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Voices on transformation

Insights from business leaders on creating lasting change

Voices on transformation is written by experts and practitioners in McKinsey & Company's Organization practice. To send comments or request copies of this edition or previous ones, e-mail us at Organization_Practice@McKinsey.com or visit mckinseyquarterly.com/voicesontransformation.

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How healthy is your organization?

Just like a person, an organization can be healthy or unhealthy. And like many people, a lot of organizations don't pay as much attention to their health as they know they should. People shun vegetables and exercise; companies don't ask if they have the capabilities and qualities they need to deliver strong performance over time.

Yet maintaining an organization's health is more important—and harder—than ever at a time when the business environment is changing profoundly. The mix of qualities that define organizational health may differ from industry to industry; an Indian heavy manufacturer and a European government have very different vital signs. But the process of identifying the right capabilities, building them, and creating the leadership and other skills to go on improving is markedly similar. And all organizations—in both the private and public sector—can do so.

This fourth edition of *Voices on Transformation* shows how. In the article "Creating lasting change," we offer our view of how organizations can simultaneously improve both their performance and their health. Our perspective is distilled from work with clients, interviews with leading CEOs, and surveys of thousands of executives from around the world. The change process has five steps: setting an aspiration for performance and health, assessing current capabilities and mind-sets, defining an integrated program for change, implementing it with rigor and in a way that renews energy throughout the process, and ensuring that the organization can build on its gains through a continuous-improvement infrastructure and skilled leadership.

The issue also includes "How centered leaders achieve extraordinary results," which underscores McKinsey's latest insights on how the personal capabilities of our centered-leadership model help leaders succeed. Centered leaders can build strong teams, encourage employees to overcome their fears, and maintain passion and energy in even the most challenging times. These qualities, in combination with

the more traditional leadership skills such as strategic thinking, problem solving, and financial acumen enable women and men to achieve and sustain company-wide change successfully.

We are also happy to share a collection of four interviews featuring senior public- and private-sector leaders who discuss their change journeys and how they have led them. A. M. Naik, of India's engineering and construction giant Larsen & Toubro, explains how he involved some 7,000 employees in developing the change aspirations that the company has implemented over the past decade.

Jeroen van Breda Vriesman, of the Dutch insurer Eureko, discusses rolling out a lean transformation from one division to all of the company's 20,000 employees—and even to its partners. Goran Persson, the former prime minister of Sweden, recounts how he led a radical improvement in public-sector finances during a crisis. And Pierre Beaudoin, of the Canadian aerospace and transport firm Bombardier, explains how he's built capabilities that help the company continually improve its performance.

Taken together, we hope you'll find this edition to be valuable input as you improve the performance and health of your organization.

Scott Keller
Director, Chicago office
December 2010

Creating lasting change

Mary Meaney,
Caroline Pung, and
Sarah Wilson

Companies that focus on the capabilities and culture supporting long-term performance in corporate transformations are likelier to succeed—and to build the basis for lasting improvement.

To thrive amid our dynamic economic, political, and social climate, organizations must be able to adapt. But organizational transformations are tough: both our research and that of others consistently show that only about a third of them succeed in reaching their targets.

We know companies can do better. The key, our most recent work shows, is to focus not just on short-term performance gains, as many companies do, but also on what we call "health": the underlying working practices and capabilities that allow companies to perform well over time. It seems counterintuitive to suggest that a transformation should have aspirations that are more, not less, complex. But we find that companies focusing on both performance and health are more likely to succeed—one and a half times likelier than those focusing on performance alone—and to build capabilities that will help them thrive in the future.

There's no single right way to implement change. Over the years, we've identified a clear set of strategies—such as setting aspirational targets, developing strong leadership and a clear structure for the transformation, and engaging the whole organization—that are important throughout any change process. Many companies, we find, tend to focus on either the process elements or the people ones. Our newest work shows not only how important it is to include both but also which tactics the companies that have been most successful at transforming performance *and* health have used most often. We have also defined a series of questions executives can ask to help shape and maintain a focus on health throughout the transformation. Organizations that have taken this approach offer guidance for others.

Why health matters

Companies that focus on building and sustaining their own organizational health—not just on next quarter's results—are the companies that can create value over time. Long-term value creation allows them to reward not only their shareholders but also their employees, stakeholders, and society at large—and to position themselves to respond to changing times. This truth has long been clear to most executives, and over the past decade, McKinsey has pinned down nine aspects of organizational health that make the greatest difference to sustaining financial performance.[1] Of course, which of these is most important will vary from one company to another—an established heavy manufacturer is very different from a software start-up.

Despite these variations, we define organizations as healthy when they can align, execute, and renew in three areas—strategic, organizational, and operational—to deliver continuously strong financial results. Organizational alignment, in its most powerful form, requires that employees fully understand and be truly committed to the organization's goals so they can contribute to them autonomously and creatively. Execution is the ability to operate at a level that meets current goals. Renewal requires an organization to have in place the systems, processes, and behavioral norms that enable it to understand, interact with, and adapt to its situation and external environment. In a nutshell, health is as much about what an organization has as about what it *does*.

When a company is contemplating a major change for any reason—even dealing with a crisis—it's crucial not to lose focus on health, which is both a means and an end in a transformation. A recent McKinsey survey of executives, for example, shows that 42 percent of companies that aspired to transform their health along with their performance were very or extremely successful in meeting their goals, compared with only 27 percent of those that aimed to change performance alone.[2]

The reason is probably that companies focusing on health were likelier to take actions, throughout the change process, that we know are tied to success—actions such as understanding their

[1] McKinsey has identified nine organizational health indicators that are statistically linked to above-median earnings before interest, taxes, depreciation, and amortization (EBITDA): accountability, capability, coordination and control, culture and climate, direction, external orientation, innovation and learning, leadership, and motivation. See Aaron De Smet, Mark Loch, and Bill Shaninger, "The link between profits and organizational performance," mckinseyquarterly.com, August 2007.

[2] The online survey, in the field from January 19 to 29, 2010, collected 2,502 responses from executives representing the full range of industries, regions, functional specialties, and seniority.

strengths as well as their weaknesses while planning the transformation, and defining which capabilities they should build to ensure success. Further, companies where change programs included health-focused initiatives (such as programs to change employee mind-sets and behavior) in addition to performance initiatives were twice as successful as the others. Executives at companies that successfully met a dual performance-and-health aspiration were much likelier than others to say that the transformation had increased their leadership capacity and their ability to improve constantly (Exhibit 1).

Five steps to healthy change

A transformation is a hectic and often stressful time, and it is only too easy for an organization's leaders to lose focus. It is thus essential to have a methodology for addressing organizational health in a change effort—a methodology that is just as rigorous as the more familiar approaches used to drive performance (such as lean or Six Sigma).

We have identified five questions executives should ask as they seek to transform an organization; the answers will define both the steps needed to achieve change and the elements of health most important to that organization. These questions are (1) "Where do we want to go?" (2) "How ready are we to go there?" (3) "What do we need to do to get there?" (4) "How do we manage the journey?" and (5) "How do we keep moving forward?" Companies in many different industries and regions have used this five-frame approach to guide successful change. In what follows, we will describe in detail the experience of a North American financial-services company that focused on health as well as performance in a recent successful transformation.

The other crucial aspect of successful transformations is more familiar: using a range of change-management strategies from planning through implementation.[3] The new survey results show us how the high performers—companies that focused on transforming both performance and health and were very or extremely successful at meeting their goals—did it. One important point is that these companies made greater use of many more change-management tactics at all stages of their effort than less successful organizations did, thus ensuring that they focused on people and process at each stage (Exhibit 2).

Where do we want to go?

At the financial-services company, a change in leadership triggered an assessment of current performance and trends. Although the company had performed very strongly for years, it faced several challenges, including aggressive new competitors and a growing expectation among customers that interactions with a financial-services company would be as easy and service-oriented as those with retailers.

The CEO recognized that the strengths leading to success in the past were different from those needed to win in the future. He insisted that the company expand its planning not only to set specific targets for improving key performance metrics (such as attrition and the company's share of customers' business) but also to be equally thoughtful about which capabilities it would need to be healthy enough to adapt and thrive in the new environment.

In looking at the elements of health most important to such a company now, he found that it needed to improve its understanding of the external world and increase its responsiveness to change. The CEO worked with his senior team to define clear, specific targets for improvement in all areas—for example, increasing the organization's ability to understand and respond to customer trends was given as much weight as short-term goals. Setting such clear aspirations is very important in ensuring that a company as a whole is aligned with a transformation's goals. Three-quarters of the survey's high performers,

[3] See, for example, Josep Isern, Mary C. Meaney, and Sarah Wilson, "Corporate transformation under pressure," mckinseyquarterly.com, April 2009. That article described six groups of tactics that were most often tied to successful change: strong leadership; clear, stretching aspirations; and clear process, as well as three for maintaining organizational energy. Companies that used none of these succeeded in only about 15 percent of all cases, while those that used all of them succeeded in more than 80 percent of all cases.

Exhibit 1

Success in achieving both performance and health raises the likelihood of an increased capacity for leadership and continuous improvement.

For respondents reporting transformations with successful outcome

Source: 2010 McKinsey performance transformation survey for example, defined both performance and health clearly; that was true of less than a third of the others.

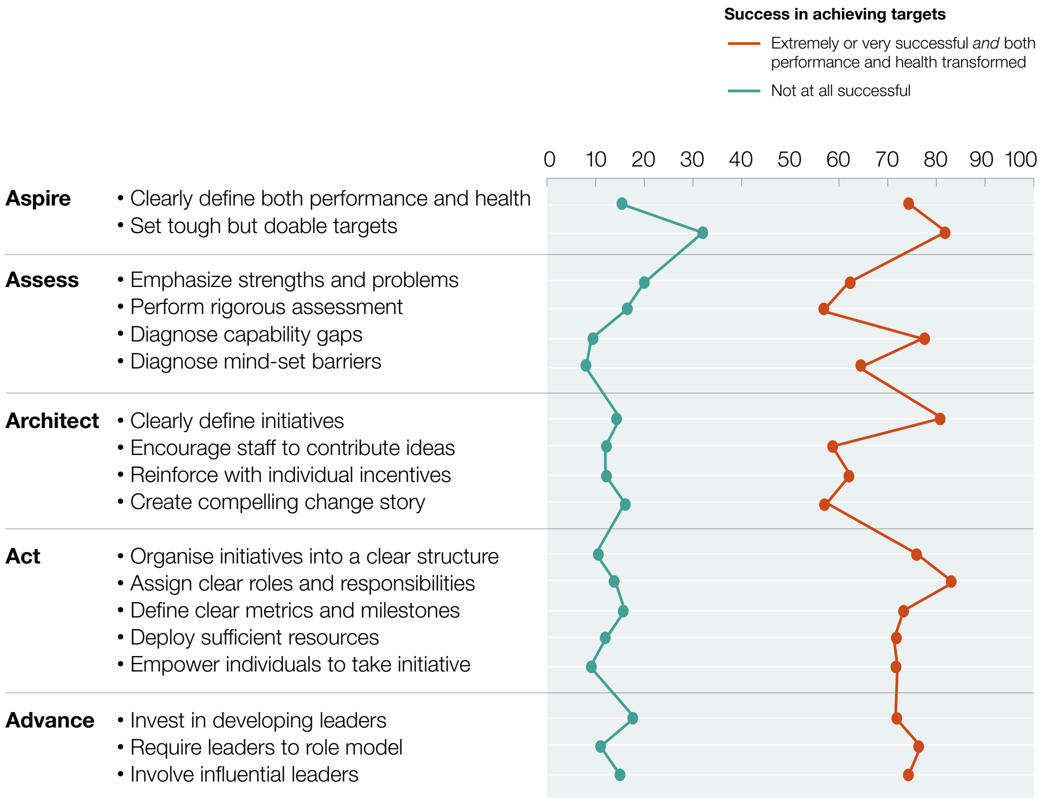
However, an important nuance about targets emerged from the survey. The management literature often talks about the need for "stretch" targets—and indeed our own work[4] has highlighted the importance of ambitious goals—but the need for a degree of realism is often overlooked. Our new research shows that respondents whose companies set "tough but doable" targets were 1.6 times more likely to succeed than those with targets that "felt impossible to reach." Eighty-two percent of the high performers set such tough but doable targets; on the other hand, we have encountered many companies where transformations failed because leaders fell into the trap of overly ambitious targets backed by little more than inflated rhetoric.

[4]See Josep Isern, Mary C. Meaney, and Sarah Wilson, "Corporate transformation under pressure," mckinseyquarterly.com, April 2009.

Exhibit 2

In comparison with less successful organizations, high performers made greater use of many more change-management tactics at all stages of their efforts.

% of respondents reporting use of tactic in transformation[1]



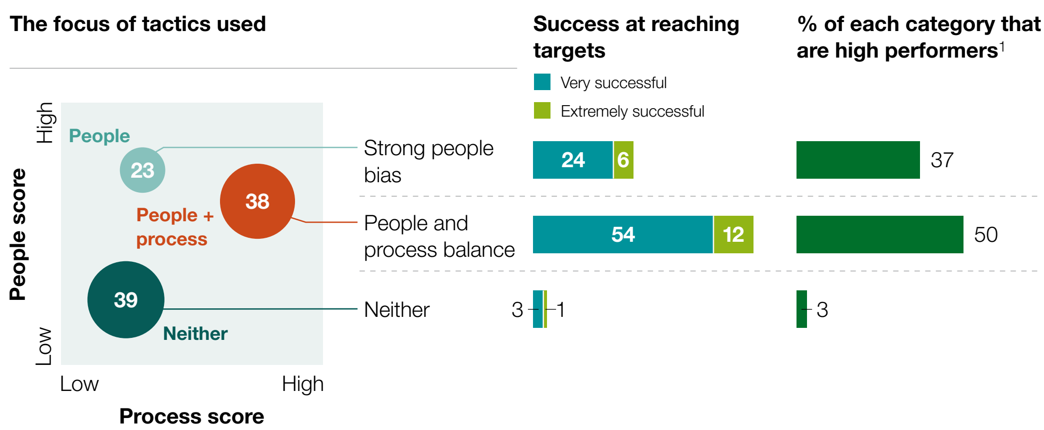
[1]Specifically, respondents who selected "extremely" or "very true" when asked if they used the tactic extensively.

Source: 2010 McKinsey performance transformation survey

Exhibit 3

Half of all companies that use a mix of people and process tactics are high performers.

% of respondents reporting transformations with successful outcome



[1]Defined as very or extremely successful at achieving targets *and* transforming both performance and health.
Source: 2010 McKinsey performance transformation survey

How ready are we to go there?

The financial-services company assessed its current position rigorously. It analyzed performance data on the link between its share of customers' business, customer satisfaction, and its existing operating model to identify which aspects of its services were most important to driving value. As a result, for example, it launched a new initiative to enable the "custom tailoring" of its product features at the point of sale. (The company drew on the customer experience at coffee shops, where you can customize your drink when you order.)

In trying to understand why the company was slower than its rivals to respond to customer demands and new offerings from competitors, it used focus groups and interviews with employees. In this way, it discovered that some mind-sets that once benefited performance were so entrenched they had become harmful. For example, there was a "company knows best" mind-set, which had come out of pride in a long record of high performance. Now, though, it had the unintended consequence of making mid-level and frontline leaders hesitant to raise issues, to pass along feedback from customers (for fear of being seen to criticize a proven model), or to feel that they had the authority to make changes. In the new context, this mind-set needed to change to "The customer knows best. It is our job to listen and enable our people to meet the customers' needs."

Our research highlights a few important elements a company should include when assessing its current situation—and that relatively few include today:

Rigor: Transformations where "considerable effort was made to create a robust fact base for setting the direction and targets" were 2.4 times more likely to be successful than those where the "direction and targets were set based largely on perception and gut feel." Yet only 37 percent of respondents said their companies took the former approach.

Understanding current and needed capabilities: Transformations in which this was done very or extremely well—only 44 percent—were 6.6 times more likely to succeed than those where it was not done at all.

Understanding mind-sets: Only 37 percent of survey respondents said that their organizations' transformations explicitly assessed mind-sets that would need to change to reach their goals. Those that did so were four times likelier to be successful.

Understanding strengths: Forty-four percent of survey respondents said that their organizations focused equally on understanding current problems and on strengths when planning the transformation. Those that did so were nearly twice as likely to succeed than those that focused primarily on problems.

It's easy to overlook these aspects of transformations because, for the most part, companies undertaking a major change effort focus on specific problems and seek to analyze them. Very often, these analyses include a great deal of operational detail, but not less tangible organizational qualities, such as mind-sets. In addition, when executives are trying to solve a problem under time pressure, we've seen that it can be very difficult for them to step back and look at a company's strengths as well.

Like many of the survey's high performers, the financial-services company also included these elements. According to the respondents, 57 percent of these companies created a robust fact base and 67 percent explicitly understood their capabilities, 64 percent their mind-sets, and 62 percent their strengths.

What do we need to do to get there?

The next challenge in a transformation process is to determine exactly which changes need to be made and how. The financial-services company involved people beyond its most senior executives in these decisions—crucial to building the kind of alignment that allows a company to execute healthy change. Irrespective of how brilliant a strategy may be, if employees do not buy into it very little will change on the ground. And the best way to build buy-in, we have found, is to create an environment in which the people most affected by change have a role in shaping it.

In this case, once senior executives had decided on the overarching goals and had a good sense of the company's starting point, they brought together the top 200 leaders to determine what to do next. Executives from different parts of the company all worked together in this process, which was a first step in strengthening their sense of accountability and creating less centralized, less tradition-bound mind-sets, as well as a way to ensure that the plans were realistic and could be operationalized quickly.

To improve the bank's performance by making it more flexible and able to meet customer needs, the executives decided to focus on enabling customers to tailor products and on ensuring best-in-class service in its call centers, ATMs, and branches. To change managers' expectations about decision making, the executives went through a rigorous process to identify the 100 decisions that made the most difference in creating value for the bank in the ordinary course of business and who was responsible for each of them (who decided the pricing for a product, for example, or which customers should be offered products).

In this way, the executives pushed accountability and decision-making authority as close to

Having clear roles and responsibilities and ensuring that the best talent is working on the transformation are the two tactics used more often than any others by high performers.

customers as possible. For example, frontline employees received tools to tailor solutions for customers they were interacting with. The executives also introduced a leadership-development program that would help build needed skills. At all levels, they linked compensation to improvement on the metrics relevant to each person's job. The end result of this collaborative work was a large group of leaders personally committed to making the changes happen and the beginnings of new ways of working and new skills.

Such collaborative planning is something that even high performers don't often undertake: only 21 percent of them did what the financial-services firm did and involved more than 50 people. Although there's no right number, we do see success increasing with greater involvement. One Indian heavy manufacturer, Larsen & Toubro, managed to include 7,000 employees in defining the vision for a company-wide organizational change that has proven very beneficial (see "Reinvigorating a corporate giant," on page 26).

How do we manage the journey?

Companies that use these preparatory tactics well have more than just a plan in place: they have energized people and have started them moving toward a new destination. Now these companies must execute at scale to deliver results. Through the initial stages of the transformation, the financial-services company had developed change themes such as external orientation and responsiveness, as well as specific initiatives to execute each theme. This clear structure enabled the company's leaders to create a coherent plan to implement at scale.

To build ownership and mobilize energy for the ongoing changes, the company identified a team of 100 "change leaders," who were involved in the execution of the initiatives and also led communications to employees through blogs and wikis emphasizing success stories focused on the themes. Finally, the company's change-monitoring process was frequent and focused on both performance and health. It ranged from weekly reviews of the progress of specific initiatives (for instance, time, budget, and impact on KPIs[5]) to quarterly reviews of health metrics (such as improvements in responsiveness, external engagement, and employee engagement).

The employee ownership that begins with collectively developing initiatives is amplified when companies devote sufficient and appropriately skilled resources to the transformation, defining clear roles and responsibilities so that individuals feel accountable for results and empowering them to take initiative. Indeed, having clear roles and responsibilities and ensuring that the best talent is working on the transformation are the two tactics used more often than any others by high performers; 84 and 77 percent, respectively, had these in place in their transformations, compared with less than half of other companies in the survey. Nearly three-quarters of respondents from the high performers also said that their leaders ensured that frontline staff felt ownership of change and that influence leaders, such as those at the financial-services firm, were engaged to help motivate employees.

[5]Key performance indicators.

Disciplined use of clear metrics—covering the progress of initiatives and their outcomes in health, performance, and enterprise value—allows companies to celebrate success and deal quickly with problems. Companies can also adjust their direction and priorities as they learn more about where and how they are generating the greatest returns on their effort.

Finally, we can now show which mix of people and process tactics the high performers—companies that successfully transformed their performance and health—most often use (Exhibit 3). We can divide survey respondents into three groups: those that didn't use many tactics in implementing their transformation; those that had a strong bias toward people-related tactics, such as empowering employees and leaders who role-model changes; and those that used a number of people and process tactics, ranging from effective steering committees to setting a clear structure to deploying the best talent on the most important change initiatives to engaging influential employees who help motivate fellow staff members. At companies that aimed to transform both their performance and their health, those in the third group were very or extremely successful in 62 percent of all cases, and fully half of them were high performers.

How do we keep moving forward?

There's a thread that runs through all of the steps above and is particularly important for the last step, sustaining change. That thread is leadership. The most senior leaders need to set the aspiration for change—and for health—and must ensure that leaders at all levels are aligned with these goals, understand how they and their jobs need to change to meet them, and can encourage others to change as well. Only in that way can a company execute change successfully and maintain its ability to renew itself over time.

Change is tough, and the vast majority of major change programs fail to achieve their objectives. But leaders who focus on performance and health, ask themselves the right questions, and use a range of proven approaches will be able to create both immediate and lasting change. o

The authors would like to acknowledge the important contributions of their colleagues Carolyn Aiken and Scott Keller to the development of this article.

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How centered leaders achieve extraordinary results

**Joanna Barsh,
Josephine Mogelof,
and Caroline Webb**

Executives can thrive at work and in life by adopting a leadership model that revolves around finding their strengths and connecting with others.

For the past six years, we have been on a journey to learn from leaders who are able to find the best in themselves and in turn inspire, engage, and mobilize others, even in the most demanding circumstances. And the business environment *has* become more demanding: the global financial crisis and subsequent economic downturn have ratcheted up the pressure on leaders already grappling with a world in transformation. More than half of the CEOs we and our colleagues have spoken with in the past year have said that their organization must fundamentally rethink its business model.

Our work can help. We have conducted interviews with more than 140 leaders; analysis of a wide range of academic research in fields as diverse as organizational development, evolutionary biology, neuroscience, positive psychology, and leadership; workshops with hundreds of clients to test our ideas; and global surveys. Through this research, we distilled a set of five capabilities that, in combination, generate high levels of professional performance and life satisfaction. We described this set of capabilities, which we call "centered leadership," in a *McKinsey Quarterly* article in 2008[1] and subsequently in a book, *How Remarkable Women Lead*.[2] Since then, through additional interviews and quantitative research, we've continued to validate the model's applicability to leaders across different regions, cultures, and seniority levels. Better yet, we have confirmed that centered leadership appears equally useful to men. In other words, it is not just for women, but for all leaders in demanding circumstances.

Five capabilities are at the heart of centered leadership: finding meaning in work, converting emotions such as fear or stress into opportunity, leveraging connections and community, acting in the face of risk, and sustaining the energy that is the life force of change. A recent McKinsey global survey of executives shows that leaders who have mastered even one of these skills are twice as likely as those who have mastered none to feel that they can lead through change; masters of all five are more than four times as likely.[3] Strikingly, leaders who have mastered all five capabilities are also more than 20 times as likely to say they are satisfied with their performance as leaders and their lives in general.

While such results help make the case for centered leadership, executives seeking to enhance their leadership performance and general satisfaction often find personal stories more tangible. Accordingly, as this article revisits the five dimensions of centered leadership—and their applicability to times of uncertainty, stress, and change—we share the experiences of four men and one woman, all current or former CEOs of major global corporations.

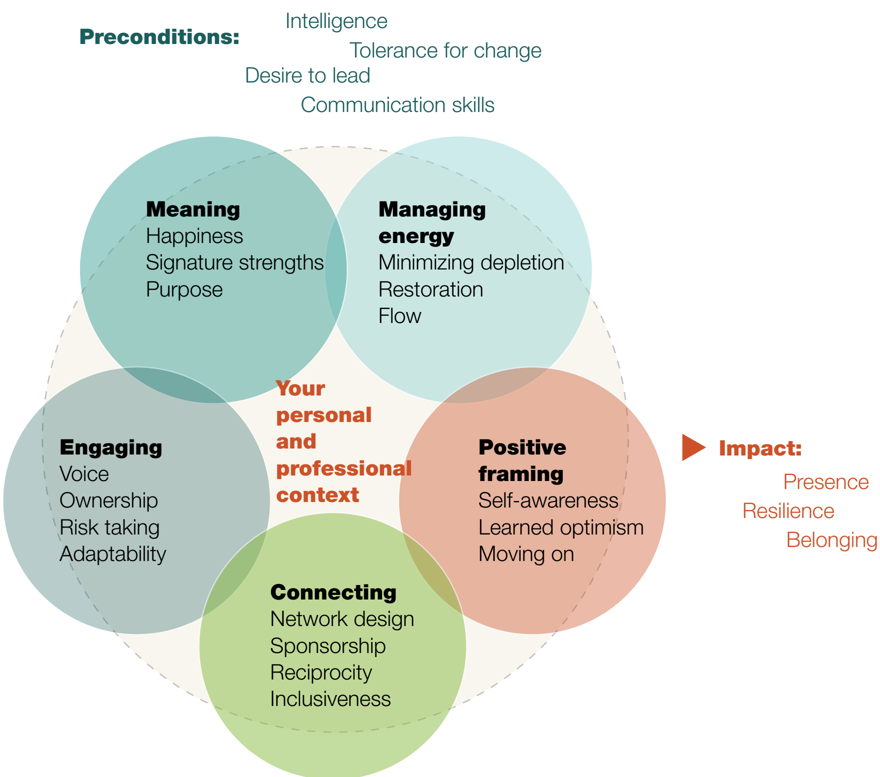
Meaning

We all recognize leaders who infuse their life and work with a sense of meaning. They convey energy and enthusiasm because the goal is important to them personally, because they are actively enjoying its pursuit, and because their work plays to their strengths. Our survey results show that, of all the dimensions of centered leadership, meaning has a significant impact on satisfaction with both work and life; indeed, its contribution to general life satisfaction is five times more powerful than that of any other dimension.

Whatever the source of meaning (and it can differ dramatically from one person to another), centered leaders often talk about how their purpose appeals to something greater than themselves and the importance of conveying their passion to others. Time and again, we heard that sharing meaning to inspire colleagues requires leaders to become great storytellers, touching hearts as well as minds. These skills are particularly applicable for executives leading through major transitions, since it takes strong personal

[1] Joanna Barsh, Susie Cranston, and Rebecca A. Craske, "Centered leadership: How talented women thrive," mckinseyquarterly.com, September 2008.
[2] Joanna Barsh, Susie Cranston, and Geoffrey Lewis, *How Remarkable Women Lead: The Breakthrough Model for Work and Life*, New York: Crown Business Publishing, 2009.
[3] The online survey was in the field from July 6 to 16, 2010. It garnered responses from 2,498 executives representing all regions, industries, functional specialties, and tenures. Respondents indicated their level of agreement with statements representing various dimensions of the leadership model. We then aggregated their answers into degrees of mastery of each dimension.

Five dimensions of leadership



motivation to triumph over the discomfort and fear that accompany change and that can drown out formal corporate messages, which in any event rarely fire the souls of employees and inspire greater achievement.

Avon Products CEO Andrea Jung described how meaning and storytelling came together when her company faltered after years of rapid growth. Andrea's personal challenge was acute because some key sources of her passion—creating a bold vision for growth and inspiring others to dream big, being a member of a close-knit community, and achieving extraordinary results—were deeply connected with her work at Avon. Suddenly, it became harder for her to see where her momentum would come from. What's more, she had to streamline her cherished community.

To remain true to her personal values, Andrea rejected the "more efficient" approach of delegating to managers the responsibility for communicating with employees about the restructuring and of sharing information only on a need-to-know basis. Instead, she traveled the world to offer her teams a vision for restoring growth and to share the difficult decisions that would be required to secure the company's future. The result? Employees felt that Andrea treated them with honesty and humanity, making the harsh reality of job reductions easier to accept and giving them more time to prepare. They also

(Continued on page 22)

The value of centered leadership:
About the research

This article rests in part on the results of our latest survey on centered leadership.[1] We asked more than 2,000 executives around the world questions that allowed us to assess their mastery of the five dimensions of centered leadership and how satisfied they are with their professional leadership and their lives overall.

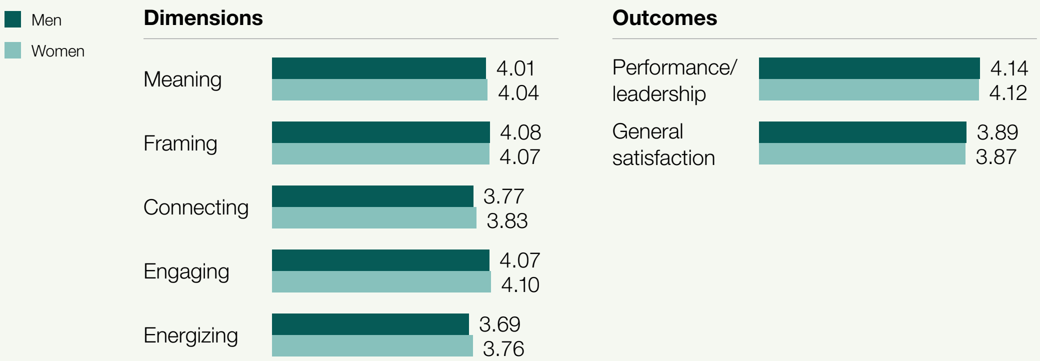
We found that men and women are very similar in the degree to which they practice the elements of centered leadership and experience satisfaction in their work performance and their lives (Exhibit 1). Further, among the 29 questions that we used to assess mastery of each dimension, there were statistically significant differences between men and women on only 11, and those differences were minimal. (For our purposes, respondents master each dimension when their answers put them in the top 20 percent of overall scores.)

Women do have a slight edge: they have a higher share of the top quintile than of the overall pool, suggesting that centered leadership remains geared to women's strengths.[2] That a very high share of men have mastered each dimension shows, however, that centered leadership is not about being a woman but rather about abilities, mind-sets, and behaviors sometimes considered feminine, such as being motivated by meaning at work—as opposed to pay

Exhibit 1

Men and women alike can master the dimensions of centered leadership and feel successful in both their performance at work and in their lives.

Net scores,[1] n = 2,177



[1] All results are mean scores calculated on a 5-point scale, where 5 is equal to "strongly agree."

or status—and seeking to forge community and collaboration.

The results also make it clear that there is a tight relationship between mastery of centered leadership and the self-assessed performance of executives as leaders and their satisfaction with life in general. Notably, the more of the relevant dimensions leaders master, the likelier they are to be very satisfied with their performance (Exhibit 2).

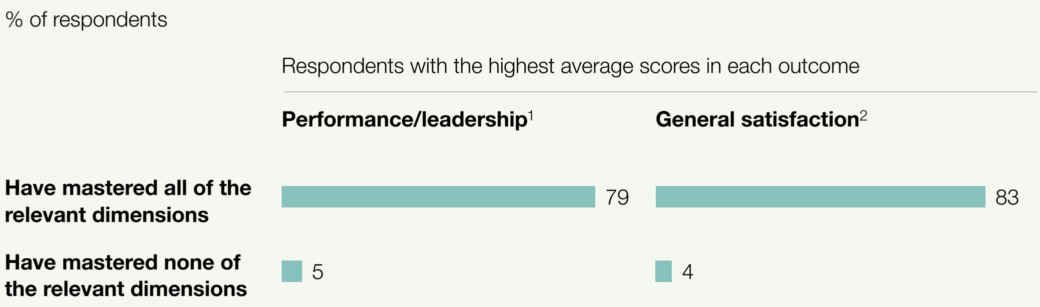
Finally, we observed that the youngest respondents—both men and women—were least likely to have mastered any dimension except connecting. This suggests that young people seeking to become leaders would benefit significantly from undertaking the centered-leadership journey sooner rather than later. Further, companies that support their young executives in doing so will reap the benefits, such as higher performance and greater corporate resilience, earlier.

[1] For more, see "The value of centered leadership: McKinsey Global Survey results," mckinseyquarterly.com, October 2010.

[2] Women made up 35 percent of the total sample; the shares of women who have mastered the various dimensions range from 34 to 41 percent, with four of the five above 35 percent.

Exhibit 2

The more of the relevant dimensions leaders master, the likelier they are to be very satisfied with their performance.



[1] For performance/leadership, the 4 dimensions that have a meaningful impact on outcome scores are, in order of descending influence, meaning, engaging, framing, and connecting; for "mastered all," n = 106; for "mastered none," n = 1,302.

[2] For general satisfaction, the 4 dimensions that have a meaningful impact on outcome scores are, in order of descending influence, meaning, energizing, engaging, and connecting; for "mastered all," n = 103; for "mastered none," n = 1,258.

experienced her love for the company firsthand and recognized that both she and Avon were doing all they could. By instilling greater resilience throughout the organization, Avon rebuilt its community and resumed growth within 18 months.

Positive framing

Positive psychologists have shown that some people tend to frame the world optimistically, others pessimistically.[4] Optimists often have an edge: in our survey, three-quarters of the respondents who were particularly good at positive framing thought they had the right skills to lead change, while only 15 percent of those who weren't thought so.

For leaders who don't naturally see opportunity in change and uncertainty, those conditions create stress. When faced with too much stress (each of us has a different limit), the brain reacts with a modern version of the "fight, flight, or freeze" instinct that saber-toothed tigers inspired in early humans. This response equips us only for survival, not for coming up with creative solutions. Worse yet, in organizations such behavior feeds on itself, breeding fear and negativity that can spread and become the cultural norm.

When Steve Sadove took over Clairol, in 1991, for example, the company had been shell-shocked by a significant decline in sales volume. "I remember going to a very creative person, who did all the packaging and creative development," Steve told us, "and saying, 'Why don't we do anything creative?' He opened some drawers in his desk and started showing me all of this wonderful work that he'd done. Nobody was asking for it; people kept their head down in that culture. So part of my role as the leader was to create an environment that was going to allow innovation and creativity and make it OK to fail."

Fortunately, we can all become aware of what triggers our fears and learn to work through them to reframe what is happening more constructively. Once we have mastered reframing, we can help others learn this skill, seeding the conditions that result in a safe environment where all employees are inspired to give their best.[5]

Steve found ways to stimulate creativity, such as exploring opposing points of view in discussions with colleagues. Over time, he convinced others that speaking up wasn't just tolerated but encouraged. He helped colleagues reframe the way they reacted to dissent, forging a less defensive and ultimately more innovative culture. Steve and his team introduced a winning hair care brand, Herbal Essences, and ushered in a golden period of growth for Clairol.

[4] Martin E. P. Seligman, *Authentic Happiness: Using the New Positive Psychology to Realize Your Potential for Lasting Fulfillment*, New York: Free Press, 2004.
[5] Michael A. Cohn et al., "Happiness unpacked: Positive emotions increase life satisfaction by building resilience," American Psychological Association, *Emotion*, 2009, Volume 9, Number 3, pp. 361–68.

Risk aversion and fear run rampant during times of change; leaders who are good at acknowledging and countering these emotions can help their people summon the courage to act and thus unleash tremendous potential.

Connecting

With communications traveling at warp speed, simple hierarchical cascades—from the CEO down until the chain breaks—are becoming less and less effective for leaders. For starters, leaders depend increasingly on their ability to manage complex webs of connections that aren't suited to traditional, linear communication styles. Further, leaders can find the volume of communication in such networks overwhelming. While this environment can be challenging, it also allows more people to contribute, generating not only wisdom and a wealth of ideas but also immeasurable commitment.

The upshot: CEOs have always needed to select exemplary leadership teams. Increasingly, they must also be adept at building relationships with people scattered across the ecosystem in which they do business and at bringing together the right people to offer meaningful input and support in solving problems.

Macy's CEO Terry Lundgren learned firsthand about the power of connecting the internal community in 1988 when, 15 months after joining the retailer Neiman Marcus, he became its president and CEO. Shaking things up was core to his role: "I was one of the first non–Marcus family members with that title for any extended period of time." Employees greeted him with widespread skepticism. "They were all thinking, 'Who is this 37-year-old guy who is going to tell us how we should run our fantastic business?'" So Terry held a town hall meeting in the library across the street from company headquarters, in downtown Dallas. He invited anybody who wanted to come. The first time, he recalls, "I had only about 30 people show up! I thought it was going to be a little bit bigger than that, but I tried to be very direct and use the time mostly to listen and respond." He kept holding meetings, noting that "it really moved the needle quickly in terms of getting things done in that company." By the time Terry left, the twice-a-year meetings filled a 1,200-seat auditorium.

Today, as Terry leads Macy's, he connects the dots internally and externally in many ways, from scheduling a monthly breakfast with new managers to forming relationships with peers who have led companies through change. Terry has also emphasized corporate connectivity, regrouping Macy's stores into 69 districts, each tasked with creating "My Macy's" for its customer base. And comparable-store sales were up this year, reversing a negative trend. Terry's top team believes its efforts to connect managers more closely to one another and to customers, through enhanced information sharing and product offerings tailored to local needs, help explain the company's trajectory.

Engaging

Of survey respondents who indicated they were poor at engaging—with risk, with fear, and even with opportunity—only 13 percent thought they had the skills to lead change. That's hardly surprising: risk aversion and fear run rampant during times of change. Leaders who are good at acknowledging and countering these emotions can help their people summon the courage to act and thus unleash tremendous potential.

But for many leaders, encouraging others to take risks is extremely difficult. The responsibility CEOs feel for the performance of the entire organization can make the very notion of supporting risk taking extremely uncomfortable. What's more, to acknowledge the existence of risk, CEOs must admit they don't, in fact, have all the answers—an unusual mind-set for many leaders whose ascent has been built on a virtuous cycle of success and self-confidence.

Doug Stern, CEO of United Media, has a number of ways to help his people evaluate risks and build their confidence about confronting the unknown. Because he has seen the destructive impact of anxiety, Doug follows an explicit process anytime he's facing a new, risky project (for example, selling some of his company's assets). The process helps everyone—himself included—prepare by devising risk mitigation strategies using these steps:

asking the team to imagine every bad scenario, even the most remotely possible—what he calls the "darkest nightmares"

giving everyone a chance to describe those scenarios in detail and then to "peer into the darkness" together

devising a detailed plan for countering each nightmare—in effect, rehearsing the best collective response to each potential issue

Once fears have surfaced and been dealt with, the team has a protocol in place for every worst possible scenario and a set of next steps to implement.[6]

Managing energy

Sustaining change requires the enthusiasm and commitment of large numbers of people across an organization for an extended period of time. All too often, though, a change effort starts with a big bang of vision statements and detailed initiatives, only to see energy peter out. The opposite, when work escalates maniacally through a culture of "relentless enthusiasm," is equally problematic.[7] Either way, leaders will find it hard to sustain energy and commitment within the organization unless they systemically restore their own energy (physical, mental, emotional, and spiritual), as well as create the conditions and serve as role models for others to do the same. Our research suggests sustaining and restoring energy is something leaders often skimp on.

While stress is often related to work, sometimes simple bad luck is at play, as Jurek Gruhn, president of Novo Nordisk US, can attest. Nine years ago he was diagnosed with Type 1 diabetes. Working for a world leader in diabetes care, Jurek was no stranger to the illness and, along with his optimistic spirit, his no-nonsense orientation became a deep source of energy: "My first reaction was, 'You may have Type 1 diabetes, but you could also have a lot of other diseases that are much worse.'" So, he told us, "I went to the hospital for two or three days of testing and then went back home. We had our Christmas break. After that, I was back in the office. My wife, who is a physician, said to me, 'That was a quick process!' I basically took on my disease as a task."

Jurek realized that one key to living a normal life with the disease is to embrace life, at work and at home. "A healthy lifestyle is important. I have five kids: my oldest daughter is 25, and my youngest is 6. Sometimes they completely drain my energy, but they can energize me a lot. And now I feel healthier because I have also changed my lifestyle: I eat breakfast now every day, I exercise much more, and I started rock-climbing on a regular basis." Everything improved—his physical condition, mental focus, emotional satisfaction, and spirit. He even learned to face what drained him most—unhealthy conflict at work—by addressing it directly and quickly, much as he handled his diabetes.

Even for leaders without such a challenge, Jurek sets another valuable example: "I saw this

[6] Psychologist Gary Klein has developed and applied in a variety of settings a similar approach that he calls the "premortem." For more on this technique, and on the broader problem of executive overconfidence, see "Strategic decisions: When can you trust your gut?" mckinseyquarterly.com, March 2010.

[7] Edy Greenblatt, *Restore Yourself: The Antidote for Professional Exhaustion*, Los Angeles, CA: Execu-Care Press, 2009.

comedian who said that a man's brain is filled with boxes, and one of them is empty. Well, when the day's really tough in the office, I go into my empty box for 10 or 15 minutes and I do nothing. If I completely switch off for a short period of time, I get my energy back. Now, I'm not switching off every 15 minutes after working for 15 minutes—maybe I do it every few days. But I do not work weekends unless I really have to. And I'm not one who wakes up and the first thing is the BlackBerry. No way!"

• • •

Centered leadership is a journey, not a destination, and it starts with a highly personal decision. We'll leave you with the words of one executive who recently chose to embark on this path: "Our senior team is always talking about changing the organization, changing the mind-sets and behavior of everyone. Now I see that transformation is not about that. It starts with me and my willingness and ability to transform myself. Only then will others transform."

The authors would like to thank Aaron De Smet and Johanne Lavoie for their extraordinary contributions to this work.

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Reinvigorating a corporate giant:

An interview with the chairman of India's largest infrastructure company

Ramesh Mangaleswaran and Adil Zainulbhai

A. M. Naik describes how he established a culture of value creation at one of India's leading companies.

A. M. Naik joined Larsen & Toubro, one of India's largest engineering and construction firms, as a junior engineer in 1965. He was appointed its CEO in 1999 and was elevated to chairman and managing director in 2003. Naik soon embarked on a restructuring mission. He says that today the transformation is about 65 percent complete but has already had a powerful impact: over the past decade, the company's equivalent market capitalization has multiplied about 30 times, dramatically outpacing the market as a whole. From 1999 to 2010, annual revenues grew to about Rs 44,000 crore (US $9.5 billion) from Rs 7,402 crore (US $1.6 billion).

Founded in 1938 by two Danish engineers, L&T began as a company that imported equipment from Denmark and grew rapidly through the rest of the past century. By 1999, when Naik became CEO, the company was a complex organization. It had multiple divisions in a wide range of businesses—some small, others large. In HR appraisals of the company's 20,000 employees, seniority seemed to matter more than performance or merit. The stock price was stagnant, and employees were leaving because they saw little chance for advancement and because the external market for talent was buoyant. L&T was ripe for a takeover and indeed was embroiled, on two separate occasions, in takeover battles by two of India's biggest corporate groups.

As chairman, Naik's main agenda was to keep the company independent. His gambit: create shareholder value and attract and retain the best employees by restoring a merit-based performance-management system and by instituting greater rewards for high performance. Naik worked on multiple fronts, pushing for scale and competitiveness in all business lines.

Naik met with McKinsey's Ramesh Mangaleswaran and Adil Zainulbhai at L&T's Powai complex, in suburban Mumbai, and discussed the role of leadership in transformation, creating value, and how he changed an entrenched culture, in part, by involving thousands of employees in the planning process.

McKinsey: *Why did you start the transformation of L&T?*

A. M. Naik: Well, it has been a long journey of 46 years in Larsen & Toubro. In the mid-1970s, local Indian management took over the reins. L&T was extremely merit-oriented until 1974. Afterward, it wasn't. I meet people who worked for ten years or more at L&T and left, and those who were meritorious should never have been allowed to go. I don't think it was actually said by anybody in authority that "now we'll slow down everyone who's young." But in reality, there was a feeling that "maybe he can wait." Promotions started to be driven by seniority. We lost a lot of people, people with the ability and the motivation to take us to the next level of growth.

McKinsey: *So is it fair to say that you had been planning some kind of transformation for many years before you became the company's leader, as you observed things you didn't like?*

A. M. Naik: Yes, I said, "Someday, when I have freedom, I'm going to bring the merit system back." The fact that the company was aging and we couldn't see who would be our successors compounded that desire. What impelled us even more was that from the mid-1990s onward, the economy in India liberalized; and external opportunities for our talent further increased. Given that L&T had a range of businesses (and therefore a range of capable managers) and had historically attracted the best talent in the country, we became a hunting ground for talent. As we had several bright people working much below their real potential because of the move away from merit-based promotions, their urge to leave was high and we could not stem the attrition.

We had a second challenge—L&T was also undervalued in the stock market, which made us vulnerable to takeover. We are good engineers. In fact, we used to jokingly refer to ourselves as Larsen & Toubro & Genius Ltd. But that made us tremendously complacent when it came to business performance, and people in the company didn't understand what it meant to create value. If the company is cheap, anyone can buy it. If the company is very valuable and expensive, people will think twice. So I was constantly thinking, "What will keep Larsen & Toubro independent? What will make it less vulnerable to a takeover?"

Through all this I was thinking, "What will I do differently when I get a chance?" In April 1999, six months before I took over, I made a document: a 90-day action agenda from the day I took charge.

McKinsey: *What was in your document?*

A. M. Naik: Talent always remained the highest priority in my mind, and therefore rebuilding the meritorious organization as a retention tool. I said, "Let me start writing this down. One, I will bring merit back in L&T. Seniority will be respected because the senior people have contributed largely to make L&T what it is, and therefore the change may be somewhat slow because it has to be smooth." Nevertheless, the direction had to be set that seniority would not be the only governing factor. That's one.

"When the vision was finalized, everyone could say, 'That word was mine'; maybe that word was in the minds of a thousand people, but the process created a shared vision everyone could believe in."

Two, L&T was in too many businesses that were too small, very diversified, and hardly understood by anyone, so the portfolios needed to be rationalized.

Three, L&T had been a professionally managed company, and we were very proud of that. However, while we were creating a marvelous bridge and making a nuclear reactor and all that, unfortunately there was no emphasis whatsoever on value creation. I think nobody understood what it really meant to enhance the value of the company and what that could mean to every individual.

And as a corollary, as a retention tool for exciting people, I gave a stock option, initially, to 500 people, which later on rose to about 3,000. We were the first major "brick and mortar"—non-IT or -finance—company to do this in India. None of the employees understood the value of a stock option at the time, because it was given at the market price as allowed by the regulator. But I knew that if the company was transformed, the value was going to multiply. Today, its effective stock price—after adjustment for splits and de-mergers—has gone up 37 times, and the market has gone up around 4 times since 1999.

McKinsey: *How did you manage the portfolio rationalization?*

A. M. Naik: I started the analysis of every single business in the company and put them into three categories: core, noncore, and "grow to sell." I defined them on multiple parameters. We are

A. M. Naik

Vital statistics
Born June 9, 1942, in Endhal, Gujarat, India

Education
Graduated with a bachelor's degree in mechanical engineering from Birla Vishvakarma Mahavidyalaya Engineering College

Career highlights
Larsen & Toubro
(1965–present)

Chairman and managing director (2003–present)

CEO (1999–2003)

President of operations (1995–99)

Fast facts
Winner of the *Economic Times*' Business Leader of the Year award (2008); received the Padma Bhushan award in 2009, India's third-highest civilian honor

Makes a point to play badminton once a week

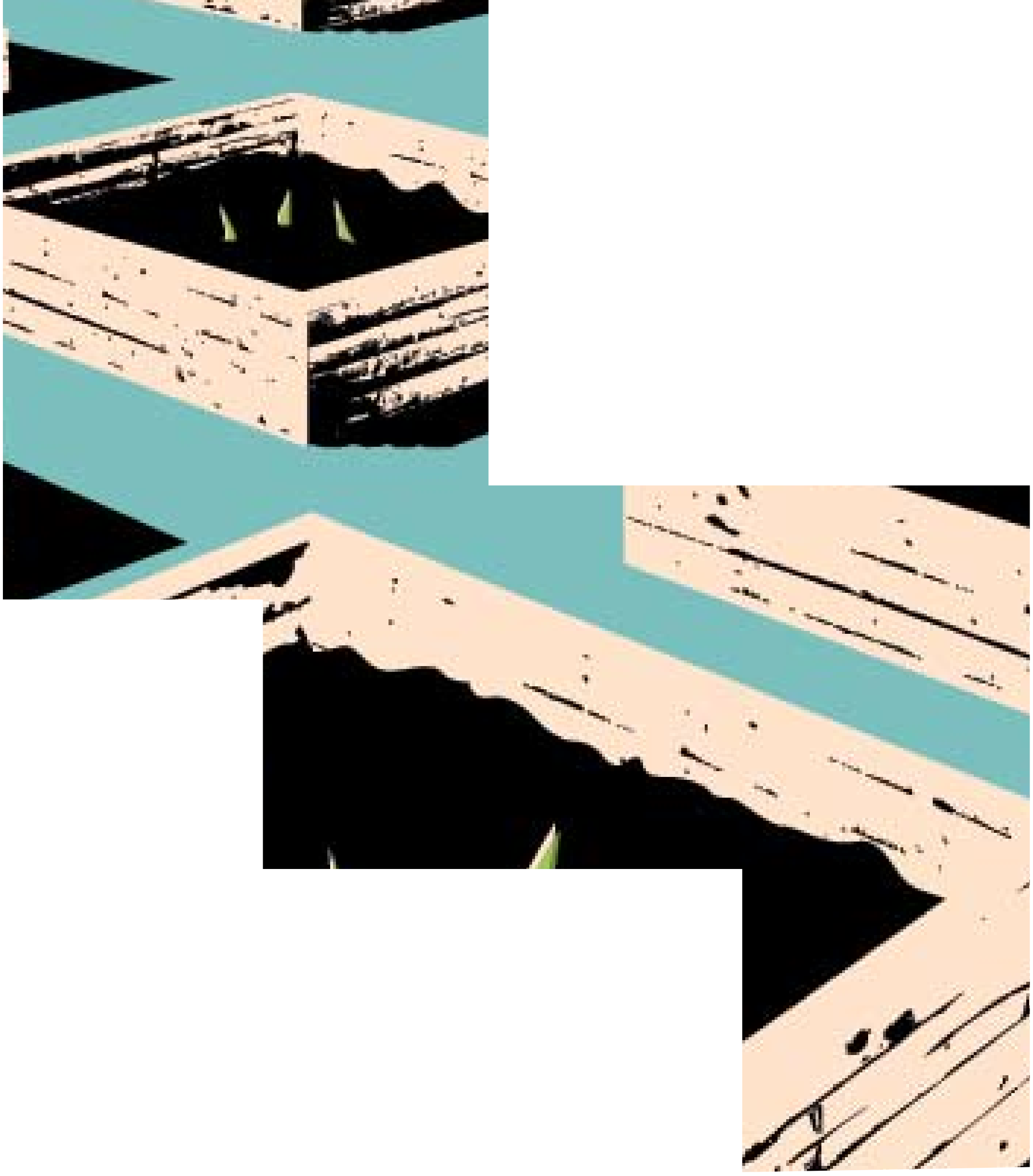
a builder to the nation, and therefore building infrastructure, power plants, and hydrocarbon plants will remain core. Though this was a difficult way of making money, we said, "This is something that many companies won't do, and let's not deviate too much from being an engineering excellence company." And what is not in line with that and is also not creating value—both at the same time—I made noncore. There were some areas where the demand was huge, but they were commodity businesses, like cement. These were labeled "grow to sell." The ones that were very marginal and absolutely noncore, I said, "Sell right away." Many of those we couldn't sell, so I said, "Close them, just get out of it."

Then I held a meeting with top managers and invited a lot of external speakers. All the speakers wanted L&T to reorient itself to create value. One of the external speakers said plainly, "Have you seen the trading of your stock? Nobody trades your stock. It's lying in one corner. Nobody is interested in your stock, because while they know it's a great company and it will do great jobs, it has nothing to offer to the shareholders."

McKinsey: *Was the company behind you?*

A. M. Naik: As of the day of that meeting, no. But by the time eight months passed, our blueprint was ready. I created excitement in the organization by being participative in creating the vision. We involved one in four employees, about 7,000 people. I visited 38 locations of the company, made my presentation, and explained why L&T was vulnerable. Slowly, everyone understood the message: saving L&T is your first priority, and to save L&T as an independent company, you have to create value.

As we started the process of creating a vision, I said the two crucial, nonnegotiable objectives were value creation and becoming an Indian multinational; you can't depend on business in one country. The rest of the vision, everyone else could fill in, modify, substitute, recreate.



A very methodical and participative process was followed at all the locations. That included workers, union leaders, supervisory leaders—everyone. When the vision was finalized, everyone could say, "That word was mine," you know? Maybe that word was in the minds of a thousand people. But the process created a shared vision everyone could believe in.

McKinsey: *How did you proceed from there?*

A. M. Naik: The first step was to create a mind-set, among employees, that value creation for the business and differentiation amongst people go hand-in-hand. Rewarding high performance also meant that we became more decisive with nonperformers, something that was tough and difficult in the Indian and in the L&T culture. I said, "First and foremost, please remove the bottom 5 percent," because there had been accumulated nonperformance of 30 years. I pushed that and, in November 1999, separation of nonperformers happened for the first time in the history of Larsen & Toubro. Then I called the union, and I said, "I'm going to give you a voluntary-retirement scheme." That was launched, also in 1999, and a few hundred people took advantage of it and left. This was less to cut costs but more to create a differential benchmark that would encourage value creation and growth.

Earlier, if a talented employee got a $100 bonus, the nonperforming person, who should never have been in the job, would still have got $65 or $70 instead of zero. If top talent got promoted in three years, then mediocre performers were promoted in five. So I created a new reference point: if you're inefficient, you will stay at zero.

Then, in August 2000, I asked my top team again: "Should we start meritorious grades for employees who are very good?" I reminded them that if you lose an employee who gets a nine or ten out of ten, that is equal to losing 20 who get four or five out of ten. Finally, that August, I was able to initiate what we call the Management Leadership Program.

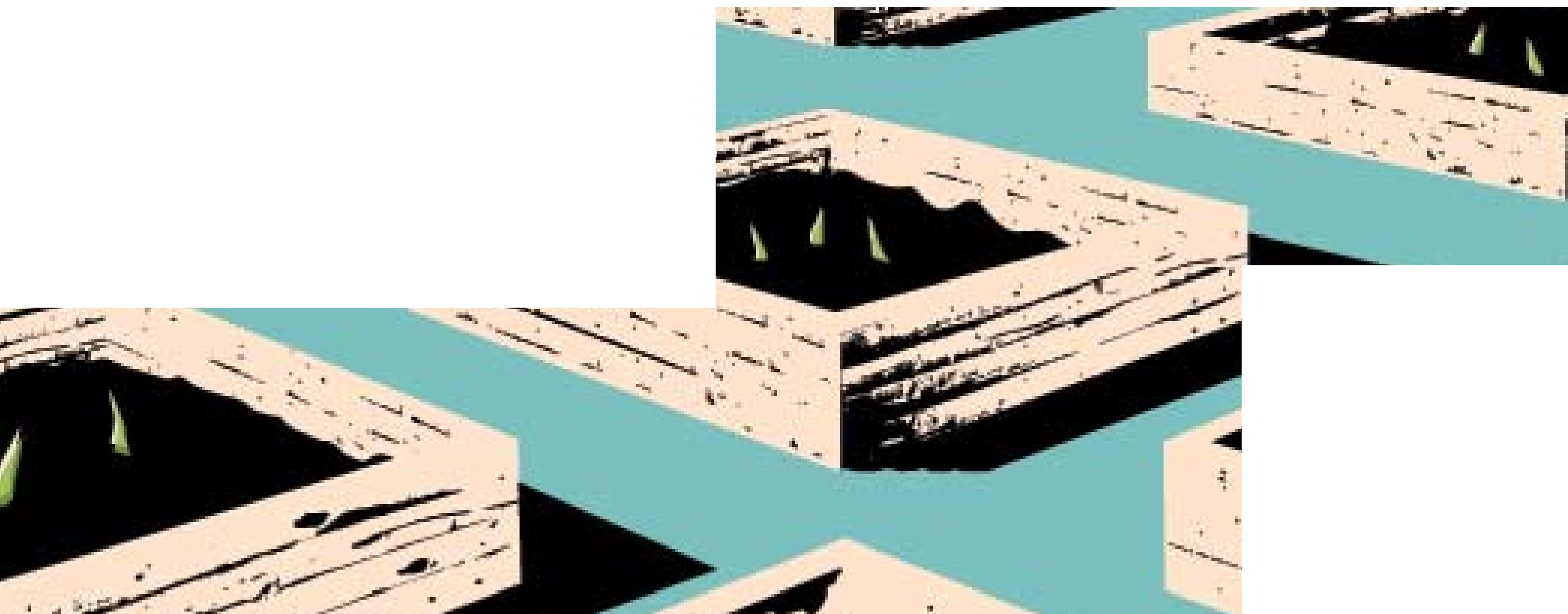
> "As we started the process of creating a vision, I said the two crucial, nonnegotiable objectives were value creation and becoming an Indian multinational."

But I didn't see any progress for some time. It wasn't just internal issues; the economy was extremely bad, and there were certain legacy issues that I had to clean up. Then there was a threat to buy us out by a large Indian business group. That took a huge amount of time to fight off.

It was early 2004 before we started to see real progress. Even then, the change was extremely slow. There was no resistance, but there was no will to make hard decisions, because when you want to create a meritorious organization, you also have some unpleasantness from the people who want seniority.

So what do you do now? You are between the devil and the deep sea. If you remove the senior people, then you'll create a trauma—ill will in the company. And if you block the young generation, then you compromise on future leadership and growth. So therefore the response was extremely slow.

I had pushed through the Management Leadership Program by sheer force, and it was for the very young people, under 30, so it did not affect anyone very senior. But slowly it began to show results. We were able to move participants faster into new jobs, and they showed real results. Then some people said, "L&T is a technology company, so we should have a Technology Leadership Program." I said, "Fine." Then another set of people said, "We have very hardworking people on the shop floor, and therefore we need them to be appreciated." I said, "Fine. We will create a Supervisor Leadership Program." An international agency was brought in to manage these programs so that everyone



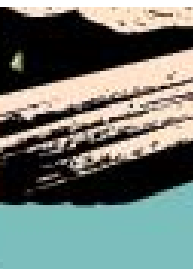
would have confidence that there was no vested interest. Never before had any company in India launched this kind of systematic and scientific program, and we *had* to do it right—otherwise our people would get upset. This was a great sign that the whole company understood the idea of a meritorious organization.

McKinsey: *What do you see as the role of leadership in a company like L&T, which is a professionally managed business as opposed to a family-run one?*

A. M. Naik: Professional managers are required to follow up on what needs to be done, and therefore they can maintain value—say, $1x$. Leaders, depending on how much motivation and inspiration they can provide, add more—they grow value by, say, $2x$ or $3x$. And if you're an entrepreneur, the multiplier is more, say, $5x$. If you have leaders who are entrepreneurial, and at the same time inspire professionals to perform at their very best, you can multiply value manifold. So do you want to be an x as a professional manager or to do more as a leader or to achieve even more as an entrepreneurial leader?

McKinsey: *How do you sustain motivation?*

A. M. Naik: Earlier, we were a somewhat diffused business. Now, we have sharpened the focus within each business, even if we have not pruned the overall businesses radically. For instance, instead of doing $2 million projects, we now do $20 million and above. The same individual therefore gets motivated to do bigger jobs. That has motivated employees and has also brought the attrition rate down.

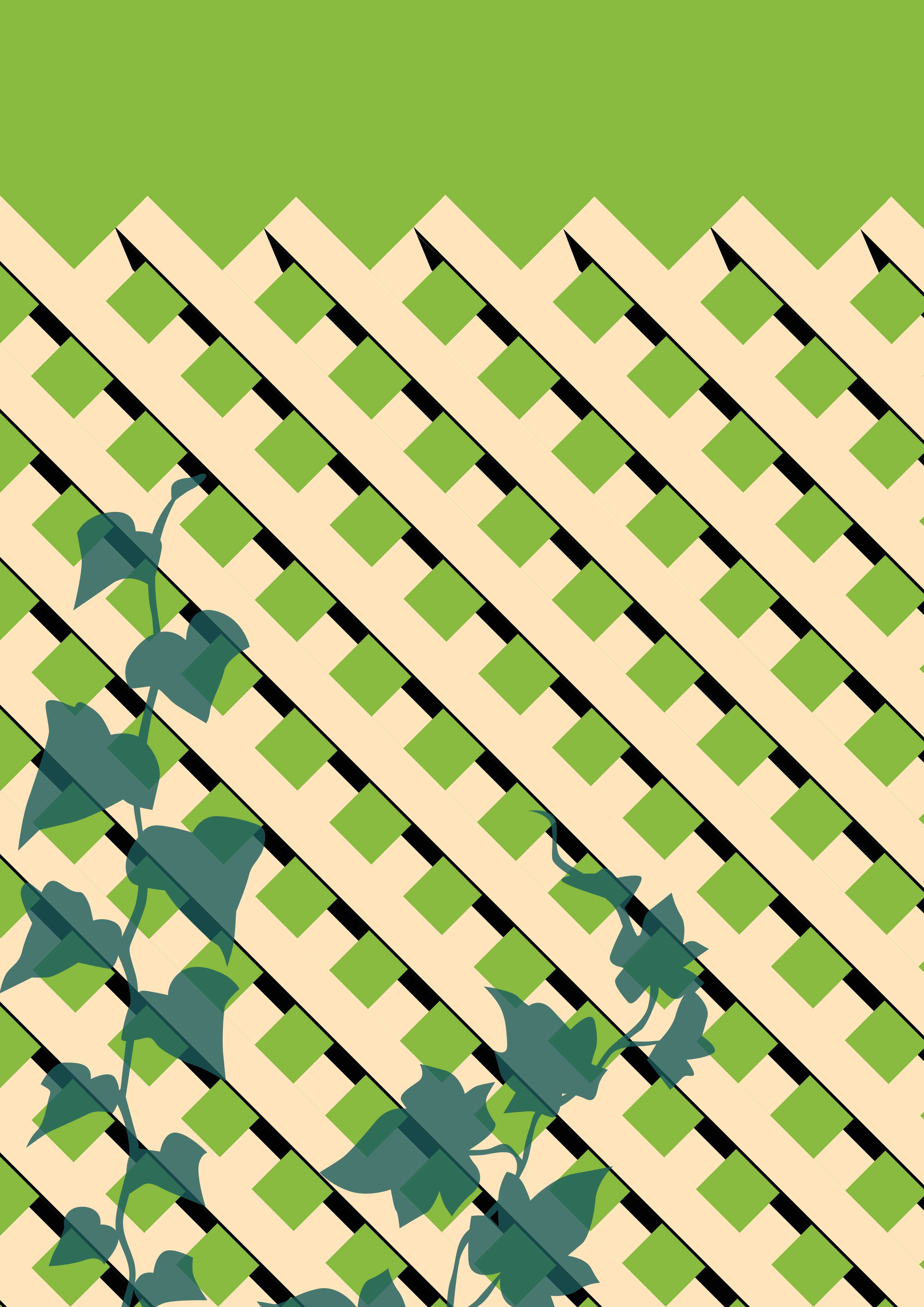


Of course, the method for focus and motivation differs from business to business. Switchgear, for example, I dealt with by motivating the product designer because that was a winning point. I used to go and sit in the design workshops. Of course, it was also done partly for me to understand the business because I didn't come from an electrical business.

McKinsey: *Where is L&T now?*

A. M. Naik: The transformation is 60 or 65 percent complete. Revenue is five times higher than it was a decade ago, net income nine times higher, and we now have more than 38,000 employees. There is a lot more that needs to be done until the next generation takes over. But we are on the right path. ○

Ramesh Mangaleswaran and **Adil Zainulbhai** are directors in McKinsey's Mumbai office.



Scaling up a transformation:

An interview with Eureko's Jeroen van Breda Vriesman

Peter de Wit

A member of the executive board describes how the Dutch insurance group first transformed its health division and then started to roll out the changes across the entire company.

Eureko, a large insurance group operating in the Netherlands under the Achmea brand, faced a tough decision in 2006. The Dutch government had implemented radical market reforms that fused a partly public, partly voluntary and private system into one mandatory national health insurance program executed by private insurers. Amid uncertainty about future cost and premium levels, many stock-listed companies opted to leave the health insurance business.

Achmea, which had grown during two centuries of mergers between mutual insurers, faced a choice of either exiting health insurance or going into it big and competing on quality to win substantial market share. "We decided on the latter because we were good on the commercial side," explains Jeroen van Breda Vriesman, Eureko's executive board member responsible for the health division and for group information management and technology. "So we went in, although we knew we would be losing a lot of money in the first year." The company launched a "lean" transformation of its health division, which went from a loss to profitability in three years, and then started to scale up that transformation across Achmea's nonlife, life insurance, pensions, and other activities in 2008.

Van Breda Vriesman recently talked with Peter de Wit, a director in McKinsey's Amsterdam office, about the importance of a compelling vision and of engaging the right leaders at every level when scaling up a transformation from 2,200 staff members in the health division, with the plan to involve more than 20,000 employees ultimately.

McKinsey: *Why did Achmea launch a transformation of its health division in late 2006?*

Jeroen van Breda Vriesman: Liberalization was a great challenge for all health insurers. Our offensive strategy worked—we gained a lot of market share—but we knew we would face two tough challenges. One was to fix our profit-and-loss numbers and meet our budget in the coming years. The other was to play the role envisioned by the legislators: to improve the health system in terms of better quality and prices. Going from one market system to another is a big shift for a company, but it does create a strong sense of urgency and it can be a driver for organizational changes.

McKinsey: *Where did you start?*

Jeroen van Breda Vriesman: We started with profit and loss, and that meant transforming our operations, including customer care and the front and back offices, which now had to cope with a much larger customer base. Even before liberalization, our operations performed below their potential. They were not meeting cost benchmarks. The administrative process itself had become more important than the customer. We hadn't been thinking in terms of continuous improvement, and we weren't giving employees the power to really improve their way of working. All that had to change.

McKinsey: *What role did strong leadership and the lean concept play for changing mind-sets and culture?*

Jeroen van Breda Vriesman: Having really good people in all the right places was the prerequisite for the success of the program, which we named "Sens" (Samen Effectief Naar Succes) in our internal communications. In Dutch, that's an abbreviation for "together effectively toward success." Starting at the top, we identified existing managers with the right mind-set and put them in positions that were critical for the change effort. We also trained managers who were underperforming or lacked the required mind-set. Occasionally, we hired external staff for certain tasks.

Interestingly, two of the division's general managers approached the task in different ways. One set out to improve efficiency, focusing on culture and behavior, without the help of lean

Jeroen van Breda Vriesman

Education

Earned a law degree from the University of Utrecht

Career highlights

Achmea
(2004–present)

Member of the executive board of Eureko
(2008–present)

Chairman of the Achmea Zorg (Health) Division
(2006–08)

Chairman of the Occupational Health Division
(2004–06)

experts. The other general manager put a lean system in place and this helped him achieve results, including cultural change. Both of these managers met the 25 percent efficiency target. The only problem was that we couldn't duplicate the improvement achieved by the manager who did it on his own. But we were able to ask the manager who was using lean to help others implement it in the same way. That has proved to be the beauty of lean. It helps you to continuously improve your company in a very systematic way.

McKinsey: *What more does it take to truly change mind-sets and behavior?*

Jeroen van Breda Vriesman: Strong top-down leadership is very important, but it's not enough. You must also have a vision and a strategy that explains to people why they are working according to lean principles—that it's not only about meeting a budget, that it's actually about creating a better company. With a vision—one that employees trust—you can make incredibly big changes in a short time. Without this vision, if you push lean just as something top management wants, it will probably not be around for more than a couple of years.

McKinsey: *How did Achmea create the vision and strategy for its health division?*

Jeroen van Breda Vriesman: More than 400 managers and key players in the division were involved. This process was important because doing it together created a sense of common ownership. This made it easier to communicate across the division why things had to change and in what ways.

McKinsey: *What are the key elements of the vision?*

Jeroen van Breda Vriesman: The most important element is that we decided we wanted

“The concept of continuous improvement puts the employee first as well. She or he has the chance to implement her or his own ideas every day; that’s a great way to work.”

to be a health insurer simply because we care about the health of our customers. As a company with a cooperative background, we put our customers first. In doing so, we balance the interests of the four stakeholders we identify in our organizational model: customers, shareholders, business partners, and employees.

That, in turn, means that we must care about the cost and quality of the health system so that it becomes truly sustainable, which benefits us as well as our customers. This was the key driver for our people to accept the lean principles. Secondly, we believe that health care will improve only in a partnership between the insurers and the providers. That’s why we are now supporting the implementation of lean at our providers—for example, the hospitals that we work with. Success means a better quality of care for our customers and higher efficiency for us. Thirdly, the prerequisite for succeeding with this vision is that people trust us.

McKinsey: *What do you mean by trust?*

Jeroen van Breda Vriesman: We mean that people in our company need to trust themselves, players within teams have to trust each other, and teams also need mutual trust. This is very important for lean because if teams don’t trust each other, they will end up duplicating work.

It goes without saying that our customers need to trust us. So we have performance indicators that measure how sales teams trust each other and how our customers trust Achmea overall, as well as its separate brands. It’s also important to learn how we can improve that trust. Finally, we have begun to measure how health care providers trust our company.

McKinsey: *How do you measure the impact of the lean program in the health division?*

Jeroen van Breda Vriesman: We measure it in three ways. One is financial impact, which, by the way, is not only costs but also turnover in terms of gross written premiums because you get more of that when you deliver better quality. The second thing we measure quite frequently—every two weeks on teams where we implement lean—is employee satisfaction. Typically, satisfaction drops in the first six to eight weeks because employees need to get used to the new way of working. Satisfaction levels then stabilize and are usually higher one year into the program.

Customer satisfaction is of course a critical metric. We measure easy things like the number of mistakes we make, the number of letters of complaint we get, and so forth. But we are now also looking at ways to assess behavioral changes among our customers. We want our customers to stay with us longer, buy more products, and recommend us to people they know. By measuring this, we believe we can really prove the importance of continuous improvement.

Looking at customer satisfaction, the results have been enormous in the health division—we’ve seen improvements of 50 to 60 percent. What astonished me was that the results in the first year were so good. Now every year, we see a 5 to 10 percent improvement in efficiency, mainly in terms of lower costs and higher employee and customer satisfaction.

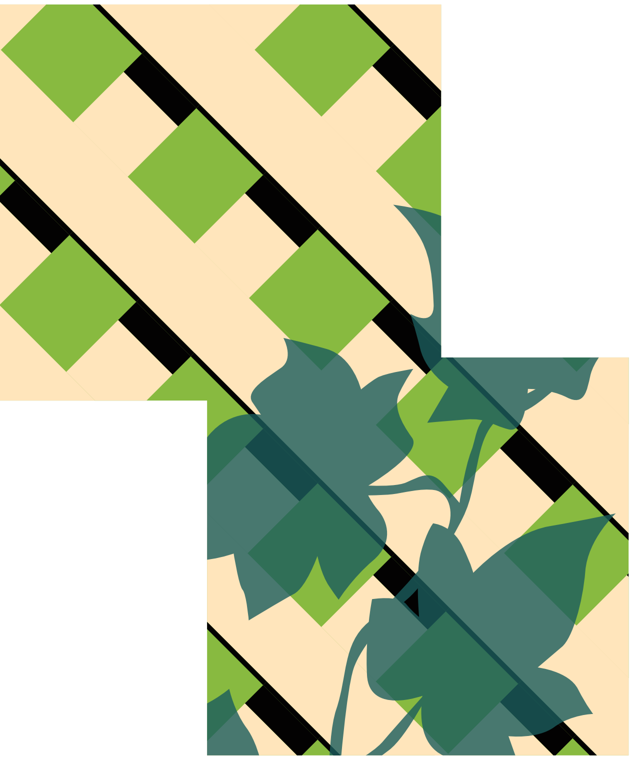
McKinsey: *Turning to the company-wide transformation, what was the case for change?*

Jeroen van Breda Vriesman: Because of the success in the health division, we decided in the summer of 2008 to implement lean across Achmea. Then, the financial crisis hit our industry, which created a sense of urgency and added momentum to the effort. We did something that I'm really proud of: we budgeted only the costs of the implementation. We didn't put the potential efficiency gains in our budget. Why? Because we wanted continuous improvement to be the main topic of discussion—not just meeting the budget.

Change in behavior, change in culture, that's the key. And you don't change culture just by saying, "Meet this budget." You need a different approach. Lean—continuous improvement—is an important part of this story because by changing your company in small steps, you can look back after two years and find that you've made a huge leap. When people in our company know their customers, know how to change processes, and are used to change, they can do bigger things more easily, such as develop new products or implement a new IT system.

McKinsey: *What is the key element of the vision for expanding the transformation to all of Achmea?*

Jeroen van Breda Vriesman: Achmea has traditionally been a decentralized company. If you want to have a more centralized, more unified way of working, you need a single vision for the whole company. So we developed one with the help of 1,200 of our managers. The core of our company-wide vision is the same as the one for our health division. Rooted in our cooperative past and present, the vision is that we put our



customers first. We have four groups of stakeholders: our customers; our shareholders, of which the largest two are cooperative or mutual organizations;[1] our business partners; and, last but not least, our employees. They are all pulling in the same direction because they all benefit from putting the customer first.

What's more, as a company whose shares are not listed on any stock exchange, we are not under pressure to meet the short-term expectations of any one group of our stakeholders. We can take a long-term view in delivering on all fronts and meeting the expectations of all our stakeholders. This means that we can take a long-term view and allow our people to get thoroughly acquainted with lean so that we can truly change the company toward what our customers really want.

McKinsey: *Compared with the health division, what was the greatest challenge in tackling a company-wide transformation?*

Jeroen van Breda Vriesman: Changing a whole company with 20,000 people is very different from changing one division with a staff of 2,200. Because there are so many managers involved, it is harder to make sure you've got the right people in the right places, which is crucial for successful implementation. In some of the cases where we are meeting some resistance, the problem is management capabilities and mind-sets.

McKinsey: *What is the key to getting senior managers really excited and committed to a big transformation like this one?*

Jeroen van Breda Vriesman: It's very important they understand that continuous improvement is not a program with an end point. It's about coming to work every day with a new mind-set. To understand and really feel that distinction is very important. You can almost see in the results whether top management is implementing continuous improvement or just implementing a program. There is no silver bullet to make this change happen. Every manager is different. Some are most excited by changing the culture, some by achieving certain metrics. You have to pull all the levers—good people, better strategy, spend time on culture and behavior, push on results, and discuss every day, week, month, and year. It's a marathon, not a sprint.

McKinsey: *How was the company-wide transformation organized?*

Jeroen van Breda Vriesman: For such a huge change effort, we needed a central program office. Its first task was to identify and build the right change competencies. We started with one external partner for lean, one for behavioral change, and one for the program's management information systems. We're now in the middle of educating, among our own people, 200 lean experts and 20 agents for behavioral change. So we were speeding things up in the beginning with external partners and are now shifting to internal champions. This approach helps us achieve consistency, which is critical as we implement, track progress, and build capabilities

[1] The majority shareholder is Vereniging Achmea (Achmea Association), which represents Achmea's customers. Dutch banking cooperative Rabobank is the second-largest shareholder.

across divisions. When you implement lean, it involves discussions on the executive board but, more important, on a division level and, even more important, on a team level and between employees themselves, because eventually they start every day discussing how yesterday was and how they can do better today.

McKinsey: *Where is Achmea today, compared with the company-wide launch of lean 18 months ago?*

Jeroen van Breda Vriesman: Some 8,000 people will be working in different stages of lean by the end of this year. If you look at team commitment, it's getting a little bit higher every time we measure it. Employee satisfaction is a little bit higher than it was when we started, and the divisions are meeting their efficiency targets.

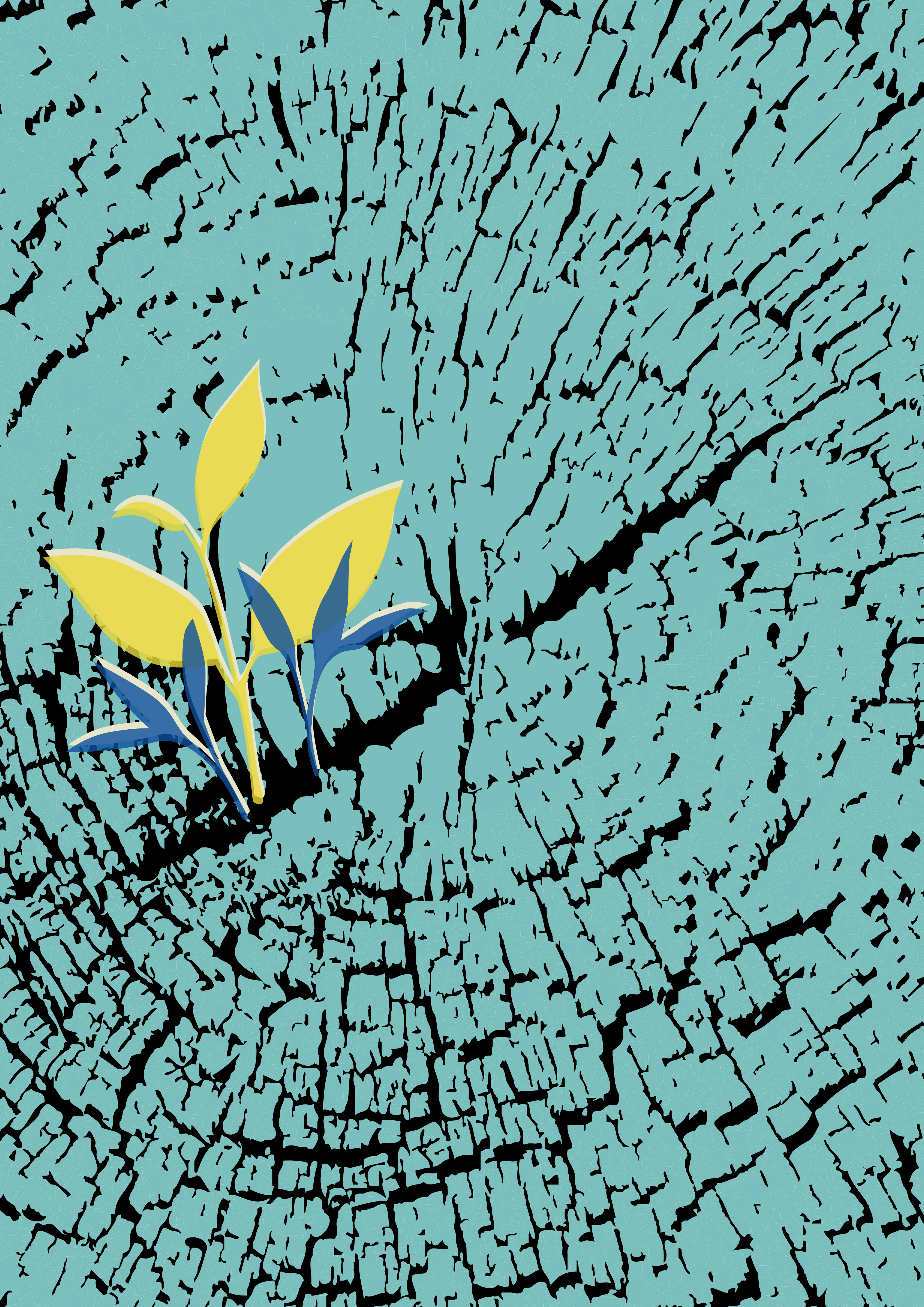
McKinsey: *Looking back at the transformation effort so far, what are the key lessons?*

Jeroen van Breda Vriesman: There are two important lessons. One is to take great care to select and train the right people, because success is so much about good leaders and good people. Almost every time we had a problem, it was essentially a management challenge. The second is about sequencing—first a vision and a strategy and then implementation of lean. Without a vision, people tend to think that lean is simply about reorganizing and cutting costs.

McKinsey: *Looking ahead five years from now, where do you see Achmea?*

Jeroen van Breda Vriesman: We will be implementing our strategy faster; we will have better consumer insights, products, and IT systems; and we will be working better with our customers. All this delivers real value to our customers, shareholders, business partners, and employees. At the end of the day, the concept of continuous improvement puts the employee first as well. She or he has the chance to implement her or his own ideas every day. That's a great way to work. ○

Peter de Wit is a director in McKinsey's Amsterdam office. **Marc van Rooijen,** a director, and **Arne Gast, Edwin van Bommel,** and **Jasper van Ouwerkerk,** all three principals in that office, made important contributions to this interview and the work described in this article.



Reforming the public sector in a crisis:

An interview with Sweden's former prime minister

Alastair Levy
and Nick Lovegrove

Göran Persson has lived a story that should encourage leaders around the world: how to stay in power while pursuing a harsh crisis program that requires sacrifices throughout society.

Government leaders around the world face a daunting dual challenge: they must control and, in the long term, slash major budget deficits fueled by the economic crisis while at the same time improving the performance of the public sector so that it can meet its complex and ever-rising obligations.

Former Swedish prime minister Göran Persson is no stranger to that challenge. Even his political foes recognize his achievement.

In the early 1990s, Sweden suffered its deepest recession since the Great Depression. Although the Swedish crisis was homegrown, its causes and effects resemble the events unfolding in the world today. After years of strong domestic growth driven by easy credit and high leverage, a real-estate bubble burst, leading to the collapse and partial nationalization of the banking sector. Domestic demand plunged as the household savings ratio soared by 13 percentage points. In three years, public debt doubled, unemployment tripled, and the government budget deficit increased tenfold, to more than 10 percent of GDP, the largest in any OECD[1] country at the time.

Persson was appointed finance minister when the Social Democrats returned to power, after the 1994 elections, and became prime minister two years later. In order to regain the confidence of international lenders—and so pave the way for stability and sustainable growth—he knew that Sweden had to reduce its budget deficit dramatically. It took four years for the Swedish government to balance its budget. By 2006, when Persson and his party lost power in the general elections, the country had almost halved its public debt, to just above 40 percent of GDP.

[1] Organisation for Economic Co-operation and Development.

Göran Persson

Vital statistics
Born January 20, 1949, in Vingåker, Sweden

Education
Studied social science at Örebro University, Sweden

Awarded honorary doctorates in medicine from Örebro University, Sweden (2004); in political science from Dankook University, South Korea (2004); and in political science from Tbilisi State University, Georgia (2006)

Career highlights
Prime minister (1996–2006)

Finance minister (1994–96)

Minister of schools, Ministry of Education (1989–91)

Municipal commissioner of Katrineholm (1984–89)

Member of parliament (1979–84 and 1991–2007)

Fast facts
Serves as chairman of the board for Sveaskog, Sweden's largest forest owner

Is a part-time consultant and lecturer

Runs a small cattle and wood farm in Sörmland County, Sweden

Göran Persson spoke with McKinsey's Alastair Levy and Nick Lovegrove about what it takes to put troubled state finances in order and, at the same time, to improve the way the public sector works.

McKinsey: *What is the prerequisite for implementing a successful crisis program?*

Göran Persson: The electorate must understand that drastic measures are required. A crisis program will hurt, and you will need a mandate from the voters if you are to succeed. This makes it difficult for an administration that is in power without such a mandate to take the lead. But it is a fantastic chance for the opposition, provided that there is broad awareness of the gravity of the situation. My party was elected in 1994 because we promised to carry out the harshest program with the deepest budget cuts and the sharpest tax increases.

McKinsey: *What advice would you give incumbent leaders who don't have a mandate from the voters for instituting radical reform?*

Göran Persson: You have to make it absolutely clear that you are putting your office at stake; that you are prepared to call new elections or, if your parliamentary group is not behind you, to resign. The forces working against a harsh crisis program are very strong—almost every area of the public sector has its own vested interests—so any sign that you might waver in your commitment will doom the program to fail.

McKinsey: *Please summarize the lessons you have learned about leading, designing, and implementing the process for putting state finances in order.*

Göran Persson: First, it is extremely important to be in the driver's seat. You must make it clear that you are responsible for the process and that you are prepared to put your position at stake. Second, the consolidation program must be designed so that the burdens are shared fairly. Public-sector cuts will hurt the most vulnerable people in society, so those who are better off need to contribute—for example, by paying higher taxes. Public support for tough policies would quickly deteriorate if they were not perceived as fair, and parliament would lose the political will to make hard decisions. Third, the consolidation program has to be designed as a comprehensive package; if you are in as deep trouble as we were, an ad hoc hodgepodge of measures will only have a limited chance of success. Moreover, by presenting the measures together, it becomes clear to all interest groups that they are not the only ones being asked to make sacrifices. It also has to be a front-loaded program. By starting with the most difficult measures, you demonstrate your resolve and increase the chances of achieving the early results, which will be important for getting the continued support that is critical for sustaining the effort.

Transparency is the fourth lesson. You must never play down the effects of the program's measures. On the contrary, remind the public again and again that this will hurt. It is one thing to get support in parliament for the program; it's another to stay in control during the implementation phase, when the measures become real for ordinary people in their daily lives. You must also be completely honest when you communicate with financial markets. Clarify assumptions and calculations. Don't use any bookkeeping tricks. Only then can you recover credibility; only then can the program earn legitimacy. Indeed, you should always go for conservative estimates. If, for instance, you estimate that economic growth will be 1.5 percent and you end up with 2.5 percent, you will have solved much of the credibility problem.

McKinsey: *The electorate's patience is never endless. How much time do you have until it runs out?*

Göran Persson: You have two years. If you are not in command of the process by then, you will lose momentum and soon face the next election—where you will be replaced. We survived the 1998 election and were rewarded politically for what we had done by being reelected once more in 2002, when the good times returned and we were in firm control of the public finances.

McKinsey: *Cutting the state budget during a crisis puts pressure on the public sector at a time when its services are perhaps more important than ever. How did you handle this problem?*

Göran Persson: Restoring the health of our public finances was the prerequisite for preserving the Swedish public sector in the long term, and this would not have been possible without sacrifices. One-third of our program consisted of tax increases, and two-thirds of spending cuts, both in the operational budgets of the central and local authorities and in the legislated levels of welfare transfers. We cut pensions, sick-leave compensation, and unemployment benefits, which hurt people who already had only small margins in their household finances. That shouldn't have been necessary in an ideal world, because lower welfare transfers reduced domestic demand and tax revenues and thus had a negative impact on growth and employment and a small net effect on the budget. But we had no choice. High interest rates made it necessary to regain the confidence of investors all over the world whose perception was that Sweden's generous welfare model was to blame for the crisis. In fact, it wasn't until we cut unemployment benefits and got into open conflict with the trade unions that market interest rates started coming down.

McKinsey: *It's often said that with a crisis comes an opportunity for reform. Did you use this opportunity to improve the long-term performance of the public sector?*

Göran Persson: Yes, the cuts in government consumption became a driver of improved efficiency, since public authorities were forced to do the same job on unchanged or reduced budgets.

In addition, we pursued targeted policies with various objectives. One strategy—aiming to improve productivity, service quality, and freedom of choice—involved the liberalization of telecommunications, mail, railways, and other infrastructure industries. It also involved allowing privately run providers to compete with public ones in providing tax-financed services for the school system, health care, child care, and care for the elderly.

Another measure was to introduce information technology to broad layers of the population through a tax-deduction scheme that allowed workers to obtain a home computer under a favorable leasing agreement with their employers. The penetration of IT in Sweden during these years outpaced every other country in the world, which made it possible for authorities like the Tax Agency to go online at an early stage. Indeed, I'm quite confident today that information technology improves government productivity as well as the delivery of its services. More and more of the communication between Swedish public agencies and citizens now takes place on the Web, and many Swedes do their annual tax submissions over the Internet, allowing for a very efficient processing of taxes. I think our tax agency is one of the most efficient in the world and very much so because we are using modern technologies. We have one of the world's largest public sectors and, along with the Danes, the world's highest taxes, claiming almost 50 percent of GDP. We are also very good at collecting these taxes.

A third strategy was to give people with basic schooling the chance to complete a secondary education that would qualify them for university studies.[2] It was a straightforward

[2] The *Kunskapslyftet*, or "Knowledge Lift," a Swedish adult-education program.

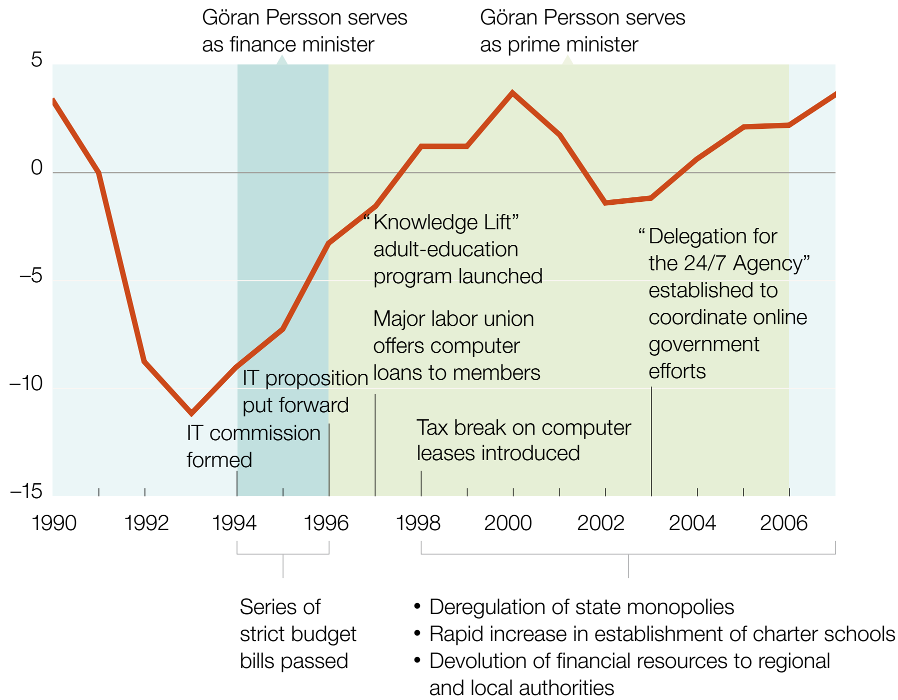
system: an employed worker would get the equivalent of the unemployment benefit if he or she entered an adult-education program and if the employer agreed to replace him or her with an unemployed person. The employer's cost was unchanged, and the state's cost was limited to the education itself. Believe it or not, more than 10 percent of the workforce seized this opportunity between 1997 and 2002. It was mainly women who did so, and many went on to study at a university. When the business cycle turned up again, they became a very good resource on the labor market, not least in the public sector. This education scheme served a dual purpose: it eased the pain of unemployment and increased Sweden's long-term competitiveness by lifting the average competence level of the workforce.

McKinsey: *What approach did you take to set efficiency targets and drive savings across the government?*

Exhibit

Göran Persson oversaw putting state finances in order and reforming Sweden's huge public sector even as his country suffered from a deep economic crisis.

Government net borrowing/net lending as % of GDP



Source: *OECD Factbook 2009: Economic, Environmental and Social Statistics*, Organisation for Economic Co-operation and Development (OECD); McKinsey analysis

Göran Persson: We introduced three-year ceilings on public expenditure for each ministry. Within this ceiling, we gave the ministries and public agencies some flexibility to distribute their expenditure levels between the years in each three-year time frame as long as they reached their final target. These caps on expenditure were the main driving force. Sweden has a decentralized system of government, so even though we set the guidelines it was up to each authority to figure out how to fulfill its service obligations while still achieving the required spending cuts. The budget cuts for the authorities and agencies amounted to a grand total of 11 percent from 1995 to 1998. After that, we built in an efficiency factor based on productivity in the private-service sector, which the public agencies had to match. By doing so, we continued to put pressure on them to improve their efficiency and produce more or the same for less. The result was that they started to examine expenditures that they had regarded as impossible to influence—for instance the location and rental cost of their offices—and they also became more careful about whom to employ and about developing the staff they already had.

“Restoring the health of our public finances was the prerequisite for preserving the Swedish public sector in the long term, and this would not have been possible without sacrifices.”

McKinsey: *As the political leader, what was your experience with trying to get the civil servants on board and making them partners in the initiative?*

Göran Persson: They had never experienced a crisis of this magnitude. Some reacted to it as a professional opportunity to perform a very significant task. Others felt betrayed by the cuts and that it was not their role to deal with productivity or efficiency issues. In the end, though, it was quite easy to get the civil servants on board because they were all conscious of the crisis and its dangers.

McKinsey: *Did you make many personnel changes, particularly in important positions?*

Göran Persson: Only gradually and in a small way. It’s very easy to get rid of people, but it’s difficult to find new ones that you can be sure are better. So I find that it’s often wiser to stick with the staff you have. It is, after all, the politicians who are responsible for restoring order in the country’s finances, so it’s up to them to lead, support, educate, and stimulate those who carry it out. Sometimes you are successful in this regard; sometimes you fail.

McKinsey: *Did you set up some kind of machinery at the center of government to monitor departments and agencies and to intervene, when necessary, to move things along?*

Göran Persson: No, we did not. We were in such acute crisis that we had to move as quickly as we could, so we executed the program without reflecting in detail on its implementation. We monitored two indicators very closely; one was the bottom line of the state finances and the other Sweden’s interest rate levels, because financial markets reacted very quickly to the program and its progress. If I had to do it all again, I would perhaps set up some centralized unit just to monitor progress and to spread ideas and best practices.

McKinsey: *Did the process lead to significant changes in the way government worked and the way it developed and delivered its services?*

Göran Persson: The efficiency targets had positive consequences for public services, at both the state and local levels. At the local level, the targets encouraged public agencies to collaborate, leading to better services for the people. Similarly, as a response to the remit we gave government agencies—such as the tax and social-security authorities—to improve their efficiency to private-sector levels, they started talking to each other and cooperating more closely than before. We didn't plan these changes, but they were positive nevertheless.

The cabinet was another example of change. People tend to view it as a tight-knit team, but it is not. Ministers are constantly competing with each other for the available resources. This was not the case during the crisis. In fact, it was the only time in my 15 years as a cabinet member when I felt that I was leading a real team where everybody was prepared to contribute and to help each other. Why? Because we all understood that the budget deficit, if left unchecked, could destroy the public sector as we knew it. We also knew that beating the crisis required us to work as a team, because if just one minister leaks to the media that his or her area of responsibility is carrying an unfair share of the burden, the whole process will soon break down. You must realize that the cabinet is one thing; the parliament, however, is something else, and you can never take the support of your parliamentary group for granted. If there is the slightest dissension between your ministers, their support groups in parliament could block bills that you are bringing to the assembly. This would be very serious. A budget-consolidation process of this kind requires not only a state budget: the budget needs to be followed by perhaps 50 or 100 different initiatives that all have to pass through parliament. So if you cannot keep your team together, you will find yourself on a very slippery slope.

McKinsey: *What levers did you have at the center for influencing change at ministries that were not making good on their efficiency targets?*

Göran Persson: Each ministry had its own bottom-line target, and if it didn't make good on that target there would be a discussion with the ministries' top managers. Where needed, I or my finance minister became directly involved in discussions with departmental ministers. In doing so, we suggested ways to move forward, but we would never tell them what to do. Giving direct and detailed orders would have broken the internal ethics of the budget-consolidation process—which we had agreed to achieve as a team. It would also have given the finance minister or prime minister ownership of somebody else's task.

In fact, what is taught in the private sector about the importance of building well-functioning top teams applies to government as well, except that it's harder in government. Much more transparency is required, and every little detail can become public knowledge. Moreover, your ownership of the process is under constant threat from the opposition and, perhaps, your own parliamentary group. This makes it essential to build loyalty and solidarity within your team of ministers or else you won't achieve anything. Political leadership is often said to be about visions and ideas. But it is also about ensuring that a transparent public organization can achieve productive results in its daily work not only once but again and again every year, and under constant external pressure. ○

Alastair Levy is a consultant in McKinsey's London office, and **Nick Lovegrove** is a director in the Washington, DC, office.

“Flying people, not planes”:

The CEO of Bombardier on building a world-class culture

Bruce Simpson

Pierre Beaudoin explains how a company driven by engineering goals learned to focus on customer expectations, teamwork, and continuous improvement.

Canada's Bombardier was founded in 1942 to make snowmobiles and similar equipment. Today, it makes trains and airplanes and is the world's number-one train manufacturer and number three in civil aircraft.[1] The company's revenue and stock price have held up during the downturn. Over the past couple of years, it has significantly boosted its investments for growth, most notably an entirely new airplane design: the CSeries, a transcontinental commercial airliner with significantly lower emissions and running costs than existing planes have.

Pierre Beaudoin, CEO and president since 2008, attributes the company's resilience in large part to its culture. He led a complete transformation of that culture over much of the past decade, beginning as president of Bombardier Aerospace. The transformation changed Bombardier from a company driven by engineering and manufacturing goals, with deep cultural divisions, to one focused on customers, an engaged workforce, and continuous improvement.

Beaudoin talked with McKinsey's Bruce Simpson at the company's Montreal headquarters about how he persuaded engineers to pursue "soft" goals and discussed the business value of implementing them.

McKinsey: *You became president of the Aerospace Division in 2001 and very quickly began a transformation. What was happening?*

Pierre Beaudoin: For us, 2001 was a very challenging year. Obviously, 9/11 was a shock to the airline industry. But, in that same year, we also made a huge acquisition in rail transportation—Adtranz from DaimlerChrysler—more than doubling our size, and as part of our Recreational Products Group we bought the Evinrude and Johnson brands.[2] So we had a year of expansion and, at the same time, we had a year where the business slowed down. The result was that a lot of the rocks came to the surface in terms of Bombardier's capabilities and structure.

We'd gotten into the aerospace business in 1986, and we grew rapidly from about 12 aircraft a year to about 400, going from a small player in the industry to leading in the business aircraft and regional-aircraft segments. To do that, we had organized as functions rather than business units, and responsibilities were not clear across the organization. This served us well for the growth period because engineers designed products, manufacturing people manufactured—we had very strong functions that gave us a lot of focus. But we forgot about the customer and about delivering a good experience overall.

So in 2001, we had an organization that was very proud of being number one and had all kinds of metrics to measure why we were very good. But when we talked to our customers, they were saying we weren't very good. And when business slows down and you've got issues, you're going to have to fix them.

McKinsey: *What led you to focus on culture?*

Pierre Beaudoin: Everyone in management recognized we had a problem but insisted it wasn't in their department. So my leadership team and I quickly realized that the division would be very hard to transform if we only focused on fixing this piece of hardware or fixing that system, because the people in the system thought that what they were doing themselves was working well.

One of the important initiatives that helped me understand how to talk about the problems was surveying our employees. They were telling us that we're very focused on hardware. But I knew that the customer doesn't really care about the hardware; he cares about his flight. We had employees explaining that the customer shouldn't really care if the video didn't work [as long as] the plane actually flew. But if the number-one thing for the customer is the experience he gets in the cabin, who are we to tell him he's wrong? We needed employees to understand we were flying people, not planes.

[1] These rankings are calculated based on a mix of existing orders for equipment (such as rolling stock, locomotives, and systems), combined with revenue from maintenance, signaling equipment, and other services.
[2] Bombardier later sold its Recreational Products Group, in 2003.

“If you want to make a change, you need the people who are willing to make themselves vulnerable, who are willing to learn, to work in teams, to promote the leadership skills that we agree are important.”

Our employees also said it was very hard for them to support where the company was going because they didn’t know what we really valued as an organization. In fact, we’d asked our employees what objectives they thought we valued, and although we had very big strategic plans, nobody could answer the question. For any team to pull in the same direction, it has to know what you’re looking for and feel a connection.

At the management level, there were cultural problems too: the culture was about avoiding putting facts on the table. All the goals were defined so that management would feel pretty good about its performance; we’d go to a leadership forum and spend three days telling each other why we were good. And if a person brought up a problem, someone else would say, “Yes, but you didn’t really understand the issue properly; we’re actually really good.” It was a culture of not facing up to issues, of blaming another department.

In addition, there were a lot of silos. People were focused on their own tasks. And it was a culture where we valued the “firefighter,” the person who would step on everybody but get the job done in a crisis. There was very little teamwork.

McKinsey: *How did these insights help you shape the transformation?*

Pierre Beaudoin: We’ve all seen quick turnarounds in companies where they got good results in the short term by doing some very drastic things. You can cut R&D, you can cut expenses, that’s easy. But when you’re building a business like aerospace, which is all long-term stuff, if you cut corners then you’re going to pay for it later. A culture change takes a little bit more time up front, but, once it starts moving, then it moves even faster because more people are engaged. So it was a bit of a leap of faith, but we thought it would be worthwhile.

So once we identified the problems, we specified three priorities and four leadership skills to address them. The priorities were creating a rewarding and safe workplace, providing superior customer service, and reducing waste in everything we do. On the leadership side, the skills were people first, teamwork, continuous improvement, and drive for results. In the longest term, we set a goal of becoming world class in all of our operations.

McKinsey: *How did you begin?*

Pierre Beaudoin: By asking our 100 top leaders how they would approach the situation—who are we and who do we want to become?

Because nobody wanted to talk about themselves, we really had to force ourselves to look in the mirror and say, “The first thing you have to recognize, if we’re going to fix this organization, is that you, as a leader, have things to address.” Asking leaders to make themselves vulnerable is not that easy. If you’re seen as a person who always makes good decisions, always delivers, you’re going to progress. And now we’re asking people to say, “Yes, but some of my leadership skills are not acceptable to this organization, and that’s where I need to focus.”

Pierre Beaudoin

Vital statistics
Born June 13, 1962, in Québec City, Canada

Married, with 2 children

Education
Earned a degree in industrial relations from McGill University Engineering College

Career highlights
Bombardier
(1985–present)

President and CEO (2008–present)

Director (2004–present)

Executive vice president (2004–08)

President and COO, Bombardier Aerospace (2001–04)

Fast facts
Director of Power Corporation of Canada and Bombardier Recreational Products

I think our leadership appreciated this in the end. But the process also told us very quickly which people would stay with us and which would decide it's not for them. It's not about making it personal, but if you want to make a change, you need the right people on board. You need the people who are willing to make themselves vulnerable, the people who are willing to learn, to work in teams, to promote the leadership skills that we agree are important.

These calls are difficult to make. Some of our very high-performing individuals really didn't behave properly. The organization was very resistant to moving these people out. The conversation we had to have as an organization was, in essence, can we live without this or that individual? And it's just not true that one individual carries a company of 30,000 people on his back.

McKinsey: *Did the change in goals—from "it's just the hardware" to "it's whether the video works"—help you or hurt you as you were redefining which goals the high performers needed to meet?*

Pierre Beaudoin: Both. At the beginning, there were a lot of people who resisted, who said this organization will never be successful again because there aren't enough hard goals and there's too much softness within the goals. You can imagine a crowd of very technical people asking, "Why do you care about a rewarding workplace? This is just going to become a really nice place where we're all nice to each other, but we won't get the work done."

But the whole idea was that while we focused on the soft stuff, we didn't let go of the hard stuff. The performance objectives were really clear right from the start—going from an EBIT[3] margin of 2 or 3 percent to 8 percent, a $500 million improvement. We made it very clear that that was where we wanted to go. And we achieved that goal.

The point is, you're in business. Whatever you do, it's about making the business more financially successful. We translated the soft goals into hard measurements too.

It was a challenge for me and for my leadership team to explain why we were spending so much time on the soft stuff when we could be fixing factories, hardware, airplanes. We had lots of conversations explaining that, if we did the soft stuff right, our employees, with our help, would be more able to do what they're supposed to do, like make our factories efficient and work on engineering problems. For Bombardier, that's a hard change. We are hardware people, and we like getting into the planes and the technical problems.

The goal was to really enable the front line to take a lot more initiative. We didn't get it done rapidly; you don't change a culture rapidly. When you have 30,000 employees, it takes time.

McKinsey: *Can you talk a bit more about how you translated soft goals into hard metrics and high-level goals into goals with meaning to individuals and whole departments?*

Pierre Beaudoin: After the first push, we implemented a system—the achieving-excellence system—that helps employees progress from where they are today, wherever that is, to being part of a fully engaged, world-class company. We call that level "diamond" and, currently, as a company, we're working toward "gold," just two steps below. It's taken a journey of six years to get there.

Connecting goals to each person's day-to-day work is important. Take the goal to "eliminate waste in everything that you do." A simple sentence like that works for everybody. If you're somebody in the factory, you can understand what waste is and you can find yourself in that goal. And someone in the office can do the same. The metrics they use would be different because the idea of "waste" is different, but it's tangible in both situations and can be tied to the very clear high-level goal.

The first step isn't even about trying to find the exact metrics that would lead to the ultimate goal of becoming world class; it's just about setting any kind of goals. Because what we find is that if you go to an office of ten people who work together and you say, "What are your goals," they'll talk about the corporation's goal. And then you'll say, "So how do you do it day to day, and what do you measure?" It's not that easy, but eventually each group of employees can find something for their department.

Sometimes you have to tolerate initial goals that are not completely linked to the corporate goal. Why? Well, that takes us to measuring something. And if that group of employees learns to work as a team, to focus on those goals, then you say, "OK, now we're ready to get a little bit tougher in the way the goals are defined." And people have become more comfortable at setting goals.

McKinsey: *How did you begin to implement these changes in Bombardier's operations?*

Pierre Beaudoin: We started by identifying discrete projects that were small enough to show the organization fairly quickly that if we accepted change, we could succeed. There were five or six. Once these were working, we could take the doubters to see them, and the employees who had been involved in the successes could talk to the others. We believed that if we could involve about 30 percent of the organization that transformed in this way, the ideas would catch on in the whole organization.

[3] Earnings before interest and taxes.

One of these involved our Learjet factory in Belfast. We assembled the fuselage of the Learjet 45 there. The changes were in part a lean approach, but really an approach where we engaged everybody in a different way of working, focusing on the three priorities. When we approached the Belfast employees, they said, "Well, maybe there's still some room for improvement here, but not much, because we've been making these fuselages for ten years." We tried, though, and the changes took about a year and a half to implement. In the end, we achieved a 25 to 35 percent improvement in quality and productivity.

Beyond those projects, though, it was very important to get more people who could spread the ideas across the organization. We had a group of champions—leaders of the demonstration projects and others who had been trained in the new ways of working and spent all their time teaching others. And I would meet with them, weekly at the beginning and then monthly, to make sure that they were getting enough support in the organization to really lead change.

McKinsey: *Looking back at this point, how successful has the transformation been?*

Pierre Beaudoin: The way I define success is that we have a much more engaged organization today. The level of engagement in employee surveys has climbed more than 15 percent since 2004, and 85 percent of employees responded to our last survey. I'm particularly happy because, in past recessions, the first thing that fell was employee engagement, and this time it's holding firm. This means that we have an organization that's much more resilient to external shocks. In addition, we were recently named the third most admired and trusted brand in Canada in a survey of consumers; the survey also ranked our workplace second most admired.[4] And we have good financial performance. We're going through a storm like this industry has never seen, and we're still achieving good results and meeting customer expectations with an engaged workforce.

What I like most, though, is that we now have an organization that wants to get better. And that's the key. We always talk about why we're not there yet; we're on a journey—how close are we to those world-class metrics? We used to make excuses for why our performance was good enough. Today we say, "What will it take to get to world class?" That is what has changed.

McKinsey: *Now you're CEO of the whole corporation. As you think about the next transformation, what would you do differently?*

Pierre Beaudoin: The most important thing would be to create even more of a sense of urgency. I spent a lot of time communicating, engaging with other leaders, yet I feel I should have done even more to engage leaders and the workforce. Also, in some cases—particularly with people who just weren't going to change and weren't going to work with a team—we should have made decisions about them earlier.

McKinsey: *You've recently defined what you call "our way forward" for Bombardier. This idea has roots in the aerospace transformation, doesn't it?*

[4] Joint survey between Global Reputation Pulse and *Canadian Business* magazine.

Pierre Beaudoin: Yes, it's about the priorities that I want this organization to focus on and how I'm going to measure them. The planning was much the same: discussing with our leadership team and our employees what we should focus on that would be common to everyone and that people could understand as meaningful goals in their day-to-day work. At Bombardier as a whole, that work was made easier because the president of the Transportation Group, André Navarri, had also led a performance transformation.

One other very important thing I learned at [Bombardier] Aerospace is that if we set three or four goals, our job as leaders should be pretty simple because after that you stick to those goals for several years. It doesn't work if you change goals year to year. In a large organization, people can't follow you that way. So the way forward for me is what Bombardier should focus on for the next five, six, seven years. Maybe it'll be longer than that, and some goals may evolve, but I see that these goals will be our focus for quite some time. And then my job becomes driving these goals across the organization. There are five areas of focus: becoming number one in customer satisfaction through flawless execution, raising our game in global talent management, actively managing risks, establishing local roots in all key markets, and enhancing our corporate social responsibility.

For example, one strategic goal is creating more of a presence in Asia. So with the additional goal of local roots, the Bombardier of tomorrow has to be a Bombardier that develops more management teams aligned with where our business is going to be in the world. We often start with expatriate managers, but we quickly need to develop local roots, local relationships, and a local team—and to teach those people about Bombardier. Local people can be very good, but if they don't understand your company, if they don't understand what you value, then you won't succeed. Doing what needs to be done takes time.

But if you're able to talk very precisely about the goals you have as a company, it certainly helps you understand what kinds of behaviors and what kinds of people you're looking for. Just recently, I was at our factory in India—where the Transportation Group is building subway cars for the Delhi metro—to meet our 900 employees. And using the simple elements of “the way forward,” I was able to talk to them about where this company’s going. Those goals translate well into any culture, just as the goals of the aerospace transformation translated into everyone’s day-to-day work.

McKinsey: *The cultural capabilities that the aerospace transformation created have helped you capture some new opportunities, such as the CSeries airplane, haven’t they?*

Pierre Beaudoin: Yes, I think the CSeries is possible today because of the transformation. People say, in aerospace you have to bet the company when you develop a new airplane. Well, the CSeries is a $3 billion investment and we have $3 billion of equity. It’s true.

Developing an airplane has to be done with great teamwork. Suppose I come to a meeting and hear about four problems, and I slam my fists on the table and say, “I don’t want to hear about problems anymore; you guys are there to fix them.” Well, guess what—I’m not going to hear about problems. And that’s how you get yourself in deep trouble in airplanes: the problems surface too late. Developing a complex product like an airplane, there will be problems every day. To get it right, the team has to work together, share the problems, fix them, make our engineers comfortable bringing an issue to the table so we can give them the tools to fix it.

In addition, part of that transformation was getting trust back from our suppliers, who had sometimes felt that they got burned in our fast-growth period. The CSeries is a great example of how we were able to get our suppliers on board, getting them to invest and to trust that we’ll give them the information and coaching they need to progress. This can be challenging, especially in China, where there can be controversy over technology transfer. So when we hit some hurdles, we have to work extra hard to be in this together.

Today, with the progress we’ve made, we have the ability and the trust to do both of these things. o

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