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Agile compendium

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GO AGILE

Introduction

Agile is a lot of things, but it isn't new, chaotic or just a fad. Simply put, agile is a set of principles that allows leaders, teams and entire organizations to anticipate and respond to change. Its elegant simplicity is what makes it both incredibly powerful and somewhat hard to grasp as an operating model, accustomed as we are to the complex, matrixed organizations of today.

No company is immune to the changes brought on by the speed at which our digitally connected and increasingly interconnected world now functions. We all need a new way of working to survive and thrive in this environment.

Machine learning, AI and automation are impacting the type of work that gets done, the kinds of products/services that are produced and how companies engage with customers and other stakeholders. At the same time, a new generation of workers has very different expectations and needs. Enterprise agility not only promises to enable this new way of working, it actually delivers.

Agile organizations are truly different. Whereas "traditional" organizations are static, siloed and hierarchical, agile organizations act as a network of teams operating in rapid learning and fast decision cycles. Traditional organizations place the most powerful governance bodies at the top with goals and decision rights flowing down the hierarchy; agile organizations instil a powerful common purpose and leverage new data and insights to delegate decisions to teams closest to the information. But agility is not a chaotic free-for-all. Non-negotiable backbone processes define the 'rules of the game' and technology is deployed in service of collaboration and radical transparency. In this way, agile organizations manage to combine velocity and adaptability with stability and efficiency.

The benefits of an agile operating model are well documented: greater customer centricity, faster time to market, higher revenue growth, lower costs and a more engaged workforce. Little wonder then that agility is catching fire. A recent *McKinsey Quarterly* survey of 2,500 business leaders found three quarters of respondents across industries and geographies said enterprise agility is a top priority, yet only 4 percent of respondents said their company had fully implemented an agile transformation. This reflects the challenge that many companies encounter when trying to capture the promise of agility and turn it in to reality—getting starting is easy, scaling is hard.

An agile transformation is exactly that: transformative. In this collection we explore the structural and cultural shifts required to go agile as well as the surprising amount of conviction and personal changes required from senior leaders. Finally, executives from a range of industries share stories of their journeys to becoming agile.

—Sherina, Krish and Shail on behalf of the agile community at McKinsey

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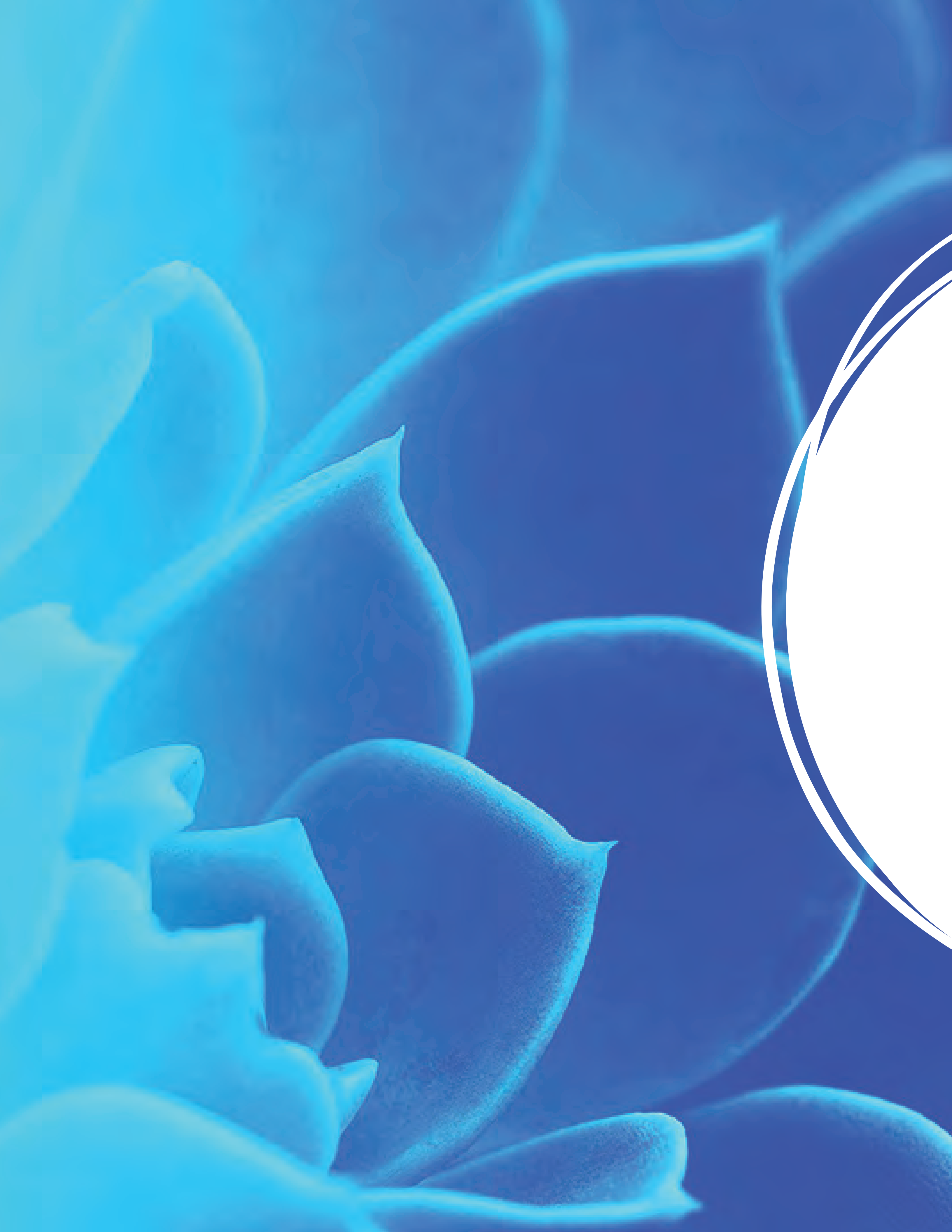
Table of contents



1

Organizing for agility

The five trademarks of agile organizations

Report, January 2018 | By Wouter Aghina, Aaron De Smet, Gerald Lackey, Michael Lurie, and Monica Murarka

Agile organizations—of any size and across industries—have five key elements in common.

This article was written collaboratively by the McKinsey Agile Tribe, a group of over 50 global colleagues bringing expertise from the digital, operations, marketing, and organization disciplines. They integrate their deep experience and thought leadership to extract the best from McKinsey's global experience as it helps organizations transform themselves into agile organizations.

Our experience and research demonstrate that successful agile organizations consistently exhibit the five trademarks described in this article. The trademarks include a network of teams within a people-centered culture that operates in rapid learning and fast decision cycles which are enabled by technology, and a common purpose that co-creates value for all stakeholders. These trademarks complement the findings from "How to create an agile organization."

The old paradigm: Organizations as machines

A view of the world—a paradigm—will endure until it cannot explain new evidence. The paradigm must then shift to include that new information. We are now seeing a paradigm shift in the ways that organizations balance stability and dynamism.

First, the old paradigm. In 1910, the Ford Motor Company was one of many small automobile manufacturers. A decade later, Ford had 60 percent market share of the new automobile market worldwide. Ford reduced assembly time per vehicle from 12 hours to 90 minutes, and the price from $850 to $300, while also paying employees competitive rates.[1]

What is an agile organization?

The dominant "traditional" organization (designed primarily for stability) is a static, siloed, structural hierarchy – goals and decisions rights flow down the hierarchy, with the most powerful governance bodies at the top (i.e., the top team). It operates through linear planning and control in order to capture value for shareholders. The skeletal structure is strong, but often rigid and slow moving.

In contrast, an agile organization (designed for both stability and dynamism) is a network of teams within a people-centered culture that operates in rapid learning and fast decision cycles which are enabled by technology, and that is guided by a powerful common purpose to co-create value for all stakeholders. Such an agile operating model has the ability to quickly and efficiently reconfigure strategy, structure, processes, people, and technology toward value-creating and value-protecting opportunities. An agile organization thus adds velocity and adaptability to stability, creating a critical source of competitive advantage in volatile, uncertain, complex, and ambiguous (VUCA) conditions.

1 "100 years of the moving assembly line," Ford Motor Company, ford.com

Ford's ideas, and those of his contemporary, Frederick Taylor, issued from scientific management, a breakthrough insight that optimized labor productivity using the scientific method; it opened an era of unprecedented effectiveness and efficiency. Taylor's ideas prefigured modern quality control, total-quality management, and—through Taylor's student Henry Gantt—project management.

Gareth Morgan describes Taylorist organizations such as Ford as hierarchical and specialized—depicting them as machines.[2] For decades, organizations that embraced this machine model and the principles of scientific management dominated their markets, outperformed other organizations, and drew the best talent. From Taylor on, 1911 to 2011 was "the management century."

Disruptive trends challenging the old paradigm

Now, we find the machine paradigm shifting in the face of the organizational challenges brought by the "digital revolution" that is transforming industries, economies, and societies. This is expressed in four current trends:

- **Quickly evolving environment.** All stakeholders' demand patterns are evolving rapidly: customers, partners, and regulators have pressing needs; investors are demanding growth, which results in acquisitions and restructuring; and competitors and collaborators demand action to accommodate fast-changing priorities.

- **Constant introduction of disruptive technology.** Established businesses and industries are being commoditized or replaced through digitization, bioscience advancements, the innovative use of new models, and automation. Examples include developments such as machine learning, the Internet of Things, and robotics.

- **Accelerating digitization and democratization of information.** The increased volume, transparency, and distribution of information require organizations to rapidly engage in multidirectional communication and complex collaboration with customers, partners, and colleagues.

- **The new war for talent.** As creative knowledge- and learning-based tasks become more important, organizations need a distinctive value proposition to acquire—and retain—the best talent, which is often more diverse. These "learning workers" often have more diverse origins, thoughts, composition, and experience and may have different desires (for example, millennials).

When machine organizations have tried to engage with the new environment, it has not worked out well for many. A very small number of companies have thrived over time; fewer than 10 percent of the non-financial S&P 500 companies in 1983 remained in the S&P 500 in 2013. From what we have observed, machine organizations also experience constant internal churn. According to our research with 1,900 executives, they are adapting their strategy (and their organizational structure) with greater frequency than in the past. Eighty-two percent of them went through a redesign in the last three years. However, most of these redesign efforts fail—only 23 percent were implemented successfully.[3]

2 Gareth Morgan, *Images of organization*, Beverley Hills, CA: Sage Publications, 1986.

3 Steven Aronowitz, Aaron De Smet and Deidre McGinty, "Getting organizational design right," *McKinsey Quarterly*, June 2015.

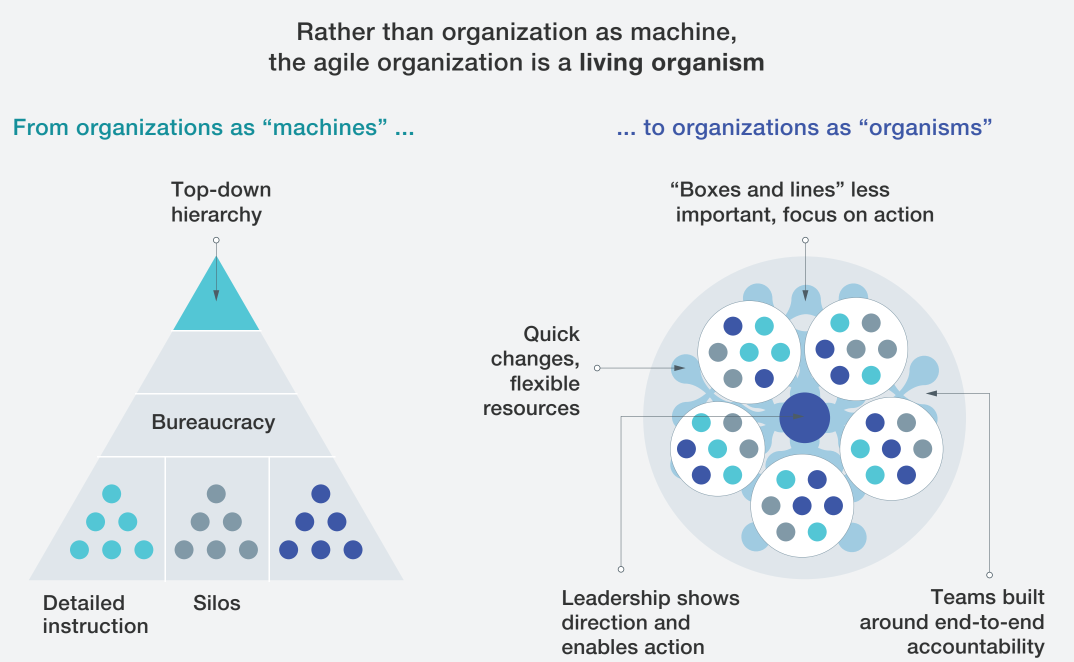
The new paradigm: Organizations as living organisms

The trends described above are dramatically changing how organizations and employees work. What, then, will be the dominant organizational paradigm for the next 100 years? How will companies balance stability and dynamism? Moreover, which companies will dominate their market and attract the best talent?

Our article "Agility: It rhymes with stability" describes the paradigm that achieves this balance and the paradox that truly agile organizations master—they are both stable and dynamic at the same time. They design stable backbone elements that evolve slowly and support dynamic capabilities that can adapt quickly to new challenges and opportunities. A smartphone serves as a helpful analogy; the physical device acts as a stable platform for myriad dynamic applications, providing each user with a unique and useful tool. Finally, agile organizations mobilize quickly, are nimble, empowered to act, and make it easy to act. In short, they respond like a living organism (Exhibit 1).

Exhibit 1

The agile organization is dawning as the new dominant organizational paradigm.



When pressure is applied, the agile organization reacts by being more than just robust; performance actually improves as more pressure is exerted.[4] Research shows that agile organizations have a 70 percent chance of being in the top quartile of organizational health, the best indicator of long-term performance.[5] Moreover, such companies simultaneously achieve greater customer centricity, faster time to market, higher revenue growth, lower costs, and a more engaged workforce:

4 We include in our sense of agile the idea—coined in the work of Nicholas Taleb—that this is "anti-fragile."

5 Michael Bazigos, Aaron De Smet, and Chris Gagnon, "Why agility pays," *McKinsey Quarterly,* December 2015.

- A global electronics enterprise delivered $250 million in EBITDA, and 20 percent share price increase over three years by adopting an agile operating model with its education-to-employment teams.

- A global bank reduced its cost base by about 30 percent while significantly improving employee engagement, customer satisfaction, and time to market.

- A basic-materials company fostered continuous improvement among manual workers, leading to a 25 percent increase in effectiveness and a 60 percent decrease in injuries.

As a result agility, while still in its early days, is catching fire. This was confirmed in a recent *McKinsey Quarterly* survey report of 2,500 business leaders.[6] According to the results, few companies have achieved organization-wide agility but many have already started pursuing it in performance units. For instance, nearly one-quarter of performance units are agile. The remaining performance units in companies lack dynamism, stability, or both.

However, while less than ten percent of respondents have completed an agility transformation at the company or performance-unit level, most companies have much higher aspirations for the future. Three-quarters of respondents say organizational agility is a top or top-three priority, and nearly 40 percent are currently conducting an organizational-agility transformation. High tech, telecom, financial services, and media and entertainment appear to be leading the pack with the greatest number of organizations undertaking agility transformations. More than half of the respondents who have not begun agile transformations say they have plans in the works to begin one. Finally, respondents in all sectors believe that more of their employees should undertake agile ways of working (on average, respondents believe 68 percent of their companies' employees should be working in agile ways, compared with the 44 percent of employees who currently do).

The rest of this article describes the five fundamental "trademarks" of agile organizations based on our recent experience and research. Companies that aspire to build an agile organization can set their sights on these trademarks as concrete markers of their progress. For each trademark, we have also identified an emerging set of "agility practices"—the practical actions we have observed organizations taking on their path to agility (Exhibit 2).

The five trademarks of agile organizations

While each trademark has intrinsic value, our experience and research show that true agility comes only when all five are in place and working together. They describe the organic system that enables organizational agility.

Linking across them, we find a set of fundamental shifts in the mind-sets of the people in these organizations. Make these shifts and, we believe, any organization can implement these trademarks in all or part of its operations, as appropriate.

1. North Star embodied across the organization

Mind-set shift

From: *"In an environment of scarcity, we succeed by capturing value from competitors, customers, and suppliers for our shareholders."*

To: *"Recognizing the abundance of opportunities and resources available to us, we succeed by co-creating value with and for all of our stakeholders."*

6 Karin Ahlbäck, Clemens Fahrbach, Monica Murarka and Olli Salo, "How to create an agile organization," October 2017.

Agile organizations reimagine both whom they create value for, and how they do so. They are intensely customer-focused, and seek to meet diverse needs across the entire customer life cycle. Further, they are committed to creating value with and for a wide range of stakeholders (for example, employees, investors, partners, and communities).

To meet the continually evolving needs of all their stakeholders, agile organizations design distributed, flexible approaches to creating value, frequently integrating external partners directly into the value creation system. Examples emerge across many industries, including: modular products and solutions in manufacturing; **agile supply chains** in distribution; distributed energy grids in power; and platform businesses like Uber, Airbnb, and Upwork. These modular, innovative business models enable both stability and unprecedented variety and customization.

To give coherence and focus to their distributed value creation models, agile organizations set a *shared purpose and vision*—the "North Star"—for the organization that helps people feel personally and emotionally invested. This North

Exhibit 2

There are five trademarks of agile organizations.

	Trademark	Core principles
Strategy	**North Star embodied across the organization**	• Shared purpose and vision • Sensing and seizing opportunities • Flexible resource allocation • Actionable strategic guidance
Structure	**Network of empowered teams**	• Clear, flat structure • Clear accountable roles • Hands-on governance • Robust communities of practice • Active partnerships and ecosystem • Open physical and virtual environment • Fit-for-purpose accountable cells
Process	**Rapid decision and learning cycles**	• Rapid iteration and experimentation • Standardized ways of working • Performance orientation • Information transparency • Continuous learning • Action-oriented decision making
People	**Dynamic people model that ignites passion**	• Cohesive community • Shared and servant leadership • Entrepreneurial drive • Role mobility
Technology	**Next-generation enabling technology**	• Evolving technology architecture, systems,and tools • Next-generation technology development and delivery practices

Star serves as a reference when customers choose where to buy, employees decide where to work, and partners decide where to engage. Companies like Amazon, Gore, Patagonia, and Virgin put stakeholder focus at the heart of their North Star and, in turn, at the heart of the way they create value.

Agile organizations that combine a deeply embedded North Star with a flexible, distributed approach to value creation can *rapidly sense and seize opportunities*. People across the organization individually and proactively watch for changes in customer preferences and the external environment and act upon them. They seek stakeholder feedback and input in a range of ways (for example, product reviews, crowd sourcing, and hackathons). They use tools like customer journey maps to identify new opportunities to serve customers better, and gather customer insights through both formal and informal mechanisms (for example, online forums, in-person events, and start-up incubators) that help shape, pilot, launch, and iterate on new initiatives and business models.

These companies can also allocate resources flexibly and swiftly to where they are needed most. Companies like Google, Haier, Tesla, and Whole Foods constantly scan the environment. They regularly evaluate the progress of initiatives and decide whether to ramp them up or shut them down, using standardized, fast resource-allocation processes to shift people, technology, and capital rapidly between initiatives, out of slowing businesses, and into areas of growth. These processes resemble venture capitalist models that use clear metrics to allocate resources to initiatives for specified periods and are subject to regular review.

Senior leaders of agile organizations play an integrating role across these distributed systems, bringing coherence and providing clear, actionable, strategic guidance around priorities and the outcomes expected at the system and team levels. They also ensure everyone is focused on delivering tangible value to customers and all other stakeholders by providing frequent feedback and coaching that enables people to work autonomously toward team outcomes.

2. Network of empowered teams

Mind-set shift

From: *"People need to be directed and managed, otherwise they won't know what to do—and they'll just look out for themselves. There will be chaos."*

To: "*When given clear responsibility and authority, people will be highly engaged, will take care of each other, will figure out ingenious solutions, and will deliver exceptional results."*

Agile organizations maintain a stable top-level structure, but replace much of the remaining traditional hierarchy with a flexible, scalable network of teams. Networks are a natural way to organize efforts because they balance individual freedom with collective coordination. To build agile organizations, leaders need to understand human networks (business and social), how to design and build them, how to collaborate across them, and how to nurture and sustain them.

An agile organization comprises a dense network of empowered teams that operate with high standards of alignment, accountability, expertise, transparency, and collaboration. The company must also have a stable ecosystem in place to ensure that these teams are able to operate effectively. Agile organizations like Gore, ING, and Spotify focus on several elements:

- Implement *clear, flat structures* that reflect and support the way in which the organization creates value. For example, teams can be clustered into focused performance groups (for example, "tribes," or a "lattice") that share a common mission. These groups vary in size, typically with a maximum of 150 people. This number reflects both practical experience and Dunbar's research on the number of people with whom one can maintain personal relationships and effectively collaborate.[7] The number of teams within each group can be adapted or scaled to meet changing needs.

- Ensure *clear, accountable roles* so that people can interact across the organization and focus on getting work done, rather than lose time and energy because of unclear or duplicated roles, or the need to wait for manager approvals. Here, people proactively and immediately address any lack of clarity about roles with one another, and treat roles and people as separate entities; in other words, roles can be shared and people can have multiple roles.

- Foster *hands-on governance* where cross-team performance management and decision rights are pushed to the edge of boundaries.[8] It is at this interaction point that decisions are made as close to relevant teams as possible, in highly-productive, limited-membership coordinating forums. This frees senior leaders to focus on overall system design and provide guidance and support to responsible, empowered teams that focus on day-to-day activities.

- Evolve functions to become robust *communities of knowledge and practice* as professional "homes" for people, with responsibilities for attracting and developing talent, sharing knowledge and experience, and providing stability and continuity over time as people rotate between different operating teams.

- Create active *partnerships and an ecosystem* that extends internal networks and creates meaningful relationships with an extensive external network so the organization can access the best talent and ideas, generate insights, and co-develop new products, services, and/or solutions. In agile organizations, people work hands-on and day-to-day with customers, vendors, academics, government entities, and other partners in existing and complementary industries to co-develop new products, services, and/or solutions and bring them to market.

- Design and create *open physical and virtual environments* that empower people to do their jobs most effectively in the environment that is most conducive to them. These environments offer opportunities to foster transparency, communication, collaboration, and serendipitous encounters between teams and units across the organization.

Like the cells in an organism, the basic building blocks of agile organizations are *small fit-for-purpose performance* cells. Compared with machine models, these performance cells typically have greater autonomy and accountability, are more multidisciplinary, are more quickly assembled (and dissolved), and are more clearly focused on specific value-creating activities and performance outcomes. They can be comprised of groups of individuals working on a shared task (i.e., teams) or networks of individuals working separately, but in a coordinated way. Identifying what type of performance cells to create is like building with Lego blocks. The various types (Exhibit 3) can be combined to create multiple tailored approaches.

The three most commonly observed agile types of performance cell today include:

- *Cross-functional teams* deliver 'products' or projects, which ensure that the knowledge and skills to deliver desired outcomes reside within the team. These teams typically include a product or project owner to define the vision and prioritize work.

- *Self-managing teams* deliver baseload activity and are relatively stable over time. The teams define the best way to reach goals, prioritize activities, and focus their effort. Different team members will lead the group based on their competence rather than on their position.

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7 Drake Bennett, "The Dunbar Number, From the Guru of Social Networks," Bloomberg, January 2013, bloomberg.com

8 David S. Alberts and Richard E. Hayes, "Power to the Edge: Command and Control in the Information Age," *Command and Control Research Program Publication Series*, April 2005 reprint, dodccrp.org

Exhibit 3

There are different types of agile building blocks.

Agile blocks	Description	Nature of work	Process
1. Cross-functional teams	Coordination among product owners on priority and vision; coordination across teams on how to deliver Teams composed of different functional expertise and form different levels of the organizations	Typically team-based, connected, and integrated	Product development, product launch
2. Self-managing teams	Stable teams define their ways of working and are jointly accountable for end-to end performance against key performance indicators	Typically team-based, stand-alone, repetitive	Customer services, sales, manufacturing
3. "Flow to work" pools	Pool of individuals staffed to different tasks full-time, based on priority of needs; tasks can vary from hours to months	Typically individual, stand-alone, repetitive	Corporate services, (HR, legal, etc)

- *Flow-to-the-work pools* of individuals are staffed to different tasks full-time based on the priority of the need. This work method can enhance efficiencies, enable people to build broader skillsets, and ensure that business priorities are adequately resourced.

However, other models are continuously emerging through experimentation and adaptation.

3. Rapid decision and learning cycles

Mind-set shift

From: *"To deliver the right outcome, the most senior and experienced individuals must define where we're going, the detailed plans needed to get there, and how to minimize risk along the way."*

To: *"We live in a constantly evolving environment and cannot know exactly what the future holds. The best way to minimize risk and succeed is to embrace uncertainty and be the quickest and most productive in trying new things."*

Agile organizations work in rapid cycles of thinking and doing that are closely aligned to their process of creativity and accomplishment. Whether it deploys these as design thinking, lean operations, agile development, or other forms, this integration and continual rapid iteration of thinking, doing, and learning forms the organization's ability to innovate and operate in an agile way.

This rapid-cycle way of working can affect every level. At the team level, agile organizations radically rethink the working model, moving away from "waterfall" and "stage gate" project-management approaches. At the enterprise level, they use the rapid-cycle model to accelerate strategic thinking and execution. For example, rather than traditional annual planning, budgeting, and review, some organizations are moving to quarterly cycles, dynamic management systems like Objectives and Key Results (OKRs), and rolling 12-month budgets.

The impact of this operational model can be significant. For example, a global bank closed its project-management office and shifted its product-management organization from a traditional waterfall approach to a minimal viable product-based process. It moved from four major release cycles a year to several thousand-product changes monthly; it simultaneously increased product development, deployment, and maintenance productivity by more than 30 percent.

There are several characteristics of the rapid cycle model:

- Agile organizations focus on *rapid iteration and experimentation.* Teams produce a single primary deliverable (that is, a minimal viable product or deliverable) very quickly, often in one- or two-week "sprints." During these short activity bursts, the team holds frequent, often daily, check-ins to share progress, solve problems, and ensure alignment. Between sprints, team members meet to review and plan, to discuss progress to date, and to set the goal for the next sprint. To accomplish this, team members must be accountable for the end-to-end outcome of their work. They are empowered to seek direct stakeholder input to ensure the product serves all the needs of a group of customers and to manage all the steps in an operational process. Following this structured approach to innovation saves time, reduces rework, creates opportunities for creative "leapfrog" solutions, and increases the sense of ownership, accountability, and accomplishment within the team.

- Agile organizations leverage *standardized ways of working* to facilitate interaction and communication between teams, including the use of common language, processes, meeting formats, social-networking or digital technologies, and dedicated, in-person time, where teams work together for all or part of each week in the sprint. For example, under General Stanley McChrystal, the US military deployed a series of standardized ways of working between teams including joint leadership calls, daily all-hands briefings, collective online databases, and short-term deployments and co-location of people from different units. This approach enables rapid iteration, input, and creativity in a way that fragmented and segmented working does not.

- Agile organizations are *performance-oriented* by nature. They explore new performance- and consequence-management approaches based on shared goals across the end-to-end work of a specific process or service, and measure business impact rather than activity. These processes are informed by performance dialogues comprised of very frequent formal and informal feedback and open discussions of performance against the target.

- Working in rapid cycles requires that agile organizations insist on full *transparency of information*, so that every team can quickly and easily access the information they need and share information with others. For example, people across the unit can access unfiltered data on its products, customers, and finances. People can easily find and collaborate with others in the organization that have relevant knowledge or similar interests, openly sharing ideas and the results of their work. This also requires team members to be open and transparent with one another; only then can the organization create an environment of psychological safety where all issues can be raised and discussed and where everyone has a voice.

- Agile organizations seek to make *continuous learning* an ongoing, constant part of their DNA. Everyone can freely learn from their own and others' successes and failures, and build on the new knowledge and capabilities they develop in their roles. This environment fosters ongoing learning and adjustments, which help deliverables evolve rapidly. People also spend dedicated time looking for ways to improve business processes and ways of working, which continuously improves business performance.

- Agile organizations emphasize *quick, efficient, and continuous decision making,* preferring 70 percent probability now versus 100 percent certainty later. They have insight into the types of decisions they are making and who should be involved in those decisions.[9] Rather than big bets that are few and far between, they continuously make small decisions as part of rapid cycles, quickly test these in practice, and adjust them as needed for the next iteration. This also means agile organizations do not seek consensus decisions; all team members provide input (in advance if they will be absent), the perspectives of team members with the deepest topical expertise are given greater weight, and other team members, including leaders, learn to "disagree and commit" to enable the team to move forward.

4. Dynamic people model that ignites passion

Mind-set shift

From: *"To achieve desired outcomes, leaders need to control and direct work by constantly specifying tasks and steering the work of employees."*

To: *"Effective leaders empower employees to take full ownership, confident they will drive the organization toward fulfilling its purpose and vision."*

An agile organizational culture puts people at the center, which engages and empowers everyone in the organization. They can then create value quickly, collaboratively, and effectively.

Organizations that have done this well have invested in leadership which empowers and develops its people, a strong community which supports and grows the culture, and the underlying people processes which foster the entrepreneurship and skill building needed for agility to occur.

Leadership in agile organizations serves the people in the organization, empowering and developing them. Rather than planners, directors, and controllers, they become visionaries, architects, and coaches that empower the people with the most relevant competencies so these can lead, collaborate, and deliver exceptional results. Such leaders are catalysts that motivate people to act in team-oriented ways, and to become involved in making the strategic and organizational decisions that will affect them and their work. We call this *shared and servant leadership.*

Agile organizations create a *cohesive community* with a common culture. Cultural norms are reinforced through positive peer behavior and influence in a high-trust environment, rather than through rules, processes, or hierarchy. This extends to recruitment. Zappos, the online shoe retailer acquired by Amazon changed its recruiting to support the selection of people that fit its culture—even paying employees $4,000 to leave during their onboarding if they did not fit.[10]

People processes help sustain the culture, including clear accountability paired with the autonomy and freedom to pursue opportunities, and the ongoing chance to have new experiences. Employees in agile organizations exhibit *entrepreneurial drive*, taking ownership of team goals, decisions, and performance. For example, people proactively identify and pursue opportunities to develop new initiatives, knowledge, and skills in their daily work. Agile organizations attract people who are motivated by intrinsic passion for their work and who aim for excellence.

In addition, talent development in an agile model is about building new capabilities through varied experiences. Agile organizations allow and expect *role mobility*, where employees move regularly (both horizontally and vertically)

9 Aaron De Smet, Gerald Lackey, and Leigh Weiss, "Untagling your organization's decision making," *McKinsey Quarterly*, July 2017.

10 David Burkus, "Why Amazon bought into Zappos's 'pay to quit' policy," *Inc.*, June 2015, inc.com

McKinsey on agile transformations

By the year 2000, product developers were facing a challenge—products were being released so slowly that by the time they were production-ready they were already obsolete and customer needs had moved on. This all changed in 2001 when 17 software developers who called themselves "organizational anarchists" were looking for alternative approaches to the typical waterfall approach to software development. They proposed a new set of values, methodologies, and ways of working that then swept through the product-development and technology arenas over next 16 years. This became known as "agile software development" or "agile technology."

In 2011, McKinsey's research into organizational redesigns uncovered a very similar problem—57 percent of companies were redesigning every two years with an average length of a redesign being 18 months. In other words, companies were barely finishing one redesign before changes in the market or customers were requiring them to start another redesign—a similar "waterfall" problem in organization design. A new emergent organization form addresses this issue. It leverages both established and novel principles of how to organize work, deploy resources, make decisions, and manage performance with the goal of helping organizations quickly adapt to rapidly changing conditions. Compared with the traditional organizational model, this new approach—which we called an "agile organization" in a nod to its roots—is emerging as a fundamentally different and higher performing kind of organization, one designed for the complex, constantly evolving markets of the 21st century.

McKinsey defines "agile transformations" broadly. For us, the term "agile transformation" is a holistic change that creates value for the enterprise. It necessarily requires a change in the operating model and ways of working. Often technology and digitization are pieces of the journey toward completing an agile transformation. We take a holistic view of a company's operating model across people, process, structure, strategy, and technology—looking for both the stable and dynamic elements that must be in place to create agility. Such transformations can be done across an entire enterprise or within just a single function, business unit or end-to-end process. They should take an industry-backed perspective to inform the agile design, looking for the latest trends around digital, technology, talent, and supply chain that are posed to make disruptive changes in the market. They should also tie organizational agility tightly to the agile delivery of projects so that organizations build the skills necessary to deliver work quickly as well as create the right organizational environment to make those teams successful.

between roles and teams, based on their personal-development goals. An open talent marketplace supports this by providing information on available roles, tasks, and/or projects as well as people's interests, capabilities, and development goals.

5. Next-generation enabling technology

Mind-set shift

From: *"Technology is a supporting capability that delivers specific services, platforms, or tools to the rest of the organization as defined by priorities, resourcing, and budget."*

To: *"Technology is seamlessly integrated and core to every aspect of the organization as a means to unlock value and enable quick reactions to business and stakeholder needs."*

For many organizations, such a radical rethinking of the organizational model requires a rethinking of the technologies underlying and enabling their products and processes, as well as the technology practices needed to support speed and flexibility.

Agile organizations will need to provide products and services that can meet changing customer and competitive conditions. Traditional products and services will likely need to be digitized or digitally-enabled. Operating processes will also have to continually and rapidly evolve, which will require evolving technology *architecture, systems, and tools.*

Organizations will need to begin by leveraging new, real-time communication and work-management tools. Implementing modular-based software architecture enables teams to effectively use technologies that other units have developed. This minimizes handovers and interdependencies that can slow down production cycles. Technology should progressively incorporate new technical innovations like containers, micro-service architectures, and cloud-based storage and services.

In order to design, build, implement, and support these new technologies, agile organizations integrate a range of *next-generation technology development and delivery practices* into the business. Business and technology employees form cross-functional teams, accountable for developing, testing, deploying, and maintaining new products and processes. They use hackathons, crowd sourcing, and virtual collaboration spaces to understand customer needs and develop possible solutions quickly. Extensive use of automated testing and deployment enables lean, seamless, and continuous software releases to the market (for example, every two weeks vs. every six months). Within IT, different disciplines work closely together (for example, IT development and operations teams collaborate on streamlined, handover-free DevOps practices).

In summary, today's environment is pressing organizations to become more agile; in response, a new organizational form is emerging that exhibits the five trademarks discussed above. In aggregate, these trademarks enable organizations to balance stability and dynamism and thrive in an era of unprecedented opportunity.

The next question is how to get there? In a rapidly changing commercial and social environment, some organizations are born agile, some achieve agility, and some have agility thrust upon them. To learn more about how to begin the journey towards an agile transformation, stay tuned for another paper in the dynamic Agile Organization series, "The journey to an agile organization."

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How to create an agile organization

Survey, October 2017

Transforming companies to achieve organizational agility is in its early days but already yielding positive returns. While the paths can vary, survey findings suggest how to start.

Rapid changes in competition, demand, technology, and regulations have made it more important than ever for organizations to be able to respond and adapt quickly. But according to a recent McKinsey Global Survey, organizational agility—the ability to quickly reconfigure strategy, structure, processes, people, and technology toward value-creating and value-protecting opportunities—is elusive for most.[1] Many respondents say their companies have not yet fully implemented agile ways of working, either company-wide or in the performance units where they work,[2] though the advantages are clear. Respondents in agile units report better performance than all others do, and companies in more volatile or uncertain environments are more likely than others to be pursuing agile transformations.

Few companies are yet reaping these benefits, but that may soon change; the results also indicate that organizational agility is catching fire. For many respondents, agility ranks as a high strategic priority in their performance units. Moreover, companies are transforming activities in several parts of the organization—from innovation and customer experience to operations and strategy—to become more agile. Finally, respondents in all sectors believe more of their employees should be working in agile ways. For organizations and their performance units that aren't yet agile, the path to achieving agility depends on their starting points. But the results indicate some clear guidance on how and where they can improve, whether they are lacking in stability or dynamism.

Organizational agility is on the rise

Across industries and regions, most survey participants agree that the world around them is changing, and quickly. Business environments are increasingly complex and volatile, with two-thirds of respondents saying their sectors are characterized by rapid change. In such environments, the need for companies to demonstrate agility is top of mind: the more unstable that respondents say their environments are, the more likely they are to say their companies have begun agile transformations (Exhibit 1).

To date, though, few organization-wide agile transformations have been completed. Only 4 percent of all respondents say their companies have fully implemented one, though another 37 percent say company-wide transformations

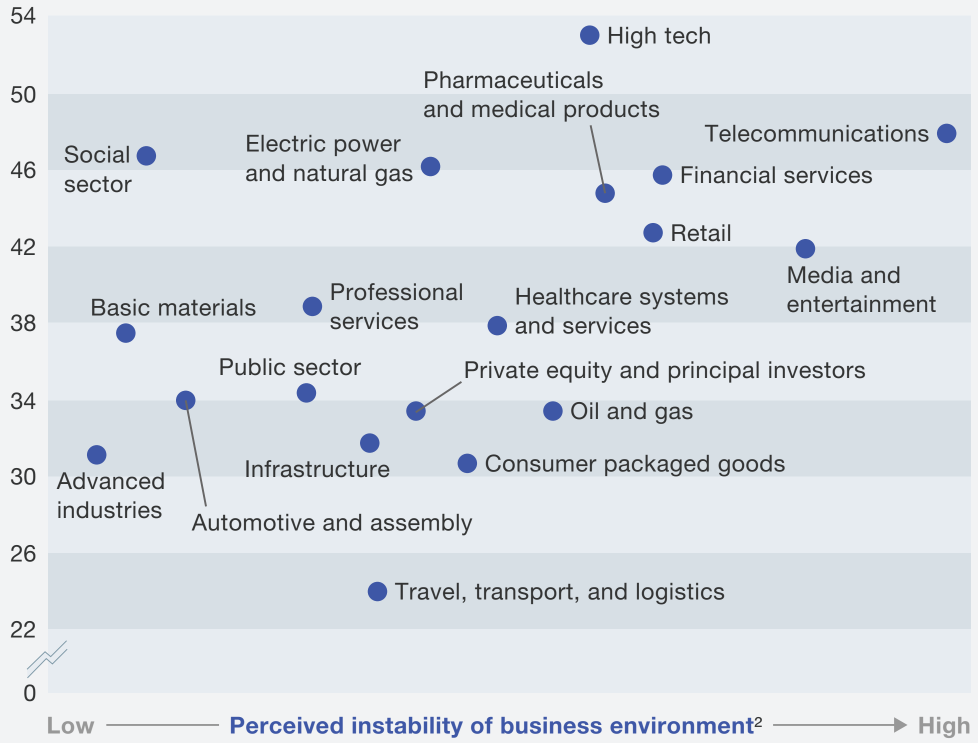
1 This definition of organizational agility was given to respondents when they began the survey and reflects McKinsey's proprietary definition, which is distinct from how we define organizations with agile software-development processes. Throughout the report, we will use "agile transformations" to refer to transformations that focus on organizational agility. The online survey was in the field from February 14 to February 24, 2017, and garnered responses from 2,546 participants representing the full range of regions, industries, company sizes, functional specialties, and tenures. Of these respondents, 207 work at nonprofits and government agencies or departments. But we will use the word "companies" to refer to all respondents' firms, whether in the private or public sector.

2 "Performance unit" refers to a part of the organization (for example, a functional team, cross-functional team, or business unit) that is responsible for the delivery of specific performance outcomes. We asked respondents to answer the survey with regard to the performance unit in which they are most familiar. Forty-four percent responded on behalf of a business unit, 31 percent on behalf of a cross-functional team, 23 percent on behalf of a functional team, and 2 percent on behalf of another type of unit.

Exhibit 1

Respondents who describe their business environments as unstable are more likely to say their organizations have already begun agile transformations.

% of respondents reporting **organization-wide agile transformations** at their companies,[1] by industry



[1]Includes respondents who said their companies' organization-wide agile transformations are either still in progress or fully implemented. Respondents who said their organizations have not begun a transformation are not included in analysis.

[2]Respondents were asked to agree or disagree with 4 statements about their industries: whether they are characterized by rapid change, whether regulations make their performance units' work complex to execute, whether shifts in customer demands in the business unit are unforeseeable, and whether new market entrants and competitors make it hard for the unit to compete successfully.

Eighteen practices for organizational agility

The survey asked respondents about a series of specific actions that underlie each of the 18 practices (9 of them stable, and 9 dynamic) of organizational agility; all of the practices are summarized in the table below. To rate respondents' organizations, we asked how frequently their performance units engaged in each action that supports a given practice.

Agility Practice	What it means
Shared vision and purpose	▪ People feel personally and emotionally invested in their work and that they serve a common purpose. ▪ Refining the strategic direction is a collective effort that includes people who drive the work.
Actionable strategic guidance	▪ Daily work is guided by concrete outcomes that advance the organization's strategy. ▪ Leaders and peers provide frequent feedback and coaching that enables people to work autonomously toward their team outcomes.
Sensing and seizing opportunities	▪ People individually and proactively watch for and act upon changes in customer preferences and the external environment. ▪ The organization actively uses customer insights (both formal and informal) to shape, pilot, launch, and iterate on new initiatives and business models.
Flexible resource allocation	▪ A quick, systematic process is in place to regularly evaluate the progress of business initiatives and decide whether to ramp them up or shut them down. ▪ Key resources (for example, high-performing individuals, leadership time, funds) are deployed and redeployed between initiatives as their performance or relative priority changes.
Action-oriented decision architecture	▪ Decision-making processes and norms are clear and widely followed (for example, if decision makers cannot attend a decision meeting, they provide input in advance, accepting the outcome of the decision made). ▪ People closest to where the work happens have the authority to make decisions that affect the implementation of their day-to-day activities. ▪ If their roles (that is, responsibilities or decision rights) are unclear in any way, people proactively resolve this with relevant colleagues across levels and units. ▪ When a performance unit's structure needs to be adapted or scaled to meet changing needs (for example, evolving customer demands or business priorities), decisions to do so are made rapidly.
Fit-for-purpose accountable cells	▪ People work in small, self-managing teams that are accountable for the end-to-end work of a specific process or service. ▪ Teams form and dissolve as strategic priorities change.
Active partnerships and ecosystem	▪ People work hands-on and day to day with customers, vendors, and other partners to codevelop new products, services, and/or solutions and bring them to market. ▪ Units maintain flexible models of partnering with external parties (for for example, to engage temporary or contract-based workers, to codevelop new products and services, to invest in start-ups)
Open physical and virtual environment	▪ The work environment was purposefully designed so people communicate and collaborate with each other, in person or virtually, even if they do not work on the same team or regularly interact in their day-to-day work. ▪ The work environment was purposefully designed so people can do their jobs most effectively (for example, people choose where they sit based on their needs or preferences; each unit's targets, metrics, and performance are clearly visible to everyone).

Agility Practice	What it means
Standardized ways of working	▪ There are common ways of saying and doing things within the unit, which enables people to work seamlessly with colleagues or teams in other units. ▪ People use their time efficiently, as a result of standardized approaches (for example, standardized meeting formats, supporting processes and policies that enable quick execution of day-to-day activities).
Performance orientation	▪ Individuals, teams, and units are evaluated by cross-functional business metrics and targets (that is, all people who are accountable for the end-to-end work of the same process or service share the same performance metrics and incentives). ▪ Internally across units and levels, and externally with partners, people provide each other with continuous feedback, both formally and informally (that is, on behavior and on progress against metrics, targets, and/or outcomes).
Rapid iteration and experimentation	▪ Innovations are iteratively developed through fast cycles of field testing and learning from mistakes. ▪ Products are developed by experimenting and prototyping using minimum viable products (that is, versions of products with the minimum set of features needed to test and learn).
Information transparency	▪ People across the unit have access to unfiltered data on its products, customers, and financial information. ▪ People can easily share ideas from and results of their work and find others in the organization with relevant knowledge or similar interests.
Continuous learning	▪ People spend dedicated time looking for ways to improve business processes and their ways of working. ▪ Structured processes and tools (for example, postmortems, knowledge marketplaces) enable people to learn freely from others' knowledge, capabilities, and on-the-job successes and failures.
Shared and servant leadership	▪ Leaders inspire people to act in team-oriented ways and be actively involved in strategic and organizational decisions that affect them and their work. ▪ Leaders influence others through coaching and development, rather than hierarchical authority, enabling people with the most relevant capabilities for the work at hand to lead.
Cohesive community	▪ People across all levels and teams trust each other to act in the best interests of the organization, its customers, and other key stakeholders. ▪ The unit reinforces a common culture through fit-based recruitment and positive peer pressure, rather than through rules, procedures, or hierarchy.
Entrepreneurial drive	▪ People proactively identify and pursue opportunities to develop new initiatives, knowledge, and skills in their daily work. ▪ People have an intrinsic passion for their work and aim to perform beyond expectations.
Role Mobility	▪ People move regularly (both vertically and horizontally) between roles and teams, based on their personal-development goals (that is, the knowledge, skills, and networks they want to build). ▪ The organization maintains an open talent marketplace where available roles, tasks, and/or projects are clearly communicated.
Technology, systems, and tools	▪ Cross-functional teams of business and technology people collaborate with each other constantly to achieve desired business outcomes. ▪ Technology (that is, architecture, infrastructure, practices, and tools) is seamlessly integrated with key processes and responsive to changing business needs (that is, modular architecture is used, technology is updated in shorter intervals of time, automated testing enables continuous software releases).

are in progress. When asked where their companies apply agile ways of working,[3] respondents most often identify activities that are closest to the customer: innovation, customer experience, sales and servicing, and product management.[4] This is not too surprising, since customer centricity is cited most often—followed by productivity and employee engagement—as the objective of agile transformations. Companies are also focusing on internal end-to-end processes. At least four in ten respondents say their companies are applying agile ways of working in processes related to operations, strategy, and technology, while roughly one-third say they are doing so in supply-chain management and talent management.[5]

Looking forward, the results suggest that companies have higher aspirations for agility. Three-quarters of respondents say organizational agility is a top or top-three priority on their units' agendas, and more transformations appear to be on the way. Of those who have not begun agile transformations, more than half say plans for either unit-level or company-wide transformations are in the works. Respondents across industries also report a desire to scale up agile ways of working. On average, they believe 68 percent of their companies' employees should be working in agile ways, compared with the 44 percent of employees who currently do. By industry, respondents in telecom and the electric-power and natural-gas industries report the biggest differences between their actual and ideal shares of employees working in agile ways—followed closely by respondents in several other industries: media and entertainment, the public sector, oil and gas, pharma, and advanced industries.

What's more, the survey also confirms that agility pays off. Eighty-one percent of respondents in agile units report a moderate or significant increase in overall performance since their transformations began. And on average, respondents in agile units are 1.5 times more likely than others to report financial outperformance relative to peers, and 1.7 times more likely to report outperforming their peers on nonfinancial measures.[6]

Agile organizations excel at both stability and dynamism

In previous work, we have determined that, to be agile, an organization needs to be both dynamic and stable.[7] Dynamic practices enable companies to respond nimbly and quickly to new challenges and opportunities, while stable practices cultivate reliability and efficiency by establishing a backbone of elements that don't need to change frequently. The survey scored organizations across eighteen practices, which our research suggests are all critical for achieving organizational agility. According to the results, less than one-quarter of performance units are agile. The remaining performance units lack either dynamism, stability, or both (Exhibit 2).

3 The survey asked which of 12 agile ways of working were currently applied in respondents' performance units. The 12 options were cross-functional teams, self-managing teams, knowledge communities, innovation hubs, scrums, integrator roles, staffing portals, hackathons, flow-to-the-work pools, Skunk Works, scaled agility frameworks (for example, Scaled Agile Framework, Large Scale Scrum), and holacracy.

4 Innovation includes R&D, new-technology development, and/or idea generation; customer experience includes marketing, branding, campaigns, customer journeys, and/or customer-experience design; sales and servicing includes customer services, sales, and commercial and/or account management; and product management includes product development and/or product engineering.

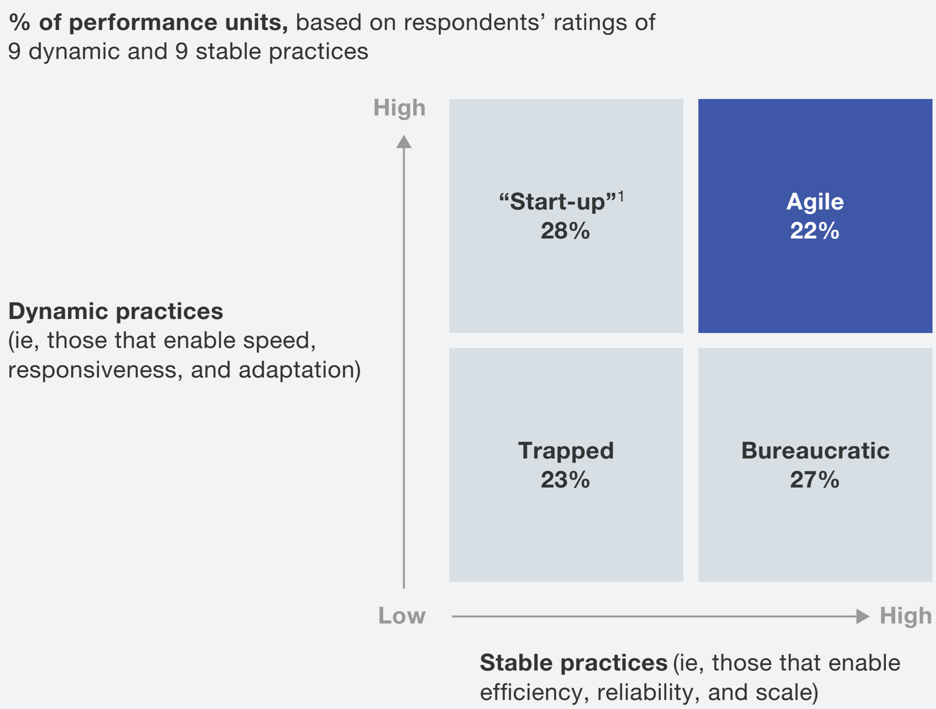
5 Operations includes production and/or manufacturing; strategy includes general management, corporate strategy, budgeting, and/or resource allocation; technology includes IT infrastructure and support; supply-chain management includes purchasing, procurement, logistics, and/or product delivery; and talent management includes organizational culture, human resources, and/or capability development.

6 The survey measured financial performance as the revenue, growth, market share, cost efficiency, and profitability of respondents' performance units, relative to units at competitors' organizations that do similar work, and nonfinancial performance as performance units' development and innovation (that is, of products, services, processes, and/or solutions), responsiveness to customer needs, time to market, productivity, and employee engagement, relative to units at competitors' organizations.

7 For more information, see Wouter Aghina, Aaron De Smet, and Kirsten Weerda, "Agility: It rhymes with stability," *McKinsey Quarterly*, December 2015, McKinsey.com.

Exhibit 2

According to respondents, less than one-quarter of performance units are agile.



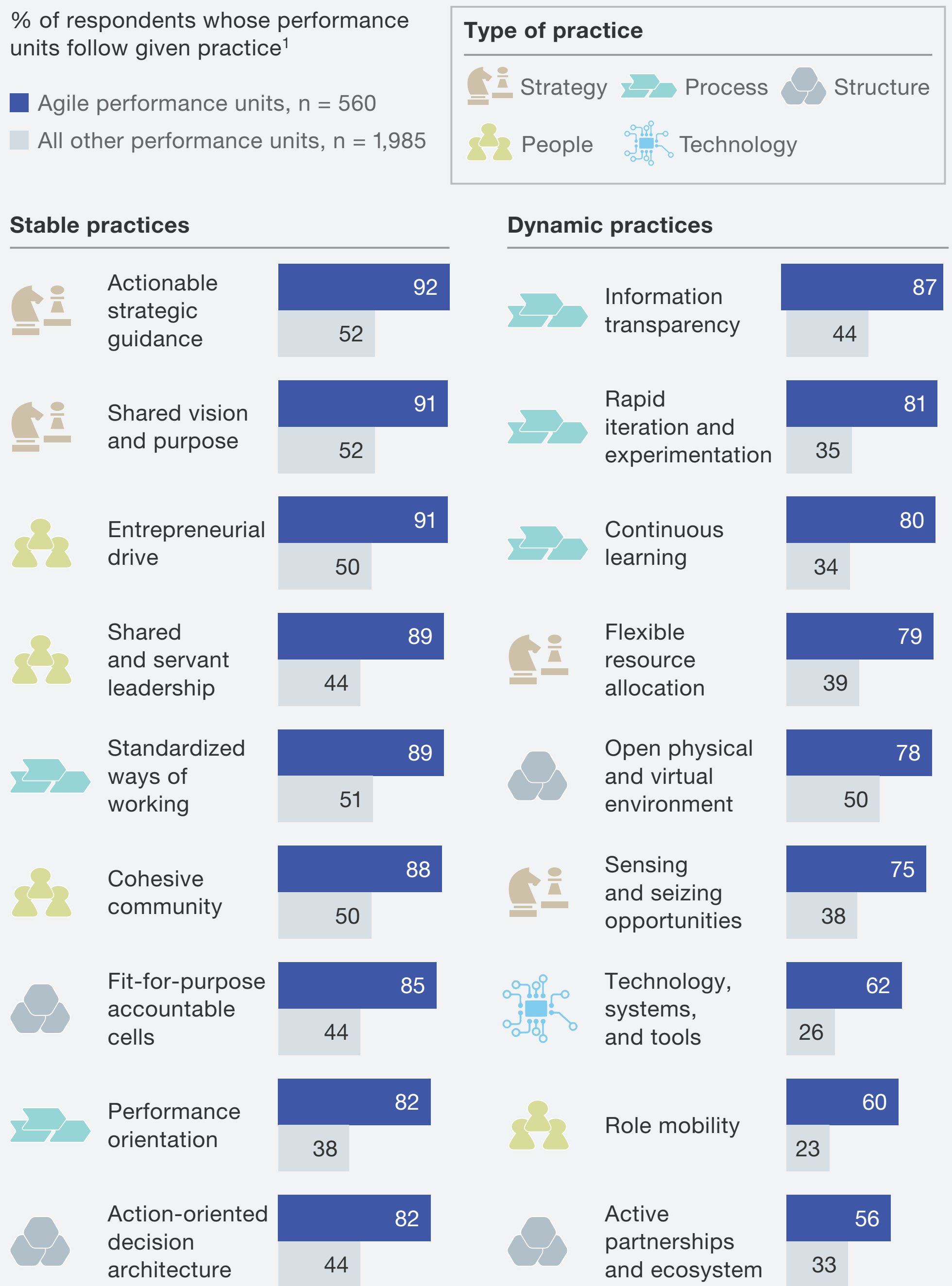
Of the 18 practices, the 3 where agile units most often excel relate to strategy and people (Exhibit 3). More than 90 percent of agile respondents say that their leaders provide actionable strategic guidance (that is, each team's daily work is guided by concrete outcomes that advance the strategy); that they have established a shared vision and purpose (namely, that people feel personally and emotionally engaged in their work and are actively involved in refining the strategic direction); and that people in their unit are entrepreneurial (in other words, they proactively identify and pursue opportunities to develop in their daily work). By contrast, just about half of their peers in nonagile units say the same.

After strategy, agile units most often follow four stable practices related to process and people: entrepreneurial drive, shared and servant leadership, standardized ways of working, and cohesive community. When looking more closely at standardized ways of working, the agile units excel most on two actions: the unit's processes are enabled by shared digital platforms and tools (91 percent, compared with 54 percent for others), and processes are standardized, including the use of a common language and common tools (cited by 90 percent of agile respondents and just 58 percent of all others).

Among the dynamic practices, process—and information transparency, in particular—is a strength for agile units. Within transparency, for example, 90 percent of agile respondents say information on everything from customers to financials is freely available to employees. Among their peers in other units, only 49 percent say the same. The second practice where agile units most differ from others is in rapid iteration and experimentation. More than 80 percent of agile respondents say their companies' new products and services are developed in close interaction with customers and that ideas and prototypes are field-tested early in the development process, so units can quickly gather data on possible improvements.

Exhibit 3

Agile performance units excel most often at strategy and people-related practices, and they outperform all other units in stability and dynamism.



[1] To score respondents' organizations on the 18 practices, the survey asked about 78 specific actions, each of which underlies 1 of the practices. For an organization to follow a given practice, respondents said they follow each action within that practice "regularly," "often," or "almost always." Respondents who said "almost never," "rarely," or "sometimes" are not included in analysis.

The path to agility depends on the starting point

For the performance units that aren't yet agile, the survey results suggest clear guidance for how to move forward. But organizational agility is not a one-size-fits-all undertaking. The specific practices a unit or organization should focus on to become agile depend on whether it is currently bureaucratic, start-up, or trapped.

Bureaucratic units

By definition, bureaucratic units are relatively low in dynamism and most often characterized by reliability, standard ways of working, risk aversion, silos, and efficiency. To overcome the established norms that keep them from moving fast, these units need to develop further their dynamic practices and modify their stable backbones, especially on practices related to people, process, and structure.

First is the need to address the dynamic practices where, compared with agile units, the bureaucratic units are furthest behind (Exhibit 4). Only 29 percent of bureaucratic respondents, for example, report following rapid iteration and experimentation, while 81 percent of agile respondents say the same. A particular weakness in this area is the use of minimum viable products to quickly test new ideas: just 19 percent of bureaucratic respondents report doing so, compared with 74 percent of agile respondents. After that, the largest gap between bureaucratic units and agile units is their ability to roll out suitable technology, systems, and tools that support agile ways of working.

At the same time, bureaucratic units also have room to improve on certain stable practices (Exhibit 5). For example, bureaucratic units are furthest behind in performance orientation; in agile units, employees are far more likely to provide each other with continuous feedback on both their behavior and their business outcomes. What's more, leaders in these units are better at embracing shared and servant leadership by more frequently incentivizing team-oriented behavior and investing in employee development. And it's much more common in agile units to create small teams that are fully accountable for completing a defined process or service.

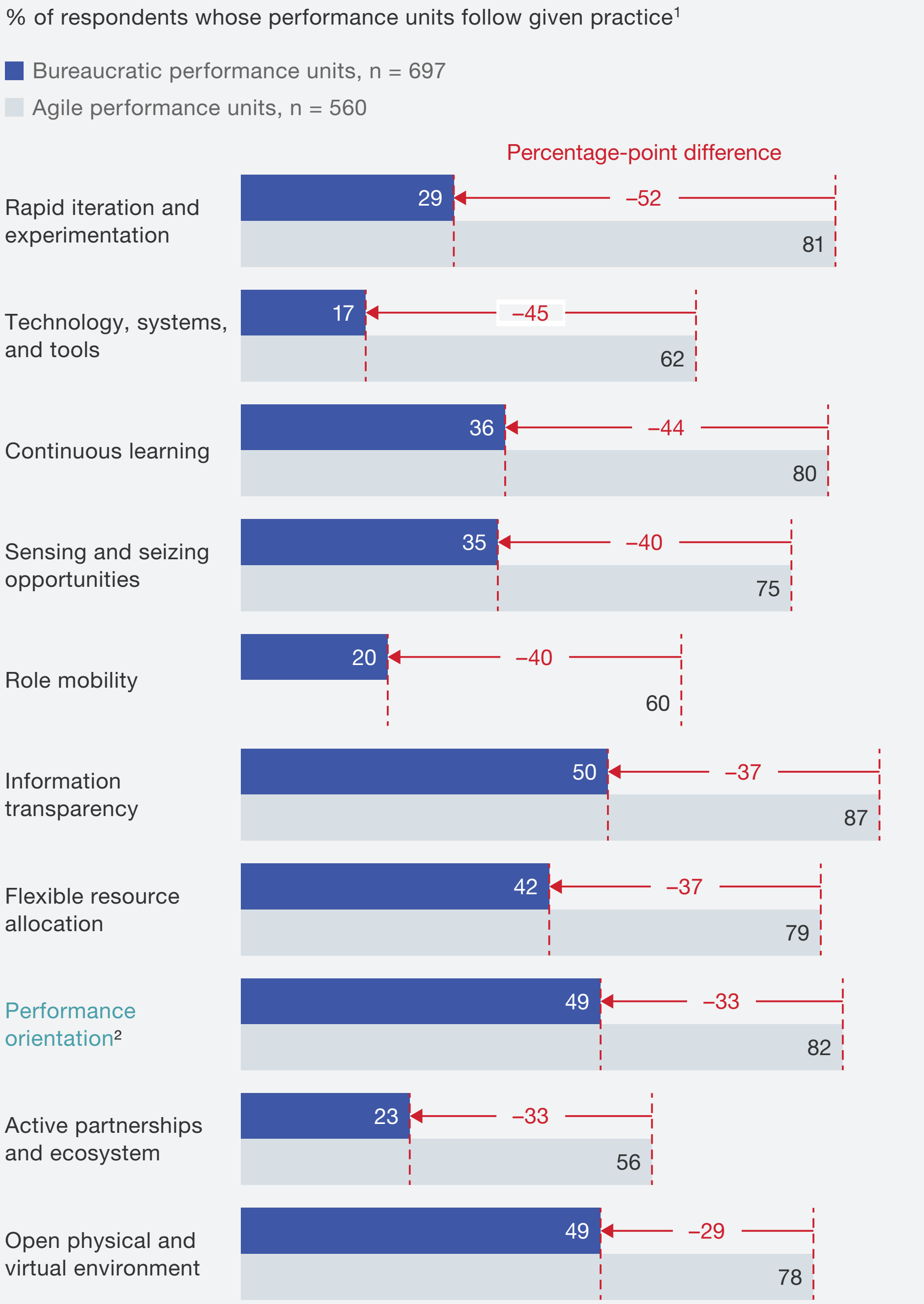
Start-up units

Start-up units, on the other hand, are low in stability and characterized as creative, ad hoc, constantly shifting focus, unpredictable, and reinventing the wheel. These organizations tend to act quickly but often lack discipline and systematic execution. To overcome the tendencies that keep them from sustaining effective operations, these units need to further develop all of their stable practices—and also broaden their use of the dynamic practices related to process and strategy in order to maintain sufficient speed.

First is focusing on a stronger overall stable backbone. On average, 55 percent of start-up respondents report that they implement all nine stable practices, compared with 88 percent of agile respondents who report the same. According to the results, a particular sore spot is people-related practices—especially shared and servant leadership (Exhibit 6). For example, just under half of start-up respondents say their leaders involve employees in strategic and organizational decisions that affect them, compared with 85 percent of their agile peers. Similar to bureaucratic units, respondents at start-up units also report challenges with process, particularly with regard to performance orientation. Within that practice, only 44 percent of respondents at start-up units say their people provide each other with continuous feed-back on both their behavior and their business outcomes; 80 percent at agile units report the same.

Exhibit 4

Compared with their agile counterparts, bureaucratic performance units are far behind on their dynamic practices.



[1] Out of 18 total practices; those shown here are the 10 practices with the largest percentage-point differences between bureaucratic units and agile units.To score respondents' organizations on the 18 practices, the survey asked about 78 specific actions, each of which underlies one of the practices. For an organization to follow a given practice, respondents said they follow each action within that practice "regularly," "often," or "almost always." Respondents who said "almost never," "rarely," or "sometimes" are not included in analysis.

[2] Performance orientation is a stable practice; all others are dynamic.

Exhibit 5

In bureaucratic units, respondents report room to improve how they execute certain stable practices.

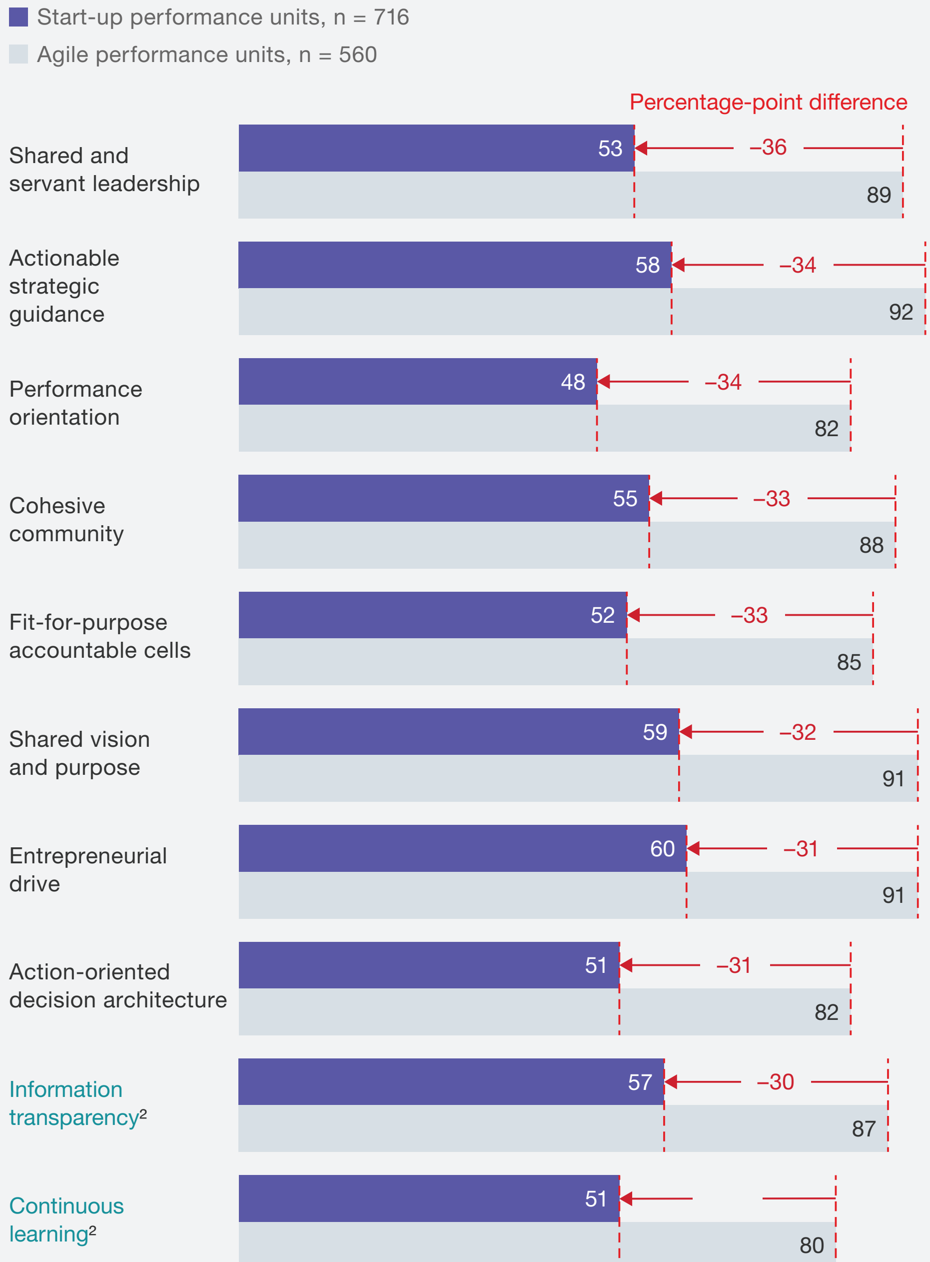
% of respondents whose performance units follow given action[1]

[1]The actions shown within each practice are the 2 with the largest percentage-point differences between bureaucratic units and agile units. The stable practices shown here are the 3 with the largest percentage-point differences between bureaucratic units and agile units.
[2]That is, employees are accountable for the end-to-end completion of a defined process, service, or method.

Exhibit 6

Among the stable practices that start-up units can execute most often, people-related practices—such as shared and servant leadership—are their biggest pain points.

% of respondents whose performance units follow given practice[1]



[1]Out of 18 total practices; those shown here are the 10 practices with the largest percentage-point differences between start-up units and agile units. To score respondents' organizations on the 18 practices, the survey asked about 78 specific actions, each of which underlies one of the practices. For an organization to follow a given practice, respondents said they follow each action within that practice "regularly," "often," or "almost always." Respondents who said "almost never," "rarely," or "sometimes" are not included in analysis.
[2]Information transparency and continuous learning are dynamic practices; all others are stable.

Start-up units also have room to improve their use of dynamic practices, particularly in process and strategy. According to respondents, the agile units excel much more often than their start-up counterparts at information transparency—for example, holding events where people and teams share their work with the unit (Exhibit 7). Moreover, agile respondents are much more likely to say new knowledge and capabilities are available to the whole unit, which enables continuous learning. On the strategy front, the start-up units are furthest behind their agile peers on flexible resource allocation—more specifically, deploying their key resources to new pilots and initiatives based on progress against milestones.

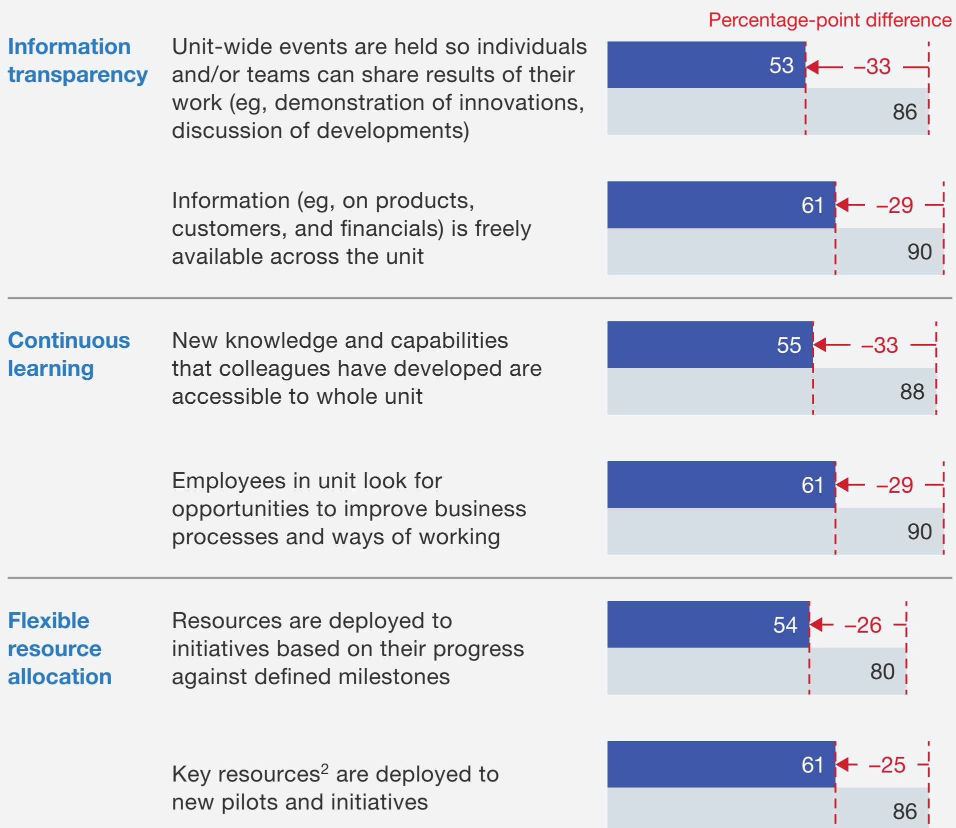
Exhibit 7

Among dynamic practices, start-up units can most improve upon information transparency, continuous learning, and resource allocation.

% of respondents whose performance units follow given practice[1]

Start-up performance units, n = 716

Agile performance units, n = 560



[1]The actions shown within each practice are the 2 with the largest percentage-point differences between start-up units and agile units. The dynamic practices shown here are the 3 with the largest percentage-point differences between start-up units and agile units.
[2]That is, high-performing individuals, leadership time, and required funding.

Trapped units

The trapped units are often associated with firefighting, politics, a lack of coordination, protecting turf, and local tribes. These organizations find themselves lacking both a stable backbone and dynamic capabilities. In applying the stable practices, the trapped units are most behind on those related to people: specifically, shared and servant leadership and entrepreneurial drive. Just 13 percent of respondents at trapped units say they follow shared and servant leadership, compared with 89 percent of their agile peers. The dynamic practices in which they are furthest behind are process related, especially continuous learning and rapid iteration and experimentation.

Looking ahead

In response to the challenges that the survey results revealed, here are some principles executives and their units or organizations should act upon, whether or not they have already begun agile transformations:

- **Embrace the magnitude of the change.** Based on the survey, the biggest challenges during agile transformations are cultural—in particular, the misalignment between agile ways of working and the daily requirements of people's jobs, a lack of collaboration across levels and units, and employee resistance to changes. In our experience, agile transformations are more likely to succeed when they are supported by comprehensive change-management actions to cocreate an agile-friendly culture and mind-sets. These actions should cover four main aspects. First, leaders and people across the organization align on the mind-sets and behaviors they need to move toward. Second, they role-model the new mind-sets and behaviors and hold each other accountable for making these changes. Third, employees are supported in developing the new skills they need to succeed in the future organization. And finally, formal mechanisms are put in place to reinforce the changes, rewarding and incentivizing people to demonstrate new behaviors.[8]

- **Be clear on the vision.** The results show that agile units excel most at creating a shared vision and purpose and aligning on this vision through actionable strategic guidance. In contrast, at companies that have not yet started a transformation, one of the most common limitations is the inability to create a meaningful or clearly communicated vision. An important first step in deciding whether to start an agile transformation is clearly articulating what benefits are expected and how to measure the transformation's impact. This vision of the new organization must be collectively held and supported by the top leadership.

- **Decide where and how to start.** Respondents whose organizations have not started agile transformations most often say it's because they lack a clear implementation plan. While the right plan will vary by company, depending on its vision, companies should first identify the part(s) of the organization that they want to transform and how (for example, by prototyping the changes in smaller parts of the performance unit before scaling them up, or by making changes to more foundational elements that go beyond a single unit). Second, they should assess which of the 18 agile practices the organization most needs to strengthen in order to achieve agility, so that the actions taken across strategy, structure, process, people, and technology are mutually reinforcing. Third, they should determine the resources and time frame that the transformation requires, so the effort maintains its momentum but the scope remains manageable at any point in time.

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They would like to acknowledge Wouter Aghina, Esmee Bergman, Aaron De Smet, and Michael Lurie for their contributions to this work.

8 See Tessa Basford and Bill Schaninger, "The four building blocks of change," *McKinsey Quarterly*, April 2016, McKinsey.com.

Unleashing the power of small, independent teams

***McKinsey Quarterly* , July 2018** | By Oliver Bossert, Alena Kretzberg, and Jürgen Laartz

Small, independent teams are the lifeblood of the agile organization. Top executives can unleash them by driving ambition, removing red tape, and helping managers adjust to the new norms.

What does it take to set loose the independent teams that make agile organizations hum? These teams are the organizational units through which agile, project-based work gets done. The typical agile company has several such teams, most composed of a small number of people who have many or all of the skills the team needs to carry out its mission. (Amazon CEO Jeff Bezos contends that a team is too big when it needs more than two pizza pies for lunch.) This multidisciplinary way of composing teams has implications for nearly every business function. Take IT management. Instead of concentrating technology professionals in a central department, agile companies embed software designers and engineers in independent teams, where they can work continually on high-value projects.

While much depends on the actions of the individual team members, senior executives must thoughtfully create the environment in which teams and their managers can thrive. In a nutshell, senior executives must move the company—and themselves—away from outmoded command-and-control behaviors and structures that are ill-suited to today's rapid digital world. They must redouble efforts to overcome resource inertia and break down silos, because independent teams can't overcome these bureaucratic challenges on their own. They must direct teams to the best opportunities, arm them with the best people, give them the tools they need to move fast, and oversee their work with a light but consistent touch. These ideas may sound straightforward, but they go overlooked by too many leaders who've grown up in more traditional organizations.

This article explores how senior leaders can unleash their companies' full potential by empowering small teams and supporting their managers, whose roles have been redefined by agile thinking (exhibit). Let's start with a glimpse of what that looks like in action.

How independent teams work

Several years ago, financial regulators in Europe decided to let banks verify customers' identities remotely through digital video chats instead of relying solely on face-to-face appointments at bank branches. When the news reached one established bank, the team in charge of its know-your-customer (KYC) process recognized that the regulatory change could help the bank win new accounts. It quickly sprang into action to create the needed service. The very existence of this KYC team was a credit to the bank's leaders, who had previously put small, independent teams to work—improving the performance of many of the bank's functions by giving them the diverse capabilities needed to address market opportunities like this one. The bank had simultaneously made a series of complementary reforms to remove cumbersome approval, budgeting, and governance processes. Without these institutional refinements, the KYC team's time to market would have been far less competitive.

Exhibit

The effectiveness of small teams requires change in both the corporate environment and managers' interactions with the teams.

The empowering executive	The independent team	The enabling manager
Focuses small teams in customer-facing areas	Authorized to conduct activities without first seeking approval	Defines outcomes for teams to pursue as they see fit
Stacks small teams with top performers	Has minimal dependencies on internal functions	Acts as a steward rather than a superior
Gives teams a clear, direct view of customers	Builds and launches digital solutions on its own	Prioritizes problem solving over decision making
Allocates resources up front, then holds teams accountable	Draws on preassigned funding with no formal budget request	Spends more time than usual on coaching and learning

Critically, senior executives had endowed small, focused groups like the KYC team with the authority and the resources to carry out projects without first seeking corporate approval. When it came to paying for the development of the digital KYC service, the team was spared the trouble of making a formal budget request and enduring a months-long holding period while the corporate planning committee took up the request as part of its regular planning process. Instead, the team drew on a tranche of funding that it had already been given, funding tied to the team's contribution to outcomes such as higher customer-conversion rates.

The bank also loosened or completely unhitched its product teams' dependence on internal support functions. New accommodations in the bank's HR processes, for example, allowed the KYC team to quickly line up outside contractors for help with front- and back-end development, without waiting for those contractors to be vetted. The IT function had streamlined the bank's technology systems and operations, too, building a modern architecture platform to more easily connect new customer-facing services with legacy back-end systems. The bank had also eliminated its traditional waterfall-development process, as well as a no-compromises protocol for testing new products before launch. Previously, a central IT group would have had to integrate the digital KYC service with core systems, a drawn-out process that could have stalled the KYC team for months. But now the KYC team could integrate testing with work flows, roll out new services as soon as they were viable, and make incremental improvements over multiple cycles. Together, these reforms allowed the KYC team to develop the new digital services in a matter of weeks, rather than the months it would have taken before the reorganization.

Senior company executives had an integral place in this process, despite the independence they had accorded teams like KYC. They evaluated progress and allocated resources according to whether teams deliver against well-defined measures of performance. But they only intervened in the team's ongoing work from time to time, and then only to remove roadblocks and provide support. By creating a supportive structure and managing it with a light touch, senior bank executives fostered this kind of innovative spirit in teams all across the institution.

How executives empower independent teams

The challenge for senior executives in an agile organization is clear but difficult: empower small teams with great independence and resources while retaining accountability. As our colleagues have written, an agile organization speeds up decision making by allowing teams that are closer to customers to make day-to-day, small-stakes decisions on their own, and only escalating decisions that could have significant consequences or that can only be made effectively with input and sign-off from multiple parts of the organization. Executives further empower teams by lessening their dependence on support functions such as finance, planning, and human resources. Yet executives still must ensure that teams operate with proper governance, that company resources are aligned in pursuit of strategic priorities, and that midlevel managers get the coaching they need to become better versed in agile ways of working. Our experience helping companies with the transition to agile ways of working suggests emphasizing the following actions:

Unleash independent teams in meaningful areas

We've argued that autonomy is especially beneficial to teams working on processes and capabilities that directly affect the customer experience. When executives begin to give their small teams more independence, they should look first at teams that are responsible for features that matter greatly to customers. This way, executives can demonstrate how independence helps teams generate more value. (Skeptics may challenge this approach on the grounds that a new, untested way of managing teams is too risky to try in significant customer-facing areas. In practice, independent teams create less business risk, because they make incremental changes that can be rolled back with ease if they don't work out.) It's also important that executives choose teams of people who represent different capabilities. When multiple domains of the company take part in independent teams, executives and managers can test the limits of the decision-making authority that these domains extend to teams, and demonstrate that autonomous teams can be trusted to exercise good judgment.

Put strong performers on independent teams, especially at the outset

Executives can be reluctant to place their best-performing employees on independent teams that aren't mission critical, because they would rather keep them engaged in "more important" activities. We hold the opposite view: that independent teams are too important to the company's future for top performers to be deployed elsewhere. Executives whose companies have been through agile transformations say much the same thing. In an interview with McKinsey, Scott Richardson, chief data officer at Fannie Mae, said, "Creating a new team is probably the most important thing managers can do, so make sure you get it right. When we created our initial agile teams, I was personally involved with structuring them and selecting team members. It might sound crazy to get so involved in this level of detail, but it is critical that the early teams become true beacons for success." Choosing high-caliber people not only sets up the teams to be successful but also teaches managers how to build more independent teams. "By the fourth or fifth team," Richardson continued, "my direct reports knew what questions to ask and how to structure a proper team, and they could scale up on their own from that point forward."

Provide teams with a clear view of their customer

At digital-native companies and agile incumbents, an unwavering focus on improving customer experiences provides each independent team, regardless of its area of responsibility, with a consistent understanding of business priorities. Each team's job is simple: to generate small but frequent improvements in the quality of the customer's experience. Executives foster this shared sense of purpose by making sure that every team has a clear, unobstructed view of customers.

In the offices of one international retailer, real-time data on the customer experience is on display almost everywhere you go. Walk through the dining hall: oversized screens on the walls bear the latest conversion rates for each of the company's sales channels. Visit an independent team's workspace: screens are lit up with measures of customer behavior and satisfaction that relate to the team's responsibilities, such as revising the script that call centers follow or tinkering with the layout of the web storefront. At any moment during the workday, a product manager might drop by a team room to see what the team is working on, ask how customers are responding, and offer to help.

So that each independent team can track the customer experience in ways that are relevant to its work, companies might need to loosen their governance of data. A "canonical data model" that standardizes the classification of data across the entire company can cause inadvertent delays because all teams have to agree on changes to the model that are required to capture new kinds of data or reclassify existing data. To avoid these complications, independent teams are ideally allowed to work with and define data within their business context.

Allocate resources up front, then hold teams accountable

At most companies, teams that work on customer-facing products and services will almost always find a way to obtain the approvals, funds, information, and staff they need for new projects. Scarcity isn't the main problem—slowness is. To eliminate delays in the work of independent teams, executives should assign them all the resources they need to do their work up front: the authority to make key decisions, the ability to quickly hire new talent or secure contractors without going through standard human-resources or procurement processes, the money to cover operating expenses, and so on. These resources should include tools for building and launching whatever digital solutions might be needed to streamline customer journeys or business processes. This kind of self-service approach to application development also requires modular, lightly connected IT architectures, which allow companies to continually develop new applications in a flexible way—an approach one might call "perpetual evolution."

The less dependent on other stakeholders small teams are, the more quickly they can get things done. And since teams invariably encounter unforeseen obstacles, such as a blanket policy preventing them from using public-cloud services, executives have to be there to help. Executives who sponsor the independent teams and make time to hear about their progress and understand their difficulties can push for additional reforms that will keep all independent teams on the fast track.

Once executives have given independent teams more resources and more authority, they need to make sure that those teams are consistently advancing the business's broader strategic priorities. As we'll discuss below, one role for managers in an agile organization is to help independent teams choose the outcomes they will pursue and measure their achievements in precise, meaningful terms. It's the job of top executives to hold teams accountable for delivering those outcomes—and to quickly allocate resources away from disappointing endeavors and toward successful ones. McKinsey research has found that tying budgets to strategic plans is more closely correlated with higher growth and profitability than any other budget-allocation practice that is linked to superior performance.

How executives can empower the agile manager

If the company's squads are going to operate at maximum speed, midlevel managers must learn and practice behaviors that let those units operate in a genuinely agile manner. (See the companion article, "The agile manager.") But if these managers are going to encourage and enable team members, they themselves have to be become well versed, and comfortable, with agility. This won't be an easy task for managers accustomed to the more predictable set of tasks they performed in a command-and-control hierarchy. Senior executives must ensure that these managers learn and embrace new ways of interacting with teams. Here are three behaviors that executives should try to encourage in managers working with small teams:

Define outcomes, then let teams chart their own path toward them

Corporate leaders at agile companies put teams in charge of product features or components of their customer's journey and give them the freedom to decide the specific improvements that should be made. An effective manager in this context will determine what the business outcomes should be, based on the company's overall priorities, and will spell it out for the team using real-world measures of business performance such as conversion rates or audience engagement. Then, rather than dictating the steps a team should take toward those outcomes, the manager must allow the team to chart its own process, intervening only when the team discovers a problem or a need that it can't address on its own.

One retailer greatly increased the pace at which it enhances customer-facing services by giving more authority to a group of small, independent teams. The retailer made the desired business outcome crystal clear: improve conversion rates by 30 percent. But the specifics of how to make that happen were left to the teams. One team responsible for the company's email campaigns decided to test whether targeting smaller groups of customers with highly specialized product offers and sales announcements would lead to more conversions. The team decided to run a trial of the new campaign against a traditional one, and the results were good. That was all the proof it needed to adopt the new approach. No formal proposals or budget discussions or senior-management approvals were required—in fact, any of those steps could have slowed down or derailed the process altogether.

Step inside independent teams to enable their success

Independent teams typically hold a daily "stand-up" meeting of around 20 minutes to review their activities, plans, and difficulties. Then they spend most of their day on productive tasks, rather than administrative ones such as writing formal progress updates.

This manner of working can require major adjustments from managers. They may find their skills in areas like planning and decision making are less needed, while other capabilities, such as communication and problem solving, must be exercised more frequently. Not every manager will welcome the pressure to adapt. Some might start updating their résumés.

Top leaders should encourage these cautious managers to step inside their independent teams. They should join the daily stand-up meetings to hear what the team is doing or try to troubleshoot situations in real time over agile-friendly platforms such as Jira and Slack. Most managers who actively engage in this way come to appreciate the agile approach. An agile organization largely relieves managers of tasks like allocating staff and resources and mapping out projects. Instead, it can spend more time on higher-value activities: applying expertise to long-term matters, coaching team members and peers, and helping teams work around obstacles.

A top-performing software developer at a rather traditional company that was still engaged in the waterfall style of software development passed up several promotions that would have put him in charge of development teams. He preferred grappling with technical challenges and writing code to managing people. But after the company reorganized its customer-facing functions into independent teams, his prospects changed considerably. He continues to work as a developer, but he also leads a network of coaches who teach the company's independent teams to follow agile ways of working. The new job combines technical assignments with the responsibility to share his expertise in agile development—and has none of the traditional management tasks that he had long avoided.

Commit to retraining managers for their redefined roles

Outside the IT function, managers who understand agile ways of working can be hard to find at traditional companies. To fit in with highly independent teams, most managers will need some help to learn how to organize their thinking around products rather than processes; to direct teams with performance goals instead of work plans; and to position themselves as stewards, not superiors. Executives can, and should, make sure that their managers have opportunities to develop these behaviors and habits of mind. They can see that managers are taught to use new tools, from collaboration software to analytics engines. They can encourage managers to rotate through assignments with various independent teams, which promotes constant learning. They should pair them with fellow managers who have more experience working with independent teams and let them see how these peers behave. And they can change the way they evaluate managers' performance, placing more emphasis on measurable outcomes and gauging their impact through 360-degree reviews.

Alfred Chandler, the renowned business historian, famously observed that structure follows strategy: companies set their strategies, then organize themselves in a way that lets them carry out their strategies to full effect. But pressure from fast-moving digital natives and digitally transformed incumbents means that traditional businesses no longer have time to rethink their strategies and reorganize themselves every few years. To promote enterprise agility, more companies are choosing to make small teams their basic organizational unit. Problems occur, however, when companies don't give their small teams enough autonomy to work at the speed required by the digital economy. Executives can change this by giving the teams the resources they need, by eliminating red tape, and by encouraging managers to learn, adopt, and enact the more flexible governance methods of agile organizational approaches. Those who do will see their small teams become more independent, and more capable of producing innovations and performance gains that keep their businesses ahead of the competition.

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How to mess up your agile transformation in seven easy (mis)steps

Article, April 2018 | By Christopher Handscomb, Allan Jaenicke, Khushpreet Kaur, Belkis Vasquez-McCall, and Ahmad Zaidi

The journey to become agile is challenging. But your organization can avoid some common pitfalls that we have seen companies encounter, including failing to create buy-in around an aspiration and forgetting to put culture first.

You have to give it to Silicon Valley: it sure knows how to disrupt industries. It has left its mark on every facet of our life—from how we socialize and interact, to how we travel, how we earn, and how we pay. The scale of impact has led to traditional companies in the ecosystem asking themselves, How do we get our large organizations to adapt and move as quickly as these nimble start-ups? The answer in many cases has to do with being more agile.

Agile principles have been one of the key drivers of Silicon Valley's ability to innovate, learn, and adapt rapidly. Agile started as a set of principles for software development to write and release code iteratively without waiting for months (or years) to release functionality. The term "agile" has now expanded to many facets of solution development with the same underlying principles—develop iteratively, release frequently, focus on the customer, and collaborate through a cross-functional team—always prioritizing test-and-learn methods over detailed planning. Beyond solution development, we are designing and implementing enterprise-wide operating models based on these principles.

While many traditional heavyweights have embarked on agile transformations, most have faced real challenges in achieving their desired objectives. Based on our experience across numerous transformations, we see the following as common missteps on an agile journey.

Misstep 1: Not having alignment on the aspiration and value of an agile transformation

Agile, fundamentally, is a redesign of the operating model of (parts of) the enterprise. We have often seen organizations embark on such transformations without first ensuring alignment among the leaders of the organization on the aspiration and value of the transformation. Further, even when there is such alignment, we often see companies that, in the spirit of adopting some agile principles—such as experimentation and empowered teams—end up creating a burning platform, as different leaders across the organization choose different approaches to implementing agile, while others dig in their heels to maintain the status quo.

While we don't encourage attempts to design an end state in granular detail, the depth and breadth of an agile transformation requires aligning at a high level on the aspiration, the value it would deliver, and a plausible plan for achieving it. The identified value drivers are then used throughout the transformation, from guiding the design of the operating model to ensure value delivery, to designing metrics to monitor value capture during rollout. Not doing so can constrain the impact the transformation might have.

For example, a large global company initiated a bottom-up agile transformation without first aligning on the end-state aspiration and the value the transformation would create. The transformation ended up having limited impact, as teams in different parts of the organization applied agile principles to varying degrees and in multiple flavors, which led to a significant increase in the overhead of managing across teams. Further, the lack of alignment on the value of the transformation meant that teams spent little time thinking through and tracking the value their efforts would deliver.

Misstep 2: Not treating agile as a strategic priority that goes beyond pilots

Too often, companies find themselves limiting agile to pilots within a small part of the organization, with a small set of leaders. While the pilot is typically successful, its impact is restricted to a few teams or a bunch of technologists. The limited nature of the pilot often prevents the CEO and executive team from grasping the far-reaching impact and strategic value a broader agile transformation could have. Companies often end up carrying a series of such pilots, before they're eventually killed once the need to reallocate funding for new initiatives arises.

While it is completely OK to start the agile transformation within, say, a small part of the organization, it is important not to stop there and to treat it as a strategic priority for the enterprise. Taking agile beyond small experiments is where the real benefits arise. For example, a large North American company was trying to implement agile in its technology organization, which encompassed 1,000-plus people. Every time business executives were asked about agile, they had a limited understanding and simply referred to it as "that project the technology team is trying to implement—we know nothing about it." The impact was limited, until 18 months into execution, when a massive change came about because one of the senior vice presidents started to take interest, understand, adopt, and make changes to his business practices to match the more agile technology organization. This led to an enterprise-wide transformation, with agile being identified as one of the top five enterprise priorities.

Misstep 3: Not putting culture first over everything else

Words cannot emphasize the cultural implications of an agile transformation. Ignoring the cultural and change-management implications of agile is one of the biggest mistakes large organizations make. Successful transformations require not only bottom-up change in the way of working at the team level but also a change in the way the executive level operates, as this has a disproportionate influence on the culture of the organization. "Culture is the king," as a senior executive appropriately said when referring to the recipe for success for an agile transformation. Conversely, an agile transformation can help drive significant cultural changes where desired, helping increase customer centricity, collaboration, learning, and more. These gains often require giving up some preexisting ways of working. A senior executive who has led multiple agile transformation puts it aptly: "The first question I ask leaders considering an agile transformation is, 'How much are you willing to give up?'"

For example, a large North American company had embarked on an ambitious agile transformation and hired several agile coaches to support teams. However, leadership in one of the businesses continued to work within the paradigms of the old culture: they were hesitant to empower teams, wanted detailed designs of the end product, and asked for project-management-office-style status reports on a weekly basis. Within the same organization, leadership in another business took a completely different approach and worked on changing the culture. Leaders empowered product owners and minimized bureaucracy. After one year of effort, the former business had little progress to show for any of its projects, whereas the latter had released multiple minimum viable products.

Misstep 4: Not investing in the talents of your people

One of the things that has made Silicon Valley start-ups successful has been their emphasis on finding and hiring the best talent. That talent is the fuel that powers the agile machine. This allows companies like Amazon to create truly cross-functional, empowered teams, with high-caliber, experienced talent embedded in them.

For many traditional organizations, talent strategy is an afterthought of an agile transformation. In the process, some crucial questions that merit careful consideration, such as the following, remain unanswered:

- What are the intrinsic skills required to be successful in the agile organization?
- Where will talented individuals with these intrinsics be sourced from?
- How will these employees be supported as they transition to an agile way of working?
- How will career paths change to a more expertise-based model?
- How will performance be managed in the new organization?
- What will happen to individuals who might not be required in the new agile organization?

The result: lack of excitement about taking on the new agile roles or joining agile teams due to lack of clarity on the career path, leading to teams that still require senior leadership to be deeply involved in decision making. For example, a midsize global company wanted to emphasize customer centricity as part of the agile organization. To achieve the goal, the client wanted to create a "design function" from zero people to more than 25 designers in various roles across multiple customer journeys. Such an endeavor required an up-front talent and recruiting strategy, diligent follow-up and interviews, and a careful scale-up approach to attract talent and excite them about the role and career opportunities. Because of a lack of detailed planning through these steps, seven months through the agile transformation, the client had not only struggled to recruit new designers to the function but also faced attrition among existing designers because of a lack of role clarity and excitement. This led to a significant amount of leadership time being spent on solving for these challenges. A similar situation occurred with a European company, where 11 out of 12 product owners in the first tribe set up as part of the transformation left for their old roles as they lacked coaching for transitioning to their new roles.

Misstep 5: Not thinking through the pace and strategy for scaling up beyond pilots

It is one thing to pilot agile in small pockets of an organization, where one can deploy resources from across the enterprise to support the pilot and make it successful. However, scaling across a broad cross-section is another story and requires up-front planning. One must think through the readiness of the organization, resourcing constraints, leadership bandwidth, and consequently the pace of the transformation, among other things. These plans need to be adjusted based on learnings through implementation.

For example, a midsize global company had planned its agile transformation around five waves. However, it had not spent enough time thinking through the scale of leadership bandwidth that would be required and the effort that would go into recruiting for the new agile organization. After completing the first two waves, the company was forced to reconsider the pace of its agile transformation and extended it to seven waves.

Misstep 6: Not having a stable backbone to support agile

Too often, agile is taken as an approach to managing projects. It is important to recognize that for teams to operate using agile methodology requires changes to core management processes and the supporting tools that a team has access to, among other things.

For example, iterative development also requires iterative funding. This is a concept that is hard to grasp for many traditional businesses. A large North American company wanted detailed estimates of every project with respect to investment required and benefits expected when the project was complete. While initial and early estimates are beneficial, a dogmatic approach made product owners panic, led teams to fight over hypothetical financials, and caused massive enterprise-wide confusion.

Agile teams also require the ability to deploy technology assets rapidly. For example, a large North American company required around six to eight weeks to provision environments, which meant that the team had to spend considerable time planning to compensate for the time lag.

Absent these changes to core management processes, teams may find it hard to execute rapidly, which hampers innovation, increases time to market, and so on.

Misstep 7: Not infusing experimentation and iteration into the DNA of the organization

If you ask practitioners about the traits of an agile organization, you're likely to hear most of them mention iterative development. While this comes naturally to a start-up, which doesn't have an established product and needs to test and learn to develop one, it is more complex to grasp for an organization that has not one but many product lines that have a reputation of excellence in the market. This also applies beyond product development—consider how your organization prepares, for example, business strategies, recommendations to the leadership team, and product-launch strategies. All too often effort is wasted by teams operating in a vacuum, second guessing what stakeholders might want to see, or perfectly executing the wrong plan rather than engaging stakeholders throughout the process to get input regularly and ensure the team is focused on what really matters.

Another aspect that often limits experimentation is the rigid application of scaled agile frameworks. Too often, companies end up shifting the focus of an agile transformation away from minimizing processes and changing mind-sets and behaviors to enable innovation, toward putting in place the right framework. While frameworks can be valuable in providing structure to the transformation, it is important not to be rigid in their adoption, and to always think of how they can be adapted to suit the needs of the organization. After all, one of the pillars of the original agile manifesto was to favor "individuals and interactions over processes and tools."

For example, while a North American company embraced iterative agile development in theory, management stuck to a rigid framework it had developed that required high-fidelity mock-ups of the end product and detailed business plans before product development had even commenced. An agile organization would have done just enough to get a version of the product out to market quickly and gather feedback from customers to guide future developments, seeking input from the real end users of the product. This rigid application of the framework ended up limiting the impact of the agile transformation.

There are undoubtedly many other examples of missteps that have derailed agile transformations. In our experience, these missteps are largely preventable but too often result in agile being written off. Becoming armed with the right level of understanding for how to drive an agile transformation, and respecting the complexity of such a transformation, is a first step toward a successful journey—and based on the impact we have seen with companies that have undergone successful agile transformations, a very worthwhile investment to make.

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Building agile leadership and capabilities

Leading agile transformation: The new capabilities leaders need to build 21st-century organizations

September 2018 | Aaron De Smet, Michael Lurie, and Andrew St. George

To build and lead an agile organization, it's crucial that senior leaders develop new mind-sets and capabilities to transform themselves, their teams, and the organization.

For many organizations, surviving and thriving in today's environment depends on making a fundamental transformation to become more agile. Those making the transition successfully are achieving substantive performance and health improvements: enhanced growth, profitability, customer satisfaction, and employee engagement.

More than any other factor, the key to a successful agile transformation is for leaders, particularly senior leaders, to develop substantially new mind-sets and capabilities. This article summarizes our guide, *Leading agile transformation*, to readying leaders for agile transformations.

The agile story

Before we dive deep, it's useful to take a broader view of agile, and particularly what sets agile organizations apart from traditional ones.

Characteristics of traditional and agile organizations

Simply put, the dominant traditional organization model evolved primarily for stability in a well-known environment. It is based on the idea of an organization as a machine, with a static, siloed, structural hierarchy that operates through linear planning and control to execute one or very few business models.

Agile[1] organizations, viewed as living systems, have evolved to thrive in an unpredictable, rapidly changing environment. These organizations are both stable and dynamic. They focus on customers, fluidly adapt to environmental changes, and are open, inclusive, and nonhierarchical; they evolve continually and embrace uncertainty and ambiguity. Such organizations, we believe, are far better equipped than traditional ones for the future.

While there are many different forms of enterprise agility, they share some common trademarks. We have identified and enumerated these in a related article, "The five trademarks of agile organizations."[2]

Leadership in agile organizations

This new kind of agile organization requires a fundamentally different kind of leadership. Recent research confirms that leadership and how leadership shapes culture are the biggest barriers to—and the biggest enablers of—successful agile transformations.

1 The term "agile" as applied to a way of working that originated in 2001 with a new approach to software development. As organizations increasingly sought to become more agile—that is, faster and more flexible—they recognized that principles of agile software development could be applied much more broadly to organizations as a whole.

2 Wouter Aghina, Aaron De Smet, Gerald Lackey, Michael Lurie, and Monica Murarka, "The five trademarks of agile organizations," January 2018, McKinsey.com.

Organizations must therefore begin by both **extending and transcending the competencies** that made their leaders successful in the past.[3] To lead an agile transformation successfully, you need to develop three new sets of capabilities. First, you must learn to transform yourself, by evolving new personal mind-sets and behaviors. Second, you must learn how to transform your teams to work in new ways. Third, it's essential you learn how to transform your organization by building agility into the design and culture of the whole enterprise.

Transforming yourself

To fully transform yourself, several shifts will be necessary—and leaders will need to make these changes in a disciplined way.

Shifting from reactive to creative mind-sets

Changing our mind-set—or adjusting it to the new context—is no easy task, but **developing this "inner agility"** [4] is essential in releasing our potential to lead an agile transformation.

Reactive, or socialized, mind-sets are an outside-in way of experiencing the world based on reacting to circumstances and other people. Creative, or self-authoring, mind-sets are an inside-out way of experiencing the world based on creating our reality through tapping into our authentic selves, our core passion and purpose.

Research shows that most adults spend most time "in the reactive," particularly when challenged, and as a result, traditional organizations are designed to run on the reactive.[5] To build and lead agile organizations, however, leaders must make a personal shift to run primarily "in the creative."

There are three fundamental reactive-to-creative mind-set shifts we have found critical to foster the culture of innovation, collaboration, and value creation at the heart of agile organizations:

- **From certainty to discovery: fostering innovation.** A reactive mind-set of certainty is about playing not to lose, being in control, and replicating the past. Today, leaders need to shift to a creative mind-set of discovery, which is about playing to win, seeking diversity of thought, fostering creative collision, embracing risk, and experimenting.

- **From authority to partnership: fostering collaboration.** Traditional organization design tends toward siloed hierarchies based on a reactive mind-set of authority. The relationship between leaders and teams is one of superior to subordinate. Designed for collaboration, agile organizations employ **networks of autonomous teams.** This requires an underlying creative mind-set of partnership, of managing by agreement based on freedom, trust, and accountability.

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3 See: Aaron De Smet, Bill Schaninger, and Mathew Smith: "The hidden value of organizational health—and how to capture it," McKinsey Quarterly, April 2014, McKinsey.com.

4 Sam Bourton, Johanne Lavoie, and Tiffany Vogel, "Leading with inner agility," *McKinsey Quarterly*, March 2018, McKinsey.com.

5 See Carol S. Dweck, *Mindset: The New Psychology of Success, New York,* NY: Ballantine Books, 2007.

- **From scarcity to abundance: fostering value creation.** In stable markets, companies maximize their shares at the expense of others. This win–lose approach reflects a reactive mind-set of scarcity, based on an assumption of limited opportunities and resources. Today's markets, however, evolve continually and rapidly. To deliver results, leaders must view markets with a creative mind-set of abundance, which recognizes the unlimited resources and potential available to their organizations and enables customer-centricity, entrepreneurship, inclusion, and cocreation.

A disciplined approach

While these mind-set shifts might be new and require a significant "letting go" of old beliefs and paradigms, collectively, they form a very disciplined approach to leadership. And because of inherent autonomy and freedom, leadership in agile organizations comes from a self-disciplined approach—leading not in fear of punishment or sanction but in service of purpose and passion.

Transforming your teams

Next, it's important to learn how to help teams work in new and more effective ways.

Help teams work in agile ways

How might leaders help teams work in new and more agile ways? And what does this new way of working require of leaders? There are three essential leadership requirements that follow from all agile ways of working.

First, leaders must learn to build teams that are small, diverse, empowered, and connected. Second, leaders must allow and encourage agile teams to work in rapid cycles to enable them to deliver greater value more efficiently and more quickly. Third, leaders must keep agile teams focused on the external or internal customer and on creating value for customers, by understanding and addressing their unmet, and potentially even unrecognized, needs.

Embrace design thinking and business-model innovation

We have found that in addition to being able to lead in this new agile way of working, it is important for leaders to understand the key elements of two other relatively new disciplines: **design thinking** and business-model innovation.

Originating in industrial and other forms of design, design thinking is a powerful approach to developing innovative customer solutions, business models, and other types of systems. This begins with understanding the entire customer experience at each stage of **the customer journey.**

In organizations that are agile, each team is viewed as a value-creating unit, or as a "business." These teams pursue business-model innovation at every opportunity, seeking new ways to meet the needs of their internal or external customers and deliver more value to employees, investors, partners, and other stakeholders.

Transforming your organization

Here, leaders must learn how to cocreate an agile organization purpose, design and culture.

Purpose: Find the north star

The first distinctive organization-level skill leaders need to develop is the ability to distill a clear, shared, and compelling purpose—a north star—for their organization. Rather than the traditional executive-team exercise, in agile organizations, leaders must learn to sense and draw out the organization's purpose in conversation with people across the enterprise.

Design: Apply the principles and practices of agile organization design

The second organization-level skill leaders need to develop is the ability to design the strategy and **operating model** of the organization based on agile-organization principles and practices. Most senior leaders of traditional companies have a well-honed skill set in this area that reflects traditional organization design as a relatively concentrated, static system: one or a very limited number of major businesses, each with a long-established business model, typically coexisting somewhat uneasily with a set of corporate functions.

To design and build an agile organization, leaders need a different set of skills based on a different understanding of organizations. They must learn to design their organization as a distributed, continually evolving system. Such an organization comprises a network of smaller empowered units, with fewer layers, greater transparency, and leaner governance than a traditional model. More specifically, leaders must learn how to disaggregate existing large businesses into a more granular portfolio; transform corporate functions into a lean, enabling backbone; and attract a wide range of partners into **a powerful ecosystem.**

Culture: Shape an agile organizational culture

The third organization-level skill leaders need to develop is the ability to shape a new culture across the organization, based on the creative mind-sets of discovery, partnership, and abundance and their associated behaviors.

Given the openness and freedom people experience in an agile organization, culture arguably plays an even more important role here than in traditional organizations. To shape this culture, leaders must learn how to undertake a multifaceted culture-transformation effort that centers on their own capabilities and behaviors. This includes the following steps:

- **role modeling** new mind-sets and behaviors authentically
- **fostering understanding and conviction** in a highly interactive way, through sharing stories and being inspired by the energy and ideas of frontline teams
- **building new mind-sets and capabilities across the organization,** including among those who do not formally manage people, and weaving learning into the fabric of daily activity to become true learning organizations
- **implementing reinforcement mechanisms** in the agile organization design

An agile approach to developing leaders

Many organizations start their agile pilots in discrete pockets. Initially, at least, they can build agile-leadership capabilities there. But to scale agility through an organization successfully, top leaders must embrace its precepts and be willing to enhance their own capabilities significantly. Eventually, a full agile transformation will need to encompass building the mind-sets and capabilities of the entire senior leadership across the enterprise. To do this in an agile way, five elements are essential:

1. **Build a cadre of enterprise agility coaches,** a new kind of deeply experienced expert able to help leaders navigate the journey, supported by a leadership-transformation team.

2. Get the top team engaged in developing its own capabilities early on, as all senior leaders will take their cue from the executive team.

3. Create an immersive leadership experience (anything from a concentrated effort over three or four days to a learning journey over several months) to introduce the new mind-sets and capabilities, and roll it out to all senior leaders.

4. Invite leaders to apply their learning in practice, both in agile-transformation initiatives already under way and through launching new organizational experiments.

5. Roll out the leadership capability building at an agile tempo, with quarterly pauses to review the leadership experiences, experiments, and culture shifts over the past 90 days, and then finalize plans and priorities for the next 90 days.

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Agile transformation is a high priority for an increasing number of organizations. More than any other factor, the key enabler to a successful agile transformation is to help leaders, particularly senior leaders, develop new mind-sets and capabilities. Doing so in an agile way will enable the organization to move faster, drive innovation, and both adapt to and shape its changing environment.

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Leading with inner agility

***McKinsey Quarterly*, March 2018** | By Sam Bourton, Johanne Lavoie, and Tiffany Vogel

Disruptive times call for transformational leaders with a knack for addressing complex problems. To navigate effectively, we must learn to let go—and become more complex ourselves.

We live in an age of accelerating disruption. Every company is facing up to the profound changes wrought by digitization. Industry boundaries have become permeable. Data, algorithms, and artificial intelligence are changing the nature of forecasting, decision making, and the workplace itself. All this is happening at once, and established companies are responding by rethinking their business models, redesigning their organizations, adopting novel agile-management practices, and embracing design thinking.

We've had a front-row seat at many such transformation efforts. Their importance, and the challenge they pose for institutions, has been well documented by management writers. But comparatively little attention has been paid to the cognitive and emotional load that change of this magnitude creates for the individuals involved—including the senior executives responsible for the success or failure of these corporate transformations. What makes the burden especially onerous is the lack of clear answers: the very nature of disruption means that even the best, most prescient leaders will be steering their company into, and through, a fog of uncertainty.

You aren't alone if you feel threatened by this—everyone does, whether consciously or subconsciously. Even seasoned leaders internalize the acute stress of such moments—so much so that their judgment and decision-making skills seem insufficient. The result? They fall back on old habits, which, unfortunately, are almost always out of sync with what the current context demands.

The *problem* isn't the problem; our *relationship* to the problem is the problem. In other words, we have many of the skills needed to handle what's being thrown at us. But when faced with continual complexity at unprecedented pace, our survival instincts kick in. In a mental panic to regain control, we fight, flee, or freeze: we act before thinking ("we've got to make some kind of decision, *now*!"), we analyze an issue to the point of paralysis, or we abdicate responsibility by ignoring the problem or shunting it off to a committee or task force. We need inner agility, but our brain instinctively seeks stasis. At the very time that visionary, empathetic, and creative leadership is needed, we fall into conservative, rigid old habits.

You can't steer your company through constant change if you are relying on the safety of your own cruise control. To spot opportunities—and threats—in this environment, we must teach ourselves how to have a more comfortable and creative relationship with uncertainty. That means learning how to relax at the edge of uncertainty, paying attention to subtle clues both in our environment and in how we experience the moment that may inform unconventional action.

Developing this kind of inner agility isn't easy. In some ways, it goes against our very nature, which wants to simplify a problem by applying our expert mind-set and best practices. To address complex problems, we need to become more

complex ourselves. We need to recognize and appreciate emergent possibilities. That’s how the complexity we face can become manageable, even exciting.

In our experience, five personal practices can meaningfully contribute to the mind-set needed for leadership effectiveness during transformative times. They are extensions of timeless principles of centered leadership; taken together, they can be the building blocks of your personal inner agility:

1. *Pause to move faster.* Pausing while remaining engaged in action is a counterintuitive step that leaders can use to create space for clear judgment, original thinking, and speedy, purposeful action.

2. *Embrace your ignorance.* Good new ideas can come from anywhere, competitors can emerge from neighboring industries, and a single technology product can reshape your business. In such a world, listening—and thinking—from a place of not knowing is a critical means of encouraging the discovery of original, unexpected, breakthrough ideas.

3. *Radically reframe the questions.* One way to discern the complex patterns that give rise to both problems and windows of emergent possibilities is to change the nature of the questions we ask ourselves. Asking yourself challenging questions may help unblock your existing mental model.

4. *Set direction, not destination.* In our complex systems and in this complex era, solutions are rarely straightforward. Instead of telling your team to move from point A to point B, join them in a journey toward a general direction. Lead yourself, and your team, with purposeful vision, not just objectives.

5. *Test your solutions—and yourself.* Quick, cheap failures can avert major, costly disasters. This fundamental Silicon Valley tenet is as true for you as it is for your company. Thinking of yourself as a living laboratory helps make the task of leading an agile, ever-shifting company exciting instead of terrifying.

To be clear, these steps are not panaceas but a set of interrelated touchstones. Nor are they trivial to tackle. (See sidebar, “Micropractices that help you find stillness.”) But with conscious, disciplined practice, you stand a better chance of rising above the harried din of day-to-day specifics, leading your team effectively, and surveying your company and its competitive landscape with creative foresight. Let’s look now at how this played out in some real-life examples, starting with two leaders who were trying to save a merger that had unfolded in unpredictable, troubling ways.

1. Pause to move faster

Anticipating tough questions at an upcoming board meeting, the CEO and CFO of a global manufacturer met to review the status of a substantial merger they had engineered about 12 months earlier. It wasn’t a pretty picture. Despite following the integration plan closely, despite intensive scenario planning, and despite clear, achievable targets, productivity was falling. The more the two dug into the results of their grand plan, the more heated the discussion. The

Micropractices that help you find stillness.

The five practices described in our main story are only the starting point for developing inner agility, and they require sustained commitment. It's easy to slip back into the groove of old habits, particularly when uncertainty inspires fear. Here is a short list of cognitive, centering micropractices—muscle builders, you might call them—that can help you stay on track.

The four-breath pause

Sometimes, when we're afraid of not knowing, we try to rush to some kind of answer. To slow down the process and gain some perspective, count through four breaths, paying attention to nothing but your inhaling and exhaling air. That's a quick way to give yourself a break from the chaos around you.

Grow roots

Leaders need the mindfulness to be both part of and yet separate from their context. One helpful way of doing this during a meeting is to put both feet on the floor and visualize roots extending from your soles down through the surface below. This centering practice can quiet overthinking, making you more receptive to new ideas.

Take ten minutes (or even one)

Meditation isn't a panacea, but many executives find it helpful. Attention management is a must for executives overloaded with information. As one leader told us, "Without those ten minutes, I have no stillness." Others make a point of grabbing one minute of stillness between meetings. "It gives me a sense of spaciousness," one CEO explained.

Listen from a place of not knowing

Listening well is an underappreciated art and a requirement for any leader who wants to be alert to today's widening range of threats and opportunities. You must put preconceptions and judgments aside to truly hear what someone else has to say. In conversation, Pixar president Ed Catmull never responds until the other person has finished speaking. This enables him to appreciate the other's full thought, and to respond articulately.

Draw a bigger weather map

Feeling overwhelmed in the face of uncertainty is like looking out your window onto a thunderstorm—you're socked in, and there's no way you're going to venture out. At times like this, it helps to expand the boundaries of your mental weather map to see the weather patterns (business trends) that created the thunderstorm (your current business dilemma). Taking the long view can diminish the anxiety caused by near-term worries.

CFO wanted to shutter a dozen factories in the company's expanded portfolio. The CEO, who had promised that the merger would lead to bold innovation, wanted to increase funding of those very plants, since they were making the ambitious products the company would need in the long run. Despite having worked together for quite a while, the two men had such differing views that neither knew how to move forward together.

The stakes were highly personal. The CFO feared that the board and his executive colleagues would blame him for failing to identify the true cost structure of the combined companies. He gave serious thought to resigning. The CEO feared that the board would begin to doubt his strategic rationale for the merger. With their competence threatened, each had reverted to fallback positions, insisting that their own experience justified the solution they proposed. That's why their two days of nonstop meetings had led to an impasse.

Then they agreed to temporarily halt their discussions. Given the urgency each man felt, this was not an easy decision. But they believed they had no other choice—they weren't going to arrive at a solution by continuing to butt heads. They agreed to cut off their conversation for a week and committed to spending the time investigating the productivity failure on their own, hunting for clues they might have missed.

The two leaders had decided to pause, in order to move faster. This kind of pause isn't an abdication; it isn't even a concession that finding an answer will take a long time. Instead, it's a real-time pause that allows you to decouple from the immediate challenge so that you can find new ways of responding. Instead of being limited by old habits, you're trying to give yourself greater freedom of choice.

Most executives have trouble pulling back from obsessive engagement with the issue at hand; for many, in fact, that focus has been a key to success. But trying to survive one crisis after another by relying on the tried and true isn't enough these days. Pausing in the chaos of great change is a counterintuitive action that can lead to greater creativity and efficiency. It carves out a safe space for self-awareness, for recentering yourself, for something new to emerge.

Claiming this space is hard, and there are no silver bullets. Some CEOs like daily meditation. We know one CEO who takes a ten-minute walk through the neighborhood around his office—leaving his cell phone on his desk. Others regularly catch a minute's worth of deep breathing between meetings. The repetition of such practices helps them pause in the moment, interrupt well-grooved habits that get triggered under duress, and create space to practice something different.

Pausing requires substantial self-awareness, and you may not get immediate results. Every bit of benefit counts, though, and if you don't start the journey of learning how to decouple from your context and the immediate response it provokes, you'll find it harder and harder to be open to new ideas, or to become a better listener—both traits that are critical at moments where your own vision is clouded.

2. Embrace your ignorance

During their week apart, the CEO and the CFO dug around for answers. The CFO met with plant managers, who described a pattern of project delays caused by costly reworking of product designs. Several HR leaders told the CEO that people at all levels—hourly workers, supervisors, and managers—were frustrated. Trying to meet the unrealistic assumptions made during the merger process, managers were serving up impossible and confusing directives to supervisors, who in turn were leaning heavily on workers.

The information was interesting. But the CEO and CFO agreed that they were still largely in the dark. They decided that they would next meet with all the members of the executive team. They needed the help of many voices.

With the whole team gathered, the CEO and the CFO listed their assumptions about what might have caused the productivity slump. Then they went around the room, asking questions: How may we be wrong? What else is happening? Who sees this differently? The chief human-resources officer, a quiet fellow during most discussions about operations, spoke up to say that absenteeism was at an all-time high. The vice president of marketing mentioned that the company's largest customer had complained recently about the call center. As more managers weighed in, patterns started to emerge, patterns that had nothing to do with numbers. The vice president of strategy, who was in the process of moving into a new house with her new husband and children, said, "This reminds me of my kids. Joe and I were so focused on making the move happen efficiently that we completely missed the fact that our kids were anxious. They needed to be reassured, not told they were moving into the perfect room! I wonder if fears and anxieties in our employee base could be driving this." Together, the managers came to a jarring realization: they had failed to reassure employees about this massive change in their lives.

The CEO and CFO would never have uncovered this answer without acknowledging their own ignorance, and without listening carefully and openly. Furthermore, as everyone around the table acknowledged, their conclusion raised a whole set of new questions, some potentially more important than the productivity problem. How could the executive team have missed this? How could they have been so wrong? Even more broadly, what kind of culture were they creating at this company? A productivity problem had become an existential question about the mental health of the company. Sometimes, ignorance can push you further than expertise. In fact, ignorance is a necessary asset in this age of disruption. Expecting that you can know everything is a hubristic concept of the past.

But embracing your ignorance is hard. Letting go of your need to know means challenging your own identity as exceptionally competent. One CEO we know pretends to have a long dinosaur tail that represents all her life experience. In meetings, she imagines that she tucks it away beneath her. It's comforting that it's there. It allows her to lean back and access a sense of self-sufficiency that can be summed up by the thought, "I am enough." That comfort shifts her into a deeper listening mode, where she's unencumbered by the urge to provide a quick answer. She feels that she's able to hear not just the words and ideas of others, but the subtext of conversations. Since adopting this practice, she's received feedback that people feel more empowered and creative when meeting with her.

A dinosaur tail isn't for everyone. Another CEO makes a conscious practice of listening with his heart instead of listening with logic. He finds himself more fully digesting what the other person is saying. His curiosity is piqued as he pays better attention to their concerns, needs, and ideas. He believes he has become more patient, which has created more space for creative dialogues.

The embrace of ignorance cuts against the grain for most of us and can take a lifetime to master. To get started, ask yourself some probing questions. First: "Do I suspend judgment and listen for what is below the words, or do I listen for what I already know or believe?" If it's the latter (as it is for so many of us), go on to this second one: "What would I have to let go of to truly listen?" Third: "What is the very worst that could happen?" The answer to that can help you find the hidden fear that you may need to befriend. And, finally, there's a fourth: "Am I the leader I want to be?" If the answer is "not yet," then you know why embracing ignorance must become a priority. Asking these questions may not dissolve the reactive habits that hold us back, but they can begin a process of letting go to find new capacities within ourselves.

3. Radically reframe your questions

The CEO and CFO of our global manufacturer could have reacted in two ways to that boardroom discussion. They might have said, "Let's get back to basics and just attack productivity. After all, that is the problem we set out to solve." But they chose to pursue a bigger question: "What kind of culture do we want to create?"

After the meeting with the executive team, the CEO and CFO set out on a "listening tour"—a valuable executive response that becomes even more important as technology increases the clock speed of our lives. For ten days, the two leaders toured plants and visited regional offices, listening to shop-floor workers, managers, division-level HR executives, and operations specialists. They didn't go in with predetermined questions. Instead, they posed open-ended questions designed to surface multiple, and often hidden, perspectives. They relentlessly asked, "and what else?" to unearth viewpoints that had gone untapped for so long.

Then the CEO and CFO again assembled the executive team. Now, armed with a panoply of varied, often colliding perspectives, the team could dig into the root causes of those productivity decreases. This wide-open, wide-ranging dialogue reset the direction of the merger. New goals were set on new timetables, based on a better understanding of what employees needed and the way employee networks in the merged company fed off one another. The CEO and other leaders revived the sense of purpose that employees had felt for so long by transparently recentering the company's transformation on the customer. They also empowered a set of shop-floor change agents to drive the shift through every layer of the company. It wouldn't be hyperbole to say that answering the bigger question—what kind of culture do we want to create?—saved the merger.

Radically reframing the question isn't just good for the company. It's a critical skill for any modern executive, and it takes time to build. Start by challenging yourself. Revisit the diversity of your personal network, which for many of us looks too familiar, too much like us, to provide significant exposure to alternative viewpoints. Another useful prod is asking yourself challenging questions, such as, "What is wrong with my assumption? What am I missing? Am I expanding the boundaries of the problem, to allow for unexpected factors?" Identify those who most oppose your view, and understand the story from their point of view. These kinds of questions and conversations take you into the unknown, which is where you'll find the most valuable answers.

When you step into the unknown, you also boost your odds of getting a glimpse of "inner blockers" that can inhibit you from leading with inner agility. The CFO realized that his initial stubbornness was driven by a deep fear of failure that had been with him for years. The CEO came to understand his own actions in very personal ways. Ever since he was 16, when his father had passed away, he had assumed responsibility for providing for his mother and for his extended family. Providing for those around him was a value that carried through to his work life and had helped him succeed. But in this case, he had been overprotective. Too focused on his own need to deliver on his promises, he hadn't listened carefully and openly to his people. After working his way through this crisis, he would never infantilize his workforce again. Since then, his people have become his most important source of innovation and ideas.

4. Set direction, not destination

Let's turn to another situation. The new CEO of a supplier to a major manufacturing sector wanted to signal quickly and clearly where the company was headed. The 150-year-old company had lost ground to overseas competitors, so he believed a transformation was in order, and fast. He replaced 60 percent of his executive staff with newcomers from entrepreneurial companies and announced that the company would be the low-cost provider of its most important part. He dubbed it the "three-dollar plan." He was sure that this clear, concrete plan would pay off in many ways: existing customers would be pleased, new ones would be won, profits would rise, and employees would be cheered by the turnaround.

One year later, however, the numbers told a different story. Expected cost savings from manufacturing efficiencies weren't showing up. Profits and sales were flat. Employee engagement, as measured by participation in the annual survey, had dropped by 20 percent. Uncertain about how to respond, he took a step back: he and some top advisors began asking a lot of questions of people at all levels of the company.

As he listened, he came to understand his big mistake: instead of sharing a vision of the general direction for the company, he had pointed employees to a destination, and given them no context for his decision. The company had long been admired for its great customer service, and many longtimers didn't understand how the "three-dollar plan" could coexist with that reputation. His clarity had denied their creativity: they saw the plan for what it was, a productivity goal, not a vision that demanded their best work and thinking. Without a supportive, engaged workforce, the plan had failed.

Fast forward to today: two years after that realization, pride in the work has been reestablished, and the company is on solid financial ground. What changed?

The CEO changed. As he was reflecting on why his staff had lost motivation, several family portraits that adorned his office caught his eye. Family was important to him, and he suddenly realized that he managed that part of his life very differently from his company. He didn't give deterministic outcomes to his children. Instead, he tried to point them in certain values-based directions and give them the tools to succeed, knowing that the outcome would depend much more on their talents than his dictates. He accepted his children's independence, but not his workers'. He determined to manage his company the way he parented. He engaged the staff in determining the direction of the company; he tasked a diverse group of employees with figuring out whether the three-dollar plan could coexist with the customization that had given the company such a great reputation for customer service and innovation. They came to believe it could, and even developed a tagline that nodded to the past while pointing to a new direction: "Building the business together for the next 150 years on a proud heritage."

We'd be the first to acknowledge that applying techniques from the home front won't work for everyone: after all, some executives are more autocratic at home than in the office! Still, we think any leader of a business that depends on the creativity of its people will find value in bringing this directional mind-set into the office.

Setting a direction that is rooted in purpose and meaning can inspire positive action and invite others to stretch out of their comfort zone. Make it personal by starting with your own personal vision: What really matters for you? What do you want to create through your leadership? What do you want to be remembered for? What do you want to discover? These are the kinds of questions that help you set a meaningful, values-based direction, for yourself and others.

5. Test your solutions, and yourself

Developing inner agility is a process of accepting less control than makes you feel safe. But that doesn't mean you're embracing chaos.

Most Silicon Valley companies are networks, designed so that ideas will spark from many different corners of the organization. How do they surface the best ones? By testing often, creating "safe to fail" experiments and then rewarding learning. Testing fast and small is critical for agile companies. It ensures that you can respond quickly to technological shifts or changed market conditions. And microfailures reduce the chance of macrofailures.

Applying this testing concept to yourself is a critical part of developing inner agility. Try to create mindful experiments for yourself. A baby step: ditch your slideshow presentation for an important meeting, and instead try to stimulate unconventional thinking by telling a story. You may bomb, but that's OK—you're starting to learn how to unearth new viewpoints. Using everyday leadership situations as a practice ground can help you build comfort with uncertainty and develop the learning mind-set needed to provide leadership at a time when, as Andy Grove once said, "None of us have a real understanding of where we are heading."[1]

1 See Jeffrey Pfeiffer and Robert I. Sutton, ***Hard Facts, Dangerous Half-Truths, and Total Nonsense: Profiting from Evidence Based Management,*** first edition, Boston, MA: Harvard Business School Publishing, 2006, p. 201.

Testing and experimentation is tightly intertwined with the other four practices of inner agility. The experiments we conduct move us in the direction we have set, while the process of setting a direction that's rooted in purpose helps us build the courage to experiment. Pausing helps us to decouple from our context and develop comfort with not knowing, a necessary condition for any meaningful experiment. And reframing and expanding the questions we ask ourselves gives us the broad perspective we need to create experiments that will move us in the right direction.

In times of complexity and high stress, we find our sense of our own competence (and sense of self!) continually challenged. We have two choices: try to reduce discomfort by falling back on trusted habits, or embrace the complexity and use it to learn and grow. Bold leaders will develop a new relationship to uncertainty. We must grow more complex from within. Taken together, the five practices we have discussed here are the foundation of a mind-set that is comfortable with leading despite, and through, uncertainty. The more you practice these steps, the more you will develop inner agility, tap into creativity, and enjoy the ride! Each small failure will teach you something, and each success will help confirm that it is possible to lead effectively without having all the answers. Today's leaders must be like eagles, who don't flap their wings harder or strain against the wind stream when they encounter great turbulence. Instead, they become even more still, knowing that they have the agility and self-possession to soar even higher.

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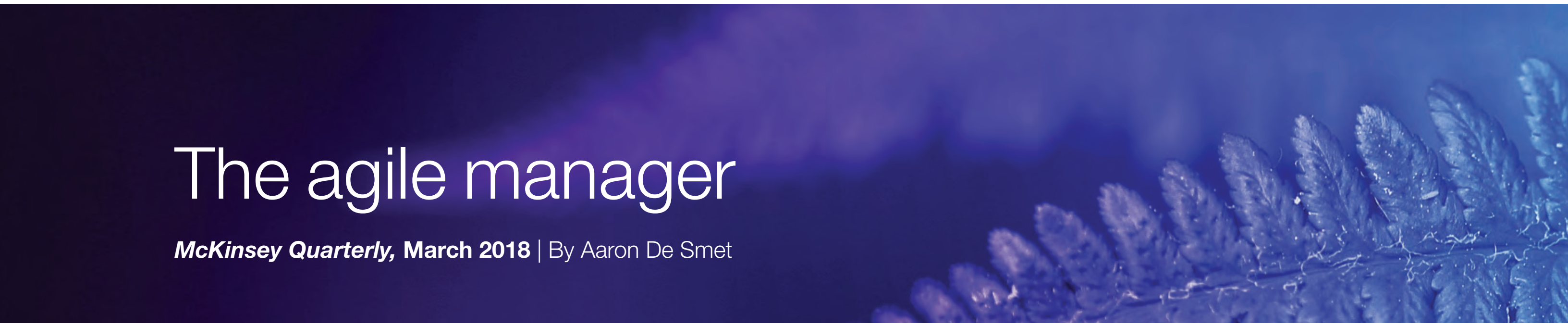


The agile manager

***McKinsey Quarterly,* March 2018** | By Aaron De Smet

Who manages in an agile organization? And what exactly do they do?

The agile workplace is becoming increasingly common. In a McKinsey survey of more than 2,500 people across company sizes, functional specialties, industries, regions, and tenures, 37 percent of respondents said their organizations are carrying out company-wide agile transformations, and another 4 percent said their companies have fully implemented such transformations. The shift is driven by proof that small, multidisciplinary teams of agile organizations can respond swiftly and promptly to rapidly changing market opportunities and customer demands. Indeed, more than 80 percent of respondents in agile units report that overall performance increased moderately or significantly since their transformations began.

These small teams, often called “squads,” have a great deal of autonomy. Typically composed of eight to ten individuals, they have end-to-end accountability for specific outcomes and make their own decisions about how to achieve their goals. This raises an obvious and seemingly mystifying question for people who have worked in more traditional, hierarchical companies: Who manages in an agile organization? And what exactly does an agile manager do?

Lay of the land

The answers become clear once you understand that the typical agile company employs a dynamic matrix structure with two types of reporting lines: a capability line and a value-creation line. Nearly all employees have both a functional reporting line, which is their long-term home in the company, and a value-creation reporting line, which sets the objectives and business needs they take on in squads.

In agile parlance, the capability reporting lines are often called “chapters” and are similar in some ways to functions in traditional organizations (you might have a “web developers” chapter, say, or a “research” chapter). Each chapter is responsible for building a capability: hiring, firing, and developing talent; shepherding people along their career paths; evaluating and promoting people; and building standard tools, methods, and ways of working. The chapters also must deploy their talented people to the appropriate squads, based on their expertise and demonstrated competence. In essence, chapters are responsible for the “how” of a company’s work. However, once talent is deployed to an agile team, the chapters do not tell people what to work on, nor do they set priorities, assign work or tasks, or supervise the day-to-day.

The value-creation reporting lines are often called “tribes.” They focus on making money and delivering value to customers (you might have a “mortgage services” tribe or a “mobile products” tribe). Tribes are similar to business units or product lines in traditional organizations. Tribes essentially “rent” most of their resources from the chapters. If chapters are responsible for the “how,” tribes are responsible for the “what.” They set priorities and objectives and provide marching orders to the functional resources deployed to them.

Management roles

In this world, the work of a traditional midlevel manager is reallocated to three different roles: the chapter leader, the tribe leader, and the squad leader. Let's examine the responsibilities of each and the challenges they pose for traditional managers looking to become agile managers.

The chapter leader

Every functional reporting line has a leader. This chapter leader must build up the right capabilities and people, equip them with the skills, tools, and standard approaches to deliver functional excellence, and ensure that they are deployed to value-creation opportunities—sometimes in long-term roles supporting the business, but more often to the small, independent squads. The chapter leader must evaluate, promote, coach, and develop his or her people, but without traditional direct oversight. Chapter leaders are not involved in the day-to-day work of squads; they don't check on or approve the work of their chapter members, and they certainly don't micromanage or provide daily oversight. Instead, regular feedback from tribe leaders, team members, and other colleagues inform their evaluations and the kind of coaching they provide. Since they're not providing direct oversight, their span of control can expand greatly, a fact that can eliminate several layers of management. In fact, chapter leaders often free up enough time to tackle "real work" on business opportunities as well.

The most difficult challenges facing new chapter leaders are letting go of the day-to-day focus, and shifting attention to building the right capabilities and helping match talent to the right roles and value-creation opportunities. Traditional managers are accustomed to closer oversight of their people. But if they can let go, they will find themselves in jobs that call on more of their leadership and creative talents. Not only can they join squads occasionally, but they can optimize their chapter-leader role in interesting ways. For example, if a company reconfigures squads frequently, reallocating talent to different roles or teams, the chapter leader might create and manage a backlog of "nice to have" functional work that his talent can help with in between their deployments.

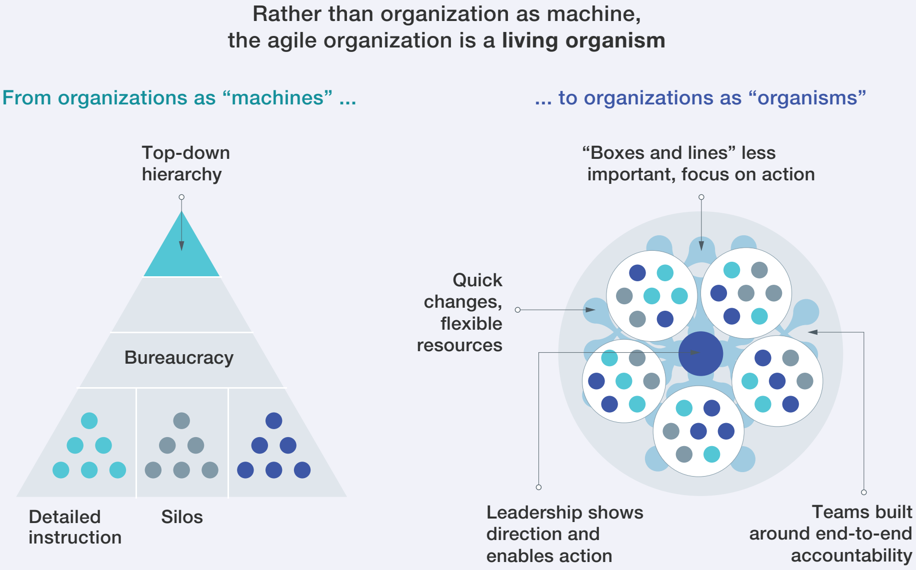
The tribe leader

Since these value-creation leaders borrow or rent most of their resources from the chapters, they no longer bear the burden of building up their own functional capabilities. Instead, tribe leaders act as true general managers, mini-CEOs focused on value creation, growth, and serving customers. They must develop the right strategies and tactics to deliver desired business outcomes and to determine what work needs to get done, how much to invest in which efforts, and how to prioritize opportunities. They work with chapter leaders to match the right people to the right squads.

Like chapter leaders, tribe leaders manage less and lead more. Since they have profit-and-loss accountability, they must develop a strategic perspective on their business and their customers, a cross-functional view of the core capabilities of the broader organization (so they can efficiently secure the resources they need from chapters), and an integrated perspective of the company as a whole and how their part of the business fits in with the larger enterprise. Those who succeed will develop more of a general-manager skill set and an enterprise mind-set that can break down

Exhibit

The agile organization is dawning as the new dominant organizational paradigm.



Mind-set shift 1: A strategic North Star embodied across the organization

From	To
In an environment of scarcity, we succeed by capturing value from competitors, customers, and suppliers for our shareholders.	Recognizing the abundance of opportunities and resources available to us, we succeed by cocreating value with and for all of our stakeholders.

Mind-set shift 2: A network of empowered teams

From	To
People need to be directed and managed, otherwise they won't know what to do—and they'll just look out for themselves. There will be chaos.	When given clear responsibility and authority, people will be highly engaged, will take care of each other, will figure out ingenious solutions, and will deliver exceptional results.

Mind-set shift 3: Rapid decision and learning cycles

From	To
To deliver the right outcome, the most senior and experienced individuals must define where we're going, the detailed plans needed to get there, and how to minimize risk along the way.	We live in a constantly evolving environment and cannot know exactly what the future holds. The best way to minimize risk and succeed is to embrace uncertainty and be the quickest and most productive in trying new things.

Mind-set shift 4: A dynamic people model that ignites passion

From	To
To achieve desired outcomes, leaders need to control and direct work by constantly specifying tasks and steering the work of employees.	Effective leaders empower employees to take full ownership, confident they will drive the organization toward fulfilling its purpose and vision.

Mind-set shift 5: Technology as enabler

From	To
Technology is a supporting capability that delivers specific services, platforms, or tools to the rest of the organization as defined by priorities, resourcing, and budget.	Technology is seamlessly integrated and core to every aspect of the organization as a means to unlock value and enable quick reactions to business and stakeholder needs.

silos, enable collaboration across organizational boundaries, and empower product owners to provide day-to-day guidance on objectives, priorities, and tasks.

The most difficult challenges for traditional managers tackling the tribe-leader role are letting go of the need to fully "own" all the people working for them, as well as shifting attention from micromanaging the day-to-day work to developing the right business strategies, setting the right objectives and priorities, and making the right business decisions. Tribe leaders must also wrestle with their reliance on getting their talent from chapters. They must resist the urge to build their own set of resources and create shadow functions so they never lack what they need when they need it. That end-around scuttles the agile matrix, which relies on healthy tensions and constructive conflict to get the right capabilities to the right opportunities at the right time.

The squad leader

Team leaders, or "squad" leaders, serve a crucial purpose in the agile matrix. They aren't the "boss" of the people on their team. They help plan and orchestrate execution of the work, and they strive to build a cohesive team. They also provide inspiration, coaching, and feedback to team members, report back on progress to tribe leaders, and give input on people development and performance to relevant chapter leaders. Think of squad leaders as individual contributors who have developed leadership skills or at least developed an interest in learning these skills. The squad-leader role can be more or less formal and can even change over time depending on what the team is working on. Once again, the challenge for someone from a more traditional company is to lead without exerting onerous control. But the rewards can be great. Some squad leaders will grow into tribe leaders, while others will continue as individual contributors with the additional skill of agile leadership.

Something old, something new

The idea of autonomous teams is not new; it's been around for decades. For instance, in the quality movement that took hold in manufacturing and continuous improvement 50 years ago, quality circles and high-performance work systems often relied on an autonomous self-managed team with an informal team leader who was not technically a boss. More recently, companies such as WL Gore (in materials science) and Haier (the Chinese appliance manufacturer) have emphasized the empowerment of small teams, even if they don't use the language we associate with agility—or focus those teams on software development, where agile has made some of its most prominent marks.

Today's agile organizations are building on these ideas (for more on the shift underway, see sidebar, "The agile revolution"). The squad leader is now a part of an agile matrix, where the value-creation, or tribe, leaders provide constant direction and prioritization around where the value is, and the capability, or chapter, leaders focus on ensuring deep functional expertise, common tools and competencies, and economies of scale and skill. If these leaders can become effective, nonintrusive managers, the agile company will enjoy the best of both worlds: the benefits of size and scale typically realized in large organizations, as well as the benefits of speed and nimbleness often associated with small entrepreneurial start-ups.

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Busting a digital myth: The naturally gifted product owner

Digital blog, June 8, 2018 | By Santiago Comella-Dorda, Christopher Paquette, Lois Schonberger, and Suman Thareja

Every great sports movie has the "preparation" scene: Exercising, training, equipping, running uphill in the snow, waxing the car, shooting countless basketball free throws in an empty gym. The stars know they won't be successful without the disciplined reps, and when the time comes, they succeed because they've put in the time and work.

While there isn't likely to be a movie with a product owner (PO) as the hero anytime soon, the best of them have a lot in common with an elite athlete. A great PO is committed to spending time in the development "gym": learning new hard skills, practicing softer leadership skills, internalizing a passion for the role, being observed and coached by expert peers, scanning the market for the next innovation, and applying these learnings in real life. This new breed of PO is a must-have for companies that want to be truly digital. The speed, adaptability, and cross-channel nature of digital require a PO who brings those skills.

Googling "how to be a great digital product owner" doesn't cut it, given the gravity of their accountabilities. They must be the "linchpins" between the product-creation teams (including disciplines like digital, analytics, and operations) and the business. They must be the key decision maker who guides the product roadmap. Why are these skills so hard to master and apply?

1. **They need to do a lot of things well.** PO responsibilities span a dynamic spectrum of hard and soft skills, and require a constant balance between strategic business goals and complex tactical objectives. They are the voice of the customer, but also play a critical and embedded decision-making role within their team. They must be leaders, counselors, innovators, and customer advocates. They need to understand the latest practices in customer research, design thinking, business strategy, and technical architecture, and wrap it all in a bow of composure while they make decisions under fire that influence key stakeholders. Strong problem-solving and leadership intrinsics are a great start but insufficient for the long game.

2. **They need to work well with a broad array of people.** By necessity, POs must interact from top to bottom of the organization and across multiple functions, as well as externally. They must seamlessly transition from discussing business results with senior executives, to driving the technical "art of the possible" with the front-line development team, to problem-solving product strategy with marketing leadership, to working with end users to validate new feature concepts through prototypes and testing. They must evaluate options from multiple viewpoints and know how to speak the language of various parts of the business to be able to influence people and guide good decision making.

3. **It takes time to develop these skills.** In the heat of the moment, decisions are made quickly, and the best POs seem to make them instinctively. Solutions to common problems such as how to rope in a passionate executive, which customer feedback to prioritize, what constitutes a minimum viable product (MVP), or how to untangle a complex feature, seem to come easily to the practiced PO. But this ease under pressure doesn't come without practice. Malcolm Gladwell and his 10,000 hours would confirm that, much like an athlete making a free throw or a penalty kick, great POs must develop a kind of "muscle memory" to guide their toughest choices. While the exact circumstances will vary, many of the challenges to successful product delivery follow patterns that can be recognized or even predicted.

So, if this is more “nurture” than “nature,” and if being a great PO takes focus and structured learning, practice and repetitions, plus time and coaching, then how do the best organizations nurture their product owners?

- **Build foundational strength.** Athletes hit the right weights in the right way to exercise the right muscles for their sport. They build up their baseline for cardio activity to be able to perform when they must. Great POs in the making hit “building block” educational materials, such as how to write great user stories, how to manage a backlog, and how to manage stakeholder conflict. They work with others to practice these foundations both in formal and informal learning environments.

- **Learn the playbook.** Athletes practice the plays that will matter over and over—serves, free throws, penalty kicks, and field goals. Great POs in the making rehearse for the moments that matter, such as managing stakeholder conflict, over and over again in a safe setting.

- **Game plan as a team.** Athletes know their game plan—who will do what, when, where, and how—and they practice the game plan together. Great POs in the making are just as diligent in practicing what it takes to develop a good game plan and, using simulations, working through them with their teams.

- **Embrace their trainer’s advice.** Athletes rely on their coaches to get them to the next level. Good coaches hold up a mirror and provide perspective. Great POs in the making also have support: agile coaches, mentors, and sponsors in their organizations. These coaches observe, provide feedback, and push the POs to be better every day.

- **Prepare, prepare again, and then keep preparing.** The best athletes squeeze practice into every possible moment, finding creative ways to get better whenever they can. Great POs in the making ensure that every minute counts. They absorb bite-size content, review the latest industry thinking on their mobile, and embrace “nudge” techniques for real-time behavior change, such as “How are you helping your stakeholders balance the hard choices between features?”

Not investing in this level of capability building can be costly. For example, a product team in the hospitality industry spent two years and $30 million building a reception-desk tool for all their locations. Rollout revealed that the product owners designed what they thought the “customers” (front-desk agents) wanted. But the customers didn’t value the features and didn’t appreciate the poorly designed experience. The tool was scrapped. The product owners had not been trained to engage with the customers to test ideas properly, and they didn’t understand how to navigate and prioritize the demands of disparate stakeholders (desk agents, hotel managers, corporate, and technology).

So, over the course of the next 16 weeks, they went back to the drawing board, with an eye to improving product ownership. Coaches were embedded with the product team and began a structured program of formal training, one-on-one coaching, and in-field pairing. They learned customer experience, effective user testing, creative prototyping, feature prioritization, and stakeholder management. The tool was relaunched just months later. This time, customers were receptive, and—most importantly—the product owners had developed the skills to be successful the first time.

Greatness as a PO is an investment, but it's worth it. Product owners are the linchpins between business and technology, and a critical foundation for a successful digital transformation.

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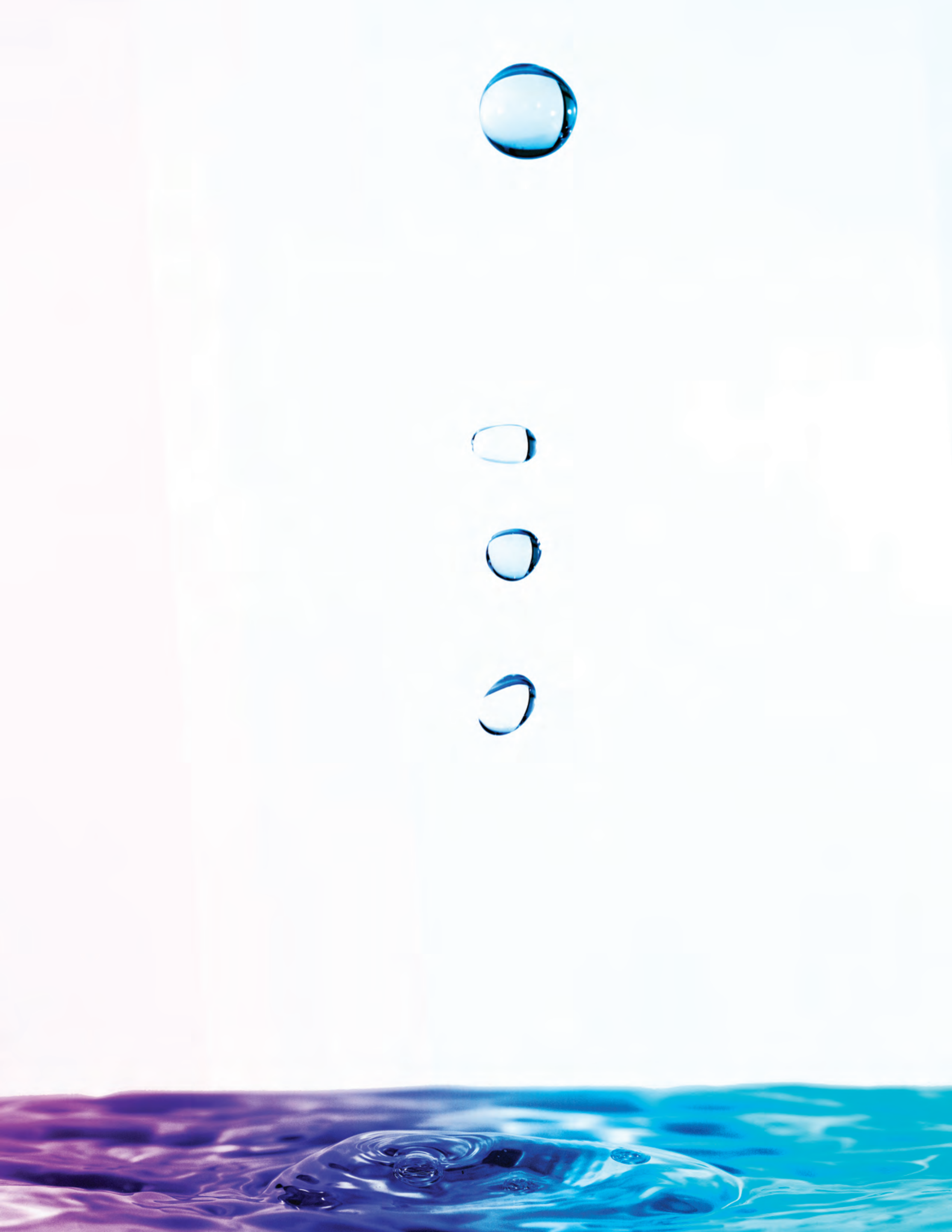

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Executive voices

Digging deep for organizational innovation

Interview, *McKinsey Quarterly,* April 2018

Organizational simplicity. Clear accountabilities. Nimble planning processes. All characterize a scrappy oil and gas company you may not have heard of. Learn more from its CEO.

Greg Lalicker

Greg Lalicker is CEO of Hilcorp Energy, where he has been since 2006. Prior to that, he worked for McKinsey & Company and BHP Petroleum.

Greg graduated with a degree in petroleum engineering in 1982 from the University of Tulsa, and holds MBA and law degrees.

Innovative organizations come in all shapes and sizes. Consider Hilcorp Energy, a privately owned oil and gas company, founded in 1989. It has more than 1,800 employees and operates assets producing over 300,000 barrels of oil equivalent per day (boe/day), all located in the United States. For the last six years, Hilcorp has been named among the top 100 best places to work by Fortune magazine and the Great Place to Work Institute; it is the highest ranked player in its sector on such lists.

What's more, as CEO Greg Lalicker describes in this interview with McKinsey's Peter Lambert, Hilcorp began embracing agile practices long before they were buzzwords, has put in place an innovative compensation system emphasizing fairness and shared rewards, and is comfortable that only half of the goals emerging from its planning process will be met. Hilcorp's approach to strategy and the unique culture it has built since its founding by owner Jeff Hildebrand are thought provoking for leaders in any industry.

The *Quarterly:* Before we talk about your organization, can you give us a quick overview of your strategy, so we have that as context?

Greg Lalicker: Yes, our strategy is very simple: acquire large, complicated assets late in their productive life and maximize their value through the efforts of our asset teams. This strategy means we have to operate differently from the previous owners to change the trajectory and profitability of these assets; and we are able to do that because of both how we think and work.

The *Quarterly:* Can you say something about the mind-set that enables this different way of working?

Greg Lalicker: I like to think of the business as a dog with a tail. The dog represents all the main sources of value creation at Hilcorp—the actual oil and gas fields and the asset teams working them every day, especially those people in the field who are closest to the wellhead. Everyone else is the tail, and it's their job to help the asset teams succeed, including the management team. Our simple precept is that the tail should never wag the dog.

The *Quarterly:* How do you make sure the tail doesn't wag the dog?

Greg Lalicker: There are four practices that we insist on, all wrapped in the idea that we want to build multidisciplinary asset teams that have the necessary autonomy and the accountability for creating value from our assets.

The *Quarterly:* That sounds like what we might describe as an agile organization.

Greg Lalicker: We didn't have agile in mind when we designed the organization, but we did want an entrepreneurial organization with clear accountabilities, a focus on value, and the ability to act quickly. Some of our practices—and I will set them out for you—probably are those of agile operations, but that wasn't our starting point. Some may say they are unusual, but we have proved they work. And I believe they are also widely applicable beyond the oil and gas sector.

There are four practices: The first is our commitment to a flat organization. We have a rule that the business will never have more than five layers above any employee, and preferably fewer: executive, asset leader, operations manager, foreman, operator. By limiting the number of layers, we can get things done faster. The mantra is: *every layer is time.*

Look at it this way: ExxonMobil is probably the world's best-run oil company, and it has an incredible track record of executing very large, very complex new developments every year. It creates value by making a small number of big decisions each year and then executing to a high standard. But Hilcorp creates value in a different way: we are trying to extract the last bits of value from a mature asset, and therefore we need to make 10,000 little decisions well each year. To do so, we push these decisions as close to the front line as is practical. Delegate down. The employees who often experience the biggest change in their working life when we acquire an asset are the foremen. Typically, their role previously has been to execute instructions conveyed to them by someone in the office. At Hilcorp, their job is to figure out what needs to be done and to make it happen.

The *Quarterly:* You mentioned reducing the layers of management. This relates to people. So, how and where are decisions made?

Greg Lalicker: This brings me to the second of our four practices; it's how we think about delegation. Our asset team leaders are the key decision makers. They are accountable for the success of the team and are given considerable autonomy in delivering the results.

The *Quarterly:* How big is a Hilcorp asset team? How is it constituted?

Greg Lalicker: Our asset model is built around cross-functional teams. A typical asset team has reservoir engineers, geologists, a geophysicist, operations engineers, and technicians in the office, all of them reporting directly to the asset team leader. One of the operations engineers is the operations manager, to whom the foremen in the field report. Reporting to these foremen are the field employees, such as operators and mechanics. The team is supported by a small number of operations assistants who work with the foreman to process all the—still inevitable—paper.

A typical asset team produces anywhere from 10,000 boe/day to 60,000 boe/day. We have a firm rule that an asset team can't get so big or so complicated as to require more layers of management—if it's so complex that it needs more layers, then we split the asset.

The *Quarterly:* Is there a typical profile for an asset team leader?

Greg Lalicker: Well, fundamentally, they are strong technical people who understand what it takes to grow both rate and reserves in oil and gas assets. They need personal and professional drive, an ability to delegate, good people skills, and, occasionally, a thick skin. Asset team leaders should never be satisfied. They are the ones looking for new ways to add value to the asset. We find that asset team leaders are usually—but not invariably—homegrown within Hilcorp.

The *Quarterly:* How do these asset teams relate to the centralized functions?

Greg Lalicker: Again, everyone not in an asset team is there to support the teams. For example, the drilling group's primary reason to exist is not to drill wells, it is to help the asset teams make more money; and that is how they are evaluated. The same philosophy holds true for all the other centralized functions.

The *Quarterly:* How do you handle procurement?

Greg Lalicker: Actually, we have no procurement department—for us, it would be antithetical to speed and to accountability. Procurement departments can lock in a poor service provider for a small discount and then force the whole line to use it. That would be the tail wagging the dog.

Put it this way, we have over half the people in the company in the field making decisions. They decide whether to use existing spare parts from the yard or to go buy new. They shop around for the best deal they can get and decide what creates the most value for the company in the long term. That way they secure what we need and hold the vendors accountable.

The *Quarterly:* Great, so those pertain to the structure. How about the processes and the people? How does Hilcorp achieve alignment with so many people making decisions?

Greg Lalicker: Yes, the third practice is the way we align goals and incentives. We want it to be in everybody's best interest that Hilcorp succeeds and, when we do succeed, that everybody shares in the rewards equitably. This alignment helps motivate everyone making the 10,000 little decisions to do the right thing.

The *Quarterly:* Can you explain how this works in practice?

Greg Lalicker: OK, first let me take goals and give you an example. Hilcorp sets company-wide targets over a series of five-year periods, with incentives for all employees if Hilcorp achieves the goals. The effect is to ensure that everyone makes decisions in the interests of meeting those company-wide targets. From 2006 to 2011, for example, the target was to double the production rate from 40,000 boe/day to 80,000 boe/day, to double reserves from 125 million boe to 250 million boe, and to double the value of the business from $1 billion to $2 billion.

The *Quarterly:* And the link to incentives?

Greg Lalicker: When the 2011 goal was met, every employee got $50,000 to spend on a car—the same amount for everyone who was here the whole five years. Our 2011 to 2015 target was to reach 120,000 boe/day, 500 million boe, and $6 billion value, and the reward was $100,000 cash per employee. Now the latest target is 275,000 boe/day.

The reward will be the cash equivalent of one boe for every day a person was employed at Hilcorp during those five years. Depending on prices, that will come out to $50,000 to $75,000 for anyone who was employed for the entire five years. Operations people like the idea that the first barrel they produce each day is theirs—as long as the company meets its targets.

The *Quarterly:* Is that it, or are there other forms of alignment through incentives?

Greg Lalicker: Hilcorp pays annual bonuses linked to overall company performance—production rate, midstream income, reserves, and operating cost. The annual bonus payout is up to 60 percent of salary and is the same number for every employee—no team component, no individual component—one number for the entire organization. We also have a program that ensures that employees own a synthetic working interest in the fields: they get to effectively buy into the assets on the same basis that Hilcorp itself bought in.

On the other hand, we target our base compensation at Hilcorp to be roughly average for the relevant job market. It is only through achieving success that people can earn significantly more. Initially, some staff might take a cut in base pay, so they have to believe that the upside potential is real.

The *Quarterly:* I notice that incentives are linked to production, reserves, and value—but not safety . . .

Greg Lalicker: That's right. Safety is too important to be in the incentive program. Safety is a requirement, not an upside. If people aren't working hard to operate safely, then they are fired.

The *Quarterly:* What are the challenges in this model of incentives and compensation?

Greg Lalicker: One challenge we have to watch out for is the "free rider" problem [employees not pulling their weight but profiting from the company's performance]. It is pretty simple to deal with: our people are expected to succeed in their job, and if they don't, then we coach them and try to help them improve. If that doesn't work, we look to see if they could succeed someplace else in the company. And if they don't succeed there, then they are out.

The *Quarterly:* Does individual freedom and team autonomy come as a shock to new arrivals? How do you imbue the Hilcorp culture in new recruits?

Greg Lalicker: It often takes about two years before new staff fully gets how the company works. It can be a bit of a shock. It's hard for people to realize they have the freedom to do something until they see that people don't get chewed out for making reasonable mistakes. New employees usually need to see us set the plan, create the bonus program, and actually pay out before they fully believe in the model. Once they get it, most of them like it—our turnover for staff who have been here more than two years is extremely low.

The *Quarterly:* Is there a set of mandatory processes or rules for Hilcorp staff?

Greg Lalicker: Like any organization, we have rules in place. But the point here is that rules and process don't "drive the bus"; they are there to help, not to be restrictive.

Our core values are different from rules and are nonnegotiable. We have five: integrity, urgency, ownership, alignment, and innovation. We have an action attached to each, so integrity is "do the right thing," urgency is "act today, not tomorrow," and so forth. Our operating procedures are the way we apply those values, but if they ever come into conflict, the values win out.

Hilcorp's core values

Integrity
"Do the right thing"

Urgency
"Act today, not tomorrow"

Ownership
"Work like you own the company"

Alignment
"When Hilcorp wins, we all win"

Innovation
"Get better every day"

The *Quarterly:* What are the limits to this way of handling things?

Greg Lalicker: Great question. And this is the fourth of the four practices—just enough process and controls. Speed is essential. For example, we start the planning cycle with the asset teams in November, by December we have a bottom-up plan from the assets, and by end of December we will have a top-down plan informed by what we know from the assets. Our aim is for a P50 plan: half the time we should be above plan, and half below. Goals should be aggressive and only slightly unreasonable.

Any more detailed planning is a waste of time, because we know it will change. The plan is to provide inputs to annual targets for rate, reserves, and costs. This is where the asset team leaders are held to account for rate, reserves, and cost targets. But we aren't strict about individual line items; if they generate better ideas over the course of the year, they should pursue them.

The *Quarterly:* In other organizations, we have seen a tendency for management to intervene as soon as something goes wrong or deviates from a plan. How have you managed to maintain the culture and principles as Hilcorp has grown?

Greg Lalicker: Maintaining our entrepreneurial culture requires lots of personal energy, discipline, and tact at the top. It's easy to deal with an event via a rule or a standard, but then you end up killing entrepreneurship and accountability. The harder way is to develop good leaders and hold them accountable.

You have to leave the asset team leaders in control. If any of them brings a proposed drill well to me for approval, I will ask some tough questions to make sure they have done their homework. If I don't like it, I may say, "I wouldn't drill the well," and explain why, but it is the asset manager's decision. If I am convinced that they have done all the necessary work to properly evaluate the investment, I won't override their judgment.

Likewise, when an asset is off track, I expect the asset team leader to understand what is wrong and what they are going to do to make things better. I only want 20 percent of the conversation to be about what went wrong—80 percent should be about what they are going to do now to make it better.

My job is simply to offer help and hopefully give good advice to the asset teams. I'm not here to tell them what to do—they are the "dogs," after all.

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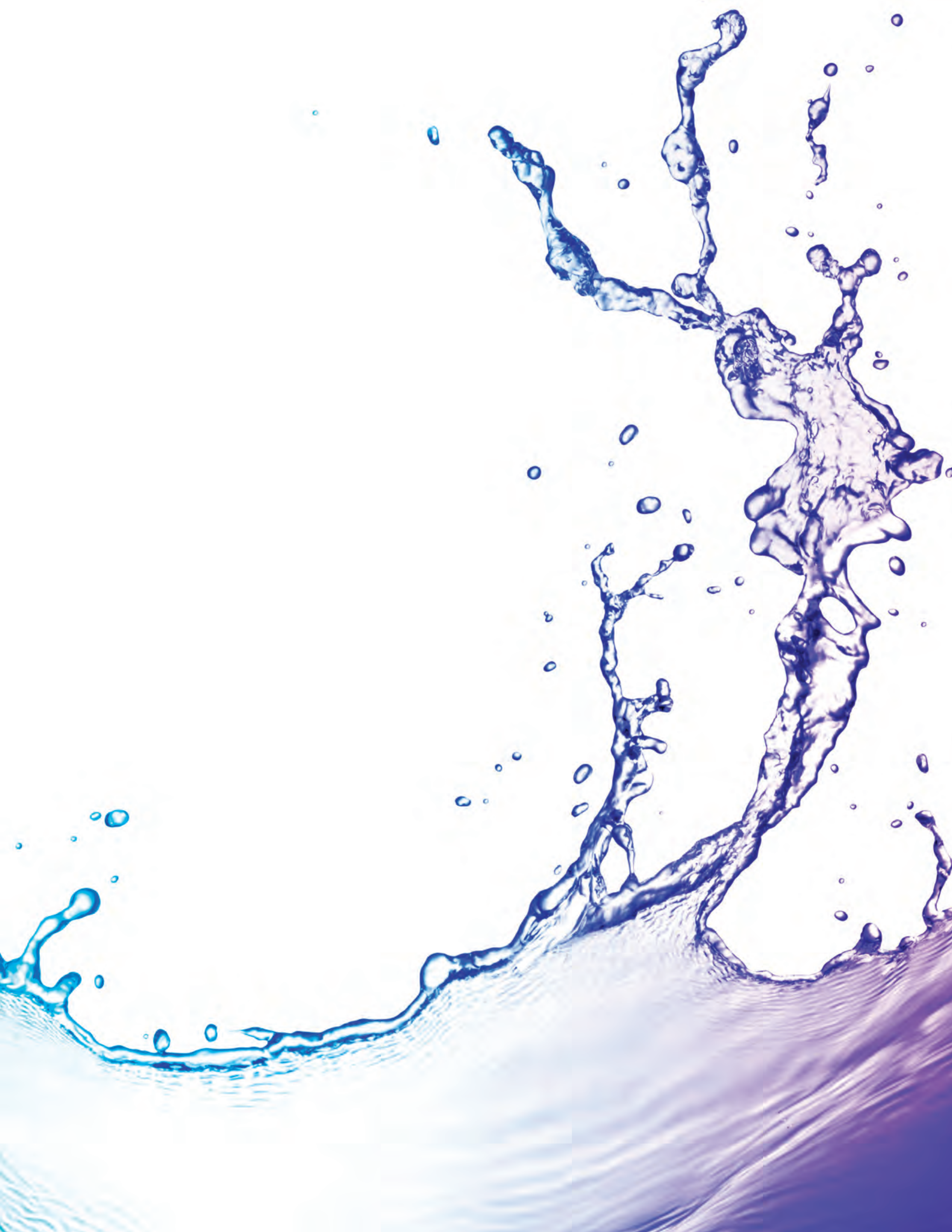
About the author(s)

Greg Lalicker is the CEO of Hilcorp Energy. This interview was conducted by **Peter Lambert**, a senior expert in McKinsey's Sydney office.



Safe enough to try: An interview with Zappos CEO Tony Hsieh

McKinsey Quarterly, October 2017

Organizations are more likely to innovate and thrive when they unleash the potential of individuals and the power of self-organizing teams, says the online retailer's CEO.

Tony Hsieh

Tony Hsieh cofounded LinkExchange, an online advertising network, in 1996 and sold the company to Microsoft in 1999 for $265 million. He began investing in the company that became Zappos in 1999, became the company's CEO in 2000, and sold Zappos to Amazon in 2009 for $1.2 billion. Tony established the Downtown Project, a $350 million effort to revitalize downtown Las Vegas near Zappos's corporate headquarters, in 2012.

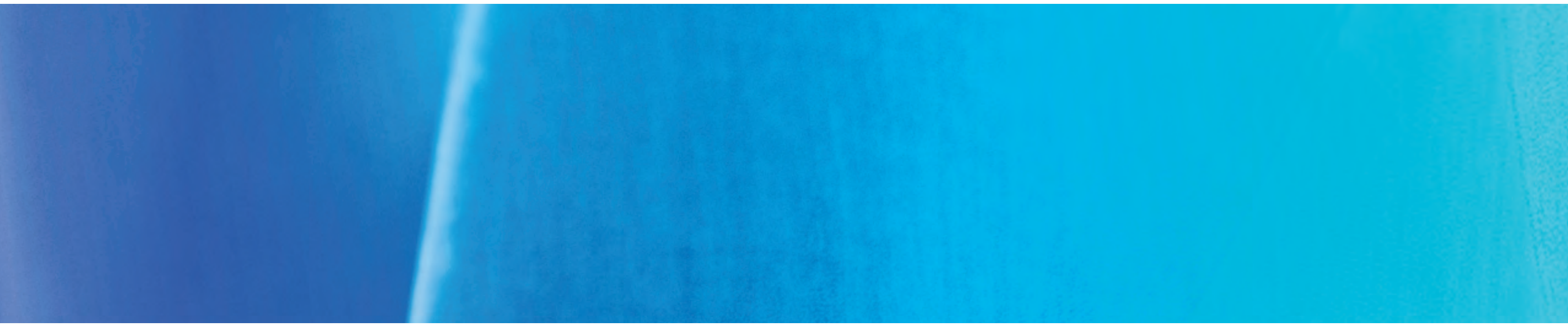
Tony holds an AB in computer science from Harvard University.

Tony Hsieh, the CEO of Zappos for more than 17 years, is not afraid to create "a little weirdness." In fact, that is among Zappos's core values. The company that got its start selling shoes online, became known for its near-fanatical devotion from customers, and was acquired in 2009 by Amazon has more recently been pushing the envelope in another area: its organization. Four years ago, Zappos kicked off its high-profile adoption of holacracy, an organizational model that distributes decision-making authority in self-organizing circles, made up of employees who hold roles (often more than one at a time) rather than job descriptions, with each circle arranged around a purpose statement. These experimental approaches, Hsieh hopes, will enable every employee to act as a "human sensor," and the organization as a whole to be more adaptable, innovative, and resilient. While Hsieh doesn't claim Zappos is an easily emulated model, the company has become a thought-provoking test bed for organizational ideas whose ultimate impact will become clearer in the future.

In May 2017, Hsieh sat down with McKinsey senior partners Aaron De Smet and Chris Gagnon to share his views on organizational values, purpose, and decision making; the importance of the individual; and the potential for self-organization to generate innovation. The interview, which took place on the Zappos corporate campus, in Las Vegas, Nevada, gave Hsieh an opportunity to get beyond the headlines as he described the philosophy behind Zappos's evolving organization.

The *Quarterly:* What does holacracy mean for Zappos?

Tony Hsieh: People can get caught up a little too much in the technical details of what holacracy is or what tools we're using. We've always encouraged employees to move around to find the intersection of what they are passionate about, what they are good at, and what adds value to the company, even in the "old days." For me personally, calling it "holacracy" was more a way of codifying or making explicit what was already implicit in our culture. We shouldn't have to be dependent on a benevolent manager or CEO to allow employees to move around within the organization,



because that's a single point of failure. Our org chart is available in real-time online and changes probably 50 times a day, and every one of our 1,500 employees can transparently view what every employee's purposes and accountabilities are. We have self-organized governance methods and meetings that happen on a regular basis, and it's all browsable and updateable online, along with, occasionally, policy updates—all of which enables any employee to contribute to the evolving structure of the organization. So it's not so much about "holacracy" as it is about "self-organization."

The *Quarterly:* If a company is self-organizing, and being dependent on a CEO can be considered a point of failure, how does the company keep its bearings?

Tony Hsieh: Imagine a greenhouse with lots of plants, and each plant represents an employee. Maybe at a typical company, the CEO is the tallest, strongest plant that the other plants aspire to one day become. That's not how I think of my role. Instead, I think of my role as the architect of the greenhouse, and to help figure out the right conditions within the greenhouse to enable all of the other plants to flourish and thrive.

Cities are another example of self-organization. Cities are the man-made organizations that have best stood the test of time. Cities last much longer than companies. Cities are resilient. Cities are adaptable. And cities aren't hierarchical the way most companies are. I read somewhere that all of Manhattan has literally three days of food supply. But there's no central food planner for Manhattan. Instead, you've got consumers and businesses "selfishly" consuming food in a self-organized manner, which creates opportunities for suppliers and so on. And that self-organized system works if there is a natural disaster; a bridge can go out and Manhattan still doesn't run out of food.

Not only do cities stand the test of time, there's plenty of evidence they actually scale in terms of productivity and innovation. One interesting statistic is that whenever the size of a city doubles, innovation or productivity per resident increases 15 percent. But in companies you get the opposite effect. As companies get bigger, they usually get more bureaucratic and less innovative per employee.

The mayor of a city doesn't tell its residents what to do or where to live; there is a certain infrastructure that a city must provide, such as the grid: water, power, and sewage. And there are certain basic laws that a city enforces. But for the most part, what happens when a city grows and innovates is a result of the self-organization that happens with a city's residents, businesses, and other organizations.

The *Quarterly:* What are the key principles of Zappos?

Tony Hsieh: The way I think about it, there are three different pillars, or dimensions, that are foundational to us at Zappos. And we need to make sure that all are working well.

The first is culture and values. Now, we're not saying that other companies should adopt our values. One of the interesting things I've learned from the research is that it actually doesn't matter what your values are. What matters is that you have them and you commit to them and align the entire organization around them. That means you're willing to hire and fire based on them. Most large companies have things called core values or guiding principles and so on. But I think what employees find at those companies is that the principles read like PR statements. You see them on the company's website, and maybe on the lobby wall in reception, but then no one really pays attention to them.

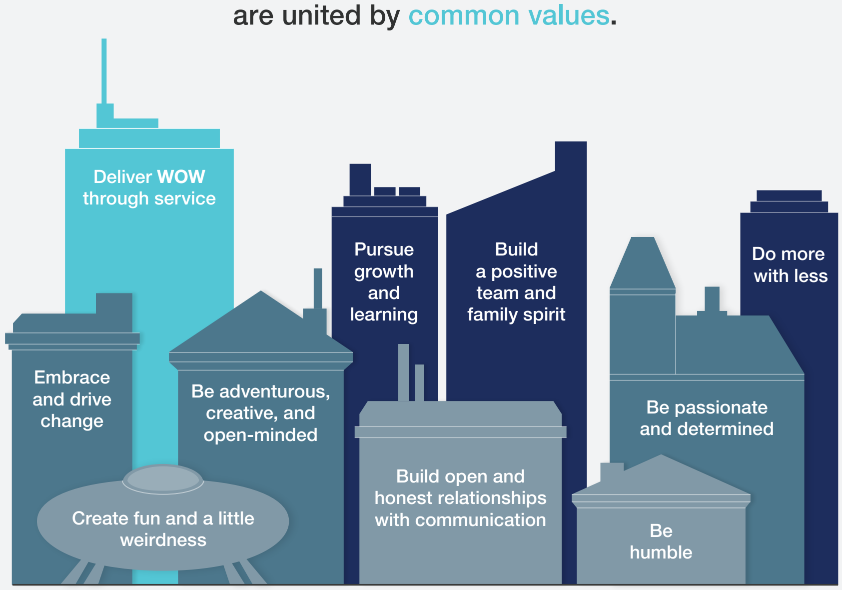
We have ten core values that serve as a formalized definition of our culture. And these ten were crowdsourced—I asked our employees what our values should be. Then we went back and forth for about a year and came up with our ten. They've become part of our culture. They're part of our employees' everyday language. Our core values actually just come up naturally in everyday conversation. And once they become part of the language, they become part of the mind-set. So that's our first pillar: values alignment.

The second pillar is purpose. Both on the individual level and on the organizational level, we are very explicit about purpose statements. And one of the things that holacracy enables is a hierarchy of purpose statements. There's the purpose of the company, which for us is "To Live and Deliver WOW." We have something we refer to as the general company circle [GCC]that holds the company purpose statement. And within that circle, there are subcircles and roles, and we cascade down from there into a hierarchy of more subcircles and roles. But you can pick any role anywhere in the hierarchy, and there's an entire set of purpose statements that all link ultimately back up to the company purpose. The purpose statements are something that we do think about occasionally, but I'd like us to get to the point where our purpose hierarchy is as top of mind as our core values. Right now, purpose statements aren't part of our everyday language, at least the way our core values are. I think that's a big opportunity for us.

The third pillar I'll call "market-based dynamics." Just like in a city, it's important to have a true market, to break up monopolies, and to have different internal teams become customers of each other. We're building an internal currency as well as the internal tools and systems to support an underlying infrastructure to allow for multiple participants, fast feedback loops, and things like crowdsourced participation. Imagine the equivalent of, say, the stock market, but for inventory purchasing. What if employees or teams could bet on inventory the same way people and organizations bet on the stock market in the real world today?

The Zappos ecosystem

Zappos strives to be like a city, where decentralized decision makers are united by common values.



The *Quarterly:* So you're trying to unleash the power of the organization as a market-based system, and also the potential of each person who makes up that market.

Tony Hsieh: Yes. One of the learnings we've had about self-organization and self-management is that it's not just a systems change; it's also a personal journey for each individual employee. Self-organization and self-management is about the entrepreneurial mind-set. A study was done several years ago that looked at what separated the great entrepreneurs from the mediocre ones. They found that the great entrepreneurs highly overindex for three characteristics: first, being comfortable with ambiguity; second, having a strong sense of curiosity; and third—not as high, but still overindexed—was emotional intelligence. And I think under self-organization, these three characteristics are even more important for us to hire for at Zappos.

A market is able to incorporate the intelligence of all the individual players and get feedback much faster than most other feedback mechanisms. I don't watch a lot of sports—except the Super Bowl—but even if I don't know who's playing, I do know that the sports-betting market, more than any other method that I'm aware of, does an amazing job of telling you what the right odds are. It does that by using the collective intelligence of the group.

To harness collective intelligence, we think of every single employee as a human sensor. Everyone senses different things, and you want a way to process all of that input. An airplane is one analogy. There are all of these different sensors. Some sensors, like the altimeter, are probably more important than others, but you want to be aware of all of them. Even if the altimeter looks fine, and most of the other sensors look fine, that doesn't mean it's OK to ignore the low-voltage warning light when it turns on. You don't allow the other sensors to outvote the low-voltage warning light and ignore it, yet the analogous thing happens all the time in organizations.

Some intern might say, "Hey, there's this Instagram thing we should pay attention to," but no one senior has heard of it, so the suggestion gets ignored. The structure that we have enables that intern—and basically all of our employees, if you think of them as human sensors—to actually do something about it, versus just getting outvoted. The idea is that everyone is a human sensor capable of sensing tensions, and it's important to note that a tension is not necessarily a bad thing. It's just the gap between the way things are and what's possible. Zappos is currently at 1,500 employees; everyone is able to actually sense tensions, and collectively our system is designed to process them. When you do that, you'll notice new tensions, and if everyone consistently does that, that's going to move the organization forward.

The *Quarterly:* How does this work in practice?

Tony Hsieh: In our organization, your tensions are based on the purpose statements for the roles that you hold or the circles you're in. And employees can belong to multiple circles. Our 1,500 employees right now are in about 500 circles, and if you want to be kept updated on what's going on in the circle meetings, you can subscribe to any of them, all of them, or just the ten or so circles that you're interested in. For example, let's say there's a circle that was originally focused on our campus, and the original purpose statement of the campus team was to have an amazing experience for employees. Then, someone else can bring up, "Well, as we've evolved over the years, we really want to be inclusive of the surrounding community as well." They can modify the purpose of the campus circle so that it's an amazing experience for employees, vendors, or someone else in our community, and that experience will help elevate the Zappos brand. And then, someone else can say, "Well, what about this other thing that you've forgotten?" So that can get added to the purpose statement or subtracted from it over time.

There are also elements that are similar to the Hollywood model. Certain people get more inspired working around other people and just kind of play off of each other's ideas. They work on projects, and then people who enjoyed working with each other decide to work together on the next project. And then, over time, what evolves is a dream team that works on the best movies.

The *Quarterly:* It sounds like a key element is tapping into the dynamics of how people work together.

Tony Hsieh: One term we use is "collisions." It's about how often you run into different, diverse people that you might have a random conversation with and ultimately end up collaborating with. We think about it in terms of density, as well.

Rapid reflections from Tony Hsieh

1. In your experience, what common leadership advice is misleading?

I think maybe the word "leadership" itself can be misleading, because it implies that there must be a certain structure—most likely hierarchical—and that the structure can only function if it is "led" . . . but in nature there are plenty of ecosystems and structures that are resilient and adapt and evolve that don't have leaders.

2. What do companies tend to get wrong about their customers?

That their customers think about their company or brand as much as they do . . . everyone is busy, including customers . . . there's a lot going on in their lives, and thinking about your company is probably not at the top of their daily to-do list.

3. What is a tech service or product—not yet invented—that you would love to see hit the market?

A replacement for email that's so much better than email that it causes everyone to abandon email.

The average density of office space in the US is about 300 square feet per employee—including hallways, conference rooms, et cetera. We're at about 100 square feet per employee here at Zappos, and the reason is because research has shown that if you sit twice as far away from someone in an office environment, you don't see them half as often—you see them half as often squared, so a quarter as often.

It's also important to understand that the best-performing teams are not created by simply putting together the best-performing individuals. Have you heard of the "super chicken" research? With chickens, you can measure productivity through how many eggs they lay. And so, in this study, Strategy One was to breed, say, ten chickens in a cage, find the best-producing ones, breed them for the next generation, and then see what happens six or seven generations down the line. And what they found was that at the end of the six or seven generations, Strategy One had these super, alpha chickens, and any one of them was an amazing producer. The problem is they killed half of the other chickens in the cage. And so, as a cage, they didn't produce as much as Strategy Two, which was to breed for the best-performing cage. Within that best-performing cage, there might be a chicken that maybe doesn't lay that many eggs but is the one that keeps the peace amongst all the other chickens. And if you're trying to maximize for overall productivity, you want to go for Strategy Two. But most big corporations go for Strategy One.

The *Quarterly:* In terms of corporate structure, what do you think you give up by optimizing for adaptability instead of predictability?

Tony Hsieh: There's a quote attributed to Charles Darwin—it may be misattributed—but it's something like, "It's not the fastest or strongest or most intelligent of species that survives. It's the one most adaptable to change." The world's moving faster and faster. Technology is enabling things to happen more and more quickly, and information flows much more quickly than it did 20 to 30 years ago. It's really going from a mind-set of, "How do we try to predict, plan, and control and execute on a specific plan?" to a mind-set that's more about, "How can we get fast feedback loops? How do we constantly sense and respond and build the organization around adaptability and resilience and longevity?" versus the more traditional mind-set of efficiency. Systems theory and research has shown that if you're maximizing for both efficiency and stability, usually that's at the cost of resilience. Resilience is harder to maximize for because it's harder to observe and measure compared to efficiency and/or stability.

It may be that, on a metalevel, what's less predictable is what our org chart is going to look like six months from now. But I don't know whether predictability is actually an advantage. I think that's how organizations get stuck, because they want that predictability of structure. But if it's the wrong structure, what's the benefit of being predictably wrong? The structure of the organization is a variable that affects the productivity and output of the organization. And most organizations aren't designed for changing their org structure in any efficient or easy way.

The *Quarterly:* Speaking of variables, your core business is very data- and analytics-enabled. How do data and analytics play into your organizational thinking? Do you use them to assess performance?

Tony Hsieh: It depends. We have a team that looks at data quite a bit. There are certain things where we know that if we spend, say, X dollars in paid advertising in this channel, we're going to get Y dollars in sales. So we should do more of that, as long as the ROI continues to make sense.

But you can't put everything in a metric. There are certain people that I get more inspired working with, where we just kind of play off of each other's ideas. I wouldn't even know how to put that into some sort of metric form that passes legal and HR.

We believe that employees are much more than just what their specific job description is. Maybe it's through volunteering at an event, or at the company all-hands meetings where an employee that's great at dancing can go do that even though that has nothing to do with their job description. But beyond just the hobby aspect, I think there's so much creative potential and intelligence that each individual employee has. We're trying to figure out how to create the best structure that releases as much of that as possible. Most structures just end up constraining, so you end up getting 10 percent of a person's potential versus, hopefully, close to 100 percent.

More than ten years ago, we made a commitment to our core values. Committing means we're actually willing to hire and fire people based on whether they're living the Zappos core values, completely independent of their actual job performance. Our hiring team interviews for the normal stuff, but then our HR recruiting team does a separate set of interviews purely for culture and values fit. Candidates have to pass both in order to be hired. We've passed on a lot of really smart, talented people that we know, in the short term, can make an immediate impact on our top or bottom line. But if they're not a fit for our values, then we won't hire them—and for that reason alone. It's the same thing for firing. If an employee is not living up to our values, even if they're the top salesperson or whatever, most companies would say, "Well, this guy is kind of a jerk, but, you know, we'll let it slide because he's bringing in the revenue." Whereas for us, it wouldn't even be a discussion.

The *Quarterly:* You seem very comfortable with the fact that you don't quite know where this ship is headed, that it's steering itself.

Tony Hsieh: We've all been brought up to believe that "If I do X, then Y is going to happen." But there are always unintended consequences. If you look at the great inventions, they emerge more from nonlinear ways of thinking. It's not, "Oh, I need to go invent X, and so all I have to do is steps one through ten, and then, all of a sudden, we come up with this random invention." I think people fool themselves into thinking things can be predicted and, therefore, controlled.

And so at Zappos, the bar is: Is it safe enough to try? It doesn't matter if other employees think it's a bad idea. I can take that input. But is it safe enough to try? At most companies, including us, historically, it ended up being more about consensus building—which is great when you're small. But consensus building doesn't scale. Self-organization, if done right, does scale.

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About the author(s)

Tony Hsieh is the CEO of Zappos. This interview was conducted by **Aaron De Smet,** a senior partner in McKinsey's Houston office, and **Chris Gagnon,** a senior partner in the New Jersey office.

How to go agile enterprise-wide: An interview with Scott Richardson

McKinsey Quarterly, August 2017

Successfully scaling agile starts with a strategy that's consistent from the front lines to the C-suite.

Adopting agile ways of working is easier said than done. It requires cultural change, well-balanced teams, and buy-in across the organization in order to succeed. Scott Richardson, chief data officer at Fannie Mae, shares his insights about going agile with McKinsey's Khushpreet Kaur.

McKinsey: What are some successful strategies that have worked to actually scale agile?

Scott Richardson: To start with, I recommend a central Agile CoE (center of excellence). Everyone brings their own flavor of agile to the table, and arbitrary differences can slow you down in the early days of a transformation. The CoE is useful in standardizing vocabulary, best practices, etc., to bring a useful level of consistency. Central seed funding is also helpful, as it's often necessary to bring in expert coaches to jumpstart the process, and most local groups don't have the means to fund their own coaches. The CoE can share the coaches across the organization until such time as the gains from effective agile practices can self-fund the program on a broader scale. The CoE also plays an essential role in establishing training programs and assessing organizational maturity with agile, and it can provide important guidance on more substantial changes, such as revising an existing SDLC (systems development life cycle).

I like the approach of starting small—one to three teams, with the right leaders and people— because this allows you to focus your energies on getting it right. It's very important that the early teams are successful, because they become beacons that attract others and prove that it can work here. Also, with the early teams you will encounter difficult organizational issues, and it's important to overcome many of them early on, because subsequent teams won't fare well until you clear the big boulders from the road.

Another key to scaling is creating two communities of champions. At the lower to middle level, local champions can learn from each other's experiences and build off each other's energy and best practices. This is a very productive way to shift the local culture and encourage self-sufficiency in overcoming hurdles. But you also need champions at the executive level. You need executives to promote it actively in their areas. This is what ultimately moves the late adopters.

One simple technique for creating executive champions is for the CIO or other top executive to track one simple metric: the number of agile teams per division or business unit. You'll find that if a C-level executive reports on this in the monthly business review, it won't be long before the divisional or business unit leaders naturally compete to have the most agile teams. That kind of productive peer pressure creates a real incentive to drive change.

McKinsey: Who needs to drive an agile transformation?

Scott Richardson: There is debate in the industry about whether you're better off driving an agile transformation from the bottom-up (activity on the front lines) or from the top-down (upper management steers the process). I've always found that both are required.

Bottom up requires local leadership on the ground and teams that are forward-leaning and energetic. But that will only get you so far, because ultimately they will run into the broader constraints that exist within the rest of the organization, which are beyond their ability to change. And people won't overtly oppose an agile program, but you'll frequently encounter passive opposition, especially in the middle ranks.

To work through this, you absolutely need top-down support at the highest levels to achieve broad and lasting change. This often doesn't require much more than a public endorsement at first. Then as you begin to scale, the continued clear, public, top-level support creates an environment where agile is allowed, encouraged, and inescapable.

McKinsey: How did you select your early agile teams?

Scott Richardson: Creating a new team is probably the most important thing managers can do, so make sure you get it right. When we created our initial agile teams, I was personally involved with structuring them and selecting team members. It might sound crazy to get so involved in this level of detail, but it is critical that the early teams become true beacons for success.

I led the management team through a series of discussions about the team's business objectives, scope of work, and what cross-functional skills were needed. We chose people with the right mix of skills, seniority, attitude, etc. We created teams that were set up for success. By the fourth or fifth team, my direct reports knew what questions to ask and how to structure a proper team, and they could scale up on their own from that point forward.

I've seen environments where teams were formed based on whoever was available or was on the last waterfall project, and most often it didn't lead to success. The teams had to be reshaped within a couple of months.

As a leader, it's important to model the right behaviors early on as well, such as paying attention to what's important, ceding authority and responsibility to those doing the work, teaching people to be self-sufficient, and stepping out and letting go from there. But being active in the early days is very important.

McKinsey: How do you drive cultural change in an organization?

Scott Richardson: Culture isn't something you can change directly—you can only impact it indirectly; it's the result of process and behavior change. For example, as you scale your use of agile, you'll hit crisis points, and your response in these moments can have a great impact on the culture.

It's human nature in these crisis moments for people to do what they've done before, which often isn't the agile way. And it's in those moments of crisis that a leader can step in and help them find the right way through the problem. When the next crisis arrives, they will have new methods and behaviors that reinforce the target culture rather than undermine it.

I remember a moment in the early days of our transformation when, during cross-team planning, several teams realized they were not able to deliver some really important capabilities within the desired timeline. This was a huge, highly visible timeline, so people were panicking. Some of my very best new agile team leaders offered to throw more people at the problem "just this once," to crash the schedule like they did in the old days. They sensed this wasn't the right answer and invited me to step in and give the blessing to their proposal or suggest something else.

It's in those moments that you need to model confidence in the agile method, to be the calm in the eye of the storm, and say, "No, what you need is to go back to your product owners, who are managing the priorities and sequence of work, and say, 'This isn't working, so what are you going to do about it? This isn't a technology problem, this is a prioritization problem. What is the MVP (minimum viable product)?'" And sure enough, after some initial wringing of hands, when the product owners saw that what they wanted wasn't going to happen, they quickly identified a revised MVP that was achievable by taking a hard look at what was really needed, cutting out extraneous requirements and features, but that still delivered the core customer value. Within a couple of hours everything was back on track with planning, and ultimately all the teams delivered, and the external customer delivery was on time.

That story has become a part of our organization's lore now: "Remember that crisis and we ended up doing the right thing, the agile thing?" Now they carry this story with them, and they are empowered to solve problems and make decisions in truly productive ways. It's part of the culture.

McKinsey: How do you manage the various maturity levels of agile teams?

Scott Richardson: In any company I've ever worked for, we've always looked at external examples but then defined internally our own agile maturity matrix. Here at Fannie Mae, we have a four-stage maturity progression. We use quarterly or semi-annual independent assessments to determine how many teams are at level one, how many at level two and so on—this is another useful function of the Agile CoE. Understanding the maturity level of each team helps us make sure we are making the right decisions enterprise-wide and determine what further support is needed—for example, more training, more coaching, different managers, etc.—for each of the teams.

I find it useful to use a tool that provides very detailed and insightful team-maturity metrics. Although aggregate results are shared outside the team, the specifics are for the team only and provide really rich feedback across some 16 different dimensions. Having this level of assessment is important so teams can see where they should move forward, why it's good to move forward, and what benefits we get from moving forward. This all encourages team members to own their own growth; it's part of the culture we encourage.

McKinsey: What did you do to encourage your agile teams to focus on customers?

Scott Richardson: My current role here at Fannie Mae is a data role, which by definition is not a customer-facing function. But from my previous role at another firm, customer-centricity was central to the agile transformation. It's a huge shift. At that previous company we thought in terms of accounts, not people. And so the big transformation was to recognize that we are in a people business, that our customers are humans with their own personal journeys, and that we'd do well to obsess over how we could help them have a better human experience—which by the way wasn't always directly related to the business we thought we were in. But these adjacencies that created a better human experience for our customers became competitive differentiators for us.

To achieve all this we needed to change the structure, goals, and compensation and rewards for our front-line staff, and we infused the entire company with an obsession for the customer by explicitly changing the language we used for internal company dialog.

Although agile is a fabulous improvement over what we had, its various modes of implementation (e.g., Scrum) are not perfect. For example, product owners do not always have all the answers. Frequently they do not have better [customer] insights nor better ability to prioritize than any other team member. Where possible, a better approach is to have the teams interact directly with customers, for example to codesign products and services with them using design thinking. It's truly amazing the insights you can get, and the superior products you can build, when you use human-centered design like this. The insights from direct customer observation or cocreation are far superior to relying on customer-survey results or the opinions of our relationship-management staff.

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Bringing agile to IT infrastructure: ING Netherlands' agile transformation

June 2018

IT executives seldom associate agile with infrastructure. In this interview, the head of ING Netherlands' IT infrastructure function explains how his team carried out an agile transformation.

ING Netherlands, the Dutch bank within the global financial group, began introducing agile ways of working at its headquarters in June 2015. One year later, the bank extended the effort to a domain where agile methods are far less common: IT infrastructure and operations. The change increased the speed and stability of the bank's IT operations and generated substantial gains in efficiency and employee engagement. In this interview with McKinsey's Vito Di Leo, René Visser, leader of the IT infrastructure tribe at ING Netherlands, explains why the bank chose to bring agile to infrastructure, how it brought about the transformation, and how it worked through the challenges that it encountered along the way.

McKinsey: Why did ING Netherlands consider transforming its IT infrastructure organization?

René Visser: Within ING, both on the business side and in the application-delivery part of the house, agile practices were more common. The infrastructure part was lacking a bit of that movement and ending up with a lot of operational dependencies.

As soon as you'd deliver a new application, for instance, you'd reach out to infrastructure colleagues to put some virtualized infrastructure in place. And in each of the next steps—delivering your application and operating and maintaining it—there was a need to touch the infrastructure for whatever reason. Every effort meant reaching out to infrastructure teams, which resulted in a huge backlog of operational needs and service requests. That was basically the issue we had to solve.

Other parts of the IT function were contributing to this problem too. Application teams didn't always build applications that were easy to operate. So the infrastructure organization had to make extra efforts to prevent application failures.

McKinsey: How did the agile transformation address these issues?

René Visser: The agile transformation for infrastructure is twofold. On the one hand, it means delivering infrastructure as a product. Not only the core infrastructure but also the full range of means to operate it, so that application-development colleagues can do that autonomously, according to their own plans. On the other hand, it means changing the way we deliver the productized services. That comes back to coding—software development.

It's possible to do that, because our infrastructure organization mostly delivers software, not hardware, and we know agile methods work for software. From my time in application development, I had learned how to work in an agile way, and agile had become the predominant way of operating for our IT function outside of infrastructure. Aligning the working style of the infrastructure organization with the style of the rest of the IT organization makes a lot of sense.

We also knew that if we could enable the application teams to deploy applications and maintain the underlying infrastructure on their own, that would bring us much closer to a DevOps model and consequently accelerate cloud adoption, which are two core elements of our IT strategy.

McKinsey: Going into this transformation, your team had to know that it might be challenging.

René Visser: We expected that it would make some people uncomfortable. Infrastructure's mission would have to change from building and operating mostly custom solutions to creating tools for developers to deploy standardized infrastructure on their own. We had some engineering talent, but we knew that not everyone would have high-caliber skills or want to do engineering work. We also needed to shift people out of their functional silos and put them onto cross-functional teams.

The application side, the "consumers" of infrastructure, would have to adapt to a self-service approach. Although the application teams were DevOps teams by definition, many of them still needed to learn about operations for infrastructure.

McKinsey: How did you get people on board?

René Visser: We knew the change would not be easy, but we also knew that there would be many benefits for our employees. In the new structure, we would simplify processes, reduce handovers, and increase our contribution toward overall IT delivery and agility. Furthermore, the new organization and roles would open up new opportunities and career paths.

We spent the next few months engaging our employees in a regular and open way. I invited our infrastructure colleagues to talk to me by the coffee machine in our office. We held these "coffee corner" meetings one to two times per week. People asked me direct questions, and I answered them as honestly as I could. So many people came that sometimes we had to move the discussion into an open space to fit everyone.

I also spent a lot of time with leaders in application development to explain the new vision and get their views on it. They helped us decide what kinds of services infrastructure should deliver, and how they should be organized.

McKinsey: What happened next?

René Visser: We did a complete redesign of the infrastructure organization, covering every last team and role, based on two key changes. First, we moved from silo teams that worked on service requests to multidisciplinary engineering squads that created infrastructure products and services. For example, the Linux squad would engineer a compliant operating system image and the tools required for application teams to perform second-day operations. We also set up squads to create products for specialized infrastructure technologies such as a mainframe or data lake. Second, we moved from a broad range of specialized roles to a simplified set of engineering roles, about ten in total. We also don't have project, service, and business-relationship-management roles anymore. The most common roles are engineers, product owners, chapter leads, agile coaches, and architects. These two changes made the target organization much simpler and slimmer than the one we had until then.

McKinsey: How did the infrastructure leaders select the right talent for each role and squad?

René Visser: We asked everyone to apply for up to three roles in the new organization, and then we put a lot of effort into assessing people. That's the standard reorganization approach at ING Netherlands.

We determined that, because we will be delivering a new product, we would also need people to have a different attitude and software-engineering skills. We made that very explicit. We posted our new job profiles quite early in the process, and we opened them to everyone in the organization.

We also had a very strict process of assessing people's engineering skills and mind-sets—as we call it within ING, "Orange Code" behavior. We also gave people a coding test. All of that together gave us good insight into people's willingness and ability to succeed in the new organization.

Everyone also went through at least two interviews, one on technical know-how and one on agile mind-set and way of working. We did all this for hundreds of employees in just ten weeks, because we wanted to minimize the uncertainty for them.

McKinsey: That sounds like an enormous effort. Who was involved in carrying it out?

René Visser: Interviewing all the employees was indeed a lot of work, in fact more than we could handle. I ended up asking people from the application side to help with the interviews. Fortunately, I had spent most of my career at ING on the application side, so I had good relationships there, and enough people stepped up to help.

Involving application-team leaders in the interview process didn't only alleviate the burden of conducting the interviews. Bringing the two sides together in these interviews also allowed people to gain a much better sense of how they'd be working together in the future. That was at least as valuable, since we weren't just transforming the infrastructure organization but also the whole model for collaboration between development and infrastructure.

McKinsey: Once the redesign of the organization was complete and people were matched with new jobs, how was the new structure implemented?

René Visser: We came up with a creative way to bring the new squads together. Employees on the same squad got hats with the same color so that they could find one another and meet face-to-face. In one day, we switched from the old structure over to the new one. We also asked the new product owners to redesign the seating areas, so that interaction among the new squads could be encouraged where it would be most needed.

To ease the transition, we set up temporary teams that would fulfill service requests, so that the new squads would have time to automate our infrastructure services and build new tools for developers. Because the transition teams would become obsolete, we staffed them with external contractors so they could be phased out more easily. Since the launch of the new infrastructure organization in November 2016, we have reduced the transition teams by more than 50 percent.

McKinsey: What was the approach to getting the agile squads up and running?

René Visser: We kicked off the squads with boot camps. We assigned them a purpose at the outset, but then they refined their own purpose. And they also developed, with one another, the first product road maps and the first backlogs. Coaches were helping with that. Later on, to help the squads get in a rhythm, the coaches helped the squads with alignment to other squads as well as with personal coaching, helping them to achieve their new goals.

There was a lot of room for training. But the best way to learn is by doing it. At least, that was my own way of working. Just do it—don't be afraid to make a mistake. We will not freak out. But let's learn from every mistake and make it even better next time.

McKinsey: How have the infrastructure squads developed over time?

René Visser: We had all varieties. Some squads were doing really well from the start. Others were struggling with agile, not finding the right rhythm. But we were very persistent about how we wanted teams to go, and so we switched our agile coaches or tried approaching things from different angles. There was quite a lot of room and freedom for teams to find their own way. And after a year, most of the teams were in good shape.

Looking back, I think we should have tried to steer the squads toward the same working methods at the very beginning. The coaches had a lot of freedom to decide what sort of coaching each squad needed, and some worked more on things like individual communication or working styles. Some teams got comfortable with agile methods after half a year, while others were still figuring things out. So the leadership team made all the coaching efforts more consistent. We wanted squads to adopt DevOps and be more uniform in how they worked.

McKinsey: Did ING's application developers respond well to the new infrastructure model?

René Visser: Some infrastructure squads did a better job leading application-development teams to use the new self-service tools. The best squads tried to understand the situation that developers were in, then spent time explaining the tools they had built. Others just told development teams what tools were there and said they had no choice but to use them. That didn't go as well.

Overall, development teams accepted the self-service model quickly. It lets them work faster and with more flexibility. For example, our agile squads have created self-service tools for development teams to do infrastructure patching. Now those teams can apply patches when they want.

McKinsey: How has the agile transformation affected the resilience of the IT landscape?

René Visser: The application developers' job is to develop and deploy applications that perform well. Yet the responsibility for making applications run smoothly ended up with infrastructure. That allowed development teams not to worry whether applications were prone to failure. For instance, we might have had an application that would crash because of a two-millisecond infrastructure interruption. There's no way for infrastructure to prevent outages completely. But that's what was expected.

Now we've increased in stability. The biggest push was not only with the infrastructure part of the house but also with colleagues from application-delivery teams. It takes two to tango. We improved our IT resiliency quite a lot by acknowledging that we need each other. It's not only infrastructure that drives 24/7 availability. You also need a good application architecture.

Our CIO in the Netherlands, Peter Jacobs, has really helped to shift the balance. His message has been that if applications fail, then developers need to fix them. They can't just expect infrastructure to keep things from going wrong. In line with this principle, we made the application teams accountable for the support and stability of their applications and systematically reduced the centralized level-one and level-two support functions. Development teams got the message and made their applications more resilient. It took them only a couple of months. Now the entire IT landscape of ING Netherlands is more robust.

McKinsey: What other benefits has the organization realized?

René Visser: Our software-development teams now have the tools they need to operate infrastructure for their applications, and the responsibility to do so. That's very much like a cloud operating model. The transformation has allowed our development squads to gain experience managing infrastructure in that way, so the next steps of adopting cloud will become easier and more natural. From a technology perspective, we have also made strides to that end. For example, we made upgrades at the level of data center and connectivity to align our environment with the requirements of our cloud architecture.

The agile transformation also helped us to improve in most operational areas. We have significantly reduced planned outages, incidents caused by infrastructure, and weekend work. Now changes are normally done during working hours. We have become more efficient. With fewer people, we have increased delivery levels by shifting activities toward engineering and automation.

McKinsey: What would you recommend to others who are embarking on a similar transformation?

René Visser: Don't try to fix things on the infrastructure side only. You definitely need your colleagues on the application side of the house to help approach [the transformation] from end to end. Which means engaging them and benefitting from their feedback from early on as you define what you're going to design, and then bring them in the loop on what you're delivering. And take them with you when you have your first successes. For instance, making patches during the daytime will go against all kinds of traditional perspectives, so you should celebrate that kind of success.

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