

DECEMBER 2015

McKinsey Quarterly

Agility: It rhymes with stability

Wouter Aghina, Aaron De Smet, and Kirsten Weerda

Companies can become more agile by designing their organizations both to drive speed and create stability.

Why do established companies struggle to become more agile? No small part of the difficulty comes from a false trade-off: the assumption by executives that they must choose between much-needed speed and flexibility, on the one hand, and the stability and scale inherent in fixed organizational structures and processes, on the other.

Start-ups, for example, are notoriously well known for acting quickly, but once they grow beyond a certain point they struggle to maintain that early momentum. Equally, large and established companies often become bureaucratic because the rules, policies, and management layers developed to capture economies of scale ultimately hamper their ability to move fast.

In our experience, truly agile organizations, paradoxically, learn to be both stable (resilient, reliable, and efficient) and dynamic (fast, nimble, and adaptive). To master this paradox, companies must design structures, governance arrangements, and processes with a relatively unchanging set of core elements—a fixed backbone. At the same time, they must also create looser, more dynamic elements that can be adapted quickly to new challenges and opportunities. This article offers early insights from our work with large global institutions that have successfully become more agile by redesigning themselves for both stability *and* speed.

The power of ‘and’

Many companies have long been striving for greater agility—and many academics, consultants, and other advisers have been searching for successful ways to help them. Much of the

management literature, however, has emphasized only one part of the equation: how to achieve speed and flexibility.

Companies have indeed been able to move quickly by creating a flexible ring that's fenced off from the rest of the organization or, more recently, self-directed team structures embodied by "holacracy."¹ But our research and experience show that these ideas, on their own, are not enough. (To test your company's current agility level, see Exhibit 1.)

A 2015 analysis of McKinsey's Organizational Health Index showed that companies with both speed and stability have a 70 percent chance of being ranked in the top quartile by organizational health. That's a far higher proportion than McKinsey found among companies focused only on one or the other.² We've long established that organizational health is itself a predictor of strong financial performance.

These results are also consistent with an analysis by Columbia Business School professor Rita Gunther McGrath.³ From a pool of more than 2,300 large US companies, she identified ten that increased their net income by at least 5 percent annually in the ten years up to 2009. Her conclusion? These high-performing companies were both extremely stable, with certain organizational features that remained the same for long stretches, *and* rapid innovators that could adjust and readjust their resources quickly.

The ability to be both stable and dynamic, the essence of true organizational agility, is most easily grasped through a simple product analogy. Smartphones have become ubiquitous in part because of their design and functionality. The hardware and operating system form a stable foundation. But a dynamic application layer builds in "white space" for new apps to be added, updated, modified, and deleted over time as requirements change and new capabilities develop.

¹ Holacracy, exemplified recently by the online footwear company Zappos, seeks to encourage employees to behave like self-directed entrepreneurs and to instill their own sense of meaning and purpose in the workplace.

² For the full research findings, see Michael Bazigos, Aaron De Smet, and Chris Gagnon, "Why agility pays," *McKinsey Quarterly*, forthcoming on mckinsey.com.

³ Rita Gunther McGrath, "How the growth outliers do it," *Harvard Business Review*, January–February 2012, hbr.org.

Exhibit 1

Worksheet: Where does your organization fall today?

Place a check mark by every word that describes how it currently feels to work at your company. Total the number checked in each quadrant to see where your company falls.

Dynamic capability	<p>Strong ↑</p> <p>“Start-up”¹</p> <p style="text-align: right;">Total <input type="text"/></p> <ul style="list-style-type: none"> <input type="checkbox"/> Start-up <input type="checkbox"/> Chaotic <input type="checkbox"/> Creative <input type="checkbox"/> Frenetic <input type="checkbox"/> “Free for all” <input type="checkbox"/> Ad hoc <input type="checkbox"/> Reinventing the wheel <input type="checkbox"/> No boundaries <input type="checkbox"/> Constantly shifting focus <input type="checkbox"/> Unpredictable 	<p>Agile</p> <p style="text-align: right;">Total <input type="text"/></p> <ul style="list-style-type: none"> <input type="checkbox"/> Quick to mobilize <input type="checkbox"/> Nimble <input type="checkbox"/> Collaborative <input type="checkbox"/> Easy to get things done <input type="checkbox"/> Responsive <input type="checkbox"/> Free flow of information <input type="checkbox"/> Quick decision-making <input type="checkbox"/> Empowered to act <input type="checkbox"/> Resilient <input type="checkbox"/> Learning from failures
	<p>Trapped</p> <p style="text-align: right;">Total <input type="text"/></p> <ul style="list-style-type: none"> <input type="checkbox"/> Uncoordinated <input type="checkbox"/> Stuck <input type="checkbox"/> Empire-building <input type="checkbox"/> Fighting fires <input type="checkbox"/> Local tribes <input type="checkbox"/> Finger-pointing <input type="checkbox"/> Under attack <input type="checkbox"/> Rigid <input type="checkbox"/> Politics <input type="checkbox"/> Protecting “turf” 	<p>Bureaucracy</p> <p style="text-align: right;">Total <input type="text"/></p> <ul style="list-style-type: none"> <input type="checkbox"/> Risk-averse <input type="checkbox"/> Efficient <input type="checkbox"/> Slow <input type="checkbox"/> Bureaucratic <input type="checkbox"/> Standard ways of working <input type="checkbox"/> Siloed <input type="checkbox"/> Decision escalation <input type="checkbox"/> Reliable <input type="checkbox"/> Centralized <input type="checkbox"/> Established
	<p>Weak</p> <p style="text-align: center;">Stable backbone</p> <p style="text-align: right;">Strong</p>	

¹Exhibiting the characteristics of a start-up.

In the same way, agile companies design their organizations with a backbone of stable elements. These foundations, like a smartphone’s hardware and operating system, are likely to endure over a reasonable period. They might last a couple of years in the smartphone’s case, and more like five to ten years in a company’s. These agile companies also have more dynamic capabilities:

organizational “apps” to plug and play as new opportunities arise or unexpected challenges threaten to destabilize formerly protected profit streams. (For examples of these capabilities, see Exhibit 2.)

Balancing the tension

Our work has highlighted three core organizational areas where balancing this tension between stability and flexibility is critical: organizational structure, which defines how resources are distributed; governance, which dictates how decisions are made; and processes, which determine how things get done, including the management of performance.

Structure

Traditional hierarchies—boxes and lines on the org chart—typically specify where work gets done and performance is measured, and who’s responsible for awarding bonuses. All this generally involves a boss (or two in matrix organizations), who oversees work and manages direct reports (see sidebar, “Moving away from the mechanistic,” on page 6).

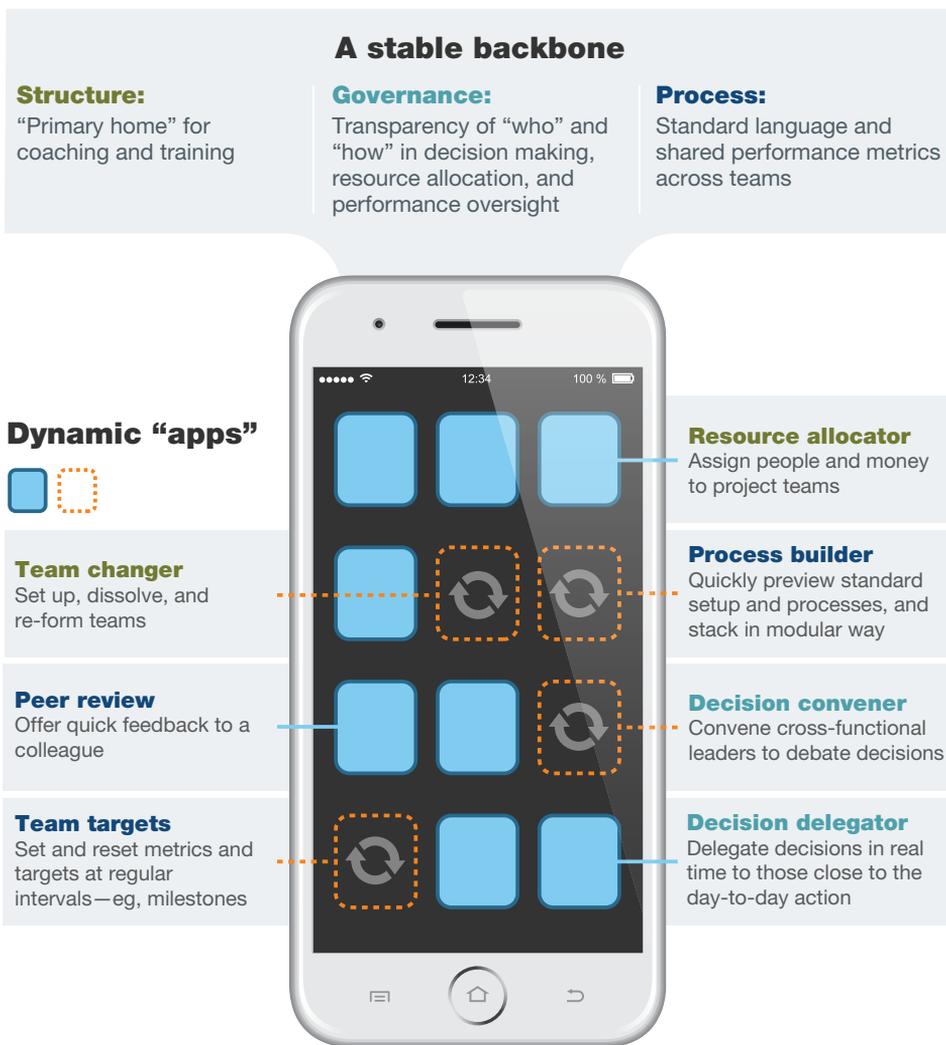
Agile organizations, by contrast, deliberately choose which dimension of their organizational structure will be what we call their “primary” one. This choice will dictate where individual employees work—in other words, where they are likely to receive coaching and training and where the infrastructure around their jobs is located. Day-to-day work, performance measurement, and the determination of rewards, on the other hand, are more likely to happen in teams that cut across formal structures. The primary home of employees remains an anchor along their career paths, while the crosscutting teams form, dissolve, and re-form as resources shift in response to market demands. Sometimes these dynamic teams show up in the org chart, typically in the form of business lines, market segments, or product units. At other times, they don’t, notably in a holacracy or other start-up organizational forms.

A global chemical manufacturer we know illustrates the benefits of this approach. Struggling to get traction on a new, increasingly international strategy, it changed its long-standing business-unit structure. Functions—that is, technical, sales, supply-chain, and customer-service resources—became the primary home for

Exhibit 2

Agility and the smartphone: An analogy

The phone's fixed hardware platform and space for new apps mirrors the agile organization's **stable backbone** and **dynamic capability** to add, abandon, replace, and update "apps." Together, these allow the organization to respond quickly to market changes.



McKinsey&Company

employees. At the same time, the company established a small product-line organization with P&L accountability, considerable decision-making authority, and a head who reports directly to the CEO. This "secondary" (product-line) organization holds the enterprise view for overall profitability and thus autonomously

Moving away from the mechanistic

To take the first step in joining the agile high-performing class, a company must challenge some of the most deeply held principles of organizational theory. Influenced by Frederick Taylor's and Max Weber's powerful ideas, first propounded roughly a century ago, many large businesses still think their organizations should operate like integrated machines comprising working parts that fit together seamlessly, like a smoothly running automobile.

In this machine view, organizations should be designed to run like clockwork. Organizational structures should follow rules that determine where resources, power, and authority lie, with clear boundaries for each role and an established hierarchy for oversight. When decisions require collaboration, governance committees should bring together business leaders to share information and to review proposals coming up from the business units. All processes should be designed in a very precise, deliberate way to ensure that the organization runs as it should and that employees can rely on rules, handbooks, and priorities coming from the hierarchy to execute tasks. Structure, governance, and processes should fit together in a clear, predictable way.

Today's problem is that by the time companies have designed this kind of structure, the world has already moved on and it's time to change again. In a McKinsey survey conducted last year, the executives responding told us that at least half of their companies are making significant structural changes, at either the unit or the enterprise level, as frequently as every two or three years. The redesigns often take one or two years to complete.¹ Why do these companies redesign themselves so frequently? A mechanistic approach logically leads executives to go back to the drawing board and redesign how the organization will work when things change. But in today's fast-changing world, this approach results in almost constant disruption and change fatigue. Even worse, only 23 percent of the redesigns in our sample were deemed successful by our respondents. They thought that most of the others had destroyed value.

The issue is that traditional mechanistic approaches to setting up and running organizations have tended to slow and restrain the creativity, innovation, and self-organization that social and technological developments could unleash. Internet companies like Wikipedia have harnessed enormous collective power with new models of collaboration. But executives in long-established and even blue-chip companies often feel trapped. Instead of developing the organization, many have yet to abandon the mechanistic model, which favors control and a precise engineering mind-set.

¹ For additional research findings, see Steven Aronowitz, Aaron De Smet, and Deirdre McGinty, "Getting organizational redesign right," *McKinsey Quarterly*, June 2015, on mckinsey.com.

synthesizes product strategy, decides where and how the company should invest its resources, and drives collaboration across functions and geographies.

Thanks to these changes, the company now has a better position to move quickly, and without major disruptions, as new and varied opportunities in emerging markets, notably China, present themselves. An application engineer in China, for example, might work in an office with the local sales team and report to a primary technical-support function in the org chart. That engineer could one moment be serving on a team developing a chemical product for the medical market and then be redeployed to a new team when an opportunity arose to supply that product to the Chinese construction industry. The roles, capabilities, and accountabilities of this engineer will be the responsibility of the more stable functional unit. But to use the smartphone analogy, the engineer's work teams are a dynamic, perhaps temporary application layer on top of the long-term organizational backbone.

A fast-growing online company we know applies the same logic. Its primary dimension revolves around functions. Dynamism comes from a series of performance units for customers with the same needs and product requirements. These market segments are not hardwired into the formal structure; they are temporary performance cells, populated by employees from across the organization (IT, marketing, finance) and reviewed every 90 days through clearly defined key performance indicators (KPIs). Senior executives then decide whether to keep these cells going, switch them off, or give them more or fewer resources. The reallocation process tends to be much more dynamic in this environment than in traditional structures. Why? The new market segments don't own the resources; the functions do. Customer units that have the greatest potential and perform well get the most resources. Those that have limited potential or perform poorly eventually die.

Another structural lesson from agile companies is that once they have chosen their primary dimension, that choice remains consistent over time. Coca-Cola, which has delivered top-quartile shareholder returns for years, has long implicitly understood this stable–dynamic paradox. Over many years, its organizational

structure has integrated dominant geographic units (regions and countries) as the primary axis, and a second dimension around a few strong central functions (marketing, finance, HR, and the like) in a well-understood, and largely unchanging, basic operating model. Adjustments are often made to the specifics as new issues and opportunities arise, but the essence of the matrix structure—i.e., geographic units as the primary axis, intersecting with strong key functions—has remained virtually unchanged for many years.

Contrast this approach with that of an international consumer-goods company we know which developed and implemented a painful redesign of its regional operations more than a year ago. It found that by the time the changes were finally taking hold, a further shift in the market had made the new organization redundant. In the smartphone analogy, this company had hardwired the anticipated needs into its structure but had not built a dynamic capability that would allow the new arrangements to endure over time.

Agile companies have learned that the stability of an organizational home is critical because it helps companies to redeploy employees in less successful cells more easily and rapidly, with little of the disruption and fear over job losses that traditionally deter and hinder change. We're not talking about fixed-term projects with a clear end date but rather about an open-ended deployment that could last a few weeks—or a few years. Functional heads therefore have the responsibility to provide coaching and develop capabilities that enable people to move on quickly to the next opportunity, opening a new door when an old one closes.

Governance

The idea behind agile governance is to establish both stable and dynamic elements in making decisions, which typically come in three types. We call big decisions where the stakes are high Type I; frequent decisions that require cross-unit dialogue and collaboration, Type II; and decisions that should be parsed into smaller ones and delegated as far down as possible, often to people with clear accountability, Type III.

It is Type II topics that most often hinder organizational agility. Companies that have successfully addressed this problem define

which decisions are best made in committees and which can be delegated to direct reports and to people close to the day-to-day action. They also establish clear charters for committee participants and clarify their responsibilities—avoiding, in particular, overlapping roles. This is the stable backbone. But these companies also make speedy decisions and adapt to changing circumstances: they dynamically rotate individual members of such committees, hold virtual meetings when necessary, and spend their meetings engaging in robust discussion and real-time decision making rather than in sharing information through endless presentations, many dealing with issues that have already been resolved.

Take an energy company which introduced a new approach after realizing that its internal governance was broken. It found, for example, that the executive committee actually had no explicit decision rights: the committee's meeting agenda was set by the CEO's executive assistant after lobbying from individual executives, and the vast majority of meeting time was spent listening and reacting to presentations. To address the problem, the company appointed a chief of staff to manage meetings and declared a meeting-time target of 90 percent dialogue, debate, and decision making. The CEO asked meeting participants to watch recorded presentations as part of their "pre-read," and that alone cut presentations and information sharing to less than 10 percent of the total meeting time. The company also clarified the responsibilities and voting rights of meeting participants and set up a strategy group to engage with a broader set of nonvoting leaders on the more important decisions. Thanks to a new spirit of collaboration and trust, there are no longer "meetings after the meeting" to talk about what didn't come up earlier.

The introduction of a mandate for balanced governance, with a charter and clear decision rights at its core, also had a galvanizing effect on the agility of a major global healthcare business we know. Previously, a simple product enhancement for a particular country required a torturous half-year approval process involving six overlapping committees. Now a single cross-functional team can make this sort of decision in a matter of weeks. (A second team is involved in certain cases, though only to improve coordination, not as part of the decision-making process.) Clear authority thresholds,

below which no higher-level approval is necessary, are in place for product-group leaders. Thanks to greater clarity about voting rights and committee-chairing responsibilities, it is now easy to convene the core team or to make urgent decisions virtually and over the phone.

Process

Much as agile companies underpin the new dynamism with a degree of stability in their structure and governance, they create a stable backbone for key processes. These are usually signature processes, which these companies excel at and can explicitly standardize but are hard for competitors to replicate. In a brand- and innovation-driven consumer-goods company such as P&G, for example, product development and external communication are high on the list of signature processes. Amazon's synchronized supply chain, with its common language and standards identifying clear decision rights and handoffs, is another. In many companies, idea to market, market to order, and order to cash are signature processes. When everyone understands how these key tasks are performed, who does what, and how (in the case of new initiatives) stage gates drive the timetable for new investment, organizations can move more quickly by redeploying people and resources across units, countries, and businesses. In other words, everyone must speak the same standardized language.

When that kind of standardization is lacking, agility suffers. Executives at one highly diversified global technology company we know noted how slowly local units were responding to new initiatives. On closer examination, the leaders discovered that those involved invariably devised their own customized processes as part of any solution. The result? Essentially identical processes had multiple variants, each with its own governance conventions and different and duplicative structures. Employees spent too much time on internal discussions about best practices, methodologies, and process frameworks and not enough on actively improving their own ways of working.

The company has now created a common operational language, codified in one standard process framework for all 60 businesses in its portfolio. It harmonized these processes where feasible but also spelled out the allowable degree of differentiation for business

models or for the needs of specific customer segments. As a result, the company could further simplify and harmonize roles and job titles. It can now execute any operational activity in just seven standard value chains covering 22 processes, such as order to cash.

Extra dynamism comes from two new overarching roles in the organization—those of a business-process owner, who champions and improves each signature process, and an integrator, responsible for cross-functional collaboration, execution, and performance management. The integrator is accountable for meeting specific end-to-end KPIs and targets and for leading cross-functional teams executing processes. The rollout is in its early stages. Nonetheless, there is a growing realization, across the organization, that while the old approach seemed fast and responsive to local needs, the new one enables the company to move even more quickly, without having to change processes constantly.

Performance management is particularly crucial in the context of agile processes. In many businesses, a top-down strategy guides efforts to realize the CEO's and top team's targets, which are cascaded down the organization to business units, smaller units, and ultimately individuals. Along the way, each function, product group, and territory develops its own metrics, often in isolation from—or even at cross-purposes with—other departments working toward the same end. Silos are thus reinforced, and dysfunction rears its head.

One company we know moved from this top-down target-setting approach to one involving a set of performance metrics jointly owned across the value chain. Originally, the sales leaders, rewarded by top-line numbers, tended to inflate inventory needs at the start of a production cycle. Meanwhile, the logistics managers, judged by waste-minimization targets, significantly reduced that figure when they could. The supply chain therefore often exceeded its targets, but salespeople frequently ran out of stock and key customers were alienated. To solve this problem, the company built a few common KPIs (sales-forecast accuracy and customer satisfaction) into the incentives of sales, logistics, and manufacturing managers, so that all functions had some stake in business outcomes. This change laid the foundation for regular team targets, reset every quarter; more frequent performance conversations, both for individuals and

teams; and additional peer reviews—changes that have enabled the company to become more agile.



Agile companies regularly rethink and, if necessary, redesign their structures, governance mechanisms, and processes to strike a balance between speed and stability. But a company attempting to become more agile may find the effort daunting. One critical prerequisite for sustaining real change is putting in place the behavioral norms required for success. This is not about making cultural statements or listing company values; it is, rather, a matter of instilling the right kinds of behavior for “how we do things around here.”

While agile companies seem to share a few behavioral norms, such as a bias for action and the free flow of information, other norms vary according to the nature of the company and the specific recipe it adopts to encourage a healthy, high-performing culture.⁴ The clearer and more widely adopted these kinds of behavior become throughout all levels and units of a company, the easier it will be to change structures, governance, and processes in pursuit of agility. ○

⁴ For more, see Aaron De Smet, Bill Schaninger, and Matthew Smith, “The hidden value of organizational health—and how to capture it,” *McKinsey Quarterly*, April 2014, on mckinsey.com.

The authors wish to thank McKinsey’s Steven Aronowitz, Monica Murarka, Kirk Rieckhoff, and Rob Theunissen for their contributions to this article.

Wouter Aghina is a principal in McKinsey’s Amsterdam office, **Aaron De Smet** is a principal in the Houston office, and **Kirsten Weerda** is a senior expert in the Munich office.