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SPOTLIGHT THE TROUBLE WITH CMOs

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FROM THE EDITOR

THE TRUTH ABOUT GLOBALIZATION

Adi Ignatius with Eric Hellweg, HBR's head of product.

Public sentiment about globalization has taken a sharp turn. The election of Donald Trump, Brexit, and the rise of ultra-right parties in Europe are all signs of growing popular displeasure with the free movement of trade, capital, people, and information. Even among business leaders, doubts about the benefits of global interconnectedness surfaced during the 2008 financial meltdown and haven't fully receded.

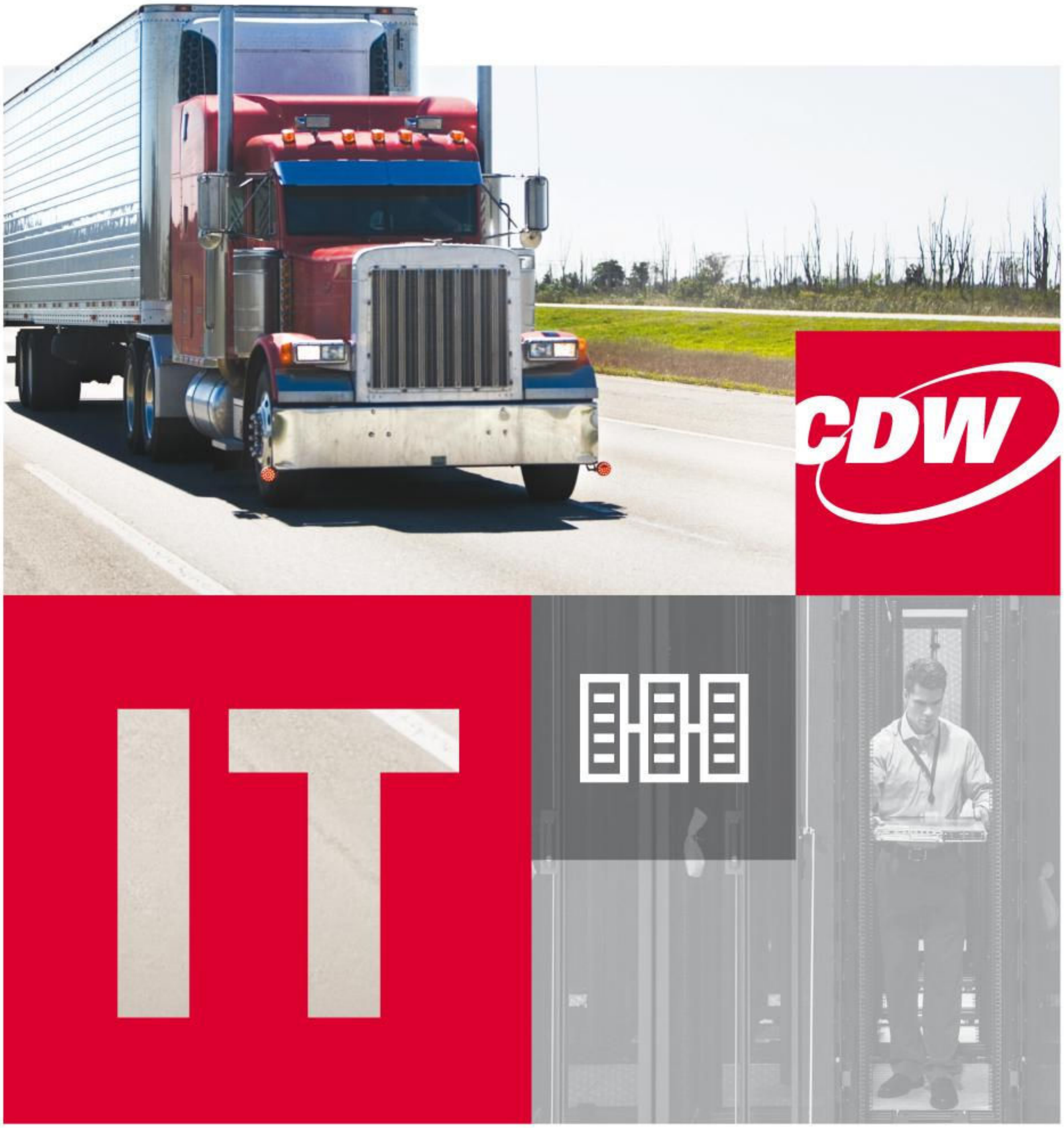
In "Globalization in the Age of Trump" (page 112), Pankaj Ghemawat, a professor of global strategy at NYU's Stern School and at IESE Business School, acknowledges these shifts. But he predicts that their impact will be limited, in large part because the world was never as "flat" as many thought.

"The contrast between the mixed-to-positive data on actual international flows and the sharply negative swing in the discourse about globalization may be rooted, ironically, in the tendency of even experienced executives to greatly overestimate the intensity of international business flows," writes Ghemawat. Moreover, his research suggests that public policy leaders "tend to underestimate the potential gains from increased globalization and to overestimate its harmful consequences."

The once-popular vision of a globally integrated enterprise operating in a virtually borderless world has lost its hold, weakened not just by politics but by the realities of doing business in very different markets with very different dynamics and rules. Now is the time for business and political leaders to find a balance—encouraging policies that generate global prosperity at a level that democratic societies can accept.

ADI IGNATIUS, EDITOR IN CHIEF

CHRISTOPHER CHURCHILL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While serving as a marketing executive at three companies in the early 2000s, **Kim Whitler** noticed how frequently CMOs changed jobs. When she left to study for a doctorate at Indiana University, in 2009, she began looking at why. "My research is designed to help CMOs perform and succeed," says Whitler, now an assistant professor at the University of Virginia's Darden School. "If this article causes just one CEO to think differently about the best way to manage the CMO role, I'll be thrilled."

45 SPOTLIGHT
Why CMOs Never Last

As a management consultant right out of college, **Leslie Perlow** was stunned by the long, unpredictable hours that she and her colleagues were putting in. Did it really have to be this way? Years later, as a professor, she did research to shed light on that question. That's when Perlow found that if a team of consultants focused on making their work a little more predictable, they could greatly improve their performance and work/life balance. After her findings turned out to be generalizable across companies and industries, she started to experiment with meetings in an attempt to achieve the same goals.

62 FEATURE
Stop the Meeting Madness

Sandra Sucher worked for 20 years in fashion retail (remember Filene's Basement?) and at Fidelity Investments before joining Harvard Business School. She knows firsthand how tough even the simplest ethical dilemmas can be, and her research focuses on practical approaches that business leaders can take when faced with them. She is at work on a book about how managers can exercise authority and earn trust as they wrestle with the implications of automation and globalization.

139 CASE STUDY
Follow Dubious Orders or Speak Up?

Pankaj Ghemawat's fascination with borders and distances began when, as a child, he moved from India to Indiana and then back again. A global citizen (he's based in both Barcelona and New York City), he has long taken issue with the conventional wisdom on global strategy. "When I published my first book on globalization, in 2007, the general conviction was that the world was flat or getting that way—and that strategies of bigger and blander were warranted," he says. "That was unrealistic. It is interesting that the pendulum has now swung to the opposite extreme." Ghemawat argues that today's focus on localization as the strategy du jour is just as wrong.

112 FEATURE
Globalization in the Age of Trump

An artist who works in both New Zealand and his native Estonia, **Eiko Ojala** likes to keep his "digital papercuts"—images of paper cutouts that he edits digitally—as simple as possible. To illustrate this article, he says, "I set myself a goal to show how many, how big, and how intense are the challenges that the U.S. Navy faces in the future."

102 FEATURE
Managing Climate Change: Lessons from the U.S. Navy

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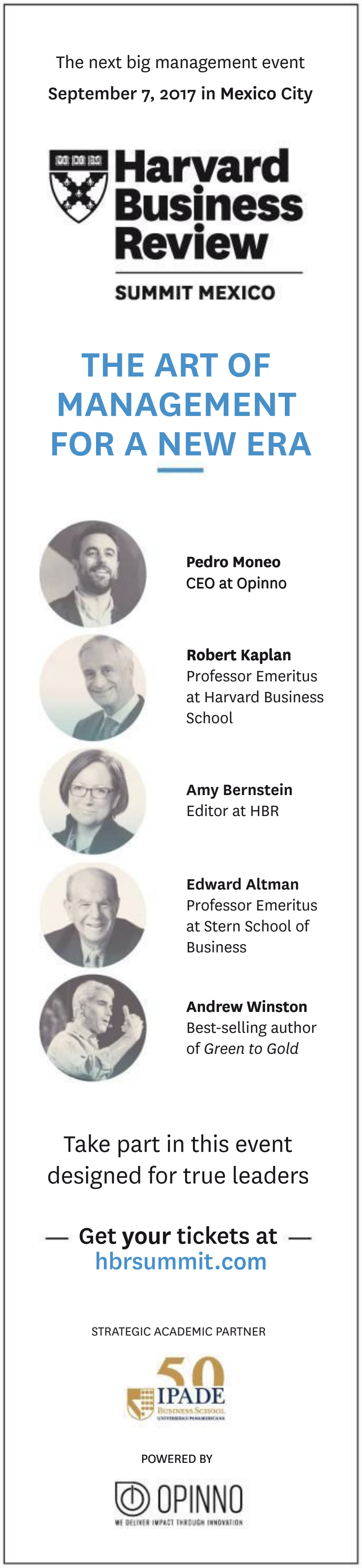

INTERACTION

The Error at the Heart of Corporate Leadership

MOST CEOS AND BOARDS BELIEVE THEIR MAIN DUTY IS TO MAXIMIZE SHAREHOLDER VALUE. IT'S NOT.

BY JOSEPH L. BOWER AND LYNN S. PAINE

THE ERROR AT THE HEART OF CORPORATE LEADERSHIP

HBR ARTICLE BY **JOSEPH L. BOWER** AND **LYNN S. PAINE,** MAY–JUNE

The idea of shareholder primacy is rooted in agency theory, laid out by academic economists in the 1970s. Simply put, the notion is that shareholders own the corporation and, by virtue of that, have ultimate authority over its business. The authors demonstrate the flaws in the theory, particularly its inability to deal with the "accountability vacuum" that arises because shareholders—many of whom are merely short-term investors—have no real responsibility to the companies whose stock they own. They argue that the current orthodoxy is an "extreme version of shareholder centricity" that is "confused" as a matter of law and harmful to society. It forces executives to focus excessively on the short term, weakening companies' long-term prospects and damaging the overall economy.

I would add that we also have to consider that companies drain a lot of resources from the system: They borrow money from banks that is provided by account holders; they benefit from regulations, laws, and market structures to sell their products, which are also provided by the system; they hire employees who are trained and educated with funds endowed by governments and the private sector; they use physical infrastructure and utilities that are built with public funds; and so on. From an economic point of view, companies have an objective to maximize social returns by behaving as citizens.

Manuel Lafuente, freelance consultant in strategy and innovation

Working primarily in the Australian market, I am not quite as pessimistic as Professors Bower and Paine about the prevailing model; I believe it has evolved to take account of many of the issues they raise.

I believe that the agency model—and the creation of independent boards as the representatives of shareholders—were adopted principally to counter the moral hazard of managers' acting to benefit themselves rather than the funders of the firm. (In Australia we overwhelmingly adhere to separating the independent non-executive chairman from the CEO.) Regrettably, corporate scandals still occur, which shows that risk is alive and well. But the real point here is about the funders of the firm. If boards and management don't address their desire to get an adequate return on their invested capital, no other stakeholder interests can be met, because there will be no firm, let alone funds to dedicate to this purpose.

In recent years in Australia, however, the concept of "social license" has become increasingly prominent in business circles: a realization that failing to take appropriate account of stakeholders other than shareholders can create an existential threat. If the community in which your key assets are located is strongly opposed to your operations, you will not succeed, no matter how many laws are passed in your favor. If Millennial employees feel that the firm is socially or environmentally irresponsible, you will not be able to attract the talent you require. Thus, in order to deliver the necessary returns to shareholders, you must take into account a broader stakeholder perspective.

The point made by the authors and the online commentators about the diversity of shareholders on the register is important. In serving the interests of "all" shareholders or the company "as a whole," my approach is to interpret the obligation as serving the long-term interests of shareholders: In other words, boards and management should make decisions not on the basis of short-term holders' desires but, rather, according to the interests of those likely to be holding the stock longer.

Nora Lia Scheinkestel, associate professor, Melbourne Business School; nonexecutive director, Telstra

> "Failing to take appropriate account of stakeholders other than shareholders can create an existential threat."
>
> – NORA LIA SCHEINKESTEL

Finally, a cogent, persuasive, compelling set of arguments that show why the current version of short-term, maximize-shareholder-value capitalism is wrong and dangerous. Might this be the moment when the scales begin to tip back toward a form of capitalism that can, will, and should survive the onslaught of negative impacts we see today? As the former CEO of five companies, and having served as a board member of 11 organizations, I applaud this effort.

Bob Vanourek, president, Vanourek & Partners

For a long time cities have been told to operate more like a business. Professionals in public administration and public service have wrestled with how terms such as "customers" and "shareholders" can apply to citizens and elected officials. This new model can open discussion about how a company-centered model might be encouraging business to acknowledge its role in the community. And it might bridge a key gap that has long frustrated and distanced the private sector from the public sector: sustaining social and community objectives for the long term.

Ann Pappert, former CAO, City of Guelph, Ontario

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PIONEERS, DRIVERS, INTEGRATORS, AND GUARDIANS

HBR ARTICLE BY **SUZANNE M. JOHNSON VICKBERG** AND **KIM CHRISTFORT,** MARCH–APRIL

Why do teams fail? The authors, both at Deloitte, say it comes down to differing work styles. By teaming up with Rutgers's Helen Fisher, a biological anthropologist, and others, they developed an assessment that helped them identify four work-style categories: pioneers, drivers, integrators, and guardians. Most of us are composites, with one or two styles predominating. Pioneers love spontaneity and hate process; guardians love predictability and hate disorder. Those two styles may alienate each other, but they don't have to. The key to leading productive teams is managing the four styles with greater awareness.

The real challenge is how people use this data to make an impact on themselves and their organizations. When I use assessments in business settings (which I do infrequently), I point out that you should get three takeaways: (1) increased self-awareness, (2) ways to work more collaboratively by understanding your colleagues, and (3) ways to improve your behavior so that you can be more effective.

Personality assessments tend to do a good job on the first two but miss the mark on the third, because they essentially box people into a profile that defines them. Afterward, people walk around thinking of themselves as that profile. But then what?

If we focus on identifying and strengthening competencies, instead of just defining ourselves with labels, we may be better able to improve where we need to.

Richard S. Citrin, president, Citrin Consulting

I don't think it is helpful to refer to psychometric profiling as a science. There are no absolutes in human behavior. As the authors acknowledge, personality profiling is not a new or even an exact science, and many variants of measures and products are on offer. In our consulting work we often use profiling tools; we stress that they are good for creating a framework for a productive discussion about how people do things differently and for providing a language in which to talk about these differences.

Labeling people as drivers, guardians, and so on overlooks the complexity of how people go about doing things. It can lead to stereotypical generalizations (such as "All drivers respond like that") and can even condone bad behavior ("As a driver, I don't pay attention to detail").

It is far more helpful to use these profiles to talk about ranges of responses and situational dynamics than to pinpoint work types as one thing.

Jan Emerton, director, WW Consulting

This article supports the long-accepted view that an understanding of personality styles can help teams function more effectively. But what's missing is a focus on the roles team members need to play and the abilities they need to perform those roles well.

Over the years, we have studied teams tasked with implementing business initiatives for which investments were significant and failure was not an option (for example, implementing change, driving innovation, entering new markets). In the process we discovered that the most successful teams had people playing four specific, well-defined roles—sponsor, manager, expert, and entrepreneur—with each of them having a unique personality profile and unique abilities. Teams with different responsibilities and objectives might require different roles.

My point is that one should first focus on the work to be performed by the team and the roles that need to be played to do that work effectively; then one can decide who should serve on the team. Adding the element of personality styles will help fine-tune and optimize team performance.

George O. Klemp Jr., partner, Cambria Consulting

The four styles the authors have identified are substantively no different from the temperaments that can be identified using either the Myers-Briggs Type Indicator or the Keirsey Temperament Sorter. I don't disagree with their observations—I just point out that these four styles, or temperaments, have been studied and discussed for a long time.

Lawrence Van De Valk, executive director, LEAD New York; senior extension associate, Cornell University College of Agriculture and Life Sciences

This article certainly offered a few interesting insights, but I disagree with the positioning of Fisher's approach as new or groundbreaking. The Herrmann Whole Brain Model, together with the Herrmann Brain Dominance Instrument—which has been featured in these pages in the past—has explored the implications of the same four brain systems on the basis of cognitive neuroscience and development in a business setting (General Electric). It has decades of research and millions of completed assessments behind it, and I wouldn't be surprised if it inspired some of the work outlined above.

Karim Nehdi, head of global innovation, Herrmann International

I was left wondering what this "new tool" does that others don't. The authors say, "Existing personality tests didn't do the… trick, and they relied too heavily on personal introspection." Many tools indeed worked, and that's why the Belbin Team Inventory is so powerful. It looks at observable

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behaviors within a team, not personality traits or inborn preferences. In addition, observers are asked to do peer assessments. The tools the authors describe don't seem to reach the same depth and validity or reliability that Meredith Belbin built up over several decades.

Whatever the tool, the key is not in the report or in the scores but in the conversations that teams start to develop, during dedicated team sessions and then outside them. But to say that this is part of "the new science of teamwork" is a bit too strong.

Peter Cauwelier, chief team connector, Team.as.one

The author Kim Christfort responds:
Not surprisingly, different style assessments, developed independently, often identify similar types, since each looks at the same underlying thing: human behavior. Our intent in creating Business Chemistry was not to make a discovery about the nature of humans but, rather, to provide a new lens on the dynamics of these types in a business environment. This tool works well for us and our clients primarily because it's pragmatic, easy to use, and memorable. But we wouldn't be practitioners of Business Chemistry if we didn't acknowledge that some people may prefer other systems. Ultimately, the deepest insights emerge not from basic identification of types (regardless of the assessment) but from analysis of how the dynamics of work style play out in a business setting. The translation of these findings into practical management approaches that help drive business performance is what makes Business Chemistry such a powerful addition to the field.

THE TALENT CURSE

HBR ARTICLE BY **JENNIFER PETRIGLIERI** AND **GIANPIERO PETRIGLIERI,** MAY–JUNE

High potentials who are being groomed as future leaders would appear to have it made—but their seeming good fortune can turn out to be a curse. As they strive to conform to company ideals for leadership, they often bury the qualities that made them special. They become reluctant to take risks, lest they prove themselves unworthy. This "talent curse" can hinder personal growth, performance, and engagement—and even push people out the door.

A slightly different but related phenomenon can also occur. Often a high performer will begin to be treated differently, regardless of his or her level of experience or developmental weaknesses. Such individuals are often deprived of the necessary ongoing feedback and challenges they need to maintain a high level of performance and to reach their full potential. They are typically promoted quickly on the basis of their performance in a particular area without any thought to their need for additional experience or development. This can result in less-than-favorable outcomes for them in supervisory or management positions. Unfortunately, their early "star" status makes them difficult to coach at this stage by interfering with their self-awareness and how they perceive the need for constructive criticism or additional growth.

Brian W. Moyer, senior administrative officer, Hernando County (FL) Sheriff's Office

As a manager, I try frequently to reinforce with my team members that they are setting standards for themselves and then to initiate open discussion of what those standards may be, encouraging the team to reflect on both strengths and weaknesses. This creates an atmosphere that I hope helps reconcile the tension between authenticity and conformity, because it allows individuals to bring themselves to work while also developing empathy for diverse perspectives in the workplace. In the end, this curse can best be addressed if both individuals and organizations take responsibility for fostering positive talent identities and an atmosphere of growth.

I sent this article to my team and asked if they have experienced this curse. I will be fascinated to hear their thoughts.

Suzan Brinker, global marketing manager, Penn State Outreach & Online Education

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Idea Watch

HOW TO PREDICT TURNOVER ON YOUR SALES TEAM

A new study sheds light on who is likely to quit and when an intervention may be in order. Plus the dark side of stretch goals, how seating arrangements affect productivity, why cognitive diversity boosts team performance, and more

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Crowded Places Make People Think More About the Future

HOW I DID IT

SoulCycle’s CEO on Sustaining Growth in a Faddish Industry

HBR ANALYTIC SERVICES

Anchoring Customer Experience in the Social Experience

Leading-edge companies are moving beyond treating customer experience as a customer service challenge and seeing it as a fundamental driver of competitive advantage at every customer touchpoint. Equally important, organizations in the lead don't treat social media as just a marketing channel. They realize that people are inherently social beings and that social media is becoming the predominant form of communication that shapes how people think and what they buy. A recent Harvard Business Review Analytic Services global survey found that companies that thoroughly integrate social media and customer experience offer vastly superior customer experiences than competitors do, which translates into stronger growth and dominant positions in their markets.

VIEW THE FULL REPORT
hbr.org/hbr-analytic-services

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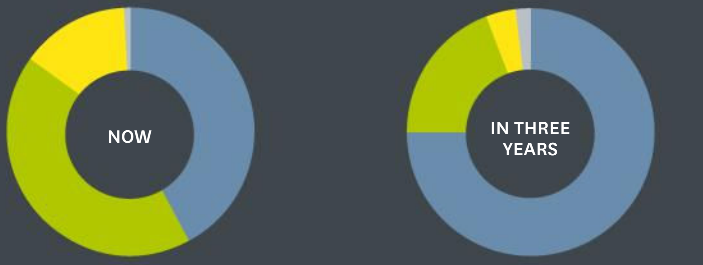

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“IN COMPANIES WITH LITTLE VARIATION IN PERFORMANCE, REPS ARE LESS LIKELY TO FEEL CHALLENGED AND MAY HAVE LITTLE INCENTIVE TO WORK HARDER; THEY’RE APT TO LEAVE INSTEAD.”

From “How to Predict Turnover on Your Sales Team,” page 22

ILLUSTRATION BY DAVE WHEELER

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IT'S NOT ENOUGH TO KNOW WHO YOUR STARS ARE.
YOU NEED TO MAKE SURE THEY DON'T LEAVE.

HOW TO PREDICT TURNOVER ON YOUR SALES TEAM

Companies worry about employee attrition in every department, but it's especially costly in one function: sales. Estimates of annual turnover among U.S. salespeople run as high as 27%—twice the rate in the overall labor force. In many industries, the average tenure is less than two years. While some attrition is desirable, such as when poor performers quit or are terminated, much of it isn't—and every time a solid performer leaves, his or her company faces a number of direct and indirect costs. U.S. firms spend $15 billion a year training salespeople and another $800 billion on incentives, and attrition reduces the return on those investments. Turnover also hurts sales: Positions may sit empty while companies recruit replacements, and the new employees must learn the ropes and rebuild client relationships. If managers could identify good salespeople who are at risk of quitting and take steps to retain them, their companies could realize substantial savings.

A new study by four marketing professors, led by V. Kumar, of Georgia State University, can help them do just that. The researchers examined more than two years' worth of data from a *Fortune* 500 telecommunications company that sells consumer electronics and software services, and created a quantitative model—the first of its kind—to predict which salespeople were likely to quit. This work builds on previous research by some of the same academics, who developed a method of estimating an individual salesperson's future profitability (see "Who's Your Most Valuable Salesperson?" HBR, April 2015). Knowing who is most likely to drive profits is useful, of course, but the new research could add greatly to that value: By learning who is at high risk of leaving and why, sales leaders can address problems *before* star performers give notice.

The researchers studied data on 6,727 salespeople working in 1,058 stores, dividing it into two batches. One set of metrics dealt with how well each salesperson was doing; those numbers measured past performance (on the basis of revenue generated), customer satisfaction, and how often monthly quotas were met. The second set measured "peer effects": the variation in performance among coworkers and the voluntary and involuntary attrition in each store. The study controlled for geography, store size, and demographics.

The researchers expected that salespeople with high ratings in historical performance and customer satisfaction would be less likely than average and low performers to quit, because the good marks would increase their sense of job security, their incentive payments, and their feeling that they controlled their ability to succeed—and that proved to be the case. When it came to quota attainment, however, the study showed an inverted-U-shaped distribution: Here, too, high-performing salespeople were less likely than average performers to quit (managers did a good job keeping their stars happy), but so were low performers (their poor showing limited their opportunities at other firms). "It is the 'middling' salespersons who [are] likely [to] turn over," the researchers write. Though those employees aren't "A" players, the loss of them still hurts their firms, because they often constitute a large and profitable part of the sales force.

The biggest surprise concerned peer effects, which turned out to be the strongest predictor of quitting. The researchers theorize that in companies without much variation in performance, people are less likely to feel challenged and may have little incentive to work harder or smarter; they're apt to leave instead. In settings with high voluntary turnover, employees often lose faith in the company's strategic direction (because they see others jumping ship), and they tend to be more aware of outside job opportunities, partly because their networks include former colleagues who recently defected. And when there's lots of involuntary turnover, employees may lack trust in managers,

JAY MINCKS

“IF I KNOW BEFORE THEY HAVE AN OFFER, THAT’S A BIG PLUS”

Jay Mincks is the executive vice president of sales at Insperity, a Houston-based HR outsourcing firm with 50 offices and a 600-person sales organization. He recently spoke with HBR about predicting and preventing attrition. Edited excerpts follow.

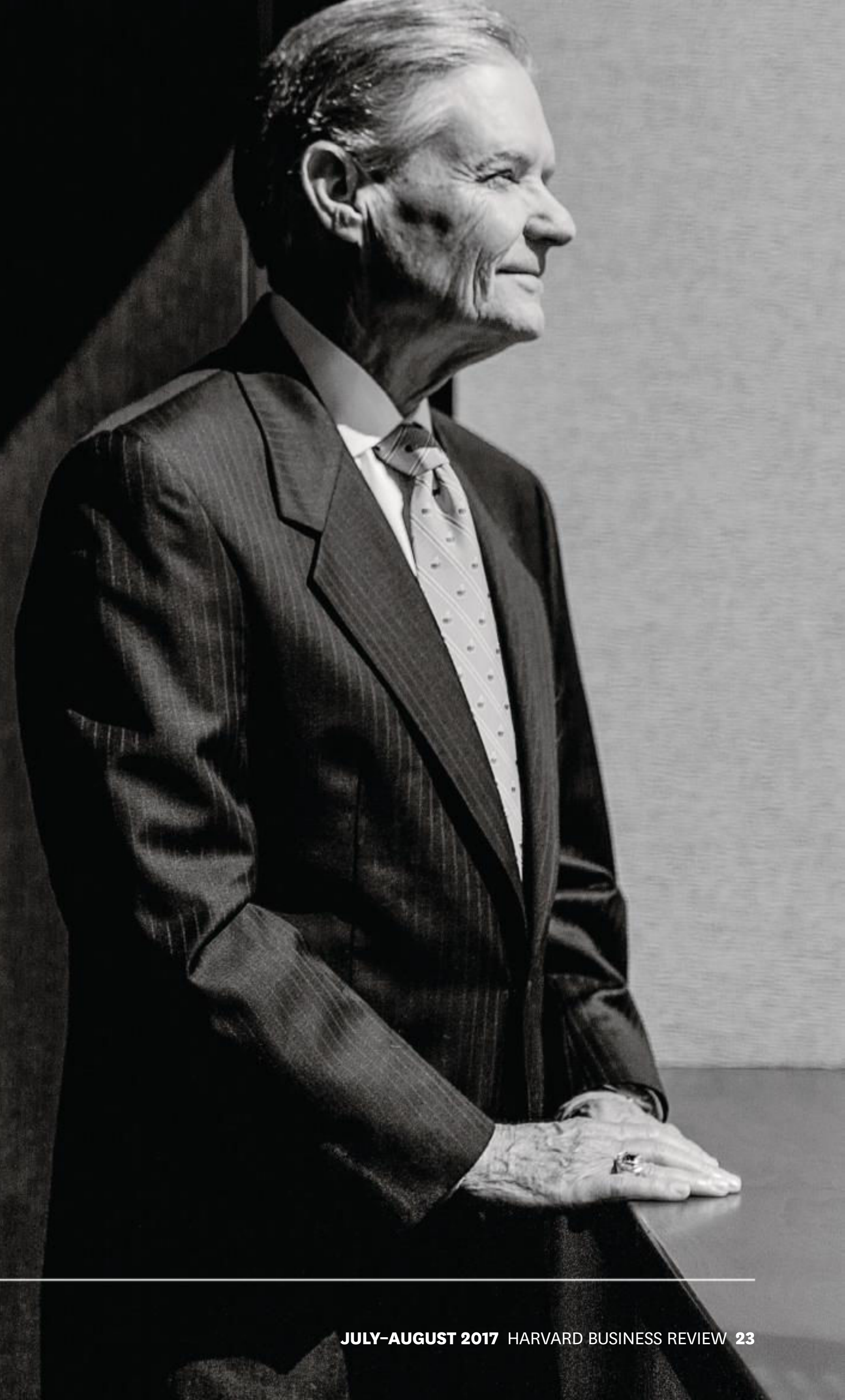
How much turnover do you experience in your sales force? It averages 28% a year, but that number is a little deceptive. We sell a complex, intangible product, so there’s a steep learning curve. It takes 12 to 18 months before someone is really up to speed, and during that time, the turnover rate is unacceptably high. But after that, turnover among our “A” players is just 5%. Our compensation plan ensures that we rarely lose our best salespeople.

If you suspect someone might leave, how effective are you at stopping that? If I know before they have an offer, that’s a big plus. You go in, sit down, and do an intervention. Usually they’ve had their feelings hurt somehow, so you have to fluff them back up, tell them they’re appreciated, and ask: What could we do to make your life better and keep you? If we catch it early, we have almost 100% success.

What about after someone has an offer? If we make a counteroffer, the success rate is about 50%. But of the half who stay, many will still leave soon. Whatever drove them to look for another job is still inherently there. Counteroffers can buy people back for a while, but if they’ve checked out once, it’s easy to check out a second time.

Would you like to rely more on data to predict who might quit? Anything I can do to take intuition out of the equation is helpful. I have to hire 12 new sales managers this year. I’m not sure all of them will have the right intuition. Being able to rely on data would be invaluable—it would take some of the mystery out of it and give us more opportunities to do an intervention before someone walks out the door.

If you could design a dashboard to manage turnover, what would be on it? Actually, I’d be more interested in data predicting which of the salespeople I hire will succeed; that would be the holy grail. We use recruiters, and we conduct interview after interview, but it’s so hard to tell—salespeople can be chameleons. We spend all this time and effort training them, yet too many fail. It’s debilitating to my sales trainers. Our organization could save millions if we could find a way to use data to drive the number much lower.



PHOTOGRAPHY BY MAX BURKHALTER

CONTINUED FROM PAGE 22

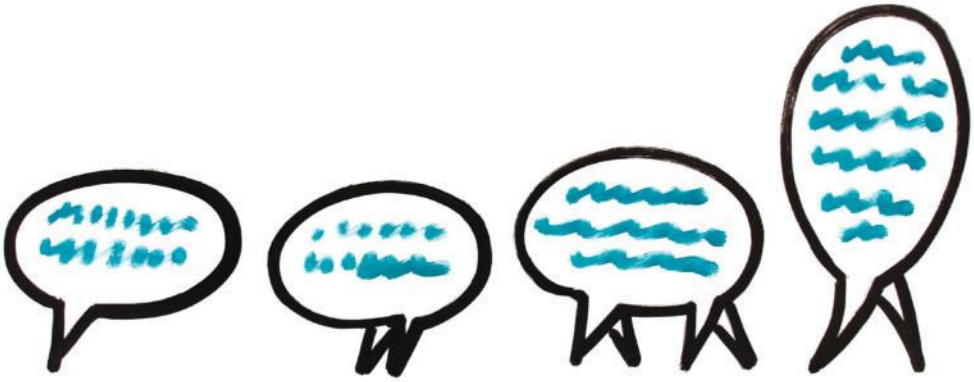
feel little job security, and move on. “An individual’s attitudes and intentions are heavily influenced by his or her environment,” the researchers write; the strength of the peer effects in the model suggests that turnover can be contagious.

This research is part of a broad trend of efforts to understand what events cause employees to seek greener pastures and what behaviors indicate that they may be doing so—issues of increasing relevance in an era of tight labor markets and the growing use of analytics. For instance, research by the advisory firm CEB examined how events in employees’ personal lives, such as milestone birthdays and college reunions, spur them to take stock and to compare their careers with others’, often prompting them to job hunt (see “Why People Quit Their Jobs,” HBR, September 2016). And a study by researchers at Utah State and Arizona State identified 13 “pre-quitting” behaviors, likening them to poker tells; these include leaving work early, showing less focus or effort, and being reluctant to commit to long-term assignments.

One implication of the new study is that managers should pay careful attention to peer effects and consider conducting interventions in settings with little performance variation among employees and ones with rising levels of turnover. But Kumar says the larger message *isn’t* that firms should plug their data into the model predicting turnover at the telecom’s stores. Rather, it’s that big data can enable companies to identify variables that predict turnover in their own ranks. In the future, managers might routinely rely on data-driven dashboards labeling employees as being at high, moderate, or low risk of quitting. They could then decide which members of the high-risk group warrant interventions to help them stay put.

HBR Reprint F1704A

ABOUT THE RESEARCH “Why Do Salespeople Quit? An Empirical Examination of Own and Peer Effects on Salesperson Turnover Behavior,” by Sarang Sunder, V. Kumar, Ashley Goreczny, and Todd Maurer *(Journal of Marketing Research, 2016)*



ENTREPRENEURSHIP

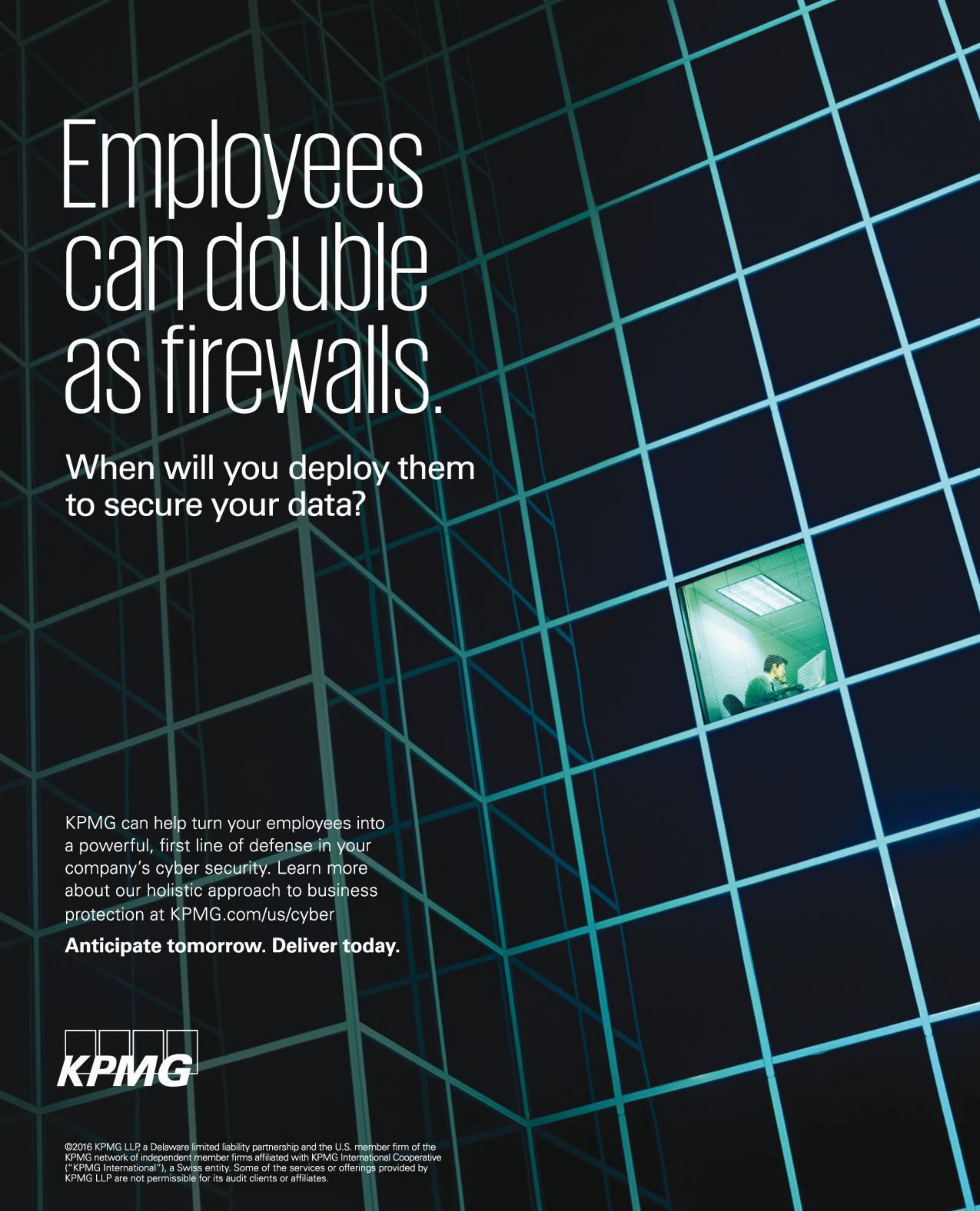
EVERY PIVOT NEEDS A STORY

FOUNDERS KNOW THAT no matter what their original business plan, managing a start-up requires navigating a fast-moving stream of hypotheses, experiments, and redirections, which often result in the adoption of a very different model. But even entrepreneurs who celebrate the pivot don’t always recognize the need to share the underlying rationale with customers, investors, and journalists, who might otherwise be confused or disappointed by the change in direction.

New research that analyzed the communications of two start-ups over a six-year period offers a three-part theoretical framework to guide fledgling firms through their own strategic shifts. Although the companies studied had similar profiles, pivots, and end products (both eventually decided to offer automated investment tools), one grew into a $2 billion company, while the other held a fire sale of assets and folded. The difference, the researchers say, was how course corrections were explained. Founders should craft an “abstract product frame” that gives them room to maneuver (the failed firm in the study got hemmed in by overly narrow initial claims); use language that links any new position to their founding principles, creating a sense of continuity; and pair major pivots with carefully paced conciliatory rhetoric to mollify supporters of the original idea.

“How startups *explain* strategic reorientations may matter as much as or more than the changes themselves,” the researchers write. “Entrepreneurs resemble scientists in that they generate and test hypotheses to find viable product solutions; but they must also resemble adept politicians by convincingly justifying deviations from plan to diverse constituencies.” ■

ABOUT THE RESEARCH “Pivoting Isn’t Enough: Principled Pragmatism and Strategic Reorientation in New Ventures,” by Rory McDonald and Cheng Gao *(working paper)*

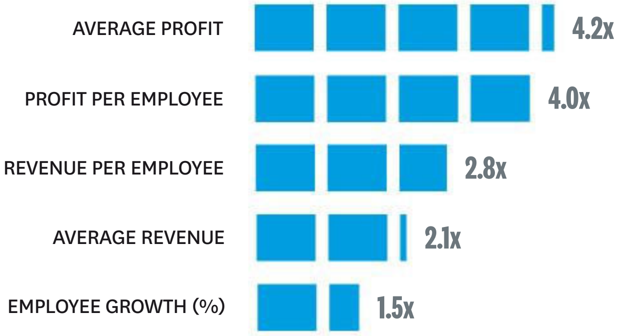

Employees can double as firewalls.
When will you deploy them to secure your data?
KPMG

TALENT

INVESTING IN EMPLOYEES PAYS OFF

After analyzing 250 companies, a researcher identified the top 6% with regard to investments in three areas of employee experience: technology, physical surroundings, and culture. Those companies, which include Adobe, Accenture, Facebook, and Microsoft, equipped employees with high-end technology, spent more than the other companies on office architecture and furnishings, and helped workers understand how their tasks contributed to the organization. In terms of shareholder returns, they outperformed the S&P 500, the NASDAQ, *Fortune*'s 100 Best Companies to Work For, and Glassdoor's Best Places to Work by considerable margins. And they surpassed the other companies in the study on the metrics below. ■

AMOUNT BY WHICH COMPANIES THAT INVESTED IN EMPLOYEES OUTPERFORMED OTHERS



SOURCE *THE EMPLOYEE EXPERIENCE ADVANTAGE*, BY JACOB MORGAN (WILEY, 2017)

TECH WORKERS IN U.S. STATES THAT STRONGLY ENFORCE NONCOMPETE EMPLOYMENT AGREEMENTS EARN LESS THAN THEIR COUNTERPARTS IN OTHER STATES—AND THE WAGE-SUPPRESSING EFFECT PERSISTS THROUGHOUT THEIR CAREERS.

"LOCKED IN? THE ENFORCEABILITY OF COVENANTS NOT TO COMPETE AND THE CAREERS OF HIGH-TECH WORKERS," BY NATARAJAN BALASUBRAMANIAN ET AL.

M&A

PRESTIGIOUS FIRMS MAKE RISKIER ACQUISITIONS

COMPANIES MAKE ACQUISITIONS for all sorts of reasons, including to gain access to new technologies, markets, or talent and to fuel growth. But the deals come with risks. Firms often overpay; markets may react badly to merger news; many acquirers struggle to integrate their targets; often the technologies driving a deal don't pan out. To assess how a company's reputation affects its M&A behavior, researchers studied 75 firms on *Fortune*'s list of most admired companies from 1991 to 2008, pairing each with a similar firm not on the list and examining the frequency with which the firms in each pair made acquisitions, the size of deals, how closely related the targets were to the existing business, and the market reaction to each event. They found that highly admired firms made more acquisitions and went further beyond their existing industries. That's a high-risk strategy, because more deals increase the odds of making mistakes, and entering new industries or markets requires developing new kinds of expertise. Those firms didn't appear to overpay; deals ran the gamut in size and included many small mergers. But surprisingly, given their status, they encountered a more negative market reaction to deals than other companies did. High-reputation firms, which averaged $50 billion in market capitalization, saw their market cap drop by $300 million more than that of their low-prestige counterparts after announcing a deal. Investors seemed to interpret their aggressive acquisitiveness as a signal that internal growth opportunities were limited, the researchers say. At a minimum, the results suggest that prestigious companies need to do a better job of explaining merger activity to the markets, in hopes of reducing the share-price penalty when deals are announced. ■

ABOUT THE RESEARCH "High-Reputation Firms and Their Differential Acquisition Behaviors," by Jerayr J. Haleblian, Michael D. Pfarrer, and Jason T. Kiley (*Strategic Management Journal,* 2017)

€12,000

The pay increase needed to give a female executive the same boost in happiness that a male executive gets from a €5,000 raise, according to a study of German managers.

"WHY MANAGERIAL WOMEN ARE LESS HAPPY THAN MANAGERIAL MEN," BY HILKE BROCKMANN ET AL.

WORKPLACES

THE DARK SIDE OF STRETCH GOALS

IT'S NO SECRET that when facing pressure to meet earnings benchmarks, managers sometimes manipulate both financial and real activities—reducing R&D, advertising, or other expenses, for example. A new study reveals another area that suffers: workplace safety. Using data collected by the U.S. Occupational Safety and Health Administration from 2002 to 2011, researchers discovered elevated injury and illness rates in firms that met or just beat analysts' forecasts—ones presumably feeling the heaviest pressure to perform. This happened, the analysis showed, because managers increased employee workloads or pressured people to work faster and looked to save money on safety-related activities such as employee training and equipment maintenance. The lowest injury rates occurred in firms that easily met earnings expectations; comfortable about their prospects, they put less added performance pressure on their workers, the study found.

"Given the opacity of real activities management, our findings indicate that timely disclosures about employee health and safety, which are being considered by some firms, could serve as signals to investors," the researchers write. ■

ABOUT THE RESEARCH "Earnings Expectations and Employee Safety," by Judson Caskey and N. Bugra Ozel (*Journal of Accounting and Economics*, 2017)

CONSUMER BEHAVIOR

LESSONS FROM THE SUSHI CONVEYOR BELT

The fashion industry has traditionally introduced new apparel twice a year (for the spring/summer and fall/winter seasons), with most retailers rolling out all their merchandise at once. But over the past decade a new model, called *fast fashion* and led by Zara and H&M, has profited by rotating merchandise much more rapidly, creating an urgency to buy. "Flash sale" websites, such as Rue La La, operate similarly. In a new paper, researchers explore how and when companies can take advantage of the "sequential assortment" strategy, in which goods are added to the shelves over time instead of all at once.

"When a fast fashion or flash sales retailer starts selling sandals in March, the customer must decide which pair(s) of sandals to purchase without knowing the new styles of sandals that the retailer will offer in April," the researchers write. "It is precisely this uncertainty that may cause the customer to purchase a pair of sandals in March, only to return in April and purchase another pair of sandals that she loves even more." If the shopper had seen the entire sandal selection in April, she might have bought just one pair.

The researchers calculate the "value of concealment," or the incremental revenue a company might win by revealing merchandise over time. They compare the strategy to a restaurant with a sushi conveyor belt that showcases items one by one; diners who choose dishes from a conveyor belt may be prone to eat more than those who order from a menu.

To determine whether concealment will add value, the researchers say, companies need to consider the category of merchandise and the type of shopper. With categories such as apparel, footwear, accessories, and children's toys, people may be open to buying additional items within a short time period, so concealment may add revenue. With categories such as appliances, automobiles, and other big-ticket items, concealment is unlikely to drive incremental purchases; it may even hurt sales, because consumers who suspect that new models will arrive in stores soon may delay or even forgo buying. The researchers also distinguish between myopic shoppers, who are less selective and more impulsive, and strategic shoppers, who are more careful and more willing to forgo a purchase. Concealment works better with myopic shoppers, but companies don't yet have an easy, practical way to determine how many of their customers fit this category. The researchers hope to partner with retailers to obtain data for that purpose in a future project. ■

ABOUT THE RESEARCH "Assortment Rotation and the Value of Concealment," by Kris Johnson Ferreira and Joel Goh (working paper)

J.D. POWER
2017
2016

PRODUCTIVITY

WHY YOU SHOULD SIT NEXT TO A HARD WORKER

COMPANIES SPEND MILLIONS configuring office architecture in an effort to enhance productivity—for example, seeking just the right balance of open areas and quiet spaces to maximize both collaboration and concentration. A new study reveals another performance driver: seating certain types of workers together. Researchers examined two years' worth of data on more than 2,000 tech workers, dividing them into three categories and studying the spillover effects each type exerted on neighboring colleagues in several aspects of performance. "Productive workers" excel in terms of output but fall short on quality, while for "quality workers," it's the reverse; "generalists" are average on both dimensions. Results showed that pairing employees with complementary strengths—seating productive workers near quality workers—boosted organizational performance by as much as 15% (generalists should be grouped together). For a 2,000-person company, this could add up to $1 million more in annual profits, the researchers estimate.

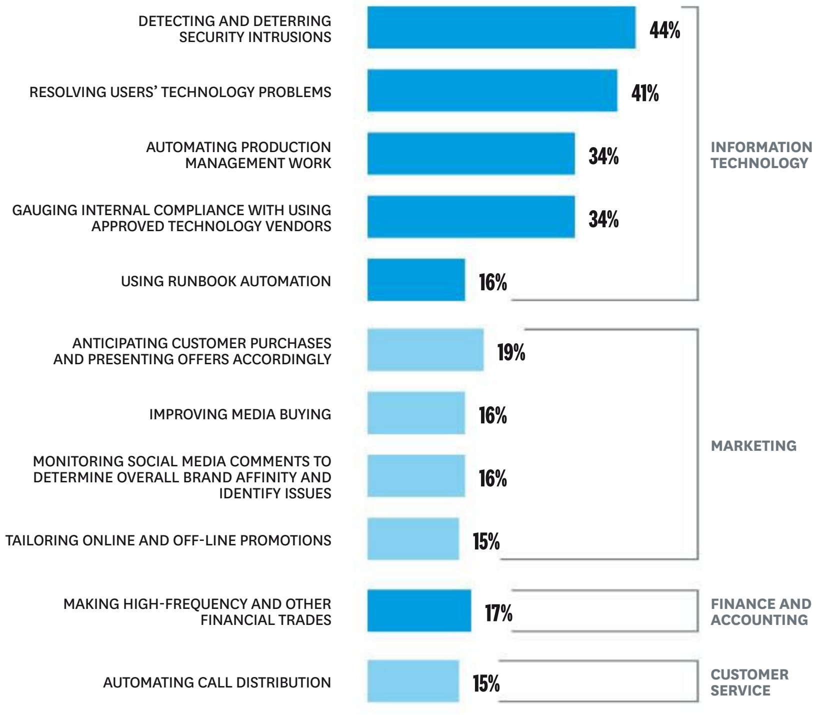
What caused the positive spillover effects? Because they appeared almost immediately—and vanished quickly if the seating arrangement was disrupted—they can be attributed to inspiration and peer pressure rather than to peer-to-peer learning, the researchers say. Exposure to complementary weaknesses did not significantly affect performance, suggesting there's little downside to strategically colocating opposite worker types. "For organizations looking to increase their returns on the human capital of their workforce, simply rearranging employee seating may be one of the most cost-effective resources at their disposal," the researchers write. ■

ABOUT THE RESEARCH "Organizational Design and Space: The Good, the Bad, and the Productive," by Michael Housman and Dylan Minor (working paper)

AUTOMATION

AI's EARLY CONQUESTS

Many workers fear that artificial intelligence means impending job losses. Some research suggests that their concern is warranted: An Oxford University study predicted that 47% of all jobs will be automated by 2033. But in the shorter term, such fears may be overblown. A 2017 survey by Tata Consultancy Services of 835 global companies in 13 manufacturing and service industries found that firms are using AI frequently in computer-to-computer activities but much less often to automate human activities. The researchers believe that these machine-to-machine transactions—not people displacement—are the low-hanging fruit for AI. For example, the survey revealed that AI is used most frequently to detect and fend off computer security intrusions. Automating that task doesn't mean eliminating IT security workers; rather, it helps a typically overloaded department face geometrically increasing hacking attempts. In that way AI makes IT security professionals *more* valuable to their employers—and the same is true in many other functions. The chart below shows the proportion of companies surveyed that use AI for each activity. ■



SOURCE TATA CONSULTANCY SERVICES

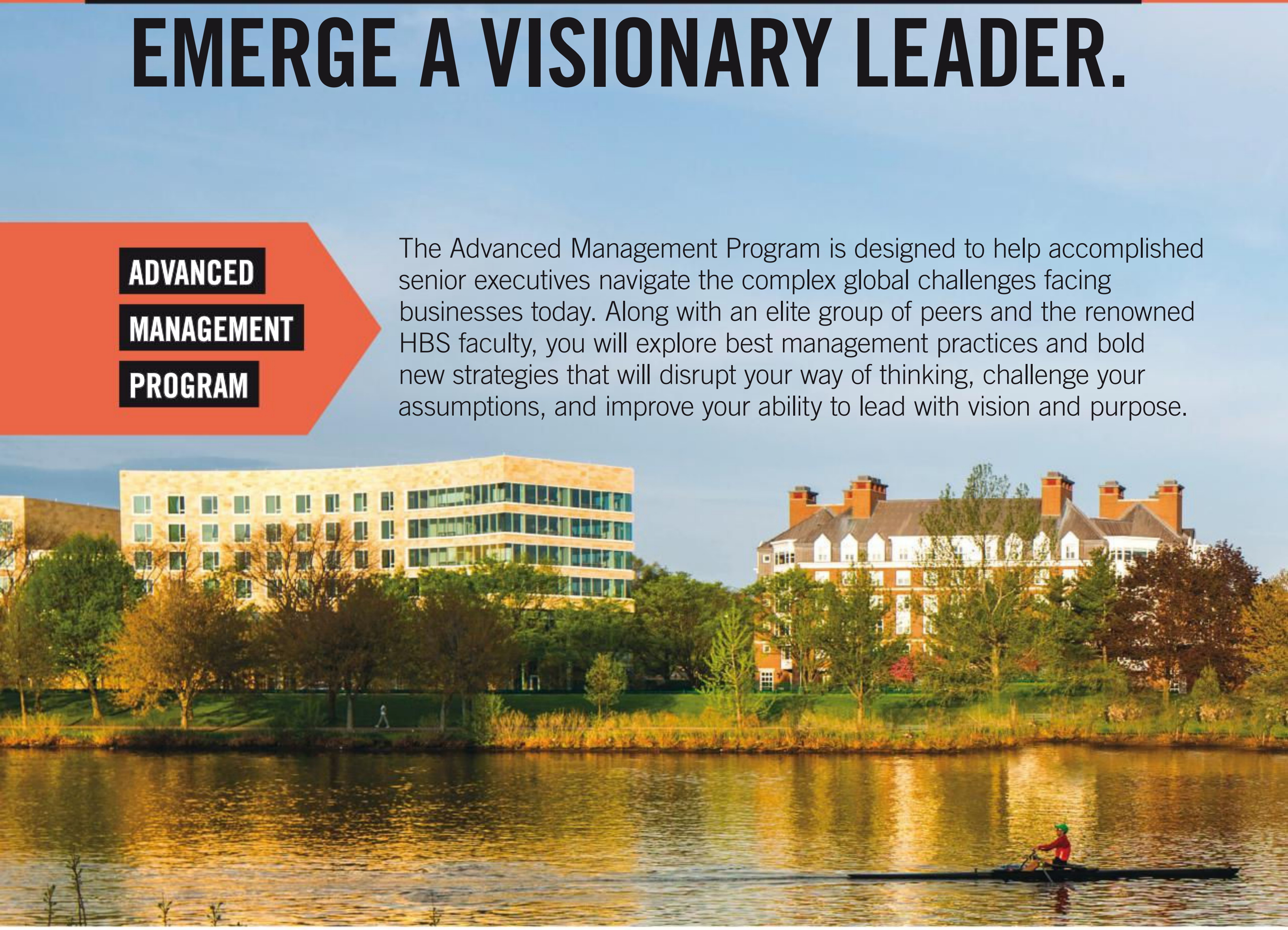
JUDGES HANDED DOWN PRISON SENTENCES THAT WERE

5% LONGER ON "SLEEPY MONDAY"

(the first workday after the switch to daylight saving time)

THAN ON THE PREVIOUS AND FOLLOWING MONDAYS, SUGGESTING THAT SLEEP-IMPAIRED BOSSES AND OTHER DECISION MAKERS MIGHT WANT TO HOLD OFF UNTIL THEY'RE BETTER RESTED.

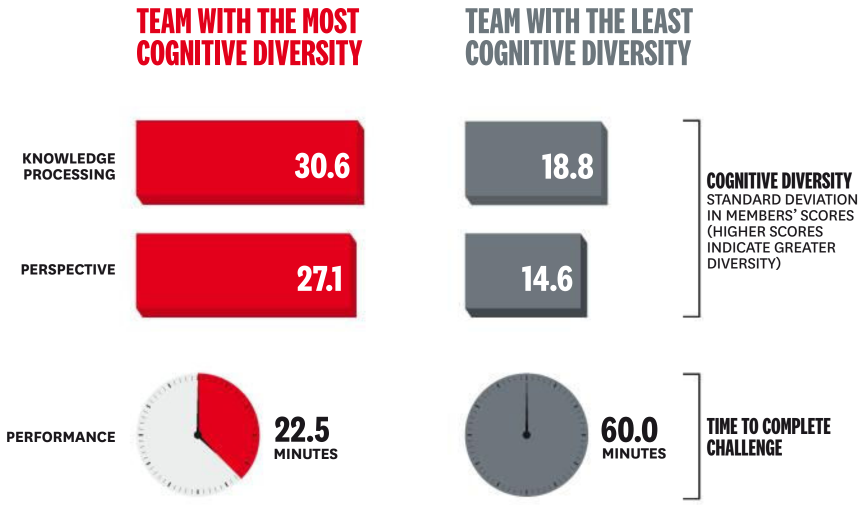
"SLEEPY PUNISHERS ARE HARSH PUNISHERS: DAYLIGHT SAVING TIME AND LEGAL SENTENCES," BY KYOUNGMIN CHO, CHRISTOPHER M. BARNES, AND CRISTIANO L. GUANARA



TEAMS

ANOTHER ARGUMENT FOR COGNITIVE DIVERSITY

In a strategy-execution exercise that asked participants to solve an unfamiliar problem under time constraints, researchers found that teams with greater cognitive diversity performed faster. Specifically, they determined that diversity in **knowledge processing** (how people create knowledge in the face of problems) and **perspective** (how they deploy their own expertise versus orchestrating the ideas and expertise of others) were highly correlated with team success and provided a better explanation of **performance** than did diversity in demographic factors such as age, gender, and ethnicity. "Intuitively, this makes sense," the researchers write. "Tackling new challenges requires a balance between applying what we know and discovering what we don't know that might be useful. It also requires individual application of specialized expertise and the ability to step back and look at the bigger picture." The graphic below shows how the most- and least-diverse teams (according to standard deviation in members' scores) differed in performance. ■



SOURCE ALISON REYNOLDS AND DAVID LEWIS

HARVARD BUSINESS REVIEW APRIL 1931

> "When we have so many more workers than are needed to do the nation's work under modern methods, clearly the logical way out is to reduce the hours of work and create more employment. This is the only fundamental solution and it is thoroughly in keeping with modern progress, both industrial and social."

"THE FIVE-DAY WEEK," BY WILLIAM GREEN

FINANCE

HOW INVESTORS REALLY USE ESG SCORES

MORE THAN 100 rating agencies provide environmental, social, and governance (ESG) data on publicly traded companies, and more than 1,400 specialized socially responsible investment firms use ESG ratings when analyzing stocks and bonds. But little is known about how mainstream investment firms use ESG data. A new survey of 413 global investment professionals (mostly portfolio managers) provides insight.

The responses show that 82% of investors believe ESG data is material to investment performance, mostly because it provides information about downside risks, including reputational, legal, and regulatory risks. Investors use ESG data primarily as a negative screen; that is, they avoid stocks with low ESG ratings out of concern that the behaviors causing those ratings will lead the stock to underperform. One third of investors expect ESG ratings to be increasingly used for positive screening (in which portfolio managers seek companies with high scores) and active ownership (in which they prod company managers to improve ESG performance) over the next five years.

Despite the widespread use of these ratings, the survey found some skepticism: Across a variety of questions, 20% of investors consistently said they don't believe ESG scores affect stock performance. ■

ABOUT THE RESEARCH "Why and How Investors Use ESG Information: Evidence from a Global Survey," by Amir Amel-Zadeh and George Serafeim (working paper)

COMPILED BY HBR EDITORS | SOME OF THESE ARTICLES PREVIOUSLY APPEARED IN DIFFERENT FORM ON HBR.ORG.

Oliver Sng—a research fellow at the University of Michigan—and colleagues at Arizona State University compared country and state population-density figures against data on residents' willingness to invest in education, save for retirement, and otherwise plan for the future. Their analysis revealed that people in more-populated areas showed a significantly stronger preference for activities with a long-term payoff. The team's conclusion:

CROWDED PLACES MAKE PEOPLE THINK MORE ABOUT THE FUTURE

DR. SNG, DEFEND YOUR RESEARCH

SNG: Based on these findings and on follow-up experiments designed to test causation, I do believe there's a link between population density and what biologists refer to as "life-history strategy." The general idea is that species and organisms either live "fast"—focusing on the present, reproducing early, bearing lots of offspring, and not investing as much in each child or in themselves—or "slow," focusing on the future, self-development, longer-term relationships, and fewer kids. Humans pursue a slower life-history strategy than other animals do, but there is variation among us, and while some of that may be genetic, we've also evolved to respond to our environment. In crowded places, where there's arguably greater competition for resources, we might feel we need to invest more in ourselves and our kids to succeed. That's the hypothesis my coauthors, Steven Neuberg, Michael Varnum, and Douglas Kenrick, and I wanted to test.

HBR: And it proved correct? Yes. In more-densely-populated countries, we saw less sexual promiscuity, lower fertility rates, higher preschool enrollment, and a greater societal emphasis on planning for the future versus solving today's problems. In more-densely-populated U.S. states, people married later, had fewer children, and were more likely to attain a bachelor's degree and participate in retirement savings plans. All these measures of future orientation build on one another, but population density seems to play a foundational role. These findings held up even when we controlled for population size, economic prosperity, and urbanization.

Couldn't it just be that forward-thinking people prefer more-populated areas? That's why we did the experimental studies. In the first one, we asked half our participants—people recruited online from all over the United States—to read a fictitious *New York Times* article about how the U.S. population was growing at an unprecedented rate. We then had them answer questions designed to gauge their future orientation, such as "Would you want to get $100 tomorrow or $150 in 90 days?" The other half, our control group, read no article but took the same survey. We found that people given the article showed a greater preference for the delayed but larger rewards. Though small, the effect was significant. By artificially introducing the idea of high density, we seem to have pushed people to think more about the long term.

PEOPLE LIVING IN DENSELY-POPULATED STATES WERE MORE LIKELY TO PARTICIPATE IN RETIREMENT SAVINGS PLANS.

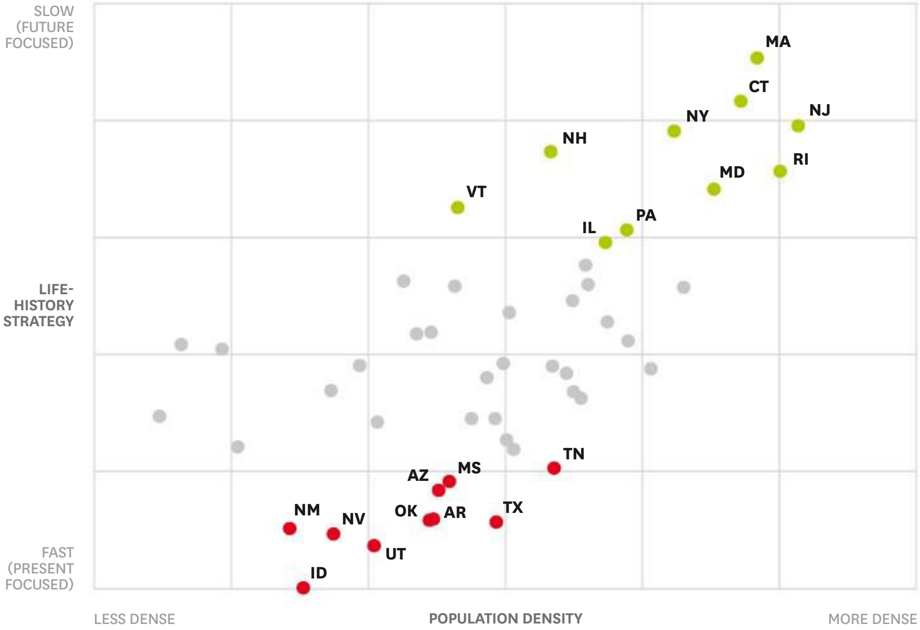
Maybe reading just got their brains working, which led them to make smarter decisions? In the next study we dropped the article and instead asked participants to listen to audio clips—of either lots of people talking or white noise—before answering the questions. Those who heard the crowd sounds were also more likely to prefer long-term rewards.

Could organizations exploit these tendencies in, say, consumer marketing? I haven't thought much about the practical applications of the research, but it could be helpful in terms of product and service design and marketing. To appeal to people in crowded environments, I think you'd want to emphasize the future benefits they and their kids would accrue. In uncrowded markets, you might instead focus more heavily on instant gratification.

If firms want their employees to shift from a short- to a long-term focus, should they relocate from rural to urban areas? Or cram people into small offices with piped-in crowd noise? Those types of moves might have a slight effect on some people. But a few caveats: First, remember that our first two studies focused on country-to-country and state-to-state differences, not

WHICH U.S. STATE RESIDENTS FOCUS ON THE LONG TERM?

"Life-history scores"—which combine average marriage age, fertility, higher-education and preschool rates, and retirement plan participation—show that people in more-densely-populated states tend to follow a "slow" strategy (investing in the future), while people in less-densely-populated states tend to follow a "fast" one (focusing on the present).



NOTE POPULATION DENSITY IS BASED ON U.S. CENSUS DATA AND PLOTTED ON A LOGARITHMIC SCALE.

city versus noncity. We did see a correlation between density and urbanization, but our general findings held when we controlled for the latter. Second, in our experiments the effects were small by academic standards. Third, we were careful to present population growth in a neutral way. If people feel that density is creating a chaotic, unpredictable environment, they might adopt a faster, not slower, strategy. They might ask, "Is this an environment where you get ahead by building your skills and knowledge or where we compete by punching each other in the face?"

SUBJECTS WHO LISTENED TO AUDIO CLIPS OF CROWDS WERE MORE APT TO CHOOSE DELAYED REWARDS.

But many of us do think of crowded places as chaotic, stressful, and even dangerous. Someone once told me that's an American bias. There's a tendency to associate population density with cities and cities with crime, or people succumbing to their baser instincts. I grew up in Singapore, which is the world's third-most-densely-populated country (behind Macao and Monaco) but is extremely orderly. I'm not saying that crowded places aren't chaotic or dangerous. They can be. But this doesn't have to be the case.

Then you moved to the United States, which ranks 161st among 214 countries in population density. Are you trying to live a faster life? Well, I just got married last year at age 32, so I guess not. But I suspect environmental density may affect life-history strategy most when people are young. One thing we did test in two more experiments is whether college students would react differently to the idea of high population density than young adults under 40. We found that students who read the fake article on the growing U.S. population, rather than one on rising squirrel populations, showed a greater preference for long-term relationships but not for fewer children. People in their twenties and thirties showed a greater preference for fewer children but didn't change their relationship plans. So density seems to affect our thinking only with our top-of-mind future goals.

How many children do you plan to have? Maybe two. But not anytime soon. It's getting crowded these days.

Interview by **Alison Beard**
HBR Reprint F1704B

HOW I DID IT

SOULCYCLE'S CEO ON SUSTAINING GROWTH IN A FADDISH INDUSTRY

It's all about friendship and community.

by Melanie Whelan

PHOTOGRAPHY BY CARMEN CHAN

I have a rule: Whenever I hear about something from three people, I need to give it a try. In 2008 I heard about SoulCycle from a few friends. At the time, it was two years old and had just one studio, on the Upper West Side of Manhattan. I was immediately curious. I loved group fitness classes, and I was a consistent runner, but I didn't Spin. I had tried indoor cycling a few times and hadn't enjoyed it. My friends promised that this studio was different.

It was. First, the studio was tucked away at the end of a long hall. A subtle grapefruit scent emanated from the doorway. The class was packed, but somehow I felt both alone and bonded with the other riders. Every song on the playlist was a remix or a killer mashup of two songs I loved. The instructor was charismatic and authentic. Her energy, and the passion in the room, were contagious. The class was actually fun. Afterward, riders mingled in the lobby with flushed faces, lingering much longer than the tiny space would seem to encourage. It was clear that this was more than just a fitness studio—SoulCycle was a full sensory experience with an engaged community of superfans. One ride in, I understood why and how the buzz of this tiny uptown business could grow.

In 2012 I joined SoulCycle full-time to develop and lead the company's operations, and in 2015 I became CEO. In both those roles my goal has been to see how far we can grow the business and the brand. When I first joined the team, we believed that SoulCycle had the potential to operate 20 or 25 locations concentrated in U.S. coastal cities. Today we have 74 studios, and we've been steadily growing by about 15 locations a year in noncoastal cities such as Chicago, Dallas, Austin, and Houston. We just opened our first international studio, in Toronto. We now know we have a long runway for growth.

A SoulCycle class in New York City.

As we expand, we stay acutely aware of a potential pitfall: The performance of the fitness and wellness industries tends to be cyclical. That's true for workouts, and it's true for diets. This is a space where things may come and go, and trends may disappear entirely. You can probably think of examples: Jazzercise and Tae Bo and a continual stream of short-lived at-home fitness products—the kinds typically sold on infomercials. Some workouts just repeat the same thing again and again; fatigue, boredom, or distraction sets in, and people decide to try something new. Our challenge is to ensure that SoulCycle never falls into this trap.

We don't think of ourselves as a fitness company; we're a player in the broader experiential economy. I've found that our smartest decisions come from understanding and connecting with our customers. The best testing ground for growth is within the walls of our mirrored studios. We recruit and train our instructors quite differently from the way other fitness companies do, for one major reason: Their role is crucial to our riders' experience. Our instructors are inspirational coaches who leave riders more empowered on their bikes and in their lives. We count on them to make every class unique, to localize the experience, and to connect with different demographic groups. We count on them to inspire in hundreds of thousands of riders every month the same things I felt during my first ride, nearly a decade ago.

BUILD AN EXPERIENCE

My career in corporate development began at Starwood Hotels in 1999, and it was an exhilarating time. The company had just acquired the Sheraton and Westin brands and launched the W brand. I worked on brand strategy, corporate finance, and real estate acquisitions. It was incredible training for developing an experience-first approach. We rethought the function and feel of a hotel's public spaces. We piped in handpicked playlists, tweaked the lighting, and created just the right energy and vibe to attract and appeal to the local community as much as the guests upstairs. From Starwood, I went to the Virgin Group, where I spent four years working on the launch of Virgin America. We scrutinized our onboard experience. We explored ways to surprise

CAROLYN COLE/GETTY IMAGES; GEORGE TIEDEMANN/GETTY IMAGES

and delight travelers and to offset rudimentary in-flight frustrations. In 2007 I joined Equinox as the vice president of business development to help expand the country's most comprehensive fitness brand: personal training, a spa, a boutique, and group exercise under one roof.

In 2010 the CEO of Equinox met with SoulCycle's founders, Julie Rice and Elizabeth Cutler. With just five studios at the time, they needed a partner to keep growing. In Equinox they found expertise in real estate acquisition and operations. By 2016 Equinox held a 97% stake in the company. Through the process, I spent a lot of time with Julie and Elizabeth, focusing on maximizing the brand's potential while maintaining its unique culture. In 2012, nine months after Equinox's first investment, I joined SoulCycle full-time.

My experience in the hotel industry couldn't have better prepared me. From the beginning, Julie and Elizabeth viewed SoulCycle as a hospitality company, with the workout just one dimension of the brand. Our most passionate riders talk more about relationship building and connecting with instructors and other riders than they do about the exercise itself. Leaving a dark studio, sweaty and wearing Spandex, and walking into a bright and crowded lobby breaks down barriers and makes it easier to have real conversations. For many people, friendships made at SoulCycle are the beginning of bigger changes in their lives. They start eating better. They prioritize sleep. Very organically, they plug into a more positive lifestyle. Aspiration becomes reality.

Our studios also differ from traditional fitness classes in the way people value the experience. At a gym you can take unlimited Spinning classes as part of a basic membership. At SoulCycle we don't charge monthly fees, but each class costs $30 to $35, and we ask our riders to book bikes in advance. We believe the pay-per-class model inspires a different level of energy and commitment that contributes to the overall experience.

OUR GREATEST ASSET

"Calories burned" is just a piece of what we deliver to our riders. Measurability matters, but we've heard repeatedly that our team is what keeps riders coming back. We use behavioral interviewing and on-the-job shadowing to ensure that our teams are motivated to make the time a rider spends at one of our studios the best part of the day. It's simple but intuitive: Inspired people want to encourage inspiration in others.

Our instructors are our greatest asset. They take riders on a 45-minute physical, emotional, and musical journey that's similar to theater. You could take a class with the same instructor multiple times in a week, and each experience would be different. Autopilot isn't an option. Lighting, playlists, words of encouragement—everything is customized in real time to the group of riders in the room. The one constant is the incredible physical challenge.

GREAT MOMENTS IN GROUP EXERCISE

Some group exercises become popular and stay popular. Others run out of steam. A sampling:

1980s: JAZZERCISE

Created in 1969 by Judi Sheppard Missett, a Northwestern University undergrad who taught jazz dance on the side, Jazzercise reached peak popularity in the 1980s. Today it has 8,300 franchises, utilizes pop music, and incorporates moves from kickboxing.

To recruit superstar instructors, we prioritize great personality and individual expression—our training program will fill in any Spinning-specific gaps. To retain those stars, our model values career trajectory. We pay above-market wages, and 78% of our instructors work at SoulCycle full-time, with health insurance, paid vacations, and continuing education, which is very unusual in this industry. (They also have free access to on-staff physical therapists.) Our retention rate over the past few years has exceeded 95%. We get about 20 applications for each opening in our training program. Instructors go through a rigorous 12-week training at our New York headquarters, where they learn everything from the elements of the workout to musicality to anatomy and biomechanics. Once they're on the podium, we invest considerably in further training and development. Because we're a growth company, they see how they can build careers with us by relocating to new markets, growing into regional development roles, or through promotion.

WHAT MAKES US UNIQUE

Soon after I became CEO, we set our sights on going public. But the stock market had other plans. As the financial climate changed, we opted to stay private, partly because the company's solid financial footing didn't require us to rush into the public market. As we prepared for a potential road show, I was peppered with questions about the appeal and sustainability of our brand. One I heard frequently was: "Why are people so obsessed with SoulCycle—and how do you know they'll stay obsessed?" It was a great opportunity for me as a new CEO to consider their concerns and figure out how to address them.

1990s: TAE BO

Tae Bo originated when the U.S. fitness guru Billy Blanks created a workout in his basement while playing the *Rocky* soundtrack. By 1992 he'd launched an exercise video that became one of the decade's most popular infomercials and has sold millions of copies. Blanks is still producing Tae Bo videos, but he's been eclipsed by Beachbody, a company best known for the P90X workout.

BOB CAREY/GETTY IMAGES

When SoulCycle launched, the boutique fitness industry wasn't well established. Arguably, we created the space. Now competitors are opening Spin, boot camp, and other hybrid-format studios in a fragmented market. We don't pay a lot of attention to other companies in the indoor-cycling or general fitness space, but competition does challenge us to innovate and reconnect with the needs of core customers—our strongest brand ambassadors.

Some of the best lessons come from outside our industry. We consider how Disney trains its staff and how Starbucks keeps its stores community oriented. We watch how Airbnb adds digital products while remaining intuitive. SoulCycle enthusiasts will tell you that it's not just one or two things that make us unique—it's the combination of many. It's the welcoming attitude of the staff, the charisma of our instructors on the podium, our clothing collection, and even our website. It's difficult for imitators to copy any of that, let alone all of it.

We do keep a lookout for blatant copycats that infringe on our intellectual property. If we believe that a studio is truly trying to make customers think they're at a SoulCycle, we pursue a resolution. We found one studio outside North America that looked exactly like our Manhattan studios, with our logo and the same mantra on the wall. We pursued the owners aggressively but appropriately, and the studio made changes.

It's never been part of our strategy, but we've attracted an influential clientele, especially in New York and Los Angeles. Some people think that relying on celebrities to create buzz is its own form of faddishness. There's no question that celebrities have brought us attention, but we don't do anything special to bring them in. From what we hear, high-profile customers appreciate that they can ride in a community setting and that our instructors will never draw attention to them. Michelle Obama rode with us in 2014, when we opened a new studio in Washington, DC. I knew she was there, but we didn't change anything. She seemed to enjoy being one of 60 people, riding a bike to an amazing playlist, sweating a lot, and pushing herself…just like the rest of us. Soon she was coming in a couple of times a week.

LOCATION, LOCATION

Choosing the right location for a new studio is a science, and we begin our research a year before we hope to break ground. There's no substitute for spending time locally and hearing from our future riders what matters to them. What do they do with their free time? Where do they exercise and when? What gets them out of bed early? By understanding their lifestyles, we can build a studio around them—not the other way around. And, of course, we consider which of our instructors can best help build community in a new market.

When we look at real estate, we're pretty adaptable. Our studios are 2,500 to 3,500 square feet—a fairly small footprint, so we can go into spaces that wouldn't work for traditional retailers. We care about parking, but we don't need to be on main streets, because we've become a destination. Over time we've also become a desirable brand for landlords, because we bring in traffic and an energy that can complement some of their other tenants. As a result of our disciplined process and approach, we've gotten all our location decisions right so far: Never in the company's history have we closed a studio.

EXTENDING OUR BRAND

When it comes to innovation, we do some things you might expect. We're always looking to improve the design of our studios, which some people have compared to Apple stores. For instance, we put iPhone chargers inside the lockers, because the charging stations we used to offer at the front desk were getting crowded. This year we plan to introduce our next-generation bikes, which use magnetic resistance and a carbon belt drivetrain. They're superior to our current bikes, which use friction-style resistance: They ride more smoothly, and they last longer. We redesigned the handlebars to accommodate our choreography and to provide greater stability for the upper-body workouts we do on the bikes. And our workout continues to evolve as our riders become stronger. Today our instructors utilize more interval training in their classes, and our hand weights are heavier than they were a few years ago.

We're also expanding our apparel and other categories. After Julie and Elizabeth launched the first SoulCycle studio, they had $2,000 left, so they had T-shirts printed. The first batch sold out in 24 hours. Last year we introduced 14 apparel collections, each a combination of performance and lifestyle pieces—the kind of clothing you can wear outside the studio too. In our most firmly established studios, revenue growth from merchandise exceeded revenue growth from riding in 2016. People wear our logo as a badge of honor, telling the world that they belong to this community.

We've also continued to widen our demographic. When SoulCycle first opened, our riders were almost entirely women from Manhattan's Upper West Side. By 2015, when we were considering an IPO, nearly 80% of our revenue came from locations in New York, Los Angeles, and San Francisco. Today less than 50% comes from those cities, and our clientele varies according to location and time of day. A typical "rooster" class—what we call our 6 AM ride—may be at least 50% men. Some studios offer a teen class at 4 PM. We encourage our instructors to create the right vibe to make every group feel welcome.

WE'RE NOT A FAD

I'm confident that we'll keep growing, because people are looking for places to connect with one another and disconnect from technology. They want experiences more than they want stuff. The reason so many wellness categories are growing is that people recognize the importance of investing in their bodies and their minds. That's why we believe that SoulCycle isn't as sensitive to the economy as some other premium brands are. Transitions have proved to be times when our brand is acutely relevant to our customers. Although we were much smaller during the Great Recession, we found that our riders needed us then as a sanctuary and an escape. Similarly, our business increased in the weeks after the 2016 presidential election, which was an uncertain and emotional time for many people. If the economy slows, people may spend less on travel or restaurants, but they'll keep investing in themselves—and we believe they'll keep coming to SoulCycle.

Simply put, we're not a fad. Indoor cycling has been around for more than 30 years because it's a safe and efficient way to get a cardio workout. It's easier on the joints than many other forms of exercise, so riders can stay with us for years. Our founders took this old form of exercise and reinvented it as a full-body workout with emotional and mental benefits that go far beyond fitness. A neon sign that hangs in one of our New York City locations captures who we are: "Pack. Tribe. Crew. Community. Soul." That's how we describe one another, and our riders apply those words to themselves. A first-timer could see that message, glowing from the studio's back wall, and feel a sense of invitation.

Friendships and communities are enduring. Because SoulCycle has those elements at its core, our brand will endure too.

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2000s: ZUMBA

The fitness instructor Alberto Pérez was teaching aerobics in Cali, Colombia, one day in the mid-1990s when he forgot his usual workout tapes. He grabbed salsa and merengue music and improvised, and the Latin-infused dance movement was born. In 1999 he took it to Miami; by 2002 he'd trademarked the name Zumba and was selling DVDs on infomercials. Zumba classes would eventually be taught in 200,000 locations worldwide.

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Harvard Business Review Spotlight

JULY–AUGUST 2017

THE TROUBLE WITH CMOs

WHY CMOs NEVER LAST
And what to do about it

THE POWER PARTNERSHIP:
CMO & CIO

REFLECTIONS OF A SIX-TIME CMO
A conversation with Joe Tripodi

REDUCING CMO TURNOVER
A recruiter's prescription

THE EVOLUTION OF THE CMO
As marketing channels and tools grew over the decades, so did the status and responsibilities of top marketing executives.

ILLUSTRATION BY PETER CROWTHER

"Eighty percent of CEOs don't trust or are unimpressed with their CMOs."

From "Why CMOs Never Last," page 46

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SEE PAGE 41 FOR INSTRUCTIONS.

WHY CMOs NEVER LAST

AND WHAT TO DO ABOUT IT

BY KIMBERLY A. WHITLER AND NEIL MORGAN

In 2012 a leading retailer began looking for a new chief marketing officer. The job description made the opening sound exciting: The new CMO would play a big, important role, leading the company's efforts to boost revenues and profits. It seemed like the kind of opportunity any would-be CMO might desire.

Sure enough, the company landed a seasoned, talented executive from the consumer-packaged-goods industry, who came on board determined to make his mark.

But a year later the new CMO was feeling deeply frustrated. Given the job description, his experience, and his conversations with the recruiter and the chain's CEO, he'd assumed he'd have the authority to create a strategy for driving growth. To his surprise, his role was limited mostly to marketing communications, including advertising and social media. He had no responsibility for (and limited influence over) product launches, pricing, and store openings. The problem, he told us, wasn't that his skills prevented him from meeting the company's goals; it was that the job was so poorly designed—and there was such a mismatch between the CMO's authority and the CEO's expectations—that it would be difficult for anyone to succeed in it. Soon after he spoke with us, the CMO left the company.

In our research into what makes CMOs effective, we've heard stories like this more often than we should. To us, they're evidence that something is going very wrong in the relationship between CEOs and CMOs. A 2012 global survey by the Fournaise Marketing Group highlights the tensions between them: The results reveal that 80% of CEOs don't trust or are unimpressed with their CMOs. (In comparison, just 10% of the same CEOs feel that way about their CFOs and CIOs.) CMOs also sense a serious problem. In our own surveys, 74% of them say they believe their jobs don't allow them to maximize their impact on the business.

This troubled relationship helps explain why CMOs have the highest turnover in the C-suite. According to an analysis by Korn Ferry, they stay in office 4.1 years on average, while CEOs average 8 years; CFOs, 5.1 years; CHROs, 5 years; and CIOs, 4.3 years. Our own research indicates that churn rates may be even worse: We found that 57% of CMOs have been in their position three years or less. (See the exhibit "Years on the Job.")

But unlike CFOs, CHROs, and CIOs, whose roles are primarily inward facing, CMOs have a direct effect on the way customers engage with the firm. When new CMOs enter companies, they often change the strategic direction—which means creating new positioning, product packaging, and ad campaigns, usually at considerable expense. If job dissatisfaction or underperformance leads to a revolving door in the CMO's office, companies can experience internal disruptions, not to mention major recruiting and severance costs.

We believe that a great deal of CMO turnover stems from poor job design. Any company can make a bad hire, but when responsibilities, expectations, and performance measures are not aligned and realistic, it sets a CMO up to fail. In this article we'll outline the four steps CEOs should take to end this dysfunctional pattern. We'll also describe how to match the right person to the CMO job and how CEOs, executive recruiters, and CMO candidates

IN BRIEF

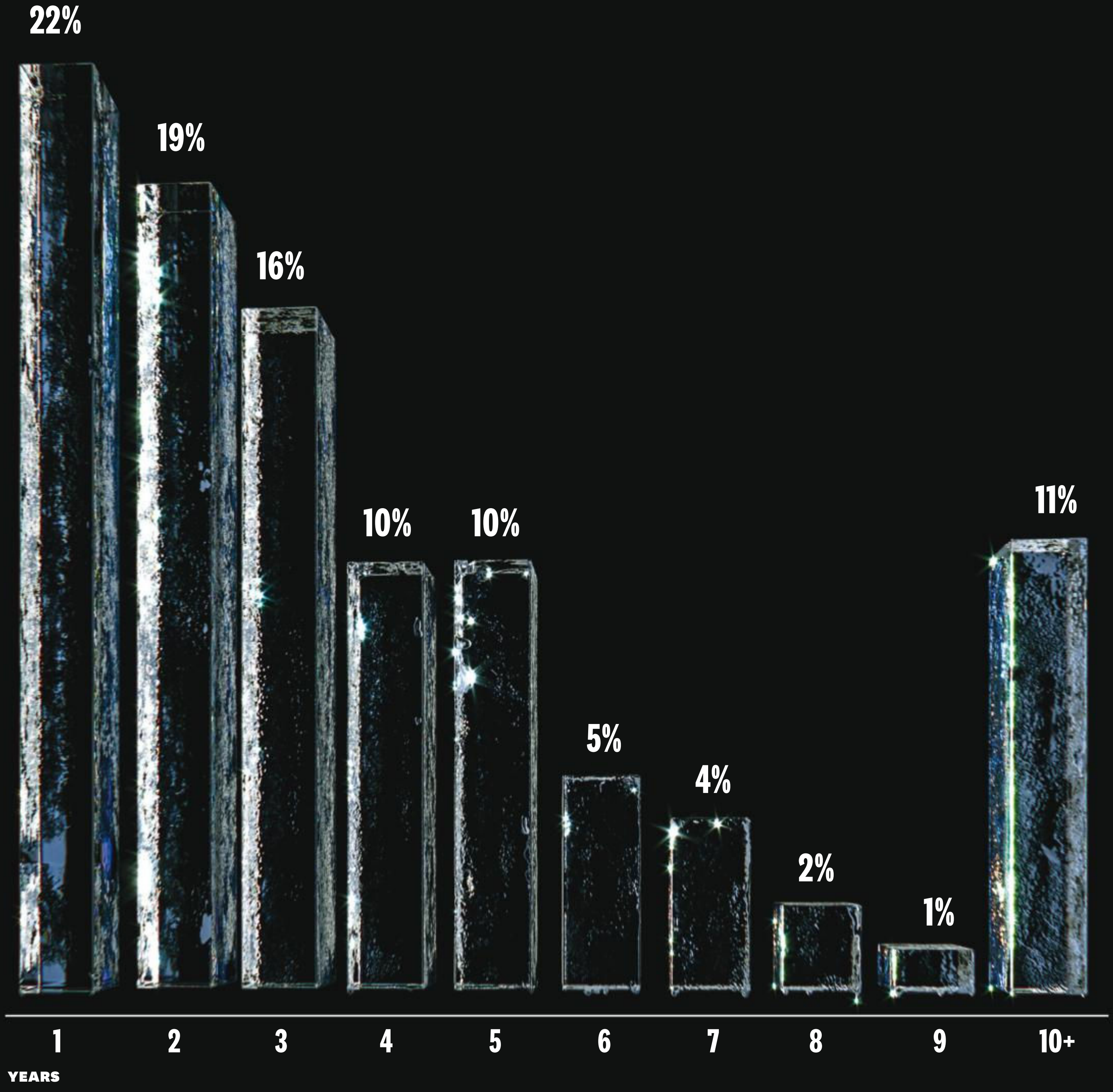
THE PROBLEM
Four-fifths of CEOs are dissatisfied with their firms' chief marketing officers. Not surprisingly, CMOs have the highest turnover in the C-suite.

WHY IT HAPPENS
Most CMO jobs are poorly designed. The expectations set for the role don't align with the responsibilities given or the metrics for success.

THE SOLUTION
CEOs must decide which type of CMO they need: a strategist, who makes decisions about the firm's positioning and products; a commercializer, who drives sales through marketing communications; or an enterprise-wide leader with P&L responsibility, who does both. Recruiters should guide them through this choice and help design the job appropriately, and CMO candidates must ensure they understand the role before signing on.

YEARS ON THE JOB

Most chief marketing officers have not been in their positions long. More than 40% have been in their roles two years or less, and 57% have been in them three years or less.



SOURCE "CMO IMPACT STUDY," 2014 AND 2015, BY KIMBERLY A. WHITLER can all work together to maximize the odds of CMO success.

STEP 1

DEFINE THE ROLE

Let's start with a simple question: What does a CMO actually do? Surprisingly, there is no clear, widely accepted answer.

In our research we've interviewed more than 300 executive recruiters, CEOs, and CMOs; conducted multiple CMO surveys; performed an analysis of 170 CMO job descriptions at large firms; and reviewed over 500 LinkedIn profiles of CMOs. We've discovered extreme variations in the responsibilities CMOs are given and in the skills, training, and experience of the people who occupy the role. (Note that we use the term "CMO" generically to refer to a company's top marketing executive; at some firms the job may have a different title, such as executive vice president of marketing.)

Most CMOs, we've observed, have a few areas of core responsibility. More than 90% are responsible for marketing strategy and implementation, and more than 80% control brand strategy and customer metrics. But beyond that, the range of duties—from pricing to sales management, public relations to e-commerce, product development to distribution—is mind-boggling.

Of course, not all CMO positions should be the same. Companies have different needs, challenges, and goals, and the CMO's role has to reflect those realities. Before even considering candidates for the job, a CEO must decide which kind of CMO would be best for the company. In our research we've identified three distinct types. (See the exhibit "Three Types of CMO Roles.")

Some CMOs focus on *strategy*. They take the lead on up-front decisions about the firm's positioning and then translate those decisions into the design of new products, services, and experiences. Often they manage the customer insight and analytics functions. In essence, strategy-focused CMOs spearhead a company's innovation efforts. Accounting for 31% of CMOs in our research, they're common in multibrand firms and in some B2B service firms where a centralized marketing group helps set firm-level strategy.

Most CMOs focus on *commercialization*. They have a downstream role and work primarily on using marketing communications to sell the products, services, and experiences that others design. Typically, their responsibilities include overseeing traditional and digital efforts to create revenue-growing relationships with consumers. Nearly half of CMOs (46%) have this kind of role. Common in firms where a function other than marketing is central to success, commercializers play a supporting role to the function that drives innovation (such as engineers in tech firms).

WHEN CONSUMER INSIGHTS DRIVE PRODUCT DESIGN, THE CMO NEEDS A STRATEGIC FOCUS.

The third kind of CMO handles both strategy and commercialization responsibilities in an *enterprise-wide* role focused on the design and implementation of strategy. Significantly, such CMOs have P&L responsibility and the broadest range of duties, including innovation, sales, distribution, and pricing. In our research 23% of CMOs have an enterprise-wide role. They tend to be common in single-brand firms and some consumer-packaged-goods companies. Because of the scope of their responsibilities and the organization-wide nature of their impact, marketers with this kind of experience have historically been seen as strong general managers and are often tapped for CEO roles at other firms.

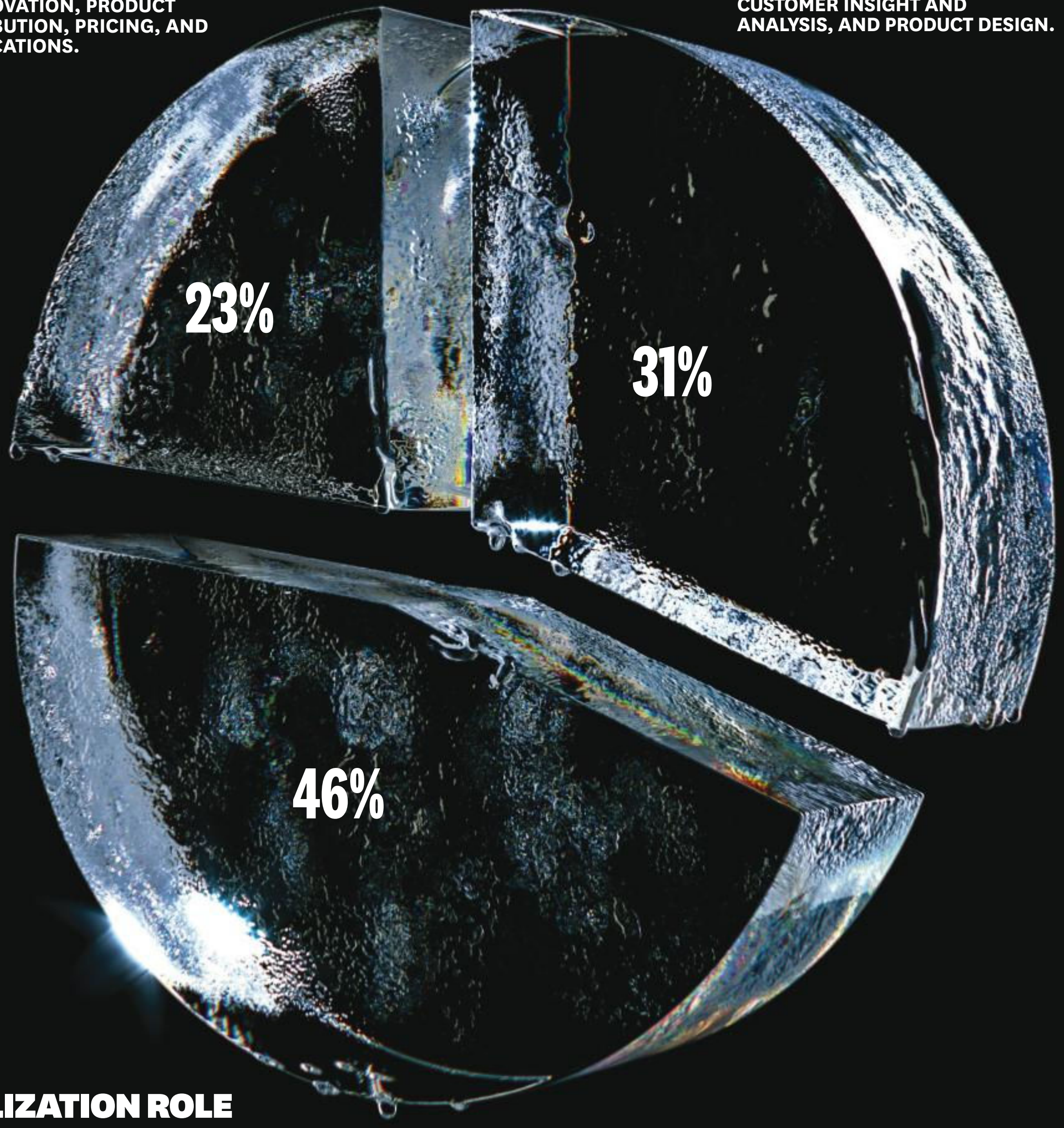
How can CEOs determine which type of CMO is appropriate for their firms? They should take into account the following three external factors:

1. The degree to which consumer insight needs to drive firm strategy. When generating consumer insight is a critical competency of the firm and determines the design of products, services, and experiences, the CMO role should skew toward a strategic or enterprise-wide focus. There's so much variation within industries that it's difficult to say definitively which kinds of companies fall into this category. But marketing's role should lean toward commercialization if finance, technology, manufacturing, or another inward-facing function leads a firm's strategy. This is often the situation in heavy manufacturing, industrials, technology, higher education, health care, and B2B firms. In general, when firms believe that their innovations create the need, they are less likely to look to CMOs to set strategy or boost profits.

2. How difficult it is to achieve firm-level growth. Companies in slow-growing or highly competitive industries are more likely to require a strategy-focused or enterprise-wide type of CMO, who can devise plans for building demand. However, if growth is easier to come by and less of a

THREE TYPES OF CMO ROLES

CMO jobs are not all alike. Some focus on strategy, some on commercialization, and some on both. CEOs need to understand which kind of executive their firm needs and make hires accordingly.



ENTERPRISE-WIDE P&L ROLE

DELIVERS PROFITABLE GROWTH BY DESIGNING STRATEGY AND OVERSEEING COMMERCIALIZATION. RESPONSIBLE FOR INNOVATION, PRODUCT DESIGN, SALES, DISTRIBUTION, PRICING, AND MARKETING COMMUNICATIONS.

STRATEGY ROLE

DESIGNS GROWTH STRATEGY. RESPONSIBLE FOR INNOVATION, CUSTOMER INSIGHT AND ANALYSIS, AND PRODUCT DESIGN.

COMMERCIALIZATION ROLE

SPURS SALES THROUGH MARKETING COMMUNICATIONS. RESPONSIBLE FOR ADVERTISING, DIGITAL CONTENT, SOCIAL MEDIA, PROMOTIONS, AND EVENTS.

challenge for the firm, then the commercialization role may be a better fit.

3. The level of dynamic change in the marketplace. When a company's business model is shifting or industry boundaries are being redrawn, CMOs with strategic or enterprise-wide responsibilities are likely to be more effective. With their broader knowledge of the environment (consumers, competitors, channel partners, the marketplace) and of their firms' internal workings (core competencies, strategic direction), they can better help their management teams steer through uncertainty and rethink ways to generate demand.

It's also imperative for the CEO to consider this set of internal factors:

1. The historical role of the CMO within the firm. If the company's top marketing executive has traditionally focused on commercialization, shifting to a strategic or enterprise-wide role will require taking responsibilities away from another function. This becomes problematic if the other function has been managing those areas for a long time and doing it well. While it's often easier to narrow the CMO's scope, there are many times when broadening it makes sense. For instance, one CMO in higher education had a commercialization role but was elevated to a strategy role after he identified a solution to his school's admissions (and thus its growth) challenges. Expanding the CMO's responsibilities requires significant CEO involvement to communicate expectations and prevent internal backlash, however.

2. The structure of the firm. If a firm has multiple business units or brands, functional leadership responsibility tends to be dispersed throughout the organization. (Each unit or brand may have its own finance, marketing, and IT leaders.) When this happens, the CMO often helps provide strategic leadership across the corporation. We frequently see this in global, multibrand firms where category or business unit managers have P&L responsibility. However, as the company gets larger and more complex, C-level roles often have to be disaggregated. This is no different for the CMO's role, which may get divided into several parts, such as chief commercialization officer, chief innovation officer, chief analytics officer, and so on. In contrast, when a firm has a single brand or all of marketing is centralized, it's easier for the CMO to play an enterprise-wide role.

THE RISKIEST JOB IN THE C-SUITE

The tenure of CMOs and other top executives

AVERAGE YEARS BY INDUSTRY	CEO	CFO	CIO	CMO	CHRO	C-SUITE
CONSUMER	8.0	5.1	4.5	3.6	4.9	5.2
ENERGY	6.1	5.0	4.5	4.6	5.3	5.1
FINANCIAL SERVICES	9.7	5.5	4.1	5.1	5.1	5.9
INDUSTRIALS	6.7	4.9	4.0	4.1	4.6	4.9
LIFE SCIENCES	9.4	6.0	4.1	3.1	5.1	5.5
PROFESSIONAL SERVICES	9.2	5.0	4.5	4.1	5.1	5.6
TECHNOLOGY	7.9	4.9	4.4	4.3	5.2	5.3
OVERALL AVERAGE	**8.0**	**5.1**	**4.3**	**4.1**	**5.0**	**5.3**

SOURCE KORN FERRY

STEP 2

MATCH RESPONSIBILITIES TO THE JOB'S SCOPE

Once the CEO decides where a CMO ought to have an impact, the role's responsibilities should be aligned accordingly. Almost all CMOs are in charge of brand strategy and insight generation. CMOs with a strategic focus also need to oversee the firm's "think tank" efforts (which originate innovations and product designs) but have little to no responsibility for converting strategy into tactics such as ads or marketing communications. CMOs in a commercialization role should have extensive responsibility for developing and converting the brand strategy into marketing plans that drive sales (through social, digital, advertising, and content initiatives; events; partnerships; and so on) but little responsibility for up-front, firm-level strategic decisions. And CMOs in an enterprise-wide P&L role should have responsibility for the whole process.

Alignment of responsibilities is the critical area where mistakes are made. It's common for companies to describe a role in which the CMO is expected to change the overall performance of the firm, but when you examine the job duties closely, it's clear the CMO has only commercialization functions. In other words, expectations typically far exceed the actual authority given the CMO.

That problem is often compounded when CEOs are wooing candidates who already have good jobs. While overpromising and "up-selling" are common in recruitment across many functions, our research suggests that they can be a bigger issue in marketing—because of the general confusion and lack of uniform expectations about what a CMO does and the knowledge and skill differences among marketing executives.

STEP 3

ALIGN METRICS WITH EXPECTATIONS

Once the job's role and responsibilities have been nailed down, the CEO needs to define how the CMO's success will be measured.

A CMO in a well-designed commercialization role will be held accountable for meeting budgetary goals; for the outcomes of projects (such as a website redesign); for the results produced by marketing programs (for example, increased traffic to stores); and for management outcomes (like improved staff satisfaction and performance). In contrast, CMOs in strategy roles should be held accountable for related elements of firm performance, such as increases in revenue or same-store sales, in addition to meeting budgets and producing management outcomes. And of course, CMOs overseeing P&Ls should be measured on the top- and bottom-line business results (and on budgetary, project, and management outcomes).

This approach may sound like common sense, but it's surprising how infrequently it's followed. Only 22% of the job descriptions we studied mentioned how the CMO would be measured or held accountable, and only 2% had a specific section that clearly articulated job expectations. While 90% made some mention of expectations, they typically were vague. The head of marketing for one technology company, for example, was supposed to "help define and execute an aggressive growth strategy for the company." What exactly is the measure of success for that? Is it producing a strategic plan? Or some sort of growth target (and if so, how is it measured)? If metrics and goals aren't predetermined, how do CMOs know if they have hit their targets?

STEP 4

FIND CANDIDATES WITH THE RIGHT FIT

Even when the CMO role is well defined, assessing candidates can be a challenge, because their training and experience vary so much. Marketers lack the professional certifications required of lawyers and accountants. Only 6% of CMOs we looked at in our research had degrees in marketing. Although 44% had MBAs, their educational backgrounds varied a lot. They included degrees in engineering, economics, mathematics, philosophy, political science, psychology, and other subjects. Consequently, the type of experience and training marketing executives gain during the formative part of their careers—and specifically, whether they have served primarily under CMOs in strategy, commercialization, or enterprise-wide P&L roles—will largely determine which roles they are best suited to later in their careers.

Another stumbling point, in our analysis, is that in almost all CMO job descriptions there are significant gaps between the responsibility given and the experience required. For instance, 39 of the job descriptions we studied indicated that the CMO would oversee product strategy but then neglected to require experience in that area. Sometimes the gaps ran in the other direction. Thirty-four of the descriptions required candidates to have direct-marketing experience even though the jobs didn't include any direct-marketing duties.

TYPICALLY, CMOs AREN'T GIVEN ENOUGH AUTHORITY TO DO WHAT'S EXPECTED OF THEM.

To understand how confusing this mismatch can be, consider the description for the CMO job at a top manufacturer. This firm wanted its head of marketing to lead the analysis of what drove customer preferences, develop a superior brand strategy, set the marketing strategy, and oversee implementation of those strategies. However, the actual position included responsibility only for a marketing insights group, a marketing project-management group, and a media group. The description led the reader to believe the CMO's role was far bigger than it actually was.

The problem didn't stop there. The description stated that candidates should have "best-in-class consumer-packaged-goods industry experience" (translation: P&L experience), demonstrated corporate/marketing strategy leadership, sales experience, and more. But the job involved neither P&L nor sales responsibilities, so these requirements made little sense. A better match for the job would have been someone with research and analysis skills, media and digital experience, and a proven ability to develop marketing programs that deliver in-market results. While the lack of internal consistency may seem obvious, few of the CEOs and CMOs we've interviewed recognize that a disconnect exists.

HOW TO IMPROVE OUTCOMES

Although CEOs express disappointment in their CMOs, they typically don't realize that they may have played a role in creating the problem. By making sure that the CMO job is designed and staffed correctly, they can increase their own satisfaction with their top marketing executive.

Before looking for a new CMO, a CEO should be sure to answer the following questions:

- What outcomes do we want the CMO to produce, particularly in light of the company's priorities? Which of the three CMO types do we need? How should this person balance out the management team's strengths (and weaknesses)?

- What functional responsibility is necessary to realize our vision for the role? Will that level of responsibility really work, given other top management team roles?

- What will success look like? What specific key milestones will the CMO be expected to reach?

- What types of skills and experience are required?

When considering this last question, too many CEOs describe someone who is the “best athlete” rather than the best player for the specific position. It’s important to avoid that temptation. For their part, CMO candidates shouldn’t view the job description as a fait accompli. In our surveys CMOs who say their roles are correctly designed often had a hand in crafting them before accepting their jobs. That indicates how critical it is for CMOs to negotiate the specifics of their responsibilities and expectations.

Before signing on to any CMO position, a candidate should make sure he or she understands the following:

- What is really the CMO’s role in the firm? Is there agreement about this across the C-suite? Do the CEO, CFO, CHRO, and the board all describe the position in the same terms?

- What is really the CMO’s responsibility? Which functions report to the CMO on the org chart, and which don’t? What departmental budget items are the CMO’s responsibility? Are any budgetary areas missing? (Though some firms may balk at sharing budgets with candidates during the hiring process, asking to see them is valid and can serve as a test of whether the firm wants to be transparent about the position’s responsibilities.)

- Are the expectations and performance metrics for the role consistent with the responsibilities and the candidate’s experience? Is the CMO being set up to succeed?

After answering these questions, the candidate should summarize in writing his or her understanding of the role and the expectations and responsibilities involved with it, and share it with both the executive recruiter and the CEO, asking for confirmation that they are all on the same page.

Executive recruiters can use the following questions to guide the process:

- Does the CEO understand the range of CMO roles? Does he or she understand that the position should be designed before a job description is written? Has he or she anticipated how altering the CMO role might affect other C-suite leaders?

- Are expectations, responsibilities, and measures of success consistent with the chosen CMO role? Is that consistency clear in the written job description? Are the skills it outlines in keeping with those expectations and responsibilities, too?

- What type of CMO expertise is the best match for the role the firm has in mind?

- Have prospective CMOs been educated on the different types of roles and the degree to which their own background and skills fit the role in question? (Being open and honest about gaps in preparation for specific positions can help prospective CMOs anticipate challenges and identify experience they should gain.)

As experts in designing CMO roles, executive recruiters must lead, rather than follow, the CEO in talks about the role. But in our interviews with recruiters who focus on CMO placements, we came across only one who had a model for guiding CEOs through a discussion of how to design the right role for the firm. While everyone has a vested interest in helping new CMOs succeed, recruiters have an additional incentive to get it right, since their compensation is traditionally at risk if a candidate they place fails within the first year on the job.

LEARNING THE HARD WAY

Together, the authors of this article have spent eight years exploring why CMO hiring so often goes off track. But one of us—Kim—has personal experience with the challenges that result when the design of a CMO role hasn’t been completely thought through.

Kim began her marketing career at Procter & Gamble, where marketers typically have P&L responsibility. As a result, she assumed that all C-level marketing jobs had it. Some years after leaving P&G, she interviewed for an exciting CMO position that the recruiter insisted would be “transformational.” But in the first week at the new company, Kim realized to her surprise that she didn’t have P&L authority. Instead of sitting in strategy-setting meetings, she was trying to figure out if advertising conformed to brand guidelines. This was not what she thought she’d signed up for.

Looking back, Kim made some mistakes that might now seem obvious. She focused on the job description and relied on the recruiter’s assurances instead of asking the right questions during interviews. Had she asked to see org charts and budgets before accepting the company’s offer, she would have quickly realized that the CMO’s responsibility was much narrower than she thought. That would have enabled her to have a pointed discussion with both the executive recruiter and the CEO regarding the importance of role design.

To fix the situation, she worked to change the scope of and expectations for her job. After a couple of in-market wins, she partnered with the COO (who had P&L authority) to design a different role for marketing. She had a terrific CEO who believed that marketing should expand its duties and supported the change. Because the economy was in turmoil, the COO was more than happy to share accountability for financial performance. Over time the key players began expecting marketing to assume more P&L responsibilities, essentially changing the nature of the CMO role.

As Kim’s story shows, it is possible to proactively change the scope of a CMO job after being hired. However, hiring mismatches aren’t good for firms or their executives, and fixing them takes a lot of time and effort. Companies would be better off if CMOs spent their energy doing the jobs they were qualified for from the outset.

Our hope is that our research will help CEOs and CMOs avoid this problem in the future. Everyone—C-suite executives, subordinates, and shareholders—will benefit if a company creates the right CMO role from the beginning and then finds the right kind of person to fill it.

HBR Reprint R1704B

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THE POWER PARTNERSHIP: CMO & CIO

BY KIMBERLY A. WHITLER, D. ERIC BOYD, AND NEIL MORGAN

Historically, chief marketing officers and chief information officers have tended to see the world quite differently. Focused on generating demand, marketers place a high priority on speed and creativity and take risks to achieve aggressive goals. IT executives are often risk-averse, prizing stability, security, and accuracy. As marketing moves increasingly onto websites and mobile devices and into social media and e-mail, the two functions have come into conflict, in part because of shifts in power and resources. Here's one stark demonstration: This year, for the first time, CMOs will control more technology spending than IT departments do, according to a forecast by Gartner. "There's been a bleeding of responsibilities as CIOs get more involved in customer-facing activities and CMOs get more involved in technology," says Anne Park Hopkins, a former recruiter at Korn Ferry who has placed executives in both roles. "The question is how to create better co-ownership to deal with growing ambiguity."

In our research, which includes in-depth interviews with successful CMO-CIO pairs, we've identified a useful technique for encouraging co-ownership: creating alignment through shared performance goals. This is not a common practice. In our surveys two-thirds of CMOs say their performance is measured against company-wide financial results such as operating earnings or sales growth. We call those *vertical alignment measures,* since they match C-level executives' performance targets with the CEO's. In contrast, only 34% of CMOs (including most of those who are adept at collaborating with CIOs) are judged on metrics closely tied to the responsibilities they share with other C-suite colleagues, or using what we call *horizontal alignment measures.*

Regal Entertainment Group provides a good example of how horizontal alignment measures can spark collaboration. Digital marketing has become a strategic priority in the theater industry, so when CEO Amy Miles decided to replace Regal's CMO in 2012, she knew the next marketing chief would need to work closely with CIO David Doyle. She tied both executives' bonuses to shared goals they could hit only by collaborating. The metrics included the percentage of tickets sold on Regal's app or website, the percentage of customers visiting Regal's self-serve kiosks, the speed of ticket lines in theaters, and metrics related to customers' website experience (such as load times) and the relaunch of the Regal Crown Club loyalty program.

To fill the CMO role, Miles hired Ken Thewes, who'd studied engineering as an undergrad (and so had technical fluency). Miles had made it clear during the job interview process that effectively partnering with the CIO was a top priority. "Earlier in my career as a CMO, there wasn't much of a relationship at all" with the IT department, Thewes says. But when he arrived at Regal, the IT and marketing teams began holding twice-weekly joint department "scrums," coordinating their efforts to achieve their common goals. Says Thewes: "These relationships don't work just because you say you want them to—you have to really get folks engaged and make sure they collaborate."

The partnership has paid off: In the past five years, membership in Regal's loyalty program has more than doubled, hitting 14 million people. Digital commerce is up by 359% since 2013, and customer engagement has hit record levels. Improvements in all those areas have helped lift corporate results: Since 2011 Regal's revenue has increased by 20% and its shareholder value by 170%.

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PHOTOGRAPHY BY WEBB CHAPPELL

REFLECTIONS OF A SIX-TIME CMO

A CONVERSATION WITH JOE TRIPODI

BY DANIEL MCGINN

Joe Tripodi was appointed to the top marketing job at Mastercard in 1989 and since then has served as the CMO of Seagram's, the Bank of New York, Allstate, Coca-Cola, and Subway. He spoke with HBR about the evolution and particular challenges of the job.

HBR: How has the chief marketing officer's role changed since you first held it?
TRIPODI: Originally, CMOs focused mostly on advertising and communications. Today the role requires a view of how to grow a brand and an enterprise—and how to partner with other parts of the business to drive that growth. There's a huge focus on data and analytics and how to use them to segment and target consumers. Smart data is the future. Analytics allows for precision marketing, as opposed to a "spray and pray" approach. And now more than ever, the focus is on customers and the customer journey. More CMOs are becoming responsible for the customer experience. It's great to create marketing plans in an ivory tower, but unless you can have an impact in the actual place where customers are—in restaurants or stores—you won't succeed.

As CMO responsibilities have shifted, how has the way you spend your time each day changed?
I spend much more time on digital issues and analyzing and understanding data, and much less time dealing with ad agencies. Since my role is global, I also spend time thinking about how to scale ideas and get people out of silos—about providing broader strategic leadership and encouraging the exchange of best practices and information across regions, rather than focusing on the marketing issues within a particular country. And I talk a lot about a large global enterprise's need to proactively manage networks. Those include internal networks of constituents who have a direct stake in your enterprise, and outside networks of influencers who can significantly impact your business, such as analysts, bloggers, opinion elites, NGOs, suppliers, and governmental entities. Most critically, you need to engage consumer networks through digital interactions. The required skills are much different from when I began my career.

How much variation is there in how CEOs view the role?
It's surprising that even in large, sophisticated organizations, many CEOs still view the CMO's primary job as advertising. If I'm going into a company, I try to shift that view to be more holistic. Advertising is only a small part of what needs to be done to build the brand and the business. A CMO should be responsible for R&D, innovation, pricing, packaging, the customer experience, and other growth levers. It does no good to create compelling ads that run in prime time and then underdeliver in the retail environment. But a lot of CMOs exacerbate the narrow views that people have of the role.

How?
The first thing many do after they're hired is conduct an advertising review, hire a new agency, and launch a new campaign. That sets up an expectation that new ads will fundamentally change the trajectory of the business. When a CMO stakes his or her claim on a new campaign and you don't see a demonstrable change, it suggests the CMO has failed, so the company gets rid of the person. The challenge might have been distribution, pricing, or product quality. Don't think that communications can solve broader business challenges. At Coca-Cola, I was the seventh CMO in 10 years. I told the person doing the hiring: "Whether you hire me or not, this kind of turnover is not good for your company, and you have to find a way to fix this problem." I'm proud to say I survived for seven and a half years there.

Hasn't the marketing function always tended to come under fire, because of the challenge of delivering revenue?
Yes, there's an inherent riskiness to it. Marketing lives in a murky world, where you're always having to explain what the company is getting in return for its large ad expenditures. That causes a lot of to-ing and fro-ing with CFOs. It's incumbent upon CMOs to demonstrate clear value and convince everyone that marketing is not an expense but an investment. Also, when it comes to advertising, everyone is an expert—employees, the public, franchisees, even retirees. You hear a lot of opinions and second-guessing. That can also set the CMO up for challenges.

As CMOs have gained responsibilities, has it been at the expense of other C-suite officers?
I don't see it that way. Many of the new responsibilities stem from entirely new ways of communicating or connecting with customers, such as social media or e-commerce, so it's not as if they've been taken away from someone else. And many of them are shared with the CIO. Today, unless a CMO's closest business partner is the CIO, you won't have a very effective organization.

Because the role is so varied, must CMO candidates do more due diligence on

potential employers than other C-suite executives do?

You really have to network and do forensic-level analysis to find the unvarnished truth. You're being sold by the recruiter and the people inside the company, and jobs often aren't what they appear to be. There is no such thing as "truth in advertising" when you're being recruited. When I became the CMO at the Bank of New York, the company said it wanted to become more customer-driven and customer-focused. When I arrived, I found they actually had little appetite to invest in those areas, so I didn't last long. You learn from your mistakes. I should have done more due diligence. Now I do.

How do you convince a CEO that the CMO role needs to be designed differently?

You need to have an up-front conversation before you take the job. How are you going to measure success? If the CMO should be the champion for growth, will he or she have the right levers or the influence over those levers? You also must be sure you understand what's really driving the business, both today and in the future. Is the company prepared to invest in the capabilities and infrastructure to win in the future? Can you agree on what is needed to be successful? If not, you are being set up to fail.

What kind of personality traits should a CMO have?

You need to be comfortable living amid inherent contradictions. You have to drive growth but do it in a sustainable way. You have to focus on global strategies but recognize that the best marketing is often done locally. You have to be able to position your brand as timeless but still relevant. You must be focused on product quality but keep an eye on cost-effectiveness. You want to offer customers choice but without overwhelming your supply chain. It comes down to having dexterity, mental agility, and the ability to balance these competing priorities and contradictions.

Is it difficult for a CMO to jump between industries, as you've done?

It hasn't been for me. A widget is a widget. Whether I was working with credit cards, liquor, insurance, beverages, or sandwiches, I've found that the fundamental principles of great marketing are the same. Each business has its own nuances and unique language, but your colleagues can help you become acclimated to them. More often I see the opposite problem: Companies write job descriptions so narrowly that they exclude people from other industries they really should take a chance on.

At which company did you have the biggest success as CMO?

It's hard to name one, because each represented different business, brand, and cultural challenges. You do very little by yourself, but I feel my team had a really positive impact at Allstate. The company evolved to be much more consumer-focused and aggressive in its marketing. It had great CEOs—Ed Liddy and Tom Wilson—who gave me the authority and flexibility to do things that hadn't been done in the category previously. We also looked at the entire customer experience, from receiving a quote to getting a claim settled, and deconstructed it to understand the pain points for customers. Then we systematically addressed those areas and improved their experience. I'm also proud of the global services infrastructure we created at Mastercard and the "Priceless" campaign we did there. Coke has always been a marketing machine, so I'm very proud of the talent we brought in to sustain its greatness and pivot to a digital world.

IT'S ABOUT HAVING DEXTERITY, MENTAL AGILITY, AND THE ABILITY TO BALANCE COMPETING PRIORITIES.

What's your biggest challenge as CMO at Subway?

We need to transform the business, brand, and culture. It's a private company, held by two families, with nearly 45,000 restaurants in 112 countries, but it lacks the infrastructure for a business of that size and complexity. In many ways it's still run like a small family business, which has its pluses and minuses. I'm in awe of what Subway has accomplished in the past 50 years—it's the world's greatest franchising machine! I'm helping its leadership think about how to structure the enterprise for growth and what the strategy should be in different markets. It's very different from the challenges at Coke or Allstate, and in many ways it's the biggest business challenge of my career—exhilarating and daunting at the same time.

What advice do you give to young marketers who aspire to become CMOs?

First, get as much experience as you can in different functional areas. Within marketing, that includes communications, social media, design, operational or commercial marketing, and brand building. But don't live just in the marketing function; try to spend time in IT, business development, or sales. Second, gain some global experience, whether it's by living, working, or studying abroad. Third, try to get experience in different industries. I was really fortunate: My first job out of business school was in strategic planning at Mobil Oil, and it gave me a very broad view of how a large global enterprise operates, which was a solid foundation. In general, aim to have rich experiences, because that creates a tapestry that will serve you well.

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DANIEL MCGINN is a senior editor at HBR.

REDUCING CMO TURNOVER: A Recruiter's Prescription

BY GREG WELCH

Every few months I get a call from a CEO asking for a private meeting to talk about the company's current CMO. Typically, the CEO has grown unhappy with the CMO and is thinking about making a change. But first, he or she wants to talk through the various options and get a quick overview of the landscape for the very best senior talent.

It worries me that these calls come so regularly. That might seem counterintuitive, given that the livelihood of executive recruiters depends on a certain amount of turnover. But my colleagues and I are unhappy about how frequently CMOs fail.

When they do, it's largely because of poorly managed expectations. CEOs today want CMOs to be growth officers, but not all marketing executives have the capabilities, experience, and leadership style needed to lift revenues and profits and simultaneously learn to navigate a new culture. Keeping everyone focused on the job specifications is part of the challenge. Too often the hiring process turns into a popularity contest that favors charismatic candidates. Charisma is important, but if it prompts a company to hire someone whose skills don't line up with what's needed in the role, it increases the odds of failure.

When my colleagues and I take these meetings, we talk about issues specific to the company. But much of the discussion focuses on the broader CMO landscape, including whom we view to be the greatest CMOs and where the best marketing talent resides.

One of the first things I ask is what kind of marketer the CEO *really* wants. Someone to simply curate ads? Someone who is skilled at engaging consumers using modern digital marketing methods? Someone with prior P&L experience who can launch innovative new products and profitably grow revenue? My objective is to help the CEO understand that the roles CMOs play vary widely by company and industry. I often bring a chart that reflects this range of skills and competencies and ask CEOs to identify the ones most critical for their companies.

As an executive recruiter, I've placed nearly 500 CMOs in their jobs during the past two decades. As you might expect, I've grown close to a number of them, witnessing not only their successes but also their failures. On the basis of what I've seen, I believe that the CMO role has changed more profoundly than any other C-suite position has.

The size of many marketing teams has grown exponentially. Some CMOs now have thousands of people reporting up to them, which rarely was the case in the 1990s. Because marketing has expanded to include data and analytics, the composition of the teams now varies tremendously, too. Often they include PhDs in math, sociologists, and designers, along with more-traditional marketing staffers. In many industries the sheer scope of a CMO's responsibilities has swollen as well. In airlines, for instance, many CMOs have broad commercial responsibility, touching virtually everything outside the cockpit doors—from sophisticated dynamic fare pricing, to credit card partnerships and loyalty and mileage-awards programs, to the extras like Wi-Fi and additional legroom.

The other significant change is the ongoing blurring of channels caused by the growth of e-commerce and the reach of social media. New marketing tools give CMOs more ways to win customers, but these same tools give vocal (and sometimes angry) customers a platform. That can create a new threat to brands and the CMOs who manage them.

Many of the people who flounder in CMO jobs are really smart, talented executives, which is why their failures are especially frustrating. To increase the odds that new CMOs will succeed, we help them construct strategic onboarding plans that ensure faster, more-productive starts. We also advise them to develop deep relationships with their C-suite peers. And we counsel CEOs to establish ambitious but achievable expectations with the CMO.

Getting the right CMO into the right role at a company can be catalytic. The results—for the CEO, the shareholders, and the customers—can be dramatic. And of course, for me, helping clients think through the future of marketing for their organizations and find the right person to lead them into it is one of the most satisfying parts of my job.

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GREG WELCH is a senior partner at Spencer Stuart.

The Evolution of the CMO

As marketing channels and tools grew over the decades, so did the status and responsibilities of top marketing executives.

BY CAREN FLEIT

1950s

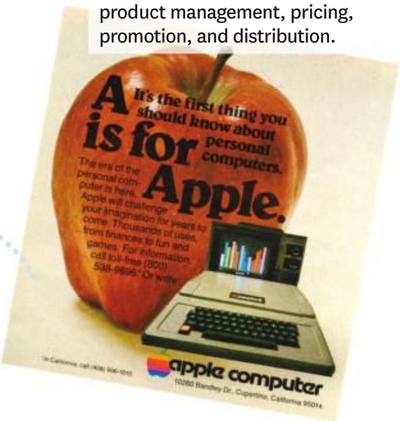
Marketing focuses largely on creating TV and print advertising to sell products to consumers. Top-level marketing executives are found almost exclusively in the consumer goods and automotive industries.

1960s

Advertising is still limited mainly to paid TV and print channels but moves away from exaggerated claims and aggressively pushing products and toward inventing creative and memorable approaches. The ad campaign is king.

1970s

Marketing adopts analytics and begins generating insights about customer choices and segmenting customers. Particularly in consumer goods, marketers become increasingly responsible for product management, pricing, promotion, and distribution.


A is for Apple.
It's the first thing you should know about personal computers.
apple computer

1980s

Cable TV, infomercials, and VCRs (which allow viewers to skip ads) make marketing's job more complex and ratchet up the pressure for advertising efficiency. Analytics become critical to precisely tracking performance in each sales channel. Consumer-goods marketers start to assume P&L responsibility and enterprise-wide roles. Other industries, like consumer finance, begin hiring top-level marketing executives, though those jobs focus more on branding and corporate communications.

1990s

A broader marketing function emerges in industries such as health care and technology, and B2B marketers appear. The role of the marketing leader becomes blurry, as companies struggle to find a balance between more-strategic responsibilities (brand positioning, segmentation, and business growth) and more-tactical ones (sales enablement, creating brochures, and manning trade shows). Marketing departments begin to set up matrix structures combining corporate functions with regional and business unit functions. Customer relationship management takes hold. The CMO title is first used.

2000s

The digital revolution changes the way companies and customers relate. As social media platforms take off, people rely more on one another for information about products. Marketers must manage omnichannel communications and both negative and positive messages about their brands. They begin focusing on building meaningful relationships with customers. The CMO title spreads but is used indiscriminately both for executives strictly focused on brand and communications and for true strategic business partners.

2010s

Big data and artificial intelligence swamp marketers with information. The focus shifts from telling and selling to customer engagement and dialogues and personalized communications and products. CMOs are expected to creatively apply insights to business challenges, validate decisions with data, create seamless customer experiences across media and revenue channels, and lead efforts to put the customer at the center throughout the organization. Most CMOs now sit on executive committees and report directly to the CEO. But there is confusion about the role, leading some to question the title and explore alternatives like chief customer officer, chief customer experience officer, and chief growth officer.

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ADVERTISING ARCHIVE

CAREN FLEIT leads Korn Ferry's global marketing practice.

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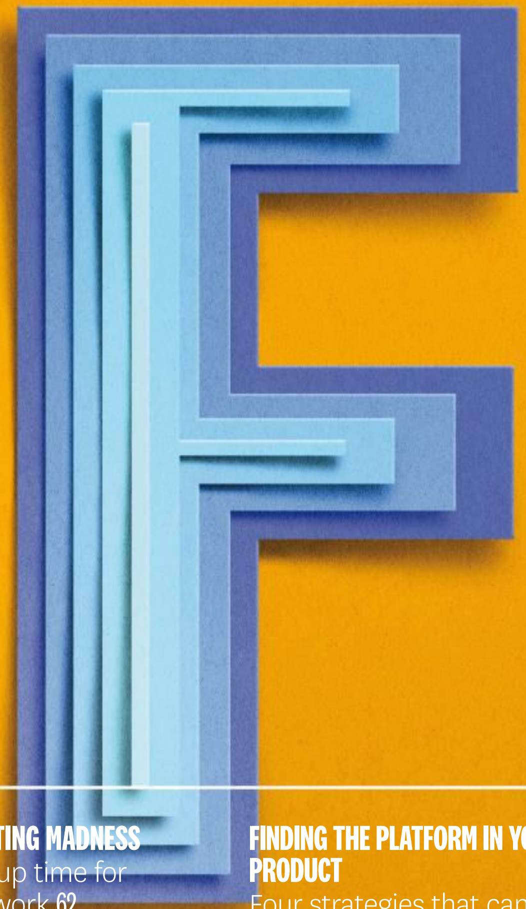

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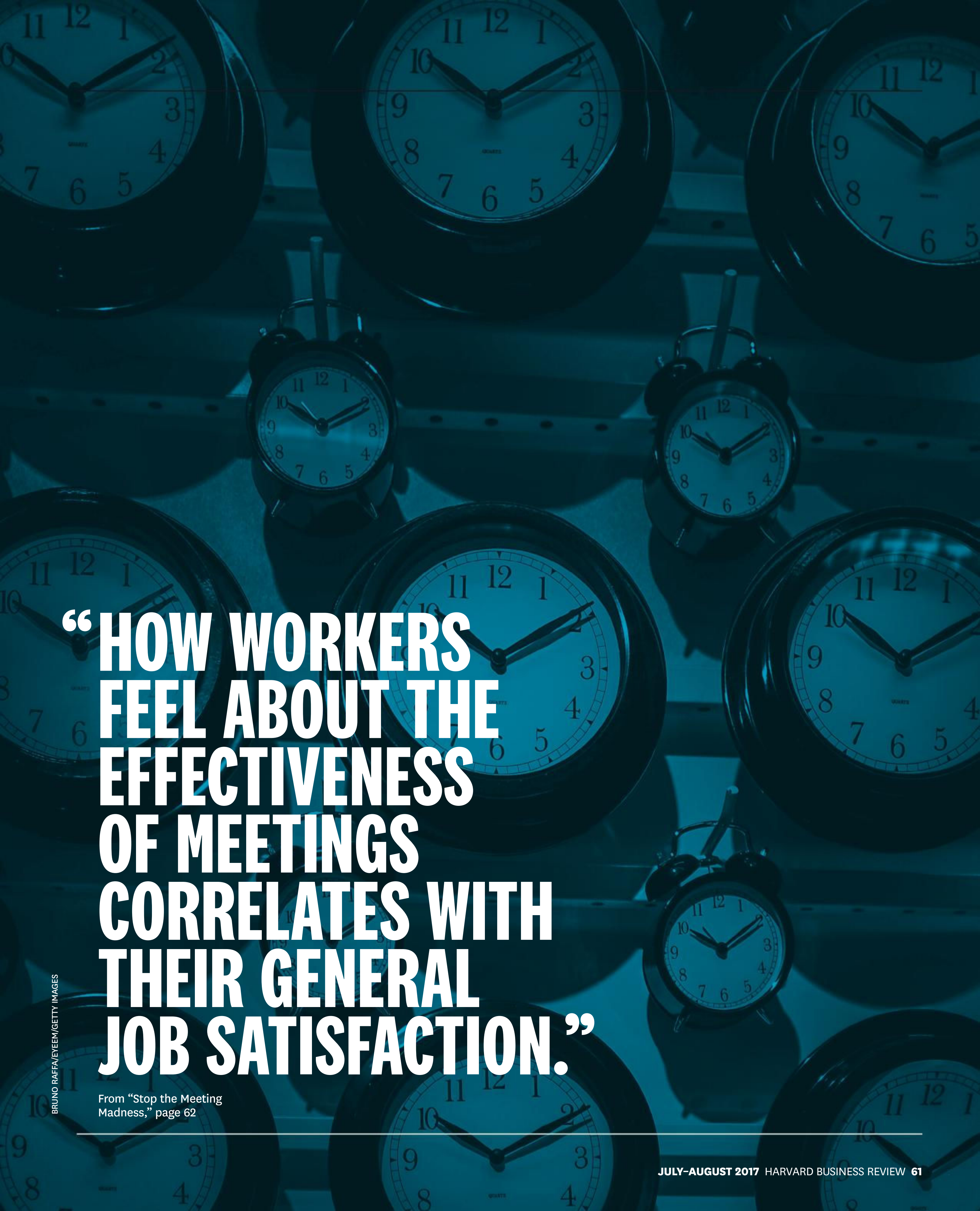

“HOW WORKERS FEEL ABOUT THE EFFECTIVENESS OF MEETINGS CORRELATES WITH THEIR GENERAL JOB SATISFACTION.”

From “Stop the Meeting Madness,” page 62

BRUNO RAFFA/EYEEM/GETTY IMAGES

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SEE PAGE 41 FOR INSTRUCTIONS.

STOP THE MEETING MADNESS

HOW TO FREE UP TIME FOR MEANINGFUL WORK

BY LESLIE A. PERLOW, CONSTANCE NOONAN HADLEY, AND EUNICE EUN

ELENA KULIKOVA/GETTY IMAGES

IN BRIEF

THE CHALLENGE
Meetings are supposed to improve creativity and productivity—but they do the opposite when they're excessive, badly scheduled, poorly run, or all three. These problems take a toll on the whole organization, and they require systemic fixes.

THE SOLUTION
Groups must first figure out what kind of time their meetings tend to waste—group, individual, or both. They can then follow a five-step process for change: (1) collect impressions from each member; (2) interpret those together; (3) choose a group goal for improving meetings that feels personally relevant and motivating; (4) measure progress; and (5) regularly check in to make sure people don't revert to old patterns.

Poking fun at meetings is the stuff of *Dilbert* cartoons—we can all joke about how soul-sucking and painful they are. But that pain has real consequences for teams and organizations. In our interviews with hundreds of executives, in fields ranging from high tech and retail to pharmaceuticals and consulting, many said they felt overwhelmed by their meetings—whether formal or informal, traditional or agile, face-to-face or electronically mediated. One said, "I cannot get my head above water to breathe during the week." Another described stabbing her leg with a pencil to stop from screaming during a particularly torturous staff meeting. Such complaints are supported by research showing that meetings have increased in length and frequency over the past 50 years, to the point where executives spend an average of nearly 23 hours a week in them, up from less than 10 hours in the 1960s. And that doesn't even include all the impromptu gatherings that don't make it onto the schedule.

Much has been written about this problem, but the solutions posed are usually discrete: Establish a clear agenda, hold your meeting standing up, delegate someone to attend in your place, and so on. We've observed in our research and consulting that real improvement requires systemic change, because meetings affect how people collaborate and how they get their own work done.

Yet change of such scope is rarely considered. When we probed into why people put up with the strain that meetings place on their time and sanity, we found something surprising: Those who resent and dread meetings the most also defend them as a "necessary evil"—sometimes with great passion. Consider this excerpt from the corporate blog of a senior executive in the pharmaceutical industry:

> **I believe that our abundance of meetings at our company is the Cultural Tax we pay for the inclusive, learning environment that we want to foster… and I'm ok with that. If the alternative to more meetings is more autocratic decision-making, less input from all levels throughout the organization, and fewer opportunities to ensure alignment and communication by personal interaction, then give me more meetings any time!**

To be sure, meetings are essential for enabling collaboration, creativity, and innovation. They often foster relationships and ensure proper information exchange. They provide real benefits. But why would anyone argue in defense of excessive meetings, especially when no one likes them much?

Because executives want to be good soldiers. When they sacrifice their own time and well-being for meetings, they assume they're doing what's best for the business—and they don't see the costs to the organization. They overlook the collective toll on productivity, focus, and engagement.

For one thing, time is zero-sum. Every minute spent in a wasteful meeting eats into time for solo work that's equally essential for creativity and efficiency. For another, schedules riddled with meetings interrupt "deep work"—a term that the Georgetown computer science professor Cal Newport uses to describe the ability to focus without distraction on a cognitively demanding task. (In a recent study, managers across the board in the United States and China told us that this happens "far too often!") As a consequence, people tend to come to work early, stay late, or use weekends for quiet time to concentrate.

Another issue is the stiff price companies pay for badly run meetings. For example, Simone Kauffeld, of Technische Universität Braunschweig, and Nale Lehmann-Willenbrock, of the University of Amsterdam, found in a study of 20 organizations from the automotive supply, metal, electrical, chemical, and packaging industries that dysfunctional meeting behaviors (including wandering off topic, complaining, and criticizing) were associated with lower levels of market share, innovation, and employment stability.

Happiness at work takes a hit too. A study by Steven Rogelberg, of the University of North Carolina, and colleagues showed that how workers feel about the effectiveness of meetings correlates with their general satisfaction or dissatisfaction with their jobs, even after controlling for personality traits and environmental factors such as work design, supervision, and pay. Instead of improving communication and collaboration, as intended, bad meetings undermine those things. Consider the executive who stabbed her leg with a pencil. Did that staff meeting advance teamwork or set it back? A few positive experiences a week cannot make up for a lot of excruciating, wasteful ones.

The good news is, we've found that changing the way your team and your organization approach meetings is possible. In this article we describe a five-step process for that—along with the diagnostic work you'll need to do in advance. Often the results can be dramatic and extend far beyond the conference room. At a financial and regulatory consultancy we studied, for example, three months after managers began to rethink the firm's approach to meetings, a survey showed that employees perceived significant improvements in team collaboration (a 42% increase), psychological safety to speak up and express opinions (a 32% increase), and team performance (a 28% increase). Other aspects of organizational life improved as well, and respondents' ratings of satisfaction with work/life balance rose from 62% to 92%.

We have seen how much organizations can benefit when they focus their energy on transforming meetings instead of just tolerating them. Here's how to identify and address the meeting problems your group may face.

HOW IS YOUR GROUP VULNERABLE?

Problems ensue when meetings are scheduled and run without regard to their impact on both group and solo work time. Often groups end up sacrificing collective or individual needs—or both—by default. Balancing those needs effectively is ideal, but few organizations do that. In a recent survey we conducted with nearly 200 senior executives from diverse industries, only 17% reported that their meetings are generally productive uses of group and individual time. Other respondents said their meetings fall into one of these categories:

Wasters of group time. Some organizations have relatively few meetings but run them poorly. As a result, individuals have sufficient time for solo tasks and deep thinking, but group productivity and collaboration are weakened because each meeting is inefficient. About 16% of the executives in our sample said this is true where they work.

A team at a global e-commerce company we studied had just one or two meetings a week, but they still felt like a waste of group time for several reasons. First, hours and locations often changed at the last minute, so many people arrived unprepared or didn't come at all. Second, the agenda was often vague or redundant with side conversations that had already occurred, so the meetings felt like a rubber-stamping of decisions made elsewhere. Third, when new issues were raised, next steps were usually left unclear, leading to more sidebar conversations outside the room. One software developer told us that he kept showing up for the meetings even though he rarely got anything out of them, because his attendance was expected by his manager and everyone else. As a workaround, he covertly did his own tasks during meeting time. While this may seem like a harmless way to maintain individual productivity in the short term, it causes group productivity and camaraderie to deteriorate over the long term. When people don't contribute to the discussion or pay attention to what's being said, the team fails to reap the full benefits of convening, and the meeting wastes everyone's time.

Wasters of individual time. Sometimes meetings are relatively high in quality and therefore technically a good use of group time—but individuals' time dissipates because the sheer quantity of meetings crowds out solo work, and poor scheduling disrupts critical deep thinking. In our survey of executives, 13% said that their organizations struggle with this particular problem.

WE SURVEYED 182 SENIOR MANAGERS IN A RANGE OF INDUSTRIES:

65%

SAID MEETINGS KEEP THEM FROM COMPLETING THEIR OWN WORK

Here's an example of how it plays out: One private equity firm we examined had a rigorous protocol for running effective meetings. For each session, prework was sent out with adequate notice, clear goals were established, and meeting time was managed against an agenda. Group updates and decisions were consequently handled efficiently. However, as the firm grew over time, more and more meetings were added to the weekly calendar. Although they were well run, their sheer volume interrupted work flow and took away time that the investment staff could dedicate to critical individual tasks, such as sourcing new opportunities and deepening relationships with managers at companies the firm owned or sought to own. As this firm's experience demonstrates, excessive meetings force people to make trade-offs concerning how and when to accomplish their solo work. Sometimes tasks get dropped or short-changed. But more often people steal from their personal time to get that work done, a sacrifice that research and practice have shown can lead to burnout and turnover—steep prices for both employees and organizations.

71%

SAID MEETINGS ARE UNPRODUCTIVE AND INEFFICIENT

Wasters of both individual and group time. Many organizations we have worked with endure the triple whammy of meetings that are (1) too frequent, (2) poorly timed, and (3) badly run, leading to losses in productivity, collaboration, and well-being for both groups and individuals. This is the worst-case scenario—and, unfortunately, the most prevalent. The majority of our survey respondents—54%—put their meetings in this category.

One manager at a pharmaceutical company described finding herself in a one- to two-hour "market readiness" meeting every other week because the organizer really wanted her to attend, claiming that everyone's input was extraordinarily valuable. However, the group also typically sent out slide decks for the team to review in advance and then just walked through those decks during the meetings. As this manager asked herself and her team, "Why would you need to get one person from each subteam from every department into a room just to go over each slide individually when you've already sent us the entire deck?" Her team members commiserated, reporting that they each attended scores of similarly wasteful meetings that left them with little or no time for their "real work" throughout the day. In situations like this, group time is wasted and individual time is obliterated.

STRIKING THE RIGHT BALANCE

Unfortunately, individuals can't solve these problems on their own. Just think how many times you've tried to reduce the number of meetings on your calendar—probably with limited success. Because so many people are involved in scheduling and running the meetings we attend, it takes a collective effort to fix them.

However, with a structured approach to analyzing and changing meeting patterns throughout your team or unit, you can make significant improvements. We've seen groups escape the meeting trap by working together to follow five basic steps:

1 **Collect data from each person.** To get a clearer view of how meetings are affecting your group, use surveys or interviews to gather data and impressions from every individual. That will help you gauge the full extent of the problem: You'll learn how much resentment is bubbling under the surface and how much work isn't getting done during the day. (See the exhibit "How Are Meetings Affecting People in Your Organization?")

2 **Interpret the data together.** Next, it's critical to come together as a team or a unit to digest everyone's feedback and analyze what is working and what is not. This must be an open, nonjudgmental discussion of the survey or interview findings. Neutral facilitators can help keep the conversation constructive. However, delegating the data interpretation to an outside consultant—or even just a subset of the team—can undermine success. You'll need contributions and analysis from all team members to generate the widespread understanding and buy-in required for the remaining steps.

At the financial and regulatory consultancy we studied, for example, exploratory interviews revealed that meetings were chopping up calendars so badly that very few two- or three-hour blocks were left for deep-thinking work. Without enough quiet time to concentrate, the consultants felt that their creativity and productivity were being sapped. These disclosures served as a wake-up call for the managers who had been

64%

SAID MEETINGS COME AT THE EXPENSE OF DEEP THINKING

POPPERFOTO/GETTY IMAGES

scheduling meetings without a full awareness of the impact they were having.

3 **Agree on a collective, personally relevant goal.** We have found that personally benefiting from the group's initiative is a great motivator. For example, you might designate a certain amount of time each week for people to focus on independent work—whether in the office or at home. Giving them such flexibility and freedom can provide necessary relief in their schedules, along with an incentive to make the arrangement work. Declaring "meeting free" periods also forces the whole group to reevaluate meetings that were normally scheduled during those times and to ask who really needs to attend. As a result, we find, teams hold fewer meetings overall, and fewer people go to each one. The additional "white space" in everyone's calendar increases individual productivity and reduces the spillover into personal time.

Here's how this approach worked at a technology consultancy we examined: Members were based in the United States and India, so a handoff meeting was held each day—early in the morning for some and late at night for others to accommodate the 12.5-hour time difference. The long days were causing significant stress and fatigue on both sides: Early-morning calls were required, family dinners were missed, workdays were more than 12 hours long. Once the team had collected survey data from its members and realized the magnitude of the problem, it altered its approach: Each person was given one workday a week when he or she didn't have to participate in the handoff call.

In order to ensure the appropriate information exchange, team members had to find ways to cover for one another and keep everyone updated. Learning how to do that gave individuals the break they needed, but it also resulted in more shared knowledge and versatility in the group. Furthermore, people gained a deeper understanding of their colleagues' work, which led to better-integrated offerings for customers.

4 **Set milestones and monitor progress.** As with any change effort, it is important that concrete and measurable progress be assessed and discussed along the way. Small, tangible wins provide something for people to celebrate, and small losses provide opportunities for learning and correction. Consider this example: At a global e-commerce company, a team of 30 employees spanning the United States and China told us that their weekly all-hands meetings were a pain point. Attendees were often on their phones or laptops. Because people were continually distracted, those who spoke had to repeat themselves frequently, making the time spent not only longer but also much less effective.

HOW ARE MEETINGS AFFECTING PEOPLE IN YOUR ORGANIZATION?

Ask them. That's a simple, direct way to collect data from each person (step 1 in the process outlined in this article). Regular "pulse checks" will help you gauge ongoing reactions, but it's also good to use surveys, interviews, or both to periodically gather responses to a series of probing questions. Include your own answers as well.

GOAL	SAMPLE QUESTIONS FOR INDIVIDUALS	WHAT THEIR ANSWERS REVEAL
TAKE EVERYONE'S EMOTIONAL PULSE	Look at your work calendar for the week ahead: • What emotions does it evoke in you? • What three words or phrases come to mind when you think about the meetings you attend regularly?	• How negatively people feel about meetings in your organization • How much rationalization or defensiveness supports the status quo
TALLY THE HOURS SPENT IN MEETINGS	Now look at your work calendar for the past three weeks: • How many meetings did you attend, and how much time did you spend in them altogether? • Week by week, did you spend more or less time in meetings than usual? What about day by day? How does that compare with your typical schedule?	• The total time your organization spends on meetings, along with the average amounts per week and day • How much those figures vary in your organization (by person, role, function, or group)
CONSIDER THE BALANCE BETWEEN GROUP AND INDIVIDUAL WORK TIME	Looking again at the meetings you attended over the past three weeks: • Did you feel you had sufficient time left to get your own work done, or did you need to use off-hours to accomplish it? • How much time outside normal business hours did you spend on your work?	• The perceived impact on people's ability to do their own work during the day • Total off-hours time spent catching up on individual work
ASSESS IMPACT ON WORK QUALITY	Now let's go to a typical week in your calendar. Of the meetings you attended, how many (or what percentage) would you say were: 1. Very productive, essential 2. Somewhat productive, marginal 3. Not very useful, a waste of time	• The perceived proportion of high-, medium-, and low-quality meetings • How much that varies in your organization
IDENTIFY BEST PRACTICES	Take a closer look at your quality ratings: • Overall, what differentiates the meetings that were consistently rated as very productive from those in the other two categories? • Take a sample meeting from each category. On a scale of 1 to 10, how would you rate the effectiveness of each one? • Do you see patterns in the best meetings that could be replicated elsewhere? • How else might you leverage the lessons from the productive meetings?	• What sets the best meetings apart from the rest • Just how bad the worst meetings are, and why • Ideas for extending positive practices throughout the organization

62%

SAID MEETINGS MISS OPPORTUNITIES TO BRING THE TEAM CLOSER TOGETHER

To help address these problems, the team decided on a simple, tractable goal: Allow no outside technology at the meetings.

At first several vocal engineers and even the team leader were resistant, feeling that they should have the right to use their devices, especially when meetings became boring or turned to topics outside their purview. For a while after the initiative was launched, friendly reminders ("No tech, man!") were necessary. But over time the new norm took hold, and even the manager self-corrected when he instinctively started to check his phone. The team began to see the benefits of this experiment. Meetings became more productive, and people were more engaged. As one engineer said, "This no-tech rule is fantastic! Now that people are more focused on the meeting, it's more efficient." Another team member started bringing a notebook to jot down thoughts rather than playing games on her phone. This small victory opened the door to setting other new norms, such as preparing materials more thoroughly ahead of time, keeping meetings as brief as possible, and ultimately reworking meeting cadences to better fit the team members' schedules.

5 Regularly debrief as a group. Finally, we have found that it is critical to regularly and openly take stock of how people feel about the meetings they attend and about their work process more generally. Frustration, resentment, and even hopelessness are signals that people are falling back into bad patterns. Moreover, changing protocols and behaviors takes time, and sustaining momentum requires consistent attention and contact.

At a pharmaceutical company we worked with, the global medical-affairs division established two regular "pulse checks" to monitor the progress of an experiment it was conducting with meeting-free days: one check within the subteam and one across the division. At the beginning of each pulse check, participants answered four questions: How are you feeling? How valuable are the ways in which you are spending your time? How well are you working as a team? Is this sustainable?

The answers to these questions triggered substantive discussions, rich in emotional, strategic, and tactical content. Early conversations focused specifically on the meeting problem, but over time they increasingly addressed how team members approached their work—and one another. One manager said, "I'm impressed with how these meetings have allowed people to open up, particularly with [the manager] listening....Pulse checks are really insightful—they give me a good dose of reality....and they surfaced issues that resulted in more cross-coverage, people development, and teamwork. It sounds crazy that this little experiment could create these sorts of results, but it has profound implications far beyond the initial goal."

We suggest brief weekly check-ins for a few months, until the new norms, processes, and attitudes are in place. After that, every other week should do it. Regardless of the frequency of pulse checks, people should have regular, structured forums in which to express their frustrations and surface problems as well as to improve how the team works together.

For all these steps, leadership support is critical—but it doesn't necessarily need to come from the C-suite. We have found that a group can change its approach to meetings as long as the team leader has the authority to encourage people to raise issues, take risks, make mistakes, and discover new ways of working together. This can happen even if the group is closely connected to other groups in the organization. For example, the global medical-affairs division's refusal to attend interdivisional meetings on meeting-free days was met first with consternation, then with curiosity, and ultimately with change throughout the organization as norms were shattered and new ways of working were modeled.

A CONDUIT FOR CHANGE

As we have witnessed at multiple companies in a range of industries, altering something as basic as meetings can have far-reaching implications. One manager reflected, "We started communicating more openly and honestly, which enabled us to better help each other.... We helped each other prioritize, we helped each other find access to other resources, and sometimes we reallocated tasks or simply helped each other do the work."

Meetings do not have to be a trap; they can be a conduit for change. A process like this one can improve productivity, communication, and integration of the team's work, not to mention job satisfaction and work/life balance. In the end, better meetings—and better work lives—result.

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FURTHER READING

For more on increasing organizations' productivity and efficiency, see these HBR articles.

"Your Scarcest Resource"
Michael Mankins, Chris Brahm, and Greg Caimi
(May 2014)

"Get Your Team to Do What It Says It's Going to Do"
Heidi Grant
(May 2014)

"Manage Your Team's Collective Time"
Leslie A. Perlow
(June 2014)

"Make Time for the Work That Matters"
Julian Birkinshaw and Jordan Cohen
(September 2013)

BEING THE BOSS IN BRUSSELS, BOSTON, AND BEIJING

IF YOU WANT TO SUCCEED, YOU'LL NEED TO ADAPT.

BY ERIN MEYER

Cultural differences in leadership styles often create unexpected misunderstandings. Americans, for example, are used to thinking of the Japanese as hierarchical while considering themselves egalitarian. Yet the Japanese find Americans confusing to deal with. Although American bosses are outwardly egalitarian—

ILLUSTRATION BY MARK BOARDMAN

encouraging subordinates to use first names and to speak up in meetings—they seem to the Japanese to be extremely autocratic in the way they make decisions. As a Japanese manager living in the United States and working for Mitsubishi put it: "I couldn't figure out how to adapt my approach from one day to the next, because the culture was so contradictory and puzzling."

Problems like this manager's are widespread. In many years of researching, consulting, and teaching executives and managers in hundreds of global companies, I've found that it's common for people from different countries to grapple with mutual incomprehension. Often that's because managers fail to distinguish between two important dimensions of leadership culture.

The first of these is the one we're most familiar with: *authority.* How much attention do we pay to the rank or status of a person, and how much respect and deference do we pay to that status? On this dimension, the Japanese are clearly more hierarchical than Americans. The positions are reversed, however, when we look at the second dimension: *decision making.* Who calls the shots, and how? Does the boss decide, or does the team decide collectively? On this dimension, which is often overlooked, the Japanese are more consensual than Americans.

Approaches to authority and decision making are not the only ways in which cultures differ, but they are arguably the most important in the leadership context. And if international managers confound the two, they will make mistakes in adapting their leadership styles to the cultures and situations at hand. (For a more general treatment of cultural differences, take a look at my May 2014 HBR article, "Navigating the Cultural Minefield.")

In the following pages, I explore the two dimensions and how they affect global leadership effectiveness, focusing particularly on how attitudes toward decision making impact global teamwork. I conclude by mapping selected cultures along both dimensions and comparing the resulting expectations about the role of the leader.

THE WESTERN MANAGEMENT ORTHODOXY OF PUSHING AUTHORITY DOWN IN THE ORGANIZATION DOES NOT FIT EASILY INTO THE EMERGING-MARKET CONTEXT.

ATTITUDES TOWARD AUTHORITY

Over the past century, the biggest leadership trend in the U.S. and parts of Western Europe has been the abandoning of hierarchical management processes for a more facilitative, egalitarian approach. Command-and-control has been replaced with empowerment. Managers have been trained to stop telling their employees what to do and instead move to "management by objective," open-door policies, and 360-degree feedback. Early on, addressing the boss by first name rather than title became the norm. Company hierarchy further dissolved when the CEO began "management by walking around," having impromptu discussions with people at all levels without even letting their supervisors know. Then the corner office yielded to open-plan spaces. Since most management literature and research still come out of the U.S., business school education has largely reinforced this trend.

But attitude toward authority is one of the most striking points of difference across cultures. In Nigeria a child learns to kneel or even lie down as a sign of respect when an elder enters the room. In Sweden a student calls her teachers by their first names and, without implying any disrespect, feels free to contradict them in front of her classmates. Unsurprisingly, the management approach that works in Lagos will not get the best results in Stockholm.

Understanding this disconnect is important. In general, the greatest business opportunities lie in the big emerging economies, which include Bangladesh, China, India, Indonesia, Russia, and Turkey. In nearly every case, these are cultures where hierarchy and deference to authority are deeply woven into the national psyche. The management orthodoxy of pushing authority down in the organization does not fit easily into the emerging-market context and often trips up Western companies on their first ventures abroad.

Take the case of an American firm I worked with two years ago. I'll call it Chill Factor, as it delivers innovative cooling solutions to consumers and small businesses. For the previous 15 years, Chill Factor had been training its employees in the latest egalitarian leadership methods, encouraging low-level workers to show initiative, while teaching the bosses to leave their doors open, accept 360-degree feedback, and set objectives rather than issue edicts. Additionally, the business had set up the flattest organizational structure possible. This progressive culture helped the company attract talent and keep employees inspired and engaged. The entire workforce was humming with creativity and innovation.

After decades of success in the U.S., Chill Factor took a big jump and negotiated a joint venture with a company in Hangzhou, China. But within weeks the Chill Factor managers were complaining about the lack of initiative shown by their Chinese staff. As one manager related to me:

> My Chinese employees don't see it as their job to have ideas or make suggestions to their leaders. They just follow instructions. Subordinates do not volunteer solutions but simply present problems. Their measure of success is to do what they are told, when they are told, and to do it well. But I expect them to produce new ideas and to give the bosses information so that we can make the best decisions for the benefit of the business.

In a session with a group of American executives and a dozen of their Chinese colleagues, I asked the Chinese managers to work as a small group and give advice to the Americans about how to handle their Chinese staff more effectively. They huddled and then presented their recommendations:

> Because Chill Factor now wants to succeed in China, we hope our American colleagues could kindly make some changes:
> 1. Before attending a meeting with your staff, prepare more ideas for yourself.
> 2. Be more specific with directions to your employees.
> 3. Have your own plan before allocating work to your subordinates.

The American managers were dumbfounded and asked for elaboration. "The most surprising comment from our Chinese colleagues," one Chill Factor executive later explained, "was that we were perceived not just as incompetent but as arrogant, because we didn't take the time to explain to our staff carefully and in detail what we wanted them to do and how." It was a valuable learning moment for this firm, which began to pull back on some of the egalitarian practices that it had so long taken for granted as the best approach.

Of course, those who already have some international experience might not be surprised that Chinese managers defer to their bosses and that American attitudes toward status don't travel well. But understanding differences in attitudes toward hierarchy and status, as we've noted, isn't the whole story.

ATTITUDES TOWARD DECISION MAKING

Many executives and managers assume that in more-hierarchical societies, decisions will be made at the top by the boss, and in more-egalitarian cultures, decisions will be reached by group consensus. Yet on a worldwide scale, we find that hierarchies and decision-making methods are not always correlated.

The U.S. is a striking example. American business culture has become more and more egalitarian over recent decades, but consensual decision making is clearly not the norm. American companies favor quick and flexible decisions, so decision-making power is vested in the individual (usually the boss). With a disdain for "analysis paralysis" and a belief that "any decision is better than no decision," the American manager may solicit input from his or her team but ultimately is the one to make the final determination. And in most cases, the team members not only are fine with this but expect it. The U.S. can thus be described as an egalitarian culture where decisions are made top-down.

In top-down decision-making cultures (India, Italy, Mexico, Morocco, and Russia are other examples), decisions are made quickly, but they are subject to change as new input or arguments arise. When people in these cultures say they've reached a decision, the decision is not a firm commitment but a placeholder that can later be adjusted.

Contrast that with what happens in Germany, Japan, the Netherlands, and Sweden. If you've collaborated with companies in those countries, you might have noticed that a lot of people seem to be involved in the decision-making process, and it takes a long time to negotiate group agreement. However, once a decision gets made, implementation is surprisingly quick, because details and stakeholders were aligned while consensus was being reached. In these consensual cultures, it's as if the word "Decision" has a capital "D," representing a commitment that can't (and shouldn't) be easily changed.

Either system can work well, and both have their advantages. Small "d" top-down decision making is particularly suited to industries where the pace of change is fast and speed to market trumps product perfection. Big "D" consensual cultures are great for industries where development timelines are long and

IN BRIEF

THE PROBLEM
Differences in leadership culture can create unexpected paradoxes. American bosses, for example, think of themselves as egalitarian, yet to the famously hierarchical Japanese, they can come across as dictatorial. Such contrary perceptions often undermine managers operating outside their home countries.

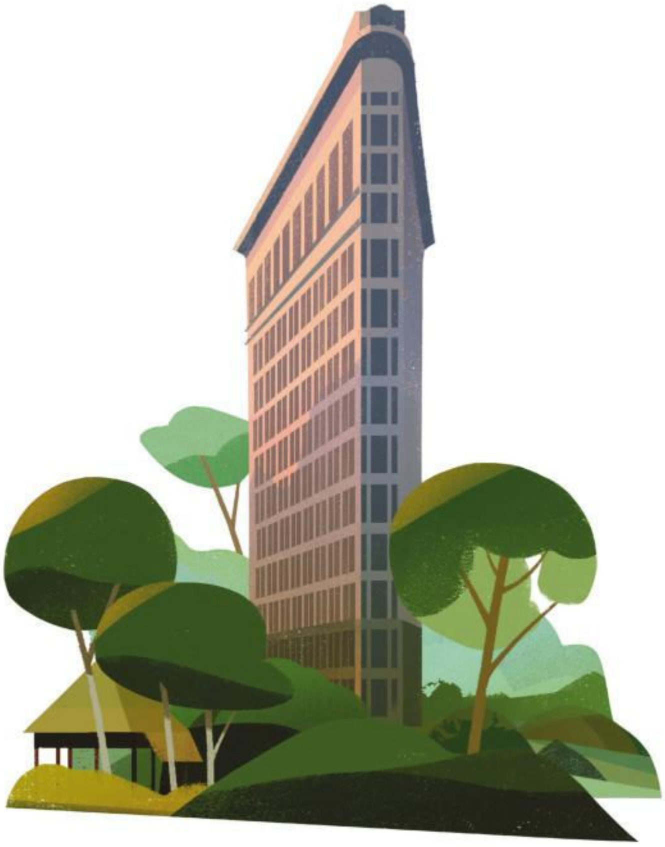
WHY IT HAPPENS
Managers often fail to distinguish between two important dimensions of leadership culture: attitudes toward authority and attitudes toward decision rights. On the first dimension, Americans are certainly more egalitarian than the Japanese. But Americans typically practice top-down decision making, whereas the Japanese have a strong tradition of building consensus.

THE SOLUTION
Leadership cultures fall into one of four categories depending on how they score along the two dimensions. Managers going into a new cultural environment must figure out which category they are moving to and adjust accordingly.

perfection of the product is essential. It's perhaps no surprise that two big "D" cultures—Germany and Japan—are among the world's greatest car-manufacturing nations.

Problems arise, however, when members of a single team have different norms of behavior. What happens, say, when a consensual big "D" Japanese company acquires a top-down small "d" American business? This was exactly the situation when Suntory became the majority shareholder in Beam (maker of Jim Beam whiskey). The success of this acquisition reveals some useful strategies for navigating safely through big "D"/small "d" collaboration.

IF GROUPS HAVE DIFFERENT SYSTEMS FOR REACHING DECISIONS, YOU MUST BE EXPLICIT ABOUT THE PROCESS.



As is the tradition in Japan, Suntory managers used a consensual big "D" system of decision making. One of them explained:

> In Suntory the management structure is hierarchical, but decisions are most often made by group consensus. Mid-level managers discuss a proposal among themselves and come to a consensus before presenting it to managers one level higher. The next-higher-ranking managers then discuss the proposal themselves and come also to an agreement. If they collectively believe in the initiative, they pass it on for approval at the next level, until it gets to the top.

Two words define this consensual process, so common in Japanese companies. The first is *nemawashi*—the practice of speaking with each individual stakeholder before a meeting in order to shape the group decision and develop agreement in advance. The second is *ringi,* which involves passing a proposal around level by level, starting at the bottom and then working through the layers of middle and senior management before arriving at the top.

This system works beautifully, provided everyone understands and follows it. The problems at Suntory and Beam arose because managers on one side didn't understand how managers on the other side made decisions. The experience of one American manager from Beam provides a nice illustration:

> There was a problem and a decision had to be made, which required a trip to Japan. The Japanese director in charge would be present, so I thought this would be the perfect moment to impact his direction. I prepared some slides for a meeting, along with my proposal. During the meeting, it became apparent that the decision had already been made by the group beforehand and was different from my proposal. Trying to discuss and convince during the meeting had no effect at all.

Learning the approach of the other culture and adapting accordingly is obviously important. Through trial and error and by asking questions, the Beam manager came to see that his assumptions about how and when decisions would get made was entirely a result of his experience working in the U.S. Over time, he learned to give his input much earlier at Suntory. But if you're managing the collaboration of two groups with different systems for reaching decisions, being flexible and adapting your individual style are not enough. You must also be explicit about the process of decision making. Define whether decisions will be made by consensus or by the boss. Establish whether 100% agreement is needed. Clarify whether a deadline for the decision is necessary and, if one is set, how much flexibility there will be for changes afterward.

Consider the case of a German-American collaboration I worked on. Early in the project, team members from both countries discussed a major decision ahead of a meeting with the company's big boss in the U.S. The team formed a point of view, and everyone seemed united on it. But during the actual meeting, after a very short discussion, the boss announced her decision, which ran counter to the team's recommendation. The Americans all agreed with the boss without a word of pushback. The German team members, however, were deeply unhappy about this turn of events, concluding not only that the American boss was arrogant but also that their American colleagues were two-faced.

Of course, these perceptions weren't exactly helping the relationships among the team members. But the situation became particularly fraught when it came to the meaning of the word "decision." One German team member explained:

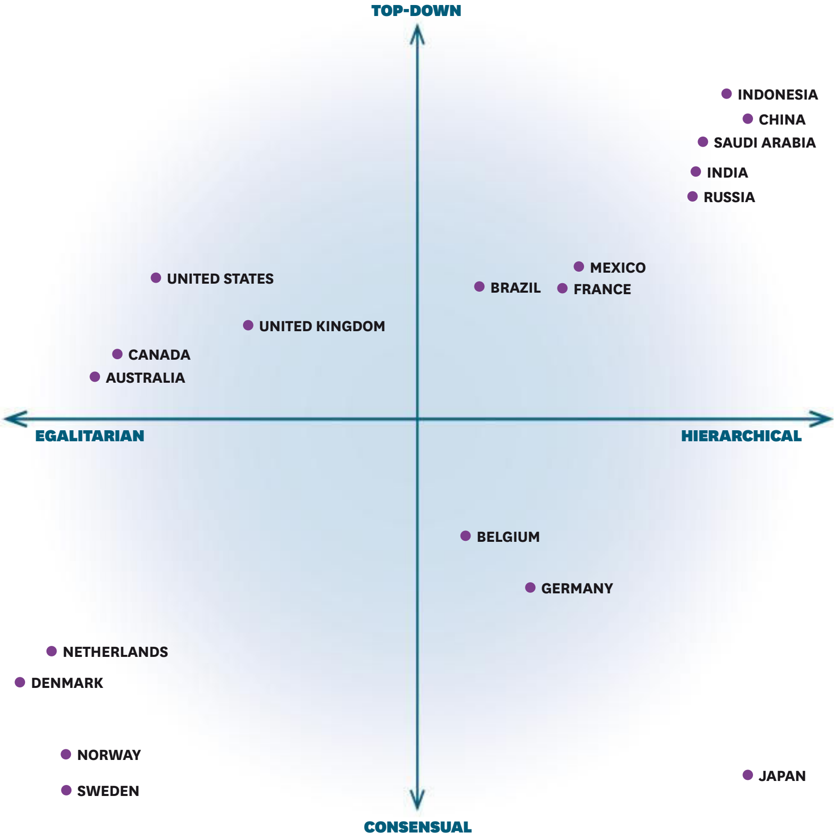
> At the end of a short meeting the boss would announce, "Great! We have a decision." For a German, when you say "We will do this," it is a promise. You can't just change your mind casually tomorrow. So we Germans would spend days working on the implementation. And then one of the Americans would call us up and casually mention that we were taking another direction, or the boss would show us more data suggesting a different path.

For the first several months of collaboration, the Germans could not shake the feeling that their American teammates were disingenuous. One manager spoke to his American boss about the situation, and the conversation was illuminating for both of them. The German commented, "I then understood that for an American, a decision is simply an agreement to continue discussions. And if you are American, you understand that. But for a German, who considers a decision a final commitment to march forward on a plan, this can cause a lot of confusion."

To get the collaboration on track, the two leaders organized an off-site retreat. The team members discussed their assumptions about how decisions should get made and what the word "decision" means in each of their cultures. They developed a system for collectively arriving at decisions and determining how flexible those would be, using the big "D"/small "d" distinction. In subsequent meetings, an American might be heard to say, "Great! Decision made!" only to pause and clarify, "Decision with a small 'd,' that is. We still need to run this by our colleagues at home, so don't start working on it yet." With the cultural difference brought to the surface and acknowledged, the collaboration took off.

MAPPING LEADERSHIP CULTURES

Attitudes toward decision making can range along a continuum from strongly top-down to strongly consensual; attitudes toward authority can vary from extremely egalitarian to extremely hierarchical. The positions for the 19 countries shown on this map were determined from interviews conducted between 2003 and 2016.



THE FOUR CULTURES OF LEADERSHIP

Making a clear distinction between attitudes toward authority (from hierarchical to egalitarian) and attitudes toward decision making (from top-down to consensual) goes a long way in helping leaders become more effective in a global context. It turns out that countries are quite broadly scattered across the two dimensions, as you can see from the exhibit "Mapping Leadership Cultures," which plots the positions of 19 countries within four quadrants. Let's look at the main expectations people have of leaders in each quadrant.

IN A CONSENSUAL, EGALITARIAN CULTURE, DON'T EXPECT THE BOSS TO JUMP IN AND DECIDE FOR THE GROUP.

Consensual and egalitarian

Denmark, Netherlands, Norway, Sweden

Early in my career, I worked as the only non-Dane on an eight-person team. As an egalitarian American, I thought it was great when my boss told me that decisions would be made by consensus. But then the e-mails started. First from him: "Hey, team, for the annual face-to-face in December, I thought we would focus on being more client-centric. What do you think?" Then from a team member: "Hi, Per. Great idea. But wouldn't it be better to focus the meeting on how to market our services more successfully?" And from someone else: "I think it would be most effective to have presentations from all team members about their individual client strategies." And then everyone began sending responses to one another, ending with: "Erin, we haven't heard from you. What do you think?" Consensual decision making sounds like a great idea in principle, but people from fundamentally nonconsensual cultures can find the reality frustratingly time-consuming. If you are to thrive in this quadrant, therefore, you need to go in with the following approach to leadership:

- Expect the decision making to take longer and to involve more meetings and correspondence.
- Do your best to demonstrate patience and commitment throughout the process, even when diverging opinions lead to lengthy ongoing discussions.
- Don't expect the boss to jump in and decide for the group. The boss is a facilitator, not the decider.
- Resist the temptation to push for a quick resolution. Take the time to ensure that the decision you make is the best one possible, because it will be difficult to change later.

Consensual and hierarchical

Belgium, Germany, Japan

A French director of Deutsche Bank once told me: "When I moved to Germany, I was aware that both our cultures are rather hierarchical. So I continued to make decisions as I would have in France, which was

basically—after some good debate—to tell the group what I'd decided, even when I knew many people had opposing opinions about what should be done." When the director received feedback from his first 360-degree review, he was upset by complaints from his German staff that he wasn't inclusive. Eventually he realized that the Germans expected him to invest considerably more time in winning their support before coming to a decision—more than would have been necessary in a French organization. If you likewise are not used to a consensual, hierarchical culture, be aware that in this quadrant:

- If you're the boss, your team will defer to your decision, yet desire and expect to be part of the decision-making process. Make a point of soliciting opinions and input from your staff.
- Be patient and thorough. Invest the time necessary to get each stakeholder on board.
- Once a group decision begins to form, take special care to listen to those with dissenting opinions.
- Focus on the quality and completeness of information gathered and the soundness of the reasoning process. Remember that in this quadrant, decisions are commitments that are not easily altered.

Top-down and hierarchical

Brazil, China, France, India, Indonesia, Mexico, Russia, Saudi Arabia

We've already visited this quadrant in the company of those Americans who moved to China with Chill Factor and perceived their Chinese staff as lacking initiative, while the Chinese viewed the new U.S. managers as incompetent. If you're operating in this quadrant:

- Remember that the boss is the director, not a facilitator.
- If you're the boss, you will be deferred to in public and probably in private too. Don't be shy about telling your team how best to show you respect.
- Be clear about your expectations. If you want your staff to present three ideas to you before asking your opinion, or to give you input before you make a decision, tell them. Old habits die hard for all of us, so reinforce—with clarity and specificity—the behavior you are looking for.
- Be careful what you say. You may find that an off-the-cuff comment is interpreted as a decision—and suddenly everyone is building that factory or reorganizing that department, when you thought you were just introducing an idea to explore.

Top-down and egalitarian

Australia, Canada, United Kingdom, United States

An American director for the World Bank, whom I will call Karen, described a challenge she was having with a Korean employee who had recently joined her team. "When I hired Jae-Sun to work for me in D.C., he had a shining résumé," Karen explained. Promoted time and again to run teams across Asia, he appeared to be an employee who knew how to get things done. Yet Karen noticed right away that if Jae-Sun was with her or another senior manager in a meeting, he seemed reluctant to express his views and instead deferred to them. "I had hoped to groom him for a bigger role in the department, but with this lack of self-confidence, I saw it just wasn't going to happen," Karen told me.

Succeeding in a top-down, egalitarian environment requires behaving as follows:

- Before the decision has been made, speak up—no matter what your status is. You might not be asked explicitly to contribute, but demonstrate initiative and self-confidence by making your voice heard. Politely yet clearly provide your viewpoint even when it diverges from what the boss seems to be thinking.
- Once the matter has been resolved, align quickly with the boss and support the decision even if it conflicts with the opinion you previously expressed. At this stage, if you show disagreement—especially in front of others—you may be viewed as difficult to work with.
- After the decision is made, remain flexible. Decisions in this quadrant are rarely set in stone; most can later be adjusted or revisited if necessary.

ONCE YOU'VE FIGURED out the nuances and complexities of the different approaches, you will make smarter choices in all your cross-cultural interactions as a leader and as a follower. During performance reviews with your Mexican staff, for instance, you might choose to explain your own approach and ask the team to adapt to you. The next week, while leading a meeting with those same employees, you might decide it will be more productive if you adapt to their cultural norms rather than expect them to adapt to yours.

The bottom line? Although you may have been a very successful leader in your own culture, if you hope to motivate and engage people around the globe, you will need a multifaceted approach. Today it's no longer enough to know how to lead the Dutch way or the Mexican way, the American way or the Chinese way. You must be informed enough and flexible enough to choose which style will work best in which cultural context and then deliberately decide how to adapt (or not) to get the results you need.

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DECODING CEO PAY

*THE TRUTH IS BURIED IN THE FINE PRINT—AND THAT'S A PROBLEM.

Each year most public companies issue reports on the pay packages of their top executives, describing how their compensation committees arrived at the numbers. These reports are part of the proxy statements sent to all shareholders, who vote on the packages. The votes are advisory or binding, depending on the country where a company is chartered.

More than 95% of the time, shareholders overwhelmingly approve the pay recommendations. Yet our research suggests that investors should be more skeptical. Compensation committees frequently adjust company performance numbers in complex and even obscure ways, for a variety of reasons. Sometimes, for example, they want to focus on the performance of a company's

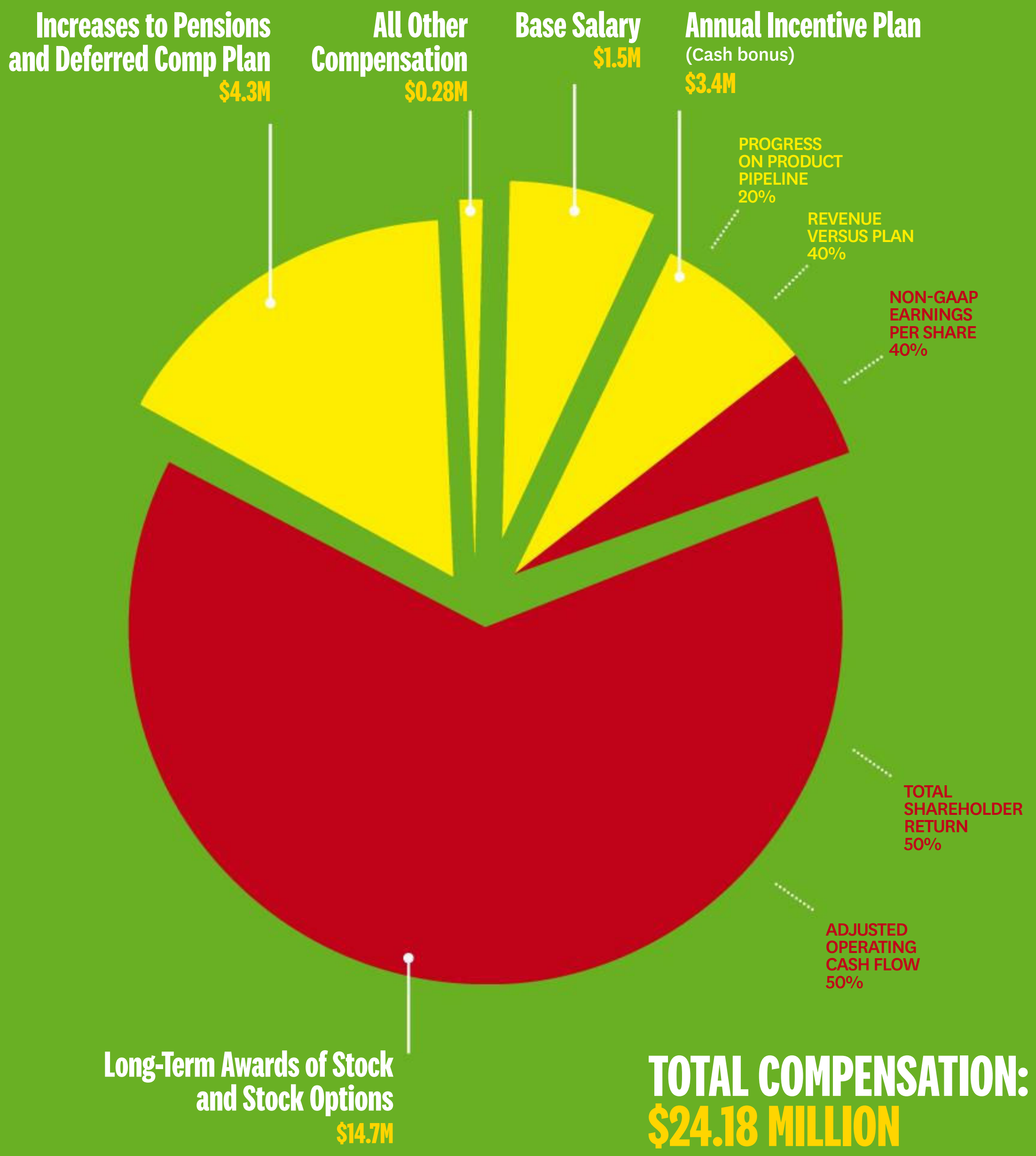
BY ROBERT C. POZEN AND S.P. KOTHARI

core or continuing operations. Whatever the motive, the upshot is all too often inflated numbers, calculated on a nonstandard basis, that rationalize overly generous compensation.

Given that reality, compensation committees need to explain the basis of their decisions more clearly in their reports. For their part, investors need to develop standards and best practices for compensation design and reporting, around which they can build a meaningful dialogue with companies. Such a dialogue is critical today in view of the public's concerns over the rising ratio of CEO pay to the average worker's wages and of shareholders' growing insistence that high pay be justified by superior managerial performance.

ONE CEO'S PAY PACKAGE

Here's how the compensation committee report of one multinational company broke down its CEO's pay package. Much of it was skewed in the CEO's favor: Large portions of the cash bonus and long-term stock awards were based on nonstandard criteria (non-GAAP earnings and adjusted operating income) that are very difficult for investors to evaluate. Furthermore, the part of the long-term awards tied to TSR was overly generous, given that the company performed in the bottom quartile of its peer group.



TOTAL COMPENSATION:
$24.18 MILLION

In the following pages we'll review the common shortcomings of compensation committee reports, especially the use of nonstandard accounting measures and the selection of inappropriate peer companies. We'll also propose ways in which companies and shareholders can improve their approach to determining top management's compensation. Let's begin by looking at an example of the problem.

GENEROUS TO A FAULT

In their reports, most compensation committees identify the criteria used to award both annual cash bonuses and longer-term stock grants—usually the two largest components of executive pay. But even at the most upstanding companies, those criteria are seldom well explained.

Take the 2015 compensation committee report of a well-known *Fortune* 500 company (which you'll find summarized in the exhibit "One CEO's Pay Package"). Running 15 single-spaced pages, it makes a serious effort to delineate the components of the $24 million this CEO received for the year and the criteria behind them. But, like most such reports, it doesn't provide enough information to allow the reader to make an informed judgment on the merits of the pay package without doing a lot of extra work. So we dug a bit deeper:

The cash bonus. The committee tied 40% of this to a revenue target and 20% to a goal for the company's product pipeline. Its report provides clear numbers for the revenue target and specific milestones for the pipeline.

But shareholders would struggle to understand the criterion for the other 40% of the bonus: non-GAAP EPS, or earnings per share calculated on a basis other than generally accepted accounting principles. Companies often use such earnings figures, arguing that GAAP numbers don't provide a fair picture of performance.

Let's examine that a little. The report discloses that the CEO's goal for 2015 was a non-GAAP EPS of $3.40 a share and describes in general terms the categories of GAAP expenses that were excluded in arriving at that number. The committee concluded that the company's non-GAAP EPS for 2015 was $3.59, which was adjusted down to $3.56 to eliminate currency effects. According to those numbers, the CEO exceeded his goal by 16 cents a share.

What the report doesn't make clear is the considerable disparity between the company's GAAP and non-GAAP earnings. Instead, a footnote refers the reader to the company's 10-K report. There the curious reader learns that this difference is approximately $7.5 billion, which constitutes more than 100% of this company's GAAP earnings for 2015. In plain English, the company's earnings under GAAP were $1.56 a share, versus $3.56 under the non-GAAP criterion used by the committee.

Why such a big difference? A review of the 10-K reveals that most of it came from eliminating charges for acquisition and divestiture costs in 2015 and earlier years. While that move may have helped the committee focus on the continuing business, the reader has no good way to evaluate whether the huge costs of these transactions were outweighed by their benefits.

In addition, the non-GAAP earnings exclude a charge of $680 million for settling litigation that began when the current CEO was the company's general counsel. The report, however, makes no attempt to distinguish between litigation charges related to decisions made by the current CEO and those for which he did not have responsibility.

Long-term incentives. The compensation committee based 50% of the CEO's grant of stock and options on "adjusted operating cash flow." This term is not explained in the company's proxy statement for 2015. All we could find is an exhibit in the company's 10-K providing the following definition:

> "Adjusted Operating Cash Flow" means the Company's after-tax non-GAAP income (attributable to the Company) less the change in working capital (working capital includes Trade Accounts Receivables and Inventory—including Trade Accounts Receivables and Inventory included in Other Assets—net of Accounts Payable) plus non-GAAP depreciation and amortization for each calendar year of the Award Period.

We could not find any quantification of adjusted operating cash flow in the proxy statement or the company's 10-K for 2015. So it would be extremely difficult for any shareholder to understand the implications of relying on this complex definition.

The other 50% of the long-term incentive award was tied to total shareholder return over the previous three years. TSR is the increase or decrease in share price plus dividends, and the report compares the company's annualized TSR to that of 11 peers—an appropriate group of large international companies.

This comparison shows that the company's annualized TSR was 10.6%—lower than that of nine of its peers, whose TSRs ranged from 12.4% to 32.2%. Although the report notes that the company's annualized TSR ranked 10th in the peer group of 12, the committee awarded the CEO 80% of his target payout on this measure. The only explanation in the report is a small chart showing that the payout was set by the committee at 80% if the company's TSR came in 10th, 11th, or 12th in the peer group.

Reasonable investors might ask why the CEO should get a large award for such lackluster performance. To give him 80% of his payout for a TSR in the lowest quartile of the firm's peers does not seem to qualify as pay for performance. In our view, if a company's TSR ranks in the lower half of its peer group, its CEO should receive less than half the base payout.

IN BRIEF

THE PROBLEM

More than 95% of the time, a firm's shareholders approve the recommendations of its compensation committee. Yet committees often adjust performance numbers in complex and obscure ways to justify overly generous pay.

HOW IT HAPPENS

Many committees add some costs and charges back into earnings, arguing that they don't affect operating performance. Many also create a misleading picture of performance by using non-GAAP numbers and benchmarking against inappropriate companies. It's not feasible for most shareholders to quantify all the nonstandard criteria used by the committee.

THE SOLUTION

Compensation committees need to explain the basis of their decisions more clearly in their reports. For their part, investors need to develop a set of best practices for compensation design and reporting.

What would have been reasonable compensation for this CEO? To estimate that, we applied the model described by John Core, Wayne Guay, and David Larcker in their 2008 *Journal of Financial Economics* article "The Power of the Pen and Executive Compensation." Although regression-based models typically aren't used by companies and their consultants, the one Core, Guay, and Larcker proposed is the most academically reputable way to calculate appropriate CEO compensation. Its main inputs are the firm's TSR, revenue, and GAAP earnings; the length of the CEO's tenure; and the ratio of the company's book to market value. This model indicates that the CEO should have received total compensation of roughly $12 million—half what he actually got.

MIND THE GAAP

The company used as our example is by no means the only one to make big adjustments to GAAP earnings. In 2015, 36 companies in the S&P 500 announced adjusted earnings that were more than 100% higher than their GAAP income, and another 57 announced adjusted earnings that were 50% to 100% higher.

All told, roughly two-thirds of S&P 500 companies reported adjusted earnings exceeding their GAAP income in 2015. And most compensation committees in firms with substantial differences between GAAP and non-GAAP numbers used the non-GAAP ones to set CEO pay. At those companies adjusted earnings or adjusted operating cash flow determined at least 40% of either annual cash bonuses or long-term stock awards, or both.

To be sure, there are often good reasons for adjusting GAAP figures. But a more nuanced analysis suggests that in many cases, compensation committees are too quick to exclude certain items or make inconsistent exclusions. Let's review the GAAP expense items most commonly involved:

External events. Compensation committees often exclude items related to events beyond management's control, and this is usually a reasonable practice. The best illustration is a shift in currency values. Committees legitimately factor these out so that they can compare this year's income to last year's on a constant currency basis. To be credible, however, a compensation committee should be evenhanded, excluding the upside as well as the downside. For example, many compensation committees at energy companies excluded losses due to the sharp drop in oil prices in 2015. But in earlier years few of them excluded windfall gains from high oil prices.

Extraordinary or nonrecurring expenses. Compensation committees typically exclude onetime losses associated with extraordinary events—such as restructuring costs after acquisitions. But they also omit onetime losses resulting from poor management or executive misbehavior, such as plant closures for safety reasons or legal settlements for alleged misstatements. Indeed, management has considerable discretion in deciding what items will be labeled extraordinary or nonrecurring. An overwhelming majority tend to be losses, and their recurrence is not so infrequent. (For more on that practice, see "Do Stock Prices Fully Reflect the Implications of Special Items for Future Earnings?" by David Burgstahler, James Jiambalvo, and Terry Shevlin, *Journal of Accounting Research,* 2002.)

Taxes and interest. Some committees exclude interest and taxes when calculating non-GAAP earnings. The typical rationale is that these items represent fiscally mandated charges, not operating expenses. But much of the money companies borrow goes into plant and equipment needed to produce goods and services. Moreover, efficient management of financing and taxes is directly relevant to the functions of the CFO and other executives.

Noncash expenses. Compensation committees may also exclude depreciation and amortization on the grounds that they aren't operating expenses. But this argument is thin: Both types of expenses represent the economic wear and tear on plant and equipment involved in generating operating income on an annual basis. Still other compensation committees exclude depreciation and amortization because they're noncash subtractions. Yet both these items represent the actual future investment required for rebuilding or replacing tangible or intangible property.

Stock grants and options. In our view the most problematic exclusions are expenses for grants of restricted shares or stock options. The Financial Accounting Standards Board, after years of extensive discussions, has ruled that these expenses should be included in calculating GAAP net income. So it is questionable for a compensation committee to undermine this accounting rule. The impact of this expense can be considerable.

LinkedIn provides a good illustration of the problem. A company press release projected that the firm would have adjusted earnings of $950 million for calendar year 2015. The accompanying table revealed that under GAAP the company's net income would be minus $240 million. The biggest reason for the difference was the exclusion of $630 million

Thirty-six companies in the S&P 500 announced adjusted earnings that were more than 100% higher than their GAAP income.

in GAAP expenses for stock options and restricted shares awarded to the company's top executives. We fundamentally question whether it's legitimate for compensation committees to use a criterion for CEO compensation that excludes large expenses for awards they themselves have granted to the CEO.

Given the lack of uniform definitions for non-GAAP measures, most shareholders cannot understand the amounts involved in GAAP adjustments simply by reading compensation committee reports. Though the reports typically describe the adjustments in general terms, they usually do not quantify the differences between GAAP and non-GAAP figures. Instead, they refer readers to the company's 10-K—a large and complex filing that is hard to digest.

TSR: RELATIVE TO WHAT?

The *Fortune* 500 company's overly generous treatment of weak performance on relative TSR is not an isolated case. Although CEO compensation is indeed higher for superior-TSR firms and lower for inferior-TSR firms over extended time periods, empirical evidence demonstrates that the difference is skewed: CEOs get large rewards for outperforming a peer group's average but modest penalties for underperformance.

Much of the problem stems from the choice of peers. The typical compensation committee compares the TSR of its own company with the TSRs of its peers over the previous three years as well as the current pay packages for its top executives with those of its peers. To provide a fair comparison, the peer group should consist of companies with similar revenues and market capitalizations and from similar industries. A biased peer group totally undermines its utility in setting compensation.

Unfortunately, the peer groups of many firms are packed with much larger enterprises, in order to provide a high benchmark for compensation comparisons. In 2010 the IRRC Institute found that S&P 500 companies with high CEO pay, relative to that at companies of similar size, were 25% smaller than their self-selected peers by revenue and 45% smaller by market capitalization. A study of the 2015 proxy statements of companies in the Russell 3000 found that they most frequently chose as peers 13 large manufacturers, such as 3M and Honeywell. But most companies in the Russell 3000 are not primarily engaged in manufacturing and are considerably smaller than such huge companies.

One office-supplies company we examined illustrates the point well. It reported revenue of $13 billion for 2015 and a market capitalization of $2.6 billion at the end of that year. But the 20 companies in the peer group the compensation committee chose all had higher market capitalizations, and eight of the 20 had market caps above $10 billion. Thirteen had higher revenues. Moreover, several of the larger companies in the group were outside the business of office supplies.

To mitigate bias in the composition of peer groups, we urge every compensation committee to choose comparison companies before the start of the period for measuring TSR rather than at the end, as now often happens. Before the start date, the committee would not know the TSR or CEO pay of any peers. In addition, the SEC should require the committee report to disclose the market capitalizations, revenues, and industry codes of all companies in the peer group.

To be fair, the SEC has made efforts to highlight the relationship between CEO compensation and TSR: In 2015 it proposed that the compensation committee report include a graph mapping the company's TSR

* * * * *

GUIDELINES FOR NON-GAAP ADJUSTMENTS

We suggest that investors create an association that asks compensation committees to comply with the following guidelines:

Committees should generally use GAAP measures of financial performance in determining both long-term and short-term compensation.

Departures from GAAP may be permitted to exclude the consequences of events beyond the control of management, provided the exclusion applies to both positive and negative changes.

Committees may also exclude GAAP expenses for onetime events such as restructuring charges, provided such charges do not recur each year.

Committees should not exclude expenses for stock-related awards to executives.

All exclusions of GAAP expenses should be justified and quantified in the compensation committee's report.

* * * * *

> **Even institutional shareholders with proxy advisers don't have the data or expertise to make meaningful assessments of executive pay proposals.**

over the prior five years against the compensation of its CEO in each of those years. Such a graph would be helpful because it would extend the typical measurement period from three to five years, but it would still highlight only the performance of the company. So we think the report should also include a table listing, from highest to lowest, the annualized TSR of the company and its peers over the five years. That move would help the committee and shareholders align the CEO's stock awards more closely with the firm's relative TSR.

CREATING A CONSTRUCTIVE DIALOGUE

Although large asset managers typically have a unit responsible for recommending proxy votes, it's usually small and hard-pressed to review the more than 1,000 proxies it might be sent during proxy season. Staffers in such units readily admit they lack the time and expertise to conduct in-depth analyses of complex issues like non-GAAP criteria and peer group composition. That's why most asset managers subscribe to proxy advisory services, such as Institutional Shareholder Services (ISS) and Glass Lewis (GL).

But shareholders should not automatically follow the recommendations of proxy advisers on compensation votes. Take GL, which screens compensation reports against a company's GAAP financial statements. While GL does in a few cases express concerns about adjustments that it believes are not well justified and that result in much higher payouts, it did not do so with the compensation report of the *Fortune* 500 company analyzed earlier.

ISS employs relative TSR as its primary screen for compensation reports, using its own methodology for creating peer groups. If this screen reveals serious concerns, ISS will assign a staffer to do an in-depth analysis of the report. However, according to ISS, its screen did not raise any major questions about the report of the company in our example, although the company's relative TSR was in the lowest quartile of its self-selected peer group.

The bottom line is that even institutional shareholders with subscriptions to proxy advisers don't have access to the data or the expertise to make a meaningful assessment of the executive pay packages that companies propose. It is incumbent, therefore, on compensation committees, which do have access, to do a better job of explaining their rationales. As we have suggested, more-transparent reporting of GAAP adjustments, preselection of a TSR peer group, and less tolerance for relatively poor TSR performance would be major advances.

But even if compensation committees do take steps to improve their reports, institutional investors still need to set standards and monitor compliance. Instead of relying on proxy advisers, investors should take matters into their own hands. The best way to do so would be to support a U.S. association dedicated to creating long-term corporate value through shareholder engagement on compensation resolutions. It could be formed under the umbrella of an existing association, such as FCLT (Focusing Capital on the Long Term) Global.

The new association could develop and promote a nonbinding set of best practices for compensation committees, which could include very basic guidelines about the use of non-GAAP criteria. (See the sidebar "Guidelines for Non-GAAP Adjustments.") The committee at each company would either apply these practices or explain its reason for departing from them. This approach would resemble the model successfully adopted in the UK, where regulators frequently impose rules—such as limits on the tenure of independent directors—but allow a company to deviate from them if it explains why to shareholders.

To further promote engagement, each company should hold a public conference call, a few weeks before its annual meeting, in which compensation committee members explain major variations from the association's best practices and respond to shareholders' questions. Pre-vote discussions with large shareholders have prompted companies to revise compensation plans and head off adverse votes on resolutions in the past. (One company we looked at dropped a plan to pay certain taxes for its CEO after such a call.)

As more countries mandate shareholder votes on executive pay, compensation committee reports could play an important role in enhancing the relationship between company boards and shareholders. Properly designed and prepared, these reports could help educate shareholders about the objectives of companies and the ways they measure success. More broadly, clear, unambiguous explanations of how the various components of pay are linked to reasonable metrics of company performance would help the business community respond more effectively to growing public concerns about excessive CEO compensation.

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WHAT'S YOUR BEST INNOVATION BET?

BY MAPPING A TECHNOLOGY'S PAST, YOU CAN PREDICT WHAT FUTURE CUSTOMERS WILL WANT.

BY MELISSA SCHILLING

OLEKSANDR KOSTIUCHENKO/SHUTTERSTOCK

When companies develop new technologies, they can never be certain how the market will respond. That said, the future of a given technology is not as unforeseeable as it might seem. When I work with tech companies on crafting or refining their innovation strategy, I start with an exercise that helps them anticipate where

the next big breakthroughs will—or should—be. Central to the exercise is an examination of the key dimensions on which a technology has evolved—say, processing speed in computing—and the degree to which users' needs have been satisfied. This can give companies insight into where to focus their effort and money while helping them anticipate both the moves of competitors and threats from outsiders.

One of my favorite examples comes from the consumer electronics and recording industries, which competed on the basis of audio fidelity for decades. By the mid-1990s, both industries were eager to introduce a next-generation audio format. In 1996 Toshiba, Hitachi, Time Warner, and others formed a consortium to back a new technology, called DVD-Audio, that offered superior fidelity and surround sound. They hoped to do an end run around Sony and Philips, which owned the compact disc standard and extracted a licensing fee for every CD and player sold.

Sony and Philips, however, were not going to go down without a fight. They counterattacked with a new format they had jointly developed, Super Audio CD. Those in the music industry gave a collective groan; manufacturers, distributors, and consumers all stood to lose big if they bet on the wrong format. Nonetheless, Sony launched the first Super Audio players in late 1999; DVD-Audio players hit the market in mid-2000. A costly format war seemed inevitable.

You may be scratching your head at this point, wondering why you've never heard about this format war. What happened? MP3 happened. While the consumer electronics giants were pursuing new heights in audio fidelity, an algorithm that slightly *depressed* fidelity in exchange for reduced audio file size was taking off. Soon after the file-sharing platform Napster launched in 1999, consumers were downloading free music files by the millions, and Napster-like services were sprouting up like weeds.

You might be inclined to think that Sony, Philips, and the DVD-Audio consortium were just unlucky. After all, who could have predicted the disruptive arrival of MP3? How could the consumer electronics giants have known that a format on a trajectory of ever-increasing fidelity would be overtaken by a technology with *less* fidelity? Actually, with the methodology outlined below, they *could* have foreseen that the next breakthrough would probably not be about better fidelity.

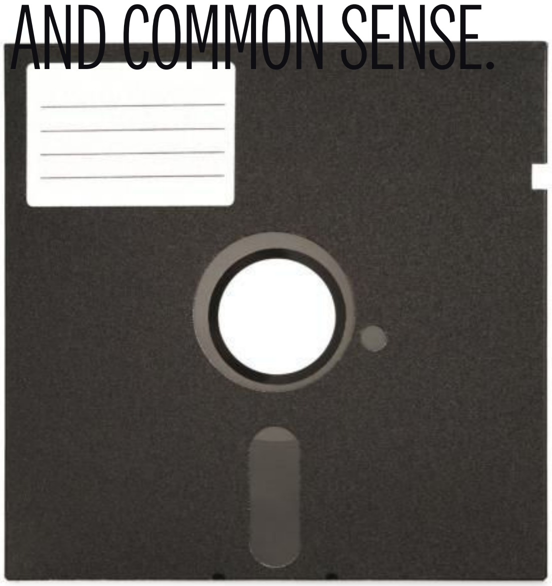
Understanding what's driving technological developments isn't just for high-tech firms. Technology—the way inputs are transformed into outputs, or the way products and services are delivered to customers—evolves in every market. I have used the three-step exercise described here with managers from a wide range of organizations, including companies developing blood-sugar monitors, grocery store chains, hospitals, a paint-thinner manufacturer, and financial services firms. It often yields an "Aha!" moment that helps managers refine or even redirect their innovation strategy.

STEP ONE: IDENTIFY KEY DIMENSIONS

It's common to talk about a "technology trajectory," as if innovation advances along a single path. But technologies typically progress along several dimensions at once. For example, computers became faster and smaller in tandem; speed was one dimension, size another. Developments in any dimension come with specific costs and benefits and have measurable and changing utility for customers. Identifying the key dimensions of a technology's progression is the first step in predicting its future.

To determine these dimensions, trace the technology's evolution to date, starting as far back as possible. Consider what need the technology originally fulfilled, and then for each major change in its form and function, think about what fundamental elements were affected.

SELECTING USEFUL TECHNOLOGY DIMENSIONS TO EXAMINE DEPENDS ON INDUSTRY KNOWLEDGE AND COMMON SENSE.



CHICTYPE/GETTY IMAGES

IN BRIEF

THE CHALLENGE
Successful technology innovation requires firms to make good predictions about product and service capabilities that consumers will value in the future. Getting this wrong can be costly.

THE SOLUTION
By studying how a technology has evolved along key dimensions, and understanding the degree to which consumers' needs have been satisfied on those dimensions, it's possible to determine where best to invest in further technology development.

THE PROOF
Applying this approach, teams across industries have conceived of promising new products that are now in development or launched, including a financial data mobile app and a noninvasive glucose-monitoring technology.

To illustrate, let's return to music-recording technology. Tracing its history reveals six dimensions that have been central to its development: desynchronization, cost, fidelity, music selection, portability, and customizability. Before the invention of the phonograph, people could hear music or a speech only when and where it was performed. When Thomas Edison and Alexander Graham Bell began working on their phonographs in the late 1800s, their primary objective was to *desynchronize* the time and place of a performance so that it could be heard anytime, anywhere. Edison's device—a rotating cylinder covered in foil—was a remarkable achievement, but it was cumbersome, and making copies was difficult. Bell's wax-covered cardboard cylinders, followed by Emile Berliner's flat, disc-shaped records and, later, the development of magnetic tape, made it significantly easier to mass-produce recordings, lowering their *cost* while increasing the *fidelity* and *selection* of music available.

For decades, however, players were bulky and not particularly portable. It was not until the 1960s that eight-track tape cartridges dramatically increased the *portability* of recorded music, as players became common in automobiles. Cassette tapes rose to dominance in the 1970s, further enhancing portability but also offering, for the first time, *customizability*—the ability to create personalized playlists. Then, in 1982, Sony and Philips introduced the compact disc standard, which offered greater fidelity than cassette tapes and rapidly became the dominant format.

When I guide executive teams through step one of the exercise, I emphasize the need to zero in on the *high-level* dimensions along which a technology has evolved—those that are broad enough to encompass other, narrower dimensions. This helps teams see the big picture and avoid getting sidetracked by its details. In audio technology, for example, *recordability* is a specific form of customizability; identifying customizability, rather than the narrower recordability, as a high-level dimension invites exploration of other ways people might want to customize their music experience. For example, they might value a technology that automatically generates a playlist of songs with common characteristics—and indeed, services like Pandora and Spotify emerged to do just that.

It's important to identify dimensions at the optimal "altitude"—neither so low or narrow that they miss the big picture, nor so high or broad that they won't offer adequately detailed insight about a specific technology. In the case of automobiles, for example, climate control may be a technology dimension, but it's so narrow that it's not the most useful one to study; examining the higher-level "comfort" dimension under which it falls will be more illuminating. By the same token, the sweeping "performance" dimension in automobiles is probably too broad a choice, because it includes speed, safety, fuel efficiency, and other dimensions where meaningful advances could be made. Even a product as simple as a mattress involves technology with multiple performance dimensions—such as comfort and durability—that are useful to consider separately.

Selecting dimensions to examine isn't a strict science; it depends substantially on knowledge of your industry—and common sense. I usually ask teams to agree on three to six key dimensions for their technology. The exhibit "A Sampling of High-Level Technology Dimensions" lists those identified by workshop participants for their respective industries. Notably, some dimensions, such as ease of use and durability, come up frequently. Others are more specific to a particular technology, such as magnification in microscopes. And with rare exceptions, cost is an important dimension across all technologies.

A final step in this part of the exercise can add further insight about the identified dimensions and in some cases suggest future dimensions worth exploring. I ask team members to disregard cost and other constraints and imagine what customers would want if they could have *anything.* This sounds like it might unleash a flood of creative but impractical ideas. In fact, it can be highly revealing. Folklore has it that Henry Ford once said, "If I had asked people what they wanted, they would have said faster horses." If any carmaker at the time had really probed people about exactly what their dream conveyance would provide, they probably would have said "instantaneous transportation." Both consumer responses highlight that speed is a high-level dimension valued in transportation, but the latter helps us think more broadly about how it can be achieved. There are only limited ways to make horses go faster—but there are many ways to speed up transportation.

Most of the time this exercise indicates that people want further improvements in the key dimensions already identified. Sometimes, however, the exercise suggests dimensions that have not been considered. Would consumers want an audio device that could sense and respond to their affect? If so, perhaps "anticipation of needs" is another key dimension.

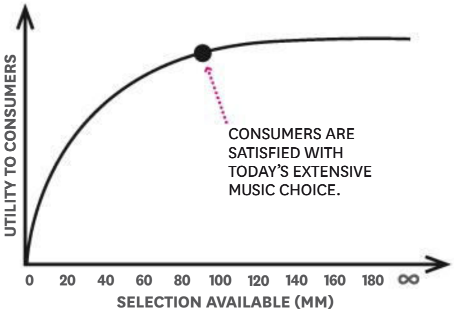
A SAMPLING OF HIGH-LEVEL TECHNOLOGY DIMENSIONS

Industry professionals can generally agree on three to six dimensions that significantly drive development of their technology.

TECHNOLOGY	DIMENSIONS
AUDIO	Desynchronization, fidelity, music selection, portability, customizability, cost
LIGHTING	Durability, brightness, comfort, design selection, cost
MICROSCOPES	Magnification, ease of use, versatility, cost
PAINKILLERS	Strength, reliability, safety, convenience, cost
TRANSPORT	Speed, comfort, safety, reliability, ease of use, fuel efficiency, cost

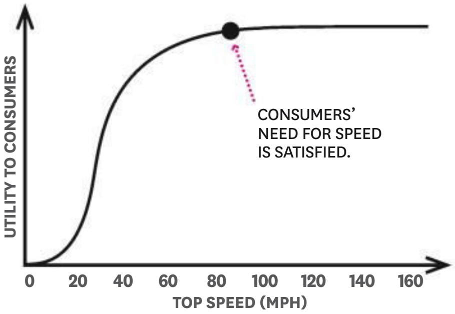
MORE MUSIC, MORE VALUE—UP TO A POINT

For some technologies, small improvements can have a big impact at first. In the early days of recorded music, listeners had few pieces to choose from, so the utility of increasing the selection even a small amount was high. Today consumers have virtually unlimited choices, so the additional utility of increasing selection is low.



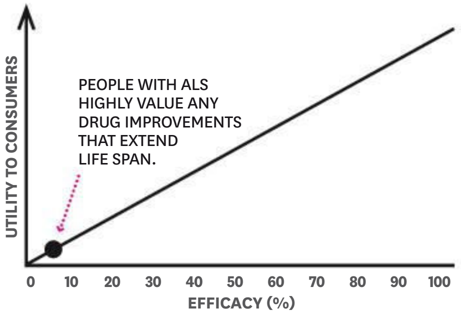
THE CAR-SPEED SWEET SPOT

Some technology improvements have little appeal early on and then quickly grow in value before their utility levels off. The first cars were too slow to be very useful. As they became faster and roads improved, consumers valued ever-greater top speeds—up to about 90 miles per hour. Beyond that, extra speed makes no difference to most drivers.



HIGH DEMAND FOR DRUGS THAT WORK

For some technologies, consumers prize even modest advances. Only one of the approved treatments for the neurodegenerative disease ALS extends life span—and only by a few months. Patient demand for effective drugs won't be satisfied until efficacy is 100%, but any improvement up to that point has high utility.



STEP TWO: LOCATE YOUR POSITION

For each dimension, you next want to determine the shape of its utility curve—the plot of the value consumers derive from a technology according to its performance—and establish where on the curve the technology currently sits. This will help reveal where the greatest opportunity for improvement lies.

For example, the history of audio formats suggests that the selection of music available has a concave parabolic utility curve: Utility increases as selection expands, but at a decreasing rate, and not indefinitely (see the exhibit "More Music, More Value—Up to a Point"). When there's little music to choose from, even a small increase in selection significantly enhances utility. Consider that when the first phonographs appeared, there were few recordings to play on them. As more became available, customers eagerly bought them, and the appeal of owning a player grew. Increasing selection even a little had a powerful impact on utility. Over the ensuing decades, selection grew exponentially, and the utility curve ultimately began to flatten; people still valued new releases, but each new recording added less additional value. Today digital music services like iTunes, Amazon Prime Music, and Spotify offer tens of millions of songs. With this virtually unlimited selection, most customers' appetites are sated—and we are probably approaching the top of the curve.

Now let's consider the fidelity dimension, the primary focus of Super Audio CD and DVD-Audio. It's likely that fidelity also has a concave parabolic utility curve. The first phonographs had awful fidelity: Music sounded thin and tinny, though it was still a remarkable benefit to be able to hear any recorded music at all. The early improvements in fidelity that records offered made a big difference in people's enjoyment of music, and sales took off. Then along came compact discs. The higher fidelity they offered was not as widely appreciated—many people felt that vinyl records were good enough, and some even preferred their "warmth." For most consumers, further improvements in fidelity provided little additional utility. The fidelity curve was already leveling out when Sony, Philips, and the DVD-Audio consortium introduced their new formats in the early 2000s.

Both formats offered higher fidelity, by certain technical measures, than the compact disc. For example, whereas CDs have a frequency range up to about 20,000 cycles per second, or 20 kHz, the new formats offered ranges that reached 50 kHz. That's an impressive high end—but because human hearing peaks out at about 20 kHz, only the family dog was likely to appreciate it. In 2007 the Audio Engineering Society released the results of a yearlong trial assessing how well subjects (including professional recording engineers) could detect the difference between Super Audio and regular CDs. Subjects correctly identified the Super Audio CD format only half the time—no better than if they'd been simply guessing.

Had the companies introducing the new formats created even a back-of-the-envelope utility curve for fidelity, they could have seen that there was little room for improvement that customers would appreciate. Meanwhile, even a cursory look at the portability curve would have suggested opportunity on that dimension. Sony, of all companies, should have recognized the importance of portability in the evolution of audio formats. Back in 1979, the company had introduced one of the most successful consumer electronics products ever created—the Sony Walkman. The device, a lightweight cassette player that could fit in one hand, was a runaway hit not because it cost less or offered greater fidelity or selection than other formats but because it was *portable.* Similarly, MP3 was successful because it made music *much more* portable; MP3 files were small enough to be easily stored on a computer and shared with friends.

Fast-forward to today. Although music lovers now take portability and selection for granted, there's still lots of room for improvement on the customizability dimension. Pandora offers primitive customizability (you can create a channel where all the songs sound more or less like Taylor Swift), but artificial intelligence may get us much further up that utility curve in the future. It's plausible (likely, in fact) that a program could identify elements of your preferred music style and then create music for you. Perhaps it would produce an endless stream of "Beatles songs," nearly indistinguishable from the real thing but not written or played by the Beatles (or by any human performer). Machine-learning programs already compose music for advertisements and video games, and in 2016 Sony released two songs composed by an artificial intelligence system called Flow Machines. The first, "Daddy's Car," is reminiscent of the Beatles, and the second, "Mr Shadow," emulates the styles of Duke Ellington, Irving Berlin, and Cole Porter. While neither quite hits the mark, both suggest what's to come—and where music companies might sensibly invest.

Parabolic utility curves like those for audio fidelity and selection show that for some technology performance dimensions, small improvements can have a dramatic impact on utility from the start. Of course, not all technologies follow such utility curves. Many dimensions have S-shaped curves: Below some threshold of performance there is no utility, but utility increases quickly above that threshold and then maxes out somewhere beyond that. Consider the utility of a car's speed for an average customer (see the exhibit "The Car-Speed Sweet Spot"). The first motor vehicles, such as Richard Trevithick's 1801 Puffing Devil, were steam-powered. They offered a proof of concept and were sometimes purchased by wealthy technophiles, but they were too slow and unreliable to be worth the cost to the average family. Horses traveled farther and faster and rarely broke down.

For the next hundred years, inventors sought to develop an automobile that was more useful than a horse-drawn wagon. During this time, the utility curve for speed remained flat; increasing a car's top speed by a few miles an hour offered no additional utility if the car was still slower than a horse—particularly if it was also less reliable, as was typically the case. It wasn't until the early 20th century, when passenger automobiles started to routinely offer speeds over 15 miles per hour, that they began to be adopted in serious numbers. By the 1990s most passenger cars had a top speed of about 120 mph, and today for many it's near 150 mph. It's uncommon, however, for drivers to exceed 90 mph; for most drivers, the utility curve for speed flattens out at that point. Improvements in other dimensions, such as fuel efficiency, acceleration, safety, and reliability, offer more utility to most customers.

The utility curve for speed reveals that the point at which improvements in a dimension are of little value can change with shifts in the environment or in enabling technologies. Forty miles per hour probably seemed more than fast enough, for example, when the Model T was introduced, since most roads at the time weren't paved. As roads improved and highways appeared, the top speeds desired by customers shifted upward. The move to autonomous vehicles may make even higher speeds safe, comfortable, and desirable. If so, the flat top of the current utility curve for speed may slope upward once again.

ONLY THE FAMILY DOG WAS LIKELY TO APPRECIATE THE MOST HIGH-END IMPROVEMENTS IN AUDIO FIDELITY.

PM IMAGES/GETTY IMAGES

FROM EXERCISE TO INNOVATION

By examining the evolution of key technology dimensions, teams across industries have conceived and launched an array of promising new products.

TECHNOLOGY AREA	KEY TECHNOLOGY DIMENSIONS	RESULTING PRODUCT CONCEPT (DIMENSION SELECTED FOR DEVELOPMENT)	STATUS
GLUCOSE MONITORING	Reliability, comfort, ease of use, cost	Noninvasive glucose-monitoring skin patch streams data to mobile device. (COMFORT, EASE OF USE)	In development by industry and university teams
SPORTS TELEVISION	Selection, social interactivity, immersiveness, cost	Virtual reality platform allows separated viewers to watch games in a shared virtual space. (SOCIAL INTERACTIVITY, IMMERSIVENESS)	2017 launch expected
FINANCIAL DATA	Speed, accuracy, breadth, usability, portability, cost	Mobile app provides instant access to proprietary high-value content and analytics. (USABILITY, PORTABILITY)	App released in 2013 is now among the top three in financial services
ACADEMIC PUBLISHING	Reach, access, impact, searchability, cost	Online portal enhances research discoverability and collaboration. (IMPACT, SEARCHABILITY)	Launched in early 2017

STEP THREE: DETERMINE YOUR FOCUS

Once you know the dimensions along which your firm's technology has (or can be) improved and where you are on the utility curves for those dimensions, it should be straightforward to identify where the most room for improvement exists. But it's not enough to know that performance on a given dimension *can* be enhanced; you need to decide whether it *should* be. So first assess which of the dimensions you've identified are most important to customers. Then assess the cost and difficulty of addressing each dimension.

For example, of the four dimensions that have been central to automobile development—speed, cost, comfort, and safety—which do customers value most, and which are easiest or most cost-effective to address? On the speed dimension, cars are already at the top of the utility curve, and top speed is relatively difficult and expensive to increase: Higher speed requires more power, which requires a bigger engine, which reduces fuel efficiency and increases cost. Comfort is probably the easiest dimension to address, but is it as important to consumers as safety? And how much does it cost to improve performance on these dimensions?

Tata Motors' experience with the Nano is instructive. The Nano was designed as an affordable car for drivers in India, so it needed to be cheap enough to compete with two-wheeled scooters. The manufacturer cut costs in several ways: The Nano had only a two-cylinder engine and few amenities—no radio, electric windows or locks, antilock brakes, power steering, or airbags. Its seats had a simple three-position recline, the windshield had a single wiper, and there was only one rearview mirror. In 2014, after the Nano received zero stars for safety in crash tests, analysts pointed out that adding airbags and making simple adjustments to the frame could significantly improve the car's safety for less than $100 per vehicle. Tata took this under advisement—and placed its bets on comfort. All 2017 models include air-conditioning and power steering but not airbags.

To assess which technology investments are likely to yield the biggest bang for the buck, managers can use a matrix like the one in the exhibit "How to Improve Glucose Monitoring?" First, for the technology being examined, list the performance dimensions you've identified as most important. (For cars, for example, that might be cost, safety, and comfort.) Then score each dimension on a scale of 1 to 5 in three areas:

- *Importance to customers* (1 = "not important" and 5 = "very important")
- *Room for improvement* (1 = "minor opportunity" and 5 = "major opportunity")
- *Ease of improvement* (1 = "very difficult" and 5 = "very easy")

The exhibit shows a manufacturer's scores on four dimensions of blood-glucose monitors: reliability, comfort, cost, and ease of use. The team identified reliability as most important to customers; having accurate glucose measures can be a matter of life and death. However, existing devices (most of which require a finger prick) are already very reliable and thus scored low on the "room for improvement" measure. They are also fairly easy to use and reasonably low in cost—but they are uncomfortable. Comfort is highly valued yet has much room for improvement. Both comfort and ease of use are moderately difficult to improve (scoring 3s), but because comfort is more important to customers and has more room for improvement, this dimension received the higher total score. So comfort became the focus for innovation efforts; the company began to develop a patch worn on the skin that would detect glucose levels from sweat and would send readings via Bluetooth to the user's smartphone.

Notably, with a simple manipulation, the weight of the matrix scores can be adjusted to reflect any organization's particular situation. For example, if a company is cash-strapped or under other duress, it may want to prioritize easy-to-improve dimensions rather than pursue those that have the greatest potential but are harder to address. If the scale for ease of improvement is switched to 1–10 (while the other scales are kept at 1–5), ease-of-improvement scores can be expected to roughly double and thus have a greater influence on total scores. Alternatively, a company seeking breakthrough innovation might extend the scale for importance to buyers, the scale for room for improvement, or both.

HOW TO IMPROVE GLUCOSE MONITORING?

To prioritize their innovation efforts, the makers of a blood-sugar-monitoring device listed the technology dimensions they knew customers cared about most and scored each one according to how important it was, how much improvement was possible, and how easily improvements could be made. The high total score for comfort led the company to develop a noninvasive device.

DIMENSION	IMPORTANCE TO CUSTOMERS (1–5 SCALE)	ROOM FOR IMPROVEMENT (1–5 SCALE)	EASE OF IMPROVEMENT (1–5 SCALE)	TOTAL SCORE
RELIABILITY	5	1	1	7
COMFORT	4	4	3	11
COST	4	2	2	8
EASE OF USE	3	2	3	8

GETTING AN EDGE ON COMPETITORS

The technology assessment exercise can help companies anticipate competitors' moves. Because competitors may differ in their capabilities (making particular technology dimensions harder or easier for them to address), or because they may focus on different segments (influencing which dimensions seem most important or have the most room for improvement), they are likely to come up with different rankings for a given set of dimensions.

For example, managers at a financial technology company realized that for some of their product offerings, Google could be considered a potential competitor. The company had identified speed, accuracy, breadth, usability, and portability as key financial-data dimensions. By considering how Google might rank those dimensions—probably giving greatest weight to speed and breadth (areas where it had particular strength)—the firm determined that Google would be likely to continue directing its focus there. The firm also realized that usability was an important differentiator and a dimension where it had a significant advantage over potential competitors. Whereas Google and others could provide large amounts of searchable, nonproprietary data, the financial technology company was better positioned to provide proprietary algorithms that would transform data into meaningful metrics and graphs. With this understanding, the managers decided to emphasize proprietary analytics in their mobile offering, rather than data feeds alone.

Similarly, a company's competitive positioning may affect which technology dimensions it emphasizes. For example, safety may be a key differentiator for an automaker such as Volvo, while speed (or, more broadly, driving performance) may be the differentiator for BMW. So although the companies make the same technology (cars), they market to different customer segments and thus emphasize different dimensions. (For more on competitive analysis, see the sidebar "Getting an Edge on Competitors.")

SHIFTING THE FOCUS

The three-part exercise I recommend can help managers broaden their perspective on their industry and shift their focus from "This is what we do" to "This is where our market is (or should be) heading." It can also help overcome the bias and inertia that tend to keep an organization's attention locked on technology dimensions that are less important to consumers than they once were. For example, at a large financial services firm I worked with, data-transfer speed had long been a key dimension where the leadership expected to see regular improvements. At its founding, the firm had developed technology to deliver financial data more rapidly than anyone else could. Being faster than competitors was, and remained, central to the company's strategy and a matter of organizational pride. However, when I used this exercise with the firm's managers, they realized that concentrating on data-transfer speed (which was now in the nanoseconds) was diverting their attention away from technology dimensions where there was greater opportunity to make improvements that customers would actually value.

For this firm, data-transfer speed had become what fidelity was to Super Audio CD: It could be improved upon year after year, but it offered diminishing utility to users. Furthermore, speed no longer provided a competitive advantage; technology to move data quickly had become ubiquitous and commoditized. The firm's proprietary algorithms for transforming raw data into strategically useful information were far more defensible. The exercise revealed much greater opportunity for delivering this information on demand. Following the workshop, a group of managers made plans to shift resources into ensuring that their most highly used and differentiated analytics-based products could be effectively delivered on phones and tablets. The result was an award-winning mobile application that is now among the top three financial-services applications worldwide.

NEW PRODUCT IDEAS are not the only—or even the most important—outcome of this exercise. Perhaps more valuable is the big-picture perspective it can give managers—shedding new light on market dynamics and the larger-scale or longer-term opportunities before them. Only then will they be able to lead innovation in their industries rather than scramble to respond to it.

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ILLUSTRATION BY ARTUR HILGER

FINDING THE PLATFORM IN YOUR PRODUCT

FOUR STRATEGIES THAT CAN REVEAL HIDDEN VALUE

BY ANDREI HAGIU AND ELIZABETH J. ALTMAN

Five of the 10 most valuable companies in the world today—Apple, Alphabet, Amazon, Facebook, and Microsoft—derive much of their worth from their multisided platforms (MSPs), which facilitate interactions or transactions between parties. Many MSPs are more valuable than companies in the same industries that provide only products or services: For instance, Airbnb is now worth more than Marriott, the world's largest hotel chain.

However, companies that weren't born as platform businesses rarely realize that they can—at least partially—turn their products and services into an MSP. And even if they do realize it, they often wander in the dark searching for a strategy to achieve this transformation. Here we provide a framework for doing so. It lays out four specific ways in which products and services can be turned into platforms and examines the strategic advantages and pitfalls of each. These ideas are applicable to physical as well as online businesses.

Why seek to transform products and services into MSPs in the first place? As one Intuit executive told us, it comes down to "fear and greed." Greed, of course, refers to the potential for new revenue sources that could speed growth and increase a company's value. Fear refers to the danger that existing and incoming competitors will steal market share from your product or service. Transforming an offering into a platform might enhance your company's competitive advantage and raise barriers to entry via network effects and higher switching costs. We're not suggesting that every company should try to emulate Airbnb, Alibaba, Facebook, or Uber. But many companies would benefit from adding elements of a platform business to their offerings.

Our goal is to help managers discern how their products or services could become multisided platforms—and what challenges and opportunities might arise—so that they can decide whether or not to make the change. Our framework derives from our combined experience studying and advising more than a dozen companies (including several mentioned below) during product-to-MSP transformations. Managers might want to use this article as the basis for a corporate-strategy offsite at which everyone is given the task of articulating MSP strategies around existing company offerings. That assignment should include answering questions such as: (1) Are there benefits to turning some or all of our products and services into MSPs? (2) Are there risks involved in doing so? (3) What key resources, relationships (including how we interact with customers), and organizational changes would be required for such a transformation?

The reason regular products and services are not multisided platforms is that they do not serve multiple groups or facilitate interactions between customers or groups. In this article we discuss four ways in which regular products and services can bridge this gap and become MSPs.

IN BRIEF

THE PROBLEM
Many companies that sell products or services either don't realize they could turn their offerings into a platform business or struggle to do so.

THE OPPORTUNITY
By becoming a multisided platform (MSP) that facilitates interactions between parties, a company may be able to provide new revenue sources while also preventing competitors from stealing market share from its product or service.

THE SOLUTION
Here are four scenarios whereby regular products or services can become MSPs. The authors take into account the advantages and pitfalls of each and the resources, relationships, and organizational changes that would be required.

1.

OPENING THE DOOR TO THIRD PARTIES

In this scenario your product or service has a big customer base that third-party sellers of other offerings are interested in reaching. You become an MSP by making it possible for those third parties to connect with your customers. "Connect with" can mean advertise or sell (or both) to them. The third-party products may be independent of your product or service or may be apps or modules that work in combination with your offerings.

Consider three examples:

INTUIT IS THE leading seller of financial management, accounting, and tax software products for consumers and small businesses in the United States. In the past six years or so it has taken significant steps to turn QuickBooks, its flagship financial-accounting product for small businesses, into an MSP. It opened up application-programming interfaces and introduced a developer program and an app store to allow third-party developers to build and sell software products to QuickBooks' customer base. Those products leverage data about small-business finances provided by QuickBooks. Since 2013 QuickBooks has also enabled its customers to apply directly to several third-party financial institutions for loans through a service called QuickBooks Financing.

HEALTH CLUBS ARE increasingly renting space inside their gyms to specialty studios so that the latter can serve health club members. This allows a club to offer a greater variety of classes, which helps it retain existing members and attract new ones. For instance, the Forum Athletic Club, in Atlanta, recently reached an agreement with Cyc Fitness, a national cycling-studio chain, which now operates a self-contained studio inside the Forum's 22,000-square-foot gym.

THE LAWSON CHAIN of convenience stores in Japan started in the 1990s to turn its shops into MSPs that facilitate transactions between its customers and third-party service providers. Today Lawson customers can pay utility bills and insurance premiums, ship and pick up parcels through postal service providers, and claim items ordered from e-commerce sites just by visiting their local convenience store.

For your product or service to become a true MSP in this scenario, at least some of the connection between your customers and third parties must be made through your product. Intuit could simply have sold aggregated (and anonymized) QuickBooks data to third-party developers and financial institutions. That would have added a potentially profitable new offering for Intuit, but it would not have turned QuickBooks into an MSP that could exploit network effects.

For this type of transition to make sense, your product or service must have an established brand and a large customer base—but that alone won't elicit interest from third parties. It must also meet one or both of the following conditions:

TODAY LAWSON CUSTOMERS CAN PAY UTILITY BILLS AND INSURANCE PREMIUMS JUST BY VISITING THEIR LOCAL CONVENIENCE STORE.

It serves a baseline need for many customers, yet leaves a large number of heterogeneous customer needs unserved. You can encourage and enable third parties to fill those gaps with products and services that are typically complementary to yours. Most third-party apps in Intuit's app store target market niches and customer needs not served by QuickBooks on its own.

It generates frequent customer interactions. That makes it a good candidate to become a one-stop shop for other, not necessarily complementary products and services. The third-party services that Lawson's customers can access are largely unrelated to its own products and services, but customers find it extremely convenient to access all of them in the same location.

It's important to be aware of several pitfalls associated with this approach to an MSP. One is that customers who come to you primarily for a product or service may object to the advertising of third-party offerings, especially if they are paying for yours. Intuit faced this when it started exploring services to offer through QuickBooks. As a result, the company is very careful to allow only offerings that align well with the needs and desires of QuickBooks customers and to obtain explicit consent to participate in tests for targeted third-party offers. In addition, Intuit has rebranded QuickBooks as "the operating system for small business" precisely to change customers' perceptions and to minimize potential backlash.

Another possible pitfall is that because you have an existing provider relationship with your customers, they may hold you responsible for the quality of their interactions with third parties. By enabling those parties to interact with your customers, you are implicitly endorsing their offerings—to a greater extent than does a company born as a multisided platform. For instance, a customer taking a spinning class offered by a third-party studio in a health club's gym is likely to blame the health club for a bad experience. As a result, you must curate third-party products and services much more carefully than a company born as an MSP has to.

Finally, some third-party products and services may cannibalize your offerings. The natural inclination would be to allow only those that are either complementary or unrelated to yours. But that approach can be misguided. In some cases it may make sense to coopt offerings that compete somewhat with yours and capture some of the resulting value to your customers. The Forum Athletic Club has replaced its own cycling classes with the Cyc Fitness classes offered at its gym. Cyc's spinning classes have proved more popular with members and allow the Forum to focus its resources on other services while converting Cyc from a competitor to a complementor.

The underlying logic is that if substitution from third parties is inevitable, bringing them onto your platform may expand its overall appeal to your customers, resulting in more demand and opportunities to sell your own services. It may also encourage you to reevaluate your offering's core competitive advantages and focus on them, which may mean ceding ground to third parties in some areas.

2. CONNECTING CUSTOMERS

In this scenario you are selling a product or service to two distinct customer segments that interact or transact with each other outside your offering. You can become an MSP by modifying or expanding your offering so that at least some element of those interactions or transactions occurs through your product or service.

QUICKBOOKS IS USED by both small businesses and accounting professionals. Intuit is in the process of adding a matchmaking function within QuickBooks that would enable small businesses to find and contact accountants with relevant expertise in their geographic area and would allow already-matched business-accountant pairs to exchange documents through the product.

GARMIN AND OTHER fitness wearables are used by both consumers and personal trainers. Many companies that offer these products also host online systems (Garmin Connect, for example) to store fitness-training and health data. Garmin could enable users to share their data with personal trainers, thereby enhancing the interactions between those two groups. To further capture value from this strategy, Garmin could charge trainers for a "pro" subscription—software tools that would let them access clients' data to oversee activities and progress.

This scenario highlights how different customer segments of the same product or service can become customer groups on an MSP. For example, men and women are customer segments for a hair salon (no interaction between them is facilitated by the salon), but they are customer groups for a heterosexual dating service. An entrepreneurial hair salon that started offering matchmaking services to its customer segments could convert men and women into customer groups.

There are two pitfalls associated with this strategy. First, you run the risk of wasting resources on a feature that ultimately creates little additional value for your customers or your company. Worse, the MSP feature can be a detriment if customers perceive it as misaligned with the value of your underlying product or service. Some customers of a hair salon that provides matchmaking services might not want to risk encountering matches that didn't work out. Others might worry that offering a dating service means the salon isn't focused on giving the highest-quality haircuts.

BLIZZARD ENTERTAINMENT'S ill-fated Auction House for its popular Diablo video game provides a cautionary tale. Having noticed that Diablo players were routinely trading digital items on eBay and other external platforms, Blizzard created the Auction House in 2012 to make those transactions easier. It allowed players to buy and sell digital items in exchange for "gold" (digital currency in the Diablo game) as well as real

INTUIT IS ADDING A MATCHMAKING FUNCTION WITHIN QUICKBOOKS THAT WOULD ENABLE SMALL BUSINESSES TO FIND AND CONTACT ACCOUNTANTS WITH RELEVANT EXPERTISE IN THEIR GEOGRAPHIC AREA.

dollars—and Blizzard was able to charge a transaction fee. It quickly became clear, however, that this feature created perverse incentives. Many players decided that buying items at the Auction House was an easier way to reach the game's advanced stages than devoting several hours to killing monsters and searching for loot inside the game. Other players strove to accumulate game items for the sole purpose of selling them in the Auction House. Realizing that this behavior was undermining the value of the game itself, Blizzard shut down the Auction House in 2014.

It is imperative that you conduct market research or run experiments to answer the following questions: Would significant proportions of our offering's various customer segments derive substantial benefits from interacting or transacting with one another? If yes, can our product or service enhance those interactions in a significant way? How will our customers react to the addition of an MSP feature, and how will that feature affect the way they interact with the original offering?

The second pitfall, as in scenario number one, is that although your offering is now simply facilitating a connection or a transaction between two parties, if one party is dissatisfied with the other, you may be held partly responsible. That means you need to put governance mechanisms in place to minimize (if not eliminate) the likelihood of unsatisfactory interactions. Intuit will have to carefully curate the accountants it recommends to QuickBooks customers through its matchmaking feature.

3. CONNECTING PRODUCTS TO CONNECT CUSTOMERS

In this scenario you are selling two products or services, each to a different customer base, and the two customer bases interact outside your offerings. You can become an MSP by modifying or expanding your offerings so that at least part of those interactions occurs through one or both of your offerings.

CARDS AGAINST HUMANITY is a popular game in which players complete fill-in-the-blank statements with humorous (and often tasteless) words or phrases printed on physical playing cards. Its creators continue to sell the game and its numerous expansion packs to consumers, but they have also created Blackbox, a separate website through which they sell back-end fulfillment services (credit-card processing, customer service, shipping) to independent artists who want to sell their products—including third-party developers of other card games. Currently these are separate offerings, but the company could create an MSP by linking them. For instance, it could allow Blackbox customers to advertise their games to Cards Against Humanity's users with expansion packs. A more sophisticated implementation would allow Blackbox customers to test game concepts on willing Cards Against Humanity users, who would provide feedback.

CREDIT BUREAUS SUCH as Equifax, Experian, and TransUnion offer a suite of services for consumers (access to credit scores, identity theft protection, and so on) and a suite of services for financial institutions (credit reports on consumers and businesses). These suites are based on the same data, but the two types of customers interact outside the services (as when a consumer applies for a mortgage); the credit bureaus do not directly facilitate those interactions.

Credit bureaus could create online MSPs where consumers could obtain their credit scores and receive targeted offers from financial institutions. (This is the business model of start-ups such as Credit Karma and Lendio.) These MSPs could go further and enable consumers to create and manage a digital data profile that they could then use to apply directly for financial products at participating institutions (similar to the way Intuit allows QuickBooks customers to apply for financial products through QuickBooks Financing).

NIELSEN OFFERS "WATCH" products to media companies (data on consumers' viewing habits) and "buy" products to consumer goods manufacturers (data on consumers' purchasing habits). One could easily imagine Nielsen's adding the ability for a consumer-packaged-goods company to connect with relevant media companies for advertising purposes.

This scenario highlights how a multiproduct company can become a multisided platform that benefits from network effects. For example, by increasing sales of credit and identity-theft-protection products to consumers, credit bureaus can improve their offerings for financial institutions (which leverage consumer data), thereby achieving greater cross-product economies of scope. While that alone might be valuable, credit bureaus could create and capture even more value by linking the two kinds of products to facilitate interactions between consumers and financial institutions (as described above). This would create an MSP and generate network effects: If more consumers use the credit and identity-theft-protection products, that

FURTHER READING

For more on multisided platforms, see these articles on **HBR.org**:

"Pipelines, Platforms, and the New Rules of Strategy"
Marshall W. Van Alstyne, Geoffrey G. Parker, and Sangeet Paul Choudary
APRIL 2016

"Network Effects Aren't Enough"
Andrei Hagiu and Simon Rothman
APRIL 2016

"Products to Platforms: Making the Leap"
Feng Zhu and Nathan Furr
APRIL 2016

"Spontaneous Deregulation"
Benjamin Edelman and Damien Geradin
APRIL 2016

"When Platforms Attack"
OCTOBER 2015

"How to Launch Your Digital Platform"
Benjamin Edelman
APRIL 2015

"Do You Really Want to Be an eBay?"
Andrei Hagiu and Julian Wright
MARCH 2013

"What's Your Google Strategy?"
Andrei Hagiu and David B. Yoffie
APRIL 2009

"Strategies for Two-Sided Markets"
Thomas R. Eisenmann, Geoffrey G. Parker, and Marshall W. Van Alstyne
OCTOBER 2006

increases the value of the offerings for financial institutions, which can then transact with more consumers more effectively and vice versa.

Two risks are associated with this strategy. First, as with scenario number two, you may waste resources on a feature that ultimately creates little value for your customers or your company relative to the underlying product or service. Second, optimizing for interactions between customers of different products may lead to design choices that limit the growth potential of one or the other product on its own. Once again, it is imperative to use market research and experiments to answer a few questions: Would considerable proportions of your offerings' respective customers derive significantly greater benefits from interacting or transacting through you? If yes, can your offerings substantially enhance those interactions? How will the customers of your two offerings react to the addition of an MSP feature? How will that feature affect the way customers interact with the original products?

4.

SUPPLYING TO A MULTISIDED PLATFORM

In this scenario you become an MSP by creating an offering for your customers' customers that enhances the value of the product or service they buy from your customers. (Although this strategy is logically possible, we are not yet aware of examples of its successful implementation.)

It is important to emphasize that this strategy goes beyond the more traditional "ingredient brand" strategy, which is also a "customers' customers" approach. Indeed, some (essential) ingredient suppliers have created brands in the eyes of their customers' customers (for example, Intel's "Intel Inside") that allow them to extract more value from their customers. But because these ingredient suppliers offer no products or services directly to their customers' customers, they are not MSPs.

The major pitfall with this scenario is that your customers are likely to react negatively to any attempt to go after their customers. Nevertheless, we believe this strategy could work under certain circumstances. The key is to convince your customers that the product or service you provide to their customers is truly complementary to—rather than competitive with—their own offerings.

SHOPIFY IS A leading provider of e-commerce tools to online and retail merchants. Currently the company has no direct connection with its customers' users. It could, however, start offering a common log-in or loyalty program to users of its customers' sites. Whether such an initiative would be successful would hinge on whether Shopify could persuade its merchant customers that the offering was a valuable added service rather than simply an attempt to take control of their customer relationships.

The decision whether and how to convert an offering into an MSP should be informed by who your current customers are, how you currently interact with them, and how they interact with one another. The most fundamental challenge associated with this endeavor is transitioning from a world in which you have 100% control over what your customers are offered to one in which you can only influence the value that is created for them (by third parties or by interactions among themselves).

A final consideration is organizational and leadership challenges. If a company has a solid reputation that is rooted in creating and offering products, shifting to an MSP-focused strategy might be difficult for employees who deeply identify with those products. And companies that sell successful products or services often have strong research and development operations and many engineers in leadership roles; shifting to an MSP strategy that depends on the adept management of third-party relationships might require putting business-development and marketing professionals in significant leadership roles, generating internal conflict. Furthermore, as a company's strategy moves from a product or service orientation to being more MSP-centric, boards, CEOs, and senior management teams may find it difficult to deal with multiple or hybrid strategies, adopt and track new performance metrics, and enforce some degree of technological or customer experience consistency between previously separate products and services.

Nevertheless, if you decide that creating a platform will provide great opportunities for growth and increased profitability and thwart potential competitive threats, the effort to make the transformation may well be worthwhile.

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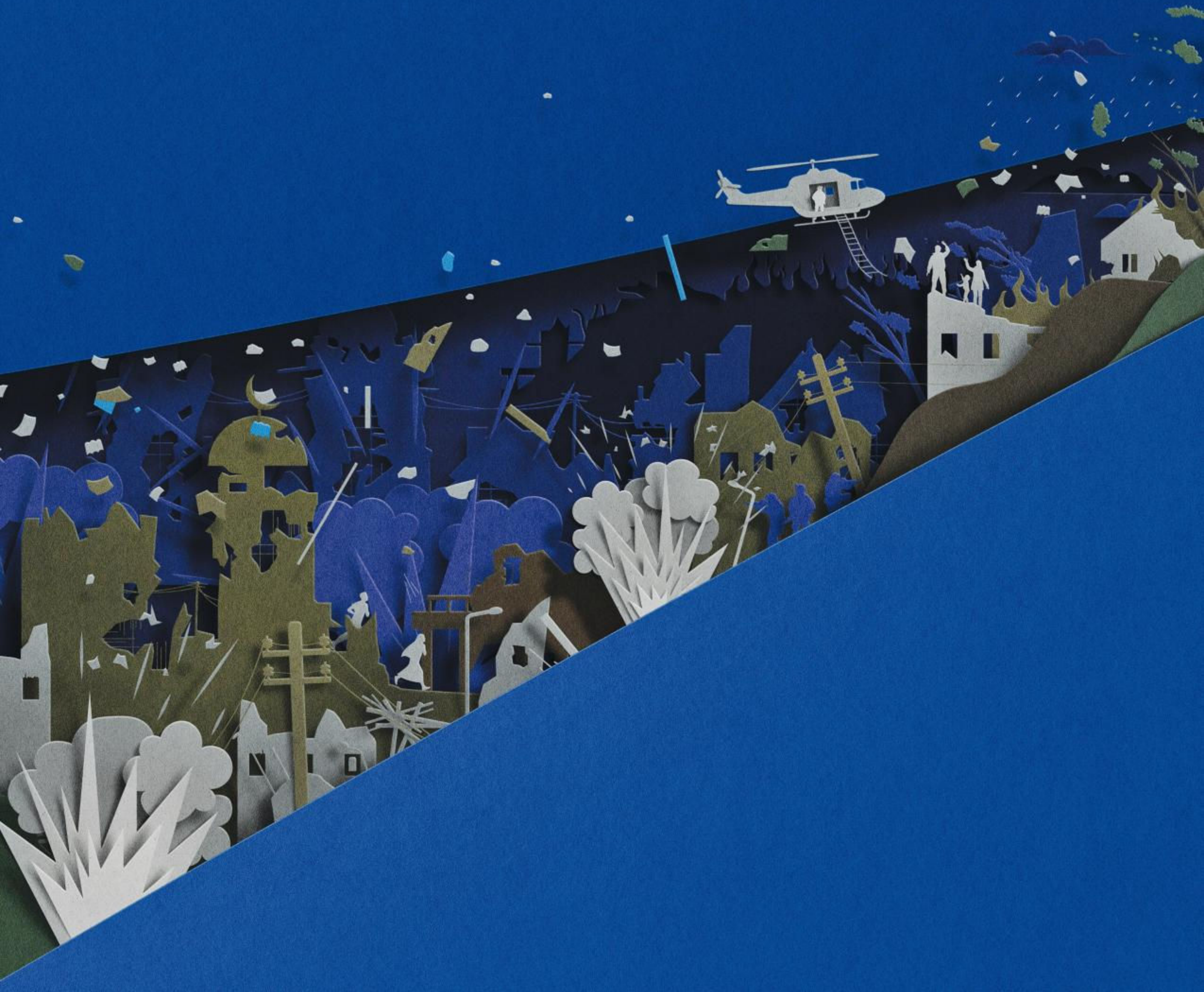

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MANAGING CLIMATE CHANGE: LESSONS FROM THE U.S. NAVY

BY FOREST L. REINHARDT AND MICHAEL W. TOFFEL

ILLUSTRATION BY EIKO OJALA

THE UNITED STATES NAVY OPERATES ON THE FRONT LINES OF CLIMATE CHANGE. IT MANAGES TENS OF BILLIONS OF DOLLARS OF ASSETS ON EVERY CONTINENT AND ON EVERY OCEAN. THOSE ASSETS—SHIPS, SUBMARINES, AIRCRAFT, NAVAL BASES, AND THE TECHNOLOGY THAT LINKS EVERYTHING TOGETHER—TAKE MANY YEARS TO DESIGN AND BUILD AND THEN HAVE DECADES OF USEFUL LIFE. THIS MEANS THAT THE NAVY NEEDS TO UNDERSTAND NOW WHAT SORTS OF MISSIONS IT MAY BE REQUIRED TO PERFORM IN 10, 20, OR 30 YEARS AND WHAT ASSETS AND INFRASTRUCTURE IT WILL NEED TO CARRY OUT THOSE MISSIONS. PUT ANOTHER WAY, IT NEEDS TO PLAN FOR THE WORLD THAT WILL EXIST AT THAT TIME.

IN BRIEF

THE SITUATION
The U.S. Navy is already coping with the consequences of climate change—higher sea levels, new precipitation patterns, and more frequent and severe extreme weather events—that will imperil and destabilize many regions domestically and abroad.

THE CHALLENGE
As the world's climate changes, the navy must address both an increased demand for its military and humanitarian services and an impaired capacity to deliver those services as risk of damage to ports and bases increases.

THE APPROACH
The navy uses a strategic mix of "no regrets" and "bets" investments to address the threats posed by climate change.

The Department of Defense is clear-eyed about the challenges climate change poses. "The pressures caused by climate change will influence resource competition while placing additional burdens on economies, societies, and governance institutions around the world," the most recent Quadrennial Defense Review, issued in 2014, states. "These effects are threat multipliers that will aggravate stressors abroad such as poverty, environmental degradation, political instability, and social tensions—conditions that can enable terrorist activity and other forms of violence."

Leaders across the political spectrum, including former Presidents George W. Bush and Barack Obama and current Secretary of Defense James Mattis, have all noted the security implications of global warming. Like many other organizations, the navy cannot afford to treat climate change as a partisan issue. The Department of Defense knows that the mid-century world for which the admirals are now planning is likely to be warmer than today's, with higher sea levels, new precipitation patterns, and more frequent and severe extreme weather events, imperiling and destabilizing many regions domestically and abroad. This creates two problems that exacerbate each other and that the navy needs to address simultaneously.

First, climate change is expected to increase the demand for the navy's military and humanitarian services. Its effects not only will expand the geographic scope of the navy's mission—from drought-prone regions experiencing heightened disputes over water rights, to coastal areas facing mass migration, to the Arctic, where melting sea ice clears the way for new shipping lanes, increased mineral extraction, and new opportunities for conflict. They also will alter the mix and frequency of demand for the navy's various services.

Second, climate change may impair the capacity of the navy to deliver its services. As sea levels rise and weather patterns become more severe, the risk of damage to the domestic and global network of bases and ports on which it depends to maintain fleet readiness will also increase. Thus, the navy must boost the resilience of its infrastructure—and of the supply chains that provide critical energy and material support to its bases and fleet.

Climate change is not a onetime bump from one equilibrium to a warmer one but, rather, a continuous, accelerating process. This creates the need to plan not for a new static world but for an increasingly dynamic one. The navy's leaders have been working to address this reality head-on, despite resistance from some politicians who continue to debate the very fact of climate change. To do otherwise would compromise its ability to meet its fundamental objectives: "to maintain, train and equip combat-ready Naval forces capable of winning wars, deterring aggression and maintaining freedom of the seas."

Military organizations are idiosyncratic and special. Their primary "output" is lethal force, controlled in ways that compel people to do what they don't want to do. No legitimate firm does anything remotely comparable. And yet there is a long tradition of business leaders learning from their military counterparts—in defining strategic goals, coordinating individuals' activities to accomplish collective objectives, setting priorities and managing trade-offs, creating resilient organizations in the face of change, and leading others. In the climate arena, too, business leaders can learn from the military.

In this article, we'll take a look at the navy's approach to climate change and reflect on the implications for business.

TWO APPROACHES

Responses to climate change are typically categorized as mitigation or adaptation. *Mitigation* refers to actions that reduce the amount of greenhouse gas emissions that are causing climate change. Prime examples include replacing technologies with more-energy-efficient ones and switching to renewable fuels. Mitigation efforts may require substantial

NAVAL STATION NORFOLK, IN PORTSMOUTH, VIRGINIA, IS THE LARGEST NAVAL BASE IN THE WORLD.

MASS COMMUNICATION 2ND CLASS ERNEST R. SCOTT. IMAGES COURTESY OF U.S. NAVY

investment by individual companies or organizations, but the benefits of reducing the potential economic and societal damages associated with climate change are enjoyed by all. As such, mitigation is a public good—which notoriously attracts less investment because the returns are shared by noninvestors.

Adaptation refers to actions that make an organization more resilient in the face of ongoing and forecasted changes in the earth's systems. Common examples include relocating water-intensive operations from increasingly drought-prone areas and siting and engineering buildings in ways that enable them to better avoid, withstand, or recover from floods and severe weather events. Adaptation differs from mitigation in that the investors in the adaptation activities are the primary beneficiaries. Thus, it doesn't face the same incentive problems that mitigation does, and for that reason, one might assume that firms—and nations—would focus their resources on adaptation. But so far they haven't.

Thirty years ago, mitigation and adaptation could have been viewed as substitutes: If we had invested in more-aggressive mitigation then, we might not need to invest so much in adaptation now. But that window has shut. To be sure, mitigation can still reduce the magnitude of problems associated with climate change over the coming decades. Companies may decide to invest in mitigation efforts on their own, and governments may either require them to take

THE NAVY'S LEADERS ARE ADDRESSING THE REALITY OF A CONTINUOUS, ACCELERATING PROCESS OF CHANGE HEAD-ON.

USS KEARSARGE AT NORFOLK SHIPYARD DURING HURRICANE ISABEL, WHICH CAUSED NEARLY $130 MILLION IN DAMAGE TO NAVAL BASES IN THE MID-ATLANTIC REGION.

FLOODWATERS FROM HURRICANE ISABEL'S STORM SURGE FILL A CORRIDOR AT THE U.S. NAVAL ACADEMY, IN ANNAPOLIS, MARYLAND.

AS SEA LEVELS RISE AND WEATHER EVENTS INTENSIFY, THE RISK OF DAMAGE TO THE NAVY'S BASES AND PORTS WILL INCREASE.

particular actions or (preferably, because it's more efficient) institute price-based incentives such as carbon taxes or cap-and-trade systems that motivate them to reduce emissions. But those efforts simply cannot obviate the need for extensive adaptation.

MITIGATION

The navy has undertaken numerous initiatives that reduce greenhouse gas emissions. Since 2009, for example, it has been working toward a goal set by then Secretary of the Navy Ray Mabus to obtain half of its total energy from alternative sources by 2020. The objective is not to engage in mitigation for its own sake; it is to reduce the navy's vulnerability to disruptions to fossil-fuel supply chains that originate in or flow through hostile regions and to better insulate the force from the price volatility that occurs when oil-producing regions are unstable.

The navy is also working to improve the fuel efficiency of its ships, aircraft, and expedition vehicles, not just to reduce costs or mitigate the speed and severity of climate change but to save lives. Supplying oil to military operations in Afghanistan led to an average of one casualty for every 24 fuel-resupply convoys. More-fuel-efficient ships, aircraft, and vehicles require fewer resupply missions.

One of the navy's most visible signs of progress is the Great Green Fleet initiative, an aircraft-carrier strike group that traveled the world in 2016 with every service ship and aircraft operating on a 50/50 blend of biofuel and petroleum. While the navy initially purchased the biofuel at a huge premium over conventional fossil fuels, it has now signed contracts with several biofuel producers at prices on par with those of fossil fuels.

The navy has successfully managed transitions from one energy source to another several times in its long history. Its ships were first powered by wind, then by coal, and then by petroleum; more recently the navy developed nuclear-powered submarines and aircraft carriers. In this historical context, the latest shift is actually quite modest.

To power its bases ashore, the navy is relying less on mainstream electricity grids and more on distributed renewable-energy sources—that is, systems that generate clean energy onsite, where it will be used. Beyond reducing dependence on fossil fuels and mitigating greenhouse gas emissions, this energy transition strengthens the bases' resilience to cyberattacks on electrical grids.

Although such initiatives are motivated by concerns over operational readiness and resiliency, they also serve to mitigate the navy's contribution to climate change by reducing reliance on fossil fuels. The Department of the Navy, which includes the U.S. Navy and the Marine Corps, accounts for 1% of America's total fossil-fuel use. It has signed long-term renewable-energy contracts for more than 1.2 gigawatts (GW) of the total 2 GW required by its bases, which exceeds its 2020 goal. This commitment to alternative energy is spurring private-sector investments in renewable energy technologies that are driving costs down, not only for the navy but for all consumers. It also buffers the alternative-fuel industry against price swings that could deplete its firms' balance sheets and its human capital, much as the navy's demand for nuclear energy to power its submarine fleet kept that industry moving forward during times when its commercial viability was in question.

The navy's efforts to shift to renewable energy are not limited to its bases. It's also developing

MATE 1ST CLASS MICHAEL PENDERGRASS. IMAGES COURTESY OF U.S. NAVY

technologies such as lightweight, flexible solar blankets that can recharge batteries to untether expeditionary forces from battery-replenishment supply chains while reducing weight in troops' backpacks.

NAVY PERSONNEL REPAIRING A DAMAGED PIER AS PART OF A DISASTER RELIEF MISSION IN PORT-AU-PRINCE, HAITI.

OFF THE PHILIPPINES COAST, A NAVY HELICOPTER TRANSPORTS SUPPLIES DURING RELIEF EFFORTS FOLLOWING SUPER TYPHOON HAIYAN.

USS BONHOMME RICHARD REFUELS DURING A ROUTINE PATROL IN THE EAST CHINA SEA.

MASS COMMUNICATION SPECIALIST 2ND CLASS CHRIS LUSSIER; MASS COMMUNICATION SPECIALIST SEAMAN CHRIS CAVAGNARO; MASS COMMUNICATION SPECIALIST 2ND CLASS DIANA QUINLAN. IMAGES COURTESY OF U.S. NAVY

THE DEMAND FOR MILITARY AND HUMANITARIAN SERVICES IS ALSO EXPECTED TO INCREASE DRAMATICALLY.

ADAPTATION

The navy is focusing most of its climate change efforts not on mitigation but on adaptation. As the world's climate alters, the navy must address both increased demand for its services and an impaired capacity to deliver those services.

Increased demand. Let's start with the likelihood that climate change will increasingly trigger international conflict, state failure, or both. The navy predicts that climate change will lead to more—and more-prolonged—droughts, which in turn will raise the potential for more military interventions. Drought is one of several climate-related "threat multipliers" that, by stressing societies and states, increase the potential for violent conflict. Such concerns are not merely theoretical: The bitter violence in Syria has been linked to drought-induced food insecurity and migration from rural to urban areas. And the U.S. Navy has sent warships into the Mediterranean Sea as a result. In this context of heightened instability, the navy expects to be called upon more frequently and in more places.

Climate change is also expected to increase the demand for humanitarian assistance and disaster response. Almost every year the navy distributes food and medicine in the aftermath of a catastrophe, whether domestically, as after Hurricane Katrina, or abroad, as in Haiti in 2016, after Hurricane Matthew. There's every reason to expect that hurricanes and typhoons will get fiercer and more widespread, and that the flooding they produce will escalate the frequency, scale, and scope of disaster response requested of the navy. Moreover, increased drought intensity will spur mass migrations that put lives at risk, and the U.S. Navy can be expected to receive more calls to aid with rescue missions.

Further, just as climate change alters the mix of services needed to meet evolving demands, it modifies the geography and distance over which those services will have to be delivered. For example, in the Arctic, the widespread melting of sea ice means increased opportunities for commerce (via shorter shipping lanes) and resource extraction (more continental shelf from which to extract more oil and gas) and hence more requests for assistance and an increased likelihood of conflict in that part of the world.

The navy doesn't currently possess all the assets it needs to operate effectively in the Arctic, making adaptation a necessity. For example, icebreaking ships are useless in both ice-free waters and waters so thickly frozen that the ships can't move; but as the ice pack thins and we spend more time between these extremes, they are critical. Alaska Senator Lisa Murkowski told *Foreign Policy,* "I get very impatient because I don't see us prioritizing icebreakers as a national asset." Pointing to the behavior of the United States' rivals, she observed, "People can quibble about what we have versus what Russia has versus what China is building. All I can tell you is we are not in the game right now." Indeed, the United States has only five icebreakers capable of functioning in the Arctic (only three of which the military operates; private companies operate the other two). Russia has 41, half of which are owned by the government, and more are under construction.

Just as climate is altering the demands for the navy's services, so it may affect the manner in which the navy fights. If conflict breaks out in an arid area, available freshwater may be a strategic asset that navy fighters can manipulate to their advantage. According to U.S. military doctrine, the objective of war is to destroy the enemy's capacity to resist. This

THE U.S. DOD'S CLIMATE CHANGE ADAPTATION ROADMAP

To assess its resilience in the face of climate change, the U.S. Department of Defense examined potential climate-related impacts on its infrastructure and supply chains. Businesses can use this excerpted list as a guide in considering potential impacts of climate change on their own operations.

SUMMARY OF POTENTIAL IMPACTS

BUILT & NATURAL INFRASTRUCTURE

- Increased inundation, erosion, and flooding damage.
- Changing building heating and cooling demand, impacting installation energy intensity and operating costs.
- Disruption to and competition for reliable energy and freshwater supplies.
- Damage from thawing permafrost and sea ice in Alaska and the Arctic region.
- Increased ecosystem, wetland, sensitive species, and non-native invasive species management challenges.
- Increased maintenance requirements for runways or roads to remain operable during extreme hot days.
- Changed disease vector distribution, increasing the complexity and cost of ongoing disease management efforts.

ACQUISITION & SUPPLY CHAIN

- Changed operational parameters for current and planned weapons and equipment, resulting in increased associated maintenance requirements or requirements for new equipment.
- Reduced availability of or access to the materials, resources, and industrial infrastructure needed to manufacture the Department's weapon systems and supplies.
- Interrupted shipment, delivery or storage/stockpile of materials or manufactured equipment and supplies.
- Alterations in storage and stockpile activities.
- Reduced or changed availability and access to food and water sources to support personnel.

SOURCE U.S. DEPARTMENT OF DEFENSE, 2014 CLIMATE CHANGE ADAPTATION ROADMAP

can occur through death or captivity, but also through physical paralysis (which is why militaries seek to deny their enemies access to fuel) or psychological paralysis (thus, tactics such as "shock and awe," designed to undermine psychological resilience). If the navy controls access to freshwater in a desert theater, it can destroy the enemy's capacity to resist. The point here is that climate change may create opportunities—grim though they may be.

Companies will have to make the same kinds of strategic shifts, both to seize new opportunities and to defend existing market positions from long-standing rivals and new competitors. For example, a company that produces seeds for farmers may see opportunities to develop new drought-resistant crop varieties. It may also find new customers among farmers in higher latitudes as growing seasons lengthen. At the same time, current customers will need more managerial and financial attention, not less, as they figure out how to cope with the short-term manifestations of climate change. Long-established giants like Monsanto and start-ups like Boston's Indigo Agriculture are already investing in the agricultural solutions that farmers in a world of climate change will demand, and their counterparts in transportation, real estate, insurance, and finance are—or should be—making similar bets.

Impaired capacity. Climate change also complicates the navy's ability to deliver its services. According to the Department of Defense's Climate Change Adaptation Roadmap, climate change will affect the military's built and natural infrastructure and its acquisition and supply chain in dramatic ways. For example, we can expect increasing flooding at naval facilities at Norfolk; flash flooding and mudslides in Hawaii, home to the navy's Pacific Fleet; and intensified droughts in California, where the navy has more than $40 billion in assets. In Alaska, the navy is being forced to rebuild and relocate roads, buildings, and airfields as the permafrost melts, and it might eventually have to relocate some of its bases. International bases are also likely to be severely affected by storm surges and higher sea levels, including Yokosuka base in Tokyo Bay, which serves as the Seventh Fleet's headquarters, and the Diego Garcia facility, on a low-lying atoll in the Indian Ocean, which serves as a critical logistics hub for operations in the Middle East, the Mediterranean, and Southern Europe.

Especially vulnerable are the navy's coastal infrastructure and the supply chains that furnish energy and materials to its bases and fleet, all of which are essential to mission readiness. Most of the navy's land-based assets—shipyards, bases, and other installations—are on seacoasts. Its 111,000 buildings and structures on bases and other installations, located on 2.2 million acres around the world, would cost $220 billion to replace.

These assets were designed and built to be resilient to historic sea levels and storm intensity. But sea levels rose on average nearly half a foot over the 20th century, a rate faster than that in any century since at least 800 BC. The rise so far is mostly owing to thermal expansion (warmer water takes up more space), but future sea level changes are likely to be driven by melting ice sheets in Greenland and Antarctica. Sea-level rise and related storm surges are the two biggest threats to the navy's coastal infrastructure, according to navy officials. Not only do such floods inundate roads and damage buildings, but they put ships being repaired in dry docks at risk. (An independent report by the Union of Concerned Scientists showed that a three-foot rise in sea levels would significantly threaten 55 naval installations in the United States valued at $100 billion.)

The average rate of sea-level rise masks substantial variation among regions. As the navy celebrates the centennial of its enormous Norfolk base, the sea level there is a foot and a half higher than when the base was established, during World War I. Since much of the base sits less than three feet above sea level, heavy rains and higher-than-usual tides are flooding it more often, submerging some of its piers and immersing the electrical wires and steam pipes that run underneath. Pier inundation now happens at least monthly, impeding training and maintenance schedules and thus fleet readiness. Sea levels are rising at the Norfolk base an inch every six years—more than double the global average rate. Tidal flooding at Norfolk is expected to increase from the current rate of nine times a year to 280 times a year by 2050, and low-lying areas could be underwater 10% of the time. And navy engineers expect sea levels to rise at Norfolk another two to four feet over the next 80 years, by which time as much as 20% of the base's land might experience daily floods, essentially becoming part of the tidal zone.

The navy must find ways to protect its bases, both by investing to prevent damage from rising seas and storm surges (raising infrastructure and creating stronger and higher floodwalls) and by enhancing its ability to recover rapidly when damage occurs. The navy now requires planners to provide additional justification when a new building is to be situated within two meters of sea-level-rise forecasts. Buildings that pass this new hurdle must incorporate flood barriers and backup systems to withstand rising sea levels and storm surges. In some cases, the navy is partnering with nongovernmental organizations to identify ways to increase the resilience of its bases. For example, to assess the vulnerability of its naval base in Ventura County, California, the navy has partnered with The Nature Conservancy, which has developed models and mapping tools that assess the resilience of U.S. coastal communities to rising tides and storm surges.

While long-term planning is under way, the navy is taking steps to reinforce its current infrastructure. For example, the Norfolk base piers that provide power and heat to navy vessels—when they are not periodically submerged—are being replaced at a cost of more than $100 million each. The new piers are designed with sea level rise in mind: Their electrical, water, and steam utilities sit on a second deck running above the piers instead of underneath them.

Yet even with these efforts, the threats from climate change are so serious that the navy will eventually need to decide which bases to protect and which to abandon. It prefers engineering solutions that keep assets in place, but that may not always be feasible as the century unfolds.

NO REGRETS VERSUS BETS

Some of the navy's actions to address climate change make sense even if climate change doesn't alter the world as much or as quickly as scientists are forecasting. These are win-win, or "no regrets," investments. For example, installing backup power generators in elevated positions at naval bases increases operational resilience by protecting them from storm surges and rising sea levels. The generators also bolster fleet readiness by protecting the bases against other threats, such as cyberattacks on electrical grids.

A STRATEGIC APPROACH TO CLIMATE CHANGE

Companies tend to focus their climate efforts in the win-win quadrant, making (mostly minor) investments that reduce emissions, pay for themselves, and make the firm look socially responsible. The U.S. Navy pursues initiatives in all four quadrants, realizing that it's often undesirable to pick just one.

	MITIGATION Investments that reduce the speed and severity of climate change	**ADAPTATION** Investments that reduce the consequences of climate change for the organization
NO-REGRETS ACTIONS yield benefits to the organization even if climate change effects are less severe than forecasted.	**WIN-WIN** •Develop portable solar blankets that can recharge batteries for mobile equipment (lightens troop loads and reduces reliance on replenishment supplies) •Increase fuel efficiency of ships, aircraft, and vehicles (extends their range and reduces refueling)	**PROFITABLE HEDGING** •Install early-warning systems for storms (valuable now, and would be even more so if storm frequency or intensity increases) •Install backup generators at raised elevations (increases resilience to power-grid failures)
BETS are valuable only if climate change effects are at least as severe as forecasted, and may be considered wasteful otherwise.	**COSTLY ALTRUISM** •Install solar farms on navy bases (betting on new regulations that will increase fossil-fuel costs)	**STRATEGIC INVESTMENT** •Raise structures (betting on sea-level rise and increasingly intense storm surges) •Build naval bases in Alaska (betting on diminishing Arctic ice)

Similarly, investments in ships and aircraft that are more fuel efficient not only mitigate the navy's contribution to climate change but also increase the resilience of its supply chains and enable the force to better fight where it needs to fight. All these investments can pay for themselves by saving on operating costs, irrespective of climate change. They follow a no-regrets strategy: They deliver payoffs whether or not climate change occurs at forecasted rates.

But many of the actions that the navy needs to take to confront climate change don't have this characteristic. Relocating naval bases to protect them from forecasted effects of climate change will require billions of dollars of investment that provides little benefit if the seas don't rise and coastal storms don't get worse. Similarly, opening new bases in the Arctic makes sense only if scientists are right about the increasing

U.S. AIRCRAFT CARRIERS LIKE THE USS GERALD R. FORD ARE FUELED BY NUCLEAR POWER, MAKING THEM LESS VULNERABLE TO DISRUPTIONS IN FOSSIL-FUEL SUPPLIES.

THE MICROGRID AT THE MARINE CORPS AIR STATION, IN MIRAMAR, CALIFORNIA, REDUCES THE RISKS RELATED TO POWER-GRID FAILURE.

THE NAVY USES A STRATEGIC MIX OF "BETS" AND "NO REGRETS" INVESTMENTS TO ADDRESS THREATS FROM CLIMATE CHANGE.

ICE CAMP SARGO, ON AN ICE FLOE IN THE ARCTIC, WAS THE 2016 BASE FOR NAVAL EXERCISES DESIGNED TO RESEARCH, TEST, AND EVALUATE OPERATIONAL CAPABILITIES IN THE REGION.

navigability of the Arctic Ocean. Given the long timeline required to build new ships and bases, the navy cannot simply wait to find out before making investments. Not every risk can be hedged, so it pursues a "bets strategy," informed by the best possible scientific forecasts. While the investments will yield benefits only if the forecasts are correct, doing nothing could be catastrophic. Making informed bets regarding climate change is not unusual for the navy, which, as Rear Admiral David Titley (Ret.) points out, "would rather plan for something that doesn't happen than be taken by surprise." (See the exhibit "A Strategic Approach to Climate Change.")

Indeed, bets strategies are the bread and butter of any commander. In combat situations, navy admirals, like patrol-boat commanders and SEAL team leaders, have to make decisions every day that may lead to regrettable outcomes. In the words of one recently retired SEAL officer, "We make decisions, and then we live with the consequences."

Businesspeople, however, like to talk about no-regrets tactics, especially in the arena of climate change—for example, making climate-related investments in supply chains that will pay for themselves even if the climate doesn't alter. These tactics may seem easy and uncontroversial; but pursuing exclusively no-regrets strategies involves choosing *not* to place considered bets. That course of action is fraught with risk—and could be disastrous.

Some organizations are responding to the need to place bets. For example, Starbucks is developing coffee plants and testing coffee-growing practices to make crops more resistant to new pests and diseases, such as leaf rust, that spread with warmer temperatures. Its early results have produced plants that are more resistant—but lower-yielding and slower-growing. This is a bets strategy that will have a favorable outcome only if temperature trends in the coffee-growing regions that are already experiencing declining yields continue, as scientists are forecasting, and are not simply a short-term anomaly. Similarly, Boston and other cities are considering investing billions of dollars in massive seawalls to protect against rising sea levels and the

MASS COMMUNICATION SPECIALIST 2ND CLASS RIDGE LEONI; PFC. LIAH KITCHEN; ADAM BELL. IMAGES COURTESY OF U.S. NAVY

increasingly damaging storm surges that scientists predict for the coming decades. Such investments will be viewed as wise only if these manifestations of climate change materialize.

The point is that coffee companies that are not investing in botanical research, and coastal cities that are not building seawalls, are making bets too: They're just betting that climate change will be unimportant or that some solution will present itself later. If you think that all your firm's climate-related activities fall into the no-regrets categories, it's virtually certain that you're making implicit bets that climate change will not affect your business. It's okay to take that risk, but you should do so consciously.

THE LEADERSHIP CHALLENGES involved in climate change are enormous. For the navy, it creates new difficulties in achieving existing mission objectives even as it expands the scope of missions the force will be called upon to undertake. Fortunately, the navy can build on centuries of tradition and insight into the ways in which humans can be led to perform extraordinarily in difficult circumstances.

For businesses, it's time to move beyond no-regrets efforts, however admirable those may appear to customers, employees, or other stakeholders. Leaders need to follow the navy's implicit checklist to ensure that their organizations can fight the battles they will face in the coming decades: They must examine their operational and supply-chain resilience in light of rising temperatures, higher sea levels, and changing precipitation patterns, leading to heavier downpours and droughts and more frequent and severe extreme weather events—the manifestations of climate change for which the Department of Defense is planning. They need to consider what sorts of products and services will be more valuable, or less, in a climate-altered world. They must identify the new geographic scope over which they can or must be active. They need to design and operate the information and control systems that will allow them to integrate the new imperatives with the old. And they need to understand the demands that climate change will impose on their ability to lead the men and women in their organizations.

The navy is a microcosm of society at large. Despite its amazing power, it cannot afford the luxury of ideology. It has to operate and fight in the world as it exists and to plan to operate and fight in the world we are creating. Exactly the same is true for the leaders of firms.

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SCIENCE AND POLITICS

Some politicians argue that the U.S. Navy should deprioritize climate change planning in order to concentrate on traditional security threats. Indeed, some have introduced legislation to prevent the navy and the other military branches from even planning for climate change.

This is not an unusual problem. Every organization has stakeholders who disapprove of aspects of its behavior and want certain activities to be curtailed. A common response in business is simply to relabel the controversial activity to make it less objectionable to naysayers.

A better approach is to address climate change head-on, using scientific evidence to build the case for investments. The navy makes no attempt to hide its climate-related planning and preparation or to cloak its activities in soft rhetoric. "Even very low probability events with devastating consequences must be considered and mitigation/adaptation schemes developed and employed," says Admiral Frank "Skip" Bowman, USN (Ret.). "We operate our nuclear submarine fleet in this fashion. That's where we should be with climate change."

There's a lesson here for stakeholders, too. Certain kinds of planning and investment may appear unwise because the contingencies involved seem remote. But constraining the managerial prerogatives of an organization can be costly—particularly for the military, its civilian counterparts in security and emergency response, and firms selling insurance and other risk-management services, whose entire purpose is to prepare for and confront low-probability but costly events. No matter how impassioned their view of the science of climate, politicians cannot responsibly proscribe the military's collection and analysis of climate-related intelligence or its preparation to manage the contingent risks.

RELATED RESOURCES

DOCUMENTARIES

Tidewater (2017) explores the challenges facing Hampton Roads, which requires $1 billion in urgent infrastructure repairs to its 900 miles of its roads and electric grid threatened by permanent flooding.

The Age of Consequences (2016) describes the effects of climate change—waves of refugees, failed states, terrorism—and their implications for U.S. national and global security.

Facing the Surge (2016) describes the vulnerability to rises in sea level of the Norfolk naval base—the largest in the world—and its surrounding Hampton Roads community.

The Burden (2015) examines the U.S. military's response to dependence on fossil fuels as a long-term national security threat.

REPORTS

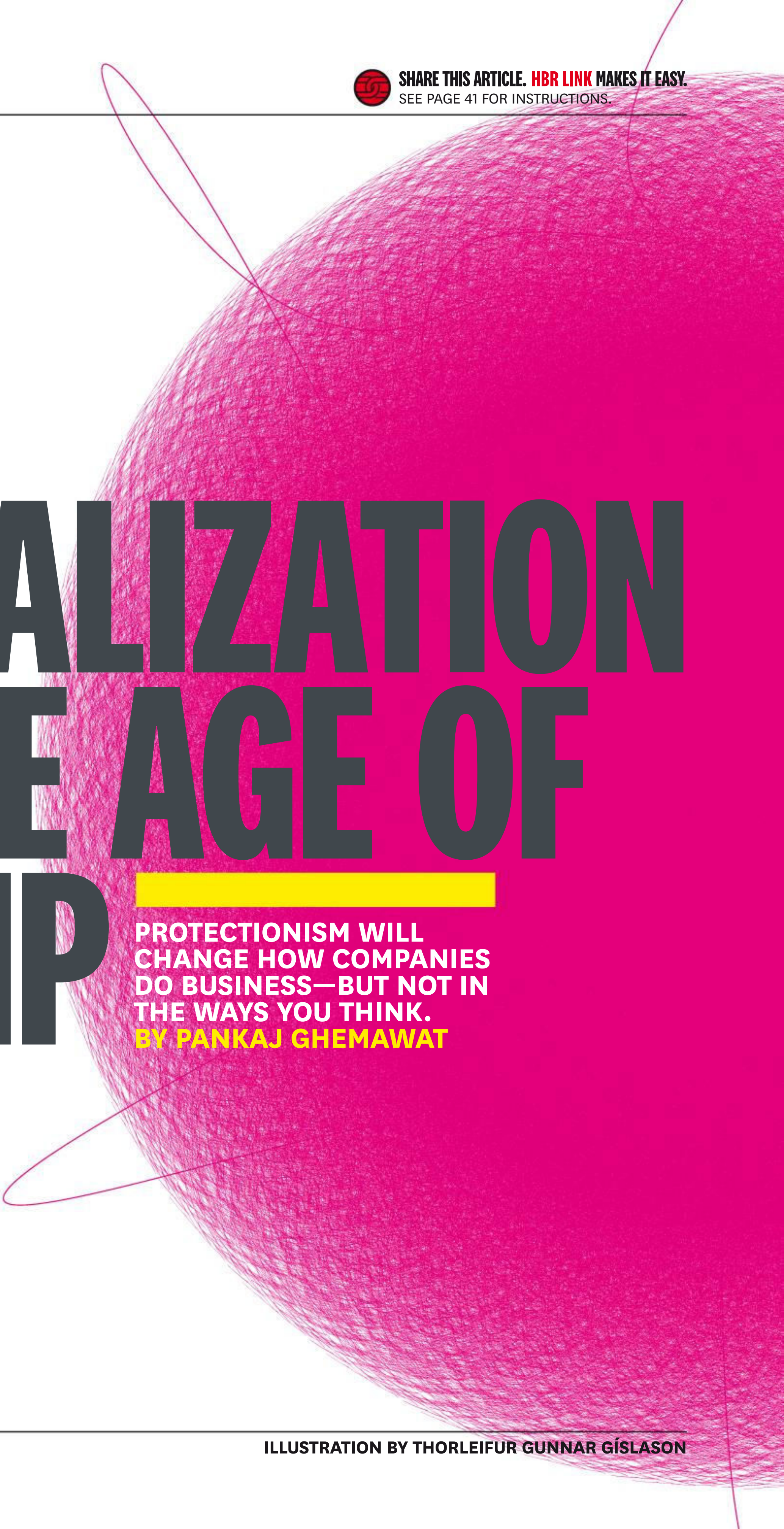
"The U.S. Military on the Front Lines of Rising Seas"
Union of Concerned Scientists, 2016

"Weathering the Next Storm: A Closer Look at Business Resilience"
Center for Climate and Energy Solutions, 2015

"2014 Climate Change Adaptation Roadmap"
U.S. Department of Defense

"National Security and the Accelerating Risks of Climate Change"
CNA Corporation, 2014

"U.S. Navy Climate Change Roadmap"
U.S. Navy, 2010

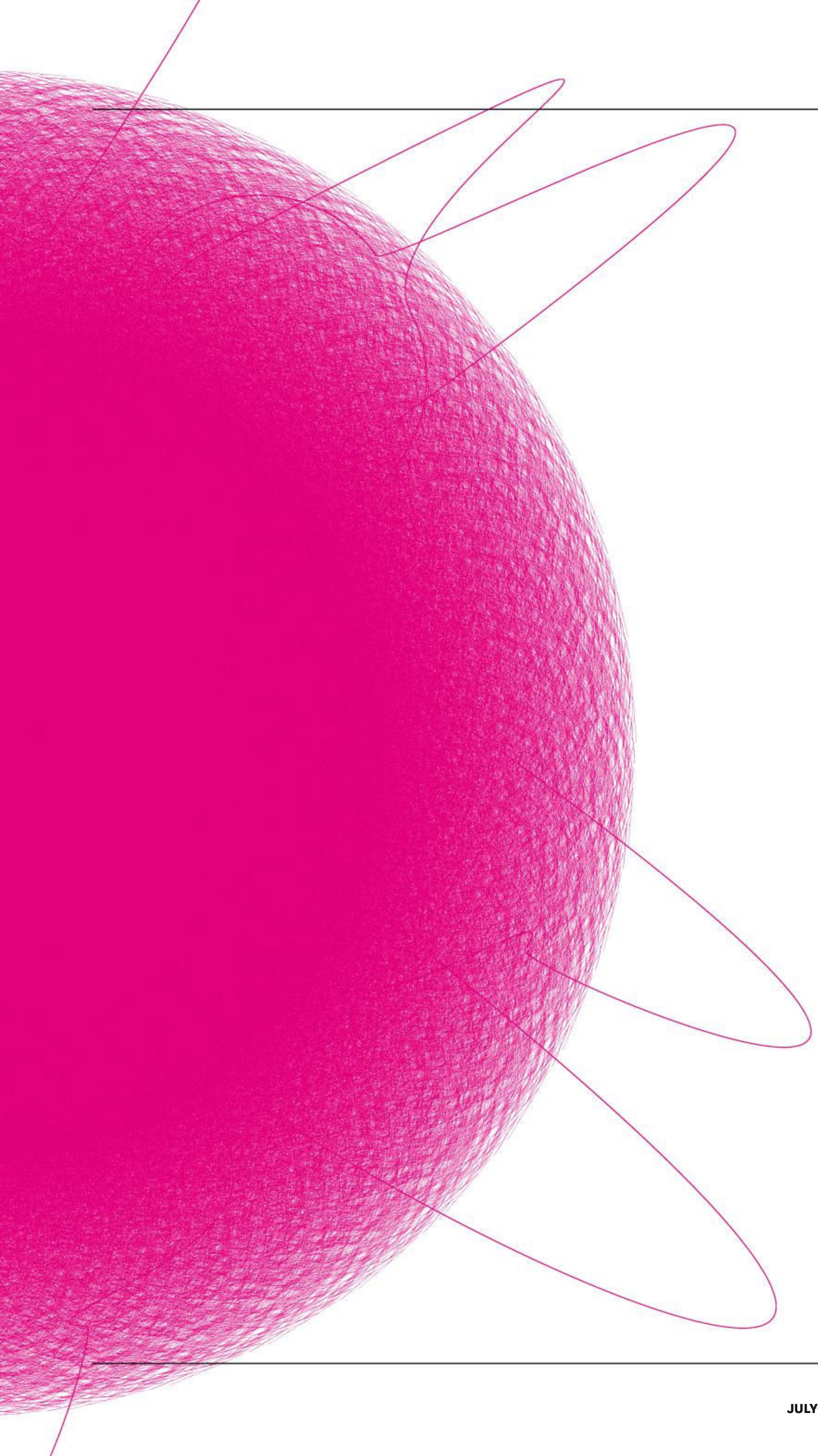


GLOBALIZATION IN THE AGE OF TRUMP

PROTECTIONISM WILL CHANGE HOW COMPANIES DO BUSINESS—BUT NOT IN THE WAYS YOU THINK.

BY PANKAJ GHEMAWAT

ILLUSTRATION BY THORLEIFUR GUNNAR GÍSLASON



BUSINESS LEADERS ARE SCRAMBLING

to adjust to a world few imagined possible just a year ago. The myth of a borderless world has come crashing down. Traditional pillars of open markets—the United States and the UK—are wobbling, and China is positioning itself as globalization's staunchest defender. In June 2016, the Brexit vote stunned the European Union, and the news coverage about globalization turned increasingly negative in the U.S. as the presidential election campaign progressed.

IN BRIEF

THE PROBLEM
Countries throughout North America and Europe have experienced waves of anti-globalization sentiment, but most business leaders are uncertain about whether to retreat, change strategy, or stay the course.

THE BIG PICTURE
Before making any decisions, it's important to understand two things. First, the world is less globalized than most people realize. Second, history tells us that even in the face of a trade war, international trade and investment would still be too large for strategists to ignore.

RECOMMENDATIONS
Don't overreact to protectionist rhetoric, but do make adjustments. If your operations are unprofitable, retrench. Focus more resources on adapting to local needs. And wherever you do business, be sure you're creating—not just extracting—value.

One week after Donald Trump's inauguration, with fears of a trade war spiking, the *Economist* published a cover story, "The Retreat of the Global Company," in which it proclaimed that "the biggest business idea of the past three decades is in deep trouble" and that "the advantages of scale and...arbitrage have worn away." And Jeffrey Immelt, GE's chairman and CEO, has talked about the company's "bold pivot" from globalization to localization.

But is a mass retreat from globalization really the right approach for companies in these uncertain times? Or, short of packing up and returning home, should they focus on localization—that is, producing and even innovating where they sell—as the strategy of choice? Not according to my research. Recall that as recently as a decade ago, business leaders believed that the world was becoming "flat" and that global companies, unconstrained by country borders, would soon dominate the world economy. Those exaggerated claims were proven wrong. Today's cries for a massive pullback from globalization in the face of new protectionist pressures are also an overreaction, in the other direction. While some of the euphoria about globalization has shifted to gloom, especially in the United States, globalization has yet to experience a serious reversal. And even if it did, it would be a mistake to talk about the end of globalization: The "rewind" button on a tape recorder shouldn't be confused with the "off" button.

A full-scale retreat or an overreliance on localization would hamper companies' ability to create value across borders and distance using the rich array of globalization strategies that are still effective—and will continue to work well into the future. Today's turmoil calls for a more subtle reworking of multinationals' strategies, organizational structures, and approaches to societal engagement. In this article, I address common misperceptions about what is—and isn't—changing about globalization, offer guidelines to help leaders decide where and how to compete, and examine multinationals' role in a complex world.

THE TRAJECTORY OF GLOBALIZATION

Doubts about the future of globalization began to surface during the 2008–2009 financial crisis. But as macroeconomic conditions improved, the gloom gave way to a murky mix of perspectives. For example, within the span of just three weeks in 2015, the *Washington Post* published an article by Robert J. Samuelson titled "Globalization at Warp Speed" and a piece from the editorial board called "The End of Globalization?"

In the face of such ambiguity, it is essential to look at the data. To see how globalization is actually evolving, Steven Altman and I compile the biennial DHL Global Connectedness Index, which tracks international flows of trade, capital, information, and people. (See the exhibit "Globalization Has Not Gone into Reverse.") The two index components of greatest business interest—merchandise trade and foreign direct investment—were hit hard during the financial crisis, but neither has suffered a similar decline since then. Trade experienced a large drop-off in 2015, but that was almost entirely a price effect, driven by plunging commodity prices and the rising value of the U.S. dollar. Updated data suggests that in 2016 foreign direct investment dipped, in part because of the U.S. crackdown on tax inversions. Complete data for 2016 is not yet available, but factoring in people and information flows will probably reinforce the conclusion that globalization has stayed flat or even increased.

What has nose-dived, however, is the tone of public discourse in the United States and other advanced economies. An analysis of media mentions for the term "globalization" across several major newspapers—the *Wall Street Journal,* the *New York Times,* and the *Washington Post* in the U.S. and the *Times of London,* the *Guardian,* and the *Financial Times* in the UK—reveals a marked souring of sentiment, with scores plummeting in 2016.

The contrast between the mixed-to-positive data on actual international flows and the sharply negative swing in the discourse about globalization may be rooted, ironically, in the tendency of even experienced executives to greatly overestimate the intensity of international business flows relative to domestic activity. In other words, they believe the world is a lot more globalized than it actually is. (See the exhibit "The Globaloney Gap.")

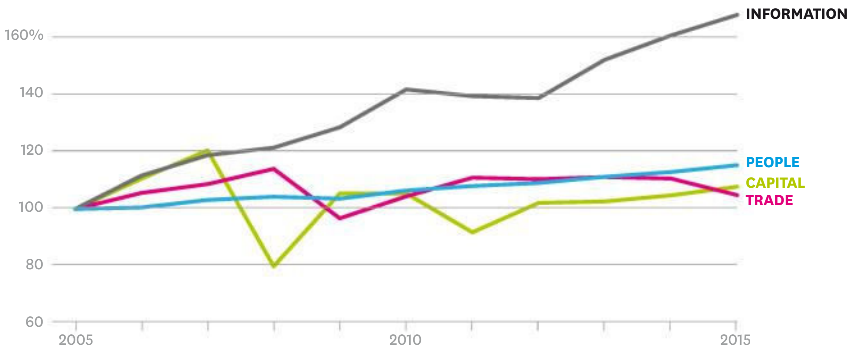
Exaggerated perceptions about the *depth* of globalization—that is, how much activity is international versus domestic—come at a cost. In surveys I've conducted, respondents who overestimated the intensity of globalization were more likely to believe erroneous statements about international business strategy and public policy. When businesspeople think the world is more globalized than it really is, they tend to underestimate the need to understand and respond to differences across countries when operating abroad. In the public policy sphere, leaders tend to underestimate the potential gains from additional globalization and to overestimate its harmful consequences for society.

Surveys suggest that people also underestimate the *breadth* of globalization—that is, the extent to which international activity is distributed globally rather than narrowly focused. In a 2007 survey of *Harvard Business Review* readers, 62% of respondents agreed with the quote from Thomas Friedman's best-selling book *The World Is Flat* that companies now operate on "a global, Web-enabled playing field that allows for…collaboration on research and work in real time, without regard to geography, distance or, in the near future, even language." However, data shows that actual international activity continues to be dampened strongly by all those factors.

GLOBALIZATION HAS NOT GONE INTO REVERSE

The DHL Global Connectedness Index—which tracks international trade, capital, information, and people flows—shows that globalization slowed down in 2015 but did not go into reverse. (Updated 2016 data for trade and investment suggests a continued slowdown but still no reversal.)

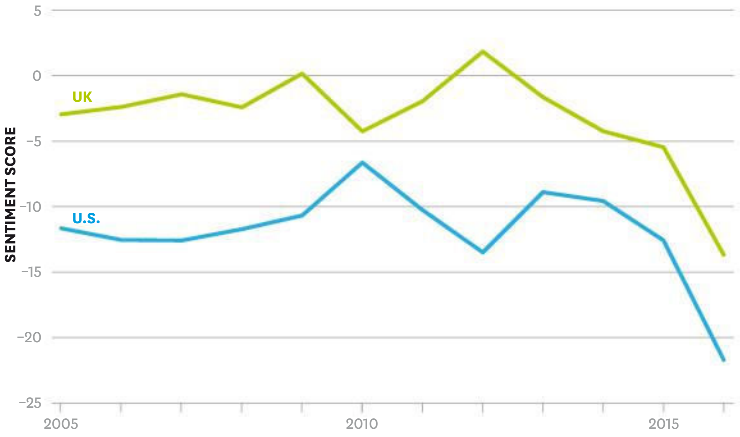
DEPTH OF GLOBAL CONNECTEDNESS, RELATIVE TO 2005



SOURCE DHL GLOBAL CONNECTEDNESS INDEX 2016

MEDIA SENTIMENT HAS SOURED

The tone of news stories containing the word "globalization" in leading U.S. and UK newspapers has taken a sharply negative swing, reflecting rising pressures against globalization in those countries.

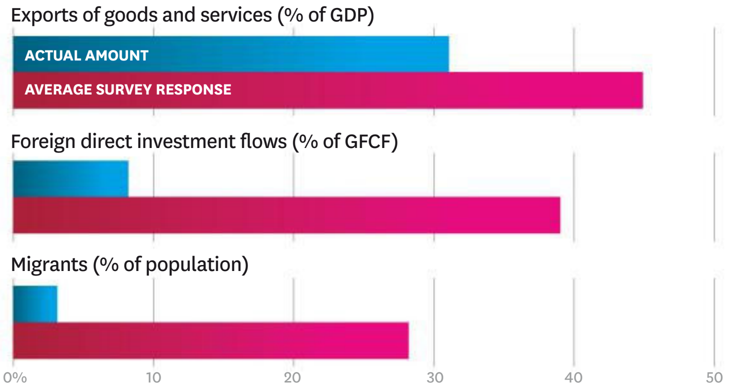


SOURCE GENERATED WITH ALCHEMYAPI USING ARTICLES FROM THE *WALL STREET JOURNAL*, THE *NEW YORK TIMES*, THE *WASHINGTON POST*, THE *TIMES OF LONDON*, THE *GUARDIAN*, AND THE *FINANCIAL TIMES*

THE GLOBALONEY GAP

In a 2012 survey, people overestimated the intensity of global business and underestimated the extent to which distances and differences between countries constrain international commerce.

EXTENT OF GLOBALIZATION



WHO'S MORE AT RISK IN A LESS-GLOBAL WORLD?

A global trade war would hurt virtually every national economy—but some countries are more at risk than others. For example, Singapore, a small but highly developed economy, exports goods and services equivalent to 176% of its GDP. It's apt to be much harder hit than the United States, whose exports account for only 13% of its GDP.

EXPORTS AS A PERCENTAGE OF GDP IN 2015

Small countries, big exports

214%	**176%**	**124%**	**82%**
LUXEMBOURG	SINGAPORE	IRELAND	NETHERLANDS

Big countries, small exports

13%	**13%**	**18%**	**20%**
U.S.	BRAZIL	JAPAN	INDIA

SOURCE WORLD BANK WORLD DEVELOPMENT INDICATORS (WDI)

To counteract such "globaloney," I offer two laws that govern, respectively, the depth and breadth of globalization:

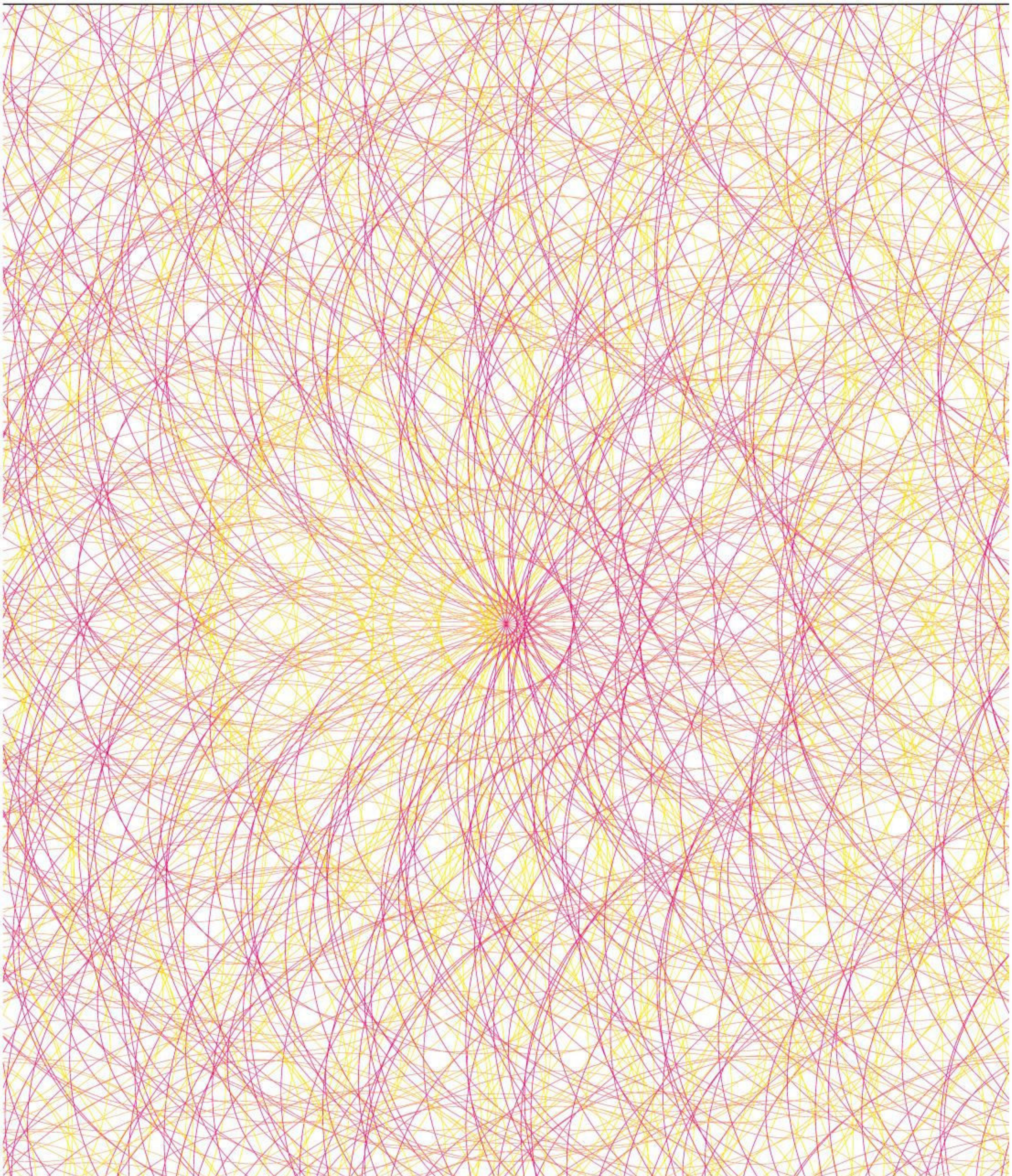
- The law of semi-globalization: International business activity, while significant, is much less intense than domestic activity.
- The law of distance: International interactions are dampened by distance along cultural, administrative, geographic, and, often, economic dimensions.

These principles, set out in my book *The Laws of Globalization,* can be very helpful for strategy making—if they can be counted on to apply in the future. Given surging protectionist sentiments and possibly even a trade war, will they continue to hold? The best way of stress-testing them—at a time when the precise policies of the Trump administration and other governments are still unclear—is to look at the last time a major trade war broke out, in the 1930s, which led to the largest reversal of globalization in history. Two major lessons, corresponding to the two laws of globalization, stand out.

The first lesson is that although trade dropped precipitously in the 1930s, it did not dry up entirely. The collapse that began in 1929 was staggering, and by early 1933, trade flows had plummeted by two-thirds. That said, the drop-off in value reflected a fall more in prices than in quantities, which declined by less than 30%. Even in the wake of the collapse, trade volumes continued to be far too large for business strategists to ignore.

The second lesson is that distance of various sorts continued to dampen international business activity. For example, from 1928 to 1935, the relationship between trade flows and geographic distance barely budged. The beneficial effects of a common language and colonial ties remained powerful: Country pairs with such ties continued to trade about five times as much with each other as pairs without such ties, all else being equal. The net result was that the trading partners with whom countries (or groups of countries) did most of their business before the crash remained largely unchanged afterward.

Getting back to the future: If global trade didn't screech to a halt in the 1930s, it's reasonably safe to say that it won't in the 2020s, either. In fact, analyses of what a trade war under Trump might look like suggest much smaller declines in trade than occurred in the 1930s. Moody's Analytics estimates that if the United States were to impose proposed tariffs on China and Mexico and those two countries retaliated in kind, that and other factors would shrink U.S. exports by $85 billion in 2019. That's only about 4% of total U.S. exports in 2015. Of course, a wider trade war would have a more significant effect, but it is very unlikely that the consequences would be as dire as in the 1930s.



ORGANIZING FOR SUCCESS

As companies reevaluate their globalization strategies in light of protectionist pressures, they should also think about structural changes that can help boost performance. While a country-centric structure makes sense if adaptation is a firm's only global strategy, companies would do better to adopt models that also support aggregation and arbitrage. Two are particularly worth highlighting:

Region-based structures. Organizing according to region allows companies to take advantage of similarities between neighboring countries. An analysis of 29 distance variables shows that in almost all cases countries from the same region average higher similarity scores than countries from different regions—and often by very wide margins. The (partial) caveat is that two vital regional agreements, the EU and NAFTA, are subject to considerable strains as of this writing.

Front-back structure. This variant on the matrix organization focuses on localizing at the front end (close to the customer) while employing a centralized back-end platform to support integration in R&D, production, support functions, and so on. Where the line is drawn can vary: Many companies integrate only back-office functions. Others—Uber and Airbnb, for example—go to market with IT platforms that enable rapid, asset-light globalization.

In addition to optimizing formal structures, companies should renew their commitment to tools that strengthen connective tissue throughout the corporation: a strong culture, internal diversity and mobility, and so forth. In today's environment of rising nationalist sentiment and sneers about "citizens of nowhere," companies must strengthen their focus on cosmopolitanism in top management—perhaps the dimension along which large companies are the least globalized.

Similarly, if the breadth of trade didn't change much despite the drastic declines in depth during the Great Depression, it probably wouldn't change much in the event of a trade war today. It is worth adding that with many more independent countries now, as well as more vertically fragmented supply chains, the estimated effects of geographic distance on merchandise trade are actually larger than they were in the 1930s.

WHERE TO COMPETE

If cross-border interactions in the aggregate are unlikely to fade away, what is the rationale for individual multinationals' pulling back? The recent *Economist* article on the retreat of global companies, which has stirred significant discussion, pointed to the performance problems they have experienced. But the declines over the past three to four years occurred in an environment of plunging commodity prices, dropping demand for globalization-related services, and, for U.S. companies, shifts in exchange rates—factors that clearly played outsize roles in the performance numbers. And longer-term declines over the past decade coincide with a period in which globalization actually slowed down.

To argue that poor performance problems over this period should force reconsideration of multinationalization would be like arguing that Singapore, the most deeply connected country in the world according to the DHL Global Connectedness Index, should pull back from globalization because of the growth problems it has experienced since the financial crisis. The latest report of Singapore's official Committee on the Future Economy dismisses that notion, saying that globalization through trade, capital, and knowledge flows is still the future, as far as Singapore is concerned. And even in countries much less dependent on exports than Singapore is, a wholesale pullback from globalization would be counterproductive.

Even when economic conditions are favorable and globalization is advancing rapidly, as was the case several decades ago, multinationals can face performance issues. My 2003 HBR article, "The Forgotten Strategy," notes that between 1990 and 2001, *Fortune* Global 500 companies consistently posted lower average returns on sales for their foreign operations than for their domestic ones. Given the difficulties implied by the law of distance, multinationalization has always been an option, not an imperative. Some firms—and industries—clearly overdid it, especially in the years leading up to the financial crisis.

What's lacking in much of the debate today is the notion of contingency: a case-by-case approach in which a globalization-related move is evaluated on its own merits rather than subjected to some sweeping injunction about whether to go forth and globalize or to come back home. That said, many multinational companies do need to pay renewed attention to where they compete—in other words, to market selection.

They must also resist the idea that a truly global company must compete in all major markets. Some 64% of the respondents to the 2007 HBR survey agreed with this (non)dictum, yet an analysis of internal financial data from 16 multinationals around that time indicated that eight of them had large geographic units that destroyed value after their financing costs were taken into account. Such problems still persist. Toyota, for example, seems to be the only major competitor in the highly globalized auto industry that has managed to build up significant market share in Japan, North America, and Europe and in key emerging economies—while remaining highly profitable. By contrast, most major automakers would be better served by following the example of GM, which shed its loss-making European operation, Opel, in March 2017.

Recent data on companies ranked among the top 100 with the most assets located outside of their home countries tells a similar story. While these companies tend to operate in dozens of countries, their top four markets—including their home market—account for about 60% of their revenues and probably a larger slice of total profits. And only a single-digit percentage of the *Fortune* Global 500—the world's largest firms by revenue—earn at least 20% of their revenue in each of the "triad" regions of North America, Europe, and Asia-Pacific.

In sorting out which markets to focus on, it's important to note that the law of distance applies to foreign direct investment as well as trade. Although FDI is less sensitive to geographic distance than trade is, I estimate the effect of a common language and a colony-colonizer link to be similar and FDI to be more sensitive to differences in per capita income.

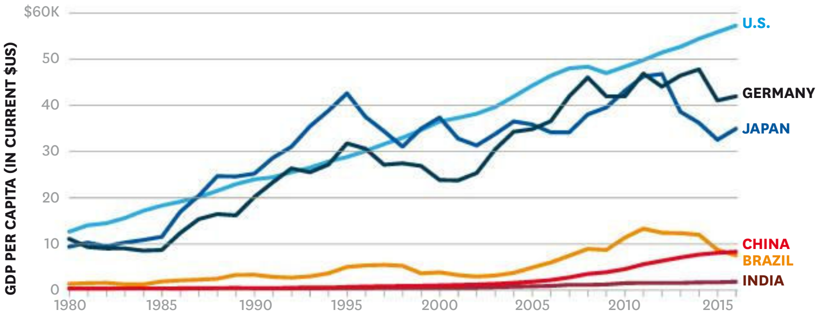
So as companies today weigh their options, they should look for opportunities where they can find cultural, administrative/political, geographic, and economic affinities. This resonates even more strongly as we recall that country relationships became even more important during the 1930s. As the political environment shifts, business leaders need to keep a careful eye on how their home countries are realigning their international ties, and engage in their own corporate diplomacy.

Remember too that staying at home is an option. Only about 0.1% of the world's firms are multinationals, although since multinationalization is highly skewed toward larger firms, this greatly understates their overall impact. (Their foreign affiliates generate 10% of global GDP, and the multinationals themselves account for more than 50% of world trade.) For companies based in large emerging economies, focusing on the domestic market, where they enjoy home court advantage as well as rapid growth, can be a particularly attractive proposition.

Of course, trade can occur without multinationalization, and this is what some tout as the wave of the future: The *Economist* points to "a rising cohort of small firms using e-commerce to buy and sell on a global scale." But e-commerce is still significantly less internationalized than off-line commerce. And in light of changes brewing in the policy environment, this seems like a particularly inauspicious time to think that one can go global just by setting up a website or joining an online platform.

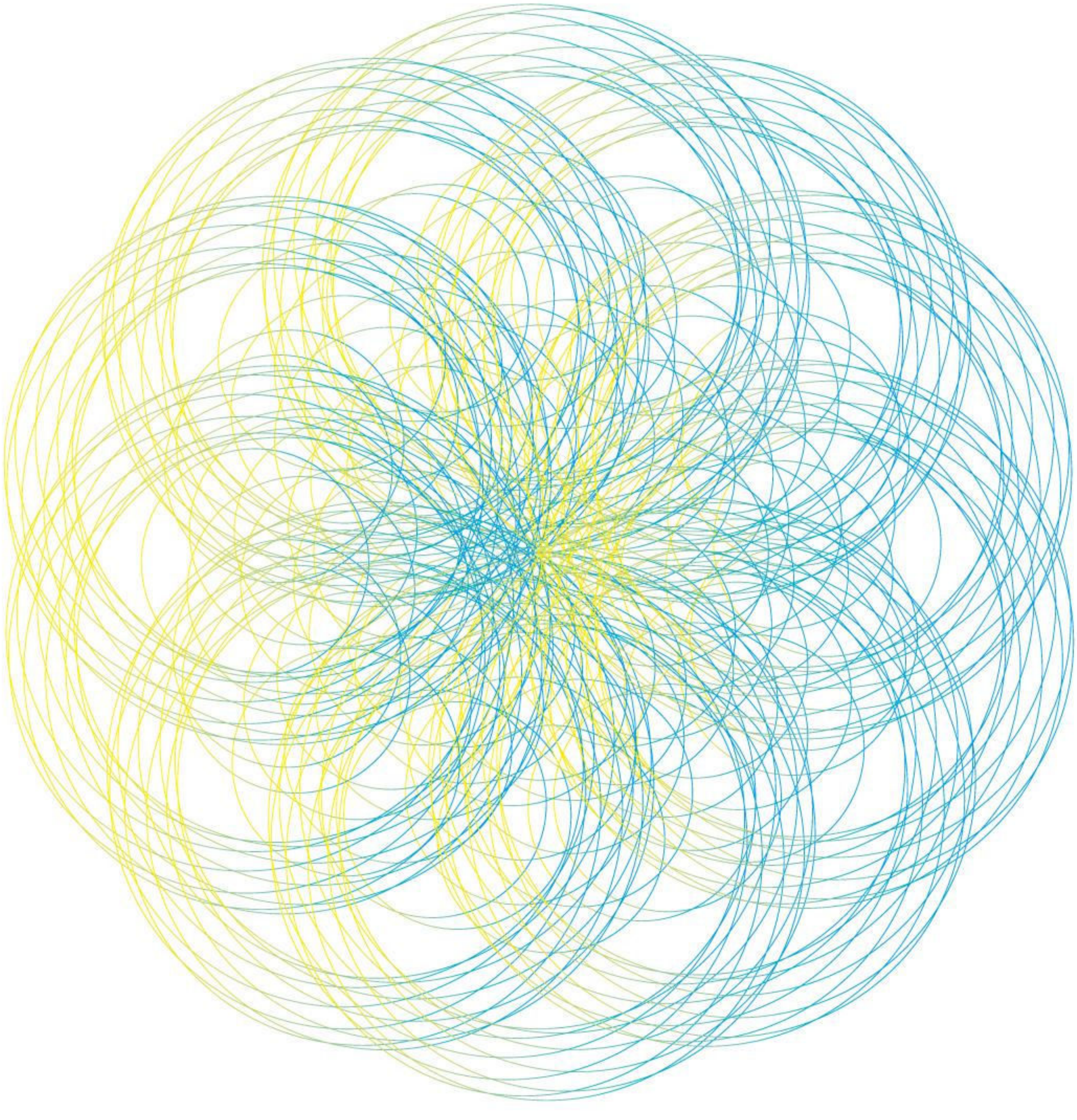
GROWTH IN EMERGING MARKETS HASN'T ERASED ARBITRAGE OPPORTUNITIES

Companies from advanced economies will continue to exploit differences in the cost of labor and other resources, and emerging markets will continue to benefit from selling into developed nations' markets.



SOURCE GENERATED BASED ON DATA FROM IMF WORLD ECONOMIC OUTLOOK DATABASE

LEADERS MUST RESIST THE IDEA THAT A TRULY GLOBAL COMPANY HAS TO COMPETE IN ALL MAJOR MARKETS.



WHAT ARE YOUR GLOBALIZATION OPTIONS?

ADAPTATION boosts revenues and market share by tailoring products and services to suit local tastes and needs.

AGGREGATION delivers economies of scale by expanding operations into regional or global markets.

ARBITRAGE exploits differences in labor costs, tax regimes, and other factors between national and regional markets.

HOW TO COMPETE

If you conclude that your company should continue to do business in a variety of markets, you still need to figure out whether to change the type or mix of strategies that you use in response to protectionist pressures. At a high level, globalization strategies have three components, as described in my 2007 book, *Redefining Global Strategy.*

Companies use *adaptation* when they want to adjust to cross-country differences in order to be locally responsive. They use *aggregation* to achieve economies of scale and scope that extend across national borders. And *arbitrage* strategies are used to exploit differences, such as low labor costs in one country or better tax incentives in another.

How companies should use these three strategies will change somewhat in a protectionist world—but perhaps less than you'd think. Take adaptation. Jeffrey Immelt isn't alone when he talks of his company's "bold pivot" away from aggregation and the importance of "localizing" in today's environment. Firms *should* look for opportunities to amp up their adaptation efforts, because becoming more responsive to differences can help reduce the impact of protectionism.

The most obvious way for a company to adapt is to vary products, policies, market positioning, and so on to suit local markets. However, each variation increases costs and complexity. Therefore, smart adaptation typically involves limiting the amount of variation as well as finding ways to improve the effectiveness and efficiency of any changes that are introduced. For example, companies can design common platforms upon which local variants are offered. Or they can externalize some of the costs of adaptation via franchising, joint ventures, or other types of partnerships.

But while more adaptation may make sense, multinationals should not automatically put it above all else—doing so would only undercut their sources of competitive advantage relative to local competitors. Global companies—especially those from advanced economies—typically justify their cross-border strategies primarily on the basis of aggregation. In the most classic cases, they invest in intangible technological or marketing assets that they can scale across national borders. Those advantages normally have to be pretty large in order to overcome the home court advantage of local competitors. The economic rationale for aggregation won't evaporate for multinationals that have built a healthy, profitable business in foreign markets—even if some countries make it more expensive to operate within their borders. Companies that have operations in markets where they're only marginally successful, on the other hand, may need to retrench.

Turning to arbitrage, the opportunities for vertical multinationals to globalize on the supply side rather than on the demand side have narrowed somewhat in recent years, but they still remain large. Even with rising prosperity in large emerging markets, U.S. GDP per capita is still seven times that of China, and 33 times that of India. Differences in tax regimes across countries are not going away either, and will continue to provide arbitrage opportunities. According to the OECD, the dispersion of corporate tax rates across countries has barely changed since 2007, and progress at curbing tax havens has been slow. Furthermore, cross-country differences in safety, health, and environmental standards continue to persist as well—although exploitation of these differences raises ethical concerns.

Multinationals coming out of emerging markets tend to get their start from advantages rooted in arbitrage—competing abroad on the basis of low costs at home. This strategy continues to be the engine that drives the growth and profitability of India's offshore IT services industry—which inspired Friedman's *The World Is Flat,* kicking off a wave of interest in arbitrage strategies. More than a decade later, programmers' salaries in India are still just a fraction of those in the United States, and cost reduction remains the top reason companies choose to outsource. The largest India-centric vendors have far outstripped their Western competitors in terms of both growth and profitability, and as of June 2016 the top four India-centric vendors enjoyed market valuations more than 50% larger than those of their top four Western competitors.

As companies from advanced and emerging countries joust for global leadership, each has to shore up its traditional weakness—for incumbents, that's arbitrage; for insurgents, it's aggregation. For example, developed-world incumbents in IT services, such as Accenture and IBM, have expanded their workforces in India, while Indian companies are trying to strengthen their brands and technological capabilities.

Returning to GE, Immelt's pivot toward localization does imply a boost to its adaptation strategy. But GE—like most other multinationals—cannot give up on aggregation or arbitrage. GE's aggregation-based advantages are what underpin its ability to compete across 170 countries. Its $5.5 billion R&D machine yields world-beating technological innovations, its $34 billion brand value opens doors everywhere, its famous management-training programs both attract and cultivate talent, and its scope across products, services, and geographies all contribute to GE's immense cross-border aggregation potential. And while Immelt's remarks shrewdly downplay wage arbitrage as "what GE did in the 1980s," in contrast to its current focus on selling more abroad, arbitrage has become sufficiently ingrained at the company over the past few decades that it will probably not disappear and will continue to be part of its globalization strategy. In my view, GE's "localization" strategy is best understood as one that retains a core strength in aggregation while toning down the company's prior emphasis on arbitrage and becoming more adaptive.

ENGAGING WITH SOCIETY

Along with where and how to compete, questions about how to engage with society are becoming increasingly prominent on business leaders' agendas. Except in highly regulated industries, companies have historically treated interactions with governments, media, and the public as an afterthought in setting strategy. But now, as Martin Reeves of BCG points out, "In many cases companies are seeing bigger impacts from political and macroeconomic factors than from competitive considerations." Those factors, he says, include Brexit-driven exchange rate movements, share price fluctuations in response to policy pronouncements, and the cost of changing investment plans in light of anticipated shifts in trade policy. I would add to the list the rise of NGOs, the proliferation of social media, and increases in anti-globalization sentiment.

Companies are constrained in their responses to these developments by a range of factors. First of all, the backlash against globalization is also—in part—a backlash against big business. The general reputation of business is at an all-time low. In a recent survey, the Pew Research Center asked respondents in the U.S. how much people in 10 occupations contributed to the well-being of society. Business executives ranked next to last, ahead only of lawyers. Just 24% of respondents said they thought business leaders contributed "a lot." The 2017 *Edelman Trust Barometer* also reports an all-time low for CEO credibility. And companies' decisions about how to deploy the reputational capital that they do possess are complicated by tensions between a country's citizens and its government—Uber CEO Travis Kalanick ran into problems with public perception when he joined Trump's business advisory council, for example—as well as by uncertainties about how the broader environment will evolve.

In such a context, just speaking up more about social issues—as business leaders today are often instructed to do—is no panacea. While it is hard to offer simple instructions about how to cope with these complexities, the law of semi-globalization does suggest one injunction and one insight. First the injunction: Falling in line with what governments want wherever a company operates is unlikely to be a sustainable strategy. Multinational companies need to craft governmental and societal agendas that are both localized and linked across countries. Anti-globalization pressures require that multinationals deliver more local benefits—and communicate about them—in the countries where they operate. Such efforts must go well beyond compliance to include contributions in the form of jobs, technology, and so forth.

Of course, there are dangers to shifting too far toward localization. Consider how IBM responded to the rise of the Nazi regime in Germany. Rather than pulling back—even as it became clear that the census IBM was supporting was being used to identify Jews for persecution—IBM sought to grow its business with the Nazi government. In 1937, then-CEO Thomas Watson was awarded—and accepted—a medal from Hitler for "service to the Reich." One would hope that such a strategy would not even merit consideration today.

The law of semi-globalization affords an important insight as well: Addressing much of our current malaise—including but not confined to anti-globalization sentiment—requires domestic policy changes rather than the closing of borders. For example, one of the principal complaints about globalization today is the sense that it has contributed to rising income inequality and that a large swath of the population in advanced economies has been left behind. In the U.S., income inequality has recently risen to levels last seen in the 1920s, and other countries, especially developed ones, have registered similar, if less dramatic, increases. Meanwhile, corporate profits are running close to their highest historical levels.

The widespread perception that globalization is primarily to blame for this problem, however, is empirically implausible. Most research suggests that technological progress and (in the United States) the decline of unions have been bigger contributors to inequality than globalization. Corroboration is supplied by real-world examples: If the Netherlands can preserve a more reasonable income distribution despite having a trade-to-GDP ratio six times that of the United States, it seems odd to blame globalization for the much higher level of inequality in the U.S. economy. And even if one is inclined to point fingers at globalization, it is clear that protectionism is a much more expensive solution than government safety nets, increases in the minimum wage, changes in tax policy, job-training programs, and the like. Such policies are not typically favored by big business, so corporate voices advocating them make a powerful statement. Furthermore, closing borders does nothing to prepare a country to deal with the automation-related threats to jobs that dominate the debate about the future of work.

My research into the 2011 book, *World 3.0: Global Prosperity and How to Achieve It,* offers an in-depth evaluation of the various harms attributed to globalization. (I expected the present backlash to arrive several years before it did.) Some, such as the risks associated with international imbalances in trade and investment, are indeed real and significant. Most others, however, turn out to be overblown in relation to actual levels of international integration. For example, the contribution of international air transportation to energy-related greenhouse gas emissions is only one-tenth as large as British air travelers estimated in a survey. To deal with global warming, it would be far more effective to tackle bigger sources such as housing or driving. My research suggests that international openness should be coupled with targeted domestic policies in addressing such side effects as globalization does have.

That perspective is, of course, the opposite of President Trump's apparent preference for domestic deregulation and international intervention, which brings me to my last point—which may seem politically partisan but is rooted in the common notion that a company's market and nonmarket strategy should be in alignment. If your company is or may eventually be global, it's not a good idea to actively support policies that build up barriers to trade and capital flows, make people less mobile, and delegitimize the idea that companies can contribute to the well-being of people in more than one country—even if all you care about is shareholder value. Over the long run, companies that rely heavily on sourcing from abroad (such as Walmart) and those that export far more than they import (such as GE) would benefit from joining forces to oppose protectionism.

THE BACKLASH AGAINST GLOBALIZATION IS ALSO—IN PART—A BACKLASH AGAINST BIG BUSINESS.

IN HIS CLASSIC 2006 *Foreign Affairs* article Samuel Palmisano, then chairman and CEO of IBM, pointed out that 150 years ago, companies that crossed borders engaged mostly in trade, but by the early 1900s, they had started to invest in localizing production. He also proclaimed the recent emergence of a new corporate form, the globally integrated enterprise, for which "state borders define less and less the boundaries of corporate thinking or practice."

From today's perspective, that seems too rosy by half. But there is some good news for those tasked with leading multinational companies. First, the global corporation never became nearly as integrated as Palmisano prophesied, so the amount of change required if globalization does go into reverse is less than people might think. Second, it's still unclear whether a retreat from globalization will occur: International activity has stagnated in recent years but has not fallen off significantly. And third, even if globalization suffered a violent reversal similar to that experienced at the beginning of the 1930s, the world would still remain more globalized in terms of trade and foreign direct investment than it was in the 1920s, let alone in the 19th century. So reverting to the multinational structure of 100 years ago or the trade-based structures of 150 years ago strains plausibility. Globalization strategy and practice have advanced well beyond the prescriptions those historical models would imply, and leaders would be ill-served by going backward.

HBR Reprint R1704J

PANKAJ GHEMAWAT is the Global Professor of Management and Strategy and director of the Center for the Globalization of Education and Management at New York University's Stern School of Business, and the Anselmo Rubiralta Professor of Global Strategy at IESE Business School in Spain.

FURTHER READING

World 3.0: Global Prosperity and How to Achieve It
Pankaj Ghemawat
Harvard Business Press, 2011

"Managing Differences: The Central Challenge of Global Strategy"
Pankaj Ghemawat
HBR, March 2007

"The Cosmopolitan Corporation"
Pankaj Ghemawat
HBR, May 2011

"The Globally Integrated Enterprise"
Samuel J. Palmisano
Foreign Affairs, May/June 2006

"Why Your Company Needs a Foreign Policy"
John Chipman
HBR, September 2016

Making Sense of **Digital Labor**

The forecasts are breathtaking. Building on fast-evolving technology like artificial intelligence, natural language processing and machine learning, software "robots" will augment or replace many knowledge workers around the globe, lowering business costs and improving productivity.

By Cliff Justice

Principal, Innovation & Enterprise Solutions,
KPMG LLP

Will it happen? Yes. Business process applications and computer intelligence are converging, promising a world where cognitive systems handle many business processes now done by humans—faster, with fewer errors. Forerunners of this sci-fi-like digital labor are already at work at select companies copying and pasting order information into spreadsheets, answering customer questions in call centers and helping technicians diagnose equipment maintenance issues. At KPMG, we're investing in these advanced technologies to improve the efficiency, effectiveness and quality of the work we do for clients every day.

Most companies understand they can't ignore these developments, but many are uncertain about where to begin or how to manage the fallout among their workforce. Here's a reassuring truth. While technological change can indeed make an impact quickly, it almost always happens incrementally. Uber seemingly disrupted the taxi business overnight, but it wasn't possible before the Internet, high-speed mobile communications, cloud computing, big data, distributed storage and advanced data analytics enabled its platform. Digital labor, too, will develop in stages—even if they move quickly—giving businesses time to start small and work toward increasingly sophisticated applications. And while some companies may find it makes short-term economic sense to reduce their workforce, others will surely find it smarter to deploy displaced workers into higher-value activities.

> *"At KPMG, we're investing in these advanced technologies to improve the efficiency, effectiveness and quality of the work we do for clients every day."*

In fact, we believe many companies will find that digital labor acts less as a displacer of employees, especially in its earliest iterations, and more as an assistant, allowing people to do their jobs faster, more thoroughly and more accurately—and to spend more time on work that makes a difference. As cognitive technologies become more sophisticated, they promise to create knowledge at an explosive rate and help companies innovate faster. Viewed this way, digital labor is not so much a threat to the human workforce as it is the next evolutionary step toward ever smarter, productive and innovative employees.

This is what we are finding at KPMG, where we are investing heavily in cognitive technologies, including IBM Watson, to supercharge our audit capabilities. For example, a typical audit today covers a statistically valid sample of data, but we see that cognitive systems could analyze the full population of available data—financial and non-financial. The result: more accurate audits; more granular audit reports; deeper insights into client controls, accounting practices and reporting processes; and a broader perspective on risk.

For companies eager to take advantage of digital labor, we suggest a three-step approach. Think about how digital labor could impact your business, and develop a business case for its application. Prioritize pilot projects, in which cognitive technologies can be used to automate strategic business activities, and leverage your findings to develop a short- and medium-term roadmap. Finally, develop a longer-term vision for your digital labor strategy and communicate it to your organization.

The time to start is now. Digital labor's entry into the workforce will be incremental, but it will be fast. How quickly you segue from a labor-centric to a technology-centric business process model will help determine where you rank among tomorrow's winners.

To learn more about getting started with digital labor, please visit KPMG.com/us/digitallabor.

“DON’T TRY TO PROTECT THE PAST”

A CONVERSATION WITH
IBM CEO GINNI ROMETTY

BY ADI IGNATIUS

DAVID BECKER/BLOOMBERG

When Virginia "Ginni" Rometty became the CEO of IBM, in early 2012, she dutifully adopted her predecessor's strategy. Sam Palmisano, who held the position for a decade, had vowed in 2010 that IBM would roughly double its per-share earnings within five years. Two-plus years into her tenure, Rometty concluded that trying to meet that goal would end up crippling IBM's efforts to reinvent itself. She abandoned the plan in October 2014, thereby taking full ownership of the company's future strategy and financial health. It's been an interesting ride ever since. Rometty, 59, is on a protracted mission to make IBM a cloud-based "solutions" business. She has invested billions in advanced technologies while selling off legacy divisions that don't fit the new model.

IBM is still hugely profitable, with net income in 2016 of $13.0 billion on revenue of $79.9 billion. But it's also still a work in progress. Amid the transformation, the company has suffered 20 consecutive quarters of falling revenue. Rometty says the decline is due primarily to her selling off legacy businesses and to unavoidable currency hits. Moreover, she says, moving to new, higher-margin businesses requires some short-term pain. "My job is to build an IBM that's durable," she says.

So far her board has been supportive. Despite the shrinking revenue, it recently raised Rometty's pay package to $33 million, making her the eighth-highest-paid CEO in the United States. The question is whether investors will remain as patient. In May, IBM's biggest shareholder, Warren Buffett, said he had dumped about 30% of his holdings, noting that the company faces "some pretty tough competitors." Rometty, who also serves as IBM's chairman and president, seems undaunted. She says IBM's ability to change is "in its DNA." She should know. She has spent 36 years at the company and earned her stripes developing IBM's business-services division and leading the successful purchase and integration of PwC Consulting.

Now she is betting the farm largely on Watson, IBM's artificial intelligence platform. Watson debuted in 2011, when it took on two former champions of the TV quiz show *Jeopardy!* Watson won, demonstrating just how far machine learning had come. IBM commercialized Watson two years later, and its big brain now does everything from advising doctors on cancer treatment to predicting the weather.

Rometty met with HBR in her office at IBM's leafy headquarters in Armonk, New York.

"WATSON, OUR ARTIFICIAL INTELLIGENCE PLATFORM, WILL TOUCH ONE BILLION PEOPLE BY THE END OF THIS YEAR."

ANDREW HARRER/BLOOMBERG

HBR: You've been running IBM for more than five years now, overseeing big changes. Do you view this process as a turnaround?

ROMETTY: I wouldn't use that term. This is a transformation. We're a 106-year-old technology company, and we're the only tech company that has moved from one era to the next. When you're in tech, you have to transform.

How much transformation can your employees and investors handle? When will you be able to declare that you've made it to the other side?

That's a good question. Let me answer in a couple of ways. First, you need to be clear about what you are transforming to. For us, it's all about data, and we have a very clear view of what our enterprise clients will need. When people talk about data, they often mean things that are searchable via public search engines. But that's only 20% of the data in the world. What we're trying to unlock is the 80% that's behind everyone's firewalls, because that's where the value is. Everybody has tons of data; they just can't make use of it. Our belief is that you'll make better decisions if you can unlock that data and that there's a $2 trillion market around better decision making. That's the market we are going after.

How do you know you're on the right strategic path? And are you making changes as you go?

Oh, goodness, have I made changes! It's important to have deeply held beliefs about the vision. But then you have to look at the results. I'm confident about where we are at this point. Our new businesses around cloud, data, and security add up to almost $34 billion in revenue. They're growing at 13% to 14% a year and make up 42% of the company. Watson, our artificial intelligence platform, will touch one billion people by the end of this year. I consider these numbers proof that we're on the right track.

Yet you've had 20 consecutive quarters of revenue decline.

Yes, but that includes divestitures and the strong U.S. dollar. Currency is responsible for $14 billion of that decline. And I divested $8 billion to $9 billion worth of revenue sources. So that is the bulk of it.

However you account for it, is this extended revenue slide part of the plan? Or is it a disappointment?

What's positive is that the plan is proceeding as we believe it should, with the growth of large new businesses that are adjacent to our core franchises. IBM will grow again. But we need to grow in the right ways. We're moving into areas that have value and shedding ones that don't. We could have higher growth rates, but we made a bold decision to divest commoditizing businesses before they commoditize further. The new areas are higher margin, but we have to invest in them and then scale them up.

Warren Buffett just sold a big chunk of his IBM holdings. Does he not get it?

I never talk about our shareholders; they can speak for themselves. But our clients vote through their use of our offerings, and they are showing that we're on the right track. H&R Block, for example, took Watson for the tax season to assist its professionals in handling millions of customers. The company gained market share and had an unbelievable Net Promoter Score.

ONGOING TRANSFORMATION

IBM's former CEO Lou Gerstner came from the outside and pretty much wrote the playbook on how to transform a company. Is it harder to accomplish something like that when you've already been at the company for a few decades?

I don't think it's any harder. I really believe the company has in its DNA the ability to change. We've done it over and over again. And Lou would agree that this is a more extensive transformation because of the convergence of multiple trends that are accelerating the pace of change. It doesn't matter if you're an insider so long as you don't try to protect the past. Then you have the freedom to reinvent yourself for the long term.

What's the hardest thing about trying to take this transformation through to the other side?

You have to have passion. And you have to have clarity. But I think the most difficult thing is perseverance. This is a large, highly profitable company that continues to do mission-critical work serving clients around the world—and at the same time reinventing itself. As the familiar metaphor has it, that's like changing the wheels while you're driving. And we're doing it all in the public eye. Above all, we need to stay focused on our clients and keep moving forward. I think the team has done a super job at this.

Do you feel pressure to get this done quickly?

Sure we do. Every leader wants things to go faster. You have to set the bar high and keep moving faster. But my job is to build an IBM that's durable for a whole era. We take seriously our ongoing responsibility to the clients that run our systems today, to make their work more productive. Supporting those clients takes my revenue down, but I'm proud of it: We run the world's systems. Without IBM, banks couldn't operate. Railroads couldn't move. Airlines couldn't fly.

Don’t you worry that advances in cloud-based computing and data analytics could commoditize some of your new areas of growth?

I don’t. Our analytics business is worth more than $19 billion. So there’s no problem there. The cloud is accretive to our services business, which makes up 60% of IBM. And the cloud works in a standardized way, which means the margins can be higher. Most important, we believe that the basis of competitive advantage in the future will be data. As I’ve said before, data is the next natural resource. Think of oil. Where it sits is not necessarily where the wealth is. The wealth goes to whoever can refine it, process it, and turn it into something else.

How is transformation affecting your processes and your people?

For starters, we’ve adopted “design thinking” in our offices around the world. The goal is to make our B2B products as consumerish as possible in terms of ease, feel, simplicity. Then, to increase our speed, we’ve adopted agile work flows in every part of the company. And we’ve changed the tools we use, forming partnerships with Box, Apple, Slack, and others. We now have probably one of the most modern work environments in the world. And we’re doing this with a workforce of 380,000 people.

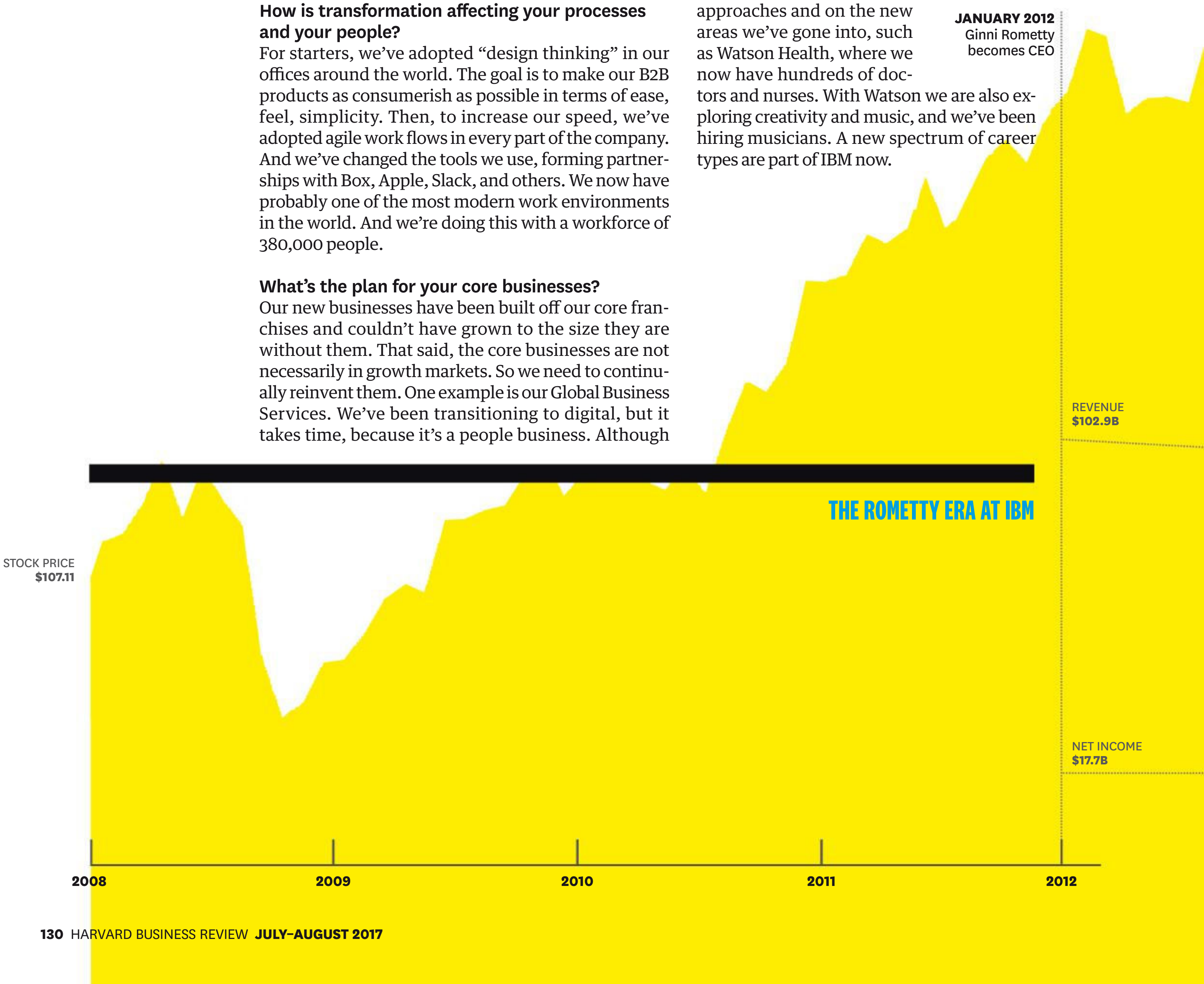
What’s the plan for your core businesses?

Our new businesses have been built off our core franchises and couldn’t have grown to the size they are without them. That said, the core businesses are not necessarily in growth markets. So we need to continually reinvent them. One example is our Global Business Services. We’ve been transitioning to digital, but it takes time, because it’s a people business. Although areas like that aren’t big growth markets, they are big cash producers, and they do mission-critical work for our clients.

BUILDING THE RIGHT TEAM

In a fast-paced environment like this, how do you construct the right management team?

I’ve brought in five direct reports from the outside, because you need people who really understand how the new systems work. About 15% of IBM’s managers up and down the company came from the outside. That adds up to a lot of people when you consider our size. We’ve spent $2 billion in the past three years on training in new methods and approaches and on the new areas we’ve gone into, such as Watson Health, where we now have hundreds of doctors and nurses. With Watson we are also exploring creativity and music, and we’ve been hiring musicians. A new spectrum of career types are part of IBM now.



THE ROMETTY ERA AT IBM

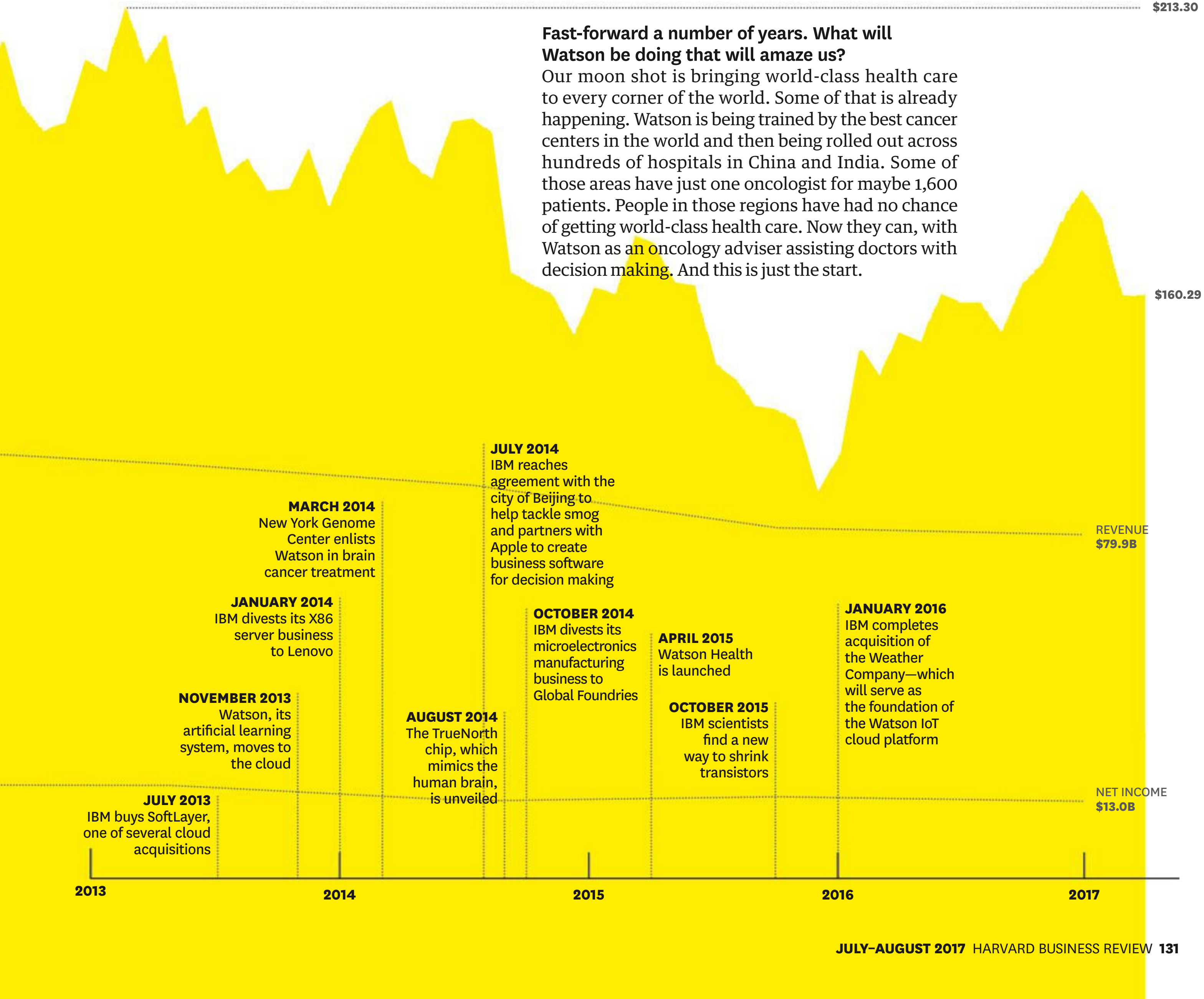
Aside from such specialties, what are the attributes you look for in new hires?
The attributes we care most about are intelligence and adaptability. Our own Watson is helping us predict people's propensity to learn.

WATSON'S ROLE

What makes Watson different from other AI platforms?
First of all, Watson is able to deal in vertical domains. It understands the languages of medicine, financial services, underwriting, and so on. That is extremely difficult to achieve, and it's a differentiation. Second is our business model: We ensure that Watson protects clients' insights. When a client brings its data, the insights go only to that client. Third is the range of data that Watson can deal with, including sight, sound, speech.

What does all this look like in practice?
Think about a conversation. Generally, people miss about 5% of the words. Watson is at 5.5%. That makes it number one in the field. It can also sense motion; the Watson Internet of Things group has developed for customers applications such as cognitive ball bearings, which use sensors to record work-process data. And Watson can "see." In analyzing melanoma, for example, Watson achieves 95% accuracy. Try to do this task with other systems, and at best they'll score 50/50.

Fast-forward a number of years. What will Watson be doing that will amaze us?
Our moon shot is bringing world-class health care to every corner of the world. Some of that is already happening. Watson is being trained by the best cancer centers in the world and then being rolled out across hundreds of hospitals in China and India. Some of those areas have just one oncologist for maybe 1,600 patients. People in those regions have had no chance of getting world-class health care. Now they can, with Watson as an oncology adviser assisting doctors with decision making. And this is just the start.



JULY 2013 IBM buys SoftLayer, one of several cloud acquisitions

NOVEMBER 2013 Watson, its artificial learning system, moves to the cloud

JANUARY 2014 IBM divests its X86 server business to Lenovo

MARCH 2014 New York Genome Center enlists Watson in brain cancer treatment

JULY 2014 IBM reaches agreement with the city of Beijing to help tackle smog and partners with Apple to create business software for decision making

AUGUST 2014 The TrueNorth chip, which mimics the human brain, is unveiled

OCTOBER 2014 IBM divests its microelectronics manufacturing business to Global Foundries

APRIL 2015 Watson Health is launched

OCTOBER 2015 IBM scientists find a new way to shrink transistors

JANUARY 2016 IBM completes acquisition of the Weather Company—which will serve as the foundation of the Watson IoT cloud platform

Do you worry that Watson and other AI programs will wipe out entire categories of jobs?
There will be an impact, of course. But in many cases AI will automate only parts of jobs, meaning people can do the rest of their jobs better. Over the years, I've watched professionals—chemists, researchers, doctors, financial analysts—say, "Uh-oh, I'm going to be replaced." And eventually they end up saying, "I can't do my job without this technology." That's what always happens when there's a dislocation in technology: We learn what it is that man innately does better.

To what extent is IBM trying to write the rules of human-AI interaction?
We're leaders in the field, and we will have influence over these technologies. In January we published our "Principles for the Cognitive Era." There are three tenets. The first is *purpose:* We believe that "cognitive" will augment humans and extend what they do, not replace them. The second is *transparency:* We need to be able to tell people not just how and when our technologies are being used, but also how they were trained and by whom. If you're sick and Watson is assisting your doctor, you want to know that it was trained by the 20 best cancer centers in the world. The third is about *skills:* We need to help prepare a whole new cadre to live in this world. We're working with 50,000 kids in 100 high schools to help build these skills.

> **"OUR MOON SHOT IS BRINGING WORLD-CLASS HEALTH CARE TO EVERY CORNER OF THE WORLD."**

ENGAGING ON THE ISSUES

You've decided to engage with the Trump administration, even though some of your employees oppose that. What have you learned from trying to navigate the new political era?
I wrote a letter to employees noting that IBM CEOs have interacted with every president since Woodrow Wilson. My view is that you have to be engaged on the issues that matter so that you can have influence. You need a seat at the table to advocate for what's really important to your company—and to the world. But we stand up for policies and positions, not for politics. In fact, we're one of the few companies in our industry that don't make political contributions.

Let's talk about gender. Some female executives like talking about gender issues, and some don't, preferring to be judged solely on their records. Where do you come down?
In the past I would have said I wasn't interested in the topic. I would rather have people just look at me for what I'm capable of doing. But some years ago I realized that wasn't a sufficient answer. I was in Australia making a presentation, and a man came up to me at the end and said, "I really wish my daughter could have been here." I realized that whether I like it or not, I have to be a role model. Women and girls need role models. There aren't enough out there.

Have you faced gender-related challenges in your career?
My biggest obstacles were self-imposed, which I think is true for many women. I often tell the story of how, years ago, my boss offered me a big promotion. I told him I wasn't sure I was ready—that I needed two more years to prepare and become more confident. Later I spoke to my husband, who asked, "Do you think a man would have responded that way?" And I said, "No, he wouldn't have." The next day I accepted the job.

So what's your advice to women who are facing such a challenge?
You have to learn to be comfortable with being uncomfortable, or you won't grow. I often ask people, "When do you feel you grew the most during your career?" They typically mention a time when they took a risk. Growth and comfort never coexist. If you're not nervous about something, it means you're not learning.

Is that why there are so few female CEOs? Women are holding themselves back? Or do you think something else is going on?
There are many reasons. One thing we've worked on at IBM is keeping women in the workforce. Many women deal with realities such as having children, taking care of elderly parents, or coming in and out of the workforce, and we focus on flexible programs that help keep women in the leadership pipeline. We also have to deal with the issue of bias. For every open position, you have to demand a diverse slate of candidates. And I'm talking not only about racial and gender diversity but also about diversity of thought. You need to be sure that your people are comfortable speaking up. As we say at IBM, "Treasure wild ducks."

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Harvard Business Review

JULY–AUGUST 2017

Experience

MANAGING YOURSELF The Science of Pep Talks
CASE STUDY Follow Dubious Orders or Speak Up?
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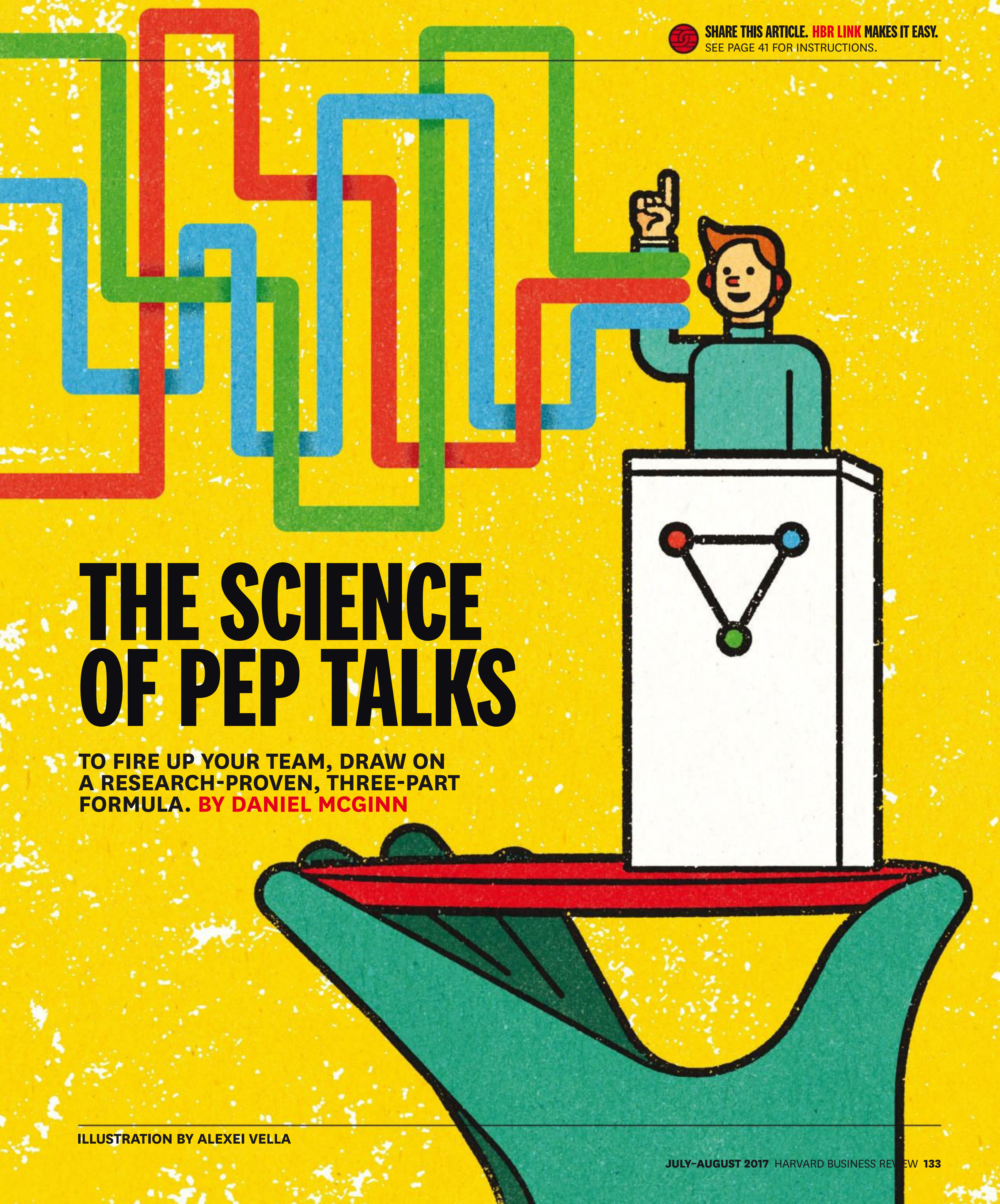


THE SCIENCE OF PEP TALKS

TO FIRE UP YOUR TEAM, DRAW ON A RESEARCH-PROVEN, THREE-PART FORMULA. BY DANIEL MCGINN

ILLUSTRATION BY ALEXEI VELLA

ERICA GALOS ALIOTO stands in front of 650 sales reps in the New York office of Yelp, the online review company, wearing a pair of shiny gold pants that she calls her lucky LDOM pants. LDOM is Yelp's acronym for "last day of the month," and for Alioto, senior vice president for local sales, it means giving a speech that will motivate her sales force to cold-call 70 potential customers each and close deals before the accountants finalize that month's books.

She speaks for 20 minutes, extolling the group for being Yelp's top sales producer. She namechecks the best performers on the team and suggests ways for everyone else to adopt the same mentality. She tells stories. She asks questions.

"This office is currently $1.5 million away from target this month.... We have an action plan here. Are we going to execute?" There's moderate applause. She asks again, in a louder voice: *"Are we going to execute?"* Big applause.

Alioto has worked hard to perfect these speeches because she knows her success depends on them. Indeed, the ability to deliver an energizing pep talk that spurs employees to better performance is a prerequisite for any business leader. And yet few managers receive formal training in how to do it. Instead, they learn mostly from mimicry—emulating inspirational bosses, coaches they had in school, or even characters from films such as *Glengarry Glen Ross* and *The Wolf of Wall Street*. Some people lean on executive coaches for help, but often the advice rests on the coaches' personal experience, not research.

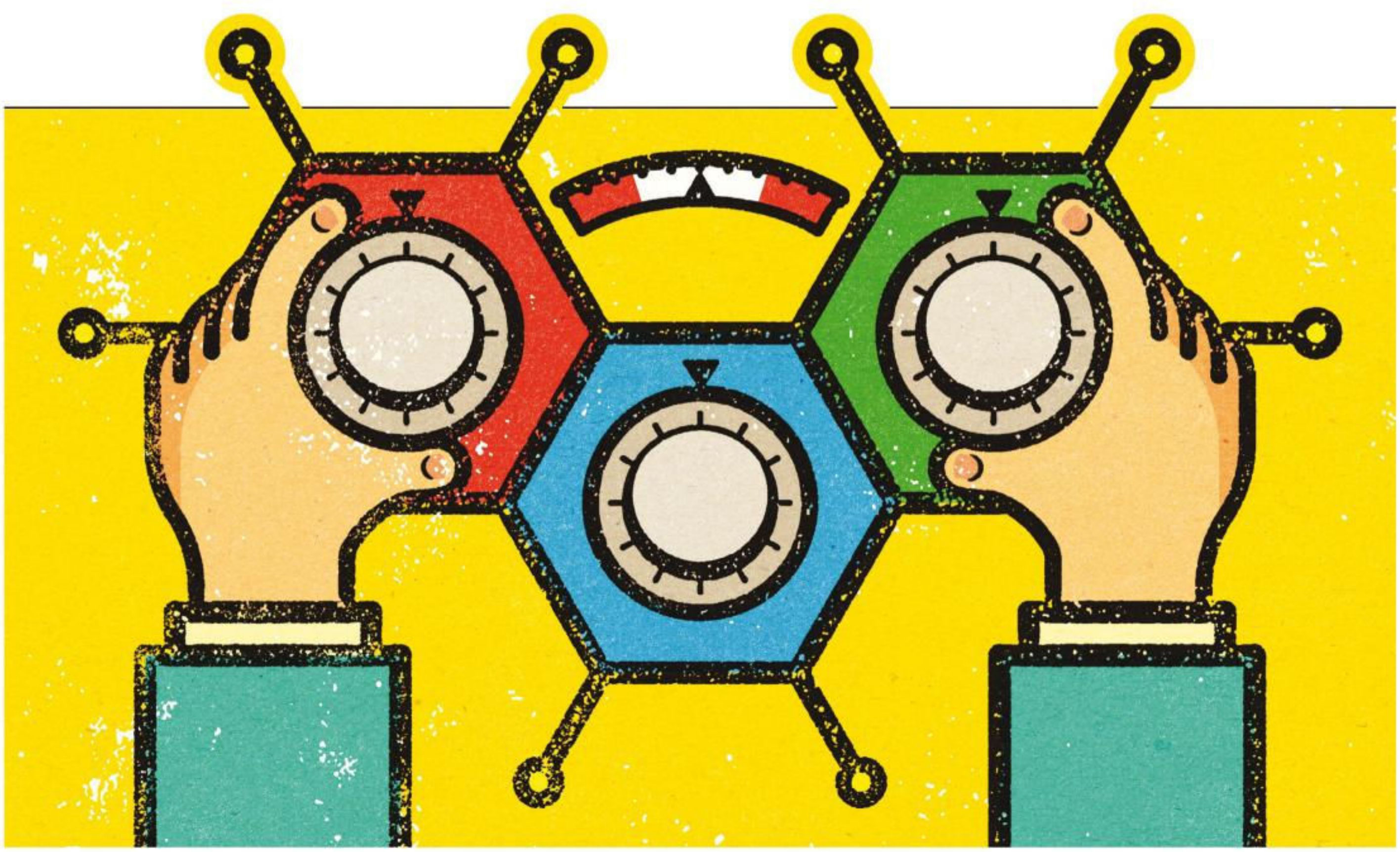
There is, however, a science to motivating people in this way. To better understand the various tools that help people get psyched up in the moments before important performances, I talked extensively with academics and practitioners in business and a variety of other fields. I discovered that while every individual has his or her own tips and tricks, according to the science, most winning formulas include three key elements: direction giving, expressions of empathy, and meaning making. The most extensive research in this field—dubbed motivating language theory, or MLT—comes from Jacqueline and Milton Mayfield, a husband-and-wife team at Texas A&M International University who have studied its applications in the corporate world for nearly three decades. Their findings are backed by studies from sports psychologists and military historians. And all the evidence suggests that once leaders understand these three elements, they can learn to use them more skillfully.

THREE ELEMENTS, CAREFULLY BALANCED

The Mayfields describe direction giving as the use of "uncertainty-reducing language." This is when leaders provide information about precisely *how* to do the task at hand by, for example, giving easily understandable instructions, good definitions of tasks, and detail on how performance will be evaluated.

"Empathetic language" shows concern for the performer as a human being. It can include praise, encouragement, gratitude, and acknowledgment of a task's difficulty. Phrases like "How are we all doing?" "I know this is a challenge, but I trust you can do it," and "Your well-being is one of my top priorities" all fit into this category.

"Meaning-making language" explains why a task is important. This involves linking the organization's purpose or mission to listeners' goals. Often, meaning-making language includes the use of stories—about people who've worked hard or succeeded in the company, or about how the work has made a real difference in the lives of customers or the community.



A good pep talk—whether delivered to one person or many—should include all three elements, but the right mix will depend on the context and the audience. Experienced workers who are doing a familiar task may not require much direction. Followers who are already tightly bonded with a leader may require less empathetic language. Meaning making is useful in most situations, but may need less emphasis if the end goals of the work are obvious.

For example, the Mayfields studied the CEO of a California pharmaceutical start-up focused on drugs to alleviate heart disease and amyotrophic lateral sclerosis (ALS). Many of the company's employees have lost loved ones to these ailments, so they bring an unusual sense of purpose to their work. As a result, at all-hands meetings, the CEO can easily make statements like this: "I know everybody here wants to help save lives and make people's lives better. That's what our work is all about."

In contrast, the supervisor of a fast-food restaurant speaking to part-time teenage employees will need to work harder to incorporate all three elements of motivating language theory into his chats with staff, but he can't rely solely on direction giving. Milton Mayfield suggests empathetic lines: "I know this work is difficult; you go home every night smelling of grease, and you're working so late that you're up until midnight finishing your homework." Or, to creatively link labor to purpose, the supervisor might say: "Our goal as a company isn't just to provide people with fast, satisfying meals; it's also to provide good, stable jobs so that employees like you have money to help your families, to save for college, or to enjoy yourselves when you're not at work. The more you help this restaurant meet its goals, the better we'll be able to continue doing that." According to the Mayfields' research, meaning making is almost always the most difficult of the three elements to deliver.

ACCORDING TO THE SCIENCE, MOST WINNING FORMULAS INCLUDE THREE KEY ELEMENTS: DIRECTION GIVING, EXPRESSIONS OF EMPATHY, AND MEANING MAKING.

Research from other fields offers additional insight into what gives the best pep talks their power. Tiffanye Vargas, a sports psychology professor at California State University at Long Beach, has published a half-dozen lab and field studies exploring which types of speeches best motivate athletes in different situations, some of which may also be applicable to business contexts. Her research suggests that across a variety of sports, coaches' pregame remarks do matter: 90% of players say they enjoy listening, and 65% say the speeches affect the way they play. She's found that people prefer an information-rich (uncertainty-reducing) speech if they're playing an unknown opponent or a team to which they've narrowly lost in the past. (For example: "We're going to beat this team with tough man-to-man coverage. Joe, your job is to neutralize that shooting guard; Jimmy, you box out that star rebounder on every play.") If a team is an underdog or playing in a high-stakes game, a more emotional pep talk (with more empathetic and meaning-making language) is more effective. (For example: "We've exceeded all expectations in this tournament. No one expects us to win. But *I* expect you to win. I know you can win.

You have to win. For your teammates, for the fans—because you deserve this victory.")

Military speeches also tend to use the three elements of MLT in varying proportions, even if the terminology is different. When Keith Yellin, a former officer in the U.S. Marine Corps and the author of *Battle Exhortation: The Rhetoric of Combat Leadership,* analyzed precombat speeches dating back to the ancient Greeks and Romans (including literary accounts, such as the "Once more unto the breach" oratory in Shakespeare's *Henry V*), he found 23 "common topics" that generals call on. These include language that qualifies as direction giving ("Follow the plan"), but most of the themes appeal to soldiers' reason (by comparing their superior army to opponents' weaker forces) or emotions (by saying God is on their side or by highlighting the evilness of the enemy). Since the soldiers are about to risk their lives, it makes sense that a commander would focus on the larger purpose of the battle and why the risk is worthwhile.

At the same time, Yellin acknowledges that precombat oratory is less common today than in earlier wars, and its balance of elements has shifted. That's partly because today's armies are stealthy (limiting opportunities for speeches), but it's also because they're now more professionalized, made up mostly of career soldiers who voluntarily enlisted, rather than civilian soldiers or draftees. While new recruits might still benefit from rah-rah pep talks, seasoned soldiers already know their purpose and don't need as much empathy.

Stanley McChrystal, the retired four-star general who oversaw special operations in Iraq and Afghanistan, echoes this view. "If you went out with Delta Force or the Rangers or the SEALS in this last war, we were fighting every night," he says. "Stuff is happening so fast, they're all business." Earlier in his career, however, when he was leading younger soldiers, he relied more on emotion and meaning: "During the last 30 minutes or so [before a mission], it was more about building the confidence and the commitment to each other." He says he tended to start with direction giving ("Here's what I'm asking you to do") but quickly shifted to meaning making ("Here's why it's important") and empathy ("Here's why I know you can do it" and "Think about what you've done together before"), and then ended with a recap ("Now let's go and do it").

The upshot of all this research and anecdotal evidence is that leaders in any context need to understand each element of motivating language theory and be conscious of emphasizing the right one at the right time.

PUTTING THEORY INTO PRACTICE

Alioto, the Yelp sales leader, has never studied the Mayfields' work, but she seems to have adopted the framework on her own. She leads with empathy—thanking the entire team for its hard work, singling out people or small teams who've been crushing it, and emphasizing that if one Yelp salesperson can put up spectacular numbers, all the reps are capable of it, since they have similar skills and training. After reading a transcript of her talk, the Mayfields point to this line in particular: "No matter what's happened to you up to this point in the month, you can make it a successful day." Then she shifts to direction giving, offering insight on a basic informational concept—often dealing with having the right mindset or a commitment to act. For example, she tells the reps to write one goal for the day on a Post-it and stick it on their computer.

GRADING A SALES LEADER’S PEP TALK

HBR asked Milton and Jacqueline Mayfield to evaluate how well Yelp sales leader Erica Galos Alioto used motivating language theory with her team. They highlighted the three elements—green for direction-giving language, blue for empathetic language, and red for meaning-making language—and offered comments on her approach. Edited excerpts follow.

Let me just say how impressed I am with this group.... Thank you for being the top office in Yelp right now, and for welcoming me with such incredible energy.

Right now the New York office is leading the company with 104% of quota, and there are two days left in the month. That’s absolutely insane.... Colleen is at $80,000. I tried to say hello to her yesterday, but she was on the phone, pitching like a madwoman, so I couldn’t....

🟦 PRAISING THE GROUP AND INDIVIDUAL CONTRIBUTIONS

Everybody knows how amazing the last day of the month is in the New York office. But LDOM isn’t really about the day of the month. It’s about how we approach that day. There’s something about that particular day that makes us come in with the ridiculous amount of grit and determination, the ability to make the unthinkable happen, the energy to achieve just about anything so that no matter where we are in relation to quota, we’re going to win. All those people who’ve been telling us no all month long—we’re going to turn that around and get a yes....

🟥 PORTRAYING LDOM AS A TRANSCENDENT EVENT AND CONNECTING THE REPS’ ACTIONS TO A LARGER GOAL

🟦 ACKNOWLEDGING THAT SOME PEOPLE ARE LAGGING, BUT EMPHASIZING THEIR SELF-EFFICACY AND RESILIENCE

Hopefully everybody has a pen and paper. I want you all to take a moment and write down what success looks like for you today. It may be how many business owners you talked to, or how many hearts and minds you won.... Write it down.

🟩 OFFERING SPECIFIC GUIDANCE ON HOW TO APPROACH THE DAY’S TASK

When you woke up this morning, what was your mentality? Sometimes we get into negative self-talk. Sometimes it may sound like this: “Why is Jon at target today? He must have a really great territory.” Sometimes we believe if somebody is achieving something that we’re not, it must be because the other person has some advantage.

🟦 RECOGNIZING EMPLOYEES’ TENDENCY TO GET DISCOURAGED, RATHER THAN BE EMBOLDENED, BY COLLEAGUES’ SUCCESS

Guess what? We also have plenty of examples of what people think of as a bad territory, and we put somebody new on it, and they go out and absolutely crush it.

If there’s anything negative in your thinking, I encourage you to turn that thinking on its head. Instead of looking at the differences between you and somebody else with a lot of success, look for similarities.

🟩 INSTRUCTING REPS TO AVOID NEGATIVITY

We’ve got two days to make it happen. Everything you do today, every action you take to make that successful outcome, every time you pitch, every business owner you talk to, every time you encourage a teammate to be better, every time you win the heart and mind of a business owner, you’re not only helping yourself—you’re helping your team, you’re helping your office, you’re helping your company, and you’re helping Yelp get where it wants to be.

🟥 CONNECTING TODAY’S WORK TO THE COMPANY’S LARGER GOAL

Alioto ends with meaning making—an emotional rallying cry that connects LDOM to a bigger goal and leaves the group energized: “Every time you win the heart and mind of a business owner, you’re not only helping yourself—you’re helping your team, you’re helping your office, you’re helping your company, and you’re helping Yelp get where it wants to be.” The Mayfields note that she could have gone a step further by connecting sales reps’ work to how Yelp improves end users’ lives by giving them access to recommendations and reviews of restaurants and other businesses. But on the whole, they give high marks to Alioto’s use of rhetoric to motivate a sales team.

It’s important to note, however, that Alioto’s instruction, empathy, and meaning making don’t stop when the salespeople file back to their desks. After her speech, she walks the sales floor, talking individually with more than a hundred reps and continuing to employ the different elements from motivating language theory. In one conversation, she talks to a rep about how to more forcefully close an ambivalent prospect. With a salesperson about to call an automobile mechanic, she talks about the specifics of that category. In other conversations, she tries to boost reps’ confidence or emphasize the team’s goals.

By day’s end, the New York Yelpers have sold $1.45 million in new ads, meeting their quota and falling just $50,000 short of that month’s stretch target. Many individual reps achieve their BME, Yelp-speak for “best month ever.”

IT’S IMPOSSIBLE TO say how much her morning remarks and one-on-one talks influenced those results, but Alioto felt the day was successful. “My speech wasn’t anything groundbreaking, but it helped them think about where they are and what they are capable of in a different way,” she says. “I try to make everyone understand that they have the power to control their day.”

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DANIEL MCGINN is a senior editor at *Harvard Business Review* and the author of *Psyched Up: How the Science of Mental Preparation Can Help You Succeed* (Portfolio, 2017), from which this article is adapted.

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GROWTH & INCLUSIVE PROSPERITY

The Secular Management Challenge

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CASE STUDY

FOLLOW DUBIOUS ORDERS OR SPEAK UP?

AN INTERN CONTEMPLATES WHETHER SHE SHOULD COMPROMISE HER VALUES FOR A JOB. BY SANDRA SUCHER AND MATTHEW PREBLE

At first, Susan Kim wasn't sure whether she'd heard her new manager correctly.

CASE STUDY CLASSROOM NOTES
Does knowing that the company has done this before make the request more acceptable? Sandra Sucher poses this question when she teaches this case.

The phone line was relatively clear for a call between San Francisco and Seoul, but she still asked Sukbin Moon to repeat himself.

Mr. Moon (as Susan had been told to call him by her half-Korean father) was the Seoul office manager of Zantech, a technology security firm with headquarters in Amsterdam. Susan was just starting her summer internship with the company, and she was supposed to be in Seoul working with Mr. Moon's team, but there had been complications with her visa. Emma Visser, the head of the company's intern program, had suggested she get started from afar.

One of her primary duties during the summer would be helping Mr. Moon with market research by reaching out to other technology firms, including direct competitors, for information on products, services offered, customers, sales, and other data. He'd already e-mailed her a list of target companies and contact names. Now he was telling her that when she contacted people on the list, it would be best to use her university e-mail address and introduce herself as an MBA student.

Perhaps sensing her hesitation, Mr. Moon added, "This is common practice. It's the only way to get accurate information."

Susan shifted uncomfortably in her chair. This was her first conversation with her new manager, and she wanted to make a good impression.

"You won't get the information otherwise," Mr. Moon said, filling the silence. "This is what other interns have done in the past. You don't need to worry."

Still unsure how to respond—or how frank she could be since her father had also told her that direct confrontation was frowned upon in

SANDRA SUCHER is Professor of Management Practice, Joseph L. Rice III Faculty Fellow at Harvard Business School. **MATTHEW PREBLE** is a case researcher at Harvard Business School. HBR's fictionalized case studies present problems faced by leaders in real companies and offer solutions from experts. This one is based on the HBS Case Study "An Intern's Dilemma" (case no. 611041-PDF-ENG), by Sandra J. Sucher and Matthew Preble, which is available at **HBR.org**.

Sucher lays out four questions for her students to consider should they be confronted with an ethical dilemma: (1) Am I comfortable with the likely consequences of this action? (2) Am I fulfilling my duties and respecting others' rights? (3) Am I respecting the community and its norms? (4) Am I meeting my and my company's commitments?

Should a company's practices differ across its offices? Many globalizing firms have difficulty effectively implementing a common set of values and behaviors.

most Asian cultures—she simply said, "OK." She asked a few more questions about the information she was supposed to get and then hung up.

Susan had badly wanted this internship. Her first job out of college had been with a management consultancy, and she'd been staffed right away on a project with a cybersecurity firm. From the start, she was fascinated with the work. She decided to go back to school to get her MBA and planned to eventually join a company on the forefront of this exploding field. In an industry expected to generate $170 billion in revenue by 2020, she knew she'd have many opportunities. And she was elated when Zantech made her an offer. If she played her cards right, it could turn into a full-time job after she graduated. But now Mr. Moon was asking her to misrepresent herself. She understood that gathering competitive intelligence required "creativity"—after all, you were seeking information that your rivals wanted to keep private—but this seemed like it might be crossing the line.

In one of her father's many mini-lectures on how business works in Asia, he had mentioned that expectations and even ethics would be different in Seoul—but that knowledge didn't ease her anxiety now. Was shading the truth "common practice" in Korea or common practice at Zantech?

PUT IT IN PERSPECTIVE

When Susan woke up the next morning, she already had several e-mails from Mr. Moon, with sample inquiries attached. She noticed right away that he had cc'd Emma Visser and a man whose name she didn't recognize. A quick search showed that he was Zantech's head of market research for Asia.

She was supposed to start making calls on Monday, and it was now Thursday afternoon. She had to figure out soon what she was going to do about the request. Rather than answer right away, she went out for a jog, hoping to clear her head. But 30 minutes in, she was still ruminating about what Mr. Moon had asked her to do.

When her phone rang with a call from her dad, she was happy for the distraction—and hoped to hear some sound advice. This was one of their routines. He'd call her around lunchtime on the East Coast, catching her on her way to a morning class or out for a run. Their conversations were always short, but Susan looked forward to them.

After she explained what was going on, her dad started in on a monologue about the importance of having a good job and building a career. Susan listened for a while until she couldn't stand it.

"Dad, stop with the life lessons. I know I need this job."

"I just want you to make a good decision, honey," he said.

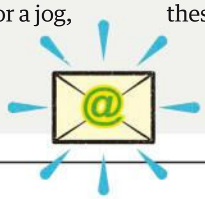
"James thinks I should quit. He says people have a right to be told the truth when they're asked to disclose sensitive information," she said. She and her boyfriend had been together for two years, but her father still hadn't entirely warmed up to him.

"That's easy for him to say. Does he plan to pay your rent this summer? Or get you a job next year? Susie, you need this internship. You know Mom and I would love to help, but we're on a fixed income these days."

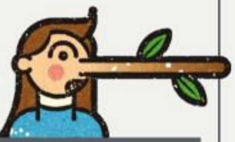
"Fixed income" had been her dad's favorite phrase ever since he retired. Her parents had supported her and her brother through their undergraduate years, but they'd made it crystal clear that from then on, they were on their own. She'd saved some money during her three years of consulting before business school, but not enough to pay San Francisco rent.

"So you're saying I should just do it? Forget everything you taught me about honesty and integrity and do whatever they ask?" She knew she was being melodramatic, but she often fell into that behavior with her parents.

"Susie, keep this in perspective. What Mr. Moon has asked you to do isn't illegal. It's not even untruthful. You *are* an MBA student. And if one of these contacts asks whether you have any corporate affiliation, you can always tell the full truth. Besides, it sounds like it's all aboveboard at



Many people think that the hardest part of an ethical challenge is deciding whether you believe an act is right or wrong. But it is equally important to decide exactly how to handle a situation once you've determined what you believe.



If Susan shares her concerns with Mr. Moon about not disclosing her connection to Zantech, does she risk looking like someone who won't be easy to work with in the future?

Zantech. If the head of market research knows about it, then you know that Mr. Moon isn't hiding anything."

"I just don't feel comfortable with it, Dad. It seems like lying. I think I need to go back to Mr. Moon and tell him how I feel. Or maybe talk to the intern manager, Emma."

"Those are perfectly good options. Just be sure to tread carefully. You don't want them to think you're difficult to work with."

She sighed loudly into the phone. "The irony is not lost on me that a company that tries to prevent people from misrepresenting who they are just asked me to misrepresent who I am."

"Welcome to the real work world, honey. It's full of contradictions."

FUTURE EMPLOYERS

"I thought you'd be in Korea by now," Melinda Sussman said, as she sat down at a café table. Melinda was a principal at the consultancy where Susan had previously worked. Staffed on a few of the same projects, the two had hit it off and subsequently tried to work together whenever they could. When Susan decided to leave for business school, Melinda had written her a recommendation letter, and since both were still in San Francisco, they'd stayed in touch.

"Not yet. Thank you so much for meeting me on the weekend."

Susan explained about the visa issues, her conversation with Mr. Moon, and her debates with James and her father. "I've even talked to the CEO."

"You talked to the CEO? About this?"

"No, no. Not about this. He just called yesterday to apologize about the visa issues." Peter Carlssen had come to Berkeley last fall to participate in a panel discussion on cybersecurity. When Susan had approached him afterward, he told her that he'd been impressed with her questions and encouraged her to apply for the internship. She'd been shocked to hear his voice on the phone and wondered if he typically checked in with interns or was taking a special interest in her. The conversation with Mr. Moon on her mind, she'd been tempted to bring up the issue with the CEO—but didn't.

"I was thinking maybe I could go to him about this," she told Melinda.

"When I saw him speak, he talked about how important ethics were in this field."

"I'm sure he has bigger fish to fry than this. Besides, 'intern rats on manager to CEO'? I don't think that's the kind of reputation you want to get. How big is this company?"

"About 1,500 employees worldwide, but it's a really friendly place. Other than this situation, I've had nothing but positive interactions—from my interviews to my conversations with HR and even my first few e-mails with Mr. Moon. Everyone's gone out of their way to make me feel welcome. There weren't any red flags."

"There's no way you can put the project off until you get over there?" Melinda asked. "Or what about talking to this Emma person? She's your manager too, right?"

"That's not entirely clear. It seems like I report to both of them. I just couldn't get a read on Mr. Moon over the phone, and since he cc'd Emma on that e-mail, it's not like she doesn't know what he's asked me to do."

"This would, of course, be easier if you knew how any of these people were going to respond to questions. If you raise this issue with anyone—Mr. Moon, Emma, HR—you have to be prepared for the worst. It's possible that they'll allow you to get the information in another way, but it's also possible—and I don't want to scare you—that they'll rescind your internship offer. You're not even over there yet, so that would probably be easy to do."

"I'd hate to have to explain that to my parents."

"And future employers. I'm sure I don't have to tell you that your career prospects could be on the line here. But if you agree to misrepresent yourself and are discovered by these companies, you might have trouble finding any job in your field at all. And you have some obligation to the university, too. If you present yourself as a student working on a project for school, and these companies discover there's no such thing, it could reflect badly on your MBA program."

Susan's shoulders slumped; she hadn't thought of that. She really didn't know what to do.

Given Susan's previous interactions with the CEO, does it make sense for her to talk to him directly about this issue? Would he be open to hearing about her concerns?

If she decides to speak to someone at Zantech about the issue, what, exactly, should she say? How should she frame her concerns about ethics? What alternatives, if any, should she propose?

SEE COMMENTARIES ON THE NEXT PAGE ➔

SHOULD SUSAN VOICE HER CONCERNS ABOUT MR. MOON'S REQUEST? THE EXPERTS RESPOND

MR. MOON IS asking Susan to do something inappropriate. While it may seem like no big deal, soliciting information without disclosing your identity is unethical, and I'm not surprised she feels uneasy. Even though she is young and an intern, I believe she should tell Mr. Moon and Emma Visser, the manager in Amsterdam, that she is uncomfortable misrepresenting herself.

The first decade of your career is an important time to learn about business, figure out the type of roles and jobs you like, and clarify what your values are. I was fortunate to get a grounding in ethics at IBM in the 1980s. Honesty and respect were part of the company's ethos, and there was no tolerance for hiding information or saying anything that wasn't true. That foundation helped me navigate many gray-area situations, both as a young professional and in more-senior roles, over the course of my four-decade career. Susan should look for the same kind of employer—one that will help her get the right start professionally and gain a clear understanding of what good business is and what it isn't.

I would recommend that she do some research on Zantech: Is this the type of company that reflects the values she holds dear? She can look at Glassdoor and other sites where employees give inside perspectives on their companies. Have employees reported that they were asked to do unethical things? Have competitors, customers, or suppliers ever complained about its business practices? Does the company have outstanding legal issues? If the answer to those questions is yes, she may decide this company is not for her.

If her research shows that Zantech is an ethical, open, friendly place to work, she should simply voice her concerns. She should send an e-mail to both Mr. Moon and Emma Visser explaining her discomfort with the assignment. Her father may be right that frankness is frowned upon in Korea, but if she contacts only Emma, she is losing the opportunity to address the issue with her manager—and he is the person she would work for.

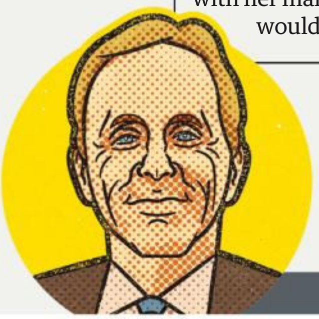
Her e-mail should be positive and focus on the risks to the company as a whole, not simply her own feelings. She might say something like, "I greatly appreciate the opportunity to do this work with you, and this project is quite interesting. However, I'm concerned that if we don't disclose the fact that I'm working for Zantech and the word leaks out, it will reflect poorly on the firm." Her tone should be collaborative and constructive, and she should use the word "we" as much as possible.

Ideally—and most likely—both Mr. Moon and Emma will respect her for speaking up, understand her position, and allow her to approach the work in a different way. It might also prompt Mr. Moon to think more about what Zantech is asking her to do. At Deloitte, our newest research shows that companies focused on mission, purpose, and ethical behavior consistently outperform their peers over a long period of time. Firms with that kind of culture encourage people to voice their concerns and are open to discussions about ethical issues. Corporate scandals erupt with alarming frequency; in most cases they are devastating to the company's brand and reputation. All too often, people inside those firms who could have sounded the alarm remained silent, perhaps assuming that no one would listen.

SHE SHOULD SEND AN E-MAIL TO MR. MOON AND EMMA VISSER EXPLAINING HER DISCOMFORT.

If Mr. Moon and Emma ignore Susan's concerns, it's a signal that she should start looking for employment elsewhere. Tech-savvy MBAs are in high demand, and she has a long career ahead of her. If she compromises her values now, it will only haunt her later.

JOSH BERSIN IS THE FOUNDER AND PRINCIPAL OF BERSIN BY DELOITTE.



RUWAN WEERASEKERA IS A NONEXECUTIVE DIRECTOR IN FINANCIAL SERVICES, HEALTH CARE, AND EDUCATIONAL ORGANIZATIONS AND A FORMER MANAGING DIRECTOR AT UBS.

SUSAN SHOULDN'T BLINDLY follow orders. But as an intern, she does need to get the work done. So my advice is that she find an alternative way to complete Mr. Moon's project that is ethical, legal, and transparent.

When I think about ethical issues, I picture a 2x2 matrix with legality on one axis and ethics on the other. I love when things fit unequivocally into the legal and ethical box, but that is not always the case in business. It is common—and difficult—to face situations that don't require you to violate any laws or regulations but do go against your values. I've faced many murky situations in my career—including conducting internal investigations into the biggest fraud and misconduct cases in bank history—and I always managed to act on my principles.

If I were in Susan's shoes, I certainly wouldn't start calling Zantech's competitors and misrepresenting myself. But I wouldn't immediately confront Mr. Moon or Emma Visser, either. Different organizations and countries have different norms, and she doesn't yet know enough about the company or working in Korea to question the way things are done. Indeed, immediately challenging Mr. Moon's request and declaring it unethical could hurt her in the long run.

But capitulation or confrontation aren't her only choices. Instead, she should suggest a workaround—that is, she should present not a problem but a solution, as any good intern or employee should.

How might she get the information she needs without hiding who she is? One option would be to talk with people at Zantech's most loyal clients, who no doubt evaluated other software vendors before signing on with the firm. Customers love to be consulted, and the discussions would help her gather intelligence on competitors and reverse engineer a product comparison.

Another option would be to talk with third-party firms like IBM, PwC, and independent consultancies that help install Zantech's products, or with analyst firms whose job it is to evaluate the competitive landscape. Their knowledge would be similar to that of customers, and they may be even more willing to outline Zantech's relative strengths and weaknesses.

A third alternative would be to look inside Zantech for information sources. Of the 1,500 people who work there, surely some came from competitors and might offer insights that could be helpful when aggregated. Some may be bound by confidentiality—and she should observe that, of course—but many may have valuable information that the company can easily and freely use.

These approaches would not only save Susan from her ethical dilemma, but they're also likely to be more effective, since a cold call from an intern to a competitor is, in my opinion, highly unlikely to yield any useful information. I'm not suggesting she tell Mr. Moon, "This will never work," but she could volunteer to test the approach on Zantech itself, making a few calls into the company, to see whether his proposed tactics work or not. That would also reveal how well the company's own employees protect sensitive competitive information.

Like many executives, I've built my reputation on my integrity, and I guard it jealously. But I also take pride in my ability to get things done. This is the balance that Susan needs to strike.

And if she's able to resolve the dilemma satisfactorily, she should remember that an internship is an extended interview. She should be evaluating Zantech as much as its executives are evaluating her. She needs to ask herself: Is this a firm I can work for? Do my values match with those of the company? The answers to these questions won't come from a mentor, parent, or partner. She needs to make her own decision.

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Reprint Case only R1704X
Reprint Commentary only R1704Z

COMMENTS FROM THE HBR.ORG COMMUNITY

Don't Worry
If someone called me and asked for sensitive information about my company, I wouldn't give it, regardless of whether the person identified herself as a student or an employee. Susan shouldn't be concerned about deceiving others, because she won't get the information she needs anyway.
Ardita M. Gjeçi
head of change management, GJEÇI

Speak Up
I've managed interns at a large company, and I always encourage people at any level to challenge superiors in a respectful way. Their questions can help the company improve. Good managers will be receptive to input.
Terrel Fish
project manager, MKEC Engineering

Quit the Internship
Companies with strong values would never engage in such practices and would provide employees access to legal advice for handling proprietary information from rivals. If this firm would ask an intern to do this, imagine what it might ask of its employees. Walk away and don't look back.
Sharon Hoeting
consumer insights director, General Mills

MARIA BARTIROMO

GLOBAL MARKETS EDITOR, FOX BUSINESS NETWORK

WHAT I'M READING...

Before I go on the air at 6 each morning, I scan the *Wall Street Journal,* the *Financial Times,* the wire services, the international markets, and Twitter. My favorite business magazine is the *Economist,* because of its no-nonsense style, but when I'm relaxing, I turn to *Architectural Digest* or *Vogue.* My bedside table is stacked with nonfiction. I'm currently reading *Johnson's Life of London,* which is about the decisions Boris Johnson made when he was mayor; *America in Retreat,* by journalist Bret Stephens; and *A Short Guide to a Long Life,* by David Agus, a health and wellness expert who's been on my show many times. I love biographies, too; one I've gone back to several times is *In All His Glory,* the story of William Paley, who founded CBS.

SYNTHESIS

LIBERAL ARTS IN THE DATA AGE

WHY THE HARD SCIENCES NEED THE HUMANITIES BY J.M. OLEJARZ

College students who major in the humanities always get asked a certain question. They're asked it so often—and by so many people—that it should come printed on their diplomas. That question, posed by friends, career counselors, and family, is "What are you planning to do with your degree?" But it might as well be "What are the humanities good for?"

According to three new books, the answer is "Quite a lot." From Silicon Valley to the Pentagon, people are beginning to realize that to effectively tackle today's biggest social and technological challenges, we need to think critically about their human context—something humanities graduates happen to be well trained to do. Call it the revenge of the film, history, and philosophy nerds.

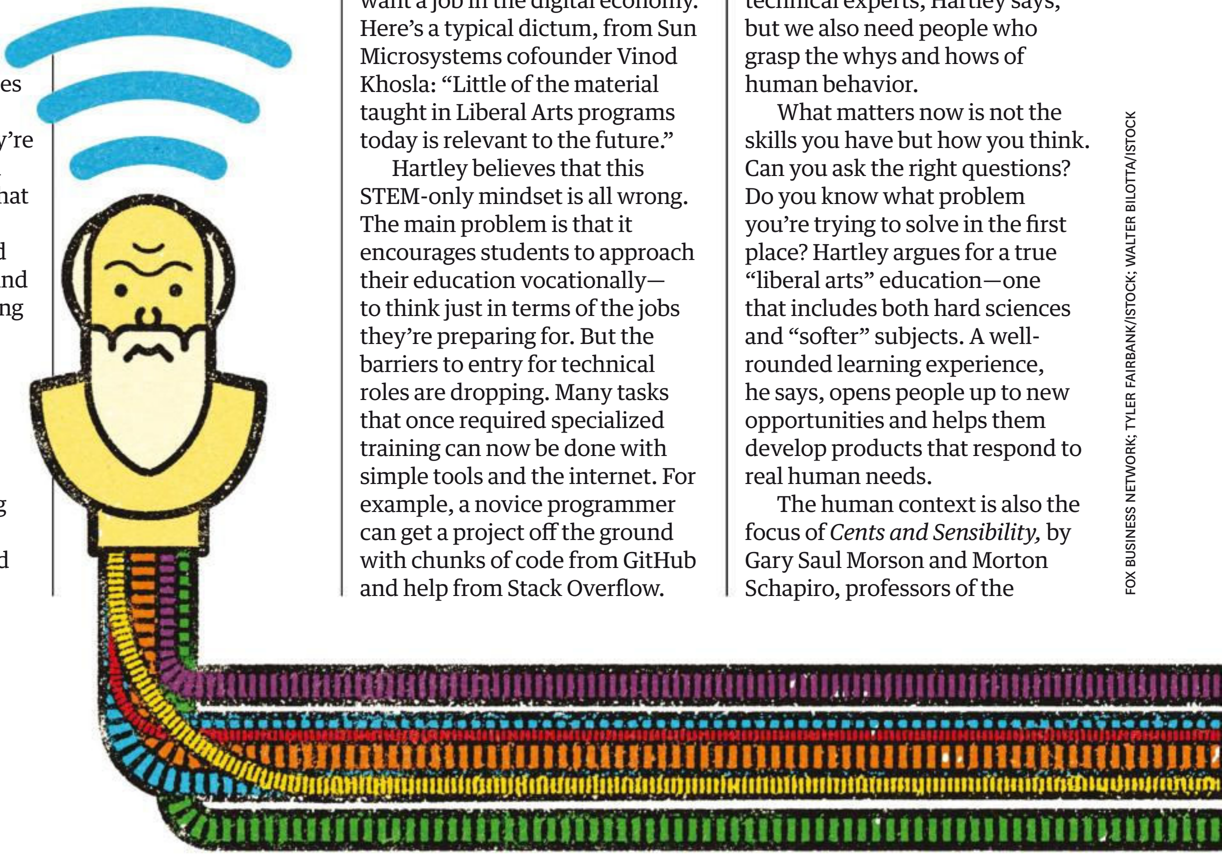
In *The Fuzzy and the Techie,* venture capitalist Scott Hartley takes aim at the "false dichotomy" between the humanities and computer science. Some tech industry leaders have proclaimed that studying anything besides the STEM fields is a mistake if you want a job in the digital economy. Here's a typical dictum, from Sun Microsystems cofounder Vinod Khosla: "Little of the material taught in Liberal Arts programs today is relevant to the future."

Hartley believes that this STEM-only mindset is all wrong. The main problem is that it encourages students to approach their education vocationally—to think just in terms of the jobs they're preparing for. But the barriers to entry for technical roles are dropping. Many tasks that once required specialized training can now be done with simple tools and the internet. For example, a novice programmer can get a project off the ground with chunks of code from GitHub and help from Stack Overflow.

If we want to prepare students to solve large-scale human problems, Hartley argues, we must push them to widen, not narrow, their education and interests. He ticks off a long list of successful tech leaders who hold degrees in the humanities. To mention just a few CEOs: Stewart Butterfield, Slack, philosophy; Jack Ma, Alibaba, English; Susan Wojcicki, YouTube, history and literature; Brian Chesky, Airbnb, fine arts. Of course, we need technical experts, Hartley says, but we also need people who grasp the whys and hows of human behavior.

What matters now is not the skills you have but how you think. Can you ask the right questions? Do you know what problem you're trying to solve in the first place? Hartley argues for a true "liberal arts" education—one that includes both hard sciences and "softer" subjects. A well-rounded learning experience, he says, opens people up to new opportunities and helps them develop products that respond to real human needs.

The human context is also the focus of *Cents and Sensibility,* by Gary Saul Morson and Morton Schapiro, professors of the



FOX BUSINESS NETWORK; TYLER FAIRBANK/ISTOCK; WALTER BILOTTA/ISTOCK

WATCHING…

I turn on Fox and the news outlets when a big story is breaking. But most nights I'll keep track of the headlines on my phone and, if I'm home, watch some escapist television. I'm addicted to *House of Cards* and DVR'ed the HBO series *Big Little Lies.*

LISTENING TO…

My husband and I love live music and are active supporters of the Jazz Foundation of America, which raises money for musicians who want a career in the field but aren't able to support themselves. I've always secretly wanted to be a backup singer.

ATTENDING…

I go to a lot of conferences. Annual highlights include the World Economic Forum in Davos, the Milken Institute Global Conference, and two sponsored by J.P. Morgan—a CEO summit in New York and a health care conference in San Francisco. The point is to listen to the conversations business leaders are having so that I can bring that information back to my viewers.

humanities and economics, respectively, at Northwestern University. They argue that when economic models fall short, they do so for want of human understanding. Economics tends to ignore three things: culture's effect on decision making, the usefulness of stories in explaining people's actions, and ethical considerations. People don't exist in a vacuum, and treating them as if they do is both reductive and potentially harmful.

Morson and Schapiro's solution is literature. They suggest that economists could gain wisdom from reading great novelists, who have a deeper insight into people than social scientists do. Whereas economists tend to treat people as abstractions, novelists dig into the specifics. To illustrate the point, Morson and Schapiro ask, When has a scientist's model or case study drawn a person as vividly as Tolstoy drew Anna Karenina?

Novels can also help us develop empathy. Stories, after all, steep us in characters' lives, forcing us to see the world as other people do. (Morson and Schapiro add that although many fields of study tell their practitioners to empathize, only literature offers practice in doing it.)

Sensemaking, by strategy consultant Christian Madsbjerg, picks up the thread from Morson and Schapiro and carries it back to Hartley. Madsbjerg argues that unless companies take pains to understand the human beings represented in their data sets, they risk losing touch with the markets they're serving. He says the deep cultural knowledge businesses need comes not from numbers-driven market research but from a humanities-driven study of texts, languages, and people.

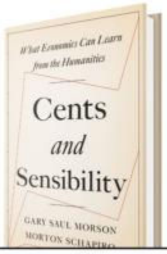
Madsbjerg cites Lincoln, Ford's luxury brand, which just a few years ago lagged so far behind BMW and Mercedes that the company nearly killed it off. Executives knew that becoming competitive again would mean selling more cars outside the United States, especially in China, the next big luxury market. So they began to carefully examine how customers around the world experience, not just drive, cars. Over the course of a year, Lincoln representatives talked to customers about their daily lives and what "luxury" meant to them. They discovered that in many countries transportation isn't drivers' top priority: Cars are instead seen as social spaces or places to entertain business clients. Though well engineered, Lincolns needed to be reconceived to address the customers' human context. Subsequent design efforts have paid off: In 2016 sales in China tripled.

What these three books converge on is the idea that choosing a field of study is less important than finding ways to expand our thinking, an idea echoed by yet another set of new releases: *A Practical Education,* by business professor Randall Stross, and *You Can Do Anything,* by journalist George Anders. STEM students can care about human beings, just as English majors (including this one, who started college studying computer science) can investigate things scientifically. We should be careful not to let interdisciplinary jockeying make us cling to what we know best. Everything looks like a nail when you have a hammer, as the saying goes. Similarly, at how great a disadvantage might we put ourselves—and the world—if we force our minds to approach all problems the same way?

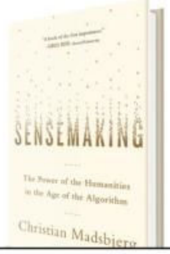
> **"IN FACT, THE LIBERAL ARTS TEACH MANY METHODS OF RIGOROUS INQUIRY AND ANALYSIS, SUCH AS CLOSE OBSERVATION AND INTERVIEWING, IN WAYS THAT HARD SCIENCE ADHERENTS DON'T ALWAYS APPRECIATE."**
> Scott Hartley, *The Fuzzy and the Techie*

J.M. OLEJARZ is an assistant editor at *Harvard Business Review.*

The Fuzzy and the Techie: Why the Liberal Arts Will Rule the Digital World
Scott Hartley
Houghton Mifflin Harcourt, 2017



Cents and Sensibility: What Economics Can Learn from the Humanities
Gary Saul Morson and
Morton Schapiro
Princeton University Press, 2017



Sensemaking: The Power of the Humanities in the Age of the Algorithm
Christian Madsbjerg
Hachette Books, 2017

SPOTLIGHT

THE TROUBLE WITH CMOs

The top marketing job in the company is a minefield where many talented executives fail. In this issue we examine what makes the position so risky—and how firms can set CMOs up for success.
page 45

SPOTLIGHT WHY CMOS NEVER LAST

WHY CMOs NEVER LAST

AND WHAT TO DO ABOUT IT

BY KIMBERLY A. WHITLER AND NEIL MORGAN

ILLUSTRATION BY PETER CROWTHER

Why CMOs Never Last
Something is deeply amiss in the relationship between chief executives and their top marketing officers. Eighty percent of CEOs say they don't trust or are unimpressed by their CMOs. Not surprisingly, CMOs have the briefest tenure in the C-suite. The churn can lead to serious internal business disruptions.

What can be done to end this dysfunctional pattern? Kimberly A. Whitler, a former CMO who's now an assistant professor at the University of Virginia's Darden School, and Neil Morgan, a marketing professor at Indiana University, have done extensive research into the problem. They believe that its main cause is faulty role design.

To begin with, there's no one clear, widely accepted answer to the question, What does a CMO do? The range of job duties and skills required are all over the map. Moreover, too often the expectations for CMOs' jobs are unrealistic and not aligned with their responsibilities and performance metrics. This unhealthy dynamic sets executives up to fail.

The authors outline the steps companies should take to rectify the situation. First, they need to understand the three main kinds of CMO roles: Some focus on strategy, some on commercialization, and some—which have enterprisewide P&L responsibility—do both. It's crucial to figure out which type of CMO a firm needs and then tailor the duties and success metrics accordingly.

CMO candidates and recruiters also have a part to play in seeing that jobs are clearly defined and that new hires are good matches. The authors include checklists of questions that all parties involved in the process should be sure to ask before making any decisions.

The Power Partnership
As digital technology becomes more critical to marketing, the line between the CMO's job and the CIO's is blurring. Although historically these executives have tended to see the world quite differently, they now must work together on a new and very high level. Giving them shared performance goals is a great tool for sparking effective collaboration, as the experience of Regal Entertainment Group demonstrates.

THE COMPLETE SPOTLIGHT PACKAGE IS AVAILABLE IN A SINGLE REPRINT. **HBR Reprint** R1704B

REFLECTIONS OF A SIX-TIME CMO

A CONVERSATION WITH JOE TRIPODI

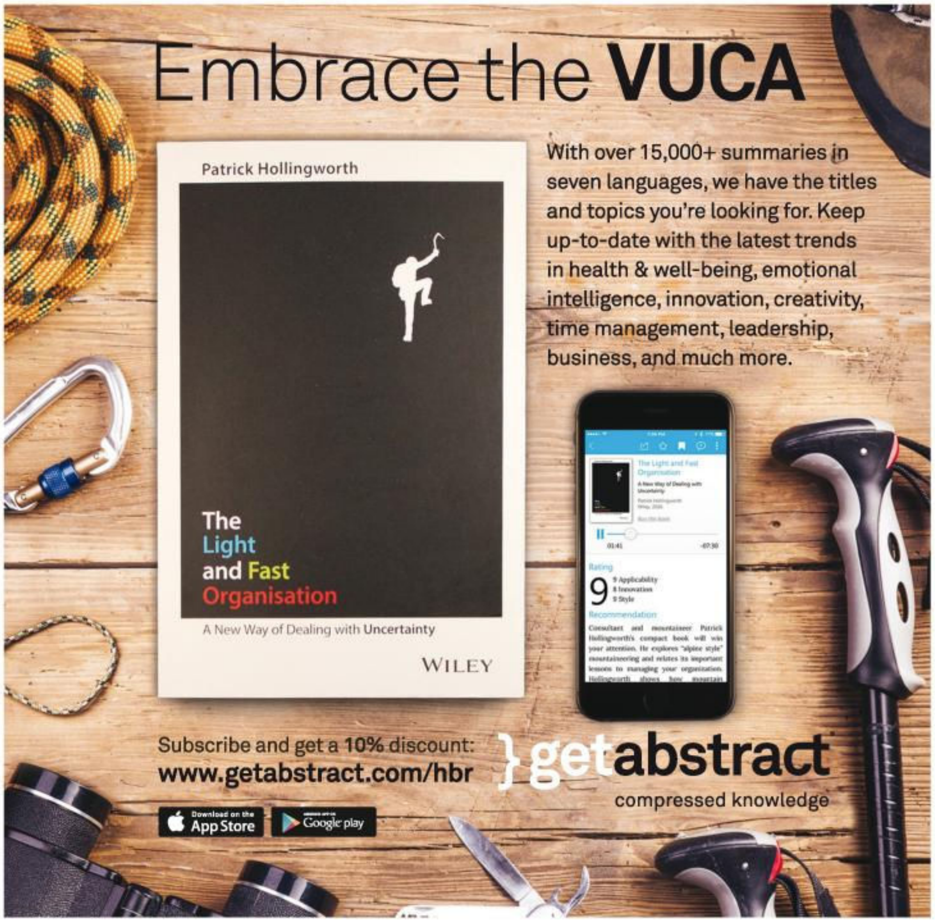
Reflections of a Six-Time CMO
Joe Tripodi has served as top marketing officer of Mastercard, Seagram's, the Bank of New York, Allstate, Coca-Cola, and Subway. In this interview he shares his thoughts on the keys to making it as CMO and on how the challenges of the job have changed since the 1980s.

REDUCING CMO TURNOVER: A Recruiter's Prescription

A Recruiter's Prescription
After placing nearly 500 CMOs over the past 20 years, Spencer Stuart's Greg Welch is frustrated by how many smart executives don't last in the position. Too often, he says, the hiring process turns into a popularity contest that favors charismatic candidates. Everyone instead needs to focus on real job specifications and setting achievable expectations. Strategic onboarding plans will also get CMOs off to faster, more-productive starts.

The Evolution of the CMO

The Evolution of the CMO
A decade-by-decade look at how the growth of new marketing tools, channels, and challenges has expanded and reshaped the CMO's responsibilities



Patrick Hollingworth
The Light and Fast Organisation
A New Way of Dealing with Uncertainty
WILEY

Harvard Business Review OnPoint
SALES SUPERSTARS: How to Seal the Deal Every Time

HOW I DID IT

ENTREPRENEURSHIP

SOULCYCLE'S CEO ON SUSTAINING GROWTH IN A FADDISH INDUSTRY

Melanie Whelan | page 37

SOULCYCLE'S CEO ON SUSTAINING GROWTH IN A FADDISH INDUSTRY

After hearing from friends that SoulCycle's very first studio was different from other cycling studios, Whelan decided to give it a try. One visit was all it took for her to appreciate the full sensory experience, the charismatic instructor, and the passion of the client community. A few years later she joined the company, which today operates 74 studios.

SoulCycle doesn't view itself as a fitness company—it's a "player in the broader experiential economy." That's why it takes a different approach to recruiting and training instructors, with the aim of making them inspirational coaches who empower riders in their lives as well as on their bikes. It doesn't charge monthly fees, but each class costs $30 to $35, and riders must book bikes in advance, on the theory that the pay-per-class model elicits greater energy and commitment. Choosing the location for a new studio involves a year of research to understand the lifestyle of future customers. Amenities such as iPhone chargers in the lockers have improved studio design. Next-generation bikes are coming in 2017, and the company's apparel line is expanding. Because SoulCycle has friendships and community at its core, Whelan writes, the brand will endure.

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FEATURES

MANAGING ORGANIZATIONS

STOP THE MEETING MADNESS

Leslie A. Perlow, Constance Noonan Hadley, and Eunice Eun | page 62

STOP THE MEETING MADNESS

"MEETINGS DON'T HAVE TO BE A TRAP; THEY CAN BE A CONDUIT FOR CHANGE."

Many executives feel overwhelmed by meetings, and no wonder: On average, they spend nearly 23 hours a week in them, up from less than 10 hours in the 1960s. What's more, the meetings are often poorly timed, badly run, or both.

We can all joke about how painful they are, say the authors, but that pain has real consequences for teams and organizations. Every minute spent in a wasteful meeting eats into solo work that's essential for creativity and efficiency. Chopped-up schedules interrupt deep thinking, so people come to work early, stay late, or use weekends for quiet time to concentrate. And dysfunctional meeting behaviors are associated with lower levels of market share, innovation, and employment stability.

The authors have found that real improvement requires systemic change, not discrete fixes. They describe a five-step process for that—along with the diagnostic work you'll need to do in advance.

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LEADING TEAMS

BEING THE BOSS IN BRUSSELS, BOSTON, AND BEIJING

Erin Meyer | page 70

BEING THE BOSS IN BRUSSELS, BOSTON, AND BEIJING

When misunderstandings arise among members of global teams, it's often because managers conflate attitudes toward authority and attitudes toward decision making. However, the two are different dimensions of leadership culture, says the author, who has extensive research and consulting experience with global companies.

Attitudes toward authority range from strongly hierarchical to strongly egalitarian. Approaches to decision making vary from top-down to consensual. The author explores both dimensions and classifies selected countries according to their position on both scales. The Japanese, for example, are hierarchical in their views toward authority—deferential to the boss and accustomed to waiting for instructions rather than taking the initiative—but they are consensual decision makers who get buy-in before they set a course of action.

The author describes the four cultural types—consensual and egalitarian; consensual and hierarchical; top-down and hierarchical; and top-down and egalitarian—and the corresponding expectations about leadership in each environment. If you keep those in mind, you'll be more successful in your cross-cultural interactions.

HBR Reprint R1704D

COMPENSATION

DECODING CEO PAY

Robert C. Pozen and S.P. Kothari | page 78

Each year most public companies issue reports describing the pay packages of their CEOs. In them compensation committees attempt to explain the rationale behind the pay figures to the shareholders, who often must vote to approve them. The issue is, in their reports many committees adjust performance numbers in obscure and inappropriate ways that lead to overly generous CEO pay. And they do so using nonstandard criteria that are difficult for even sophisticated institutional investors to decode.

In this article, the former executive chairman of MFS Investment Management and an MIT professor of accounting and finance sort through the reports' fine print and expose practices that stack the deck in CEOs' favor: Adjusting earnings to be 100% higher than GAAP income. Paying out 80% of an incentive award for bottom-quartile performance. Choosing "peer companies" that are not comparable in size or in industry. And more.

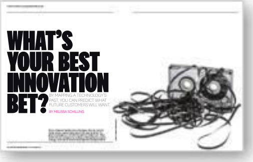
Shareholders should be more skeptical, say the authors, and comp reports must start providing much clearer explanations. But what's needed most are new standards for compensation design and reporting.

HBR Reprint R1704E

STRATEGY

WHAT'S YOUR BEST INNOVATION BET?

Melissa Schilling | page 86


WHAT'S YOUR BEST INNOVATION BET?

Whether you make cars or mattresses, operate a hospital or a grocery store, or are in some other business, successful innovation depends on understanding what's driving the technological changes in your industry and anticipating what product and service features consumers will value in the future. In this article, the author describes her proven system for gaining those vital insights.

The first step is to look back at the evolution of your business's technology and identify three to six dimensions where advances have significantly furthered its development—"big picture" dimensions such as cost, comfort, and safety. Next, plot the utility curve for each dimension (to see how progress on that dimension correlates with customer appreciation) and pinpoint the technology's current position on the curve. Third, decide where to focus your innovation efforts—a task made easier by using the author's matrix for scoring each dimension according to its importance to customers, its potential for improvement, and the ease with which improvements can be made. By following this three-step approach, a host of diverse companies are already creating promising new products.

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STRATEGY

FINDING THE PLATFORM IN YOUR PRODUCT

Andrei Hagiu and Elizabeth J. Altman
page 94

Five of the 10 most valuable companies in the world today—Apple, Alphabet, Amazon, Facebook, and Microsoft—derive much of their worth from their multisided platforms, which facilitate interactions or transactions between parties. Many MSPs are more valuable than companies in the same industries that provide only products or services: For instance, Airbnb is now worth more than Marriott, the world's largest hotel chain. However, companies that weren't born as platform businesses rarely realize that they can—at least partially—turn their offerings into one, say the authors. And even if they do realize it, they often wander in the dark searching for a strategy to achieve this transformation.

In this article, Hagiu and Altman provide a framework for doing so. They lay out four specific ways in which products and services can be turned into platforms and examine the strategic advantages and pitfalls of each: (1) opening the door to third parties; (2) connecting customers; (3) connecting products to connect customers; and (4) becoming a supplier to a multisided platform. These ideas can be used by physical as well as online businesses.

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SUSTAINABILITY

MANAGING CLIMATE CHANGE: LESSONS FROM THE U.S. NAVY

Forest L. Reinhardt and Michael W. Toffel | page 102

> IT'S TIME TO MOVE BEYOND "NO REGRETS" EFFORTS.

The U.S. Navy operates on the front lines of climate change. It manages tens of billions of dollars of assets on every continent and on every ocean, which take many years to design and build and then have decades of useful life. This means that it needs to understand now what sorts of missions it may be required to perform in 10, 20, or 30 years and what assets and infrastructure it will need to carry them out. Put another way, it needs to plan for the world that will exist at that time.

The navy is clear-eyed about the challenges climate change poses. It knows that the effects of a warmer world will expand the geographic scope of its mission and increase demand for its military and humanitarian services. Climate change will also decrease its capacity to deliver those services, as the risk of damage to its bases and ports increases.

This article examines the navy's approach to climate change and reflects on the implications for business.

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INTERNATIONAL BUSINESS

GLOBALIZATION IN THE AGE OF TRUMP

Pankaj Ghemawat
page 112

Business leaders are scrambling to adjust to a world few imagined possible just a year ago. The myth of a borderless world has come crashing down. Traditional pillars of open markets—the United States and the UK—are wobbling, and China is positioning itself as globalization's staunchest defender. Countries throughout North America and Europe have experienced waves of anti-globalization sentiment.

In the face of such uncertainty, leaders of multinationals wonder whether they should retreat, change strategy, or stay the course. In making that decision, they need to understand two things. First, the world is less globalized than even experienced executives realize. Second, history tells us that even in the face of a trade war, international trade and investment would still be too large for strategists to ignore.

Today's turmoil calls not for a mass retreat from globalization but for a more subtle reworking of multinationals' strategies. This article examines common misperceptions about what is—and isn't—changing about globalization and offers guidelines to help leaders decide where and how to compete in a complex world.

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THE HBR INTERVIEW

"DON'T TRY TO PROTECT THE PAST"

IBM CEO Ginni Rometty, interviewed by Adi Ignatius
page 126

Ginni Rometty has spent 36 years at IBM, where she now serves as president, CEO, and chair of the board. She is on a protracted mission to reinvent the company as a cloud-based "solutions" business. That transformation involves moving into areas that have higher value and shedding ones that don't. IBM's new businesses around cloud, data, and security account for almost $34 billion in revenue. They're growing by more than 13% a year and constitute 42% of the company.

In this interview Rometty says that IBM is trying to "unlock" the 80% of data behind the firewalls of client companies so that those organizations can use it to make better decisions, adding, "There's a $2 trillion market around better decision making." She talks about why IBM's earnings have declined for 20 consecutive quarters, what kinds of employees the company's new course demands, gender-related challenges in her career, and more.

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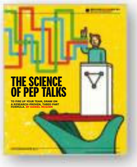
MANAGING YOURSELF

THE SCIENCE OF PEP TALKS

Daniel McGinn | page 133



The ability to deliver an energizing pep talk is a prerequisite for any business leader. But few managers receive formal training in how to give one. Instead, they learn mostly by emulating inspirational bosses, coaches, or even fictional characters.

However, research shows there is a science to psyching people up for better performance. According to motivating language theory, most winning formulas include three key elements: direction giving, or describing precisely how to do the task at hand; expressions of empathy, or concern for the performer; and meaning-making language, which explains why the task is important.

All the evidence suggests that, once leaders understand these three elements, they can learn to use them more skillfully.

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COMING IN JULY: ARTIFICIAL INTELLIGENCE, FOR REAL

THE BIG IDEA

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JANUARY 2017

MANAGING YOURSELF

GENEROSITY BURNOUT

Adam Grant and Reb Rebele

BEING SELFLESS at work leads to exhaustion—and often hurts the very people you want to help. Here's how to share your time and expertise more effectively. This program is anchored by the feature article "Beat Generosity Burnout," by Adam Grant and Reb Rebele. The series of audio postcards "Leaders Who Get How to Give" profiles leaders who learned how to avoid burning out, with an accompanying article by HBR editor Curt Nickisch. For more on Grant and Rebele's research, watch the video explainer "How and When Selflessness at Work Backfires." Find out if you're prone to giving too much with the assessment "Generosity Burnout—Are You at Risk?" Hear more from Grant and Rebele, with HBR editor Amy Bernstein, in the webinar "Managing Collaborative Overload." And see answers to questions they couldn't get to in the webinar in "More on Being Generous Without Being a Doormat."

MARCH 2017

ECONOMY

THE BUSINESS OF INEQUALITY

Nicholas Bloom

HERE'S A part of the income-inequality debate you may not know about: Today's winner-take-all economy rewards workers at top firms and leaves the rest behind. In his feature article "Corporations in the Age of Inequality," Stanford economist Nicholas Bloom presents his case for how that happened and what we can do about it. For a primer, watch the video "The Other Kind of Inequality, Explained." Former White House economist Jason Furman offers his perspective in the interview "Competition Is on the Decline, and That's Fueling Inequality." Craig Rowley, of executive search firm Korn Ferry, explores the wage gap in "Why Some Firms Pay Better Than Others." Top economists share data visualizations in "The Inequality Story, in Charts." For a look at how inequality plays out in one industry, read an interview with Silicon Valley financial planner Lavina Nagar. Finally, Harvard Business School professor Rebecca Henderson's call to action, "Why Inequality Is an Urgent Business Problem," explains management's vital role in finding a solution.

MAY 2017

TECHNOLOGY

THE DRONE ECONOMY

Chris Anderson

AT BREAKNECK speed, drones have moved from expensive technology for the military to toy for tech enthusiasts and now to tool for business. Experts expect that within the year, hundreds of thousands of commercial drones will be in the skies. But if you think this is about little helicopters dropping off packages, think again; in fact, consumer delivery is one of the more difficult and less interesting drone apps. Drones are platforms—less pilotless planes and more flying smartphones. Chris Anderson, CEO of a drone company, explores how drones are disrupting business in his feature article "Drones Go to Work." For a discussion of new drone apps and where the industry is headed, watch a video interview with Helen Greiner, a cofounder of iRobot and now founder of a drone company. We talk with a drone lawyer about the state of regulations, and drone industry entrepreneur Dyan Gibbens tackles drone ethics. In a short video case study, we show how AT&T is disrupting itself with drones. And you can test yourself with the interactive quiz "Does a Drone Do That?"

For more from Alda, go to **HBR.ORG**.

LIFE'S WORK
ALAN ALDA
ACTOR

Best known for playing Hawkeye Pierce on the TV series *M*A*S*H,* Alan Alda is also a director, scriptwriter, book author, science-show host, and founder of two organizations that help people improve their communication skills—the topic of his new book.

Interviewed by Alison Beard

HBR: Colleagues have described you as diligent, the hardest worker, a perfectionist. How do you keep that up over the course of a career?

ALDA: I don't think I'm a perfectionist. My early training as an improviser got me used to the idea of uncertainty and the value of the imperfect. Everything is a stepping-stone to something else, whether it's perfect or lousy. I'm always looking to get better. It will never be perfect.

Could improv skills help the rest of us?

The kind of improvising I value is not designed to entertain people. In its purest form, it puts you in touch with other people in a way that is intimate, informal, and fully engaged, so you can be aware of what they're feeling and thinking. That's an extremely useful power to have in any type of communication, from the boardroom to the bedroom. We're social animals, but we often avoid developing this capacity to relate to others. It's a shame because without it, we won't make much headway together.

How do you get a new team, like a cast, to gel?

Usually in making a show, when you're not needed, you go back to your dressing room. But during *M*A*S*H* we would instead sit around in a circle and kid each other and go over our lines. The sense of a group was fortified all day long. The laughing was important because when you laugh you're vulnerable, opened up. After that whenever I did a play, I wouldn't make it an overt ritual, but I would try to work it so the cast was sitting and laughing together, and the performance became just an extension of that playful experience. We were cooking.

Who are some of your favorite collaborators?

Martin Scorsese, because he was so encouraging. Even if he didn't like what you were doing, you got the impression you were great, and little by little you saw the value of moving to something else. Also Woody Allen, because he never said anything. He just had you do it until it got better—although he only does a couple of takes. And there's almost no rehearsal, so you have to relate to the other people. I've learned that there's no certain way to get the most out of people, and if you're in a relationship with a leader, you've got to be able to work with and get the best out of that person, too.

You weren't immediately successful as an actor. Why did you stick with it?

I often hear that you're supposed to have a goal and keep working toward it. But if you're an actor, it's hard to do that. You take whatever opportunity is in front of you and make the most of it. I was guided not by a goal but by the love of what I was trying to learn to do and the deep desire to do it as well as I possibly could. And that made a difference, because whichever way it led me, I'd be OK. At a very early age, I wanted three things: to work with material I valued and people I respected in front of an audience that got it. I could have been in a small regional theater for the rest of my life, and I wouldn't have been disappointed.

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> **"WHEN I START A NEW THING—WHETHER IT'S ACTING IN A PLAY, WRITING A BOOK, OR GOING ON A DIET—IT USUALLY TAKES ME ABOUT THREE WEEKS TO FOCUS, AND THEN I'M OBSESSED."**

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