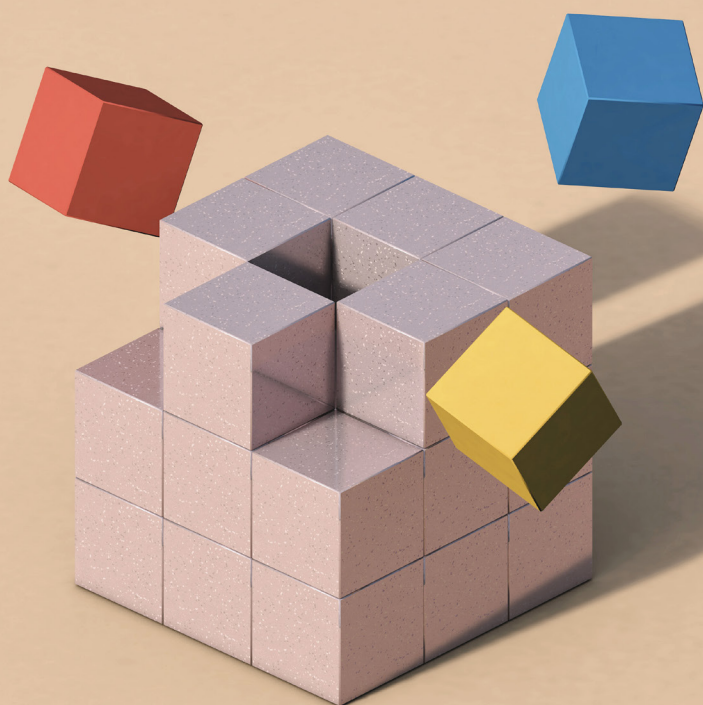


Transformation Practice

How capability building can power transformation

A well-designed program to promote productive behavior and skills can not only energize an organization's workforce but also become an essential element of any successful transformation.

by Hugh Bachmann, Dominic Skerritt, and Elizabeth Young McNally



Picture this: an international manufacturing corporation with thousands of workers is spun off from its parent. In less than a year, its stock price drops more than 80 percent, morale plummets, and measures of the organization's health drop into the bottom quartile of its sector. Something has gone very, very wrong.

Fast-forward four years, and the company's stock price has increased sixfold. A step change in organizational health has taken the corporation from the bottom to the second quartile, with its employees feeling more connected to each other and invested in the success of the company. Plant safety has dramatically improved, with increased discipline and effective risk management. Customers have noticed and celebrated the changes. One even calls the CEO to say the manufacturer will be the customer's preferred vendor going forward.

So what changed? In this real-life example, the manufacturing company undertook a full-scale transformation effort to change its trajectory on performance, organizational health, and one other crucial value-building element we call "capabilities," or the hard and soft skills needed to help organizations reach—and sustain—their full potential.

When it comes to enterprise-wide transformations, we know that most companies miss the mark on capabilities during their initiatives. While the majority of organizations recognize the importance of a skilled and motivated workforce, many don't devote enough time and resources to developing one. The priorities lie elsewhere, and an irreplaceable opportunity is missed. For others, foundational capability building sounds too simple—we are already doing this, a CEO might think. But in our experience, what sounds like common sense is rarely common practice across an organization, and that leaves opportunities to better performance on the table.

Capability building goes well beyond traditional training of employees: it's about fundamentally changing how the work gets done. It's also one of the best ways to energize people, from the C-suite

to the factory floor, to support the transformation in the first place. Without that energy, achieving and sustaining a successful transformation becomes exceedingly difficult—perhaps impossible. But with effective capability building, companies develop the mindsets and behaviors to deliver transformational gains and add to these gains over time, embedding an execution engine for continuous value improvement.

In this article, we explore the essential elements of a robust capability-building program. We show how empowering employees with new skills not only enables sustainable change at scale but also helps the bottom line, as it did during the holistic transformation eventually undertaken by the international manufacturing corporation previously described.

The building blocks of an effective capability-building program

Capability building changes the way people go about their jobs. It strips the workday down to its most basic components and rebuilds it, embedding new habits around timeworn tasks. The lessons can be basic (for example, how to hold a meeting in 30 minutes instead of an hour and how to write the most effective emails) or more sophisticated (for example, how to prioritize responsibilities and how to anticipate, and thus ward off, poor project outcomes). They can also be technical or functional in nature. For example, to create an efficient supply-chain organization, employees can build capabilities in forecasting, segmented networks, demand planning, inventory management, and more. Many of these core ideas sound like common sense, but we've found that they are rarely common practices consistently applied across an organization (see sidebar, "Approaches to closing capability gaps").

Because this disconnect is ultimately behavioral, we turned to behavioral science for solutions. Three key elements are necessary for an effective capability-building program: leadership role modeling, widespread employee engagement, and virtual delivery.

Approaches to closing capability gaps

Closing the loop

At the end of every meeting, its organizer can summarize what needs to happen next, who is doing it, and by when it needs to happen. That approach helps ensure that accountability and the ownership of deliverables are clear. The following is an example of the approach:

- **Situation.** The procurement team at a global manufacturing company finds that initiatives frequently miss deadlines and the ownership of deliverables is unclear.
- **Approach.** During daily check-in calls, the team devotes the final five minutes to deciding on clear actions and identifying owners and deadlines.
- **Impact.** With this added accountability, 90 percent of milestones meet their targeted deadlines.

The ‘premortem’

Colleagues can identify risks and anticipate problems before a project begins. They can then develop plans to prevent or reduce any potential negative impact. The following is an example of the approach:

- **Situation.** The manager of a coastal manufacturing plant recognizes the site’s lack of preparedness should a natural disaster strike.
- **Approach.** To prepare for “doomsday scenarios,” the plant invests in extra equipment and develops special procedures to respond quickly if the site goes offline.
- **Impact.** When a category 5 hurricane makes landfall, the plant is back online weeks ahead of nearby competitors.

Effective meetings

Meetings can play important roles in capability building if they are effective. All participants in a meeting should understand its payoff, purpose, and process; be able to provide input on how it will be run; and know who should do what once it’s over. The following is an example of the approach:

- **Situation.** A healthcare company holds a recurring growth-committee meeting that covers an ever-widening range of subjects discussed at executive-committee meetings.
- **Approach.** The top team sets clear agendas for both committees’ meetings, streamlining how decision and growth priorities are made.
- **Impact.** Meetings run on time and without redundancy, and decision rights for participants are clear.

Role modeling

Research tells us that people mimic—both consciously and unconsciously—the actions of the individuals and groups around them. One of the best ways to drive the adoption of new mindsets and behaviors is by ensuring that senior leaders model the desired change.¹ When employees see highly visible colleagues behaving differently, it reinforces the new way of working and signals a commitment to the transformation.

Indeed, when senior leaders role model the behavior changes they’re asking employees make, transformations are 5.3 times more likely to be successful. This means it’s often best for senior leaders to be the first participants to complete a capability-building program.

This was the case at the international manufacturing corporation mentioned previously. When executives first took the pulse

¹ In both research and practice, we find that transformations stand the best chance of success when they focus on four key actions to change mindsets and behaviors: fostering understanding and conviction, reinforcing changes through formal mechanisms, developing talent and skills, and role modeling. Collectively labeled the “influence model,” these ideas were introduced more than a dozen years ago. Emily Lawson and Colin Price, “The psychology of change management,” *McKinsey Quarterly*, June 1, 2003, McKinsey.com.

of its employees, the company scored in the bottom quartile of McKinsey's Organizational Health Index (OHI).² Survey results and further discussions showed that many employees lacked trust in top management as the organization's financial position deteriorated. Leaders weren't communicating their goals or progress clearly, and no one was accountable for results.

By role modeling new norms, senior leaders helped rebuild trust in the organization and the transformation itself—capability building included. By changing their own behaviors, they signaled to the organization that this change was real, thereby building trust.

The company's former chief transformation officer recalls that employees were convinced that capability building was a worthwhile endeavor only when they learned that they could trust what management was saying. "Management had to actually do things that were different, show some evidence of change, take some risks."

The CEO joined in as well, attending many of the capability-building workshops that the company held and interacting with employees across role levels around the world. Employees, watching closely, responded in kind when it became clear how important the program was to the boss. A virtuous cycle of encouragement and recognition was born. The CEO even began calling employees directly if they did something well or demonstrated the behaviors that the program was trying to enforce. To this, frontline employees at first expressed disbelief. Some actually hung up on the CEO, thinking that the call was a prank. When it became clear that it wasn't, employees proudly related the turn of events to one another.

Not all top managers readily accepted the program, however. For one, the company's head of talent,

a key player, was skeptical. He thought that the skills felt too basic and that the company was already doing enough. He changed his mind when he realized that however simple the capabilities may have sometimes appeared, the organization didn't consistently apply the skills effectively, which dragged down productivity, reinforced silos, and generally short-circuited the value building, threatening the ultimate aspiration: the success of the broader transformation.

Widespread employee engagement

For capability building to occur, transformation-program participation must be sufficiently widespread. Even when propelled by top-level buy-in, capability building still needs to be scaled well beyond a few rounds with a chosen few because employees who aren't included in a transformation feel disengaged, disconnected, and left behind. Anything less than broad engagement defeats the purpose.

In fact, we've found that to create the foundation for truly widespread change, a capability-building program must directly engage at least 25 percent of the workforce. In our experience—and in behavioral-science research—this is the tipping point that must be reached for a minority of employees to create a new cultural norm.³ In other words, by engaging at least 25 percent of employees, the critical mass of the workforce can overturn deeply embedded behaviors within the organization and enable transformational change to scale across the enterprise.

To inspire behavioral change in all levels of an organization, a capability-building program ought to start by targeting the organization's top influencers. Those people, whatever their rank, should be among the first to go through it. The idea is that these influencers will serve as evangelists for the new ways of working. Influencers can

²OHI by McKinsey is a benchmark that provides company leaders with a detailed picture of their organizations' health compared with peers. With more than one billion data points across geographies and industries, it offers a global standard to measure and manage organizational health.

³Damon Centola et al., "Experimental evidence for tipping points in social convention," *Science*, June 8, 2018, Volume 360, Number 6393, pp. 1116–9, science.sciencemag.org.

inspire their colleagues to change through use of personal anecdotes and compelling arguments.

Before the COVID-19 pandemic limited in-person learning, one global manufacturing organization asked the head of each of its production plants to complete the company's capability-building program and then lead in-person workshops on the skills for the employees in their plants. Most of these production chiefs had no formal experience as facilitators or public speakers, but their influence was felt across each of their sites. As one frontline employee said later, "The power of this program was not just that I got to spend time in the same room with the factory head, but they were actually supporting me to grow—supporting me to improve and do my job better."

The struggling international manufacturing corporation presented as our first example also took the influencer approach to heart. It made sure to run workshops in a number of locations around the world, and at least two members of its executive committee attended each one. The company was sending a message: we care about you and your development.

Shaping a new learning environment:

Virtual delivery

Shaping the learning environment is another essential part of capability building. In the age of the COVID-19 pandemic (and in all likelihood, going forward), that means capability building must be deployed primarily through virtual means. Fortunately, capability building easily lends itself to virtual learning.

Moreover, there is evidence to suggest that virtual environments can deliver experiences that are equivalent to or better than those of traditional in-person programs and workshops. Some 87 percent of participants in newly adapted virtual experiences in recent months agreed that the programs were at least as effective as in-person events would have been.

Perhaps the most significant aspect of a virtual capability-building program is the opportunity

for global reach. At multinationals, it's paramount that as many employees as possible, in every geographical nook and cranny, have the opportunity to learn and embed new skills. In the more traditional in-person workshop protocol, as meritorious as it is, that's very hard to achieve because of logistics and cost; imagine flying thousands of people in and out of regional hubs.

For the international manufacturing corporation's head of talent, the program's digital evolution was a game changer, solving any concerns over the breadth of participation. "After the first few in-person workshops, people were knocking down my door to get in. The program had gone from 'this is too simple and doesn't make sense to me' to 'Why am I not invited to this workshop?' Once we launched the digital program, it was available to everybody."

Because of a transnational nature, live virtual learning allows for a greater and deeper level of feedback. Chat functions in videoconferencing platforms enable participants to converse easily and ask real-time questions in ways that would be too disruptive in a conference-room setting. Virtual formats also allow for configuration and tailoring. When the transforming manufacturing company launched its digital program, lessons were translated into multiple languages, reinforcing, once again, the underlying message: management is investing in you.

Capabilities and transformation

Typically, there are four sequential capability-building steps in supporting a successful transformation. First, individual employees learn new capabilities. Second, teams apply them, and capabilities and behaviors change. Next, the organization begins to see improving effectiveness. Finally, the company achieves its financial aims and other goals.

Knowing this, it would seem that adopting a capability-building program would be common sense. However, as noted, it's not at all common practice. Unfortunately, the reasons that companies don't prioritize capability building—the learning outcomes are too basic or too distracting or a

key C-suite player just isn't interested—amount to lost opportunities and leave the outcomes of transformation programs to chance.

At the same time, organizations that prioritize skill building often have programs that are ineffective. In a recent McKinsey survey of 1,240 business leaders around the world, nearly 80 percent—up from 59 percent before the COVID-19 pandemic—said capability building is extremely or very important to the long-term growth of their companies. Yet just one-third of these respondents believed that capability-building programs are often or always successful in achieving their objectives and business impact.

The international manufacturing corporation's experience, however, shows how a robust capability-building program can propel a transformation. As noted previously, the company had landed in the bottom quartile on its OHI score. But within four years of the transformation's start, the company's score had more than doubled, placing the organization in the second quartile.

On the ground, the issues with accountability and business-unit communications that were at the forefront of the company's problems both changed for the better. Newly engaged employees generated almost 5,000 ideas for improvement, many of which impacted the company's bottom line.

Those ideas for improvement brought great value to the corporation and vested more people in its success. As the company's former chief transformation officer put it, "We can't see everything from up here. Great ideas often come from other parts of a company. Through capabilities, management can give frontline employees a process to take an idea, champion it, and get recognized for the work."

Other data underscored the importance of capability building in a transformation. The capability-building program's module on effective meetings freed up 2 to 3 percent of the time

on employees' calendars. That may not sound like much, but when applied for a year across a company with thousands of employees, that's a lot of time that can be used for more productive work or even personal activities.

Compared with peers, the company became more nimble thanks to its capability-building efforts. In one instance, a group that had taken "premortem" coaching in the capability-building workshop sat down to forecast what black-swan events might adversely affect the plant over the course of the ensuing year. One of the answers was a category 5 hurricane, which isn't an everyday (or even annual) occurrence. Planning for that contingency, the company bought extra equipment and developed special procedures, just in case. When such a hurricane actually did occur, the plant came back online weeks before those of nearby competitors did. Implementing the transformation and the capability building that supported it also correlated with a sixfold increase in share price in fewer than four years.

Anecdotal evidence aside, research points to the power of capability building. A recent McKinsey analysis of organizations undergoing at-scale transformations showed that the proportion of employees engaged in capability building during transformations has an effect on improvements in organizational health (Exhibit 1).⁴ Organizations exposing at least 10 percent of their employees to such programs were twice as likely to improve their OHI scores as were organizations that didn't. The average rate of improvement was nine percentile places—versus no improvement at all. Organizations that included upward of 30 percent of their workforce in formal capability-building programs improved their OHI scores by an average of 12 percentile places.

The economic benefits are also real (Exhibit 2). Our analysis of 38 publicly listed companies showed that when companies included more than 30 percent of their workforces in capability-building programs, they enjoyed total returns to shareholders that were 43 percent above

⁴ To understand the impact of capability-building programs on organizational health, we identified 22 organizations that had launched at-scale transformations and measured their OHI scores at transformation beginning and end. We then compared each company's change in OHI scores with the proportion of its employees who were engaged in capability-building programs during the life of the transformation.

Exhibit 1

Companies with capability-building programs in their transformations make greater improvements in organizational health.

Improvement in Organizational Health Index scores of employees engaged in capability-building programs, %



Source: Organizational Health Index by McKinsey; McKinsey analysis of 22 organizations undergoing at-scale transformation

Exhibit 2

Companies with capability-building programs in their transformations deliver better total returns to shareholders.

Excess total returns to shareholders (TRS) by extent of capability building as part of transformation, TRS peer index, %



Source: Organizational Health Index by McKinsey; McKinsey analysis of 38 publicly listed companies that conducted at-scale transformations for a measurable 18-month period and had TRS that could be paired with a representative off-the-shelf sector and geographic stock index

benchmarks after 18 months.⁵ Just as important, the benefits flow both ways: employees are excited to develop valuable new skills and knowledge.

Transformations are difficult to execute and even harder to sustain. Tens of thousands,

sometimes hundreds of thousands, of employees need to be engaged and aligned, regardless of where they live, the language they speak, or the culture they know. Effective capability-building programs enable organizations to develop the mindsets, behaviors, and skills needed to power a transformation and achieve their full potential.

⁵To understand the economic benefit of capability-building programs on organizational health, we identified 38 publicly listed companies that went through at-scale transformations for a measurable 18-month period and whose total returns to shareholders (TRS) could be paired with a representative off-the-shelf sector and geographic stock index, which allowed us to measure excess TRS against the index for a 18-month period following the launch of a transformation. Each of the 38 companies was compared with its own appropriate index by sector and geography for the same period.

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