What Everyone Gets Wrong About Change Management

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Corporate transformations still have a miserable success rate, even though scholars and consultants have significantly improved our understanding of how they work. Studies consistently report that about three-quarters of change efforts flop—either they fail to deliver the anticipated benefits or they are abandoned entirely.

Because flawed implementation is most often blamed for such failures, organizations have focused on improving execution. They have embraced the idea that transformation is a process with key stages that must be carefully managed and levers that must be pulled—indeed, expressions such as "burning platform," "guiding coalition," and "quick wins" are now common in the change management lexicon. But poor execution is only part of the problem; our analysis suggests that misdiagnosis is equally to blame. Often organizations pursue the wrong changes—especially in complex and fast-moving environments, where decisions about what to transform in order to remain competitive can be hasty or misguided.

Before worrying about *how* to change, executive teams need to figure out *what* to change—in particular, what to change *first.* That's the challenge we set out to investigate in our four-year study of 62 corporate transformations.

When companies don't choose their transformation battles wisely, their efforts have a negative effect on performance. Consider what happened after Ron Johnson took over as CEO of J.C. Penney: He immediately gave store design and pricing an overhaul to attract younger, trendier customers. Sales sank by a quarter, and the stock plummeted by half.

Johnson's first priority should have been a better integration of JCP's in-store and online operations. At that time customers could not find in the stores what was being showcased online, and vice versa. The two channels were run separately, each with its own merchandise and supply chain. Johnson's eventual replacement, Marvin Ellison, recognized the misalignment and restored JCP to profitability. Under Ellison's leadership, JCP became nimbler and more responsive to customers looking for deals (who had left in droves because of Johnson's changes). The retailer redesigned its shopping app to make it easier for in-store customers to find discounts, improved its website, and caught up with rivals by offering same-day in-store pickup of items ordered online.

As JCP and many other companies have learned, the costs of setting off on the wrong transformation journey are significant: First, underlying problems will persist and worsen as attention is invested elsewhere (JCP fell further behind in online sales as it freshened up store design). Second, new problems may emerge (JCP alienated loyal, deal-driven customers with its new pricing strategy and saddled itself with more than $5 billion of debt, which hampered its ability to invest in technology). And third, the

executive team risks undermining employee commitment to future initiatives (Ellison had to remobilize a workforce still traumatized by JCP's near collapse under Johnson). Having "fixed the plumbing," Ellison's leadership team has turned its attention to making JCP more relevant to shoppers in the coming decade. Although it has averted disaster, the company still has a lot of work to do. After a rough holiday season in 2016, the executive team decided to close almost 140 stores to compete more effectively with online retailers. The need for transformation is ongoing.

So how can leaders decide which changes to prioritize at the moment? By fully understanding three things: the catalyst for transformation, the organization's underlying quest, and the leadership capabilities needed to see it through. Our analysis of stalled transformations suggests that failing to examine and align these factors drastically reduces the odds of producing lasting change. In this article we illustrate this dynamic with several classic case studies that provide enough distance to observe and compare clear, verifiable outcomes. We also offer tools to help diagnose what's needed in your company's transformation efforts.

The Catalyst: Pursuing Value

The trigger for any corporate transformation is the pursuit of value. Ideally, that entails both improving efficiency (through streamlining and cost cutting) and reinvesting in growth. But many transformation efforts derail because they focus too narrowly on one or the other.

In some cases, attempts to streamline the business through productivity improvements, outsourcing, divestments, or restructuring undermine growth. The cuts are so deep that they hollow out capabilities, sap morale, and remove the slack that could have fueled new endeavors.

Consider Norske Skog, once the world's largest newsprint producer—now, according to Bloomberg, the third largest in Europe, in a dwindling market. Hit by falling demand for paper more than a decade ago, the Norwegian company was forced to divest unprofitable operations across four continents. Thanks to its profitability improvement program, it became so good at identifying where to make cuts that it was praised by *BusinessWeek* in 2009 for turning "shrinking into a science." But although the company has survived, it has not found a way to rebound. Like many companies in contracting or commoditizing industries, it is stuck in turnaround mode, with its share price consistently in decline. By contrast, its Swedish-Finnish paper rival Stora Enso also went through several rounds of painful restructuring but has since reinvented itself as a renewable-materials company.

In other cases, reinvestment in growth spins out of control. Lego had this problem. The Danish toy maker made two large-scale attempts to transform itself through greater innovation. The first, launched in 2000, delivered a wealth of freewheeling experimentation that over the next few years drove the company to the brink of bankruptcy. The second, launched in 2006 (once the company had recovered its financial stability), catapulted Lego past the two U.S. giants Hasbro and Mattel to become the world's most profitable toy company by 2014, with margins greater than 30%. Why the big difference? The second time around, under then CEO Jørgen Vig

Knudstorp, Lego maintained a dual focus on growth *and* discipline. The company set up a cross-functional committee (the Executive Innovation Governance Group) to fund, monitor, and strategically coordinate innovation activities, ensuring that they remained "around the box" rather than drifting way outside it.

This example brings us to a larger point about catalysts for change: While you're striving for growth, discipline—through governance, metrics, and other controls—allows you to stay on track later on, after you have chosen your journey's direction. Without such controls in place, your company can easily lose its way. This often happens through the hasty purchase of an overpriced or tough-to-integrate "transformative acquisition" that is meant to redirect the strategy but just ends up sucking value out of the corporation. Hewlett-Packard is a notable recidivist in this domain: Recall its ill-fated acquisitions of Compaq, EDS, and Autonomy. But how can you and others on the leadership team figure out what kind of transformation to pursue, once growth opportunities or declining performance has alerted you to the need for major change of some kind? That's the second step in the process—defining the quest.

The Quest: Choosing Your Direction

Next the organization must identify the specific quest that will lead to greater value generation. Executives increasingly use the term "transformation" as shorthand for "digital transformation." But the ongoing digital revolution does not itself constitute a transformation—it is a means to an end, and you must define what that end should be.

Studies and analysis that we have conducted show that most corporate transformation efforts are either derivatives or combinations of five prototypical quests:

1. *Global presence:* extending market reach and becoming more international in terms of leadership, innovation, talent flows, capabilities, and best practices
2. *Customer focus:* understanding your customers' needs and providing enhanced insights, experiences, or outcomes (integrated solutions) rather than just products or services
3. *Nimbleness:* accelerating processes or simplifying how work gets done to become more strategically, operationally, and culturally agile
4. *Innovation:* incorporating ideas and approaches from fresh sources, both internal and external, to expand the organization's options for exploiting new opportunities
5. *Sustainability:* becoming greener and more socially responsible in positioning and execution

Each quest has its own focus, enablers, and derailers, and each requires the company to do something more or different with its operating model, customers, partners, internal processes, or resources. "Going digital" can support any of the five quests, and all of them call for discipline.

Let's return to the paper giant Stora Enso to see how it defined its quest. The catalyst for transformation was the plunging demand for paper along with the rise of digitization. Stora desperately needed not only to cut costs but also to rethink its business focus.

Members of the top team consulted widely with various divisions and layers of the company and engaged in lengthy deliberations. Weighing the options, they concluded

that pursuing nimbleness, global presence, or customer focus would merely yield more market share in a declining industry. Innovation would not solve the main issue either. But the company had developed some breakthrough green offerings, including environmentally friendly packaging for the expanding e-commerce delivery market. Its greatest opportunity lay in shifting the whole axis of the business to specialize in offerings made with renewable and bio-based materials. So Stora's was a sustainability quest. That turned out to be a shrewd pivot. Traditional paper-based products now represent only 8% of Stora's profits, and the company's share price has almost tripled since November 2011.

It can be difficult to choose the right quest. Should the company expand into new regions, get closer to customers, innovate with more partners, get faster and more responsive, or become more sustainable? Executives sometimes say "all of the above"—but that's too much to handle at once. The right quest should be a compelling and uncontested priority. In some of the cases we analyzed, companies straddled quests (customer focus and agility, for instance, or innovation and sustainability). That can work as long as the components are fused into one cogent focus.

With multiple organizational challenges jostling for attention, top teams are liable to disagree on the transformation priority. That's why we created a 15-question audit. In our research and consulting engagements, we've found that this tool allows executives to do their own systematic review so that they can make smart decisions regarding transformation. For example, at a French utility company we worked with, the top 200 executives participated in a "transformation jam" where they all filled out a status report that identified the critical enablers and blockers for each potential quest. This and the quest audit helped to clarify and reconcile the priorities of different parts of the organization, from the boardroom and the C-suite to the front lines.

The Capabilities: Developing Leaders

Finally, to support the chosen quest, the company must develop leaders who can see it through. Sustained transformation depends on this.

Again Stora Enso is a useful case in point. Jouko Karvinen, the company's CEO until July 2014, realized that his executive team—all Nordics, all industry veterans—could continue to squeeze costs out of core businesses but would struggle to explore prospects for fresh growth. So, in close consultation with then HR head Lars Häggström, he set up a parallel "Pathfinders" leadership team—a dozen managers from various parts of the organization—and gave them a mandate to identify sustainability opportunities that were falling between silos and, more broadly, to challenge the old ways of doing business. Each year the organization replaces its Pathfinders with a new cohort of up to 16 members. At first this was mainly a way to keep bringing new perspectives into high-level decision making, but it expanded into a program for identifying and developing change agents within the organization who would then serve as internal management consultants. The Pathfinders program became the centerpiece of the company's new leadership-development activities. Transformation journeys run out of steam when companies neglect leadership development. In order to keep an organization moving in the desired direction, executives and managers at all levels must

understand which mindsets and behaviors will take the company there and then take care to model them so that employees know how to act in the new context.

Any mismatch between the leadership-development effort and the transformation quest is bound to impair value generation. The need for alignment is well demonstrated by the familiar but instructive story of two Asian rivals in personal computing.

The right quest should be a compelling and uncontested priority.

In 2008 Taiwan's Acer and China's Lenovo ranked third and fourth respectively in global market share, well behind HP and Dell. By 2015 Lenovo had claimed the top spot and Acer had slipped to sixth. They had defined similar quests—achieving global reach—and they pursued similar strategies, seizing opportunities to generate value and transform their global presence by acquiring embattled Western businesses. Lenovo grabbed IBM's PC division in 2005; Acer snapped up Gateway in the United States in 2007 and Packard Bell in Europe in 2008. But a key difference between Lenovo and Acer was their commitment to globalizing the senior leadership ranks.

Acer's board struggled with "de-Taiwanization," rejecting CEO Gianfranco Lanci's bold plans to hire foreign talent with expertise in mobile technology and to triple the number of engineers. (It's worth noting that Lanci soon left Acer to head up Lenovo's PC group.) In 2010 Acer had six foreigners among its top 24 executives; by 2014 it was down to three out of 23. In the same period, the board went from having two foreign directors to having none. Predictably, the top team's decision making became increasingly cautious and inward-looking. In 2016, for example, it hired the founder's son to head up the company's cloud services, which prompted the *TechNews* headline "Is Acer Becoming a Family Business?"

By contrast, leadership development at Lenovo was fully in line with the company's quest for a greater global presence. By 2012 its top team of nine represented six nationalities. Its Chinese CEO, Yang Yuanqing, relocated to the United States, and other members of the team were scattered globally, gathering for one week each month in a different strategic market. Aware of the challenges his team faced as a result of its members' varied backgrounds, the CEO brought in a coach to work with the executives on cross-cultural issues. And to promote diversity as a source of competitive advantage—in both hiring and operations companywide—Lenovo elevated the role of cultural integration and diversity VP to the C-suite. Such efforts paved the way for ambitious acquisitions and joint ventures with German, Japanese, Brazilian, and U.S. companies—enabling Lenovo to extend into new software and services categories globally.

Transformation Traps

Many transformation efforts are set up to fail at the quest stage. Top teams get sidetracked or overreach when they lose focus on what value is worth pursuing—or they take on more change than their leadership capabilities can steer. Our investigations reveal three common failings:

Neglecting the quest.

In companies that don't identify a mobilizing theme, value generation and leadership development can become ends in themselves—generic efforts, not really linked to the strategy. For example, India's Infosys developed a widely admired approach to leadership development but ran into trouble because it failed to tie that to the transformational needs of the business—forcing the IT giant to turn to an outside CEO to drive the necessary changes.

Being seduced by the wrong quest.

The board and the top team may be led astray by the vision of a forceful CEO (like Ron Johnson at J.C. Penney), try to copy the strategic moves of competitors, or fall for recommendations from consultants who favor particular quests. In those situations, the chosen quest misfires because it was not the product of deep deliberation or shared conviction or it fails to address the central issue. For example, GE transplant Bob Nardelli tried to transform Home Depot by selling supplies to construction professionals as well as to homeowners. The pursuit of customers in adjacent markets distracted attention from Home Depot's core problem of slumping store sales. When Nardelli resigned, under intense pressure from shareholders, the strategy was immediately reversed and the wholesale arm sold off to allow the company to refocus on its core retail business. From seventh-largest global retailer, Home Depot has since jumped to third.

Focusing on multiple quests.

The quest choice may be muddled if leaders can't agree on which direction to go. Different parts of the business (regions, functions, levels) see different problems and priorities. Some corporations overreach, taking on too many quests at once or overestimating their leadership capabilities in a given area. Back in 2009 the incoming Carrefour CEO, Lars Olofsson, launched an ambitious transformation plan for the retail giant based on seven strategic initiatives, including enhanced innovation, customer engagement, agility, and global expansion. The result was confusion, a loss of domestic market share, and a 53% plunge in share price in one year. Olofsson lasted barely two years in the job. His replacement, Georges Plassat, panned the leadership capability of the previous team, labeling the members "incompetent in mass retailing." In a successful recovery plan, Plassat first focused on shedding operations in noncore markets and streamlining internal operations. He then reignited domestic sales by cutting prices and diversifying stores. Three years later Carrefour had regained a clear lead in the French market.

Getting Started

It can be useful to think of value generation and leadership development as the chariot wheels that support a transformation, and the quest as the horse that provides direction and momentum. Alignment among the three is critical if you want to reach your destination.

The quest audit facilitates alignment by making it easier to diagnose the current situation, identify which transformation could be a game changer, and decide which enablers and blockers to target to make it happen. This tool has been validated with more than 500 executives and road tested by a dozen companies (across industries and continents) seeking to transform themselves. It helps address these underlying challenges:

Facing reality.

Having a structured way to solicit and gather input allows senior teams to take a cold, hard look at the company. Knowledge, competencies, or activities that were once central to the organization may have become what Harvard's Dorothy Leonard-Barton calls core rigidities. If so, they need to be adapted or jettisoned. The more radical the transformation, the greater the chance that such limitations will be exposed. Confronting harsh reality may also involve identifying and addressing blind spots.

For the HR head of a European postal services group, a quest audit revealed a disconcerting pattern. "The low scores on value, customer focus, and innovation seem to highlight our company's ineffectiveness in listening respectively to the market, to our customers, and to suppliers or partners," she told her team. "It's hard to admit, but it's better to recognize now the inertia of our organization that needs to be tackled urgently." Similarly, the head of HR at a Japanese food group observed that doing the exercise opened up team dialogue on issues that were previously off-limits: "It provided 'permission' to reflect on the current reality and how we got to where we are. That immunity led us to frame some breakthrough questions to understand our challenge and what we needed to do to solve it."

Debating priorities.

Often the diagnosis reveals multiple challenges and the debate centers on which of them matters most—or which can be tackled immediately, given the company's current leadership capabilities. Conceptual tools can't tell top teams what to do, but they can support a smarter discussion, with much of the critical information visible at a glance.

By mapping out where various parties see opportunities and hazards, executives can avoid a major decision-making trap: getting stuck with a false choice between pursuing one strategic option and doing nothing. Articulating the pressures and challenges makes it easier to debate and evaluate the relative merits of various responses.

Take the case of Cosentino, a Spanish manufacturer of engineered surfaces for kitchens and bathrooms. Because the company had established a solid distribution foothold in the United States, the most obvious strategy was to keep extending its global presence. But after using the quest audit to weigh their options, the top 70 executives decided instead to prioritize co-innovation—not just with Cosentino's supply chain partners but with other high-end kitchen and bathroom businesses (facades, flooring, and equipment)—to anticipate new trends. They elected to work on their biggest weakness rather than to build on an obvious strength.

Top teams are liable to disagree on the transformation priority.

Reconciling perspectives or priorities and developing a shared understanding of the cause of the current state of affairs is not painless. But sidestepping that discomfort only reduces the chances of selecting a viable transformation objective. According to the head of finance of an Italian fashion group, "Our discussions highlighted areas where we perhaps were not as aligned as we thought and emphasized common pain points regardless of where you sit in the organization. The reflection drove convergence about what we needed to do and stop doing."

Joint consultation also builds a sense of involvement that boosts the perception of fair process and therefore commitment to the chosen course of action.

Communicating choices.

Having debated the priorities and challenges, an organization's leaders can feel more confident in advocating a particular course of action and communicating the message to others. They are better equipped to explain how they reached this conclusion, what alternatives they scrutinized, and why they think this is the right transformation journey. If employees feel that the analytical work was thorough and inclusive, they are more likely to accept the decision, even if they don't like it.

Of course, analysis alone seldom inspires people to act in unfamiliar and perhaps unwelcome ways. When leading people into an uncertain future, it helps if the decision makers can get people talking about enablers and blockers. That gives everyone a sense of where the organization stands, what it must transform—and why, beyond "survival," the journey is worth making.

Here's an example of how this can play out: At GroupM, the world's largest media investment group, the top team of the South Asia operation concluded that its competition in the digital age consisted of not just the traditional agency networks but also disruptive start-ups and digital platforms that could cultivate direct access to its clients. As the team debated priorities, innovation through deeper partnerships with potential new competitors emerged as number one. Further discussions, including one mediated by a "youth committee" made up of highfliers under the age of 30, revealed that a key enabler was the ability to pick the right innovation partners. A key blocker, according to C.V.L. Srinivas, the division's CEO, was "getting people working in a successful organization to change their mindset and accept that we needed to change in order to stay relevant." So the top team chose a communication strategy that balanced hard and soft approaches: setting tough targets for employees to increase their proportion of digital work while making it clear that they would receive the support and training to achieve those goals.

CONCLUSION

As the shelf life of business strategies grows shorter, a corporation's transformation capability becomes its only enduring advantage. A quest for innovation provided a focus for Lego's transformation under Knudstorp. But now, as Lego nears saturation in its lead markets, such as the United States and Germany, its attention is on fast-growth emerging economies—the new quest being to transform a Danish brand with global appeal into a truly global corporation.