Toward a Definition of Corporate Transformation

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WHAT IS CORPORATE TRANSFORMATION AND HOW CAN WE DEFINE A SUCCESSFUL ONE? THE AUTHORS PROPOSE A DEFINITION BASED ON behavioral changes throughout the organization and suggest a framework, built on their analysis of cases and interviews, for comparing transformations among firms.

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Recent articles and books have detailed how firms, in an effort to transform themselves, either succeed brilliantly or fail miserably. Academics and consultants have found a large audience for the lessons learned and techniques used at Xerox, Motorola, Ford, General Electric, British Airways, and AT&T, to mention a few. There is equal interest in the most troubled cases, as a *Fortune* cover story on dinosaurs — Sears, GM, and IBM — makes all too clear.[1]

In October 1992, we attended a Strategic Management Society conference entitled "Strategic Renaissance — The Transformation of Economic Enterprise," where presenters discussed everything from the challenges of introducing brand management, to implementing a merger, to a complete reengineering of business processes — all under the heading of transformation. With such a broad range of issues to solve, it is not surprising that the lessons often seemed either inconsistent or "all over the map." To add to the confusion, there were debates on whether some of the most cited cases like Ford and GE were, in fact, *successful* transformations.

In our opinion, a consensus on what transformation is will not emerge until it is better defined and given a framework so that firms facing similar issues and circumstances can make meaningful comparisons. Here we propose such a framework and use it to compare some of the best-known transformations. Our analysis is based on a review of dozens of transformation cases and interviews with senior managers, academics, and consultants. We have also relied on our own experiences working with some of the largest firms in Europe, many of whom are in the midst of transformation efforts.

While the goal of all transformations is to improve performance, many efforts to improve performance are not transformational. We propose that to qualify as a corporate transformation, a majority of individuals in an organization must change their behavior. Thus, for most employees, the difference is palpable. Industry after industry is discovering that new capabilities — global quality, continuous improvement, innovation, learning, networking — demand extensive changes in how work gets done, as employees are asked to think globally, cooperate with other units, challenge managers, and show sensitivity for customer needs.

In the mid-1980s, British Airways decided to differentiate itself by focusing on marketing and customer service. The employees had extensive training to change the way they performed their jobs. During the first two years, every employee and manager attended a "Customer First" seminar, followed by a program on managing people, which was initially offered only to senior managers. British Airways is now offering the fourth round of Cus-

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tomer First seminars to continually reinforce the firm's commitment to customer service.

Our definition of transformation highlights a distinguishing feature of all cases: creating behavioral change is a difficult and long-term process that requires management's concerted and persistent effort. It also creates a distinction between transformation and other changes, such as restructuring, in which a firm is reshaped by buying or selling businesses, increasing its level of debt, or changing the formal structure, without necessarily affecting the nature of managers' and employees' work.

When such a definition is applied, many changes that are regularly referred to as transformational are not. During the implementation of a merger, even a horizontal merger of equal-size partners, management's immediate task is to change the power structure, meld work processes, and create a new sense of identification, while rethinking how the firm competes is put on the back burner. Thus, four years after its creation and a long process of integration and operations improvement, SmithKline Beecham has begun to examine new ways of working to take full advantage of the firm's enhanced position in the industry. This process could very well transform the firm in a more fundamental, although less dramatic, way than the merger itself.

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Three Types of Transformations

The first step, of course, is to recognize that the firm is or will become uncompetitive. Sometimes the CEO senses the threat and sounds the alarm, as GE's Jack Welch did in the early 1980s. On occasion, management remains complacent until outside forces — the board of directors or the banks — push the need for dramatic change, as happened at Tenneco, General Motors, and Eastman Kodak.

Once the need for change is recognized, all change efforts in a large organization face a similar problem, namely, how to create a sense of urgency and overcome resistance to change. The dynamics of change have been well documented and much has been learned generally about techniques and interventions to create permanent changes.[2]

But, to a great extent, the lessons learned and techniques used depend on the specific target of the transformation effort. In analyzing dozens of cases, we find three processes that approach change in critically different ways. Each process seeks to create a significant improvement in firm performance by using different levers.

Improving Operations

The goal of the change process to improve operations is to achieve a quantum improvement in the firm's efficiency, often by reducing costs, improving quality and service, and reducing development time. Improvements are achieved by reengineering business processes, restructuring roles and responsibilities, and redefining performance standards and measurements. Typically, these changes require employees to work in teams, work across functions or other organizational boundaries, and play a larger role in identifying and resolving problems, while managers learn new skills, such as coaching and facilitating, and rely less on monitoring and controlling.

For many firms, improving operations is the cornerstone of their drive to regain competitiveness and the overarching theme for the transformation effort. At Xerox, quality became an overriding goal, an appropriate target for a firm involved in the design and manufacture of a complex technology on which millions depend every day. For British Airways, customer service was a critical theme in its service business. Ford faced the need to cut costs dramatically and improve the quality of its products. We do not mean that other strategic issues, such as geographical expansion or entry in new markets, were not important to these firms. But success weighed heavily on their ability to make dramatic improvements to their operations.

Reengineering, particularly when processes are redesigned across organizational boundaries, can provide a step change in performance in as little as one year. Employees may find they are working across organizational boundaries, not only in designing new processes, but also in executing them on a daily basis. Yet not every reengineering story is transformational. Those firms that merely eliminated layers and downsized operations often have made very few changes to the roles of those employees and managers who remain.

Strategic Transformation

The process of changing strategy seeks to regain a sustainable competitive advantage by redefining business objectives, creating new competences, and harnessing

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these capabilities to meet market opportunities. If an outdated strategy can be remade with a few strategic moves by top management, then transformation is not called for. But increasingly, CEOs find their ability to reshape with a few bold strokes is limited, as competitiveness depends on new competences, skills, and behavior that must be infused into the organization.

The course of strategic transformation can vary greatly, depending on when and how a new strategy is chosen and implemented. A strategic transformation can begin with a formal review and full debate of the strategic alternatives, followed by a clear decision on major issues. Through workshops, the debate can extend to many levels, allowing management to obtain useful input and create a shared commitment to action.

For other firms, strategic transformation takes place against a background of changing technology, shifting market demands, emerging standards, and aggressive competitors, making it extremely difficult and risky for management to decide quickly on a single course of action. Instead, management may begin by merely framing the firm's strategic intent, rather than its detailed strategy, and create a goal that is significantly beyond its current capabilities. At the same time, management identifies the core competences the firm must invest in to reach its goal.[3] While the choice of strategic intent and core competences provides a general direction, the role of middle managers is critical because they are responsible for creating initiatives and experiments and developing competences. Reaching clarity on the firm's strategy is therefore a gradual process between top and middle managers and is intertwined with the implementation of new capabilities.

The strategic answers for a company like IBM, for example, are not at all obvious. Its past formula for success, charging high prices and securing 70 percent profit margins from a customer base locked into proprietary systems, is no longer sustainable now that customers can switch to open systems. The search for other formulas that can generate comparable profit margins is likely to prove futile, except in limited niche markets. Which of IBM's many strengths will be relevant in the changing world of information technology? What advantages can be derived from its sheer size, market recognition, competencies, and (dwindling) financial resources? The only answers may be to try a variety of markets and approaches and only later to choose and dedicate resources to what works. In such circumstances, the strategic framing approach is clearly superior to classic strategic decision making.

What role should strategic vision play when a firm is in a period of decline? An exciting vision is important in motivating employees to accept change but can be effective only if top management, and the firm, have established some degree of credibility. IBM's CEO Louis Gerstner recently declared, "The last thing IBM needs now is a vision. What IBM needs right now is a series of very tough-minded, market-driven, highly effective strategies in each of its businesses."[4]

Whether a transformation is needed depends entirely on the roles the chosen strategy requires. As a firm's strategy shifts from a full product line to a narrow one, from a domestic to a global focus, from a centrally run global business to a set of strong domestic businesses with global coordination, from a technology-driven firm to one with a stronger customer focus, managers must learn new roles.

All strategic transformations face a similar set of challenges. The first is to convince managers and employees that change is needed. According to Peter Drucker, until managers begin to question existing business theory, fundamental change cannot occur.[5] The second challenge is to give managers the tools to think strategically. In many successful firms, managers have relied on the logic of past business theory and are not well trained in the strategic analysis needed to change course. Finally, even when a new business theory has been defined and agreed on, implementation can be difficult. It is often surprising to what extent managers' routines, habits, and reflexes are inextricably tied to the old formula, and much training, coaching, and time are needed to become adept.

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For employees, strategic shifts are often more threatening than other types of change. Long-time employees' experience, which was once greatly prized and rewarded, becomes irrelevant to the firm's success. An example is the large number of executives and employees who grew up in the era of mainframes and have suddenly become obsolete. While some competences can be developed in-house with training programs, firms often find it neces-

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sary to hire new employees or managers with the necessary skills and competences.

Strategic transformation is a more difficult, riskier, and longer transformation than operations improvement. There is no guarantee that a new strategy or set of competences will succeed, and the cost to make the shift can be enormous. Firms like Motorola and K mart have invested billions of dollars to reposition themselves against new competitors and develop new sources of competitive advantage. Given the costs and the risks, divestiture is a more attractive alternative for many diversified U.S. firms. But for IBM, Sears, and GM, strategic transformation offers the only real hope for survival.

Corporate Self-Renewal

Self-renewal creates the ability for a firm to anticipate and cope with change so that strategic and operational gaps do not develop. Self-renewal demands particular types of behavior — such as facing reality, setting high standards of performance, and accepting responsibility for results — by large numbers of managers and employees. To support these behaviors, firms often find it necessary to make a variety of organizational changes, such as stripping away unwieldy structures, eliminating bureaucracy, and speeding up decision processes.

> Corporate self-renewal must be encouraged during a period long enough to create a fundamental behavior change in the managerial ranks.

Several change programs, most notably the creation of a learning organization and continuous improvement programs, are designed to provide the firm with a capability for self-renewal. While some authors describe elements of the programs somewhat differently, for our purposes, they share a common goal of self-renewal and a central focus on behavioral change within the firm. They seek to create a new way of managing so that the firm is able to stay ahead of the competition.

In the much described transformation at GE, the central goal was to become a self-renewing organization by pushing managers to face reality, accept criticism, engage in open communication, make fast decisions, and accept responsibility for those decisions. Mastering these behaviors enabled GE managers to address strategic issues effectively and launch hundreds of projects to improve productivity throughout the firm. Focusing on management behavior rather than on strategy was appropriate in a firm like GE, where managers were well versed in the finer points of strategic thinking, competitors' analysis, and the virtues of strategic planning. For other firms, where the art of management is less well developed than at GE, pushing managers to behave differently must be accompanied by interventions and training to address specific strategic and operational issues.

What type of firms require corporate self-renewal? Among the firms that have had the most difficulty reacting to the need for change and implementing change during the past ten years are some of the household names of world industry — Philips, GM, Sears, and IBM — firms with long histories of success and dominant market positions. These firms have let an ever-increasing gap develop between actual and required competitiveness, until they were suddenly confronted with a performance crisis. For these firms, which suffer from what we call "success sclerosis," a transformation that closes the performance gap is not enough, and corporate self-renewal is required.

Firms suffering from success sclerosis have not adapted to a changing world, evidenced by their inefficient operations and outdated strategies. Thus, management must orchestrate a long and complex transformation that attacks self-renewal, operations, and strategy simultaneously. During a five- or ten-year effort, keeping attention focused on self-renewal can be an enormous challenge for management. As the firm begins to fix short-term operational and strategic issues, and performance improves, it is tempting to declare the battle won and lose the drive to institute the difficult behavioral changes required for self-renewal.

Differences in Transformations

Our definition of transformation, which places the emphasis on behavioral change, reinforces the similarity of management's challenge across transformation cases. At the same time, the typology we have presented is a reminder that not all transformations are the same. In practical terms, there are many differences in technique, interventions, and lessons for each of the three transformation processes we have described. While a comprehensive comparison is beyond the scope of this paper, we would like to highlight two important differences, the time to achieve results and the role of top management.

Achieving measurable results in operations improvement can take as little as six months; in two years, sig-

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nificant benefits can result from process redesign and shifts in roles and responsibilities. Strategic transformation can take longer, particularly when new skills and competences must be developed. Corporate self-renewal must be encouraged during a period long enough to create a fundamental behavior change in the managerial ranks. After twelve years, GE's Jack Welch expects the process to continue until the year 2000. Similarly, Sir Colin Marshall at British Airways argues that the pressure must be kept on for one generation of employees.

There are conflicting views on top management's role in a successful transformation. In our view, strategic transformation requires strong leadership from the top team, not always to decide on the strategy, but to set the direction, establish a process to resolve strategic issues, and begin the process of building new competences. Conflicts are inevitable when there are major shifts in strategy, as they imply shifts in the allocation of resources and in power between business units, functions, and key managers. Without leadership from the top to build a consensus and occasionally to resolve disputes, progress would be difficult. Similarly, if the CEO doesn't take responsibility and push for corporate self-renewal, it is unlikely that a grass-roots movement will spring up.

The debate on top management's role seems to be centered on operations improvement, which is a highly decentralized change process. Some authors emphasize the role of top management in any type of transformation,[6] while others do not view top managers as central to the transformation process.[7] According to Beer, Eisenstat, and Spector, "Task alignment, starting at the periphery and moving steadily toward the corporate core, is the most effective way to achieve enduring organizational change."[8] They cite instances where strong CEOs have played a counterproductive role in pushing for change by focusing on programmatic change and by relying too heavily on formal structures and systems to bring about behavioral changes.

In our view, top managers can play a unique and powerful role in ensuring the direction and progress of change, even for a decentralized change process such as operations improvement. They can raise performance targets, put leaders in key positions, and remove managers who pose an obstacle to change. For a firm facing strong competitive pressure, a severe financial crisis, or a fiercely dominant culture, there is not enough time for a grass-roots change effort, and stronger intervention from the top is required, not to enforce programmatic change, but to jump-start the change process at the unit level.

A comparison of Ford and GM as they struggled in the 1980s to regain their competitive positions illustrates the benefits of strong leadership. Beginning in the late 1970s, the top management of Ford, particularly Donald Petersen, became convinced that employee involvement (EI) was the key to regaining Ford's competitive position. For more than ten years, Petersen used his position as president and then CEO to push managers to embrace the new approach. By 1984, EI had become a way of life at Ford.

GM's top management, on the other hand, focused on technology rather than on organizational and cultural change to revitalize the company. Below the top level, there were many managers who were firm believers in the EI approach, and many experiments blossomed during this period, including NUMMI and Saturn. Still, EI has yet to become a companywide tenet as it has at Ford. Without a committed leader and pressure from the top to adopt a new approach, the experiments were not powerful enough to overcome the strong resistance of GM's culture. Given enough time, perhaps the bottom-up approach will take hold as new managers move up in the organization. But in today's competitive climate, firms like GM do not have the luxury of waiting.

What Is a Successful Transformation?

What then qualifies as true transformation, and how can we define a successful one? We argue that a successful transformation is one in which management has succeeded in institutionalizing the behavioral change required for long-term financial success. Success depends not only on management's skill in leading a change process, but also on how accurate the diagnosis is, which operational or strategic issues to attack, and whether the new behaviors are appropriate for achieving the firm's objectives.

Managers should be wary of making comparisons or drawing conclusions about the success or progress of a firm's transformation based simply on financial measures such as profit margins or stock price. First, the early stages of transformation are disruptive and can exacerbate declining performance for some time before internal changes take root. Second, numerous outside events can affect a firm's financial performance, so a decline is not necessarily a sign that the transformation has failed. Despite Ford's losses in recent years, there is evidence that the fundamental changes in place — employee involvement, quality first, and cross-functional teams — have had a positive impact on the firm's competitiveness.

Even the best-managed transformation may be accompanied by declining return on equity and lower stock

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valuation due to fundamental shifts and consolidation affecting the entire industry. Most notably, mainframe computer firms, defense contractors, and, more recently, pharmaceutical firms have faced a sea change in their industry structure that will have an adverse effect on performance, no matter what they try. What is required, of course, is for firms to focus on a difficult situation and eventually emerge in a better position than their competitors, given the new environment. In fact, an industrywide crisis highlights the importance of managing the transformation process, because some firms react quickly to the external forces, while others do not react until much later. Some recognize at the outset the need for new behaviors, while others rely on structural changes and strategic maneuvers to improve performance.

A successful transformation does not guarantee successful performance forever. There are too many other factors that affect a firm's long-term performance. There is no guarantee that Ford's next Taurus will be as popular or that GE will create the next breakthrough jet engine. But given the massive changes that have taken place in these firms, the odds are much improved. ◆

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