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Leader To Leader Journal

The Real Keys to High Performance

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It appears that the old aphorism, "people are our most important asset," is *actually true*. Compelling evidence suggests that organizational success comes more from managing people effectively than from attaining large size, operating in a high-growth industry, or becoming lean and mean through downsizing -- which, after all, puts many of your most important assets on the street for the competition to employ. But while many leaders believe that putting people first makes strategic sense, all too few of their organizations do it.

What can you actually do to implement high-performance management practices and enjoy the benefits that will almost certainly accrue? Unfortunately, there are no easy answers -- if there were, this strategy would not be such an important foundation for sustainable competitive success. But there are things that high-performing organizations do that can spur new thinking about the question.

Achieving profits through people requires consistent leadership attention -- and that is the biggest barrier to success. The scarcest resource in most organizations is time and attention -- what leader has enough? Time spent focusing on one thing cannot be spent on others, and too often quarterly financial results crowd out the long-term management of people. Leaders of truly successful organizations -- such as Whole Foods Markets, Southwest Airlines, the Men's Wearhouse, and AES Corporation -- see their role as systems architects, engaged in the critical task of building values, cultures, and a set of management practices that enable the recruitment, retention, development, and motivation of outstanding people. They also engage in the important work of building work practices that ensure that the ideas of *all* people become known and used.

Whole Foods, which has grown in the 1990s from $100 million to $1 billion in sales -- in the grocery business, no less -- is famous for its use of self-managed teams. The company shares detailed performance and financial information with all its people -- so much information that, because many people own stock in the company, all employees are considered insiders for purposes of Securities and Exchange Commission regulations. The company even makes data about individual salaries available to *all* its employees. It also shares productivity gains with its people through team-based incentive compensation, in the process of fostering decentralized decision making.

The Men's Wearhouse has succeeded in the retailing industry -- notorious for its use of part-time, low-paid, undertrained, and poorly treated help -- by doing exactly the opposite: investing heavily in training, using few part-time staff, and paying above-industry-average wages and encouraging employee stock ownership. The company recognizes that what is important is not what people *cost*, but what they *do*. AES, a global developer and operator of electric power plants, has succeeded by fostering radical decentralization, sharing financial and performance information (all of its people are also insiders), recruiting on the basis of cultural fit, and eschewing bureaucracy. How many companies with several thousand employees do you know that have no human resources staff, and that make business development and strategic planning part of everyone's job, not just the province of some centralized staff?

The Real Source of Success

It may seem obvious that building organizational capability and ensuring the implementation of high-commitment management practices is a key managerial responsibility. But this prescription is frequently honored in the breach. Conventional wisdom argues that senior leaders should focus on making strategy, seeking some technological edge, and worrying about financial engineering, mergers and acquisitions, and restructuring.

But the data on the sources of sustained success are clear. Is being in a high-technology industry an essential source of competitive success? It can be, but not necessarily. When the *Wall Street Journal* ranked industries by their five-year returns to shareholders, in 1997 only 3 out of the top 15 industries were in high technology. In the *Journal*'s 1996 list, restaurants (ranked 26) provided a higher five-year return to shareholders than did medical devices (ranked 28), and footwear (ranked 30) outperformed pharmaceuticals (47). The computer industry ranked only 78th, behind industries such as automobile parts (34), heavy machinery (29) and even railroads (33). *Inc.* magazine's list of the fastest-growing companies in 1996 was headed by a toothbrush manufacturer, a consumer products distributor, and a human resources service company.

Does being in a rapidly growing industry matter? A study by consultants at Booz, Allen and Hamilton of over 1,800 companies with a market capitalization of more than $500 million in 1994 found that industry growth rates were completely unrelated to the growth rates of individual companies, as measured by the 10-year return on shareholder

equity. Another study of growing companies found a similar disconnect between company growth rates and the growth rates of their industries. The Men's Wearhouse, for instance, has enjoyed compound growth of more than 30 percent annually in both sales and profits over the past half-decade. In the relatively stagnant market of men's tailored clothing, the firm grows by taking business from the competition.

Does size matter, and in particular, does the wave of mergers and consolidations undertaken to presumably achieve economies of scale make sense? My analysis of 80 nonfinancial industries shows that in 44 percent of the industries, the

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correlation between sales volume and return on capital is actually negative. Chrysler has been more profitable than General Motors, as has Ford. Southwest is the most profitable and efficient airline, although it is far from the largest. Even in financial services, the banks with the highest return on assets, an important measure of profitability, include virtually none of the largest. Across industries, the average correlation between size and two measures of profitability, return on assets and return on shareholders' equity, was only 0.1. This means that size is almost completely unrelated to firm profitability.

Should leaders worry about having the right strategy? Sure, but implementation is a lot more important. As a senior officer at one of the leading strategy consulting firms admitted to me, "*finding* the answer is relatively easy; doing the answer is frequently impossible." Richard Kovacevich, CEO of Norwest, the enormously successful financial services company, recently told the *Wall Street Journal*, "I could leave our strategic plan on a plane ... and it wouldn't make any difference. No one could execute it." As Tom Farmer, the CEO of Kwik-Fit, the largest supplier of automotive repair services in the United Kingdom, says, "In a service business [and in today's world, all businesses are service businesses], there is only one successful strategy -- providing your customers outstanding value and service -- customer delight."

The evidence is also clear on the effects of downsizing and restructuring -- these actions will not increase stock price (over an 18-month or two-year period), nor will they increase productivity or efficiency. Rather, downsizing will do only one thing: make the organization smaller. So leaders would do well to spend less time worrying about finding the right competitive niche, searching for technological silver bullets, and massaging financial statements, and spend more time developing their people to provide the competitive edge. Numerous studies indicate that managing people using high-performance or high-commitment practices can produce enormous economic returns (see box). Moreover, really making people your most important asset turns out to be difficult to copy.

Three Guiding Principles

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 have observed three basic principles that leaders use to transform their organizations to a high-commitment model of management: build trust, encourage change, and use appropriate measures of performance. Each of these principles makes as much sense as

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the idea of building organizations that develop and apply employees' knowledge and competence. But again, experience reveals that common sense is not common in managerial practice.

Building Trust

At the most basic level, one builds trust by treating all members of the organization as though they can be trusted. This means, among other things, sharing information with everyone. When John Mackey, CEO of Whole Foods, was asked why the firm shared all of its performance information with everyone, and even made it possible for each team member to know the salary of everyone else in the company, by name, he replied that to keep secrets implied that the organization didn't trust those from whom information was withheld. Knowledge is power, and sharing information entails sharing power. But not to share information suggests that there are some in the organization who can be trusted with its secrets, and others who can't. This is the wrong message to send if you want to harness the efforts and energy of everyone.

You cannot build trust without treating people with respect and dignity. It is now all too common to have layoffs in which those let go are immediately escorted off the premises. This process deprives them and those left behind of the opportunity to say good-bye and, more fundamentally, signals distrust and disrespect. Consider instead the New Zealand Post, which, since becoming a state-owned enterprise expected to operate like a private company in 1987, has accomplished amazing things (for instance, actually *reducing* the cost of a stamp). People laid off were offered generous severance, given parties on their leaving, and recognized for their contributions to the company. Indeed, the Post even let the staff help decide who would go and who would stay -- for it turned out that some people the organization intended to keep wanted to leave or retire and others wanted to stay.

Building trust also means taking the organization's values seriously. At AES, the annual report discusses how well the organization is doing in living up to its four core values of fun, fairness, integrity, and social responsibility. Whole Foods Market's annual report prominently presents the results of its employee satisfaction survey. These organizations signal that they take seriously their commitments to both their values and their people by publicly discussing where they are succeeding and where they are falling short -- and what they are going to do about it.

Encouraging Change

Leaders can encourage change in many ways. One is by exposing themselves and their colleagues to alternative models of management. It is useful to read about Southwest Airlines or AES or the Men's Wearhouse, but it is much more compelling to visit these companies, talk to their people, and experience firsthand what a different way of treating people feels like. When Citibank recently became interested in using quality as a way of organizing and motivating change, it invited people from Motorola to visit. The reverse of that process -- having Citibankers spend time actually experiencing Motorola -- might have been even more powerful.

Another way organizations can encourage change is by doing things that break old ways of organizing. The New Zealand Post did two such things. First, it reorganized frequently. Putting people in new roles in a new organizational structure almost automatically ensured that they would have to do things differently and not be bound by old habits and assumptions. In addition, the company physically reconfigured the workplace to promote new ways of working and thinking about customer service processes. At the Dallas plant of AT&T in the late 1980s, the new plant manager, Ken Weatherford, encouraged change by making visible changes to the plant's operations -- changing the dress code so that ties were no longer worn, moving the engineers out to the production area, reorganizing the plant into four focused factories by moving equipment and rearranging production process. In a world in which new initiatives are greeted with skepticism, the easiest way to convince people that this time it's for real is to begin doing things that demonstrably signal that change is occurring and that put people in new places with new work roles that require them to work in new ways.

Measuring What Matters

Finally, leaders who have successfully built high-performing workplaces make sure to measure the practices that constitute high-commitment management. They also measure related management processes that determine how the organization is functioning. The problem is simple: most financial reporting systems provide tremendous detail about what *has* happened, but much less information about the organization's present condition or the reasons for its performance. It is, as the saying goes, like trying to drive by looking in your rear-view mirror. A positive response to this problem is Robert Kaplan and David Norton's balanced scorecard approach, in which financial measures are weighed against measures of customer satisfaction and retention, employee attitudes and retention, new product and new business development, or readiness for change. Some of these indicators are more difficult to measure than past financial performance, but sophisticated leaders recognize that measurement systems focus organizational attention, and that the adage "what gets measured gets done" is accurate.

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Every business has a few key drivers of success. It is the job of management to lead a process in which these key success factors are understood, measurements for them developed, and then attention focused on those measures. If people are an important source of competitive advantage, then the attraction, retention, development, and spirit of an organization's people requires as much attention as the financial statement. At the SAS Institute, a $650 million, privately held developer of statistical software for business applications, employee recruitment and retention are key measures of performance. A visitor hears much more discussion about the number of people applying for jobs and the company's turnover rate than discussion of sales or finances. The CEO, James Goodnight, recognizes that in a knowledge-intensive business, if you can hire and retain the best people, the other results will follow.

Measuring what really matters, not what the current information system happens to routinely track, is critical. It is no accident that great companies develop unique standards of performance -- and that these often involve people. For example:

- Hewlett-Packard evaluates managers on their subordinates' assessment of managerial behavior and adherence to H-P values.
- Motorola has had a goal of giving each employee at least 40 hours of training per year, and measures managers by the proportion of their people who get the requisite amount of training.
- Singapore Airlines spends 15 percent of its payroll costs on training -- no wonder the firm is a model of service. What is most important, however, is that the firm takes its commitment to training seriously enough to track it.
- The SAS Institute measures employee turnover; managers know their numbers and talk about them.
- Southwest Airlines tracks the number of job applicants (currently more than 120,000 a year). Some would see processing so many applicants as a waste of resources, but Southwest views this activity as critical to ensuring access to the best possible workforce.

It is also possible for organizations to assess the proportion of the workforce working in teams, the number of people who know the organization's strategy and its performance measures, the number of layers in the hierarchy (a reasonable indicator of decentralization), and similar factors related to a firm's people management practices.

Wise leaders use measures not only to focus attention but also to drive change and continuous improvement. Comparisons across teams at Whole Foods Market stimulate everyone to do better in an atmosphere of friendly competition. At the Men's Wearhouse, sales per square foot, sales per employee, and the size of the average sale are all tracked and reported internally. This measurement and comparison process stimulates internal benchmarking and the sharing of sales and merchandising ideas among people and across stores, providing a standard for continuous improvement.

A New Role for Leaders

In today's world, knowledge and capability have become keys to success because everything else -- product offerings, marketing strategy, sourcing schemes -- is easily acquired or imitated. Putting people first, or at least taking people issues seriously, is more important than ever. But implementing high-commitment practices requires a different view of management and competitive advantage. From this perspective, leaders build systems -- systems that build distinctive competence and capability and that, because of their internal coherence, are robust even as the competitive landscape and the macroeconomic environment change. These leaders don't necessarily make a lot of business decisions, even decisions about strategy, or worry a lot about financial engineering and restructuring. They make more important decisions about systems for recruiting, motivating, and developing people that, if successful, will ensure the organization has the talent necessary both to develop an effective strategy and to execute it. It may seem strange to see the leader's role as being the chief people (or culture) officer, but that is exactly what you will find in organizations that have really achieved profits through people.

In hindsight, it is relatively straightforward to assess whether or not this effort at systems architecture has been successful. Some years ago, three colleagues did a study of productivity in the worldwide automobile industry over a 40-year period. Using sophisticated statistical methods, they were able to estimate not only overall productivity growth but also, more specifically, growth in labor and capital productivity and the effects of various CEOs' tenures on all this. With one exception, every automobile manufacturer showed the results of a particular CEO's strengths or weaknesses. For instance, Donald Petersen at Ford was associated with continual increases in productivity. In other companies, some CEOs had positive effects, others negative. The one company in which there was no CEO effect was -- could you guess? -- Toyota. That makes perfect sense. Toyota, after all, is famous for its Toyota Production *System*. Although that system has been refined over time, the point is that it is, in fact, a system -- a set of interrelated elements that has provided the company with competitive advantage during dramatic changes in the value of the yen, in the location of manufacturing facilities, and in product mix and consumer tastes. I can think of no better example of the power of systems architecture.

An organization need not be born doing the right thing with respect to people. The New Zealand Post wasn't, nor was Ford Motor. As long as leaders recognize the importance of building business success around their people and learn to manage with trust, encourage change, and make sure that their measurement systems contribute rather than cause problems, organizations of all sizes and in all sectors can accomplish great things. It just requires leaders to focus on what is, after all, their most important asset.

Five Cases for High-Performance Management

Studies in a wide range or manufacturing and service industries show that management systems that encourage personal commitment and competence achieve greater productivity, quality, and cost efficiency than systems that impose direct control. Highlights of five studies suggest just how much people can deliver when supported by effective management.

Among 702 large firms in many different industries, being one standard deviation better on an index of high-commitment human resource practices resulted in an increase in shareholder wealth of *$41,000 per employee*, according to a study by Mark Hustled of Rutgers University and Brian Becker of SUNY-Buffalo.

Motor vehicle manufacturing firms implementing flexible production processes and associated practices for managing people enjoyed 47 percent better quality and 43 percent better productivity than firms relying on traditional mass-production approaches, according to a world-wide study by Wharton School's John Paul MacDuffie.

The five-year survival rates of initial public offering showed that firms whose human resource practices scored in the top one-sixth of IPO firms had a 33 percent higher probability of surviving than those in the lowest one-sixth. Firms in the upper one-sixth in providing financial rewards to all employees, not just managers, had almost twice as much chance of surviving for five years, according to research by Theresa Welbourne of Cornell and Alice Andrews of Vanderbilt.

Steel minimills using a high-commitment approach to management required 34 percent fewer labor hours to make a ton of steel and had a 64 percent better scrap rate than minimills using a command and control approach, according to Jeffrey Arthur of Purdue.

Apparel manufacturing firms that had changed to modular production, relying on teams of multi-skilled people paid more on a group (rather than individual piecework) basis, had 65 percent better operating profit as a percent of sales, 22 percent higher gross margins, and 49 percent more growth in sales from 1988 to 1992 compared to firms that relied on traditional bundle manufacturing and paid single-skilled operators on the basis of individual piecework. So found John Dunlop of Harvard and David Weil of Boston University.

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A high-performing team never really loses sight of its goals--and in most cases, it's largely self-sustaining. Your team takes on a life of its own, and can skyrocket your business to new heights. But that's the end game: no team starts out that way. It develops from strong leadership. Managing the performance of your team has the most significant impact on sustainable growth for your business. Unfortunately, a lot of companies still rely on outdated models for annual performance reviews that don't directly engage the individual or involve them in the process. Effective performance management The real vision of your organization will crystalize once you create organization-wide buy-in among your employees. 4. Create a customer-centric focus. Learn how the Four Keys open source project lets you gauge your DevOps performance according to DORA metrics. At a high level, Deployment Frequency and Lead Time for Changes measure velocity, while Change Failure Rate and Time to Restore Service measure stability. And by measuring these values, and continuously iterating to improve on them, a team can achieve significantly better business outcomes. Baselining your organization's performance on these metrics is a great way to improve the efficiency and effectiveness of your own operations. But how do you get started? The journey starts with gathering data. High performance work system (HPWS) is a specific combination of HR practices, work structures and processes that enhances employee skill, knowledge, commitment, involvement and adaptability. The key concept in HPWS is the system. HPWS is composed of many interrelated sub-systems that complement one another to attain the goals of an organization, big or small. Though it may be difficult to list the 'best practices' in HPWS, there are a few important components of HPWS. Arranging for the right environment to learn in 'real time' on the job, using innovative new approaches to solve real problems. v. Making employees aware of the firm's progress and. vi.