The work of leaders in a **lean management** enterprise

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in a **lean management**
enterprise

The continuous improvement leader:
Engaging people for a digital age

Lean management creates enormous value, but improvement that's truly continuous is often elusive. Innovation in fields such as digital and IT make it more urgent, achievable, and human.

Zachary Surak

Over the past two decades, the world has embraced lean-management thinking. What was once a set of ideas for building better cars now drives better work in general—and better results—in everything from the world's largest companies to a new generation of start-ups and in every sector from healthcare to IT to financial services to nonprofits. Lean transforms the entire organization, creating new forms of leadership, new ways of working together, and, above all, shared mind-sets and behavior that strengthen an organization's capabilities and performance.

Yet today's chronic state of upheaval, with disruption compounding disruption, means that even some of the most successful organizations find it harder to build on lean management's gains and instill the right beliefs and behavior more deeply. Momentum flags just as the challenges seem greatest. Digitization, automation, analytics, design thinking—all are competing for the attention of leaders in the constant search for new ways to improve customer experiences and transform how businesses generate value.

These new capabilities all matter. But to find the right combination, business leaders need every worker to be more engaged and productive than ever. And because few combinations will remain right for long, organizations will keep needing more engagement and more productivity. That makes the role of the leader even more critical in sustaining an environment where engagement can thrive.

A few organizations are therefore realizing what the phrase "continuous-improvement culture" really implies: the very practices that support continuous improvement must themselves improve continuously. What these leaders are called on to lead is a continuous-improvement system that's centered on people: the lean management system (exhibit).

Exhibit

The lean management system is articulated through four integrated disciplines.

Connecting strategy, goals, and meaningful purpose

Discovering better ways of working

Enabling people to lead and contribute to their fullest potential

Delivering value efficiently to the customer

The need to engage people

Fundamentally, organizations are fighting commoditization: faster innovation means that any competitive advantage solely from technical excellence is now more fleeting than ever.

Take product quality. Over the past few decades, the average number of defects in new automobiles has plummeted, despite dramatic increases in the product's complexity—to the point where the quality among many brands barely differs. Likewise, in the United States, customer-satisfaction gaps between the largest retail chains, food manufacturers, banks, and household-appliance makers are now quite small.

Instead, what increasingly matters is a whole range of human capabilities related to how companies communicate and work with customers. Recorded via smartphone, a single poor service encounter can now cause real reputational damage, amplified in social media to a potential audience in the hundreds of millions.

In this environment, lasting competitive advantage comes from the ability to learn faster, respond faster, and develop deeper ties to customers. Technologies will naturally play a crucial role. The McKinsey Global Institute estimates that at least 30 percent of the activities in about 60 percent of all occupations could be automated, potentially freeing up people for more valuable contributions.

But too often, organizations think that technology alone will get them out of a competitive hole. In focusing so intently on the latest algorithm or big data application or straight-through processing platform, corporate leaders easily lose sight of what the new techniques are supposed to do: help to serve clients more effectively, directly or indirectly. The new tools take on a life of their own, consuming time and talent for an impact that dissipates quickly.

By contrast, the most promising opportunities are revealing themselves to the organizations that best manage the human beings who shape, use, and revise the new capabilities every day. What enables these exceptional organizations to break through barriers that block so many others?

New value from lean management

What distinguishes these leaders is that they are not only redoubling their efforts with lean to create new operating models that deploy human skill with unmatched agility and responsiveness but also focusing on delivering value. As a result, such companies can respond to new problems in real time. Rather than wait for decisions to march up and down a bureaucratic citadel, teams of workers can rely on their own skills (and managerial support) to test and implement new solutions on their own.

Lean thinking informs every aspect of these organizations' work, from transforming customer journeys—the steps cumulatively involved in providing a service or product spanning multiple touchpoints and channels—to accelerating value creation as part of an enterprise strategy of adapting to the digital world. They're combining digital technologies and process-improvement capabilities in an integrated, sequenced way that drastically improves customer journeys and internal processes. The Dutch banking group ING, for example, uses lean principles to create new product experiences for customers, as well as an unusually flexible organizational model that constantly evolves.

Companies are further building upon a foundation of lean management by applying digital technologies to synchronize their strategies, activities, performance, and health. They're generating better data to drive the management system, with clear strategies and goals (and tight feedback loops) that cascade throughout the organization.

And they're building a more flexible, modular architecture for improvement. Commonwealth Bank of Australia, for example, has changed the way it structures change, so that people can adapt to it more quickly and deeply.

These same organizations are successfully realizing an even greater advance: they are making continuous improvement an enterprise-wide reality, including in business areas that traditionally haven't been seen as fertile ground for lean concepts because their operations do not resemble factories. Corporate business functions, such as HR, risk, and finance, are not only just as ripe for lean's rewards as any other group but can also multiply the benefits of lean by encoding it into the organization's governance and people processes. Moreover, these functions' constraints, such as a heavy reliance on experts, mean that their successes will open yet more areas for lean management to target—such as highly complex expert-led functions and businesses. In Chicago, for example, the international law firm Seyfarth Shaw fosters a deeper understanding of its clients by using lean to help traditionally siloed experts align with others.

Leaders building new leaders

But the most striking difference in these enterprises is the way that their leaders work—how they have changed the daily management of the business, from the routines they practice to the expectations they set with their people.

These leaders become not just role models but anchors keeping their organizations from being dragged back to old habits. As work with lean management starts to mature, they systematically transfer the scientific mind-set to other leaders across the enterprise. Their codifying and role modeling of crucial practices (such as "standard work)" help their companies develop people and sustain improvement and help the entire organization to keep pace.

But this means achieving a shared understanding of the purpose of lean work—with rigorous planning that outlines how the company will get there—to develop the behavior, leadership, and systems that help all employees learn from the work they do. Ultimately, it means positioning continuous improvement not as a thing to achieve, but as a way of thinking and working that becomes self-reinforcing.

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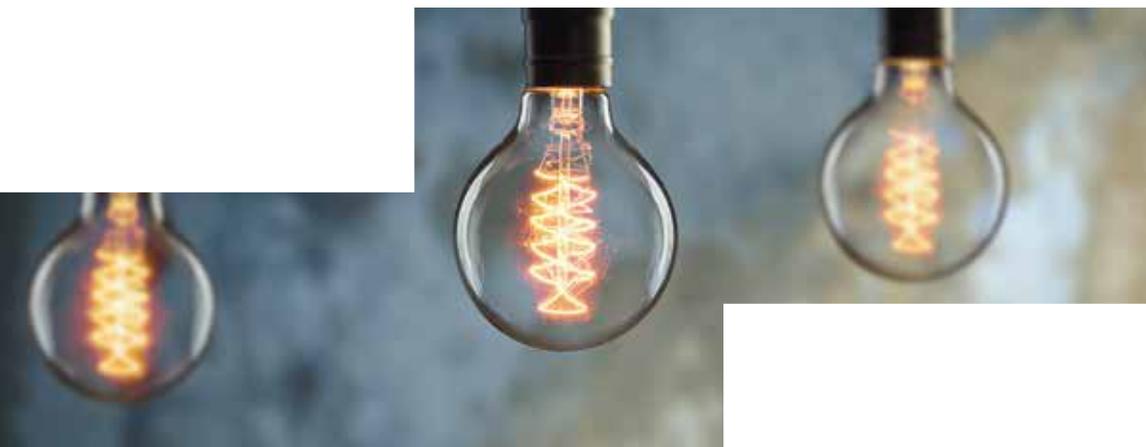
Exceptional lean companies win in the short term and thrive in the long term. This system of learning and continuous improvement becomes a virtuous cycle of more engaged workers coached by more capable managers whose more agile organizations can make more effective decisions. The complete lean management system gives any business the opportunity to face its toughest competitive pressures—to compete through learning—by building an agile, responsive, and adaptive enterprise focused on finding and attacking a wealth of new challenges. ∎

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Sustaining continuous improvement: Five leaders' views

We asked five executives with decades of experience in lean management about the most important lessons they learned in helping their organizations sustain continuous improvement.

Erin Ghelber, Ted Iverson, and Christian Johnson

The statistics are well known: only a small minority of transformations manage both to increase an organization's performance and sustain it over time. We therefore spoke with executives who have been using and thinking about lean-management concepts for many years across a wide range of industries, which together illustrate some of the potential that lean management offers when organizations commit to it both deeply and broadly across the enterprise.

The interviewees included:

Tom Hartman, who spent almost 20 years as a senior executive adapting lean management at global auto-safety-systems manufacturer Autoliv.

He is now an executive coach at Catalysis, a training and coaching organization for the health-care industry.

DJ Johnson, vice president for transformation at steelmaker Worthington Industries, is a former McKinsey consultant who spent 12 years as an officer in the United States Navy.

Gary Peterson, a member of the executive advisory board of the Shingo Institute, is executive vice president for supply chain and production at O.C. Tanner, a global employee recognition and engagement company that provides technology solutions and manufacturing capabilities.

Scott Powell, director of operational excellence at Export Development Canada (EDC), has been deeply involved since 2013 in EDC's transformation via lean management.

Rich Sheridan, cofounder and CEO of Menlo Innovations, a software design and development firm that pioneered many of the concepts of agile, collaborative software development.

They spoke with Erin Ghelber, Ted Iverson, and Christian Johnson from their respective offices, and their responses have been edited for publication.

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McKinsey: *Where would your organization be today without lean management?*

Gary Peterson: Without lean management, I suspect we would have become a distribution business, which would have taken away our most important differentiator: our ability to create custom products for our customers. I love it when international manufacturing leaders come to our facility and I see the look of disbelief in their eyes as they say, "You really are manufacturing in the United States!"

Scott Powell: It would be harder to innovate and be relevant for our customers. We would still be siloed, fragmented, taking much longer to get things done. We would have less humble, respectful leaders, employee satisfaction would not be as high, and it would be harder for us to innovate and be relevant for our customers.

DJ Johnson: I think we started to become complacent; our CEO likes to say that success is a mighty enemy. We had an intense focus on performance, on making data-driven decisions, and above all on overall equipment effectiveness (OEE). In time, I think, we started to lose sight of what

OEE is for, without considering the system as a whole. OEE could be great for a particular piece of equipment, but if the rest of the system can't absorb what that equipment is producing, you end up with piles of inventory. That's why we needed a broader perspective, one that would take us back to first principles in thinking about how we run our business.

Tom Hartman: Looking at my previous work, for Autoliv, it would have been very difficult to keep up with the demands of the automotive industry without a much deeper understanding of the principles of lean. Our technology was good, but the technology alone would not have been enough. In healthcare, we are still in the early days. The potential is huge: healthcare has a history of command-and-control leadership. In contrast, we are teaching them leadership techniques such as humble inquiry and respectful engagement.

Rich Sheridan: In our organization, we didn't fully realize that what we were doing was essentially lean management. We just saw a lot of problems accumulating in the software industry in the late 1990s. Software development had long been a story of individuals with amazing expertise, but Moore's Law—the doubling of transistors every two years in integrated circuits—made computers more capable; we had to go from individual heroes to teams. Yet across the industry, teams were still built on "towers of knowledge" that couldn't scale up or scale down, even in the middle of a society that was ever more dependent on software. Too often, IT didn't know how to communicate with customers or users. Instead, we blamed them. We wanted to fix that.

McKinsey: *What advice would you offer leaders who wonder what happens after the intensive transformation ends?*

> "The journey is a continuum. It's not about abandoning what came before, but constantly building, driving hundreds of thousands of small improvements at every level. That's the point of *kaizen*, of continuous improvement."

Tom Hartman: The journey is a continuum. It's not about abandoning what came before, but constantly building, driving hundreds of thousands of small improvements at every level. That's the point of *kaizen*, of continuous improvement.

Scott Powell: You'll hit walls. And you'll probably hit a plateau, too. You have to keep trying, and when something doesn't work, try something else—keep learning, keep improving.

Rich Sheridan: "Let's run the experiment" is one of our mottos. Some will fail, some will run for a while but eventually outlive their usefulness, and others become a permanent part of our process.

Gary Peterson: As a leader, you have to believe—and you have to help every single person in your organization believe—that you will never arrive. You never say "mission accomplished," even after the tipping point where the majority of people are driving lean themselves.

DJ Johnson: I'd say that you can't let the intensity end. When you feel it fade, that's when you have to change. You don't let off the gas pedal.

McKinsey: *What are the biggest challenges your organization has faced in adhering to lean ideas?*

DJ Johnson: Honestly, it's keeping people from reverting back to pre-lean-management ways.

Gary Peterson: No matter how good you get, you will have people who want to try to do things the old way, even if you've known for ten years that the old way doesn't work well.

DJ Johnson: One of the ways we try to combat that impulse is to avoid putting too much focus on "projects," or on *kaizen* "events" where there's a big push to demonstrate continuous improvement. Those are useful for helping people learn but over time, the big money comes from solving problems on a daily basis.

Scott Powell: It's easy to think that you are doing really well at this across the organization when in fact you may not be. A few years ago, we made that discovery when we asked the Shingo organization to assess our lean-management maturity. Our score was much lower than we expected. Initially that was hard to hear, but it meant we had a lot more opportunity waiting for us.

Tom Hartman: The biggest challenge is weathering the turbulence created by operating in the world of traditional leadership methods, while building the foundations and management systems of principle-based leadership that will make future challenges much more achievable and sustainable.

McKinsey: *How has lean management evolved over time, for you and your organization?*

DJ Johnson: Early on, we emphasized building a central team to guide our transformation. That was necessary but not enough; we needed to engage our employees more and have them working on continuous-improvement activities that people in the central team would not have the resources to lead.

Gary Peterson: That's true throughout the organization. As leaders, it's about relying less on your own decision making and more on helping other managers and executives develop their people.

Scott Powell: Development has been crucial for us. Since the Shingo assessment, our focus has been top-down at the enterprise level, among our executive team.

Tom Hartman: We started with tools and techniques like almost everyone but quickly moved on to a principle-based approach that was critical to building a culture of continuous improvement. This applied in all areas: product development, human resources, finance, supply chain, as well as operations.

McKinsey: *There's no question that senior-leadership engagement is crucial to sustaining lean management, but how do you best engage senior leaders?*

Tom Hartman: You start by recognizing that for most people in the C-suite, the idea that the greatest value they can contribute is by teaching and mentoring their people is not natural. Regardless of their background, whether they were engineers or MBAs or physicians, that's not the way they were trained.

DJ Johnson: We developed an executive immersion program for lean management, a two-week program in which senior leaders visit

other sites to see what their peers are achieving. But what matters more than seeing is doing, so the training culminates in a *kaizen* event. For capability building, these events are incredibly valuable because they provide a way for senior leaders to learn how to make continuous improvement happen. At a given location, we'll have the business-unit COO, the general manager, the operations manager, and the whole leadership team all participating and developing their skills at once.

McKinsey: *How do you make sure that it isn't a one-time exercise for them?*

DJ Johnson: We changed our performance reviews to incorporate lean-management behaviors, such as the impact achieved from problem solving in the area the executive or manager leads.

Scott Powell: We put a lot of effort into developing a strong core of coaches and support mechanisms to help deepen the sustainability of what we call the EDC Way. For example, the workplan of every employee—including our CEO and executive team—includes a performance measure that requires improvement in critical EDC Way indicators. One of the CEO's most important *hoshin kanri* (or policy-deployment) initiatives is to improve the culture through the EDC Way. Our strategy-creation tools require identification of essential lean management systems, and we have a senior executive–level annual development plan cycle for the EDC Way, which helps drive our systems forward year over year.

Tom Hartman: We emphasize that the C-suite must be constantly learning, which is important not only on its own but also because it implies a degree of humility—which is crucial to driving improvement and thinking at a higher level of performance. We ask executives the question, "How many times have you missed an opportunity to learn because you were blinded by your own knowledge?"

McKinsey: *That's a significant mind-set change to build into an organization. To what degree do you develop it from within, and to what degree do you bring in new talent?*

Scott Powell: To supplement our coaching and development-plan methods, we also build EDC Way capabilities into all leaders, as well as into important sustainability teams and associates. Also, it becomes easier as you build lean management into your approach to finding talent. I'd say that about 70 percent of our executives are promoted from within, and with generational rollover, that means about 70 percent were frontline leaders back when we started with lean management. At this point, our executive team has had enough experience in hiring lean leaders that we're pretty optimistic about supporting our culture.

Rich Sheridan: We were a new organization, which might seem easier, but one of our central challenges was overcoming the traditional culture of software development. The classic work setting is a cube farm, everyone listening to headphones, coding silently, often at weird hours. And yet, when the company releases a product to the world that makes no sense, leaders lament the serious communication problems in their engineering organizations.

My cofounder and I decided that it doesn't have to be that way. We don't do traditional interviews, which I think of as two people sitting across a table lying to each other. Instead, our process is immersive; we give people actual work and have them work together the way our employees do. That's how we find out whether people can succeed in our culture.

Gary Peterson: When we hire or promote a leader, we don't actually give them the job for three months. We give them a project in an area that's

unfamiliar to them and that cuts across the enterprise. They're expected to get big results, of course, but the really important thing is how well they follow lean-management behaviors. We design the assignment so that it comes with no authority: no one is obligated to help them. We watch how they perform, and give them intense training on the principles of lean management.

If in three months they don't quite make the cut, they either revert to their previous job and try again later or leave the company. That's how important it is for people to lead in the right way. We also do day-to-day connections, monthly coaching sessions, and semiannual review cycles that are all very clear on our expectations as to how individuals lead, how they develop their people, and how they reach out and help.

Tom Hartman: Whenever possible, it is better to promote from within, I think. Promoting those who are already immersed within your culture enables the organization to accelerate its primary mission, which is to unleash the creativity of its team members, thereby building a perpetual improvement machine. Hiring from outside is occasionally necessary, but each of these new team members must learn the delicate balance of distributed, empowered leadership.

McKinsey: *How do you make sure these behaviors reach the middle manager and frontline levels?*

Scott Powell: We zigged and zagged over the past ten years, initially starting in the middle and frontline levels, then really putting an emphasis from the top down. Now we're in a great position to reengage the middle and front line, because once the role modeling and alignment were strong enough at the top, we could move on to the rest of the organization. The knowledge training we offer at every level is now deeper, with stronger coaching

so that people can really integrate different streams of value together.

Tom Hartman: Autoliv also invested heavily in people, starting with the top leaders and moving progressively down the organization. The messages became more concrete and granular as we got closer to the factory floor. Over time, however, we realized that people becoming team leaders needed more than the tools-and-techniques training they had as operators. They needed to understand the reasons why the tools exist. That led us to develop a whole new type of capability building—a sort of Lean 201 that followed from Lean 101.

Gary Peterson: Rotating people is also essential, at every level. At O.C. Tanner, after three years on the job, you're due to be moved, almost always to a different value stream if you're a manager or above. Even frontline leaders get rotated within the same value stream. It's about supporting teams, not the personality and connections of a particular individual.

One of our managers was very good at running a particular system, so we didn't rotate her for five years. I was on a bus tour in Japan and mentioned how essential she was to a local executive. He looked confused, asking, "Don't you like her?" He wasn't moved by my argument. When I came home, we moved her. Her replacement picked up the role, refined it, and made improvements. Meanwhile, she's moved on yet again and is doing really well.

McKinsey: *What would you say is the most powerful effect that lean management has had for your organization?*

DJ Johnson: One of the biggest things we got out of lean management was capability building. We realized we couldn't rely on central offices all the time; we needed more from the shop floor. That changed our idea of what is possible.

Gary Peterson: Number one has to be the empowerment of our people. They've gone from basically sitting there, quietly doing what they're told, to doing real strategy implementation. On the other hand, when people hear our story, where I see the most disbelief is in the idea of trusting the power of your own people.

Scott Powell: Employee engagement was the first thing that came to my mind as well. Our mindsets have shifted—our whole approach to what we do has evolved—and we're using a common language to ensure we build capacity and greater relevance for our customers.

Rich Sheridan: Belief in our people—our teams— is what's enabled us to help change the way software is made, and the way people interact with software.

Tom Hartman: I would say that the key to building a culture of continuous improvement is respecting the capability of the people. One of the people who taught lean management at Autoliv used to walk the floor, see people doing the same thing every day, and ask, "Is this a people job or a dog job? If people aren't changing, they're doing work they're trained to do like dogs. Why don't you engage them every day so that this is a people job?" ∎

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What leaders do:
Integrate new technologies and approaches

In a lean management system, one of the essential responsibilities that leaders have is to serve as role models for finding new ways of working. The leaders' perspective lets them see improvement opportunities for the system as a whole, as well as the entire range of innovations that people are starting to apply both inside and outside the organization. A leader's task is to bring those insights together so that the system can keep improving.

In the current context, the most obvious source of innovation would appear to be technology. Indeed, the digital revolution—the intersection of connectivity, data, analytics, and mobility that has fueled so much of the last decade's growth—is already leading to breakthroughs in how organizations work. The authors of "Transforming operations management for a digital world" (p. 18), for example, find that digital and lean reinforce one another in powerful and unexpected ways. The conversation in "ING's agile transformation" (p. 22), an interview with two of the global bank's senior executives, further reinforces that technology is only part of the picture, revealing the many parallels between agile methodologies in the software industry and lean management in manufacturing and service environments. Both arise from a common focus on the creation of customer value, steady flow, and continuous improvement.

"Speed and scale: Unlocking digital value in customer journeys" (p. 30) examines the specific ways that organizations can use technological change to transform customer experience (and themselves) at two speeds: quick, high-impact, low-cost moves to help customers today, and more substantial, long-term investments that enable even deeper change over time. In "How to start building your next-generation operating model" (p. 39), the authors lay out a series of essential building blocks that enterprises can use in reimagining their businesses. Finally, "The next acronym you need to know about: RPA (robotic process automation)" (p. 46) describes the potential of a new development in business automation that, crucially, frees employees from tasks that do not take full advantage of their capabilities—a form of waste recognized from the earliest days of lean manufacturing.

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Transforming operations management for a digital world

When combined, digital innovation and operations-management discipline boost organizations' performance higher, faster, and to greater scale than has previously been possible.

Albert Bollard, Alex Singla, Rohit Sood, and Jasper van Ouwerkerk

In every industry, customers' digital expectations are rising, both directly for digital products and services and indirectly for the speed, accuracy, productivity, and convenience that digital makes possible. But the promise of digital raises new questions for the role of operations management—questions that are particularly important given the significant time, resources, and leadership attention that organizations have already devoted to improving how they manage their operations.

At the extremes, it can sound as if digitization is such a break from prior experience that little of this history will help. Some executives have asked us point blank: "If so much of what we do today is going to be automated—if straight-through processing takes over our operations, for example—what will be left to manage?" The answer, we believe, is "quite a lot."

More digital, more human
Digital capabilities are indeed quite new. But even as organizations balance lower investment in traditional operations against greater investment in digital, the need for operations management will hardly disappear. In fact, we believe the need will be more profound than ever, but for a type of operations management that offers not only stability—which 20th-century management culture provided in spades—but also the agility and responsiveness that digital demands.

The reasons we believe this are simple. First, at least for the next few years, to fully exploit digital capabilities most organizations will continue to depend on people. Early data suggest that human skills are actually becoming more critical in the digital world, not less. As tasks are automated, they tend to become commoditized; a "cutting edge" technology such as smartphone submission of insurance claims quickly becomes almost ubiquitous. In many contexts, therefore, competitive advantage is likely to depend even more on human capacity: on providing thoughtful advice to an investor saving for retirement or calm guidance to an insurance customer after an accident.

That leads us to our second reason for focusing on this type of operations management: building people's capabilities. Once limited to repetitive tasks, machines are increasingly capable of complex activities, such as allocating work or even developing algorithms for mathematical modeling. As technologies such as machine learning provide ever more personalization, the role of the human will change, requiring new skills. A claims adjuster may start by using software to supplement her judgments, then help add new features to the software, and eventually may find ways to make that software more predictive and easier to use.

Acquiring new talents such as these is hard enough at the individual level. Multiplied across an organization it becomes exponentially more difficult, requiring constant cycles of experimentation, testing, and learning anew—a commitment that only the most resilient operations-management systems can support.

Seizing the digital moment
And if digital needs operations management, we believe it's equally true that operations management needs digital. Digital advances are already making the management of operations

more effective. Continually updated dashboards let leaders adjust people's workloads instantly, while automated data analysis frees managers to spend more time with their teams.

The biggest breakthroughs, however, come from the biggest commitment: to embrace digital innovation and operations-management discipline at the same time. That's how a few early leaders are becoming better performers faster than they ever thought possible. At a large North American property-and-casualty insurer, for example, a revamped digital channel has reduced call-center demand by 30 percent in less than a year, while improved management of the call-center teams has reduced workloads an additional 25 percent.

Achieving these outcomes requires organizations to tackle four major shifts.

Digital and analog, reinforcing each other
Digitization can be dangerous if it eliminates opportunities for productive human (or "analog") intervention. The goal instead should be to find out where digital and analog can each contribute most.

That was the challenge for a B2B data-services provider, whose customized reports were an essential part of its white-glove business model. Rather than simply abandon digitization, however, the company enlisted both customers and frontline employees to determine which reports could be turned into automated products that customers could generate at will.

Working quickly via agile "sprints," developers tested products with the front line, which was charged with teaching customers how to use the automated versions and gathering feedback on how they worked. The ongoing dialogue among customers, frontline employees, and the developer team now means the company can quickly

develop and test almost any automated report, and successfully roll it out in record time.

Driving digital, enterprise-wide

Developing new digital products is only the beginning, as a global bank found when it launched an online portal. Most customers kept to their branch-banking habits—even for simple transactions and purchases that the portal could handle much more quickly and cheaply.

Building the portal wasn't enough, nor was training branch associates to show customers how to use it. The whole bank needed to reorient its activities to showcase and sustain digital. That meant modifying roles for everyone from tellers to investment advisers, with new communications to anticipate people's concerns during the transition and explain how customer service was evolving. New feedback mechanisms now ensure that developers hear when customers tell branch staff that the app doesn't read their checks properly.

Within the first few months, use of the new portal increased 70 percent, while reductions in costly manual processing means bringing new customers on board is now 60 percent faster. And throughout the changes, employee engagement has actually improved.

Realigning from the customer back

In the next shift, the organization redesigns internal roles so that they support the way customers work with the organization. That was the lesson a major European asset manager learned as it set out on a digital redesign of its complex, manual processes for accepting payments and for payouts on maturity. The entire organization consisted of small silos based on individual steps in each process, such as document review or payment processing—with no real correlation to what customers wanted to accomplish.

The resulting mismatch wasted time and effort for customers, associates, and managers alike.

The company saw that to digitize successfully, it would have to rethink its structure so that customers could easily move through each phase of fulfilling a basic need: for instance, "I've retired and want my annuity to start paying out." The critical change was to assign a single person to redesign each "customer journey," with responsibility not only for overseeing its digital elements but also for working hand in glove with operations managers to ensure the entire journey worked seamlessly. The resulting reconfiguration of the organization and operations-management systems reduced handoffs by more than 90 percent and cycle times by more than half, effectively doubling total capacity.

Making better leaders through digital

The final shift is the furthest reaching: digital's speed requires leaders and managers to develop much stronger day-to-day skills in working with their teams. Too often, even substantial behavior changes don't last. That's when digital actually becomes part of the solution.

About two years after a top-to-bottom transformation, cracks began to show at a large North American property-and-casualty insurer. Competitors began to catch up as associate performance slipped. Managers and leaders reported high levels of stress and turnover.

A detailed assessment found that the new practices leaders had adopted—the cycle of daily huddles, problem-solving sessions, and check-ins to confirm processes were working—were losing their punch. Leaders were paying too little attention to the quality of these interactions, which were becoming ritualized. Their people responded by investing less as well.

Digital provided a way for leaders to recommit. An online portal now provides a central view of the leadership activities of managers at all levels. Master calendars let leaders prioritize their on-the-ground work with their teams over other interruptions. Redefined targets for each management tier are now measured on a daily basis. The resulting transparency has already increased engagement among managers, while raising retention rates for frontline associates.

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Organizations investing in human and digital capabilities can start by asking themselves several critical questions:

- Do we really understand how customers interact with us now, and how they want to in the future?

- How can we give customers the experience they want, no matter which digital and human channels they use?

- How would a faster metabolism help us uncover new opportunities for better performance?

- Can our culture become flexible enough for us to collaborate effectively with our customers through constant change?

Capturing the digital opportunity will require even greater operations-management discipline. But digital also makes this discipline easier to sustain. Adding the two together creates a powerful combination. ■

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ING's agile transformation

Two senior executives from the global bank describe their recent journey.

Deepak Mahadevan

Established businesses around the world and across a range of sectors are striving to emulate the speed, dynamism, and customer centricity of digital players. In the summer of 2015, the Dutch banking group ING embarked on such a journey, shifting its traditional organization to an "agile" model inspired by companies such as Google, Netflix, and Spotify. Comprising about 350 "squads" in 13 so-called tribes, the new approach at ING has already improved time to market, boosted employee engagement, and increased productivity. In this interview with McKinsey's Deepak Mahadevan in October 2016, ING Netherlands chief information officer (CIO) Peter Jacobs and Bart Schlatmann, who, until recently, was the chief operating officer of ING Netherlands, explain why the bank needed to change, how it manages without the old reporting lines, and how it measures the impact of its efforts.

McKinsey: *What prompted ING to introduce this new way of working?*

Bart Schlatmann: We have been on a transformation journey for around ten years now, but there can be no let up. Transformation is not just moving an organization from A to B, because once you hit B, you need to move to C, and when you arrive at C, you probably have to start thinking about D.

In our case, when we introduced an agile way of working in June 2015, there was no particular financial imperative, since the company was performing well and interest rates were still at a decent level. Customer behavior, however, was rapidly changing in response to new digital distribution channels, and customer expectations were being shaped by digital leaders in other

industries, not just banking. We needed to stop thinking traditionally about product marketing and start understanding customer journeys in this new omnichannel environment. It's imperative for us to provide a seamless and consistently high-quality service so that customers can start their journey through one channel and continue it through another—for example, going to a branch in person for investment advice and then calling or going online to make an actual investment. An agile way of working was the necessary means to deliver that strategy.

McKinsey: *How do you define agility?*

Bart Schlatmann: Agility is about flexibility and the ability of an organization to rapidly adapt and steer itself in a new direction. It's about minimizing handovers and bureaucracy, and empowering people. The aim is to build stronger, more rounded professionals out of all our people. Being agile is not just about changing the IT department or any other function on its own. The key has been adhering to the "end-to-end principle" and working in multidisciplinary teams, or squads, that comprise a mix of marketing specialists, product and commercial specialists, user-experience designers, data analysts, and IT engineers—all focused on solving the client's needs and united by a common definition of success. This model [see exhibit] was inspired by what we saw at various technology companies, which we then adapted to our own business.

McKinsey: *What were the most important elements of the transformation?*

Peter Jacobs: Looking back, I think there were four big pillars. Number one was the agile way of working itself. Today, our IT and commercial colleagues sit together in the same buildings, divided into squads, constantly testing what they might offer our customers,

in an environment where there are no managers controlling the handovers and slowing down collaboration.

Number two is having the appropriate organizational structure and clarity around the new roles and governance. As long as you continue to have different departments, steering committees, project managers, and project directors, you will continue to have silos—and that hinders agility.

The third big component is our approach to DevOps[1] and continuous delivery in IT. Our aspiration is to go live with new software releases on a much more frequent basis—every two weeks rather than having five to six "big launches" a year as we did in the past. The integration of product development and IT operations has enabled us to develop innovative new product features and position ourselves as the number-one mobile bank in the Netherlands.

Finally, there is our new people model. In the old organization, a manager's status and salary were based on the size of the projects he or she was responsible for and on the number of employees on his or her team. In an agile performance-management model, there are no projects as such; what matters is how people deal with knowledge. A big part of the transformation has been about ensuring there is a good mix between different layers of knowledge and expertise.

McKinsey: *What was the scope of this transformation? Where did you start, and how long did it take?*

Bart Schlatmann: Our initial focus was on the 3,500 staff members at group headquarters. We started with these teams—comprising previous departments such as marketing, product management, channel management, and IT development—because we believed we had to start

ING's new agile organizational model has no fixed structure—it constantly evolves.

P Product owner
★ Chapter lead

Tribe

	Squad	Squad	Squad	Squad	Tribe lead	Agile coach
	👤	👤	👤	👤	🟠	🟢
Chapter	★	👤	👤	👤		
Chapter	👤	👤	👤	★		
	P	P	P	P		

Tribe
(collection of squads with interconnected missions)

- includes, on average, 150 people
- empowers tribe lead to establish priorities, allocate budgets, and form interface with other tribes to ensure knowledge/insights are shared

Agile coach
- coaches individuals and squads to create high-performing teams

Squad
(basis of new agile organization)

- includes no more than 9 people; is self-steering and autonomous
- comprises representatives of different functions working in single location
- has end-to-end responsibility for achieving client-related objective
- can change functional composition as mission evolves
- is dismantled as soon as mission is executed

Product owner
(squad member, not its leader)
- is responsible for coordinating squad activities
- manages backlog, to-do lists, and priority setting

Chapter
(develops expertise and knowledge across squads)

Chapter lead
- is responsible for one chapter
- represents hierarchy for squad members (re: personal development, coaching, staffing, and performance management)

Source: ING

Bart Schlatmann

From 2007 to 2017, Bart Schlatmann was the COO of ING Netherlands, after previously serving in a range of roles starting in 1995. He is a board member of Bruna, the Dutch Payments Association, and WestlandUtrecht Bank, and he is a member of the supervisory board of Interhyp Germany. Mr. Schlatmann holds a master's degree in economic science from Erasmus University in Rotterdam.

Peter Jacobs

Peter Jacobs is the CIO of ING Netherlands, a position he assumed in 2013 after previously serving as director of application management. Earlier in his career, he was an associate partner and consultant at McKinsey & Company. He is a member of the supervisory board of Equens, a European payment processor, and holds a PhD in systems engineering from Delft University of Technology.

at the core and that this would set a good example for the rest of the organization.

We originally left out the support functions—such as HR, finance, and risk—the branches, the call centers, operations, and IT infrastructure when shifting to tribes and squads. But it doesn't mean they are not agile; they adopt agility in a different way. For example, we introduced self-steering teams in operations and call centers based on what we saw working at the shoe-retailer Zappos. These teams take more responsibility than they used to and have less oversight from management than previously. Meanwhile, we have been encouraging the sales force and branch network to embrace agility through daily team stand-ups and other tactics. Functions such as legal, finance, and operational risk are not part of a squad per se, as they need to be independent, but a squad can call on them to help out and give objective advice.

It took about eight or nine months from the moment we had written the strategy and vision, in late 2014, to the point where the new organization and

way of working had been implemented across the entire headquarters. It started with painting the vision and getting inspiration from different tech leaders. We spent two months and five board off-sites developing the target organization with its new "nervous system." In parallel, we set up five or six pilot squads and used the lessons to adapt the setup, working environment, and overall design. After that, we were able to concentrate on implementation—selecting and getting the right people on board and revamping the offices, for example.

McKinsey: *Was agility within IT a prerequisite for broader organizational change?*

Peter Jacobs: Agility within IT is not a prerequisite for a broader transformation, but it certainly helps. At ING, we introduced a more agile way of working within IT a few years ago, but it was not organization-wide agility as we understand it today, because it did not involve the business. You can certainly start in IT and gradually move to the business side, the advantage of this being that the IT teams can test and develop

the concept before the company rolls it out more widely. But I think you could equally start with one value stream, let's say mortgages, and roll it out simultaneously in the business and in IT. Either model can work.

What you can't do—and that is what I see many people do in other companies—is start to cherry-pick from the different building blocks. For example, some people formally embrace the agile way of working but do not let go of their existing organizational structure and governance. That defeats the whole purpose and only creates more frustration.

McKinsey: *How important was it to try to change the ING culture as part of this transformation?*

Bart Schlatmann: Culture is perhaps the most important element of this sort of change effort. It is not something, though, that can be addressed in a program on its own. We have spent an enormous amount of energy and leadership time trying to role model the sort of behavior—ownership, empowerment, customer centricity—that is appropriate in an agile culture. Culture needs to be reflected and rooted in anything and everything that we undertake as an organization and as individuals.

For instance, one important initiative has been a new three-week onboarding program, also inspired by Zappos, that involves every employee spending at least one full week at the new Customer Loyalty Team operations call center taking customer calls. As they move around the key areas of the bank, new employees quickly establish their own informal networks and gain a deeper understanding of the business.

We have also adopted the peer-to-peer hiring approach used by Google. For example, my

colleagues on the board selected the 14 people who report to me. All I have is a right of veto if they choose someone I really can't cope with. After thousands of hires made by teams using this approach at every level in the organization, I have never heard of a single veto being exercised— a sure sign that the system is working well. It's interesting to note, too, that teams are now better diversified by gender, character, and skill set than they were previously. We definitely have a more balanced organization.

A lot is also down to the new way we communicate and to the new office configuration: we invested in tearing down walls in buildings to create more open spaces and to allow more informal inter- action between employees. We have a very small number of formal meetings; most are informal. The whole atmosphere of the organization is much more that of a tech campus than an old-style traditional bank where people were locked away behind closed doors.

McKinsey: *Was a traditional IT culture an impediment to the transformation?*

Peter Jacobs: In IT, one of the big changes was to bring back an engineering culture, so there's now the sense that it's good to be an engineer and to make code. Somehow over the years, success in IT had become a question of being a good manager and orchestrating others to write code. When we visited a Google I/O conference in California, we were utterly amazed by what we saw and heard: young people talking animatedly about technology and excitedly discussing the possibilities of Android, Google Maps, and the like. They were proud of their engineering skills and achieve- ments. We asked ourselves, "Why don't we have this kind of engineering culture at ING? Why is it that large enterprises in Holland and Western Europe typically just coordinate IT rather than being truly inspired by it?" We consciously

encouraged people to go back to writing code—I did it myself—and have made it clear that engineering skills and IT craftsmanship are what drive a successful career at ING.

McKinsey: *Can you say more about the companies that inspired you?*

Peter Jacobs: We came to the realization that, ultimately, we are a technology company operating in the financial-services business. So we asked ourselves where we could learn about being a best-in-class technology company. The answer was not other banks, but real tech firms.

If you ask talented young people to name their dream company from an employment perspective, they'll almost always cite the likes of Facebook, Google, Netflix, Spotify, and Uber. The interesting thing is that none of these companies operate in the same industry or share a common purpose. One is a media company, another is search-engine based, and another one is in the transport business. What they all have in common is a particular way of working and a distinctive people culture. They work in small teams that are united in a common purpose, follow an agile "manifesto," interact closely with customers, and are constantly able to reshape what they are working on.

Spotify, for example, was an inspiration on how to get people to collaborate and work across silos—silos still being a huge obstacle in most traditional companies. We went to visit them in Sweden a few times so as to better understand their model, and what started as a one-way exchange has now become a two-way exchange. They now come to us to discuss their growth challenges and, with it, topics like recruitment and remuneration.

McKinsey: *Without traditional reporting lines, what's the glue that holds the organization together?*

Bart Schlatmann: Our new way of working starts with the squad. One of the first things each squad has to do is write down the purpose of what it is working on. The second thing is to agree on a way of measuring the impact it has on clients. It also decides on how to manage its daily activities.

Squads are part of tribes, which have additional mechanisms such as scrums, portfolio wall planning, and daily stand-ups to ensure that product owners are aligned and that there is a real sense of belonging. Another important feature is the QBR [quarterly business review], an idea we borrowed from Google and Netflix. During this exercise, each tribe writes down what it achieved over the last quarter and its biggest learning, celebrating both successes and failures and articulating what it aims to achieve over the next quarter—and, in that context, which other tribe or squad it will need to link up with. The QBR documents are available openly for all tribes: we stimulate them to offer input and feedback, and this is shared transparently across the bank. So far, we have done four QBRs and, while we are improving, we still have to make them work better.

In the beginning, I think the regulators were at times worried that agile meant freedom and chaos; that's absolutely not the case. Everything we do is managed on a daily basis and transparent on walls around our offices.

McKinsey: *Can traditional companies with legacy IT systems really embrace the sort of agile transformation ING has been through?*

Peter Jacobs: I believe that any way of working is independent of what technology you apply. I see no reason why an agile way of working would be affected by the age of your technology or the size of your organization. Google and ING show that this has nothing to do with size, or even

the state of your technology. Leadership and determination are the keys to making it happen.

McKinsey: *Are some people better suited to agile operating approaches than are others?*

Bart Schlatmann: Selecting the right people is crucial. I still remember January of 2015 when we announced that all employees at headquarters were put on "mobility," effectively meaning they were without a job. We requested everyone to reapply for a position in the new organization. This selection process was intense, with a higher weighting for culture and mind-sets than knowledge or experience. We chose each of the 2,500 employees in our organization as it is today—and nearly 40 percent are in a different position to the job they were in previously. Of course, we lost some people who had good knowledge but lacked the right mind-set; but knowledge can be easily regained if people have the intrinsic capability.

Peter Jacobs: We noticed that age was not such an important differentiator. In fact, many whom you may have expected to be the "old guards" adapted even more quickly and more readily than the younger generation. It's important to keep an open mind.

McKinsey: *How would you quantify the impact of what has been done in the past 15 months?*

Bart Schlatmann: Our objectives were to be quicker to market, increase employee engagement, reduce impediments and handovers, and, most important, improve client experience. We are progressing well on each of these. In addition, we are doing software releases on a two- to three-week basis rather than five to six times a year, and our Net Promoter Score[2] and employee-engagement scores are up multiple points. We are also working with INSEAD, the international business school, to measure some of these metrics as a neutral outsider.

McKinsey: *Do you see any risks in this agile model?*

Peter Jacobs: I see two main risks. First, agility in our case has been extremely focused on getting software to production and on making sure that people respond to the new version of what they get. If you are not careful, all innovations end up being incremental. You therefore have to organize yourself for a more disruptive type of innovation—and you can't always expect it to come out of an individual team.

Second, our agile way of working gives product owners a lot of autonomy to collect feedback from end users and improve the product with each new release. There is a risk that people will go in different directions if you don't align squads, say, every quarter or six months. You have to organize

"It's important to keep an open mind. Among our people, many of the 'old guard' adapted even more quickly and readily than the younger generation."

in such a way that teams are aligned and mindful of the company's strategic priorities.

McKinsey: *What advice would you give leaders of other companies contemplating a similar approach?*

Bart Schlatmann: Any organization can become agile, but agility is not a purpose in itself; it's the means to a broader purpose. The first question you have to ask yourself is, "Why agile? What's the broader purpose?" Make sure there is a clear and compelling reason that everyone recognizes, because you have to go all in—backed up by the entire leadership team—to make such a transformation a success. The second question is, "What are you willing to give up?" It requires sacrifices and a willingness to give up fundamental parts of your current way of working—starting

with the leaders. We gave up traditional hierarchy, formal meetings, overengineering, detailed planning, and excessive "input steering" in exchange for empowered teams, informal networks, and "output steering." You need to look beyond your own industry and allow yourself to make mistakes and learn. The prize will be an organization ready to face any challenge. ■

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[1] The integration of product development with IT operations.
[2] The Net Promoter Score is a standard industry measure of customer satisfaction.

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Speed and scale: Unlocking digital value in customer journeys

Even as organizations assemble digital building blocks for the long term, they also need short-term, pragmatic moves that meet customer expectations and protect core businesses today.

Driek Desmet, Shahar Markovitch, and Christopher Paquette

Digitization is a profound transformation. When a global bank reinvented its onboarding process for commercial clients, the results included dramatically reduced costs, a market-beating customer experience—and an exhausted organization wondering how ambitious it should be. Could it repeat what it just went through for the rest of its business? How could it possibly do more than one of these at the same time? Would it take years?

Companies that are achieving digitization at scale have found a better way. They have developed a distinct structure that enables them to digitize their most important customer experiences at scale and at speed—in a consistent

way, with consistent resources, to produce consistent results. In doing so they transform much of the rest of their organizations, from product and process design through to technology and culture, becoming truly digital businesses.

Crucially, these companies not only understand the digital stakes confronting them—they also act on that knowledge. Think of how consumers behave in the digital world. Most of us will try a new app once, or maybe twice, and if we can't get it to work, we abandon it. That behavior leaves companies only one or two chances for their digital offerings to make a good impression and win adoption from their customers.

Yet today's customers do not want digital versions of the same manual, bureaucratic processes they faced yesterday. They search, download, pay, and listen to music all in one go, so why should their electrical service or car insurance still make them run a gantlet of separate steps for searching, price quotation, purchasing, invoicing, delivery, payment, and activation?

Companies that want to win at digital adoption are therefore recognizing that they must reimagine and digitize entire "customer journeys." These are the beginning-to-end processes that customers experience in getting the product or service they need, across whichever channels they choose (see sidebar "How many journeys?").

Streamlined, simplified journeys show impressive results quickly—usually on several fronts at once. Faster mobile-phone sign-ups raised a telecommunications company's customer satisfaction by 20 percent and reduced costs by 30 percent. For a European lender, time for account opening and loan approval fell from days to minutes, customer-engagement opportunities rose from once a month to three or four times a week, and IT became far more agile, delivering new releases in a month instead of a year (Exhibit 1).

A structure for scale and speed

In much the same way that the leap to digital means rethinking how an analog process works, the leap from transforming a single journey to tackling many at once means rethinking how digitization works. Even as the organization is building the new capabilities that digital businesses require, it must deploy its existing capabilities very differently in order to achieve scale and speed. The challenge is to balance all of the conflicting demands.

In our experience, six critical, parallel shifts combine to make digitization more manageable and predictable. Depending on an organization's starting capabilities and strategic needs, the amount of effort the elements require will naturally vary. But all six are essential to ensure that an organization actually makes the changes, derives their full benefit, and can keep improving once the changes are made.

Start with your story

It begins with a story. From the very earliest stages, the organization needs a consistent way to describe what customers should experience across all of the journeys that they may undertake with the company. This "enterprise customer experience story" will be unique to the company and will distill its strategy, brand, and positioning into practical guidelines that together support the rest of the transformation.

For one North American bank, customer focus groups provided direction by identifying two qualities—accessibility and flexibility—as top priorities in their banking relationships. These became the central theme of the bank's story, which then informed a series of design choices centering on the first steps customers experienced with the bank.

But the bank then had to determine which possible journeys would, with digitization, most effectively deliver the accessibility and flexibility the story promised. Each journey passed through a series of filters assessing its strategic and customer-experience value, its potential for economies of scale, the regulatory and technological hurdles facing it, and the organization's readiness to commit adequate financial and leadership resources to it.

The final output of the analysis was a road map for making the journeys a reality, prioritized according to the filters. For the bank, the top priority turned out to be a new onboarding process that would let customers open a

Exhibit 1   **Digitizing customer journeys yields impressive results.**

| **Commercial-bank loan** Time to approve new loan top-up/extension	**Day-to-day account** Time to open account	**Customer engagement** Touchpoints per year	**IT** Time to release major new feature
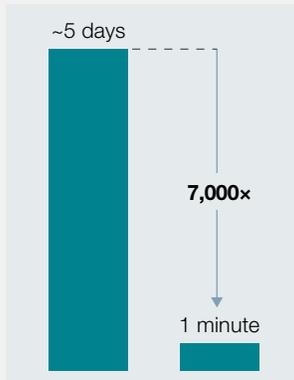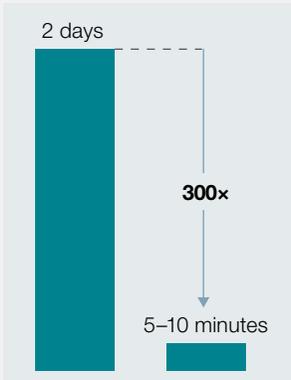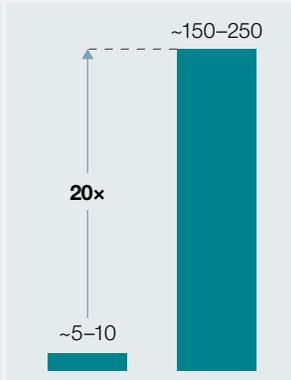
~5 days

2 days

~150–250

13 months

7,000×

300×

20×

13×

1 minute

5–10 minutes

~5–10

1 month
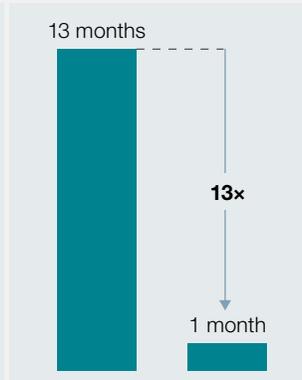
Source: Interactive Advertising Bureau; Pew Research Center; Searchmetrics

How many journeys?

Ask any reasonably complex, large organization how many journeys its customers might experience and the list will quickly grow to the dozens, if not the hundreds. Revamping all of them would be daunting. But in our experience, it's also unnecessary. Typically, a small number of core customer journeys cover about 80 percent of the customer interaction and 50 percent of the workforce. Digitizing that subset will digitize much of the business with far fewer resources.

The total number of these "core journeys" will naturally vary by company, but a few patterns hold among major industries. For banks, the core usually consists of between 10 and 20 journeys, with account opening and onboarding (across

products); payments; mortgages; service requests (such as the ever-popular lost PIN codes); and credit-card issuance as especially prominent. Life and retirement players look similar to banks, with 10 to 20 core journeys across account opening or enrollment, onboarding, servicing, and guidance. The number is slightly smaller for telecommunications companies, where mobile postpaid sales, customer-care requests (such as one-off data usage adjustments), fixed-line provisioning, network repair and maintenance, and prepaid top-ups rank highly in a core of 8 to 15 journeys. For electrical utilities, the number usually drops to fewer than 10, with sign-up, payment, meter reading, and change of address taking the lead.

"relationship" without naming a specific product or account type.

Sequence your tech transformation

Of all of the changes an organization must make to support digitization, the ones that are the most challenging, time consuming, and resource intensive are in IT. Nowadays, designing a one-off mobile app is fairly easy. The real challenge is to link that app to all of the other channels customers use and to integrate it into back-end systems for everything from authentication to credit scoring and postsale servicing.

But this is what it means to digitize at scale. Companies must resist two temptations. The first is to try to digitize each journey separately, which only re-creates the internal silos that most organizations are trying to break apart. The second is to invest heavily in specific Internet or mobile-channel IT, which usually is unnecessary. Instead, once the company has identified the core journeys it will digitize, it should choose its IT components and its sequencing so that the IT architecture changes naturally as the journeys build on one another.

For example, one way to accelerate digitization and reduce overall costs is to identify horizontal components, such as business-process management (BPM) layers, central administration platforms, or externally facing channels, that can be shared across all the journeys. Similarly, standard components such as eSignature, authentication, or document scanning and data-extraction systems are easily reused across many different journeys and product types.

The opportunity to use these techniques led one organization to use its customer onboarding journey as its initial test case. The organization reduced rework and extra expenses for later journeys by modernizing its common BPM

architecture and mobile front-end framework up front, and by developing reusable e-archiving and authentication components. It also built in an additional interface layer, which allowed for back-end services developed during later journeys to be connected easily once they were ready. The lessons learned from the test case therefore informed the entire remaining architecture transformation.

Turn, shift, accelerate, and repeat

In the predigital world, a retail chain might renovate its stores on a five- or seven-year cycle. Once a store was done, it stayed done, at least for a while. The leading digital platforms now release major revisions of their operating systems every year, with substantial upgrades every few months. Some update cycles are nearing daily or even hourly frequency, especially for data models and analytics. That rapid adaptation represents a fundamental cultural shift for incumbents in almost every industry, especially in heavily regulated fields in which perfectionism and caution are the default behaviors.

First, the pressure for speed means companies must identify a new type of "MVP"—not the "most valuable player" of sports teams, but the "minimum viable product" of the tech industry. The critical—and, for perfectionist organizations, uncomfortable—tension is between "minimum" and "viable." Compromise too much on viable and customers will think the new digital option is no option at all. Yet compromising on minimum can be equally dangerous, and more tempting for companies accustomed to longer timelines. Every delay to add extra features leaves openings for faster-moving competitors.

Reconciling the two requires discipline, both to describe a customer need accurately (without excess scope) and to fulfill it efficiently (without excess complexity). And it requires a real

change of perspective. For example, digital's speed alone is a huge advantage: a digital product providing only 80 percent of its analog counterpart's features may still succeed simply by being 10 or 20 times faster. Furthermore, by the time a digital product could reach 100 percent replication, some of those functions would likely be irrelevant. Accordingly, rather than view digitization as a project with an end date, people must understand it as a continual process of finding the right 80 percent that will help customers now.

Build talent—and your digital 'factory'

For the cultural change to last, the organization will need to change how it works. This includes acquiring digitally oriented talent and developing their capabilities. It also includes rethinking and streamlining governance, management, and budgeting processes so that the organization can move quickly and innovate.

As many organizations discover, employees who combine business expertise, digital acumen, and the leadership skills necessary to lead a digital journey transformation are rare. Several solutions are possible. One large retailer acquired a few specialized technology companies. A telco relied on a large digital agency to augment roles in areas such as enterprise architecture, while in parallel it hired external talent and trained internal employees. A bank took an even more comprehensive approach by setting up an internal academy to teach a combination of leadership, digital, and execution skills.

But that talent will become frustrated unless enterprise-wide governance models adapt to an environment demanding rapid iteration, learning, testing, and reacting. The solution, as organizations from banks to telcos have found, borrows the lean-management concept of the "work cell." In a comparatively simple operation, a work cell assembles representatives from the internal groups involved in the beginning-to-end process of, say, mortgage approval—sales, underwriting, credit analysis, document production—into a single team, so that each mortgage can be approved much more quickly and accurately. The employees may continue to report into their respective businesses and functions, but their day-to-day feedback comes from the work cell, and they can move between work cells or from work cells to other parts of the organization as needed.

This same concept works at much larger scale to cover all of the specialties that contribute to a digitization effort: product experts, compliance managers, user-experience designers, coders, financial analysts, and the like. A Southeast Asian telco enabled the work-cell idea by reworking its human-resources practices to provide a clear path for people to join work cells, build experience, and move to other positions. What started as about a dozen specialists expanded to become a full-fledged digital factory that quadrupled the capacity of the digitization program: everything that once happened only on a monthly cadence is now happening within a week.

Create a 'game plan' to guide the factory

The digital factory operates as a combination design firm and software hothouse, using the latest methodologies such as design thinking, zero-based process reengineering, and agile software development. But the way the factory works day to day is defined by a "game plan," a set of standard operating guidelines and methodologies that lay out the required deliverables, governance steps, and working processes—such as which decisions can be made by factory leadership and which require escalation. The goal is a balance between the structured predictability required to transform a large organization and the flexibility and agility required for a rapidly changing digital world (see sidebar "Approaches for execution").

Approaches for execution

Depending on factors including depth and breadth of existing digital capabilities, strength of executive alignment and support, and level of technological investment the company is making, we see three basic approaches in which organizations are embarking on digitization at scale.

A. Create one or two 'demonstration events' to build momentum. When an institution has high clarity on the priority journeys to digitize but is facing high cultural resistance, this is an ideal place to start. Proving that digitization is a success with a journey or two can showcase the benefits that are achievable and the need for a new way of working.

Maintaining the momentum requires clear communication, most importantly that demonstration events are not "the end" but rather the means to the real end, which is digitizing at scale. This message must come both from the top of the organization and from influential leaders at each level.

B. Launch a full program to build foundational capabilities. Institutions that have a proverbial burning platform, along with executives who believe in digitization at scale and understand its value, can instead start planning a complete program. But they must guard against two dangers: first, that everything is a priority, and second, that resources to execute are either insufficient or insufficiently understood. Taking a step back and spending a few weeks or months to build a longer-term structure for driving a digitization program—with a detailed prioritized road map, additional capabilities, and new e-talent—can minimize the risks.

C. Engage a third-party vendor for a build-operate-transfer approach. Finally, when moving quickly is of utmost importance and economics prevent a quick internal ramp-up of talent, institutions are beginning to explore "outsourcing transformation" for the highest-priority journeys. They are working with external resources to transform, refine, operate, and when ready, transfer back to the organization. One large financial institution partnered with a global vendor to help fill gaps in the talent pool for the digital factory, such as for customer-experience designers, developers, testers, architects, and project managers. The contract allowed the vendor to provide resources for only half of each transformation. The vendor was then responsible for building the institution's digital capabilities by recruiting candidates on the open market and training people from within the organization, who together would finish the remaining half of the transformation.

Ideally, a game plan emphasizes three points. First, rather than describing detailed answers, it sets out a series of questions for each transformation stage, framed in a way that suggests specific options but allows for a range of possibilities. Instead of describing compliance steps that wouldn't all apply to every product, the game plan would ask a few probing questions: What have the compliance specialists for the product area suggested? Did the team adequately challenge the status quo? Were other geographies consulted for solutions to customer or regulator pain points?

The game plan's second task is to provide a list of templates for important artifacts that should be delivered for each journey, such as market-research summaries, customer-experience design, economic modeling, operational implications, or interface mock-ups. Again, the templates should not be set in stone, but they should balance creativity and flexibility while ensuring that the key questions are answered.

The final and most important requirement for the game plan is to evolve, which can happen only after it is tested. Accordingly, the organization should launch a small-scale factory to start trying the concepts behind the game plan, digitizing real products and making changes to the game plan based on actual experience. Under the best conditions, the game plan becomes a living, breathing asset that is centrally administered while being cocreated by the organization.

One large UK organization tested its game plan for its customer-journey transformations in two very different business units. Even before the transformations were launched, the game plan's streamlined governance approach and clearly demarcated roles and responsibilities reduced stakeholder friction, speeding decisions. Moreover, by allowing both transformations to proceed under similar methodologies and deliverables, managers could more easily compare the journeys and refine the transformation process—and the game plan itself. Continual revisions to the game plan's step-by-step processes mean that the organization can now launch a new journey transformation in a matter of weeks instead of months.

Track it all the way

Measuring the impact of a large-scale digitization effort is essential to ensure it achieves the dramatic business results that are usually possible. Yet traditional measures of performance will only go so far in supporting the new culture and work habits.

First, the metrics themselves typically must change. Some measures, such as short-term return on investment, may unintentionally discourage employees from taking the risks that digital innovation requires. Others may impede collaboration. For example, to allocate resources optimally, an organization should abandon promotion metrics that emphasize the number of reports a manager has and instead reward those who reassign team members to high-growth businesses.

Next, reporting must happen faster: once the metrics are aligned with digital's demands, dashboards will ideally report the relevant data as they come in. Where possible, the organization builds a version of the network-operations centers that govern utility operations. The resulting insights ensure not only that each transformation delivers what it should but also that leaders know where to prioritize their investments. Over time, the organization applies the data for rapid testing and revision cycles to keep improving the digital experience customers actually see.

As part of its digitization process, a manufacturer aggregated a wide range of indicators—everything from batch quality and inventory availability to total full-time employees involved in delivery—

Exhibit 2 **How digitization made bank processes simpler (before) . . .**

Commercial-client onboarding

■ Process 1   ■ Process 2   ● Handoff

Client relations
Processing center
Legal/accounting
Compliance
IT
Testing

Start

Time ———— **70 days (approximately)** ————→
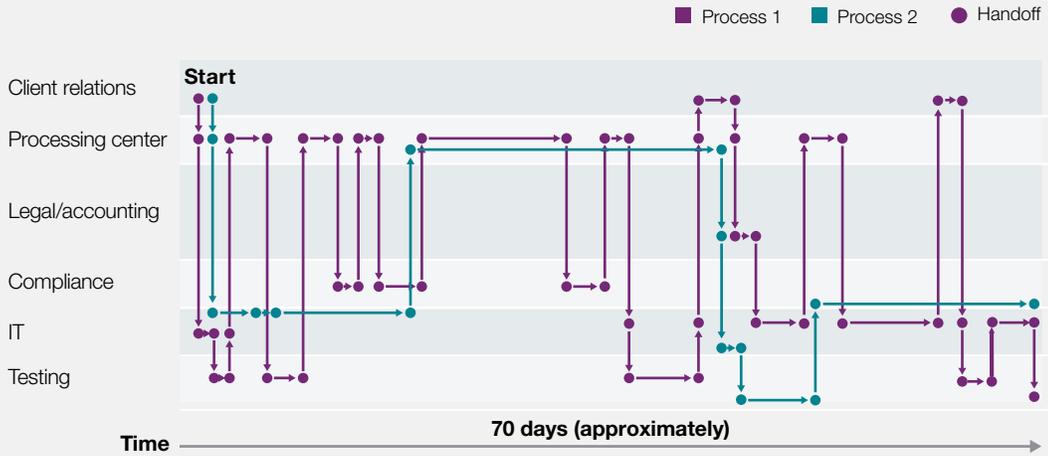
Exhibit 3 **. . . and more than twice as fast (after).**

■ Process 1   ■ Process 2   ● Handoff

Client relations

Compliance coordination

IT

Time ———— **25 days (approximately)** ————→
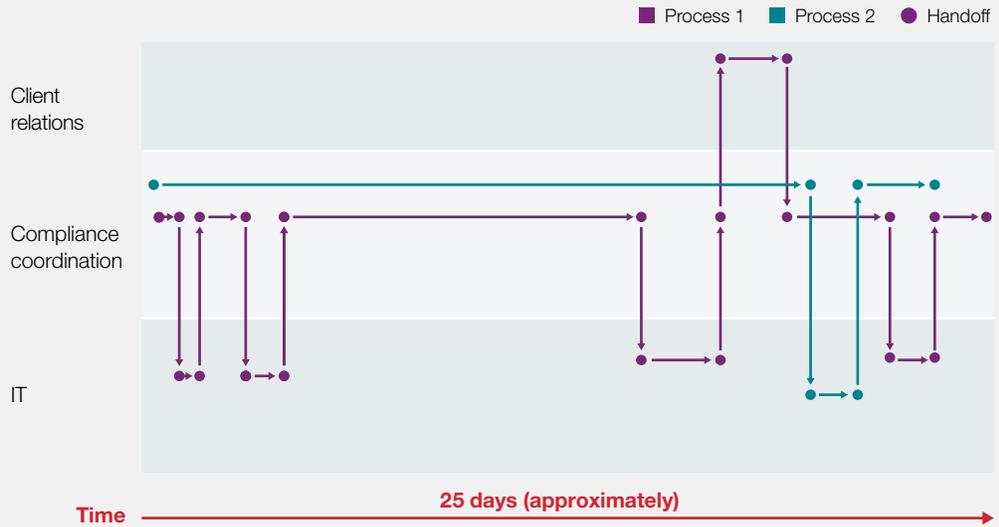
into a single, enterprise-wide, real-time dashboard. Management could then divert resources to struggling areas. For example, when a local transformation failed to improve batch quality, leaders could fly in experts from other facilities that had resolved the issue. And, knowing that each facility's transformation results were highly visible, the new transparency created a constant tension for line managers to deliver results.

Putting it all together

So how does it all come together? One of Europe's largest banks is winning the adoption game after fully digitizing an entire series of customer journeys. The initial focus of the bank's digitization story was on relieving retail-banking customers from their most "irritating service requests"—the lost debit cards, forgotten PIN codes, and similar "minor" problems that have a major impact on customer satisfaction and bank resources (Exhibit 2).

Using standardized components, a small, cross-functional team redesigned the processes underpinning these requests to assemble a mobile solution within six weeks (Exhibit 3). Rapid adoption boosted confidence in the organization's newfound digital capabilities, reinforcing the leaders' message that digitization would dramatically improve customers' experience. And employees reported that the changes reduced their frustration as well.

The cross-functional team grew to take on more journeys, leading it to redesign the front end of the bank's digital and mobile channels and deploy analytic tools that allow for more-precise targeting of support and live allocation of call-center

specialists. Over a period of 18 months, the team became a combination user-experience center and digital factory, which together employ more than 100 specialists who are now tackling complex journeys in areas such as corporate lending and export finance.

The bank as a whole has completed five of its most important journeys, with the factory now at sufficient scale to work on two major ones simultaneously, each taking between four and five months. The end result, across businesses as diverse as personal credit cards and commercial financing, is that customers report dramatically better experience and higher engagement. ∎

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How to start building your next-generation operating model

Each company's path to a new operating model is unique. But successful transformations are all constructed with the same set of building blocks.

Joao Dias, David Hamilton, Somesh Khanna, Christopher Paquette, and Rohit Sood

A North American bank took less than two years to shift 30 percent of its in-branch customer traffic to digital channels and dramatically reduce its brick-and-mortar footprint. A European cruise line redesigned and relaunched five core products in nine months to increase digital conversions by three to five times and sales by 150 percent.

These companies have been able to transform because they have developed next-generation operating models that provide the speed, precision, and flexibility to quickly unlock new sources of value and radically reduce costs. The operating model of the future combines digital technologies and process-improvement capabilities in an integrated, sequenced way to drastically improve customer journeys and internal processes.

Lean management has already played a significant role in putting in place processes, capabilities, and tools to improve how businesses operate. But the digital age has increased both the opportunities for businesses that know how to react and the difficulty of getting it right. For one thing, tasks performed by humans are more complex, whether it's accessing information in multiple formats from multiple sources or responding to changing market and customer dynamics at ever-increasing speeds. And as an increasing number of tasks become automated or are taken over by cognitive-intelligence capabilities, companies will need to

take many of the lessons learned from lean management and update them. Like a sprinter who needs all her muscles to be finely tuned and working in concert to reach top speeds, fast-moving institutions must have a system to continually synchronize their strategies, activities, performance, and health.

But how? Many institutions understand the need to change how they work and have embarked on numerous initiatives, yet few have been able to get beyond isolated success cases or marginal benefits.

We have found that companies that successfully build next-generation operating models do two things well. They focus on putting in place the building blocks that drive change across the organization, and they select a transformation path that suits their situation. These practices don't apply only to companies that have yet to start their digital transformation. In our experience, even companies that are well along their transformation journey can pivot to putting in place a next-generation model that delivers massive value while significantly reducing costs.

Building blocks of the next-generation operating model

Whatever the path companies choose to develop their next-generation operating model (a subject we return to later), we have found there is a set of building blocks of change that successful leaders put in place. Think of them as the mechanics of change—elements needed to underpin the development of the operating model. Given the dynamic nature of digitization and the fast pace of change, it's important not to think about perfecting the implementation of each building block before the operating model can function. The process is highly iterative, with elements of each building block tested and adapted to grow along with the model through a constant evolutionary cycle.

Building Block #1: Autonomous and cross-functional teams anchored in customer journeys, products, and services

Successful companies constantly rethink how to bring together the right combination of skills to build products and serve customers. That means reconfiguring organizational boundaries and revisiting the nature of teams themselves, such as creating more fluid structures in which day-to-day work is organized into smaller teams that often cut across business lines and market segments. This approach includes empowering teams to own products, services, or journeys, as well as to run experiments. These organizations are also becoming nimble in how they build skills across their teams by making "anchor hires" for key roles, setting up rotational and "train the trainer" programs, and committing to ongoing (often weekly) capability building and training for key roles.

Many insurers, for example, are dismantling traditional claims and underwriting units and reconstructing them to embed subject-matter experts such as lawyers and nurses into service groups. In the best companies, these teams also work side by side every day with technologists to design the tools and technology to improve efficiency and effectiveness.

Iteration is crucial to making this approach work. Leaders test various team configurations and allow flexibility in response to changing customer needs. One credit-card company, for example, shifted its operating model in IT from alignment around systems to alignment with value streams— the sources of the value being generated—within the business. Cross-functional teams were pulled together to work on priority journeys and initiatives to deliver on the value stream. These changes dramatically simplified the operating model, lowered direct leadership expenses, and contributed to a 200 percent increase in software-development productivity within three months.

Building Block #2: Flexible and modular architecture, infrastructure, and software delivery

Technology is a core element of any next-generation operating model, and it needs to support a much faster and more flexible deployment of products and services. However, companies often have trouble understanding how to implement these new technologies alongside legacy systems or are hampered by outdated systems that move far too slowly.

To address these issues, leaders are building modular architecture that supports flexible and reusable technologies. Business-process management (BPM) tools and externally facing channels, for example, can be shared across many if not all customer journeys. Leading technology teams collaborate with business leaders to assess which systems need to move faster. This understanding helps institutions decide how to architect their technology—for example, by identifying which systems should be migrated to the cloud to speed up builds and reduce maintenance.

This approach both accelerates development and prioritizes the use of common components, which in turn leads to development efficiency and consistency. Another important reason for building more flexible architecture is that it enables businesses to partner with an external ecosystem of suppliers and partners.

Similarly, leaders are investing heavily in DevOps and combining people, process, and technology changes to automate software testing, security, and delivery processes as well as infrastructure changes.

Building Block #3: A management system that cascades clear strategies and goals through the organization, with tight feedback loops

The best management systems for next-generation operating models are based on principles, tools, and associated behaviors that drive a culture of continuous improvement focused on customer needs. Leading companies embed performance management into the DNA of an organization from top to bottom, and translate top-line goals and priorities into specific metrics and KPIs for employees at all levels. They make visible the skills and processes needed for employees to be successful, put clear criteria in place, and promote the sharing of best practices.

The best institutions are evolving their management systems to create feedback mechanisms within and between the front line, back-office operations, and the product teams that deliver new assets. They are also using their management systems to harvest the surfeit of data generated by day-to-day activities to create user-friendly dashboards and reports, some of them in real time.

Performance management is becoming much more real time, with metrics and goals used daily and weekly to guide decision making. These metrics are supported by joint incentives—not just for individuals—that are tailored to each level of the organization and reinforce behaviors to support customers regardless of organizational boundaries.

One North American insurer struggled to make the predictive analytics models developed by central teams relevant to its frontline claims adjusters, who therefore failed to adopt the new capability. Knowing it was leaving significant value on the table, the company established daily feedback sessions between the central development team and the claims adjusters and embedded analytics specialists into customer-service teams to develop better insights into customer issues. The teams created shared goals based on customer value that were consistent with the organization's strategy and the daily work of adjusters. Under this new management system, the analytics specialists and claims adjusters shortened cycle times and dramatically improved their effectiveness. This freed up time for leaders to coach, problem

solve, and iterate on the next opportunities for the teams to pursue.

Successful companies prioritize speed and execution over perfection. That requires agility in delivering products to customers and quickly learning from them, as well as a willingness to take appropriate risks. The best organizations have already made agility a cornerstone of how they work beyond IT. One credit-card company brought together law and compliance personnel to sit in with marketing teams to intervene early in processes and have daily conversations to identify and resolve issues. Law and compliance functions have also begun to adopt agile methodologies to change their own work. As functions and teams collaborate, they are on track to reduce effective time to market by 90 percent for some core processes while also reducing operational risk.

Critical to success is leading the change from the top and building a new way of working across organizational boundaries. Senior leaders support this transformation as vocal champions, demonstrating agility through their own choices. They reinforce and promote rapid iteration and share success stories. Importantly, they hold themselves accountable for delivering on value

quickly, and establish transparency and rigor in their operations. Many manage the change aggressively, often changing performance incentives, mothballing outdated processes, assembling communication campaigns to reinforce culture, and writing informal blogs. At one asset-management company, the top team jettisoned its legacy budgeting process and asked leaders to be aggressive about capturing more value. They established an ongoing process for redistributing funding to the highest-value experiments that were working.

Defining the path for your organization

There is no one way to develop a next-generation operating model. It depends on a company's existing capabilities, desired speed of transformation, level of executive commitment, and economic pressure. We have seen four paths that leading companies take to drive their transformation, though organizations often move to a different path as their capabilities mature. These paths offer a guide for the first 12 months of a transformation journey.

An innovation outpost is a dedicated unit set up to be entirely separate from the historical culture, decision-making bureaucracy, and technical infrastructure of the main business. It creates inspiring products that illuminate the digital art of the possible (sometimes with questionable

Successful companies prioritize speed and execution over perfection. That requires agility in delivering products to customers and quickly learning from them, as well as a willingness to take appropriate risks.

economic impact), and hatches new business models in informal settings such as over foosball tables. This path has traditionally been popular as a first move but is now less common.

One retailer with an ineffective online business chose to open such an outpost. It introduced next-gen analytics, focused on customer experience rather than technology, and drove the mobile interface. Staying largely separate from the main business, the outpost created a buzz around innovation, attracted better talent, and repatriated many of its creations into the broader organization.

This path works well when there is limited alignment among executives on the importance and value of transformation, a need to move very quickly in response to market pressures, and significant legacy culture challenges to overcome. However, it is less effective as the "tip of the spear" for changing the culture or building sustainable capabilities, and often yields a low return on investment.

A fenced-off digital factory is a group of ground-breakers that works in partnership with businesses and functions (such as IT infrastructure and security, legal, compliance, and product development) while enjoying a high degree of autonomy. It typically houses specialized capability groups in technologies such as robotics or analytics, and deploys them to support the development of specific journeys in concert with business and functional partners. It both models a new way of working and integrates developed capabilities into the main business. As such, it focuses internally on integrating with and shifting the culture of the organization.

This is the most common starting point, as it balances the need for incubation with that of broader transformation. One European bank built a digital factory in a building on a campus. Each of the lower floors is dedicated to a separate journey, while the top floor is dedicated to creating reusable components and utilities—such as customer identification and verification or eSignature—that the other journeys can deploy in a modular way.

Business and functional colleagues come together to work with teams in the factory. Each of these teams develops products and services, moves them quickly from prototype to deployment, and then transfers them into the main business. As part of the management system, the team continues to monitor and iterate the product or service based on economic performance and customer feedback.

This path works well when there is a broad-based belief in and commitment to transformation, and a need to incubate a critical mass in internal capabilities. Many organizations have used this approach to attract digital talent, combat large-project inertia within IT groups, and speed transformation. Culture change is slower within the rest of the organization, but it happens over time as business and functional specialists partner with the factory for each journey. It can, however, also create a "have and have not" split within the business if not managed appropriately, and can require significant initial C-suite support and funding.

A business-unit accelerator is a scaled-down digital factory that incubates a transformation inside a business unit to tackle local customer journeys and business functions. The business unit builds its own skills, such as process-redesign and robotics capabilities, and has control over specific capabilities and investments. This means it doesn't need central funding or organization-wide agreement on a host of issues to get going.

One North American bank shifted to a business-unit accelerator model after the first few years of its transformation. It found that this move gave it more control and a closer connection to business

strategy and the customer—benefits that outweighed centralized scale and capability building. The bank invested heavily in talent and tools, with the aim of building a reputation among customers as a digital business that happens to produce banking products and experiences.

This path works well for organizations with large business units that operate independently. It's also a good starting point when one business unit is particularly far ahead in its thinking and belief, or where digital services have disproportionate value-creation potential. However, companies that choose this model must mitigate several risks. When business units choose their own digital tools and processes, for instance, complexity and costs increase for IT teams managing maintenance, licensing, and enterprise architecture. This model can also make it harder to build and share capabilities across the organization, since the skills developed are specific to the business unit.

A full-scale evolution is a comprehensive transformation in which the enterprise reorganizes itself almost entirely around major journeys. This is the natural operating model for many digital natives, as technology, digital services, and product delivery are basically inextricable. Companies focus on specific digital initiatives that deliver on business priorities, deploying specialized talent and cross-functional teams to support each one. The model is

highly attuned to the customer and rapidly develops, tests, and iterates on new products or services. Team members may be managed through a center of excellence or by business-unit leaders. This path is the aspiration for many incumbents, especially those that deliver services rather than physical products.

In one European bank undergoing a full-scale evolution, agile has become the default way for people to work, with colleagues from multiple functions, including IT, sitting side by side. Results are measured by value streams and journeys, flowing from the customer need back to the performance of the bank. Prioritization and resourcing take the form of active daily and weekly conversations about the next most important thing to work on. This approach is initially almost like shock treatment, but it offers important benefits, allowing companies to shake up the traditional management system and achieve culture change quickly and at scale. The organization builds agile skills broadly, identifies high and low performers, and pinpoints valuable and missing skills.

This path works well when there is a broad and top-down organizational mandate for change. Given the time it takes to move the needle, there should be no pressing near-term economic imperative. Companies that choose this model need to mitigate

several risks, such as ensuring that best practices are shared across the operating model rather than being confined to individual teams. In addition, organizations must share any scarce resources across business functions to drive impact, and ensure coordination with IT as it seeks to keep up with the technical architecture.

No-regret steps leaders should take

Every organization's transformation journey will be different. However, a simple set of immediate, no-regret steps can help leaders shape their first set of priority decisions and provide clarity on the way forward. These often include:

- Creating clarity on enterprise strategy and on where digital services can quickly enable sustainable value creation.

- Challenging the board to be explicit about the importance of the transformation and its support for investment; or, as a board, making this decision and challenging the executive team for a bold vision.

- Building top-team excitement and belief in change through visits to leading digital natives or incumbents pursuing their own transformation paths.

- Assessing the maturity of the management system using benchmarking against other organizations to identify strengths to build on and risks to mitigate.

- Investing in targeted capability building, especially for the top 50 leaders in the organization, and exploring core concepts such as digitization, agile, design thinking, and advanced analytics to create a shared vocabulary and spur action.

- Making an honest, objective assessment of talent and capabilities within the organization, benchmarked against peers and cross-sector leaders—given that disruption often comes from outside an industry rather than within.

- Surveying the cross-sector landscape for ideas and inspiration. (It's easier than ever to learn from others, and a rapid inventory of ideas can shed light on potential execution challenges to resolve.)

- Assessing the level of change that the organization can realistically absorb in the near and long term given its other priorities.

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Most companies recognize the need for a next-generation operating model to drive their business forward in the digital age. But how well they actually develop it makes all the difference between reinventing the business and just trying to do so. ◼

Joao Dias is a partner in McKinsey's Cologne office; **David Hamilton** is an associate partner in the Detroit office; **Somesh Khanna** is a senior partner in the New York office; **Christopher Paquette** is a partner in the Chicago office; and **Rohit Sood** is a partner in the Toronto office.

The next acronym you need to know about: RPA (robotic process automation)

RPA is a promising new development in business automation that offers a potential ROI of 30–200 percent— in the first year. Employees may like it too.

Xavier Lhuer

Robotics are beginning to have a profound effect on business. In this interview, Xavier Lhuer, a partner in McKinsey's London office, speaks with Leslie Willcocks, professor of technology, work, and globalization at the London School of Economics' department of management, about his work on robotic process automation—its impact on work, and how companies can capture its strategic and financial benefits.[1]

McKinsey: *Can you start by defining robotic process automation (RPA)?*

Leslie Willcocks: RPA takes the robot out of the human. The average knowledge worker employed on a back-office process has a lot of repetitive, routine tasks that are dreary and uninteresting. RPA is a type of software that mimics the activity of a human being in carrying out a task within a process. It can do repetitive stuff more quickly, accurately, and tirelessly than humans, freeing them to do other tasks requiring human strengths such as emotional intelligence, reasoning, judgment, and interaction with the customer.

There are four streams of RPA. The first is a highly customized software that will work only with certain types of process in, say, accounting and finance. The more general streams I describe in terms of a three-lane motorway. The slow lane is what we call screen scraping or web scraping. A user might be collecting data, synthesizing it, and putting it into some sort of document on a desktop. You automate as much of that as possible. The second lane in terms of power is a self-development kit where a template is provided and specialist programmers design the robot. That's usually customized for a specific organization. The fast lane is enterprise/enterprise-safe software that can be scaled and is reusable.

You can multiskill each piece of software. It's lightweight in the sense that you don't need a lot of IT involvement to get it up and running. Business-operations people can learn quite quickly how to configure and apply the robots. It's lightweight also in that it only addresses the presentation layer

of information systems. It doesn't have to address the business logic of the underlying system or the data-access layer.

McKinsey: *How is RPA different from cognitive intelligence?*

Leslie Willcocks: RPA deals with simpler types of task. It takes away mainly physical tasks that don't need knowledge, understanding, or insight—the tasks that can be done by codifying rules and instructing the computer or the software to act. With cognitive automation, you impinge upon the knowledge base that a human being has and on other human attributes beyond the physical ability to do something. Cognitive automation can deal with natural language, reasoning, and judgment, with establishing context, possibly with establishing the meaning of things and providing insights. So there is a big difference between the two.

In addition, whereas RPA is pretty ripe as a technology, cognitive automation isn't. I've not seen a wave of powerful, cognitive automation tools appear in the market or many companies using them yet.

McKinsey: *What are the business benefits of RPA?*

Leslie Willcocks: Over 16 case studies, we found a return on investment varying between 30 and 200 percent in the first year. But it's wrong to look just at the short-term financial gains, particularly if those are simply a result of labor savings. That approach does not do justice to the power of the software, because there are multiple business benefits.

For example, companies in highly regulated industries such as insurance and banking are finding that automation is a cheap and fast way of applying superior capability to the problem of compliance. You also get better customer service because you've

RPA and lean

One large financial institution is now building RPA into a broader lean-management solution to speed customer onboarding and product renewal. A small developer team released several robots in just ten weeks, for an efficiency gain of more than 5 percent. Overall, onboarding time has decreased by almost half, backlogs in renewal have fallen more than 25 percent, and employee engagement has risen more than 25 percent.

Leslie Willcocks

Leslie Willcocks is a professor in the Information Systems and Innovation Faculty Group of the London School of Economics. He is a coauthor of more than 35 books and has published almost 200 academic papers. A fellow of the British Computer Society, he is also the editor-in-chief of the *Journal of Information Technology*. He holds a doctorate in information systems from the University of Cambridge.

got more power in the process. A company that receives lots of customer inquiries, for example, can free staff to deal with the more complex questions.

There are benefits for employees, too. In every case we looked at, people welcomed the technology because they hated the tasks that the machines now do. Every organization we have studied reports that it is dealing with bigger workloads. I think there will be an exponential amount of work to match the exponential increase in data— 50 percent more each year. There is also a massive increase in audit regulation and bureaucracy. We need automation just to relieve the stress that creates in organizations. One online retailer measures the success of RPA in terms of the number of hours given back to the business. So it's not just shareholders, senior managers, and customers who benefit, but also employees.

McKinsey: *Can you describe a process where you have seen RPA in action?*

Leslie Willcocks: One insurer used to take two days to handle 500 premium advice notes. It now takes 30 minutes. It worked like this: a range of

brokers would issue insurance policies for clients, and there was a central repository into which the policies had to go and a process that someone had to manage to get the premium advice note (i.e., notification/details of the business written for accounting purposes) from the broker into the repository, a system that tracks policies. A number of operations had to occur for that advice note to be fully populated with all the data, and the process operator might find that the data had not been completely filled out, perhaps because the advice note wasn't structured very well. So the data had to be structured to standardize it so that it could be a common document like all the other advice notes. And if any data was missing, that person might have had to go back to the broker, or add things from the systems of record in the back office. Then, once the note was complete and the process operator had signed off, it went into the repository.

Now a lot of that sort of work can be automated. But some of it requires human intervention, human reasoning, judgment. So an RPA engineer would say, "Which bit can we automate?" The answer is, "Not everything"—it can't structure the data. There may at some stage be cognitive-automation technology that could structure the data, but RPA can't, so the human being has to structure the data at the front end and create a pro forma, ideal advice note. Clearly, the RPA can't deal with exceptions either. The engineer has to intervene and look at the exceptions and create a rule to deal with them, so that gradually you educate and configure the RPA to do more and more work. Eventually it can do 90 or 95 percent of the work, and very few exceptions have to be dealt with by a human.

McKinsey: *What are the most important considerations for those wishing to adopt RPA?*

Leslie Willcocks: The most important consideration is strategy. You can use automation tactically for cost savings. But if you use RPA

as a broader strategic tool, you get a lot more out of it. That's number one. Number two concerns the launch. You need to get the C-suite involved and appoint a really good project champion, and you have to pick the right process. It has to be stable, mature, optimized, rules-based, repetitive, and usually high volume. Start with a controlled experiment on a visible bottleneck or pain point.

The third consideration is change management—persuading the organization to change and adopt automation. It is a key issue from the outset. And the fourth is building a mature, enterprise-level capability for RPA. Long-term users have built centers of excellence over time, usually within business operations, and developed skills and capabilities within that center. They have people who assess the feasibility of a proposal from a business unit. They have people who configure a robot, install it, and develop it, and controllers who switch it on and off and plan its work and how it fits with human work. They have some sort of continuous-improvement capability and relationships with IT, governance, and security. Organizations signing up for RPA now should probably think about building a center of excellence immediately.

McKinsey: *How do companies choose whether to implement an IT solution or RPA? And how do the two departments work together?*

Leslie Willcocks: At one organization, the return on investment for RPA was about 200 percent in the first year, and the company could implement it within three months. The IT solution did the same thing but with a three-year payback period, and it was going to take nine months to implement.

In addition, many business operations find going through IT frustrating because it's so busy. Often the business wants something relatively

small, but the IT function has bigger fish to fry, and the business has to go to the back of the queue. So if an RPA tool is usable, cheap, and doesn't require much IT skill to implement, it's a no-brainer for the average operator in a business unit. The reason IT gets worried is that they know the disruptive, potentially disastrous effects of people playing around with IT in the organization without understanding how it's going to upset infrastructure, governance, security, and all the important touchpoints that IT is held responsible for. It's crucial, therefore, that IT is brought on board early.

McKinsey: *What do you think will be the long-term impact of robotic process automation?*

Leslie Willcocks: In the longer term, RPA means people will have more interesting work. For 130 years we've been making jobs uninteresting and deskilled. The evidence is that it's not whole jobs that will be lost but parts of jobs, and you can reassemble work into different types of job. It will be disruptive, but organizations should be able to absorb that level of change. The relationship between technology and people has to change in the future for the better, and I think RPA is one of the great tools to enable that change. ◼

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[1] Leslie P. Willcocks and Mary C. Lacity are coauthors of *Service Automation: Robots and the Future of Work*, Stratford-upon-Avon, United Kingdom: Steve Brookes Publishing, 2016.

Xavier Lhuer is a partner in McKinsey's London office.

How leaders do it:
Drive the management system

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Once an organization has created a new way of working, a new danger looms: that it stops evolving. Leaders therefore recognize that it isn't only the business—or even the larger organization—that has to keep changing. The fundamental management systems that define how people get their work done must evolve as well. With new, better ideas constantly arising, it's up to leaders to adapt them to their management systems so they help people at every level become more effective.

And that means understanding how the management systems are performing. Regular, rigorous assessment of these systems provides an invaluable starting point for organizations that want to know where their systems need to improve, say the authors of "Holding a mirror to the management system: How mature is it?" (p. 52). More specifically, "Advancing lean leadership" (p. 60) describes how leaders must change in order to instill a new culture. "Continuous improvement—make good management every leader's daily habit" (p. 64) then examines how digital innovation is making it easier for leaders to make the transition to a very different set of behaviors.

In a lean management system, one of the new expectations for leaders is to build even more leaders. In "Getting better than the tools we'd been taught: Lean and people" (p. 71), an auto-industry veteran expands on how fostering leadership at every level helped his organization break through a performance plateau. More broadly, "Bringing out the best in people: Capability building at scale" (p. 75) looks at the success factors that matter in maintaining a long-term commitment to helping everyone in an organization learn new skills of all varieties.

The last article in this section, "A package full of change: An interview with Ian Andrews of Commonwealth Bank of Australia" (p. 82), provides a practical example of how leaders can improve a crucial management system—in this case, the mechanism for transmitting major changes through to the front line. One of the world's largest banks created a new approach to change management so that changes are easier and faster for people to absorb.

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Holding a mirror to
the management system:
How mature is it?

To keep its performance improving, an enterprise must keep its management system improving, too.
A regular, rigorous cycle of assessing itself reveals actions that help make the system more mature.

Randy Cook, Stefan de Raedemaecker, Jacek Fabianowicz, and Alessandra Fantoni

Over the past 20 years of evaluating and diagnosing lean transformations, our research keeps confirming the familiar statistic: fewer than 30 percent of organizations succeed in improving both their performance and their long-term health.[1]

Much of our work has therefore focused on what makes those 30 percent different. Certainly, their paths aren't easy. The enduring transformations, like their less-successful counterparts, encounter barriers where performance plateaus or even slips. But what's unusual among the successful organizations is that the barriers aren't the end of the story. Instead, they become new beginnings.

One difference, we find, is how the 30 percent learn: they undergo repeated problem-solving cycles—identifying issues, finding root causes, implementing countermeasures, and taking the time for reflection. These cycles reexamine not just how the companies operate but also how they think about their operations. Their rigorous use of this basic structure expands their capacity for change and strengthens the interrelated disciplines of the lean management system: delivering value, developing people, discovering new ways of working, and connecting broad strategy to goals and a meaningful purpose.

The entire cycle is based on an even more critical difference. A successful organization understands itself—its strengths and, most especially, its weaknesses—to a depth that keeps its people from ever being entirely satisfied with its performance. From the front line to the C-suite, all of them know that there's always something important they can help to improve. And the scope of what might need improvement includes how the organization goes about improving itself.

The resulting clarity keeps it from becoming overconfident about its success, so it can understand the terrain ahead, deal with the perils of the journey, and set off in a new direction as conditions dictate. With these insights, one basic-materials company, for example, has increased its agility in a challenging market, recommitting itself to develop its people and to change constantly by rating their ability to use its management systems in all performance reviews and by enhancing cross-functional training. A leading insurer is developing a new generation of leaders to handle digital disruption. And a financial institution is reinforcing its senior management's capabilities to prepare for a major expansion of its business.

How success can lead to failure

Fundamentally, the problem many organizations face with lean management is how to respond to the performance advances the initial effort often produces. Ideally, organizations would continue to pursue improvement, compounding the early impact. But, paradoxically, early success may instead play out negatively in several ways.

Losing business purpose. The experience of the basic-materials company illustrates how an organization can get sidetracked by (and ultimately recover from) one of the most common dangers of lean transformations: a loss of focus on business objectives, so that transformation increasingly

occurs for transformation's sake. Certain diagnostic tools helped the company to identify waste so effectively that people started thinking about where the tools could be applied next rather than which challenges were truly most important. Over time, the company recognized that simply doing more lean things wasn't enough to ensure it was changing in the way its business required.

Focusing on tools, not ideas. Typically, focusing too intently on particular tools points to a deeper issue: people haven't fully assimilated the ideas underlying the tools, whose point is to reinforce a continuous-improvement culture, not to create experts in the tools.

Performance boards, for example, are often the single most visible evidence of a lean transformation. The data they display is essential to how a transformed organization works. Yet it isn't the boards that are truly important, or even the data. It's the ideas they represent: that people measure what truly matters to customers (and the company's strategy), that those measurements define good performance, and that people use them to talk openly about ways to improve. The boards can disappear at any time if whatever replaces them is at least as effective in reinforcing the same ideas.

Changing behavior but not mind-sets. The change-management literature[2] has long focused on the need to overcome resistance. But resistance can imply intent, when in reality people often revert to old behavior out of habit or instinct, reflecting old mind-sets that may persist even after an apparently successful initial transformation.

One financial institution, for example, adopted lean management enthusiastically after an early round of changes cut project-time requirements almost in half and helped the company to weather a crisis. But over the following years, the gains started to

erode. Managers reported that they felt they were spending more time enforcing standards than questioning whether the old ones still made sense.

The continuous-improvement culture the institution thought it had created hadn't fully taken hold. Consequently, under stress, many leaders reverted to command-and-control behavior, making decisions and solving problems for their teams or managing solely by outcomes rather than developing the skills of those teams. Some leaders paid only lip service to the new ways of working: they remained spectators rather than coaches and failed to shape expectations by modeling the desired behavior.

Building without balance. In the deepest sense, this problem's root cause is an incomplete or unbalanced approach to lean management. Our analysis of survey data on organizational transformations[3] underscored the point that lean management works when its four disciplines reinforce one another (Exhibit 1). To deliver more value, a company must find new ways of working, so its people must develop new capabilities consistent with its strategy and purpose. Accordingly, no single discipline will remain stronger for long unless the rest get stronger as well. Of course, at any given time, an organization may have to emphasize some aspects of lean management more than others, but ultimately all of the disciplines must work in unison. That means finding out how good the organization is at each of them.

The value of management-system maturity
To find out exactly why a transformation is no longer producing the expected results, an organization must look in the mirror and truly see itself. Because a few organizations have built such an advanced self-awareness into their management systems, they have little need to ask how mature those systems are or which components may need further work. They know

that improvement tends to happen in cycles and are probably already at work on the next one's most important opportunities.

But such organizations are rare, particularly among large enterprises where informal practices and tacit knowledge don't scale very well.

How can you assess a management system's maturity?
Most enterprises instead need a more explicit approach to assessing themselves—one that allows leaders to pinpoint exactly where (and how) to intervene so that improvement remains truly continuous.[4] In our review of several organizations that successfully strengthened their management systems, a few characteristics came to the fore:

■ *Comprehensive coverage of the system.* For anything as comprehensive and interdependent as lean management, an assessment must be just as comprehensive, covering all disciplines in equal depth. Assessing only parts of the system may be tempting, especially when leaders have a strong hypothesis about which disciplines seem weakest. But that shortcut risks missing critical issues and leads to ineffective half measures as a result.

■ *Detailed standards.* Lean management systems require new behaviors such as root-cause problem solving, systematic coaching and mentoring, and in-person confirmation that processes actually work as planned. These are so different from long-standing norms that the assessment must set clear expectations. For each behavior, it should provide examples of different levels of performance. Consider root-cause problem solving. Companies might decide that basic performance is characterized by problem-solving sessions that are frequently preempted by other priorities. By contrast, the

proficient standard might require the sessions to be held on a consistent schedule, with regular follow-up by senior leaders and only rare preemption.

- *Aspirational top-level descriptions.* Descriptions of the top level require particular care

because they serve as a motivator to keep people reexamining how well they are doing—a true north that represents a perfect (and unattainable) score. To return to problem solving, the top-level standard might require that leaders always allocate sufficient time and resources to this discipline, so that preemption never occurs.

Exhibit 1   **Implementing the four disciplines of lean management dramatically increases the chance of sustaining improvements over time.**

Each of lean management's four disciplines comprises two elements

Connect
- All employees understand how their work relates to the organization's vision
- Everyone is fully engaged in meeting individual goals and targets

Discover
- Best practices are systematically identified, shared, and improved
- Everyone is actively engaged in identifying errors and defects before they reach customers

Enable
- The organization develops its people so that they can surpass expectations for performance
- Managers understand that their primary role is to lead and develop their teams

Deliver
- All employees adapt their day-to-day capacity to changes in demand
- Everyone starts the day with a formal team discussion about the previous day's results and the current day's work

Success rate by number of elements implemented (n = 1,624)

— Sustainability

% of transformations that sustained improvement over time

Number of elements of the four disciplines that were implemented
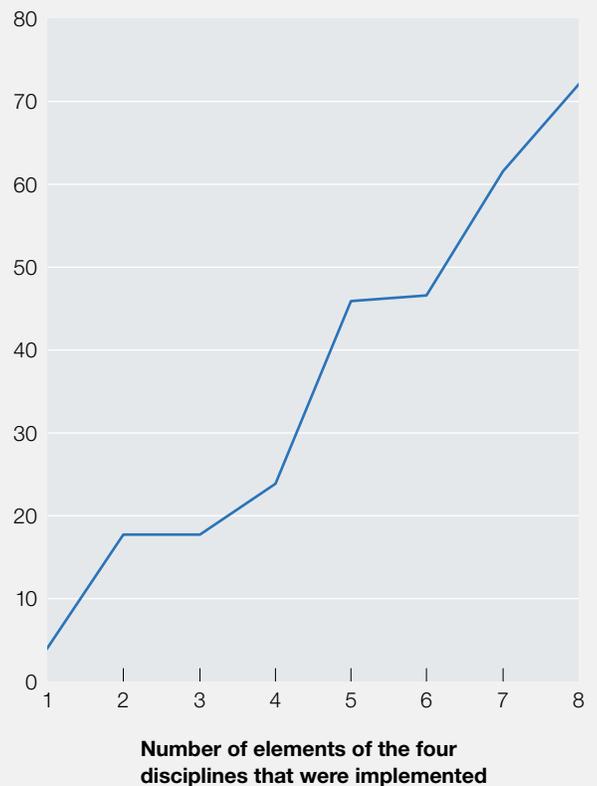
Source: *McKinsey Quarterly* transformational change survey, November 2014 (correlation analysis and factor analysis)

■ *Expert assessors.* The people who perform the assessment must not only understand the standards well enough to grade particular kinds of behavior consistently but also provide practical suggestions about what to change. Internal assessors, such as core people from the team that led the transformation or from other parts of the organization, are therefore especially valuable because their suggestions will be grounded in its culture and operating environment. Training internal assessors takes time and work, but the effort can pay off. If, say, the follow-up for root-cause problem solving is inconsistent, the assessor should be able to suggest realistic ways to determine which current activities could be eliminated to free up time. And as a European conglomerate has discovered, internal assessors help accelerate the cross-pollination of the best ideas.

Enabling a practical follow-up
For the assessment to have a lasting impact, the reports it generates must lead to thoughtful, pragmatic action. Leaders should be able to understand what they must do to advance the company from one level of maturity to the next—for example, creating clear implementation mechanisms so that new solutions are fully disseminated, or incorporating problem-solving expectations into all role descriptions.

Well-designed digital innovations provide further advantages in converting assessment data into results. First, they help the expert assessors to evaluate behavior and calibrate the findings more quickly. Second, and more important, they make the results more accessible—not only physically, by putting them in the hands of anyone with the right screen access, but also psychologically, by improving the way companies visualize data.

Consequently, managers can see, for example, exactly how many problems teams are resolving and how many other problems haven't been addressed. That creates a new sense of urgency, which makes it easier to undertake moves such as protecting time for problem solving in team schedules or prioritizing implementation when solutions are ready. The result is a dramatic increase in the number of problems resolved.

Assess, improve, repeat: Keeping the value-creation cycle humming
The value an organization gets from assessing itself keeps increasing as the process is repeated across the organization over time.

Assessment as teaching tool
Continual exposure to the assessment process teaches leaders at every level to view the organization and themselves more objectively,

The value an organization gets from assessing itself keeps increasing as the process is repeated across the organization over time.

Exhibit 2   **A European conglomerate's assessment cycle helps build the continuous-improvement system.**

Yearly scanning

Automated KPI[1] monitor → Preparation → Walkthrough by team → Feedback session → Improvement plan → Development → Automated KPI[1] monitor
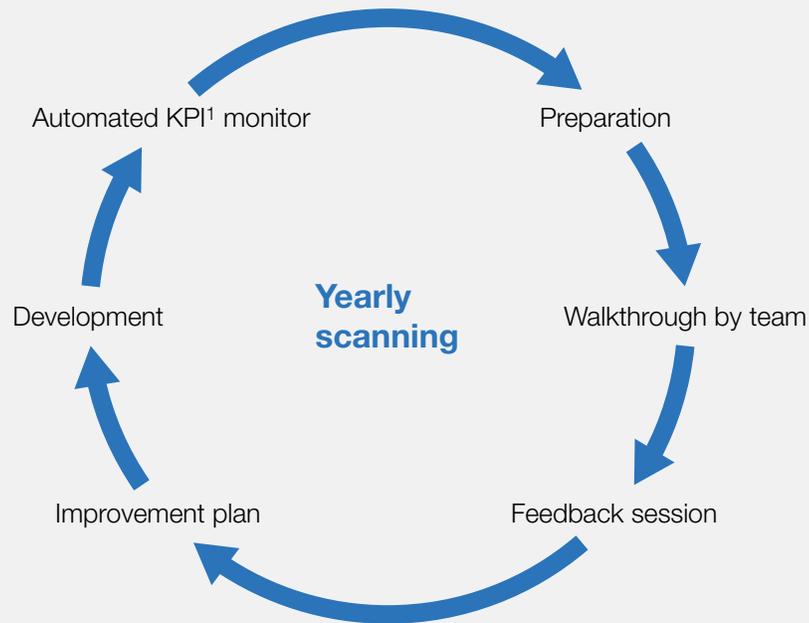
[1] Key performance indicator.

particularly if the assessment provides comparisons against benchmarks from mature organizations. Even internal comparisons of units with one another can highlight patterns and best practices that create significant value—initially, just by providing hard evidence of performance that's regarded as really good. Over time, the structured assessments encourage organizations to pursue balance across the detailed leadership behavior in all four lean-management disciplines.

This knowledge often reveals that organizations have a significant new improvement potential—an almost inexhaustible supply of targets, setting up a continuous-cycle journey of improvement and learning. That in turn leads to better business results.

Accelerating continuous improvement

Organizations that stick to an assessment timetable are seeing a wide range of improvements.

- *Breaking through plateaus.* The basic-materials company detailed earlier has used its assessment to achieve new levels of performance. Its leaders focused the assessment on a small number of top-performing sites—an approach that not only exposed opportunities unique to each of them but also helped the leadership as a whole to see common themes. That led to a reexamination of company-wide practices and behavior.

- *Jump-starting a deeper transformation.* At companies in sectors from mining and metals to industrial equipment, an in-depth assessment

has identified core strengths for improvement by targeting a few critical opportunities. The transformation initiatives of these organizations hit the ground running, and the leaders were better able to describe their future ambitions and to tell their people what the journey would look like. Moreover, these leaders report a greater understanding of how their own behavior had to change to sustain performance improvements. More broadly, the preparation kept people committed and engaged through temporary setbacks.

- *Reinforcing an annual improvement cycle.* The European conglomerate mentioned earlier now undertakes yearly assessments for each of its units as part of an annual improvement cycle (Exhibit 2). Since managers report over time that they have a better understanding of what they are expected to do, they can improve their skills substantially and find new S-curves of better performance for their teams.

Recommitting to culture change

One of North America's largest asset managers has been building its lean management systems for more than five years. It has recorded major improvements in critical metrics, such as customer satisfaction and average account-funding levels. But as new pressures on the industry grew, particularly from digitization, the company's leaders realized that they needed a broader understanding of how these systems would have to evolve. The company therefore launched its first assessment of its systems.

The basic findings seemed clear: in the four years after the initial transformation, 80 percent of the assessed sites showed continuing progress, while 20 percent had stagnated. But a deeper examination of the results showed that some of the reported progress was more apparent than real, especially from a sustainability perspective. Some sites showed worrying lapses in essential forms of behavior—lapses that, if allowed to persist, would

probably lead to declining performance. In short, parts of the organization had reverted to boosting their results in the wrong way.

The company then recommitted itself to cultural change, particularly emphasizing its line leaders' responsibility to encourage problem solving. Since then, the number of problems identified and solved has more than doubled, to upward of 50,000 a year. Most important, an assessment conducted two years later shows clear business results: customer satisfaction, employee engagement, quality, and productivity have all increased.

■ ■ ■

The experiences of these companies show how the perils of the continuous-improvement journey are in fact essential to learning—so long as organizations have the self-awareness to understand that the most important perils lie within. A cycle of well-structured assessments builds that self-awareness, so the management systems enabling continuous improvement can themselves continue to improve. ■

[1] "How to beat the transformation odds," April 2015, McKinsey.com.

[2] For example, see John P. Kotter, "Leading change: Why transformation efforts fail," *Harvard Business Review*, March–April 1995.

[3] "How to beat the transformation odds," April 2015, McKinsey.com.

[4] The examples discussed in this article are based on a McKinsey capability: the Operational Excellence Index and its predecessors.

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Holding a mirror to the management system: How mature is it?

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Advancing lean leadership

Transforming an organization's performance usually means changing its culture—and that means its leaders must change how they lead.

Alison Jenkins

Few organizations undertake a transformation with the goal of changing their own culture. Their focus is on the transformation itself: an intense, organization-wide program to boost both performance and organizational health.[1] But once they start realizing benefits, they want to keep achieving them. They quickly realize that the new ways of working are so different that making them stick is impossible without a cultural change.

That means the leaders will need to change themselves.

The transition is not easy. As with everyone else in the organization, leaders will need to know not only what they need do differently, but why changing their behavior matters—not just to the organization's success, but to their own. More-

over, almost by definition leaders have more years of old habits to unlearn. As a result, most will need meaningful support over an extended period of time to master this new way of leading.

That support will typically take the form of an integrated learning journey that builds their understanding, conviction, and ability to lead in a new way. The investment that leadership transformation requires is therefore substantial. But without it, an organization risks losing the continuous-improvement momentum that was the crucial reason for changing in the first place.

So what must leaders change?
Three essential, fundamental **behavioral shifts** illustrate the challenge of building everyday leadership, with each representing a profound

break from the typical way that large organizations have long encouraged leaders to behave (exhibit).

The first is **asking questions rather than giving answers**. It reflects three foundations of lean management: that everyone, at every level, should build new capabilities; that the people closest to a problem generally understand it best; and that one of a leader's primary responsibilities is to provide effective coaching to their teams. Yet leaders often see their main value to the organization as providing answers—indeed, some may think that's what coaching means. Learning how to listen, reflect, and trust in the team on the ground takes practice and time, but ultimately some of the most successful leaders let go of the idea that they should be at the center of problem solving. One senior executive at a large US company told us that she was willing to let her team try their ideas out—"so long as I'm there to give them the guidance they'll need to get to the real solution." She eventually realized that her questions were more valuable than her answers, but it took coaching and repetition for her to get there.

The second shift, **digging for root causes of problems** rather than looking for quick fixes, recognizes that when problems aren't fully solved they inevitably return—creating still more waste that the organization could have avoided. But the discipline and time required for root-cause problem solving are demanding for busy leaders, who may be tempted to redirect the effort toward taking actions with more immediate payoffs. As a utility construction-and-maintenance supervisor put it, "Every minute that my team isn't working on their service calls is work that they aren't getting rewarded for." But demonstrating what it means to eliminate a problem rather than paper it over is an essential form of role modeling. And one that the utility now incorporates into everyone's performance-development plans, so that frontline staff and managers are recognized for solving problems and leaders are recognized for building people's problem-solving capabilities.

The third behavior involves **connecting the future to today**—not by making grand pronouncements, but by translating the organization's

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Exhibit   **Three fundamental behavior shifts are essential for leaders.**

From

Providing the right answer	→	Asking the right questions
Looking for immediate fixes	→	Digging for root causes
Setting general goals for everyone to follow	→	Connecting the organization's goals to individuals' work

To

purpose and business objectives into practical targets that people can work toward each day. That constant cycle requires more than simply setting targets: it requires leaders to understand and explain how their people's work contributes to the organization's ambitions. And they must understand their people's goals as well, recognizing that work is more engaging when it has meaning to the individual. One senior vice president noted, "Seeing that our people really wanted to be proud of what they were doing for our customers was really eye-opening for a lot of our managers. They realized that they could explain our new way of working not only as making a better product but also as creating more ways to do right by our customers. Reaching this point was hard but worth it."

Indeed, the challenge is to make these behaviors feel second-nature to leaders who have spent entire careers leading very differently.

How to build better leaders
Building understanding and conviction is a personal journey for each individual leader. That said, several experiences can help leaders both envision the future and harness the will and skill to change.

Understanding the need to change
Many organizations use external or internal go-and-sees to help leaders see the potential of a transformed organization and how it differs from their current environment. However, these visits often focus only on the behavioral shifts that are happening at the front line, when an even more critical step is to help senior leaders understand how and why they must change their own behavior in order to sustain and amplify the change they want to see. One transformed company now initiates every executive-learning journey with a diagnostic on its current leadership performance, providing an evidence-based analysis to show leaders how well they are setting

direction, solving problems, and developing team members. This builds a much greater conviction among the leaders to use the new management concepts in addressing problems in their own work.

Helping leaders learn
Once leaders are ready to change, they will need support to build the skills and capabilities required of successful leaders. Most organizations develop structured learning programs on leadership to address this need. Adult learners typically retain roughly 10 percent of what they learn in lectures but two-thirds of what they learn by doing, so it is important that these programs include a mix of learning experiences. One organization has therefore developed a structured learning program for leaders at all levels, from frontline supervisors to top executives, incorporating prework, group learning sessions, and fieldwork supported by experienced internal coaches. Another offers senior leaders access to a coaching pair—one with technical expertise and another with an executive coaching background—who work in tandem to support each leader through on-the-job coaching in priority areas.

Building a supporting infrastructure
Once leaders have made the initial steps toward leading in a new way, organizations must put the infrastructure in place to continually reinforce this behavior. The idea is to create transparency into whether leaders are spending their time in a way that is aligned with desired principles and behaviors. Additionally, organizations often need to adjust their formal talent system, particularly competency models, performance ratings, leadership-development programs, compensation, and promotions, to ensure that they are rewarding desired leader behaviors.

Standard performance indicators remain important for meeting practical business targets. But over time, behavioral indicators—such as

how well leaders develop their people—are what enable the business to make good decisions about what its targets should be. With the view that ideal behaviors drive ideal results, a large conglomerate restructured its performance-management process such that 51 percent of a leader's annual evaluation is informed by behavioral elements. This same company implemented a monthly all-employee pulse survey to understand whether every employee was receiving the agreed standard of two hours of one-on-one coaching each month, and whether it was meaningful. The results of this survey are now regularly discussed in monthly management meetings.

Following good examples

Finally, to sustain their new behaviors, leaders should see their role models behaving differently, too. In a large organization, the CEO is an obvious focal point, but not every CEO will adopt the new behaviors right away. Indeed, as important as the CEO's support is, a recent McKinsey survey underscored that the real differentiator in successful transformations is the engagement of line managers and frontline employees, not the CEO.[2]

Instead, leaders may find their role models in many places—among their own senior leaders or teammates who are going through the same transition, in a frontline leader who was among the earliest to test and adopt the new behaviors, or among their external network. While each individual leader will need to connect with role models who are personally inspiring, organizations can increase the likelihood of a match by identifying, supporting, and celebrating potential role models.

Practically, this can take many forms—asking leaders who are embracing the new form of leadership to participate in town halls or leadership panels, investing in senior leaders early to

tap into their formal influence, and including great leadership stories in company communications. One North American company has pushed this idea even further by initiating leadership-transformation deployments at the vice president and director levels. These leaders learn to apply the core concepts to their own work before cascading down within their organizations. As a result, the leaders are already role models for supporting broader transformation.

■ ■ ■

Leading an organization through an extraordinary change takes more than simply telling people what to change. It means embodying that change in a way that few leaders have been trained to do. But learning how creates an organization that can keep evolving and improving over time. ■

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[1] Michael Bucy, Stephen Hall, and Doug Yakola, "Transformation with a capital *T*," *McKinsey Quarterly*, November 2016, McKinsey.com.
[2] "The people power of transformations," February 2017, McKinsey.com.

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Continuous improvement—make good management every leader's daily habit

Continuous improvement at scale—across a whole enterprise—requires management discipline at scale. At a few organizations, digital innovation is helping managers make a daily habit of good discipline.

Andy Eichfeld, David Golding, David Hamilton, and Kathy Robinson

Think of the last time your organization made a real effort to instill a continuous-improvement culture, whether in a plant, function, or more broadly throughout the business. Think of the investment and effort that went into identifying the first wave of improvements, and changing how people work and leaders lead every day.

How much commitment did it take—of time, money, human energy?

How much did performance improve after the first wave of changes? Is it still improving today?

How many managers and senior leaders changed their daily routines? How many reverted to their old habits?

The hope for any organization is that instilling a continuous-improvement culture becomes a catalyst that makes further improvement easier. But even organizations that have spent many years successfully investing in continuous improvement are telling us that they are not achieving the ongoing, incremental impact they want. The reason? Their leaders and managers haven't fundamentally changed how they lead and manage.

Identifying what managers should do on a regular basis is straightforward. If you ask any group of people about the best managers they've encountered, they'll typically start describing the same characteristics. Essentially, good daily management rests on a few basic disciplines: understand how people are actually delivering for customers, give people regular feedback and coaching, teach people how to solve problems, and create a physically and emotionally safe environment where people can engage in meaningful dialogue about their work.

Indeed, a recent survey of 189,000 people at 81 organizations, each with 7,500 to 300,000 employees, underscored the importance of these principles. Four leader behaviors—be supportive, focus on results, seek different perspectives, and solve problems effectively—accounted for almost 90 percent of the variance in leadership quality between strong and weak organizations. And, as many organizations we have worked with illustrate, the more consistent leaders and managers are in these behaviors—in other words, the more they turn the behaviors into a new standard for how they work—the more continuous improvement they are likely to achieve.

On the ground, these organizations look and feel different from their peers. Their people collaborate much more often, and much more effectively, because they know what they're working toward and why. Every person has a deep understanding of how their daily activities contribute to the overall goal or strategy. There's a confidence that people can rely on one another to ask questions and contribute ideas.

That's not typical yet of most organizations that have attempted to instill continuous improvement at any meaningful scale. The uncomfortable truth is that few leaders and managers make the choice to follow these behaviors well or consistently. And in any one organization, the odds are vanishingly small that many, let alone all, leaders and managers are following them well and consistently.

For continuous improvement to take off, the vast majority of management must consciously work together, as one very large team, to execute these disciplines every day as "leader standard work." We'll highlight observations from two organizations that are trying new approaches to overcome this fundamental challenge: one of the world's largest banks, and a multinational food manufacturer with more than 100,000 employees. Both are tapping into the new power of digital and analytics to help large groups of leaders internalize the routines and habits needed for continuous improvement at scale.

Four leader behaviors—be supportive, focus on results, seek different perspectives, and solve problems effectively— accounted for almost 90 percent of the variance in leadership quality between strong and weak organizations.

Turning new behaviors from burden into boon

If organizations know that these leadership disciplines are instrumental to their long-term health, what's getting in the way of actually doing them?

Part of the answer is simply that few sponsors of continuous-improvement transformations recognize just how hard these changes are. Instead, they make an implicit, conflict-avoiding assumption: that "leaders" should be able to figure out how to adjust their routines and habits once they become aware of the promised benefits for them and the company. They can internalize these new routines and habits while paying 100 percent attention to everything else that comes their way, too, such as the new product launch that's run into problems, the acquisition that needs to be integrated, or the new CFO who wants a new set of monthly reports.

As a result, the effort to learn and practice these new routines becomes something for leaders and managers to do in their spare time. That's a new hobby, not a new habit. And without a clear link between the new behaviors the company says it wants to see and the business results the leaders are expected to achieve, the vast majority of leaders gravitate back to their old ways.

The bank and the food company both recognized that they had to make the new behaviors easier for their leaders to keep following. Each created a supporting leader-standard-work infrastructure to help clarify what the leader's priorities really are—while, equally important, helping the organization understand how well the leader is doing at fulfilling them. Leaders throughout the organization saw their peers and mentors changing as well, creating further reinforcement. Over time, the behaviors become so intrinsic to the job that leaders stop seeing them as anything separate or additional.

Building better leaders everywhere

At heart, leader standard work comprises four fundamental elements that an organization tailors to its needs.

1. Define what leaders do—every day

Because the expected behaviors aren't new, what differentiates organizations is how they make the behaviors pervasive. They start by defining very precisely what the behaviors involve, on a practical, day-to-day basis, for all levels. At the food company, for example, a plant manager follows a pattern each day (exhibit).

That's a lot of her day. Top organizations understand the implication: if leaders are to do all of these new things, they'll probably have to stop doing some—or even most—of what they're doing now. What follows is a difficult round of trade-off discussions in which the top team commits to protect leaders' time for fulfilling the new set of standards. They do this by making explicit, synchronized calendars for all managers and leaders, sometimes referred to as a WILO or MILO ("week in the life" or "month in the life"). For each leader, low-value activities, such as information-sharing meetings, are either canceled or replaced, so that the leader can instead devote the time to engaging in real performance dialogues with his teams, solving problems, improving standard work, building skills, and providing coaching.

At the bank, a new digital app makes adhering to these behaviors easier while also reinforcing accountability in real time. Innovative smartphone applications, meanwhile, build activities such as coaching sessions into the executive's calendar and the team member's development plans. At the end of the session, the app prompts the coach and team member to record how the session went against a set of best-practice questions. If the executive starts missing sessions or if team members

Define what leaders do—every day. Start by defining precisely what the behaviors involve, on a day-to-day basis, for all levels.

A day in the life of a food-company manager
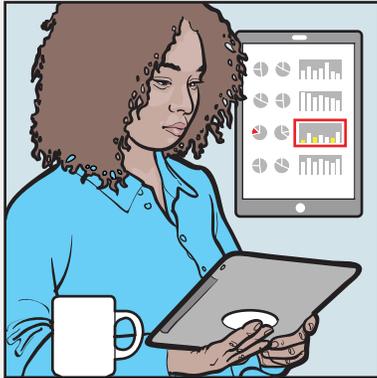
1. The plant manager starts her day by reviewing the overnight and previous day's production, quality, and maintenance reports

2. She joins production manager and frontline supervisors for a walk-through of shift change; departing shift supervisors walk floor together, noting production-line condition and performance

3. Shift huddles begin; plant manager visits different department each day to get deeper understanding of issues

4. Most issues can be resolved without her help, but some involve other departments, so she marks them down for weekly huddle; she also notes coaching opportunities for one-on-one coaching with direct reports

5. Attends cross-functional problem-solving session to address recurring maintenance issue; team analysis during huddle found that combination of a process with recent changeover produced unintended consequences

aren't getting a lot out of them, a senior leader can see the gap and help the manager solve what is getting in the way of completing the leader standard work.

2. Help leaders use their time effectively

But just freeing up leaders' schedules isn't enough: a leader who dutifully "goes and sees" how her teams are working without understanding what she's seeing can't add much value. Instead, leaders need better information so they can develop deeper insights.

Companies are generating terabytes of data, but leaders struggle to find the most important nuggets. Rationalizing the data to the few critical metrics that really matter for performance, and reporting them on a simple dashboard, allows leaders to prepare more quickly and thoroughly for every interaction. Similarly, creating transparency into the commitments leaders are making to their teams and the effectiveness of them allows leaders to focus on a few things with each and every interaction with their team. There's an enormous difference between leaders who walk the floor and leaders who walk the floor with intent.

Making insights portable produces even more impact by allowing leaders to engage in better real-time discussions. The food company is now transitioning to tablet-based reporting, so that executives can easily analyze data during their visits rather than send a flurry of emails after returning to their desks. Site visits are now more purposeful, giving executives updated information at their fingertips in a matter of hours instead of weeks. Moreover, teams now receive the updates in time for their daily huddles and ahead of their regular problem-solving cycle instead of being informed only after performance dips.

3. Double down on continuous improvement

The trouble with defining a new standard of behavior is that it can quickly congeal, impeding

the operational flexibility and faster information flows that the behavior is supposed to support. Accordingly, part of the standard needs to be an expectation that the standard itself must be continually examined and improved (see sidebar, "Pause and take stock of 'leader standard work' every few months").

For the food company, that meant refining how leaders coached frontline managers. Early on, the leaders congratulated themselves for the impact that frontline problem solving had in reducing machinery breakdowns and plant downtime. But the early successes quickly plateaued, and frontline managers and staff both started to see the problem-solving sessions as empty rituals.

On further examination, the company recognized that the issue was not with the frontline staff or managers: it was with the leaders further up in the hierarchy, who were learning how to ask the right questions and coach effective problem solving. Once the leaders engaged more fully in teaching the behaviors in depth—such as training frontline managers to see opportunities in metrics that were stagnant, rather than only those that were declining—problem solving became deeper and the solutions that resulted became more permanent.

The 10 percent reduction in downtime achieved in the first year became a 25 percent reduction in the second year. All production employees and all layers of management now use the same digital app to support their problem solving, allowing leaders to measure the velocity and effectiveness of their problem solving, with full transparency into the problems each team and leader is solving—and thus how they are driving the performance gains.

4. Change isn't just for everyone else—it's for you

Leaders often seem to believe that change is for other people. After all, what they've done

throughout their careers must be right, or they wouldn't be where they are today, would they?

But there is little reason to believe that what worked for leaders—and for you—in the past is likely to keep working in the future. Already, leaders tell us that they often feel isolated, that information reaches them too slowly for them to make effective decisions. That can't change without leaders themselves changing, so that strategic priorities flow more quickly down the organization and intelligence about the business flows more quickly up.

That's why leader standard work is so important for senior executives—especially when it operates on a digital platform. First, it provides leaders with

essential feedback on what people at every level are actually doing: what's working now, what could be working better, and what hasn't even been properly tried yet. Those insights are critical to making better strategic and resource-allocation decisions. Second, it guides executives in their own work, allowing them to make better use of their time in solving high-level problems, developing their reports' capabilities, and serving as role models for the rest of the organization.

■ ■ ■

Companies looking to realize the full promise of continuous improvement at scale will need new ways to help entire groups of managers choose to commit to leader standard work. The good news

Pause and take stock of 'leader standard work' every few months

Keeping track of all of the changes happening across an organization that's instilling a continuous-improvement culture—and making sure that they're having the right effect on performance—can be daunting. But over time, it becomes even more important for leaders to see on a macro level where they are progressing and where they aren't. That's why the food company, the bank, and organizations that have been following the new behaviors undertake objective assessments that score the maturity of their behaviors at every level. They deploy teams of unbiased examiners who spend a day or two up and down the management cascade, scoring management practices against databases of benchmarks from world-class organizations.

The resulting reports give leaders and managers a detailed picture of where their organization should make additional efforts on instilling leader standard work, and where pockets of excellence could help raise standards for the entire business. That's a powerful way to find new opportunities to improve. When the assessment is in digital form, the data are even easier to analyze for reflection and follow-up— and the assessment itself becomes easier to conduct on a regular basis, further accelerating the continuous-improvement cycle.

is that a variety of new digital capabilities are emerging with the promise to make it easier for organizations to see exactly how effective their leaders are—and to help them become more effective by reinforcing the behaviors that leaders need to follow. With the right commitment and creativity, the result is a leadership standard that keeps improving along with the organization's performance. ∎

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Getting better than the tools we'd been taught: Lean and people

An auto-industry veteran describes how rededication to lean-management principles—especially to fostering leadership at every level—led his organization to new performance breakthroughs.

Erin Frackleton, Erin Ghelber, and Christian Johnson

Since 1949, Denso has grown from its roots in Japan to become one of the world's largest automotive suppliers, with more than $40 billion in revenues as of the year ended March 31, 2016. Almost one-quarter of that total comes from Denso's North America operations, which includes more than 14,000 employees in the United States alone.

Denso's origins mean that the principles underlying lean management have been a part of the company's culture almost since the beginning—not only in its home country, but also as it expanded overseas. That dedication to lean management led to receiving the Shingo Prize, which was awarded to two of Denso's North America units, one in 2007 and another in 2008.

Don Tracy, an auto-industry veteran who is a vice president at Denso, spoke with McKinsey's Erin Frackleton, Erin Ghelber, and Christian Johnson from his office in Maryville, Tennessee.

McKinsey: *Denso had a long history of applying lean concepts, well enough to be recognized by Shingo. But then the pace of improvement accelerated. Could you tell us more about what Denso did to trigger the sudden shift?*

Don Tracy: Denso had long experience with lean management—it was one of the automotive suppliers that transplanted into North America to supply the big Japanese automakers when they expanded here. Even 29 years ago, when I started at

the company, Denso was already perceived as a leader in applying the tools of lean manufacturing.

At that time, from the director level on up, the leadership was all Japanese. Their early challenge was to empower and engage the workforce in applying *kaizen* principles—meaning continuous improvement—to their own processes.

McKinsey: *That would already have been a major change from the way most companies operated at the time.*

Don Tracy: It was. But in retrospect I now realize that there was a real gap in the development of leaders. Instead, we developed great process managers.

Including me.

Moving into management made me realize how limiting the process focus was: we couldn't get better than the tools we'd been taught.

We'd been in a child-parent relationship with our counterparts in Japan for many years. But your parents can only teach you to tie your shoes

so many times. We wanted not just to follow, but also to lead.

McKinsey: *Was there a moment when the need to become a leader rather than a manager clicked for you? Or was it a gradual realization?*

Don Tracy: There was actually a moment. I knew that I was not comfortable being a manager; something in my core didn't like it. I was managing by results. And, quite frankly, I was expecting a lot of people but not supporting them as much as I should.

I thought I had to answer all of the questions. It's natural as a manager; you want to show your knowledge. But in the back of people's minds, it gives the impression that you don't trust your people.

One day, a person brought a question to me that was really important to that individual, but didn't seem important to me. I wasn't very accommodating.

Later on I apologized, and said, "I really think this is something that you can handle. Just let me know

Don Tracy

Don Tracy, vice president of Denso International America's North America production innovation center, has more than 34 years of experience in automotive engineering and management. After joining Denso in 1989, Tracy assumed a series of managerial and leadership roles at the company's site in Tennessee, particularly in the body-electronics division. He is also responsible for leading the Tennessee site through a cultural transformation centered on changing leadership behaviors and practices. A member of the executive advisory board for the Shingo Institute, Tracy holds a bachelor's degree in management and mechanical engineering. He has been an instructor in the Denso and Toyota production systems both in the United States and in Japan, for both companies.

what you decide." The reaction surprised me—the person's eyes lit up, and the result he achieved was far better than I expected.

This was in November of 2007. From that point on, I realized what I needed to do. I committed to myself that, although I may make decisions on strategy and direction, I'm not going to manage by results anymore. And the results have taken off exponentially. That's the reality.

McKinsey: *How did that realization change how you lead?*

Don Tracy: I did lot of research on mind-sets, especially growth mind-sets versus fixed mind-sets. My old style was a perfect example of operating on a fixed mind-set. In a growth mind-set, you need to push people into thinking on their own and let them struggle.

That led to a question about leadership at the individual level—how to become more of a leader, not a manager of people. In manufacturing, it's all about problem solving. You have to go through struggle to be a learning organization, not just a managing one.

McKinsey: *What did that mean for the organization as a whole?*

Don Tracy: We hired industrial-coaching psychologists to do a 360-degree review for us, followed by leadership-development classes and discussions among top managers. Over a four-year period we have almost completely transformed—we don't know if we'll ever be finished, but we're a much less top-down organization. Our structure has gone from a triangle to more of a circle. We're trying to establish ownership at all levels instead of a hierarchical mentality that tells people to get everything approved by upper management.

We have to empower associates, and as leaders we have to learn how to function and teach. I'm now looking two levels above my position to understand what's expected, and two levels below to train, so my successor comes in with a similar consistency of leadership investment and the whole cycle sustains itself.

McKinsey: *How do you create that infrastructure?*

Don Tracy: I started talking with our HR team, because this is not the sort of change that you can drive into the organization—you have to develop it within people.

We needed to establish a common language about what the organization should do, with training at each level that worked from top to bottom. Our environment is so heavily influenced by top management. People had to feel their engagement, their example.

McKinsey: *How does HR interact with the rest of the organization?*

Don Tracy: The head of HR is part of our strategic leadership team, which meets once a week to talk about overall direction—including leadership transformation. HR's role is critical because they're the voice and advocate of associates at all levels.

For example, if you're serious about adopting a growth mind-set, you start by recognizing that something isn't working well. That's hard—it can feel like you're walking through fire. But you find an insight, make changes, and the situation improves. And morale follows.

But you have to go through the fire first. HR was a great advocate to help us communicate this idea effectively.

McKinsey: *What was the reaction to these changes?*

Don Tracy: Even with a group as big as 900 people, if just 5 people are extremely negative, they can have a big impact, especially if they've been with the organization a very long time. I asked HR, could you help me to help them? There's something they aren't understanding. I want to turn them around. How do we do it?

Their answer: communication, communication, communication. At a general level, we had engagement surveys where I would see specific feedback. And I started taking time to engage with people who I knew were having a negative experience. It took time, but putting myself out there much more made a difference.

McKinsey: *How could you tell?*

Don Tracy: The most vocal person turned into our number-one cheerleader. We recently celebrated a quality breakthrough, and the associates decided to hold a pep rally—something that had never happened before. I now have a video of him running up and down our office during the pep rally waving a Denso flag.

McKinsey: *What challenges do you see for HR and the company coming up?*

Don Tracy: We're a big organization with plants around North America, so it's been a struggle to make sure our policies promote all of these changes. But we're now taking this transformation to our other facilities: Tennessee, California, Mexico, Canada. So, for example, now we want a one-HR policy for all of North America. Our plant-level HR head has just taken on all of North America, so that's his mission.

We really need HR to help us avoid becoming complacent or falling back into a fixed mind-set. And we have to develop our talent. Our frontline associates are functioning at what was once a leadership level, so now we need to give them some more autonomy in order for them to keep building.

And we have to keep being vulnerable—willing to say, "I've made a mistake." That was our catalyst for change. ■

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Bringing out the best in people:
Capability building at scale

At organizations that are transforming themselves through lean management, four success factors make a major impact in helping make capability building permanent.

Stefan De Raedemaecker, Javier Feijoo, David Jacquemont, and Elixabete Larrea Tamayo

Providing good service has never been easy. And service expectations are only rising: unprecedented technological change and access to data have made customers better informed and more demanding than ever, while the rise of social media gives them more power to publicize their experiences—making each customer interaction more important.

As organizations get larger, moreover, the sheer number of customer interactions becomes a disadvantage in that the risk of a customer-experience problem increases. The rapidly consolidating US banking industry is a case study: for 20 years, customer satisfaction at the largest banks usually underperformed that of the rest of the sector.

With services accounting for an ever-increasing share of economies from Canada to China, improving service quality has never been more important to more large organizations. And the way many organizations are achieving this impact—in sectors from banking and retail to government and telecommunications—is by adopting and reinforcing the four integrated lean-management disciplines: delivering value, enabling people, discovering better ways of working, and connecting strategy, goals, and meaningful purpose.

One of the four—enabling people to lead and contribute to their fullest potential—is especially critical in transforming a large organization

at adequate scale and speed, as well as in ensuring that it will continue improving into the future. At its core is a strong focus on capability building at all levels, which then becomes an integral part of how the business operates.

An example is a regional financial institution whose transformation reached more than 15,000 employees over four years. By investing heavily in capability building, the leaders changed the way the organization worked. Faster processing times and fewer errors meant that customer satisfaction rose by 11 points while the company's cost-income ratio fell by 20 percent. At the same time, employee satisfaction rose: the proportion who scored the strength of their affiliation to the company as four or five on a five-point scale rose by 15 percent, to almost 80 percent of employees.

To make these results possible, however, the organization did more than just build the right capabilities, which can fade surprisingly quickly. It also followed several success factors that helped the capabilities persist even after the core transformation work was complete.

The importance of capability building

Why is capability building so important in a services context? Much of the answer concerns variability. In services, the work itself tends to be highly variable—both in terms of content (such as the wide range of questions customers may have) and in form (such as the major swings in demand that may occur depending on the time of day or year). Moreover, providing services usually means relying mainly on people, who are far more variable than machines. This compounded variability can make consistent delivery appear almost impossible, unless people are able to perceive the issues that are produced by variability, react to them, and provide solutions on a continuous basis.

Over the long term, these capabilities become even more important so that the organization can identify new customer needs, take advantage of new opportunities, and create new value. Senior leaders and managers cannot know everything about what their customers want or how their products are doing. The closer people are to the front line, however, the more likely they are to have a real answer—but only if they have built skills in listening to customers and analyzing problems.

Capability building thus involves more than just teaching people how to complete their day-to-day tasks. Instead, it focuses on a broader set of skills that increase each employee's value to the organization, such as learning to reach problems' root causes, or providing effective feedback. With the greater value that more skilled people can create, the organization will enhance its unique competitive position. That means tailoring the capability building to the organization's business context, culture, and needs—especially to the factors that allow the organization to create value.

A Latin American bank, for example, sought to build on its service reputation by enabling employees not just to respond to customer requests, but to anticipate them based on a combination of external circumstances (such as the level of activity in the bank), emotional cues (such as the customer's visible stress or fatigue), and the customer's history with the bank (such as a record of the customer's interactions and their outcomes). For employees to respond effectively from the moment they encountered the customer, they needed greater interpersonal awareness, faster information gathering, and a deeper understanding of the bank's own products and processes. Together these formed the core of a new capability-building program that comprised more than two dozen initiatives, ranging from in-person training

for the front line on how to provide clear product explanations to a new performance-management system and in-house "university." In one year, customer satisfaction rose from second to first place in the market across all three of the bank's major segments: corporate, small business, and retail banking.

Once an organization knows which capabilities it must build, though, the next challenge is to start building them quickly and at scale—two prerequisites for a transformation to build credibility across an organization and sustain its momentum. That's where additional factors come into play.

Four success factors

Those large organizations that have most dramatically accelerated their capability building have integrated four success factors, which together support the transformation and the organization's continued progress once the major changes are in place (exhibit).

Engage every level of the organization

The first success factor concerns the scope of the capability building. Too often, leaders assume that the capability gaps that matter are only at the front line. But in fact, capability building is necessary at every level, all the way to the executive suite. Indeed, with role modeling critical to sustain almost any organizational change, a clear example from the top is usually the most important success factor in a capability-building effort.

Coaching direct reports is an essential skill for every executive, up to the CEO. At a global asset manager, the CEO began convening a recurring problem-solving meeting for the top team, underscoring for everyone in the company the importance both of the new skill, and of capability building more generally.

Support from the next level of leaders, who may head entire businesses or functions, will also be critical for persuading the rest of the

Exhibit

Capability-building programs multiply transformations' effects.

Performance

Transformation with strong capability-building focus
Traditional "quick savings" transformation

Time

Capability-building success factors

- Engage every level of the organization
- Create excitement and pride
- Apply a range of learning techniques
- Institutionalize through HR
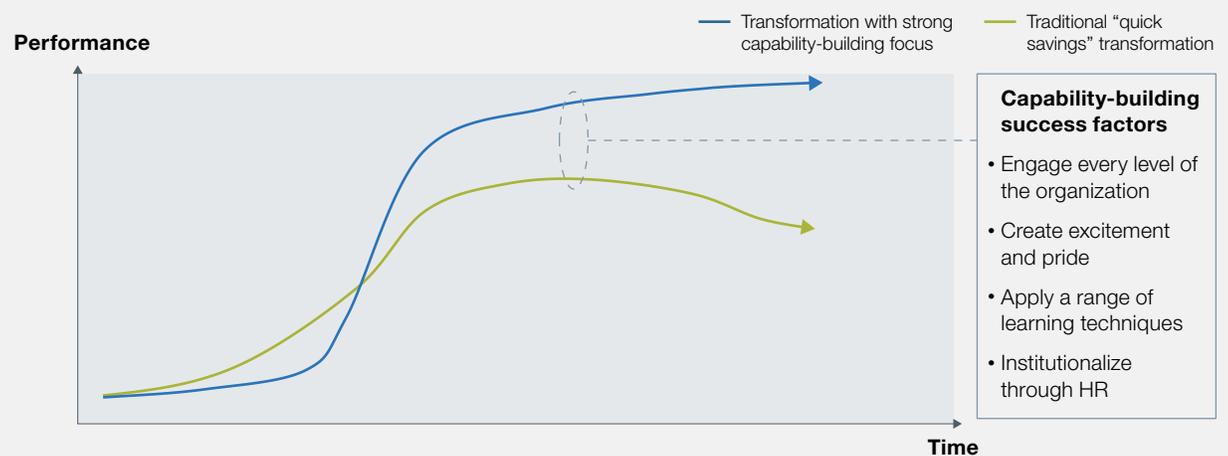
Source: McKinsey Service Operations Practice

organization to embrace the new capabilities. These executives should be involved as early as possible in designing curricula to help their respective teams become more effective. At one US insurer, the resulting development program started yielding results so quickly that the CEO is now accelerating the transformation across the enterprise worldwide.

The middle-management level is where scale starts to become especially difficult. Middle managers' development needs involve more customization than is typical at the front line, but there are so many middle managers that the type of one-on-one coun-seling offered to senior leaders is not feasible. The content differs as well. Like senior leaders, middle managers need to understand the enterprise-level picture, but they also must translate that understanding into the detailed, concrete actions that the front line is taking every day.

Accordingly, the aforementioned insurer's midlevel curriculum centered on these "translation" skills—such as how to analyze the leadership team's strategic messages into operational trade-offs. For example, if leaders announced that they were reviewing the company's privacy policies, a service-center manager would need to be able to recognize the resources implications for her contact-center teams (see sidebar, "The pressure for capabilities"). What could they de-emphasize to

Capability building focuses not just on teaching day-to-day tasks, but on increasing the value that employees can contribute.

provide additional capacity? What would the balance look like between the telephone and instant-messaging channels?

Create excitement and pride

For capability building to endure, people must see it as representing an opportunity for the future rather than a critique of past practices. The best programs therefore communicate a well-defined value proposition that encompasses each level of the organization and reaches well beyond promises of career advancement.

In this type of environment, people see capability building not just as a mandatory box to tick, but as a way to build an individual reputation. Leaders can reinforce the message by celebrating their organization's programs: serving as faculty, hosting graduation ceremonies, and boosting exposure for the program throughout the enterprise. These symbolic measures are especially important in the first few years after launch, when the capability-building program is still developing its reputation and people need reassurance that their leaders are truly committed to it.

Over the longer term, robust capability building can raise the profile of a company as a desirable place to work and deepen the connection people feel to their employer. One of the insurer's ambitions has been to become known in the financial-services industry for its capability-building opportunities, so that it can both retain and attract the high-potential individuals who are most committed to

learning. That message is reinforced at the start of every curriculum the company offers, so the entire organization knows that the program's goal is to make the company an even more attractive place to work. Employees see the value, with more than 90 percent of participants saying they are satisfied with the program.

Apply a range of learning techniques

Traditional corporate training programs still rely on classroom learning, even though researchers have long found that the classroom alone is a poor fit for adult learning patterns. Most adults instead need a mix of concrete experience, reflective observation, abstract conceptualization, and active experimentation.

In practice, this means that as much of the learning as possible should occur in the actual workplace, ideally based on actual work during the course of the workday. Leaders, managers, or even peers can work with the "student," providing immediate feedback as he or she practices the new skills—such as at a multinational retailer, where each store manager now confirms standard procedures with employees while they are performing the relevant tasks. The approach works for virtually any skill, ranging from how to handle a particular type of customer request in a store to how to provide coaching for senior executives.

When "sit withs" such as these are not possible, capability building works best in settings that resemble the actual work environment as closely as

possible: an office or retail floor, for example, rather than a classroom. These surroundings allow for realistic role playing that tests real problems in the workplace. Indeed, a model setting can allow people to envision solutions that might not seem possible under the constraints of their current offices.

One European company with more than 50,000 employees built an advanced "model office" to increase the capabilities of about 3,000 leaders and managers, who are overseeing the company's transformation. The office uses actual company data to set up real problems that particular regions or businesses are facing—and that participants learn to solve over the course of their training.

As people progress through each module, the underlying IT system replicates the work environment by generating emails setting up realistic scenarios for role-playing exercises. Participants then use the lean-management techniques they are learning to understand and address the issues and to think more critically about the matters they deal with every day. Once they return to their roles, program graduates report that they can recognize difficulties at a far earlier stage and have a far easier time thinking of solutions.

Institutionalize through HR
The final step is to embed capability building in HR processes so that they become part of the organization's culture. A financial-markets company started by redefining required competencies and skills for all leaders, including problem solving, daily-meeting facilitation, and coaching, with personalized follow-up from HR. In parallel, HR revamped the company's compensation systems to reward capability-building efforts and progress, with lean-skills development

incorporated into performance objectives for all employees. Over subsequent years, the changes made lean management so fundamental to the organization that it became simply the way it operated. The impact is visible through almost every measure: volume of completed work increased by 30 percent and errors fell by 80 percent, while client and employee satisfaction both rose by more than 10 percent.

Finally, the regional financial institution mentioned previously illustrates how the four success factors come together. The CEO launched the company's transformation by describing how he wanted everyone—including him and his leadership team—to learn new approaches for understanding and acting on customer expectations. The core of the new capability program was squarely in the middle of the organization: in addition to 200 "change agents," 500 middle managers went through intensive capability building. The organization also developed a new internal brand, supported by a comprehensive communications platform encompassing all media— from wall posters to sophisticated video presentations. Their collective message emphasized what teams were achieving with their new skills, and thereby generated new demand for the changes. As the program expanded, the company built an experiential-learning center that could train about 1,000 people per year. Company leaders now require all managers above a certain level of seniority to complete the program, which certifies them in their new skills.

Four years into the program, the changes have helped increase the company's return on equity and cement its leadership in customer services in its market.

■   ■   ■

The experiences of these organizations demonstrate what companies can achieve when they build their transformations around the capabilities that their people need in order to make full use of their talents. Once people see the value they can create, they engage more deeply in their work in ways that give an organization not just short-term performance, but the long-term flexibility and resilience that are essential to thrive over the long term. ∎

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A package full of change:
An interview with Ian Andrews of Commonwealth Bank of Australia

The fast pace of change in financial services can whipsaw frontline employees. One bank has responded with a new approach that makes change easier and faster for people to absorb.

Christian Johnson and Jonathan Michael

In a strong banking environment, Commonwealth Bank of Australia (CBA) outperformed the larger market: as of December 31, 2015, the retail-banking business's profits had grown by 8 percent since December 31, 2014.[1] A fundamental reason for this achievement is the bank's customer-service performance. According to Roy Morgan Research, an Australian market-research company, CBA's customer-satisfaction scores rose from the lowest among the country's four largest banks in mid-2011 to the highest in early 2013—and by May 2016, CBA had held the number-one rank for 12 consecutive months.

But the battle for sales and service leadership in Australia's financial-services sector remains fierce as customer expectations evolve and competition intensifies. In this mid-2016 interview, Ian Andrews, CBA's executive general manager of group sales and service, discusses how these forces have promoted a new approach to help the organization evolve more quickly, starting with the front line. Mr. Andrews spoke from his office in Sydney with McKinsey's Christian Johnson and Jonathan Michael.

McKinsey: *How do you see the standard for sales and service leadership evolving, both at CBA and across the financial-services industry?*

Ian Andrews: Over the last ten years, we've worked hard to develop our sales and service practices across CBA. But to remain in a leadership position in the industry, it is important to continually engage with customers, understand their expectations, and improve our service accordingly. The challenge now is to respond more deeply to the new, more dynamic ways customers want to engage with us, including mobile and digital channels.

This is really a challenge in our experience with the finance industry. You have to deal with changing customer expectations and new competition, whether from well-established organizations with large client bases or fintech start-ups. This all adds up to more complexity and competition, so we're undertaking a major transformation that will allow our operating model to evolve more rapidly.

Our expectations for leadership are becoming much more complex as well. At every level, our people will need stronger commercial acumen to maximize the insights created by our new tools and resources. And they'll have to become more agile as we adjust how we deliver change in response to market dynamics.

McKinsey: *What are the most important changes in customer expectations?*

Ian Andrews: They fall into two categories. The first concerns how customers want to deal with us. That's largely a matter of achieving the right balance between assisted interactions—whether face-to-face, over the phone, or via instant messaging—and unassisted, digital interactions. We need to know when customers want each type of interaction and what features they are looking for. The second category arises from our broader role in supporting people's financial well-being, ideally through relationships that last a very long time.

McKinsey: *As some of these larger changes start to take hold, what does CBA's leadership see as the top changes financial institutions must make in response?*

Ian Andrews: Traditionally, financial-services organizations—particularly banks—were product focused and channel focused. The focus is now more customer-centric. This requires the whole organization to operate more cohesively in delivering true value for the customer, when and how the customer wants and expects it.

McKinsey: *How does an organization make that degree of change happen?*

Ian Andrews: Previously, we delivered each program by itself, with its own change plan, its own communications plan, and its own definition of success. But we knew that rolling out several large programs that way in rapid succession would create too much complexity for the front line, reducing the odds of reaching our goal.

We decided instead to pull major initiatives into single "packages of change," each around a core theme. That way, from the frontline perspective, the program would feel like a single, predictable piece of change rather than multiple disparate, overlapping changes. At the same time, we developed a new governance process to ensure that the narrative explaining the change package would support the theme and align with our strategy. We also give careful consideration to which leaders should deliver the narrative, so that everyone hears it from someone they know and believe in.

McKinsey: *What goes into a package?*

Ian Andrews: Each package addresses all of the distribution channels—branches, call centers, digital operations. It provides a complete set of

Ian Andrews

With more than 20 years of experience in banking, Ian Andrews assumed the title of executive general manager of groupwide sales and service at Commonwealth Bank of Australia (CBA) in 2014. Earlier in his career, he served in a variety of leadership roles at CBA, as well as St. George Bank and Bankwest. He holds a master's degree in leadership and management from Curtin University.

transformation elements covering everything from transaction-migration initiatives and new report templates to new tools and technology. The packages also include capability training for frontline sales and service personnel, and any necessary sales-operation changes.

The right timing for our packages is critical, too. We now aim to deliver two major packages a year, so each time we need to make sure that there's sufficient capacity at the front line to absorb the package. A validation process follows each rollout—first, a quick self-assessment by the business of how well it received the package, and then an annual reassessment of how well the adoption of all changes has gone. If there are areas where adoption is lagging, we provide support and allow a reasonable window of time for the business to remediate. And if there are widespread adoption problems, we will defer future change packages until adoption has reached the right level.

McKinsey: *So if I'm on the front line at CBA, how does this process feel?*

Ian Andrews: Let me give an example. Our next change will introduce a number of new customer initiatives, including enhanced customer-analytics capabilities and improvements to technologies delivered in earlier packages. Historically, we would have delivered most of this scope independently, each part with a whole supporting change program. That would feel overwhelming and disjointed. Instead, we have crafted everything together into a single package.

For the front line, the message is fairly simple: "We've given you new technology to help you have better conversations with customers and to better identify their needs. On top of that, we're launching new offerings to help you satisfy important customer needs when it matters most to them." We also see a huge benefit in overtly calling out that the package is aligned with and built on capabilities introduced in the preceding package.

McKinsey: *And those involved see the package as one set of changes rather than two?*

Ian Andrews: Yes. People see the continuity among the various components, so it makes sense both to them and to their customers. Over time, this type of experience makes change much easier—as a frontline worker, you're not having to switch your mind between different communications coming in different formats, with different focuses and different terminology.

All the packages follow the same methodology in communications format, language, look and feel, and training materials, as well as in how the change is delivered and embedded. One of the real benefits we're striving for is the sense of familiarity that rolls through with each package. It should feel like there's less change happening to you because the change is more consistent and of a higher quality.

McKinsey: *With a cadence of two major packages a year, how do you decide what to include in them? Do some changes still move forward separately?*

Ian Andrews: Yes, some do—there's a limit to how large a package can become, and of course some initiatives may be time sensitive. Through experience, we've come up with a short list of criteria to guide our decisions. If a change involves a serious shift in mind-sets or in how we work with our customers, it's more likely to be included in a package. Likewise, if the change will affect our entire organization or even an entire channel, a package is probably the right answer. On the other hand, narrower changes targeted to a particular product or campaign may be able to proceed on their own, especially if they don't involve interdependencies with other changes we're making.

McKinsey: *What sorts of capabilities does an organization need to make this new approach work?*

Ian Andrews: The most important capabilities center on managers supporting people through the changes—making sure that the rationale aligns with our long-term strategy and that the narrative resonates with the front line, so everyone can see how the packages ultimately support the strategy and satisfy our customers. But we've also had to become far more effective in many other respects, such as in building the right training programs, designing the rollout process, and identifying the metrics that will reinforce success.

We've had to develop stronger capabilities in our frontline leaders, who are dealing with a lot more complexity than they used to. And then there are the technical capabilities involved in deciding which initiatives should go into a package, for what reasons, and what the sequencing should be.

McKinsey: *How do senior executives feel about bundling their initiatives into packages?*

Ian Andrews: When we first introduced this concept, everyone understood the idea and saw its benefits. But when we started the practical application, we had to deal with the personal connection people naturally have with the projects they sponsor. We had some tough discussions on how to prioritize collectively rather than individually, putting aside personal agendas for the good of the whole.

McKinsey: *Many organizations ask whether it's better to rely more on a parallel change organization to lead the way in delivering change or to rely more on line management. How did CBA make that decision?*

Ian Andrews: Although in some respects we ended up with both, from day one we believed that for change to be effective, it must be led through line leadership. As a practical matter, our view was that the only way frontline people will actually adopt change is to see and hear it from the leaders they know. That's far more credible than hearing it from a head office.

But we're also conscious that frontline leaders already have very busy, complex roles. To make the delivery of change as easy as possible, we've centralized and "industrialized" all of the practices and resources frontline leaders can make use of. That way, they can focus on leading and owning the delivery process.

McKinsey: *What are some of the surprising things that CBA learned along the way?*

Ian Andrews: It was important to get very specific in explaining how the new approach would create value for everyone in our organization and our customers, as there can be levels of resistance to change and of commitment to legacy practices. But getting all of that right—the messaging, the narrative, the engagement from people—creates a

multiplier effect. The benefits are far greater than what anyone would achieve through individual initiatives, with potentially contradictory messaging and processes.

McKinsey: *What is the biggest change that people working in a branch or contact center see in how they're working with their customers?*

Ian Andrews: I think there are two things. First, a shift in mind-set from "What products interest this customer?" to "How do I better understand this customer?" The second big shift is from a product point of view to a service point of view. The idea is not just to provide what customers want but to enable them to bank how and when they want, through digital means or assisted channels.

McKinsey: *How has this experience changed your views of organizational transformation?*

Ian Andrews: Traditionally, many change programs defined success only as the handing over of the program or work following implementation. The leadership might see the logic of how all the pieces of a program came together, but that connectivity may be less obvious further down in the organization.

Now we define success by the value that change generates over an extended period of time, beyond the implementation date. That means we focus much more on how we deliver and embed change

at every level—especially on how effectively leaders communicate the "why," so that the front line adopts the behavioral changes and can see the benefits that are being delivered to customers.

McKinsey: *Frontline employees really want to see that customer benefit, don't they?*

Ian Andrews: Organizations often underestimate how strongly their people identify with their customers. I think if you ask the majority of our frontline staff what brings them to work every day, they'll show a strong sense of pride in their ability to deliver good outcomes for their customers. If they can't see that clear customer benefit, they could resist the change in the belief that in doing so they are continuing to help their customers.

McKinsey: *How has the past year changed the way you lead and how you want to lead in the future?*

Ian Andrews: My position has no direct authority over any of the businesses undergoing change— I can't compel anyone to do any of the things that I am charged with doing. I've had to be very conscious about influencing rather than directing, accepting people's diverse viewpoints and opinions, and being very patient. But at the same time, you need to have the confidence to remind people of what we're trying to achieve collectively.

"I've had to be very conscious about influencing rather than directing, accepting people's diverse viewpoints and opinions, and being very patient."

McKinsey: *How is CBA building on the momentum?*

Ian Andrews: Right now, we're reviewing what we've learned so we can refine the model and become even more disciplined, while also allowing natural evolution to occur in the larger business as we deliver change that will be sustainable. I know I've had to change my own approach over the last 12 months—I'm constantly reviewing how effective I'm being in leading this particular methodology. So it's a continual cycle of action, assessment, and improvement, both as individuals and as an organization.

McKinsey: *What parts of this process have been most rewarding to you?*

Ian Andrews: It's when I visit a branch or contact center and have a candid discussion with people who don't quite know what my role is, and they tell me about the benefits they're seeing or what they can do now for their customers that they couldn't before. Our frontline staff in branches and contact centers now talk about seeing the connections between the components of a package or even among various packages and about how the packages add value to customers. And people tell me what isn't working well, too. That kind of account of what you've done right and what could be improved is really what's most rewarding. ■

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[1] Growth in net profit after taxes.

Christian Johnson is a senior editor in McKinsey's Hong Kong office, and **Jonathan Michael** is a partner in the Sydney office.

Why leaders do it:
The value of a single enterprise culture

As an organization's management systems become more mature, leaders expand lean management's reach well beyond parts of the business that resemble the assembly lines where lean ideas originated. If anything, lean management proves itself even more valuable when it tackles some of the most complex areas of modern enterprise. And doing so creates a single culture that guides how the entire enterprise does its work.

For example, improving operational effectiveness and client experience has been especially difficult in the B2B world, which often revolves around specialized expertise. "Transforming expert organizations" (p. 90) recounts how accountants, securities analysts, electrical engineers, and other experts can learn to work far more effectively with one another—and actually increase the value of their expertise. In "A new order for law" (p. 97), senior leaders at a global law firm discuss the transformation of what traditionally had been one of the most inflexible, risk-averse businesses into one that can withstand unprecedented disruption.

Meanwhile, "Purchasing power: Lean management creates new value in procurement" (p. 104) illustrates the impact that lean ideas can produce even in functions whose expenses are already low. With little fat to cut, lean instead shows its real worth: freeing people to use their skills where they can make the most difference. "Transforming HR and culture: An interview with Banco de Crédito del Perú's Bernardo Sambra" (p. 111) shows how lean management not only increased a bank's efficiency but also created a better environment for people. And the concluding article of this compendium, "Mining for leadership with lean management" (p. 116), interviews three leaders who never expected that lean could achieve lasting results in a business subject to extremes of variability. One of the most important lessons learned was to keep improving how they and their colleagues lead, in a way that's changing the whole organization.
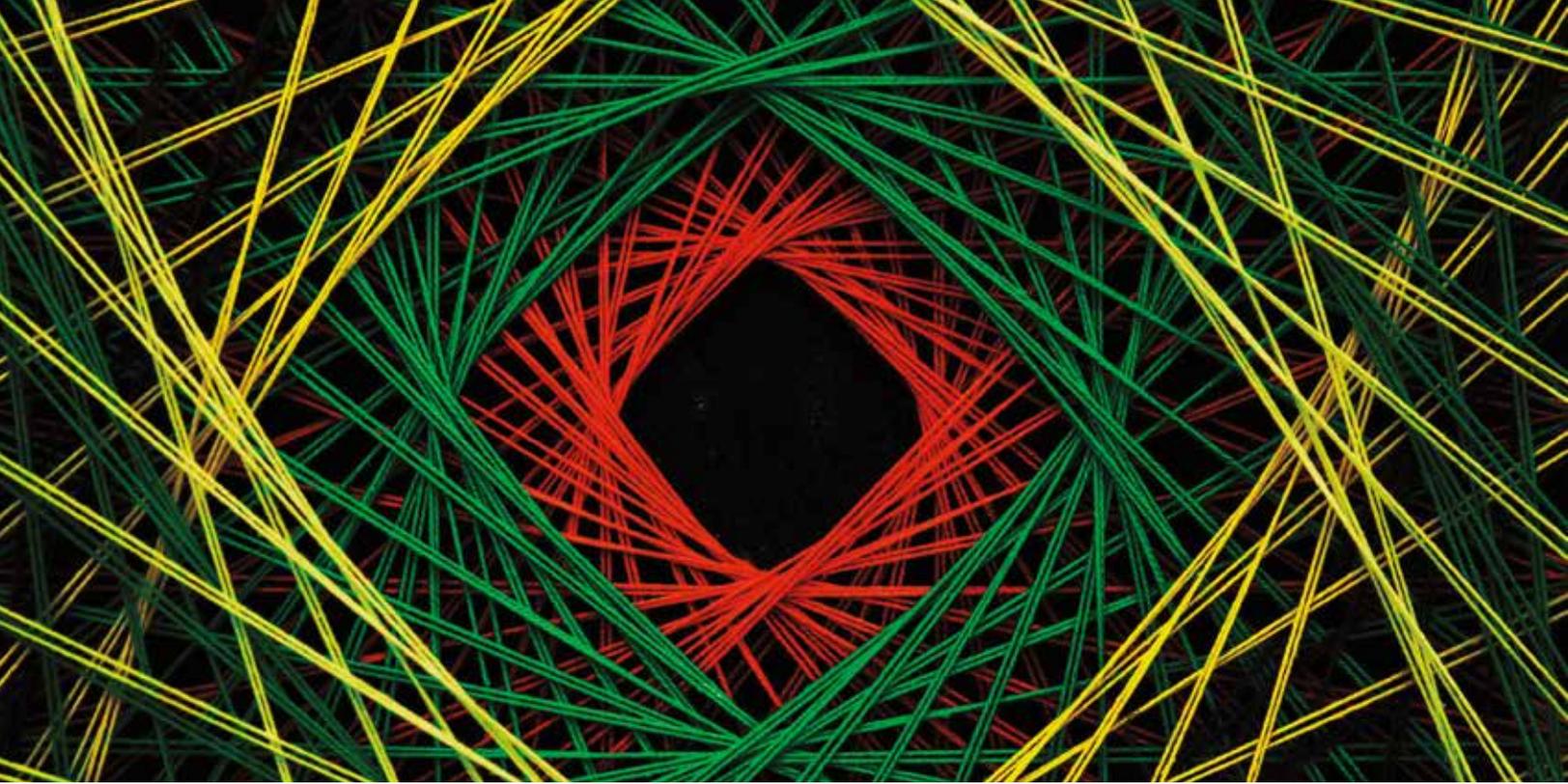
Transforming expert organizations

Improving operations and client experience in B2B organizations is hard because they rely so heavily on highly skilled experts. But those experts can also be the source of a solution.

Albert Bollard, Clark Durant, Rohit Sood, and Matt Tobelmann

Think back 20 years. Buying a mortgage or filing an insurance claim was difficult and time consuming for almost everyone: days of phone calls and appointments, mistakes to correct, and duplicates to send in the mail.

Then a few leading companies started giving consumers what they wanted within days or even minutes rather than weeks. Faster processes also had to be more reliable and easier to understand. And now consumers can file a medical claim or apply for a basic loan with just a few taps on a mobile phone, and check the status at any time with a couple of more taps.

The value these leaders created was vast. For many of them, what made it possible were the four

integrated disciplines of lean management. The combination of delivering value efficiently, enabling colleagues to contribute their best, discovering better ways of working, and aligning strategy and purpose to day-to-day work helped these organizations perform better on multiple indicators at once: shorter turnarounds and increased accuracy and higher employee engagement and faster adaptation to the digital world. Early leaps in performance were followed by consistent increases year after year.

What kind of value could B2B and other expertise-heavy organizations—from law firms or utilities to financial-information providers and risk-management departments—create if

their processes were as transparent, reliable, and time sensitive as these consumer leaders?

Yet even organizations that recognize the threat from potential disrupters—particularly those offering the latest digital tools—often remain unmoved, citing the complexity and expertise that specialized sectors require. "We aren't a factory or call center. Our work requires unique insights from experienced, credentialed professionals. Treating each project as unique is a big part of our value to customers." That, in a nutshell, is why changing expert organizations is so hard. Despite what some may believe, what experts do really is a hard-to-define art—at least some of the time— and that makes experts skeptical of ideas that try to make their work more "efficient."

Nevertheless, there's also a science to expertise. That means that even in the most complex, bespoke projects, a lot of the work is actually standard—or

could be. That's where the insights underpinning lean management can help. The problem is identifying those standard elements, understanding them, and improving them, so that experts can spend more of their time on the art—while clients get an improved experience and the organization can improve its strategy.

Who better to solve the problem than the experts themselves? That's what a few standouts have discovered. Aiming experts' intellectual firepower at the organization's own practices can lead to unexpected operational breakthroughs. A financial-information provider, for example, took only four months to reduce its backlog of documentation issues by about 70 percent, and its time to market by 15 to 20 percent (exhibit).

Engaging experts and helping them work in this new way requires care. But the reward is a business whose clientele get even more of the specialized

Exhibit

Lean management transformed a financial-data provider.

Higher client satisfaction

18–22%

Lower compliance risk

70%

Faster time to market

15–20%

High employee support for new way of working

80%

Source: McKinsey analysis

support they are paying for, along with customer experience that makes them even more willing to pay for it.

The view from the (expert) field

The fundamental change that an expert organization must make is in its experts' perspective. Their perception of themselves as artisans affects almost every aspect of how they, and the businesses they support, usually operate.

'Right' and wrongs

Whether they are securities lawyers or financial analysts or electric engineers, experts are much more likely to identify themselves by their expertise than by their employer. As a result, they're also more likely to pursue deeper expertise for its own sake. For the organization, the danger is that being right about a particular technical point can become more important to experts than solving whatever larger issue the organization is confronting.

Automation lite

For too many companies, "automation" conjures up preconceived notions of blown budgets and intractable delays. But today, advances in technology and nimbler application-development techniques have enabled a new type of automation whose impact is often much greater than its required investment.

One international bank recently discovered how much it could improve just by creating an online tracker for complex deals in one of its portfolios. Using modular application-development tools, the bank designed an app that pulls data from existing systems into a simple grid that shows the current status and sequence of steps for each deal. At any moment, underwriters, relationship managers, product specialists, and other experts could see what stage a deal was in, and where it was supposed to be according to the schedule promised to the client. Basic color coding highlighted steps that were behind schedule (red) or in danger of being so (yellow).

Building the tool required very little with respect to time or funding, but it has already helped cut the average deal's time to completion by almost half. Much of the benefit came from simply making the data visible. It turned out, for example, that the average deal took a lot less time than most people assumed. That discovery alone helped reset everyone's expectations for speed.

The tool also became the starting point for identifying better ways of working: the fact that Deal A was finished much more quickly than Deals B through E naturally led to questions about why, and whether the lessons from Deal A might apply more broadly. But the tool could only start the discussion. To keep it going, experts needed confidence that the company's ultimate goal wasn't to cast blame or override genuine risk concerns. They needed to see and experience conversations that objectively evaluated sources of delay, separating those that added value (because they protected the bank) from those that didn't (because they duplicated other steps or had become irrelevant for other reasons).

At one corporate lender, for instance, experts from legal, finance, and other specialties were so intent on solving problems with their own assessments—which often depended on input from one another—that deals would be backlogged for months, even when a borrower's assets and credit history were more than sufficient to justify the proposed credit line. Each group of experts focused on its own domain, with only a weak connection to the client's goal (getting the deal done) or to other groups of experts. From the experts' perspective, the risk of being wrong was far greater than the risk of delay.

The same bias can affect the structure of an entire operation. At a large North American utility, for example, each of its local offices was largely autonomous, with local leaders and "job owners" responsible for allocating work. The idea was that the "locals" had the deepest expertise in their market and geography, and knew their crews' capacity the best. But allocating jobs at the local level left too little flexibility to accommodate natural, systemwide peaks and troughs in work supply and labor demand. Weekly and daily scheduling became highly unpredictable, and performance varied enormously: output in one area could be 50 or 100 percent higher than in another area, even with the same labor capacity.

The expertise silo

Over time, an expert's isolation can become self-perpetuating. Because expertise is difficult for outsiders to understand, only experts can credibly lead experts. But their value to the organization as experts leaves them less capacity and fewer incentives to focus on general management. Instead, they focus on resolving the most difficult and complex issues that arise. Meanwhile, capability building usually follows an ad hoc apprentice-ship mode—which is time consuming yet leaves little room for cross-training—and automation tends to be minimal (see sidebar "Automation lite"). The result is not just a silo but a hardened one.

That isn't good for the organization—or even for the individual experts, who often feel frustrated by the bureaucracy they are part of. Continually struggling with antiquated technology, infrequent learning opportunities, and opaque processes takes a toll. And cancelling a vacation because you are the only person with the right expertise to answer an emergency client request is a heavy price for a seemingly guaranteed stream of work.

That dissatisfaction, combined with experts' long-standing role as problem solvers, provides an opening for organizations seeking to transform themselves. By engaging experts in solving a problem that mainly affects them, the organization helps the experts discover new skills and working habits that are critical to untangling the complexity of their work. As the approach progresses, experts become leaders who can develop their colleagues' capabilities, see how their work relates to the organization's purpose, and—most important—deliver better results for customers (see sidebar "One culture, no exceptions").

Testing a hypothesis together

What organizations often discover, however, is that experts at all levels are prone to some of the same basic problem-solving errors that bedevil almost all organizations: superficial analysis, failing to map out consequences, and implementing the first idea that seems to work as the final answer. From entry level to leader, experts will likely need practice in following structured problem-solving methods that are much more likely to result in long-term solutions. A large US-based financial institution provides an example.

The first attempt: Worse, not better

To engage expert financial analysts in problem solving, the first step the institution took was to ask them to identify challenges in serving the relationship managers who were their primary customers. The answer quickly came back:

One culture, no exceptions

Organizations are often tempted to give more leeway to senior experts who resist change, exempting them from some or all of the changes expected of everyone else. It's a dangerous tactic. "One of our managers had a very difficult time letting go of his role as problem-solver in chief. Intellectually, he knew that his team needed the space to practice its own problem solving—and to sometimes come up with 'wrong' answers. But he hated to see what he thought was time wasting," says a top executive at a US financial institution.

"We could see the damage he was creating by the lagging performance of his team. We should have acted right away, but it was only when other teams started slipping in their performance that we realized how he was undermining our whole program. Other managers looked at him and thought we weren't serious about the changes. He finally broke through, though, when he allowed a 'mistake' to continue until he saw the team fix it—and come up with a better solution."

"Correcting errors in data generated by the offshore centers." The institution then pushed the analysts to come up with ideas: "We need your input because only you have the expertise necessary to get to the heart of the problem."

The initial solution was an extra quality-control step to check the offshore teams' calculations. But once implemented, it exacerbated delays and occasionally introduced even more errors into data that supposedly had been double-checked.

The second attempt: Preconceived ideas
Once the shortcomings of the initial attempt became apparent, the analysts' leader proposed a different answer. The problem with the offshore data, in his view, was incompatible IT standards, with the IT platform as the inevitable solution.

Yet this solution was the product of an unacknowledged bias: the leader was aware of certain technical issues that were contributing to slow responses. He therefore defined almost every problem as having IT as its core, so that the solution would be a new IT platform that he viewed as a panacea.

The third attempt: Uprooting the real cause
A new IT platform would have required at least a year to design and integrate. The institution's leaders asked for another attempt, noting that the first two lacked input from either the offshore teams—the centers the analysts had initially targeted as the source of the problem—or the IT staff.

The solution started by bringing representatives from all of the groups involved in day-to-day work—offshore and onshore analysts, IT specialists, relationship managers, and experts from related fields such as compliance and legal—together into a single team, a "virtual" work cell. Their mandate was not just to solve the problem but also to practice new behaviors: reliance on factual analysis, avoidance of blame, and deference to the expertise of the people closest to any given issue. That discipline allowed the team to keep pushing for underlying causes.

Together, they discovered that the data the offshore personnel were using was already compromised even before it arrived. After tracing the data back to a different division in the organization, the team

developed a customized data feed that required very little IT investment and eliminated the need for the offshore specialists to check and adjust the numbers in the first place.

Once the cross-functional work cell had demonstrated its effectiveness, the experts continued to expand on their newfound capabilities. For the first time, they recognized that they were the ones responsible for making their process better—not their managers, or some remote part of IT, or the senior executive team. Process times for projects soon became 15 to 20 percent faster. Error rates fell by about 70 percent. And the work cell identified new efficiencies that freed up more than 15 percent of its capacity, so that later work cells could achieve the same output with fewer dedicated people.

Connecting to the customer

Building on this type of success requires an organization to foster a deeper understanding of the ultimate customer—not just the internal customer the experts see, but the customer the organization as a whole serves. For the organization, that means aligning the interests of the expert, the internal customer, and the external customer all at once.

At a Latin American asset manager, attorneys working in the claims unit helped assemble elaborate paper trails before the company approved routine payouts from investment accounts.

Although the process protected the institution's legal interests, the delays sometimes caused real hardships for clients seeking access to funds, which typically took months to complete.

To persuade the lawyers of the need for change, the company returned to first principles. Everyone agreed that lawyers had a duty to defend the institution from risk. But the categories of risk needed to be broader than the ones the lawyers typically focused on. Long, bureaucratic payout delays posed a reputational risk that, over time, was at least as material as the possible fraud the lawyers were trying to prevent. Moreover, the work they were doing took the lawyers' time away from complex issues that truly required detailed legal analysis.

For the institution, managing risk appropriately meant devoting more attention to the cases that posed the greatest threat of incorrect payment. By reinforcing the lawyers' value to that process, leaders were able to persuade them to adjust their priorities so that smaller, predictable claims could get processed much more quickly—from months down to a few days. The ultimate customer received a prompt payment, the institution received the risk protection it needed, and the lawyers were relieved from work that many admitted was not very interesting.

■ ■ ■

Building on this type of success requires a deeper understanding of the ultimate customer—not just the internal customer the experts see, but the customer the organization as a whole serves.

What if your clients could close their next deal in three weeks instead of three months? And you could give them a completion date with full confidence that your organization will be able to meet it?

What if you could be sure that there would be no compliance surprises, because all of the compliance was already built in to the way your organization works?

What if everyone working on a project—you, your team, your clients—could see the status of every task, continually updated, so that questions could be resolved as soon as they arose? How would that change what you do as a leader?

This journey is not easy. It requires substantial commitment, particularly from the senior team, to demonstrate the value of working very differently. But harnessing experts' intellectual firepower to improve the way an organization does business is far too valuable an opportunity to overlook. ∎

A new order for law

One law firm's story shows how lean management can transform even the most complicated, tradition-bound, and intellectually demanding of businesses.

Alex D'Amico and Christian Johnson

Since 2005, the 900-lawyer, Chicago-based international law firm Seyfarth Shaw has been rethinking how it practices law, applying lean-management principles to create greater predict-ability, transparency, and collaboration—even in highly complex specialties. That experience has enabled Seyfarth to expand the scope of its advice beyond the resolution of legal problems, and now includes improving workflows within clients' law departments and providing training on high-risk compliance issues. Seyfarth has sustained its commitment, winning accolades in the industry and showing unusual resilience through a period in which many storied law-firm names disappeared in mergers or bankruptcies. Over the past four years, the firm's revenues have grown more than 20 percent, and profits are up more than 25 percent.

In mid-2015, McKinsey's Alex D'Amico and Christian Johnson jointly interviewed four members of Seyfarth's management team: Andrew Baker, then-director of legal products and technology; Kim Craig, then-director of legal process improvement (and now managing director of lean solutions); Lisa Damon, a member of the executive committee; and Steve Poor, the firm's chairman from 2001 to 2016 and now chairman emeritus.

McKinsey: *If we turn the clock back a few years, what were some of the challenges that you saw for the legal industry?*

Steve Poor: "Disruption" may be a buzzword in the legal industry today, but not ten years ago.

Firms were growing, profits were growing, rates were growing, and demand was outstripping supply.

That cycle camouflaged a structural problem. Corporate legal departments were facing more demands from internal clients to deliver higher value at a lower cost. As a result, the solutions that general counsels needed were becoming more sophisticated, driven by their desire to become value centers rather than cost centers. Law firms were not meeting that challenge.

One of our clients likes to say that he doesn't buy legal services so much as he buys business solutions delivered by lawyers. His distinction points to a fundamental paradox: How do you raise the value of your services while controlling their cost?

McKinsey: *Within Seyfarth, was there a shared view of where you were competing strategically and where the market was going?*

Steve Poor: Not at that time, no. It posed an educational challenge for us, to help our colleagues see the problem in the same way we did. But it helped that we had already developed an executive-training program with the Kellogg School of Management, which gave our partners a business literacy that law school alone doesn't provide.

Lisa Damon: As a firm, we have always set an expectation that our partners would invest serious effort into their clients. Getting our partners to stand in their clients' shoes extended this idea. We hosted a series of client speakers that included Tom Sager, who became DuPont's general counsel. When Tom described how DuPont was bringing lean ideas into the legal department, it helped our partners see the potential because of lean's focus on delivering value to clients.

McKinsey: *How did you galvanize the leadership team around this idea?*

Steve Poor: We started with two projects. The first was the review process for conflicts of interest—a complex, difficult task at any law firm. It is a high-pressure process requiring accuracy and speed, and it centers on the continual evaluation of client relationships for conflicts that might require the firm to recuse itself. This was a pain point across our organization, so improvement would be highly visible.

The second project focused on a type of real-estate lending in which we were having trouble matching the market rate for the work. The lawyers who specialized in it were a small, well-defined team, so the scope was limited. And if we could help them become more successful, they would help convert their peers in other practice areas.

Once both projects were showing strong results, we started the next partnership meeting by saying, "We are embarking on this journey. We know you're sitting there reading your paper and waiting for this latest management fad to pass. It's not going to—this is going to be part of who we are and what we do as an organization, and here's why." One of our partners spoke about the changes in conflicts, where we reduced processing time by 86 percent and the number of errors by 90 percent. Then a partner from the lending group described how the changes led to better allocation of resources and higher fee recoveries.

McKinsey: *Did anybody say, "That's great for securitization, but my practice area is totally different"?*

Andrew Baker: They did. In fact, one of our early training documents started with a slide saying almost exactly that. And, given the frequency at which we heard that response during the early years, we wanted to address that misconception whenever possible.

Steve Poor: But as we gathered more success stories, we began to eat into the mind-set of "my work is different—what I do is magic." There are moments of magic in the practice of law, which you recognize and celebrate. But unless you can get people to think about it as a process, you can't see all of the steps that make the magic possible or everything that needs to happen afterward to turn the magic into something tangible.

McKinsey: *What was it like to define all of those steps?*

Lisa Damon: So far, we've created "process maps" for more than 500 different workflows associated with legal work. For each type of project, such as a corporate acquisition, we assemble the best practitioners—partners, associate attorneys, project managers, technology specialists—around a table. They come up with a list of all of the tasks involved and estimate how much time each task should typically take. The end result is a form of what lean-management practitioners would call "standard work," setting guidance for what each project should look like.

Andrew Baker: These aren't exact scripts, but they give us more discipline. If our process map estimates that writing a particular contract should take two hours, and an associate starts to think the task will take closer to eight hours, that's a signal to her that she should probably talk to somebody.

Lisa Damon: To avoid that result—and increase quality and efficiency—our process maps include "artifacts" such as model documents, checklists, and the like at each important step in a given process. Of course, we continually curate the process maps based on experience, legal developments, and client-based process improvements.

McKinsey: *How have these maps changed the way you serve clients?*

Lisa Damon: Having standards lets us be much more transparent, because we actually know what it takes to complete a given assignment. They provide more context for everyone involved. We make everything visible to clients through our collaborative technology platform—the to-do lists, the tasks, the status of each item against agreed-upon standards. That way, clients can immediately see the quantity and type of work they must manage, and can adjust workloads among their in-house and outside attorneys in line with strategic, financial, or other priorities.

Andrew Baker: Knowing that a client can log in at any particular point in time and see what's happening is a huge motivator. That transparency creates powerful incentives, which shape the right perspective and behavior.

Lisa Damon: We also go through this process-mapping exercise with our clients. We put our process for corporate acquisitions on the wall and ask the client's in-house counsel to add their activities. Invariably that conversation uncovers huge disconnects within the client's own legal department and between the legal department and service departments. Once these gaps are identified, we can work together to solve the disconnects.

McKinsey: *How did your attorneys react to the idea of being so open about their work?*

Steve Poor: Historically lawyers have not been big on transparency or on standards to guide how they do their day-to-day tasks. But once you open the black box, you and your client can see the same data and the same problems. The conversations become more meaningful because you're working together to improve how legal services are performed.

Andrew Baker: That has led to further shifts in how we run our engagements. The core team

may now include not just a few partners and associates but also two project managers, a data specialist, and a technologist—all of them interacting with the client.

Lisa Damon: The organization has become very flat, because often a secretary knows more about a particular process stage or root-cause issue than the lead partner will. It's an example of "adhocracy," the idea that people have authority based on their actual expertise and knowledge of a situation rather than their title. That lack of hierarchy has become incredibly important to us in reinforcing collaboration. It's an intense sense of cohesiveness; you feel it in the room as people are working together differently.

McKinsey: *That is a big change for partners, no? How did you help them move from "I'm the center of this universe" to "I'm integral, but not essential for everything"?*

Steve Poor: We were fortunate in that our organization has always been relatively flat; our founders insisted that everyone roll up their sleeves and work together. But we also recognized the fear of displacement, which comes from a belief that we lawyers are an artisanal guild. We've had to help our partners understand that following this approach raises their strategic value to the client, because it enables them to help clients solve much larger problems. Clients have more and different needs, and we have more and different capabilities to serve them.

We see the same story replicated over and over again: senior partners who insist on leading discussions, but discover that the people they thought should sit quietly in the back of the room—people such as Kim or Andrew—are actually the ones the client wants to speak with. I won't say that partners come out of that type of experience completely changed, but

they do get a deeper understanding of the different roles we play. And they start to recognize the value that clients put on an entire package of capabilities.

McKinsey: *How would a partner have seen his or her value ten years ago versus today, working in this new way?*

Kim Craig: Many partners told us that they thought the main reason clients came to them was because of their deep expertise, so they worried that asking general questions about a client's business problems might make them appear uneducated.

Andrew Baker: They always want to be Yoda. Our internal training helps partners feel more comfortable asking questions—even outside of their core area of expertise. This has opened up a lot of opportunities and allowed us to better align our services.

One of our apparel-industry clients was having trouble keeping track of what it had licensed to whom in which territory. The more questions we asked, the broader the solution became. While our solution definitely relied on legal expertise, technology and data visualization were equally important. Client personnel told us later that what we developed was completely different from what they had expected. And it led to more projects: Can you help set up a system that automatically routes contracts to the right person? Can you help us better orchestrate our activities across the globe so we meet important deadlines?

Kim Craig: The really critical outcome, though, was when one of our partners asked the general counsel: What keeps you up at night? He replied that he'd never heard a law firm ask him that, except during open bids for new business. It turned

out that what he really wanted was a better work-life balance. He hoped that better processes would let him spend fewer hours worrying about work. It's amazing to realize that these changes can actually improve someone's quality of life.

McKinsey: *How has Seyfarth's relationship with clients evolved?*

Lisa Damon: The changes enabled us to avoid the vendor mentality that has become so prevalent

Andrew M. Baker

Andrew Baker is a former global director of legal products and technology for SeyfarthLean Consulting, a subsidiary of Seyfarth Shaw. He holds two bachelor's degrees from the University of Illinois at Urbana-Champaign and a law degree from Chicago-Kent College of Law, Illinois Institute of Technology.

Kim Craig, Project Management Professional

Kim Craig is managing director, lean solutions, for SeyfarthLean Consulting, leading a team of legal project managers and process-improvement consultants. A faculty member of the Practicing Law Institute, Ms. Craig holds an associate's degree from MacCormac College and has completed business-studies coursework at DePaul University.

Lisa J. Damon

Lisa Damon, a member of Seyfarth's executive committee, leads the firm's Lean Six Sigma program and is the national chair of the firm's labor and employment department. She was named one of the top ten "Agents for Change" in the *Financial Times' US Innovative Lawyers 2012* report. In addition to a bachelor's degree from Beloit College, Ms. Damon holds master's and law degrees from Fordham University.

J. Stephen Poor

Steve Poor was the chairman of Seyfarth from 2001 to 2016 and is now chairman emeritus. Mr. Poor started his career with Seyfarth as an employment lawyer, with particular focuses on trial work and Employment Retirement Income Security Act litigation. He previously was chair of the firm's labor and employment-law group, and was named the 2011 "Legal Innovator of the Year" by the *Financial Times*. He holds a bachelor's degree from Indiana University and a law degree from the University of Virginia.

> "Being a really good 'classic lawyer' is no longer enough. Our people have to be facile with technology. They have to follow a different approach to problem solving. And they have to operate in a changed environment."

among law firms, some of which see themselves as just one among many vendors their clients use. The beauty of this approach is that it all but eliminates those blinders, because now we're in a nuanced business relationship that supports an entirely different set of conversations.

McKinsey: *Let's say that, for whatever reason, a client hasn't started down the path you are opening and instead prefers a vendor relationship. What do you do?*

Lisa Damon: Our teams work in the same way—our tools, our processes, our thinking—regardless of the client's situation. This is not marketing; it's simply how we operate.

Steve Poor: One of the challenges we faced early on stemmed from our own view of this methodology. To us, it seemed so good for clients that we thought the value would be self-evident. We sometimes forgot that our clients are lawyers, too, and the same resistance to change would play out in their organizations as it did in ours.

McKinsey: *Where does the resistance typically come from with clients?*

Andrew Baker: Lately the problem seems to be that everybody wants the easy button and the "one software package" to solve every issue. But once you start asking a few questions—to see which legal problems the organization has, how their business

operates, who the gatekeepers are, how they track who is doing what—most clients start to realize how much complexity there is and how much of it is driven by their distinct needs.

McKinsey: *This sounds like a very different form of client service, requiring different skills from the ones law schools teach. How have Seyfarth's changes affected how you develop your people— from recruiting through each career stage?*

Steve Poor: There's always been a gap between what law school teaches and what you need to do as a practicing lawyer. I think that gap is bigger now than ever, because being a really good "classic lawyer" is no longer enough. Our people have to be facile with technology. They have to follow a different approach to problem solving. And they have to operate in a changed environment.

Andrew Baker: Right now we need candidates with multidisciplinary backgrounds—mixes of law, business, process, project management, technology, and others areas. For instance, one of our roles calls for a connection to both statistics and law. There aren't many people like that, so we're working with several law schools to try to create more of them. We've invested a lot in our current people to bolster those skills and create programs in emerging disciplines such as design thinking and systems design. But it would be wonderful if our candidates came in already having these capabilities.

McKinsey: *How do you see this evolution continuing?*

Steve Poor: We're opening new channels for people to come into our organization. The standard associate track from law school is no longer the only option.

Kim Craig: More and more students are interested in combining the practice of law with the business of law. So we hire law-school graduates into our project-management and technology roles.

Steve Poor: Much of our management infrastructure rests on measuring people's competencies. That is how we make promotion decisions— not because someone has been here for a certain number of years.

McKinsey: *How do you expect the practice of law at leading firms to evolve over the next decade?*

Steve Poor: A handful of firms probably won't change much, because they have a mystique. The vast bulk of firms, however, will need to find a different path. The solutions that companies need are becoming more diverse, and the competition is becoming more diverse as well, with specialists targeting particular streams of work and technology companies moving into the field. The idea that you can simply get bigger or raise rates every year will not hold.

McKinsey: *How do you see client expectations changing?*

Lisa Damon: Some of our clients are already talking about "horizon expertise"—helping them see what's coming, instead of paying us to solve the current problem.

Steve Poor: Increasingly we're called on to present hybrid solutions that incorporate law, technology, service-delivery mechanisms, and other expertise. One global company is trying to identify patterns of workforce utilization worldwide, so we are working with economists and related experts to try to predict some of the emerging dynamics.

McKinsey: *How has the way that you lead changed as part of this journey?*

Steve Poor: I've been learning patience and persistence. You have to recognize that people won't necessarily accept change just because of a flash of insight that you so graciously share with them. It's a matter of taking pride in the small victories, rather than needing the big victory.

Lisa Damon: To me, it's about listening—meeting a partner or client or team at whatever stage they are in and finding affinity with them. What do they need? What is their value story? What can we tap into to help create what's often a revolutionary change? This is a huge transformation, and it's up to us to find the opportunity to help people push forward. ■

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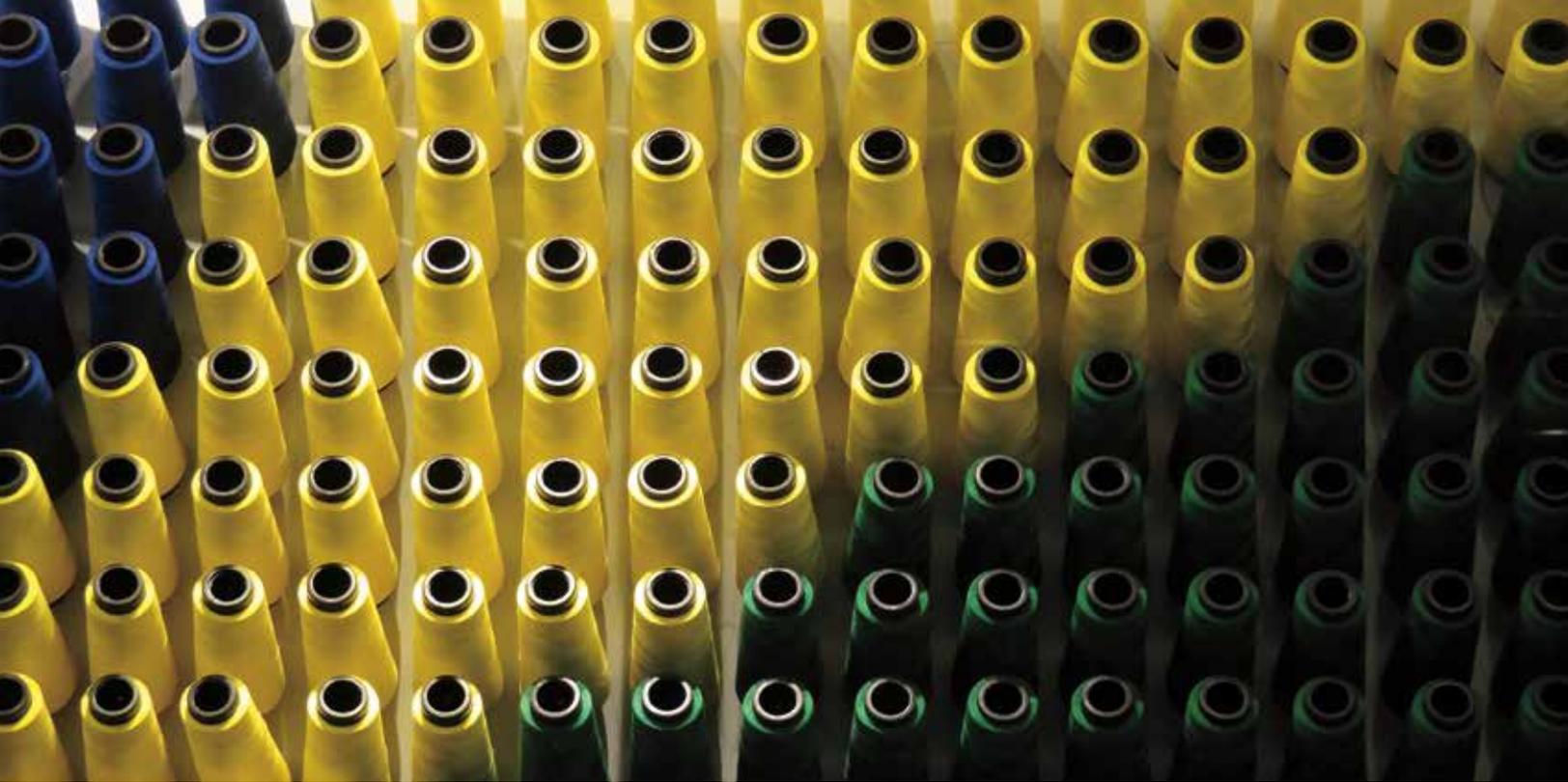
Purchasing power:
Lean management creates new value in procurement

Lean management is about much more than cost reduction, making it a powerful set of disciplines for increasing purchasing's effectiveness.

Koen De Backer, Björn-Uwe Mercker, Marco Moder, and Peter Spiller

From its roots in automotive manufacturing, lean management has expanded quickly through much of modern business, from manufacturing-related functions such as maintenance and R&D to industries as varied as healthcare and financial services. Whatever the concept has touched, it has transformed, delivering dramatic improvements in productivity and quality while empowering employees to continually improve the systems in which they work.

In most organizations, however, lean management runs into an important wall: the one by which the

purchasing department sits. In our experience, to the extent most procurement functions have thought about lean management at all, they have viewed it primarily as a way to streamline and automate procure-to-pay (P2P) activities. Lean management's capacity to deliver significant value in strategic procurement has largely been ignored.

The reason may be obvious. Despite procurement's influence, its operating costs are usually very low: on average, between 0.3 and 1 percent of spend in most industries. For procurement leaders who

see lean as a tool for wringing out efficiency improvements, those numbers hardly seem to promise much potential.

That mind-set should change. Properly applied, the disciplines and systemic thinking of lean management can become a strategic weapon: aligning purchasing more tightly to internal customers' real interests, helping leaders rethink the end-to-end procurement process (from suppliers through to manufacturing and ultimately to external customers), and transforming the effectiveness of strategic procurement activities.

Think of what procurement people do each day. How much time do strategic buyers spend on truly value-adding activities, such as building a deeper market understanding in key categories, identifying and qualifying new potential suppliers, or negotiating the best possible contracts? In all likelihood, much less than you think. At one large industrial company, our workload analysis found that strategic buyers often devoted less than 40 percent of their time to these core activities. The rest was lost on distractions such as administration, filling in reporting templates, and completing tasks that should have been the responsibility of operational procurement staff.

Now imagine you could change that situation. Cutting your administrative and reporting burden and optimizing your core processes could allow your buyers to focus more than 70 percent of their time on strategic activities. That's the equivalent of doubling the size of the strategic procurement function without adding a single person.

A broader and more thoughtful lean-management perspective doesn't just help companies maximize the effectiveness of their current processes. It also allows companies to take a more integrated view of the value each individual buyer creates. It helps them answer important strategic questions,

such as which activities should be kept in-house and which should be automated, allocated to near- or offshore shared-service centers, outsourced, or stopped altogether. Standardized activities, fewer processes, better-qualified buyers, continual people development, and resources sharply focused on activities that add real value—this is what we understand as lean procurement.

The advent of lean discipline in purchasing is timely for another reason: digital is set to have huge impact on the function, with many new solutions that extend beyond today's P2P automation and could transform the end-to-end procurement process. Tools such as standardized should-cost analyses, workflow portals to manage the full strategic-sourcing process, and access to huge external supplier databases for market research will allow strategic buyers to spend even more of their time focusing on the right things. And the efficient, structured processes enabled by lean management provide the perfect framework for integrating these new tools.

Applying a lean lens

Bringing lean-management discipline to purchasing requires action in five areas (see sidebar, "How one leader brought lean management to procurement"). The first step is to develop a deep understanding of the needs of procurement customers: not only the business units that work directly with the procurement department, but also the organization's end customers. Next is to simplify, automate, and streamline processes to meet those needs as efficiently and effectively as possible, both in strategic procurement (such as with standardized request-for-quotation—or RFQ—systems) and in operational procurement (such as with no-touch order processing). Third is to build the skills and structures procurement needs to achieve those goals, including a clear split between strategic and operational procurement roles. Fourth, the function must tighten its

How one leader brought lean management to procurement

The head of procurement at a global insurer describes how lean management enabled her team to increase capacity dramatically while reducing risk and delays.

When we started, we were already tracking a wide range of metrics—too wide, actually. The challenge became, "So what? What are the metrics telling us?" We started digging further into the purchase requests, or "tickets." Most were for fairly minor purchases, such as hiring a training consultant for a few weeks for $100,000. Only a few were for bigger deals, say, $50 million to outsource a significant amount of work for one of our business lines. The trouble was that the low-risk, low-dollar tickets and the high-risk, high-cost tickets went through exactly the same process.

Where's the **value for our customer** in that? The person requesting the trainer was waiting for days or even weeks to get a reply. Meanwhile, my people were having a hard time finding the capacity to think through all of the due-diligence issues that a big outsourcing contract raises.

We had to think through **standardization in a new way**. Now each of these types of ticket has its own standard, one that relies on automation for low-value tickets so that we free more time for the high-value, high-risk ones. We're separating our strategic decisions from our day-to-day operations.

Most of these changes are coming from our own people, **building their capabilities** for problem solving along the way. They told me what the top five problems were, and I then asked them to get their own teams to solve them within 90 days. My view is that even if the idea your associates come up

with solves only 80 percent of the problem, because the solution came from them, they'll implement it so much better than they would a 100 percent solution that came from somebody else. My job is to coach and guide and ask questions.

We're also reconfiguring how we **assess performance**, and using it to make further improvements. The ticket process sends out an automatic survey after every request. Although the response rate could be higher, even what we have received has helped. Quite a few requesters said they didn't know how long the process would take. Now we send an email within 24 hours to set expectations: "Joe or Jane will be handling your request. Given the dollar value, etc., we expect that the approval process will take X days."

We've standardized how we do due diligence on our larger vendors, and outsourced some of the work so that we can get a report in 15 minutes instead of hours or days. That means I can use people's skills a lot more effectively.

All of these changes have allowed us to reduce the number of tickets in our queues by about 40 percent. But the **biggest changes are in people's mind-sets**. They're pushing for bigger improvements, bigger targets. They understand that it's better to set an 80 percent target and achieve only 60 percent than to set a 25 percent target and achieve 32 percent: 60 percent is a lot more than 32 percent.

performance management, using indicators that focus on real value creation (for example, the function's overall cash and profit-and-loss contributions). Finally, and most importantly, the organization must systematically change the mind-sets and behaviors of its people, creating a culture that focuses on continuous improvement in meeting customer needs and eliminating waste.

Understand the customer

The starting point for lean management is always the customer. Sometimes, purchasing functions are guilty of delivering what they *think* is best for the rest of the business, rather than what *actually* is best. To bridge the gap, companies need a systematic approach to understanding their customer needs, with structured interactions, business collaboration portals, and voice-of-the-customer interviews. Strategic procurement councils, for example, ensure that representatives from individual business units and their counterparts in procurement can meet to discuss current performance and future plans. At one company, the council learned that business-unit leaders don't actually read the company's centrally generated purchasing reports. Scrapping these reports, which were labor-intensive to produce, freed up central purchasing capacity to focus more effort on strategic raw materials.

The most advanced companies ensure these platforms are a forum for two-way conversation. Their business units recognize the role of procurement as a "demand shaper," and they value its input on topics such as specification management or purchase volumes that can often unlock savings.

Standardize processes

Once a company understands how procurement's activities generate value for the business, it can explore new paths to do deliver the value more efficiently. Value-stream mapping—a tool adapted from manufacturing—can be a powerful way to separate the worthwhile steps in a process from the wasteful ones, so that the process can be simplified and redesigned.

The approach applies equally well to strategic and operational procurement processes, but with a few important differences in execution.

Standardize strategic processes

Understanding exactly why particular activities exist can lead to rapid, significant savings in time and resources for strategic personnel, whose workloads tend to be more complex and varied to begin with. Long, tedious update meetings become dramatically shorter through simple measures such as exercising better control over the agenda or sharing data with participants in advance.

Standardization can considerably reduce repetitive or duplicate activities. For example, a central department can find potential new suppliers in external databases, while developing standard criteria for supplier selection can greatly accelerate the prequalification process. Similarly, standard templates simplify the development of category strategies, and modular contract terms make agreements faster to generate and less likely to omit important safeguards. To avoid stifling creativity and entrepreneurship, however, companies must carefully distinguish between the activities that can be standardized and those that need more flexibility. A collection of the best "carrots and sticks" for negotiation preparation, for example, can provide the right balance.

Automation, already widely used in operational processes, is an underdeveloped area in many companies' strategic-procurement activities, and can further support standardization.

Electronic request-for-X (eRFX) tools simplify the collection and comparison of supplier quotes, and e-auctions can speed up regularly recurring negotiations. Cleansheets linked to raw-material price indexes can be updated at the push of a button, giving teams powerful support for fact-based supplier negotiations.

Standardize operational processes

In operational processes, traditional lean-management tools such as value-stream analysis can reveal significant opportunities to improve efficiency and effectiveness. One industrial company using this tool discovered that the number of purchase orders its operational buyers handled every year varied by a factor of four. It therefore captured the highest performers' practices and codified them into new standard operating procedures for the entire organization. Providing additional coaching and training to lower-performing staff helped fill the remaining skills gap.

Standardization in strategic procurement can be a starting point in enriching operational buyers' jobs, by making it easier to automate, consolidate, or outsource repetitive tasks such as managing supplier master data. In many companies, operational procurement activities could be automated much more thoroughly. For example, electronic catalogs and automated systems allow business units to place orders directly, and automated tracking systems can follow those orders' progress.

Build the organization and capable people

Becoming lean in procurement usually means redefining the organization from the ground up—starting with a clearer distinction between strategic and operational purchasing roles. That way, the procurement function's most expensive staff, the strategic buyers, spend more of their time on their most valuable work.

Ultimately, the resulting changes make these strategic personnel remarkably cost-effective. With process standardization and automation, rapid access to valuable internal and external data, and the ability to focus more than 70 percent of their time on high-value work such as category strategies, demand management, and negotiations, strategic buyers in a lean organization can deliver several times the value they would in most of today's purchasing departments.

As their roles evolve, people's skills and capabilities make an even more decisive difference to procurement's overall performance. Advanced procurement organizations therefore pay considerable attention to capability building. Leading companies work hard to capture and share their knowledge—for example, by building central databases on supplier interactions and specification data, or by creating communities in which purchasers and their customers can share insights on the newest market developments.

Often, the best way to develop purchasing capabilities is to put all strategic buyers through a procurement "academy," with modules covering not only purchasing-specific skills—such as category knowledge, cleansheet cost modeling, and structured negotiations—but also more general competencies in value-stream analysis, root-cause problem solving, and interpersonal communication. Over time, academies reinforce practice standardization, supporting a single "way of working" that ultimately defines much more than how to run RFXs or build cleansheets—it defines the company's culture.

Manage performance

Lean procurement functions look at performance management from a few different perspectives. They monitor the performance of suppliers, to ensure they are meeting quality, cost, flexibility, and service targets. They monitor the performance of individual buyers, both strategic and operational, to ensure they are working efficiently and retaining a focus on the true needs of their customers. And they monitor the performance of the function as a whole, to ensure it continues to deliver real value to the business it serves.

Effective performance management supports lean purchasing departments in two ways. First, the right metrics, targets, and review processes show where the function is performing well and reveal

opportunities for further improvement. Second, by focusing on the metrics that matter, and rigorously applying automation and standardization, companies can often reduce their overall tracking and reporting burden, freeing up more time for value-adding activities.

Encourage the right mind-sets and continuously improve

Lean procurement organizations make new demands on their personnel, requiring them to continually refine and improve their everyday tasks and to think and act in new ways in their interactions with customers, managers, and colleagues. It becomes the responsibility of each purchaser to continually question the activities he or she conducts and to propose better ways of doing them.

A range of powerful methods helps these new ways of behaving take root. Organizations see significant improvements from even seemingly basic steps, such as a 15-minute daily huddle where each procurement team discusses one best-practice element and one critical problem (and its resolution). At one company, managers encouraged their purchasing teams to start each purchasing project by writing a detailed RFQ template to collect all the relevant information up front, preventing time-consuming additional requests down the line. Once developed, the template was adopted as a standard for future RFQs in related categories, and the team's efforts were publicly acknowledged by leadership.

■ ■ ■

Procurement functions that have embraced lean management have achieved rapid, significant impact. One large European industrial player, for example, adopted lean disciplines as part of an organization-wide procurement transformation across all its diverse business units. Through

a single set of standard methods, the company increased the efficiency of its direct-sourcing activities by around 20 percent and its indirect-sourcing activities by 25 percent. But rather than reduce procurement staffing, the company assigned its newly freed people to a center of excellence responsible for driving the adoption of new tools. In tandem, it increased its savings targets and invested more time in negotiations than before. The new focus enabled the company to reduce spend by double-digit percentages across a wide range of categories. ∎

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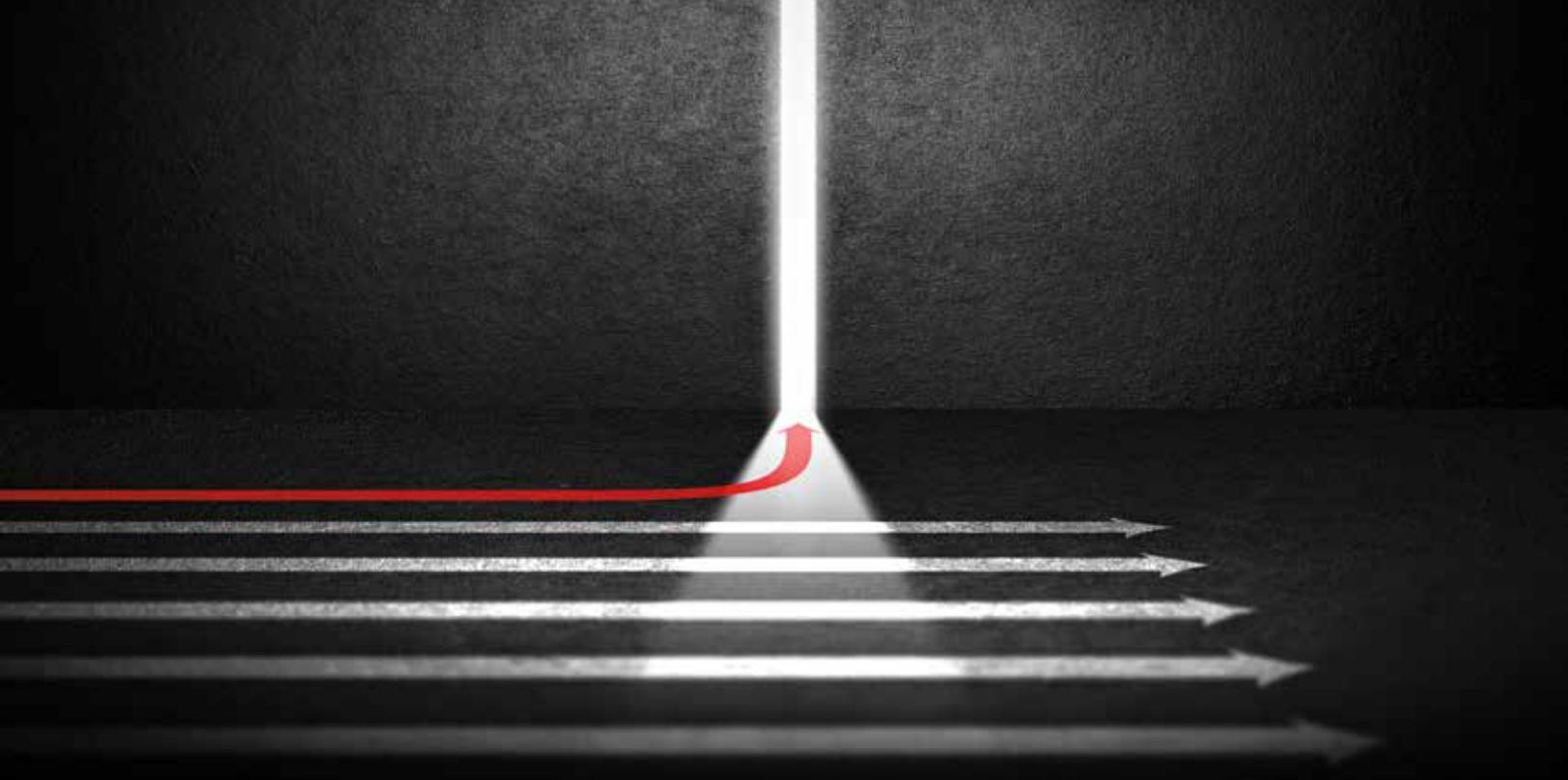
Transforming HR and culture:
An interview with Banco de Crédito del Perú's Bernardo Sambra

An HR leader describes how an effort to increase his bank's efficiency meant challenging the bank's culture—and himself.

Rodrigo Chaparro Gazzo and Christian Johnson

As Peru's oldest and largest bank, Banco de Crédito del Perú (BCP) is no stranger to change, and the pace has only accelerated. In 2009, a major transformation of its branch network and central operations yielded quick results: customer wait times fell by more than 50 percent, while employee productivity rose.[1]

Over the next several years, Peru's banking sector grew rapidly in tandem with the larger economy. But more recently, BCP's share of that growth began slowly but perceptibly to decline. Moreover, the bank's cost-income ratio remained stubbornly high compared with several of its major competitors in the region. BCP's leaders saw a need to take action ahead of an economic cooldown.

That led to a new call for change: not only for the bank's operations to become more efficient but also for its entire organization to challenge the bank's traditional culture. Bernardo Sambra, BCP's chief human-resources officer, has been at the forefront of this effort—which actually increased employee satisfaction, even as it reduced the bank's cost-income ratio by almost one-fifth.

In early 2016, Mr. Sambra spoke with McKinsey's Rodrigo Chaparro Gazzo and Christian Johnson in McKinsey's Lima office.

McKinsey: *What were the challenges that BCP saw over the past few years?*

Bernardo Sambra: By many measures, we were doing well: we were the leading bank in Peru across a wide range of sectors, we were making good profits, hiring good people. Most people thought everything was great.

But when we compared ourselves with our peers, we saw one big gap: we were not where we deserved to be in terms of efficiency. This was like a bell that kept ringing—in the boardroom, in committee meetings, all the time.

McKinsey: *What does efficiency mean for BCP?*

Bernardo Sambra: That was the real question. It seemed as though everyone had a different idea of what efficiency was and—more importantly— what becoming more efficient would enable the bank to do.

So we needed to start by aligning ourselves on the definition of efficiency, balancing several long-standing principles.

The first principle was simple austerity, doing more with less. Our next principle emphasized leadership and our tradition of seeking to be number one at everything we do—every product, every function. The third principle was to make decisions as if the resources to be used were our own. And the final one took an enterprise perspective, looking at success for the bank as a whole rather than just for each business or function.

McKinsey: *There's clearly some tension among the principles.*

Bernardo Sambra: And they're all important. That's why our workshops and discussions involved so much of the organization: more than 350 managers and leaders participated. We suspected that the type of changes BCP needed to make would require a really broad consensus on trade-offs. So, for example, we decided that aiming for number one in a particular product or function makes sense if it benefits the bank as a whole—if it contributes to revenues or helps us recruit talented people, that sort of impact—but may not make sense if the only benefit is a really narrow one.

McKinsey: *What was the outcome of these conversations?*

Bernardo Sambra: The most important outcome was alignment among our leaders on a plan to shape efficiency on three different fronts. The first front was deep performance improvement, across all our support functions, our IT and operations, our product portfolio, and our commercial model. At the same time, our second front looked at cost in much more detail. We wanted a new discipline on cost consciousness, to guide people's thinking in the same way that client service always has—in a constant cycle of finding new opportunities. That would need sharper discipline, so we created a central team to scrutinize cost deviations, along with new governance committees to review the business case for each proposed investment above a certain amount.

But ultimately, to make all of these changes last, we knew we would need to change our culture. That was the third front.

McKinsey: *Where do you start in changing a culture?*

Bernardo Sambra: We launched on all three fronts at once, so we were working on our culture in the same places we were making performance

Bernardo Sambra

Since 2010, Bernardo Sambra has led BCP's division of human-resources management. Previously, he served as advisory manager to the division and as head of transactions in whole-sale banking. Mr. Sambra holds a bachelor's degree in administration from the University of Lima and a master's degree in finance from the University of the Pacific in Lima. In addition, he has completed advanced coursework in human resources at the Stanford University Graduate School of Business and the University of Michigan's Ross School of Business.

and cost changes. Our first efforts focused on our corporate functions—and the function I lead, HR, was among the first functions to be transformed.

McKinsey: *How was that experience for you as a leader?*

Bernardo Sambra: I discovered that I had the same mentality as everyone else. I understood how important this transformation was, but I remember saying, "How can you ask me to change when BCP is recognized as the best employer in Peru? Think of all the awards we have received." At the time, I was busy thinking about the world-class HR model that I thought would be the function's next step.

I wanted BCP to have the best HR function in Peru. But I came to realize that this ambition was for me. I wanted to be number one.

What I learned through this transformation process was very difficult. The message was, "No. You do not need to hire more people to 'rebuild HR.' You are already good—find opportunities to keep doing what you're doing in a more profitable way."

McKinsey: *You had to make a big change as well.*

Bernardo Sambra: Yes. It led to a really positive realization: I could change my unit, manage in a different way, implement different processes, and look in the mirror and still see the value that I was creating.

That breakthrough was critical for the next phases of the transformation and defined our change-management approach.

Now, before a transformation team arrives in a particular unit, the top managers and their direct reports hold a four-hour workshop in which they discuss why they must implement these specific changes, at this time, in this unit. This step helps ensure that the managers own the transformation.

McKinsey: *How is that different from what BCP might have done in the past?*

Bernardo Sambra: In the past, we had issued everyone targets with Gantt charts for meeting them. But we didn't want to make wholesale cuts. In some respects, wholesale cuts may seem easier because everything's done very quickly. That's exactly what we wanted to avoid because it can so damage an organization in the long run.

But that decision also meant that everyone would go through several months of uncertainty as the managers determined which changes they needed to make. Instead of assuming that all the cuts will be the same, our process asks managers to start with a funnel of ideas. They start out very broad

and gradually become sharper and better defined until they turn into specific initiatives that each manager commits to make.

McKinsey: *That's a lot of uncertainty while they make their decisions, and uncertainty is dangerous to morale, no?*

Bernardo Sambra: That leads to the second point. In parallel, each organization goes through a change-management exercise, focusing on how people think about cost and efficiency. We found that people saw certain costs as unavoidable— as unquestionable. We wanted them to realize that they could work differently, ask more questions, and come up with different answers.

But what probably mattered more than anything was very simple: thanking people. "Thank you, thank you, and thank you one more time for helping BCP during this time."

McKinsey: *What effect have you seen on the staff?*

Bernardo Sambra: Earlier this year, we received our most recent employee-climate-survey results, which have been rising for several years. In the units being transformed, employee satisfaction held steady in 2014 and rose in 2015. It's now 10 percent higher than it was in 2011, when it was already more than 70 percent favorable.

McKinsey: *Stepping back for a moment and reflecting, what sorts of things can the organization do today that it couldn't before this transformation started?*

Bernardo Sambra: Let me use HR as an example of what we have done in our support functions. In recruitment and selection, we're much more focused on strategic questions now because a third-party provider takes care of time-consuming, lower-value tasks—in our case, things such as

collecting CVs and setting up interview logistics. In training, we used to be specialized by business line, which subjected the team to huge peaks and valleys in demand. Pooling all of our training resources has let us manage capacity much more effectively and made people's jobs easier.

Throughout our organization, leaders who previously had a hard time prioritizing their teams' work can now rely on visual-management tools to see the projects their people are working on, the status of each task, and the skills that are available or needed at any given point in time. They're becoming better managers. When I walk through the HR department in the morning and see everyone meeting for 15 minutes, looking at yesterday's performance and finding every single opportunity to make an improvement, it really makes me proud.

Replicate these results across every function being transformed, and it adds up quickly. In two years, our cost-income ratio has fallen from 49 to 41.

McKinsey: *How do you keep from slipping back?*

Bernardo Sambra: We set up a completely new structure for making decisions. Now, even if you have enough funds in your budget, you must clearly explain your spending: one of the legacies of this transformation is an efficiency division that's responsible for asking difficult questions. This is all simply a way of life now.

McKinsey: *What sort of lessons would you give to another organization, based on BCP's experience?*

Bernardo Sambra: First, in deciding to act, our most important step—and a very difficult one for us—was to have a conversation without PowerPoint. We needed to think about BCP's future, and for that type of discussion, PowerPoint is of limited use.

Second, get a clear mandate from the CEO. It may sound commonsensical, but it makes all the difference.

Third, people need a compelling story to help them understand why they must change. Without the compelling story, a mandate is just an order.

Fourth, make the managers the owners of the process, not the victims of the process. HR can provide support.

Fifth, be consistent, no matter how painful it may be. If you start making exceptions, people will lose faith in the process.

And finally, when you start getting the results you want, it is very easy to relax. Don't. ∎

[1] "Building conviction for lean management: An interview with Jorge Ramirez del Villar of Banco de Crédito del Perú," *Lean Management: New frontiers for financial institutions*, 2011, McKinsey.com.

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Mining for leadership with lean management

Three executives at one of the world's most unusual mining operations describe how even in a highly unpredictable context, lean management improves not just productivity, but also how people lead.

Christian Johnson and Ferran Pujol

The brine ponds that Chilean mining company Sociedad Química y Minera (SQM) operates in the remote Atacama Desert cover more than 50 square kilometers (19.3 square miles). Together, these ponds constitute some of the world's largest sites for extracting essential minerals, such as potassium for fertilizers and lithium for batteries. Combined with the more conventional mining of iodine and nitrate ores, they underpin a business with sales of more than $1.7 billion in 2015.

When the early 21st century's commodity boom ended abruptly, SQM was unexpectedly left vulnerable. More recently, however, the company has found a new source of growth: its own people. In mid-2016, Juan Carlos Barrera (SQM's vice president

for potassium and lithium operations), José Miguel Berguño (vice president for people and performance), and Carlos Diaz (vice president for nitrates and iodine) spoke with Christian Johnson and Ferran Pujol at McKinsey's office in Santiago.

McKinsey: *Thinking back to 2013, what pressures led SQM to consider transforming itself?*

Juan Carlos Barrera: The previous year, 2012, was really good for us in terms of results. Production, profitability, sales—almost every metric seemed to be increasing. But we saw that costs were increasing, as well. That made us concerned about what might happen should prices fall.

Carlos Diaz: That was when we started thinking about cost reductions, because it was clear that would be essential to our business over the long term. In early 2013, we launched a program that became SQM-100, a major cost-reduction effort.

José Miguel Berguño: The savings from SQM-100 were substantial—close to 10 percent of our cost base. But then we realized that our organization wasn't necessarily prepared to take full advantage of our new competitive position.

McKinsey: *That's a very different goal.*

Carlos Diaz: Yes, one that needed a different organizational structure. That wasn't a surprise—I'd say that over the past two decades, we've reorganized about every five to seven years. Plus, every three or four years, we do another cost-reduction project.

Juan Carlos Barrera: But then the costs would creep back up. So the new question became "Why don't we do something different, so we don't keep having to do these restructurings and cost campaigns?"

José Miguel Berguño: That was our hope. Our immediate aspiration, though, was only to sustain what we had achieved. But we made a visit to a company in the US that has a long history of lean management in manufacturing. That really changed our view.

McKinsey: *What was it about their operation that captured your attention?*

Juan Carlos Barrera: Two things stood out, because they seemed to be contradictory. On the one hand, employees really identified with the company, in their hearts as much as in their minds. Yet on the other hand, the company was much less dependent on individual people than we were.

In our organization, we knew there were a lot of places where, if the "wrong" person went on vacation, we would see performance fall.

José Miguel Berguño: Certain people were almost like artists for us—their expertise was unique.

Juan Carlos Barrera: Relying on "artists" made us vulnerable. After this big cost-reduction process, we wondered how we could ever improve productivity again if we were so dependent on specific individuals. But in the company we visited, people could substitute for one another much more easily.

McKinsey: *Yet at the same time, people seemed even more committed to the company. How do you reconcile these two ideas?*

Juan Carlos Barrera: Initially, we thought that maybe our people didn't have the right qualifications to do the sorts of things that people at the other company were doing. I remember watching their line workers and thinking, "I would hire them as supervisors."

Carlos Diaz: That was eye opening. Over time, I came to realize that the main challenge in a transformation is how to transform leaders. You may think that the problem is your workers. But in reality, it's probably you who have the problem. At the start I thought, "I'm a vice president. I've been doing the right things for 20 years, so why do I have to change?"

McKinsey: *What persuades someone who's been successful for 20 years to change?*

Carlos Diaz: We did have a few advantages. One was that we have a history of adapting quickly. Another is that we like challenges. For example, the geological conditions of northern Chile are so different from those anywhere else that we can't look to others' processes for lessons. We're constantly having to come up with our own new techniques.

Juan Carlos Barrera: Plus, our operations are very different from what you'd see at a typical manufacturer that does lean management. We aren't molding a certain grade of steel or aluminum into standard auto components. Our raw materials can change dramatically from one day to the next.

José Miguel Berguño: We could see what lean management could do, but because we were so different, it was a risk. The challenge was to adapt the ideas—the manufacturing mind-sets—to us. That's what engaged our people, starting from our CEO on down.

McKinsey: *So the challenge of adapting lean management engaged your leaders. What was in it for everyone else?*

Juan Carlos Barrera: Our commitment was to improve our people's work lives. The fact that we were so dependent on specific individuals to do specific things made work more difficult than it had to be.

McKinsey: *The company had just been through a major cost-cutting effort in SQM-100. Did people buy into the objective of a better working life?*

José Miguel Berguño: At first, some people thought this was just going to be "SQM-200"—more cost cutting. We gave it a different name, "M1," to underscore that it would be different, and spent a lot of time communicating with everyone that this was about changing our culture. And we chose one of Carlos's plants to act as a pilot.

Carlos Diaz: It was an old plant with very stable processes, so that it would be easy to see lean management's effects. Also, two branches of the nitrates business had recently been combined, so we realized that the integration would be a good opportunity to introduce new ideas. And we had a couple of very strong leaders on site.

McKinsey: *How did people react?*

Carlos Diaz: In the beginning, a lot of people said, "OK, we've done this lots of times before, under lots of different names. We put up a bunch of white boards, write our key performance indicators on them, and in four months the initiative fails. So in four months, this will fail too and we'll go back to normal." Sometimes, people took improvements—even major ones, like 10 or 20 percent production increases—as a criticism, as if they must have been doing something wrong before.

José Miguel Berguño: That made us work even harder on including everyone in the process, the workshops and problem-solving sessions, and the new tools for finding improvement potential. We wanted everyone to see and, more important, feel that the changes were really coming from them.

"Over time, I came to realize that the main challenge in a transformation is how to transform leaders. You may think that the problem is your workers. But in reality, it's probably you who have the problem."

Juan Carlos Barrera: And the results were good. I kept hearing about them even though I'm in a completely different business line. In fact, over here in potassium and lithium, we were so persuaded that we decided to launch with not just one plant but two.

McKinsey: *What was it like starting two more at the same time?*

Juan Carlos Barrera: It was probably too soon to do two; we are naturally competitive within the company, and that caused us to try to do too much. One of the plants was already running at very high production levels, so there wasn't much opportunity to show improvement. We realized that our managers and supervisors were stretched too thin—this wasn't improving their work life, and that was our goal.

José Miguel Berguño: We decided to pause. That was a difficult decision to make, but it let us adapt lean-management concepts some more to make sure they worked for our people. We started changing the order for introducing new skills, so that what people were learning fit more closely with the actual problems they were working on. We simplified the language, too. That way we could keep the general structure but answer more immediate needs, so that people could see how lean management could help them.

McKinsey: *Given that your plants are in remote areas, how did you make sure the changes felt credible to people on the ground?*

José Miguel Berguño: We know that in some transformations, companies create an almost duplicate structure of change agents. But we decided from the beginning that our change agents had to come from the line organization and that their role was to support the line leaders, not create a parallel leadership structure.

Carlos Diaz: And they needed to be on location. Our processes are technically complex, so it really wasn't feasible to base the change agents in Santiago and have them visit northern Chile once a week to give a few recommendations. They needed to be on the ground, working with me, the supervisors, and our people on the site. And they needed to understand the processes really well, so that meant they had to be high performers.

McKinsey: *Now you're about three years in. How does it feel across the organization?*

Juan Carlos Barrera: For me, the biggest result is that we've improved our performance—costs, production, safety—and we're even more flexible now. Recently, we decided to target another plant for lean management. To jump-start the transformation, we transferred 15 people from one of the first plants that we transformed. That was almost one-quarter of the team, including the manager and the assistant manager. That first plant has actually kept improving, same as it was before anyone left, and the second plant is making a lot of progress.

José Miguel Berguño: This is completely new for us. We can now move people to help performance in one area without sacrificing performance in the areas they came from.

Carlos Diaz: To be honest, initially my goal was just to reduce costs some more. But during the process, I've become much more focused on people development. I can see what people can do and how that matters over the long term.

McKinsey: *What are people doing differently now?*

Carlos Diaz: We used to say "we work as a team," but most of the time it wasn't much of a team— the supervisor gave an order and the workers followed. Today, it's more of a conversation; people

are more open to hear each other. Anyone can give a presentation or express an informed opinion. And because of that, people work more as a team to try to solve problems.

Juan Carlos Barrera: Many more of our people now see themselves as problem solvers. Before, they would take problems to their supervisors or managers, but now, step by step, they are learning how to refine what we can do as a company.

José Miguel Berguño: Two years ago, I would say that it was the job of managers or leaders to achieve new goals by pulling their people along.

Juan Carlos Barrera

Juan Carlos Barrera has served as SQM's vice president of potassium and lithium operations since 2007. Mr. Barrera first joined SQM in 1991 as an adviser in business development. Promoted in 1995 to business-development manager for SQM Nitratos, in 2000 he became the head of corporate supply-chain management. In 2006, he was appointed general manager of Soquimich Comercial, where he remains a member of the board. Mr. Barrera holds a degree in industrial and civil engineering from the Pontificia Universidad Católica de Chile, along with MBAs from Tulane University and the Universidad de Chile.

José Miguel Berguño

José Miguel Berguño was appointed SQM's vice president for people and performance in 2016, after serving in a range of leadership roles in areas such as performance management, strategic sourcing, SQM-100, M1, and human resources. Earlier in his career, Mr. Berguño served as director of Chile's National Training and Employment Service (under the Ministry of Labor and Social Security) and led human resources for Vitamina Work Life. He holds a degree in industrial and civil engineering from the Pontificia Universidad Católica de Chile, where he also earned an MBA.

Carlos Diaz

Carlos Diaz, vice president of SQM's nitrates and iodine operations since 2012, joined SQM in 1996 as a planning engineer in the sales division. He was promoted to planning manager in 1998, becoming deputy financial manager of the commercial offices in 2002 and logistics manager in 2006. He holds a degree in industrial and civil engineering from the Pontificia Universidad Católica de Chile, where he also earned an MBA.

Now, we have so many more people all trying to improve everything we do, throughout the company, that it's the people who are pulling the managers along. The managers' role is much more about facilitating the implementation of their people's ideas.

McKinsey: *And what are you doing differently now as leaders?*

José Miguel Berguño: My style as a leader used to be to exercise as much control as I could about what happened in my area. I thought that was how I created value for the organization, so I made a lot of decisions, even small ones. I think I really was a bottleneck. Now I obtain better results if I try to develop people more and ask questions, so that they can make the decisions rather than me.

Juan Carlos Barrera: I used to focus on so many details. But we have to be humble and see that people can make good decisions and that our task is to help them. And it's not just developing the people who immediately report to me; it's looking at every level because people are the future of our company.

Carlos Diaz: It's easier for me to talk with people. In the past, if I needed to talk with the frontline workers, I had to organize a special meeting. Now, because I'm visiting the performance-board discussions all the time, I can immediately understand what is happening in each plant and have conversations with people informally as

needed. I'm also much more conscious of everyone's time. I want to demonstrate to my people that what they're doing is important to SQM, and that means minimizing any interruptions of their day.

McKinsey: *What do you see as the next challenges for lean management at SQM?*

Carlos Diaz: For me, the next task is innovation. That's the deeper meaning of continuous improvement—finding the new ideas that help us with our unique processes.

Juan Carlos Barrera: All while keeping our flexibility and responsiveness.

José Miguel Berguño: And the new way of working. I see how people have more information, more space to discuss ideas—and that makes their daily work better. That's why we're doing this. ∎

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For service organizations, the goal of sustained improvement has been at least as frustrating as attractive. But a select group is pointing the way forward by adhering to four management disciplines: delivering value efficiently to the customer, enabling people to lead and contribute to their fullest potential, discovering better ways of working, and connecting strategy, goals, and meaningful purpose. Together, these form the lean management system, an integrated approach that transforms the entire organization from the front line to the executive suite, allowing it to renew itself continuously for lasting value.