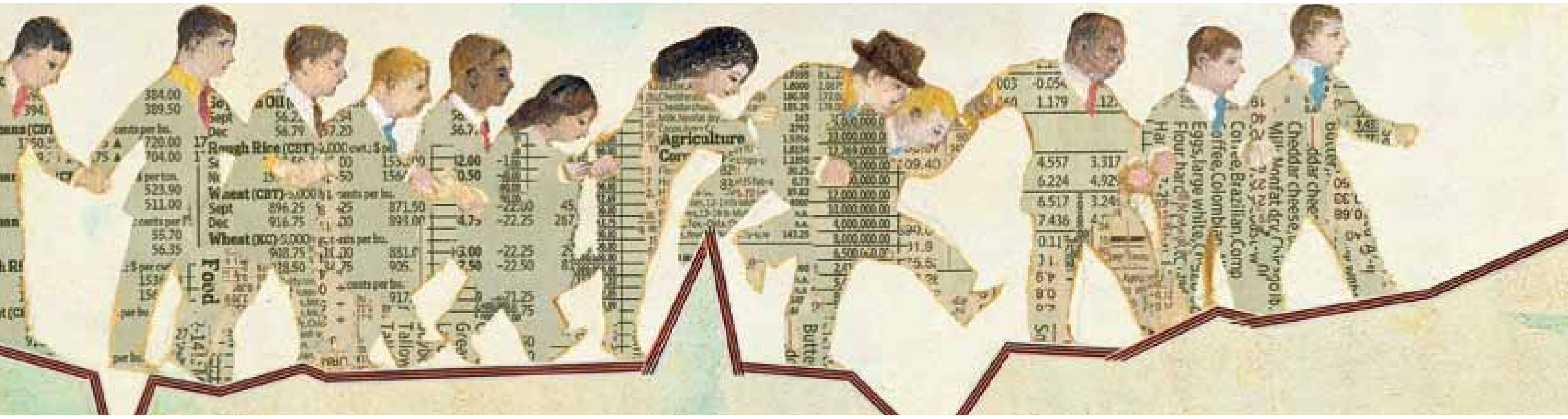


Improving cooperatives' agility

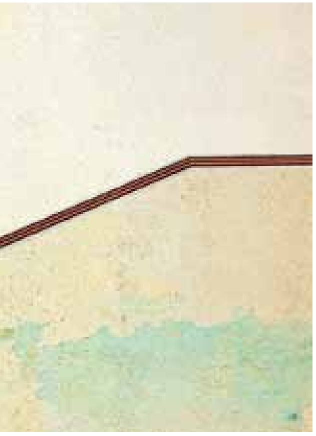
Coops excel at gaining organizational alignment and mobilizing employees but can be slow in responding to emerging challenges and opportunities. Some leading coops are finding ways to beat the odds.

Vincent Bérubé, Eric Lamarre, and Scott Rutherford

Cooperatives differ substantially from publicly owned companies in their ownership structures and governance models. Coops limit ownership to their members, who in many cases are also the organization's customers or suppliers. And they are also known for their participatory and democratic decision-making processes—one member, one vote.

But do these characteristics translate into any differences between cooperatives and their publicly owned counterparts with respect to organizational effectiveness, which we define as the ability to align around a strategy, to execute it, and to renew a company faster than competitors do? The answer is yes. The ownership and governance construct of cooperatives provides them with some clear advantages over public companies, but the model also creates distinct challenges.

We set out to explore these differences in more depth using McKinsey's organizational-health index, a proven tool for diagnosing the nine elements of organizational health (see "An introduction to the organizational-health index (OHI)," page 16). We surveyed over 600 employees from nine cooperatives in different industries and compared the aggregated results against a comparable set of 4,133 respondents from 136 publicly listed companies with a similar industry profile. We supplemented this analysis with



50 interviews with senior executives (chairmen, CEOs, and executive vice presidents) from leading cooperatives around the world. These interviews helped us interpret the results and gain a better understanding of the governance and managerial practices these executives employ to strengthen their organizations.

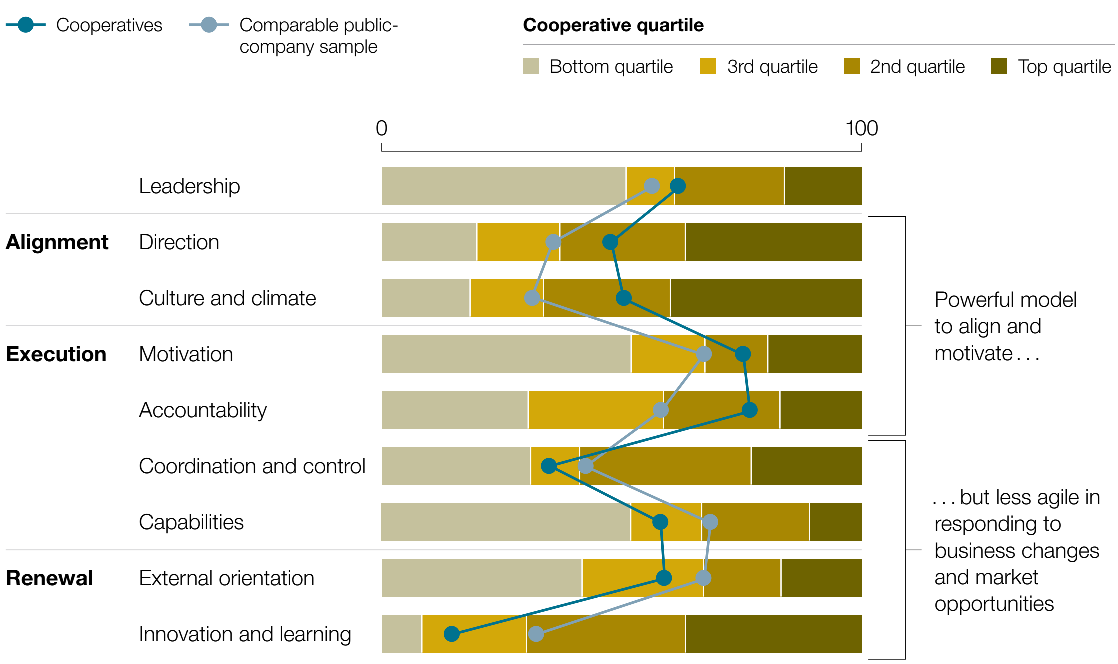
A powerful model to align and mobilize

We found the cooperative model to be particularly effective in creating organizational alignment and employee mobilization (Exhibit 1). Because owners are also members, and because members participate in the cooperative's direction-setting process, the organization's strategy is usually well aligned with members' needs. In addition, the fact that cooperatives adhere to a service-oriented mission (as opposed to public companies' mission of creating value for shareholders) tends to create a sense of higher purpose, which appeals to and mobilizes coop employees. As a result, coop employees experience a strong sense of ownership of, and belonging to, their organization. This explains why cooperatives outperform publicly owned companies in customer-satisfaction surveys. For example, Exhibit 2 shows the results from 2009 through 2011 from McKinsey's customer-satisfaction survey for North American banks. Credit unions, which operate under a cooperative model, have consistently achieved higher customer-satisfaction scores than their rivals over this period.

Exhibit 1

Coops do well on alignment and motivation but need to improve their agility.

% of respondents who believe their institution performs well on each dimension

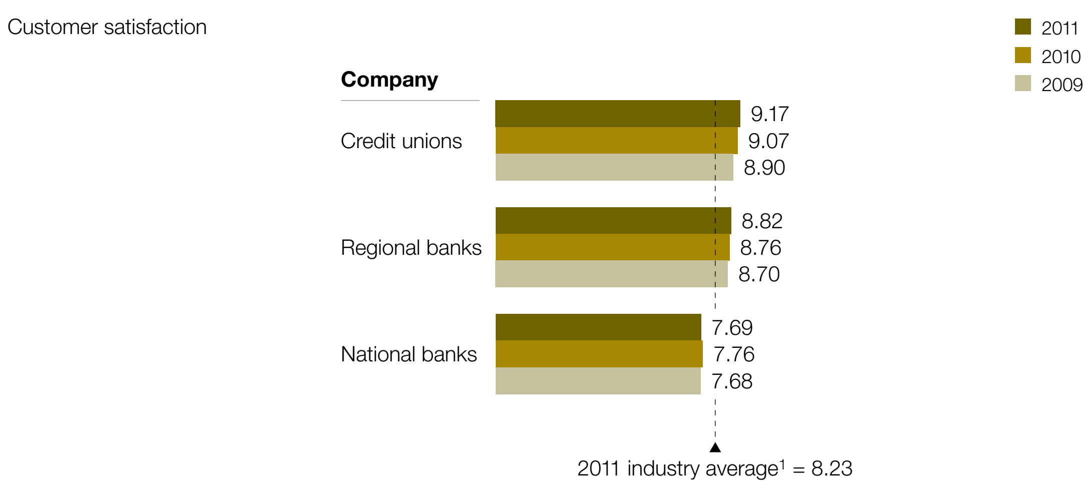


The coop model also has its challenges, particularly with regard to organizational agility, as the lower part of Exhibit 1 suggests. Coops' lower score on *coordination and control* indicates that they less consistently measure and manage business performance, translating into slower action to address problems or opportunities as they arise. Part of this is attributable to less effective performance-management systems and part is—according to our interviews—due to the naturally slower pace of democratic decision-making processes. Their lower scores on *external orientation* and *innovation* mean that cooperatives are slower and less agile when it comes to renewing themselves (that is, their organizations change more slowly) than their publicly traded cousins. Finally, a lower score on *capabilities* shows that coops place less emphasis on ensuring that they have the institutional skills and talent to execute the strategy and create competitive advantage than their publicly owned competitors. In essence, coops are less agile in hiring and developing the talent they need.

To illustrate at a more granular level the agility challenge that cooperatives face, we have compiled in Exhibit 3 a sample of practices measured in the OHI survey and the specific questions regarding those practices for which coop employees reported important gaps (as will be discussed below, "consultative leadership" is noted in the exhibit as a strength, but it also creates agility-related challenges). Based on cooperatives' performance on these practices and on our interviews with senior coop executives, we see three areas in which coops can improve their agility: making decisions, pursuing new opportunities, and sourcing and developing talent.

Exhibit 2

North American coop banks outperform rivals on customer satisfaction.



[1] Customer satisfaction was measured on a scale of 1–10; all data are weighted.
Source: 2009–11 McKinsey survey of cross-industry customer experience

Exhibit 3

Coops face particular challenges in seven areas related to agility.

Cooperative quartile

- Top quartile
- 2nd quartile
- 3rd quartile
- Bottom quartile

OHI[1] practices	Coops' spread to public-company reference sample[2]	Sample questions	
Consultative leadership	5	Leaders in the company ask the opinions of others before making important decisions	Agility in decision making
Financial management	–8	The company's financial control systems monitor financial performance deep in its business units	Agility in decision making
Business partnerships	–5	The company pursues joint performance initiatives with external business partners	Agility in pursuing new opportunities
Knowledge sharing	–5	The company's systems and processes facilitate cross-functional initiatives	Agility in pursuing new opportunities
Capturing external ideas	–7	The company uses external contacts to maximize the flow of ideas into the company	Agility in pursuing new opportunities
Sourcing and developing talent	–6	The company uses job rotation to broaden the experience and capabilities of its talent	Agility in sourcing and developing talent
Outsourcing expertise	–13	The company outsources functions or activities that can be better done by others	Agility in sourcing and developing talent

[1] Organizational-health index.
[2] Percentage-point differences in respondents' answers.

Increasing organizational agility

In our interviews with coop senior executives, they told us how they were responding to these challenges, which allowed us to distill a few effective managerial and governance practices. The rest of this article will outline some ideas coops might consider implementing based on the successes of their peers.

Agility in decision making

One of the main strengths of cooperatives, their consensual and consultative decision-making processes (Exhibit 3), also contributes to one of their greatest weaknesses—delayed action due to healthy but lengthy debates that take place at multiple levels of the organization. To increase their responsiveness to changing conditions, coops must strike a better balance between their democratic nature and executive agility. Leading coops are finding three actions to be helpful: clearly distinguish the respective roles and responsibilities of executive officers and elected officials (such as board members), create more efficient processes for consulting with members on strategic direction, and improve performance-management systems to

continued on page 18

An introduction to the organizational-health index (OHI)

Drawing on extensive research of academic literature and decades of work with institutions across the public, private, and social sectors, we have identified nine dimensions by which we judge an organization's ability to sustain performance over time (exhibit).

First, organizational effectiveness requires alignment: everyone must be working toward the same goal in a shared context, and in a shared way. This requires ***direction*** (a clear sense of where the organization is heading and how it will get there that is meaningful to all employees), successful ***leadership*** (including, among other things, the quality of decision making and the ability of leaders to inspire action), and a strong ***culture and climate*** (the shared beliefs and quality of interactions within and across organizational units).

Second, an effective organization can consistently execute its strategy because, in addition to strong leadership, it maintains the necessary ***capabilities*** (individuals with practical and leadership skills, as well as institutional enablers), ***motivation*** (the enthusiasm that drives employees to put in extraordinary effort to deliver results), ***accountability*** (the extent to which individuals understand what is expected of them, have authority, and take responsibility for delivering results), and ***coordination and control*** (the ability to evaluate organizational performance and risk, and to address issues and opportunities when they arise).

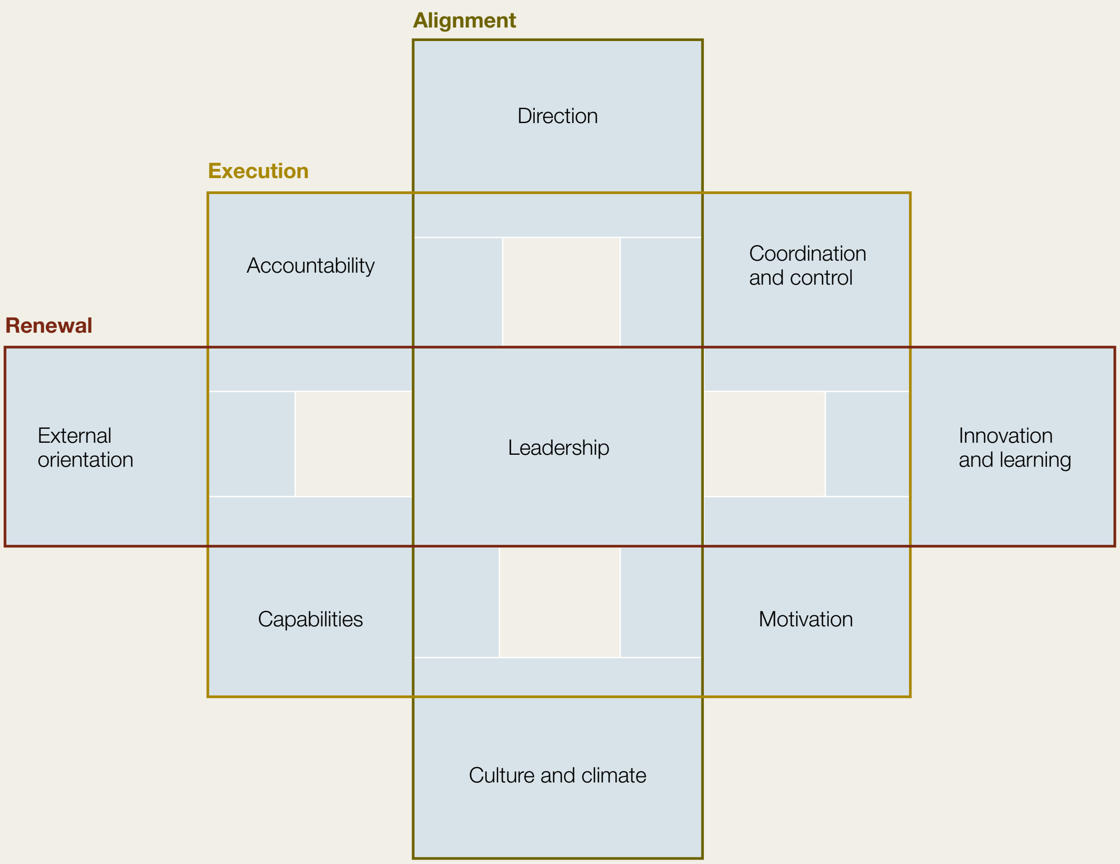
Finally, an effective organization can renew itself. Leadership affects the ability to renew as well. In addition, a healthy organization has the ability to adapt and change over time, because it is ***externally oriented*** (it engages well with customers, suppliers, partners, and other external stakeholders to reach the organization's objectives, and it is sensitive to market trends and the competitive landscape) and has practices in place to systematically drive ***innovation and learning*** (new ideas flow into and through the organization, and help to adapt and shape the organization as needed).

McKinsey has shown empirically that over time organizations that score well on the OHI outperform those with poor OHI scores financially and operationally. Organizations with a top-quartile OHI score, for example, are more than twice as likely to deliver above-median financial performance as those with bottom-quartile performance.[1]

[1] Scott Keller and Colin Price, "Organizational health: The ultimate competitive advantage," mckinseyquarterly.com, June 2011.

Exhibit

The organizational-health index measures nine dimensions related to organizational alignment, execution, and renewal.



Agile decision making requires effective performance-management systems that surface issues quickly and enable corrective action.

enable rapid identification and correction of the sources of underperformance.

FrieslandCampina, the Dutch dairy cooperative, provides a good example of how a cooperative clarified the roles between executive and elected officials to remove bottlenecks from decision-making processes. The cooperative formed a separate operating company with its own board. The cooperative remained a full owner of the new operating company but, by creating a separate entity, it created a healthy distance between the cooperative democratic processes and the day-to-day rapid operating decisions required to compete effectively in the market. The cooperative's members elect 9 of the operating company's 13 board members, giving them continued control over that company by virtue of their two-thirds majority vote on the board. However, these board members' roles are well defined, and in fact are identical to those of publicly traded companies' board members under Dutch law. As one senior executive puts it, "Although there is limited interference in the daily management of each other's business between the executive team and the cooperative members, we feel very close to our members."

The Co-operative Group—a UK-based diversified coop involved in retail and financial services—is a good example of how to use technology to gain efficiency in consultative processes related to key strategic decisions. The consensus-driven processes that define most cooperatives' governance models are fundamental to creating organizational alignment, but unfortunately, they often take too much time. The Co-operative Group has found that technology can help get members more quickly and directly involved in key strategic decisions: it uses the "crowd" to inform its decisions. For example, when the organization wanted to open 300 new food stores over the course of three years, it asked its seven million members to suggest new sites through a technology solution that helped capture and synthesize the voluminous input received from members. This initiative significantly accelerated the consultative process and allowed members to be more broadly involved in setting the direction of the coop.

Agile decision making also requires effective performance-management systems that surface issues quickly and enable corrective action. Many coops find this to be a challenge because they are often decentralized and their managerial (executive) and board (democratic) structures often overlap. BPCE, a financial coop based in France, offers a good example of effective performance management. It created a transparent data warehouse that allows its 37 regional cooperative banks to compare their performance on key indicators and share best practices. The indicators include internal benchmarks to favor transparency and internal competition (banks are ranked based on their scores and performance is tracked over time), as well as external benchmarks that ensure the group considers outside best practices.

Agility in pursuing adjacent opportunities

One of the founding principles of the coop model is to provide services to members at an attractive price point. If a new business opportunity falls outside the immediate needs of the membership base, a coop can have difficulty seizing it. Members may not be willing to spend their capital pursuing opportunities that do not offer them direct tangible benefits. This explains, in large part, why coops do better at gaining market share than publicly owned companies but underperform at growing in adjacent product or customer segments (see "How cooperatives grow," page 4). Our interviews highlighted three managerial practices that can help coops become more agile in their pursuit of new opportunities: expose the cooperative to more external perspectives, put in place explicit processes enabling different parts of the organization to work together and share ideas, and develop mechanisms to finance emerging opportunities that may not have immediate or direct benefits to the current membership base.

One way that cooperatives can bring in external perspectives is to invite independent professionals from outside the organization's membership to serve on the board of directors. CBH Group, a cooperative of grain farmers (and the largest coop in Australia), has found that by appointing 3 of its 12 board members from outside the organization, it has enriched the board's composition with knowledge and skills it needed for continued success. For example, as CBH Group was investing to reform its grain-rail network in Western Australia, the recently added external board members were able to help evaluate several technical questions that could not have been answered as easily using only internal expertise. One such question related to financial deal structures for infrastructure projects, which have become extremely important to the future success of this agricultural coop.

The MONDRAGON Corporation—a worker-federation cooperative in Spain that is involved in manufacturing, retail, and financial services—is a cooperative that pursues new business opportunities with agility. This cooperative, whose slogan is "humanity at work," was created to support employment for residents of the Basque

region. Faced with increasing competitive threats that resulted from the liberalization of European markets in the early 1990s, MONDRAGON put in place three practices to increase its business innovation, productivity, and capacity to create jobs. First, it created research-and-development "networks" dedicated to developing new products and services: 14 technology centers and R&D units specialized in fields relevant to MONDRAGON, such as lifting systems, packaging machines, and thermoplastics.

Second, it developed processes at all levels of the cooperative to encourage cross-functional and cross-business-unit innovation. For example, MONDRAGON has established three groups that specialize in cross-product initiatives. These groups convene employees from different divisions to explore new business ideas, which are eventually elevated to the coop-wide level for production and commercialization. These interdivision initiatives are made possible by clear coordination among top managers to ensure appropriate transfer of technology and know-how among divisions.

Finally, MONDRAGON put in place funding mechanisms to ensure the survival and success of new initiatives. The coop invests a minimum of 10 percent of its gross profits into a "development fund" that finances innovation, research, and international business development. According to MONDRAGON, 21 percent of its sales are from products that are less than five years old.

Agility in developing and sourcing talent

Public companies have become much more agile in sourcing and developing talent. They systematically hire outside talent. They outsource noncore activities. They create job-rotation and mobility programs to broaden the experience and capabilities of their top talent. They provide leadership training to develop their high-potential executives. Of course, cooperatives also do all these things, but our survey and interviews suggest that they are less agile at doing it than publicly owned companies, as Exhibit 3 showed. Our interviews highlighted two practices that can help cooperatives be more agile in talent management: first, actively identify top talent and create leadership-development tracks combining experiential and "classroom" learning, and second, adopt recruiting and training practices that change how the younger generation of potential employees views coops in comparison with public companies.

Mouvement Desjardins, a diversified financial cooperative based in Québec, offers a good example in the area of leadership development. It created a renewed mandate for its institute, the Institut coopératif Desjardins, and expanded its education mission to include programs for leadership development and technical skill building. The institute offers its courses to both elected and executive leaders, separately or jointly, depending on the topic. In the organization's leadership and performance program, for example, over the course of three months, the top 400 executive leaders attend a series of workshops and field-based training sessions focused on honing their leadership skills at the personal, team, and organizational levels. In another program, elected and executive participants work together to develop their performance-dialogue skills—each set of participants improves these skills in a way that's relevant to its members' roles, but the goal is to get the two groups to more effectively work together for the betterment of the whole organization. Over the course of just two years, the institute launched 13 strategic talent-development programs. Many participants have taken on more senior leadership roles in the organization. In formal feedback, a vast majority are finding the institute an invaluable contributor to their career development.

Coop employees and leaders told us that their organizations have a difficult time attracting talented young people, who tend to view them as less exciting than public companies. But some cooperatives display great agility in adapting their recruiting and training practices to suit the needs and interests of younger people. For example, P&V, a Belgian insurance coop, recognized that its more local focus put it at a disadvantage when competing with multinationals for top talent (many coops face this issue, as they tend to limit their operations to a single region or country). The coop overcame this challenge by joining Euresa, an alliance of European insurance cooperatives and mutuals, the members of which offer a rotational program that allows selected early-tenure managers to work in other countries and get international exposure.

Another way to connect with the younger generation is to move to where the talent is. Farmers Cooperative (FC), a coop of grain farmers in Iowa, was experiencing explosive growth of 23 percent per year but was finding it difficult to attract the young talent that could help it stay on this trajectory. Beginning in 2008, the coop rolled out a bold recruiting campaign in collaboration with Iowa State University, which has one of the most prestigious agriculture schools in the United States. Every quarter, the CEO and his executive council organize events with high-potential students to offer mentoring and networking opportunities. FC offers scholarships to increase its visibility among college students and gives the best students paid internships. The organization even moved its headquarters close to the university to help make these programs accessible. The move allowed FC to double its intern pools and improve retention by hiring people who already had ties to the areas in which the coop operates.

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As cooperatives continue to grow and become large enterprises, organizational agility will increasingly determine their ability to competitively serve members in a fast-changing world. Improving their organizational agility while preserving their mission and principles is a fundamental organizational challenge of modern cooperatives. The examples illustrated in this article may not be suited for all cooperatives, but to be more agile each cooperative ought to evaluate the effectiveness of its decision-making processes, its capacity to innovate and mobilize to pursue adjacent opportunities, and its ability to source and develop the best talent in its industry.

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