self-enhancing fashion. As a consequence, they regard themselves as more intelligent, skilled, ethical, honest, persistent, original, friendly, reliable, attractive, and fair-minded than their peers or the average person . . . On the job, approximately 90 percent of managers and workers rate their performances as superior to their peers."[21] It is no wonder then that such a bias would lead supervisors to evaluate more positively the work they have been involved in creating.

Both of these processes contribute to the same prediction: work performed under more oversight and control will be perceived as better than the identical work performed with less oversight. This effect will be particularly strong for the person doing the supervision. In a real work setting, these social psychological processes would, of course, be counterbalanced by pressures to achieve results and by the knowledge that participation and empowerment may be helpful in improving performance. Nonetheless, these beliefs may be significant factors hindering the use of high performance work practices and the participation and delegation they imply.

Perverse Norms About What Constitutes Good Management

Two norms about what constitutes good management are simultaneously growing in acceptance and are enormously perverse in their implications. The first is the idea that good managers are mean or tough, able to make such difficult choices as laying off thousands of people and acting decisively. The second is that good management is mostly a matter of good analysis, a confusion between math and management. The two views are actually related, since an emphasis on analysis takes one away from such issues as motivation, commitment, and morale, and makes it more likely that one can and will act in a tough fashion.

An article in *Newsweek* stated that "firing people has gotten to be trendy in corporate America . . . Now you fire workers—especially white collar workers—to make your corporate bones . . . Wall Street and Big Business have been in perfect harmony about how in-your-face capitalism is making America great."[22] *Fortune* magazine regularly runs an article entitled "America's Toughest Bosses." Does one want to appear on that list, especially since many of those on it do not last very long in their jobs, having been "fired—in part, for being too mean"?[23] Little evidence exists that being a mean or tough boss is necessarily associated with business success. "Financial results from these bosses' companies vary from superb to pathetic. The median return on shareholder's equity over the past five years for seven of the ten companies for which data are available ranged from 7.3 percent . . . to 18.1 percent . . . That com-

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pares with the median for the *Fortune* 500 of 13.8 percent."[24] Nonetheless, *Fortune* predicts that "toughness . . . will probably become more prevalent. Most nominees for this list rose to prominence in industries shaken by rapid change . . . As global competition heats up and turmoil rocks more industries, tough management should spread. So look for more bosses who are steely, super demanding, unrelenting, sometimes abusive, sometimes unreasonable, impatient, driven, stubborn, and combative."[25]

The belief that the good manager is a skilled analyst also has questionable merit and validity. The belief first arose after World War II with the emergence of Robert McNamara and systems analysis in the Defense Department. It spread to operations research and mathematical analysis in such business schools as Carnegie Mellon and such businesses as the Ford Motor Company. The emphasis on mathematical elegance and analysis as cornerstones for effective management implicitly derogates the importance of emotion, leadership, and building a vision. It represents an attempt to substitute data and analytical methods for judgment and common sense. Emphasizing analytical skills over interpersonal, negotiating, political, and leadership skills inevitably leads to errors in selection, development, and emphasis on what is important to an organization.

A One-in-Eight Chance

Firms often attempt piecemeal innovations. It is difficult enough to change some aspect of the compensation system without having to also be concerned about training, recruitment and selection, and how work is organized. Implementing practices in isolation may not have much effect, however, and, can actually be counterproductive. Increasing the firm's commitment to training activities won't accomplish much unless changes in work organization permit these more skilled people to actually implement their knowledge. If wages are comparatively low and incentives are lacking, the better-trained people may simply depart for the competition. Employment security can be counterproductive unless the firm hires people who fit the culture and unless incentives reward outstanding performance. Implementing work teams will not accomplish much unless the teams receive training in specific technical skills and team processes, and are given financial and operating performance goals and information.

Implementing and seeing results from many of these practices takes time. It takes time to train and upgrade workers' skills and even more time to see the economic benefits of this training in reduced turnover and enhanced performance. It takes time to share operating and financial information with people, and to be sure that they understand and know how to use it. Even more time is needed before suggestions and insights can provide business results. It certainly requires time for employees to believe in employment security and for that belief to generate trust and produce higher levels of innovation and effort. Consequently, a long-term view of a company's development and growth is at least useful, if not absolutely essential, to implementation of high performance organizational arrangements.

One must bear in mind that one-half of organizations won't believe the connection between how they manage their people and the profits they earn. One-half of those who do see the connection will do what many organizations have done—try to make a single change to solve their problems, not realizing that the effective management of people requires a more comprehensive and systematic approach. Of the firms that make comprehensive changes, probably only about one-half will persist with their practices long enough to actually derive economic benefits. Since one-half times one-half times one-half equals one-eighth, at best 12 percent of organizations will actually do what is required to build profits by putting people first. Don't like these odds? Well, consider this: almost every other source of organizational success—technology, financial structure, competitive strategy—can be initiated in a short period of time. How many other sources of competitive advantage have a one-in-eight chance of success?

In the end, the key to managing people in ways that lead to profits, productivity, innovation, and real organizational learning ultimately lies in the manager's perspective. When managers look at their people, do they see costs to be reduced? Do they see recalcitrant employees prone to opportunism, shirking, and free riding, who can't be trusted and who need to be closely controlled through monitoring, rewards, and sanctions? Do they see people performing activities that can and should be contracted out to save on labor costs? Or, do they see intelligent, motivated, trustworthy individuals—the most critical and valuable strategic assets their organizations can have? When they look at their people, do they see them as the fundamental resources on which their success rests and the primary means of differentiating themselves from the competition? With the right per-

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spective, anything is possible. With the wrong one, change efforts and new programs become gimmicks, and no army of consultants, seminars, and slogans will help.

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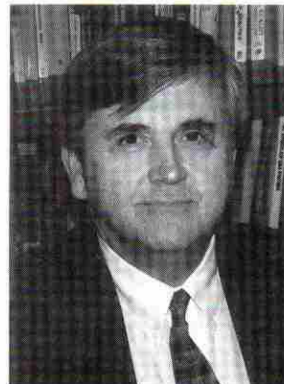

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