

Capability for Performance



Four top-team imperatives for capability building

August 2012

Stephen Bear

Richard Benson-Armer

Tomas Koch

Jonathan Kolodny

Contents

Four top-team imperatives for capability building

1. Identify and quantify the capabilities that are holding you back	1
A snapshot of the C4P framework	2
2. Invest in experiential programs and other adult-learning techniques	3
3. Take a smart approach to piloting	4
Inside the capability center	4
4. Make continuous improvement a part of the company's DNA	5

Four top-team imperatives for capability building

If there were ever a time when companies could rest on a distinctive set of capabilities and enjoy a competitive edge, it has long passed. By capabilities, we mean not only the practical and leadership skills individuals need to do their jobs, but also the overall institutional capabilities (core knowledge and processes, experience, proprietary methodologies, governance structures, and so on) that are needed to sustain performance. Technology, consumer tastes and behaviors, global markets, and the competitive environment are among the factors that today are changing faster than ever before. To keep pace—and to stay ahead—organizations must constantly renew their capabilities and anticipate future needs.

From years of research and experience working with companies in all industries around the world, we have developed an approach called “capability for performance” (C4P), which enables sustainable capability building and improved performance with great emphasis on speed and scale. This distinctive approach, which is explained in our recent publication, *Capability for Performance: The path to excellence*,¹ focuses on employee-led initiatives—programs owned and led by line managers who have direct responsibilities for their own profitability—and uses the latest thinking in adult learning to deliver results (see Box, “A snapshot of the C4P framework”). Our approach helps to ensure that individual skills are developed in the people who will need them; it also delivers performance improvements that add to the bottom line and builds the institutional capabilities needed to sustain these improvements.

But despite its employee-led nature, our approach is heavily dependent on the company’s top leadership. The CEO and the top team must set the stage for a successful program launch and rollout. This article reviews four critical imperatives for this type of direction setting: identify and quantify the capabilities that are holding you back, invest in experiential programs and other adult-learning techniques, take a smart approach to piloting, and make continuous improvement a part of the company’s “DNA.”

1. Identify and quantify the capabilities that are holding you back

Our research shows that organizations that expressly develop the capabilities required to meet their aspirations are seven times more likely to succeed than those that do not.² The research also indicates that when senior leaders set the agenda, it is more often explicitly linked to immediate business goals than when others take the lead. In setting the agenda, high-level leadership often designs a targeted, comprehensive, and effective program that develops the skills needed to meet strategic goals.

Why are top leaders better than others at designing the agenda? In large part, because they have a strong firsthand sense of the missing corporate and functional capabilities that are keeping the organization from meeting its financial and growth aspirations. But that intuition is not enough. Executives should calculate the performance improvement—with regard to increased revenues and margins, productivity improvements, cost savings, or other tangible measures—that should result from building these capabilities. This can be done by evaluating current performance either at a high level (using peer benchmarks, for example, to compare the company’s manufacturing costs or sales, general, and administrative costs as a percentage of revenue) or in a more detailed, bottom-up manner (for instance, by conducting an assessment of the company’s procurement practices in each product category and comparing that performance with relevant benchmarks).

This exercise reveals actions that will drive value and highlights capabilities with the greatest potential to contribute to performance. The company should then adopt a “less is more” attitude, focusing its efforts on this limited set of critical capabilities.

Having gone through this exercise, the company in Exhibit 1 identified sales-force effectiveness as its number-one priority. Other areas of opportunity to prioritize included pricing excellence, supply-chain redesign, procurement improvement, and maintenance effectiveness. By attaching quantified goals

¹ Stephen Bear and Tomas Koch, *Capability for Performance: The path to excellence*, May 2012.

² “What successful transformations share: McKinsey Global Survey results,” mckinseyquarterly.com, March 2010.

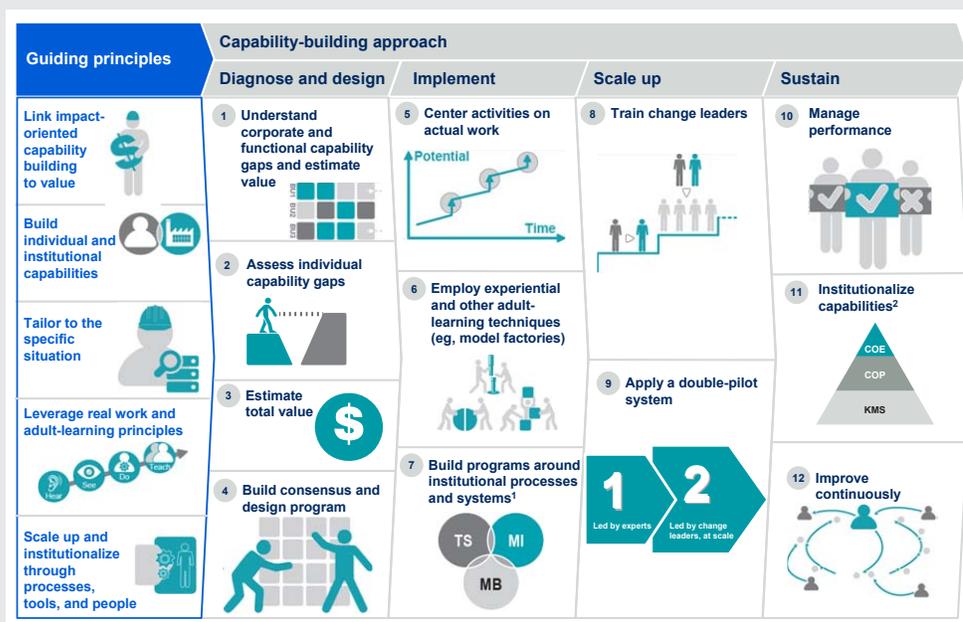
A snapshot of the C4P framework

The “capability for performance” (C4P) framework (exhibit) draws from McKinsey’s experience working with companies around the world and in all industries on capability-building programs that have produced sustained improvements. The framework is structured around five guiding principles:

- Capability building must be firmly linked to value generation and business impact, showing clear results in day-to-day work that can be sustained over time.
- Capabilities must be built within individuals who work better as a result and within groups of individuals who function better as a team. Capabilities also must be built within institutions—within functions or business units, for instance—that use improved processes, support systems, and other measures to perform better.
- Efforts to build relevant capabilities must be tailored to each organization’s unique starting point.
- Programs must be founded on modern principles of adult learning, which show that adults respond best to self-directed learning that is active; based on experiences, real-life tasks, and immediate problems; and focused on finding solutions and building skills.
- Although external experts might guide a program in its early stages, internal change leaders, relevant tools, and supporting processes are necessary to build sustainable capabilities throughout an organization.

By incorporating these principles into each of the 12 elements of the program (which are implemented in four stages—diagnose and design, implement, scale up, and sustain), we ensure that the effort and resources invested have the greatest potential for generating quick and sustainable performance improvements.

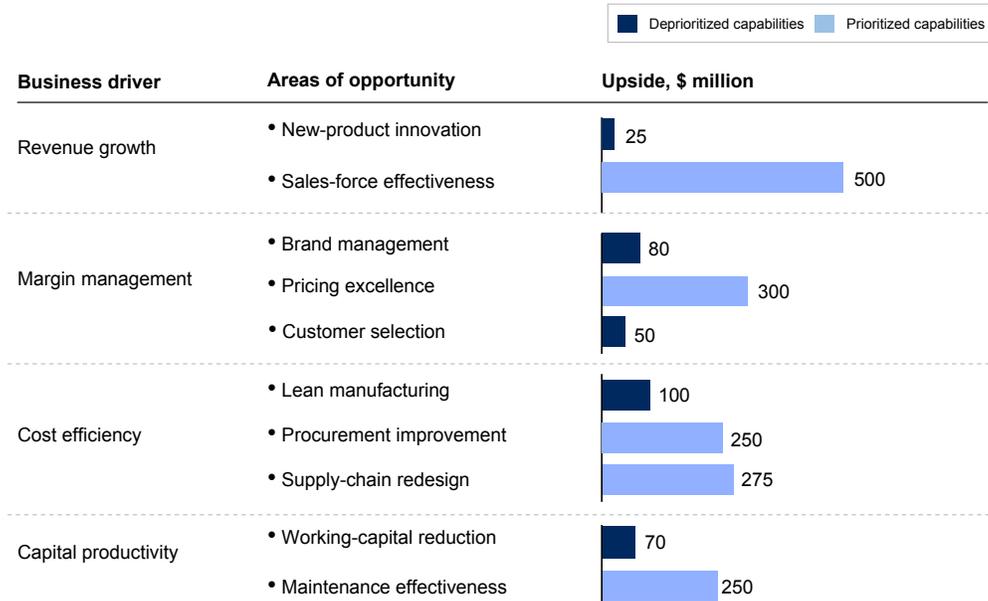
Exhibit Five principles guide the ‘capability for performance’ approach.



¹ TS = technical systems; MI = management infrastructure; MB = mind-sets and behaviors.

² COE = centers of excellence; COP = communities of practitioners; KMS = knowledge-management system.

Exhibit 1 Leaders must set aspirations and identify potential upside.



to each opportunity, the process ensures that success has the most significant impact on the bottom line and that capability building does not devolve into an exercise for its own sake.

Next, leaders must identify the capabilities employees need to produce improvement in the prioritized areas. The company performs an assessment of employees’ capabilities, compares them with industry benchmarks, and quantifies how much those improved capabilities will be worth. In Exhibit 2, for example, the two types of capabilities related to sales-force effectiveness in which the company’s employees are particularly weak—acquiring new accounts and up-selling—also can provide the most revenue growth.

2. Invest in experiential programs and other adult-learning techniques

In many cases, employees cannot immediately apply their new skills in real work situations, and so it is difficult to reinforce their new capabilities. Experiential learning and other techniques

can be helpful here—more so than lectures or demonstrations. One study found that after three months, people retained only 10 percent of the small, simple chunks of information they had been taught through oral methods. When visual teaching methods were used, retention rates after the same period increased to 32 percent. And when people learned the same information by doing, they remembered 65 percent of it.³

To ensure that the organization builds enduring capabilities, the top team should make the decision to invest in experiential programs. These programs come in a variety of forms, including boot camps (an immersion classroom-learning experience combined with fieldwork), simulations and role-playing games that provide exercises for practicing a new skill, and e-learning (self-paced modules that individuals can complete at their own pace on their computers). They allow participants to experiment with new ideas in a risk-free atmosphere and to test-drive tools and processes before using them in their daily work.

One valuable technique employs capability centers, which can include model factories (with shop floors that produce straightforward goods such as tripods or electric motors),

3 John Whitmore, *Coaching for Performance*, 3rd ed., Boston: Nicholas Brealey Publishing, 2002.

Exhibit 2 Focus on the capabilities that will drive the most value.

Increase revenue	Required capabilities	Estimated growth potential	Capabilities assessment
Increase share in core clients	<ul style="list-style-type: none"> Deep understanding of customer needs and direction—building rapport Objection handling 		
Penetrate new categories	<ul style="list-style-type: none"> Understanding customer needs Articulating a tailored value proposition Objection handling 		
Develop solutions for key accounts	<ul style="list-style-type: none"> Consultative skills to understand needs and shape agenda Navigating the organization and developing supporting tools 		
Acquire new accounts	<ul style="list-style-type: none"> Prospecting effectively Prioritizing accounts Allocating time for hunting activity 		
Focus on up-selling	<ul style="list-style-type: none"> Probing for needs and filling the needs Selling value vs price Closing 		

design labs for product development, functional back offices (in areas such as banking and service operations, for example), and other work environments. In the model factory, for instance, by rearranging assembly or tooling processes and seeing the result, trainees can use their new capabilities in actual production settings. Volkswagen’s leadership team decided to invest in developing “lean centers” where participants can test different production improvements for impact on efficiency, quality, and ease of use. Capability centers can create a diverse range of learning-by-doing situations in which trainees are confronted with a problem, work out a solution, and discover its impact (see Box, “Inside the capability center”). Often, opportunities for participants to apply these capabilities within their organizations come within days of completing the program.

3. Take a smart approach to piloting

The running of pilot projects is a well-known method for developing new capabilities. Pilots are designed to address directly the improvement or savings opportunity that executives have prioritized and then allow employees to exercise their skills in real work situations. As such, these

Inside the capability center

McKinsey is involved with multiple capability centers around the world, in some cases with partners such as universities. Three of these, described below, are located in Atlanta, Munich, and Singapore. The Atlanta center⁴ focuses on manufacturing operations (continuous flow and batch manufacturing), call centers, and service operations. The Munich center⁵ provides training on such things as improving performance of manufacturing lines, applying lean principles at a model financial institution, building leadership skills for hospital staff, and running a “green” factory. It also allows senior executives to deepen their understanding of digital marketing by shaping the marketing decisions of an operational online business and then watching actual customer reactions. The Singapore center is dedicated to building green capabilities, with a focus on process industries.⁶

4 For more on the Atlanta center, see mckinsey.com/client_service/operations/expertise/model_factories.

5 For more on the Munich center, see capability-center.mckinsey.com.

6 For more on the Singapore center, see greencampus.mckinsey.com.

projects build leadership and functional capabilities while delivering bottom-line performance improvements. And integrating capability-building programs into real work situations also helps make breakthrough projects a way of life within an organization, particularly among leadership trainees.

A problem that often arises, however, is that leaders get impatient about completing a pilot program because they want to press on with broader implementation. But experience shows that driving change too quickly can derail the process. In many instances, high success rates in pilots are produced by a significant investment of resources, management attention, and outside expertise. Such pilots, it seems, can never fail. But in a normal situation, where pilots must compete with other groups and projects for resources and attention, and leaders with multiple responsibilities drive the effort, results can be very different.

Our approach incorporates a double-pilot system that corrects for these flaws by proving the concept in an initial pilot guided by external experts and then demonstrating through a second pilot led by company managers how the program can be scaled up. Top executives should insist on this second pilot to ensure that their teams have gained the necessary capabilities and can lead the rest of the change effort themselves.

Equipped with ample resources and executive attention, the first pilot tests the technical solution. In this pilot, less energy is given to testing the changes needed in management infrastructure or “soft” elements of the rollout. Its main objective is to ensure that the skills being built have a demonstrable business impact.

The second pilot takes a broader look at the program’s ability to scale up by testing it under normal working conditions, at several locations at once, with ordinary, steady-state funding and resource allocations and with outside experts shifting to a role in which they coach company managers who will lead the future rollout. Management-infrastructure and human-resource capabilities are tested more acutely during this pilot and refined as needed. If successful, the program is ready to be rolled out throughout the organization led by the newly trained change leaders.

A double-pilot system was instrumental in helping a European health care provider increase the time medical staff spent on patient care. After a successful initial pilot at one location,

the organization created an “industrial strength” model that was robust enough to be rolled out more broadly, and then tested it in a second pilot at multiple sites. This “go slow to go fast” pacing led to rapid acceptance of the program when it was rolled out across the organization. In other cases, the second pilot has shown that newly trained change leaders take longer to lead the same activities that had been led by external experts during the first pilot. For subsequent waves of the rollout, the organization builds in more time for groups of new change leaders to embed their skills in their daily work.

4. Make continuous improvement a part of the company’s DNA

Once all the initiatives are in place, leaders must ensure that the organization can sustain and build on early gains by instilling a culture of continuous improvement. Often, this means that people throughout the organization must change their mind-sets and behaviors; new attitudes must be internalized and not simply mimicked. This change must start with four roughly concurrent actions by the top team.

The first of these four actions involves much of what we have been discussing already—the creation of a capability-building program that helps employees develop relevant skills and gives them the opportunities to behave in the new way. Second, leadership must create a compelling case for change that clearly communicates what people are expected to do in a way that makes sense. Third, these executives need to ensure that the company’s structures, processes, and systems are aimed at driving change—usually through a performance-management system that integrates business and personal performance metrics and evaluates short-term performance and long-term health. These metrics must cascade throughout the organization, from the executive suite to the shop floors and cubicles, and they should be supported by tracking systems that help reward superior performance or mete out consequences for poor performance. Finally, the top team needs to role model the new behaviors. If everyone else is expected to change, management must lead by example.

To track ongoing progress, the organization should establish a cadence of meetings and review sessions at the right intervals that will allow for course corrections when needed. At the frontline level, for example, review sessions may happen daily. For middle management, results might be summarized in a

weekly meeting. And for the top team, aggregate results might be reviewed every two weeks, or even once a month. The top team's key role here is to keep the pressure on by monitoring the few things that make the biggest difference to the company's bottom line, following up with those accountable for initiatives that may be stalling and asking what they can do to help.



Our experience has shown that capability building can create longer-lasting impact when the program is tailored to the needs of the organization, incorporates experiential learning, and is

rolled out through a double-pilot approach, as well as when the organization creates the necessary infrastructure to ensure continuous improvement. Leaders also must recognize that launching an institutional capability-building program that brings rapid and sustainable performance improvements calls for courage, conviction, and commitment: courage to step beyond comfortable, short-term measures and embrace new approaches, applications, and technologies; conviction in the organization's readiness to change and ability to reach a higher level; and commitment to make it happen by investing time and resources to develop the capabilities to create and sustain change.

Stephen Bear is a director in McKinsey's Toronto office, **Richard Benson-Armer** is a director in the Stamford office, **Tomas Koch** is a director in the Seoul office, and **Jonathan Kolodny** is a director in the Tel Aviv office. Collectively, the authors lead McKinsey's C4P initiative in the Americas, Asia, and Europe.

Contact for distribution: Patti Schaar
Phone: (216) 274-4574
E-mail: Patti_Schaar@mckinsey.com

