HARVARD
Management Update

Why Managing Up Matters

It isn't manipulation. Clarifying the goals and limitations of the boss-employee relationship enables everyone to move on to the real business at hand.

BY LIZ SIMPSON

WHY IS IT SO HARD TO FIND a treatment of boss-employee relations that doesn't characterize the boss as an ass or a psychotic and the subordinate as a helpless underling? Case in point: *Fortune* columnist Stanley Bing's recent book, *Throwing the Elephant.* Bing describes a workplace jungle in which the boss is an elephant that can easily crush you by accident or whim. Your job—indeed, your survival—depends on your becoming a slavish "student of this elephant," learning and accommodating yourself to its various likes and dislikes.

Admittedly, the book is a facetious take on that well-charted Dilbertian world of feckless managers and workers resigned beyond all hope to their fate. It's not intended to be taken seriously (right?), but its underlying characterization of bosses as dumb beasts that must be placated at all costs is widespread.

Progress won't come from catering to this notion. It trivializes a serious management issue—the need to "manage up." The goal of managing up is to develop a pattern of interaction between your boss and you that delivers the best possible results for your organization (and by extension, for each of you). The accommodations you make help you gain better insight into your boss's context: his strengths and weaknesses, the pressures he feels from above and from his peers, and the combination of organizational and personal objectives he's trying to meet.

Articles in this newsletter draw on a variety of sources, including published reports, interviews with practicing managers and consultants, and research by management scholars, some but not all of whom are affiliated with Harvard Business School. Articles reflect the views of the author.

"Too much has been written about managing up in a self-centered, get-mine way," says Harvard Business School professor John P. Kotter. "This may have worked in a slow-moving world of oligopolies, where internal politics can dominate and the enterprise can still win. But not today." To Kotter, clarifying the boss-employee relationship is important because it enables the people involved to move on to the true business at hand—grappling with the challenges and opportunities facing the organization.

Kotter's new book, *The Heart of Change,* profiles firms that do this well. "Manipulative boss management plays no part" in the process, he says. "Zero. You do sometimes need to help the boss develop a sense of urgency, to craft a vision, to communicate the vision, and more. But the word is help, not manipulate for your own selfish needs."

Beyond politics and the power differential

The whole notion of managing up was considered inappropriate when Kotter and fellow Harvard Business School professor John J. Gabarro wrote their now-classic article "Managing Your Boss" (*Harvard Business Review,* January–February 1980). In the top-down business culture of the early '80s, good managers paid attention to their relationships with subordinates and peers, but managing upward didn't make sense unless you were interested in political maneuvering. Gabarro and Kotter's work helped change managers' thinking. The goal of managing up is not currying favor, they emphasize, it's becoming more effective. After all, relationships with key customers, suppliers, and vendors are crucial to your business success. Your relationship with your boss is simply another critical relationship.

What makes the boss-subordinate relationship a special case, however, is the power differential. To put it bluntly, your boss can fire you but you can't fire him. This power differential will always affect the dynamics of your interaction, resulting in "a certain degree of frustration" when your actions are constrained by your boss's decisions, write Gabarro and Kotter. "The way in which a manager handles these frustrations largely depends on his or her predisposition toward dependence on authority figures."

"Counterdependent" managers, they continue, unconsciously resent the boss's authority. Seeing the boss almost as an institutional enemy, they often pick fights—especially with an

> *The more thoroughly you understand the goals, constraints, and pressures under which your boss operates, the better you'll be able to help her succeed.*

authoritarian boss—just for the sake of fighting. At the other end of the spectrum, "dependent" managers "swallow their anger and behave in a very compliant fashion when the boss makes what they know to be a poor decision." Although altering your attitude toward authority is very difficult, "an awareness of these extremes and the range between them can be very useful in understanding where your own predispositions fall and what the implications are for how you tend to behave in relation to your boss."

This awareness is important, but not more so than understanding the wider context of the boss-subordinate relationship. As the subordinate, you may find it difficult to see the ways in which your boss "can be severely hurt" if she doesn't receive the "cooperation, dependability, and honesty" she requires in order to do her own job, write Gabarro and Kotter. In fact, the relationship is one of mutual dependence. The more thoroughly you understand the goals, constraints,

and pressures under which your boss operates, the better you'll be able to help her succeed. In return, she'll be more likely to link you to the wider organization, ensure that your priorities are aligned with strategic company goals, and secure the resources you need to excel.

How do you make good on your end and develop that thorough understanding of your boss's situation?

Begin with a discussion of goals and expectations. "Forty percent of my clients tend not to be aware of their boss's needs," says Relly Nadler, a psychologist and executive coach at True North Leadership in Santa Barbara, Calif. "There's a vague notion that they're just not clicking but they're not able to articulate why. I ask them to clarify their top five responsibilities with their boss so that both understand and agree on what those priorities are. That's a conversation everyone needs to have."

Few bosses spell out their expectations as explicitly and with all the detail that you'd like. Gabarro and Kotter cite the example of a new vice president of marketing at a recently acquired company who didn't know until it was too late that "improving marketing and sales had been only *one* of the president's goals." The president's most immediate goal had been to make the company more profitable in the short term because, as a strong advocate of the acquisition within the parent company, his credibility was at stake. As a result, the vice president "ended up taking actions that were actually at odds with the president's priorities and objectives," write Gabarro and Kotter. The lessons here: Don't take information at face value. Don't make assumptions about areas in which you lack information. Regularly seek clarification and updates about your boss's objectives—concerns and priorities have a way of changing over time.

In addition, don't focus only on organizational goals. Your boss's personal objectives can have just as much effect on how satisfied he is with your performance, as Ken Montgomery discovered while working for the CEO of a Silicon Valley IT outsourcing company.

"My team had achieved press coverage in many major publications, always around what the company was doing," says Montgomery. "What my boss really wanted was a splash in one of the new-economy magazines like *Fast Company* that focused on his personal contribution to the space. Instead of rolling my eyes and thinking this guy's got a major ego, I made it happen for him. Doing that small thing for him not only bought me credibility as an achiever, but greater trust and respect that resulted in getting his buy-in on projects that were important to me."

Pay attention to clues in your boss's behavior. One CFO that Relly Nadler was brought in to coach drove his boss crazy by always closing the office door when they were discussing things. The boss prided himself on

his open-door policy and felt that his CFO's action compromised his integrity. "I gave the CFO feedback that he didn't have conversations, he took prisoners," says Nadler. "While he was extremely competent in other ways, he never got himself out of that habit, and when there was a restructuring he was one of those released."

The boss's preference for an open door was more than a pet peeve; it was a symbol of his availability to his employees. By failing to notice that preference, Nadler's client was inadvertently sending the message that he didn't support one of his boss's strongly held values.

Observing your boss—paying special attention to her preferences about such things as meetings and modes of communication—offers many clues about how best to interact with her, note Gabarro and Kotter (see sidebar). Obviously, you score points with your boss by accommodating your work style to hers. But if impressing the boss has become your primary goal, you're missing the point. Eventually you'll undermine your own credibility with your boss, who needs to be able
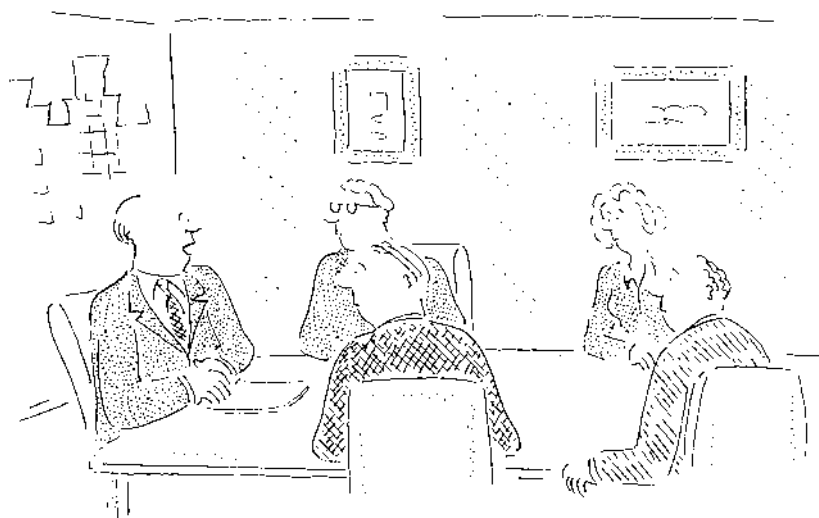
"Good point, Remson. You couldn't be more right if you were me."

to rely on you for an accurate reading of events.

But you don't have to deny your own goals in the process, says Anita Belani, senior human resources manager at a large high-tech firm. For three years, she worked as a member of the human resources team of a financial services company in India. Although she loved her job, her relationship with her supervisor was a constant source of frustration and anguish. Her efforts at managing up did nothing to instill a more respectful or collegial attitude in her boss, she says. Even so, their collaboration produced business results that other department heads noticed.

Eventually, Belani became HR director at a different financial services company, an opportunity that she doubts would have materialized had she left the first firm prematurely because of her difficult boss. "Managing up is not about changing your personality or giving in to your boss all the time," she says. Learning to adapt to the boss's preferred way of doing things actually helps you "maintain control of your career. Once you have that skill, you need never feel apprehensive about working for anyone."

Maintaining the proper focus

"Managing the boss is a constant, like being in a good marriage," says Deborah Singer Dobson, coauthor of *Managing Up.* "You don't go around saying you've done enough modifying your behavior for your spouse. We're all in the business of modifying our behavior on a daily basis in relationships that are important to us." Sharon Jordan-Evans, coauthor of *Love 'Em or Lose 'Em,* agrees. But once you and your boss have established a trusting relationship, she adds, the time you have to spend managing your boss should decrease dramatically. ❖

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Accommodating Your Boss's Work Style

Use the following questions as a starting point for determining how best to adjust to your boss's preferences, advise Harvard Business School professors John J. Gabarro and John P. Kotter:

■ **Does he prefer a more formal and organized approach?** Make sure that meetings with him have set agendas.

■ **Does she become impatient or inattentive** when you veer off the topic at hand? Keep digressions, background detail, and informal chitchat to a minimum.

■ **How does he process information best?** If he likes to be able to study it by himself, give it to him in written form. If he likes to be able to ask questions, present it to him in person.

■ **What is her decision-making style?** If she is a high-involvement manager, touch base with her often on an ad hoc basis. If she prefers to delegate, keep her abreast of important changes and major problems, but handle the other details on your own. Does she seem to have difficulty figuring out what she wants, often responding to your proposals, which you think incorporate her preferences, by saying that you haven't given her what she wants? What's probably happened is that she's continued to reflect on the issue after discussing it with you but hasn't kept you up to date on her latest thinking. You must take the initiative here to ensure that you're in constant contact with such a boss, frequently asking her to articulate her objectives, respond to your proposals and ideas, and let you know if there's anything else she needs from you. Document these conversations with follow-up memos; these will provide opportunities to correct any misunderstandings.

■ **How does he handle conflict?** If he seems to thrive on it, be prepared for lively, spontaneous exchanges with him; if they become heated, it's not necessarily a sign that he's angry with you. If he tends to minimize conflict, respect that preference without falling into the trap of telling him only the happy news. He needs to know about failures and important problems, but it may be best to inform him about these in private.

RESOURCES

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Managing Up: 59 Ways to Build a Career-Advancing Relationship with Your Boss by Michael and Deborah Singer Dobson AMACOM • 1999

Love 'Em or Lose 'Em: Getting Good People to Stay by Beverly Kaye and Sharon Jordan-Evans Berrett-Koehler • 2002

The Heart of Change: Real-Life Stories of How People Change Their Organizations by John P. Kotter and Dan S. Cohen Harvard Business School Press • 2002

"Managing Your Boss" by John J. Gabarro and John P. Kotter *Harvard Business Review* • January–February 1980

The Right Skills at the Right Time

In an era when connecting concepts, people, and communities is crucial, how can leaders learn to integrate the contradictory forces of individualism and interdependence?

"Y OU CAN HAVE the most wonderful qualities as a leader, but if they're wrong for the times, you'll be ineffective," says Jean Lipman-Blumen, a professor of organizational behavior at Claremont University's Peter F. Drucker Graduate School of Management.

As she explains in her 1996 book, *The Connective Edge: Leading in an Interdependent World* (Jossey-Bass), the evolution of leadership has witnessed three distinctive eras. Stage 1, the Physical Era, called for leaders to defend the physical boundaries that protected their group. In Stage 2, the Geopolitical Era, "geographical boundaries and ideologies still defined the important differences among us," and gave rise to authoritarian, "heroic" leaders. As Stage 2 is superseded by a Connective Era of increasingly close "connections among concepts, people, and the environment," managers are discovering that successful leadership in this third stage requires the knack for finding "commonalities that can bring people together."

Lipman-Blumen recently spoke with writer David Stauffer about how business and political developments of the past year have placed a premium on the ability to lead connectively.

Q: Why do you say that Stage 2 heroic leaders get publicity while Stage 3 connective leaders get results?

A: Heroic leaders want to capture the imagination of the media and push themselves forward; connective leaders are perfectly happy having less visibility. They don't believe they always have to take charge of every situation. They're often behind the scenes, collaborating with others and encouraging still-wider collaboration. They're willing to entrust others with some of the most important tasks. And they're often mentors. This is not the stuff of newspaper headlines or *Forbes* and *Fortune* covers. But the times demand connectivity. Our reluctance to give up Stage 2 ways of leading will increasingly stand in the way of being successful.

Q: For instance?

A: Look at the initial strategies of the current Bush administration. After taking office, they wanted to disengage, for example, by not joining in some international agreements. They said they intended to do only what was in our national interest, as if our national interest were neatly separable from the national interests of other countries. It was impossible. September 11 brought the issue front and center. This tragedy may demonstrate, in part, that none of us can ignore others who hold different values or who perceive us quite differently from the way we perceive ourselves.

Q: If connective leaders tend to avoid the limelight, is it impossible to identify one?

A: Occasionally an extraordinary event thrusts a connective leader to the fore. That happened after a fire destroyed three buildings at Malden Mills in Lawrence, Mass., in December 1995. CEO Aaron Feuerstein, whose grandfather had founded the mill, could have taken the $300 million insurance payment and said goodbye to Lawrence. Instead, he spent millions of dollars of his own money to provide three months' pay for all 1,400 of his temporarily unemployed workers. He replaced the destroyed buildings and kept those jobs right where they'd been. This brought worldwide acclaim to Feuerstein, which—in typical connective style—he had no taste for. But it brought to light a story that's different from the media story. Here is a leader who had been quietly connective for

> *Connective leadership makes the organization, not the individual, the hero.*

decades. He not only *said* his company and its workers were family; he treated them like family. And he's recently been doing it again, fighting on behalf of his people in the face of Chapter 11 bankruptcy.

Q: Do those bankruptcy proceedings say anything to you about the limits of connective leadership?

A: Malden Mills' bankruptcy came about presumably from the combination of several warm winters—not exactly controllable—and less expensive fleece manufactured by competitors. Taken together, these factors have resulted in weaker sales in overseas markets.

But that doesn't mean connective leaders don't bring something extra to the table. Feuerstein has a connective eye; he sees links among new ideas, products, places, and people. I think the creditors who want to replace him may not fully appreciate that Feuerstein leads in a more complex way that will only be more effective in a global environment. For example, he's looking to increase Malden Mills' competitiveness by opening a Polartec plant in Asia and by experimenting with

such innovations as electronic textiles. And the personal capital he's built up with his people works to the company's advantage.

Q: Why are American leaders particularly hard-pressed to move from authoritative to connective leadership?

A: I think it's a vestige of our frontier past. We're rugged individualists. We have a profound and quite American need to laud individual—as opposed to group—achievement. We want heroes, and we want to be heroes.

Q: So what chance do even well-intentioned leaders have of migrating from heroic to connective?

A: It's not easy, but the answer lies in making the organization, instead of the individual, the hero—the cause for which everyone is fighting. This cause becomes more important than any individual, and leaders, along with their supporters, are ennobled not by their heroic achievements, but by their contribution to the cause.

Connective leadership is becoming more of a necessity all the time. Think about the Internet and other forces in globalization. The world is far more tightly connected today than it was when my book was published only six years ago. What's clearer to me today is the challenge confronting leaders to integrate two simultaneous but contradictory forces—diversity and interdependence—that pull in opposite directions.

Diversity talks about our uniqueness; it's expressed in mission statements that say we're distinctive, different from any other organization. But the times demand interdependence, which speaks to mutuality: a focus on common interests and values, and on how we all need each other. It's still rare to find leaders who integrate both.

Q: As if that's not daunting enough, why do you say followers are more likely to question the leadership abilities of the connective leader than the authoritarian leader?

A: Many followers look for consistency in leaders. But connective leaders know that rigid consistency won't work anymore—not in a world of mind-boggling complexity and constant change. They employ a variety of styles in varying combinations, as called for by ever-changing situations. They *are* consistent, however, in their dedication to the organization and to high ethical standards.

Q: How can connective leaders convince their followers that they're on the right track?

A: At first glance, they may be seen by followers as erratic or flighty. Some may say, "This guy doesn't seem to know what he's doing," or "She's a hypocrite." But the leader gains credibility among followers through her authenticity, accountability, and ethics.

By authenticity, I mean the leader is consistently dedicated to the larger goals of the group—to the cause. Followers learn this over time, seeing that apparent inconsistency in behavioral styles or actions is directed at a more overarching consistency. So although they don't always immediately understand what the leader is doing, the followers still have faith that the leader is acting on behalf of the organization.

By accountability, I mean that the leader will always be willing to explain her actions—whether the outcome was a success, a failure, or ambiguous. In the U.S., we tend to think the exemplary leader says, "I take responsibility," and that the next words will be, "Let's put that behind us." Wrong. A leader should take a problem-solving approach to examining and explaining the failure. An

even worse mistake is to do what Arthur Andersen did—throw a scapegoat like [Andersen's lead Enron auditor] David Duncan into the arena to be gobbled up by the ravenous critics. That's not accountability.

Q: Why did that fail?

A: Because the world has gotten smarter and more interconnected. To suggest, as Andersen implicitly did, that its interconnectedness with Enron started and stopped with one person is ludicrous—and the public knew it. Today's organizations have vast and intricate interconnections, as Andersen and Enron did, through people, policies, and practices. Contrast Andersen's failure to act with what Warren Buffett did in 1991, when Salomon Brothers [now Salomon Smith Barney] faced serious charges. Some experts at the time predicted Salomon's indictment and demise. But Buffett, a Salomon investor and director, launched a housecleaning that swept out executives, processes, and policies. And he did this in full view of the Securities and Exchange Commission. There are significant differences between Salomon then and Andersen now, but I think they're comparable at least in this way: Buffett implicitly acknowledged modern interconnections; Andersen implicitly denied that they exist.

You may get away with a bad decision by not being called to account for it. But if you haven't put your misadventure out on the table for examination and reflection, you'll probably make the same mistake again. So accountability isn't just important for dealing with the external environment; it's also important for the internal health of the organization.

Q: What about the third element, ethics?

A: Ethics provides direction for the connective leader. He or she is headed

for a wreck when behavior is disconnected from an ethical compass. That's what happened to Bill Clinton. Here was a brilliant connective leader; he knew how to reach out to other groups and to bring people together. But he undermined himself because he lacked an ethical compass.

Q: **You maintain that Aaron Feuerstein has always been a connective leader. Is there any hope for the career-long authoritarian who wants to learn a new way of leading?**

A: Absolutely. Consider the advantages you have today, starting with technologies. The Internet is a metaphor for the Connective Era. The first time I was ever connected to the Web and hit on one link, and then another, I entered worlds to which I hadn't known I was connected. We're all interconnected, whether we perceive it or not, whether we do anything about it or not. But the technologies are only mechanisms. What's much more important is a mindset—one that impels you to seek commonalities with others, even those who are very different from you.

It's not enough to say you believe in connective leadership, any more than it is to say you believe in profits or motherhood. Your behavior has to demonstrate your belief. You don't necessarily give up skills that have made you successful; you expand your repertoire. Take the advice of that great management consultant Mae West: "When choosing between two evils, I always like to pick the one I've never tried before." ❖

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Putting Real Options to Work to Improve Project Planning

A decision-tree approach to mapping out your options can help you coordinate your decisions more closely with unfolding opportunities.

FOR MORE THAN a decade, consultants and academics have been touting real options valuation (ROV) as a means of improving the decision making that goes into a project. To date, however, ROV has not been widely adopted as a planning tool. Many project managers worry that the esoteric Black-Scholes equations frequently used to evaluate real options would require the addition of expensive software and a specially trained finance expert to the project team.

But Black-Scholes is not the only valuation tool available. The familiar decision-tree framework is well-suited to many of the contingencies that arise over the course of a project. When used as a strategic planning tool, decision analysis can help managers address issues such as how to allocate resources to ensure that the project meets specific deadlines, when to scale up or delay investments, and when to exit a project.

Matching the tool to the level and type of uncertainty

Much like a stock option, which gives the holder the right to purchase stock at a future date or at a set price, a real option gives managers a set of choices about capital investment that can be made as business conditions evolve. Think of it as a road map that optimizes decision making by enabling you to take multiple contingencies into account, plan your responses to them as they unfold, and phase your investments accordingly. When compared to net present value (NPV), the traditional formula for analyzing

financial decisions, ROV has obvious advantages.

NPV assumes conditions of low uncertainty: the market conditions are known, the costs to completion of the project are predictable, the technologies involved are reliable, and the odds of winning any necessary regulatory approval are favorable. Whatever uncertainty exists is not enough for managers to contemplate changing the strategic plan in response to any of the outcomes. Opportunities are evaluated based on current information, and the NPV calculation of the projected cash flow of the investment under consideration results in one of two choices: go or no-go.

Most business decisions, however, are not of the now-or-never variety. Rather, their strategic plans change in accordance with the magnitude of the uncertainty. By assigning a quantifiable value to uncertainty, ROV enables decision makers to gauge and react to risk over time—quite a boon in a world besieged by constant price shifts, fluctuating interest rates, fickle consumer tastes, and emerging technologies.

Is the nature of the project you're managing such that you can alter your investment or resource-allocation decisions as the uncertainty is revealed or resolved? If you can, then ROV can play a valuable role in developing a strategic map to guide you through the decision-making process. A second question helps you determine the appropriateness of the decision-tree approach to ROV: is the uncertainty occasional or ongoing? In some

arenas—energy and currency markets, for example—volatility is high and the future unfolds as an almost infinite number of possible outcomes. In most service industries and R&D–intensive industries, however, the uncertainties related to the management of a project tend to be milestone-driven. They arise as a result of a series of discrete choices presented under a limited number of scenarios; the decision-tree framework is best suited to such uncertainties.

Increasing value through project redesign

A simple decision such as whether to develop a new technology in-house or acquire it from an outside party illustrates the utility of the decision-tree framework. In-house development requires three years and leads to three possible outcomes. In two of these outcomes, the firm expects to create significant value. But there's also a 25% chance that the in-house development would fail; obviously,

this outcome would have no payoff. Figure 1 shows this decision using a decision-tree framework. The probabilities of the three outcomes are based on a combination of managers' experience and judgment.

After calculating the value of each alternative, the manager is able to pick the highest-valued alternative. For the acquisition alternative, subtracting the $10 million cost of acquisition from the $20 million payoff yields a value of $10 million. For each of the three outcomes in the in-house development alternative, you have to subtract the cost from the payoff and then multiply the result by the probability of success. Thus, for the most successful of the three outcomes, the expected value would be:

($25 million – $7 million) $\times$ .35 = $6.3 million

An expected value calculation—the weighted average of the outcomes,

with the probabilities used as weights—is used to blend the value of the three outcomes into a single number. A 10% cost of capital is used as the discount rate. Performing this calculation reveals the value of the in-house alternative to be $7.14 million, or less than 75% of the value of acquiring the technology from outside.

The decision-tree framework is useful not only for "organizing multistage projects that are subject to uncertainty," it can also help you redesign projects "for even higher value," writes management consultant Martha Amram in her new book, *Value Sweep.* Let's say that a manufacturing company is considering a $20 million investment to upgrade its existing plant so that it can introduce a new product line. This investment requires an additional $16 million in market research. If the research yields positive results, the company will proceed to launch the new product line. That launch is valued at $94 million (based on a discounted cash flow calculation). Both the infrastructure investment and the market acceptance have uncertain outcomes; those probabilities and a decision-tree diagram of the decision are shown in the top half of Figure 2.

Doing the calculations yields a negative NPV of $3.3 million for the project according to this initial design, which means that it's not worth doing. Another option is to redesign the project by running a smaller pilot market test while the infrastructure is being developed. Results from this pilot will help to resolve some of the market risk before the next decision point. If the infrastructure is successfully deployed, and the subsequent, comprehensive market research is successful, the project can move to product launch, saving time and money over the initial project design. The bottom half of Figure 2 shows a decision-tree diagram of the project after it has been redesigned along these lines.

Figure 1

A Sample Decision Tree: Acquire New Technology or Build In-House?

- Spend $5 million to develop a new technology over the next three years?
  - yes
    - 35% — Good initial results. Spend additional $7 million to complete. Payoff is $25 million.
    - 40% — Fair initial results. Spend $12 million to complete. Payoff is $20 million.
    - 25% — Poor initial results. Drop project. Payoff is $0.
  - no — Purchase technology for $10 million. Payoff is $20 million.

Today — Year 1 — Year 2 — TIME

Figure 2

The Gain from Project Redesign

Initial Project Design

Successful deployment?
yes (70%)

Spend $20 million on IT?

Spend $16 million for market research

Market acceptance?
yes (50%)

Launch products

no (30%) — Stop

no (50%) — Stop

Today — Year 1 — Year 2 — Year 3 — TIME

After Project Redesign

Successful deployment?
yes (70%)

Spend $20 million on infrastructure and pilot test?

Market acceptance?
yes (50%)

Launch products

no (50%)

Reassess plans and spend $14 million on additional market research

Market acceptance?
yes (80%)

Launch products

no (30%) — Stop

no (20%) — Stop

Today — Year 1 — Year 2 — Year 3 — TIME
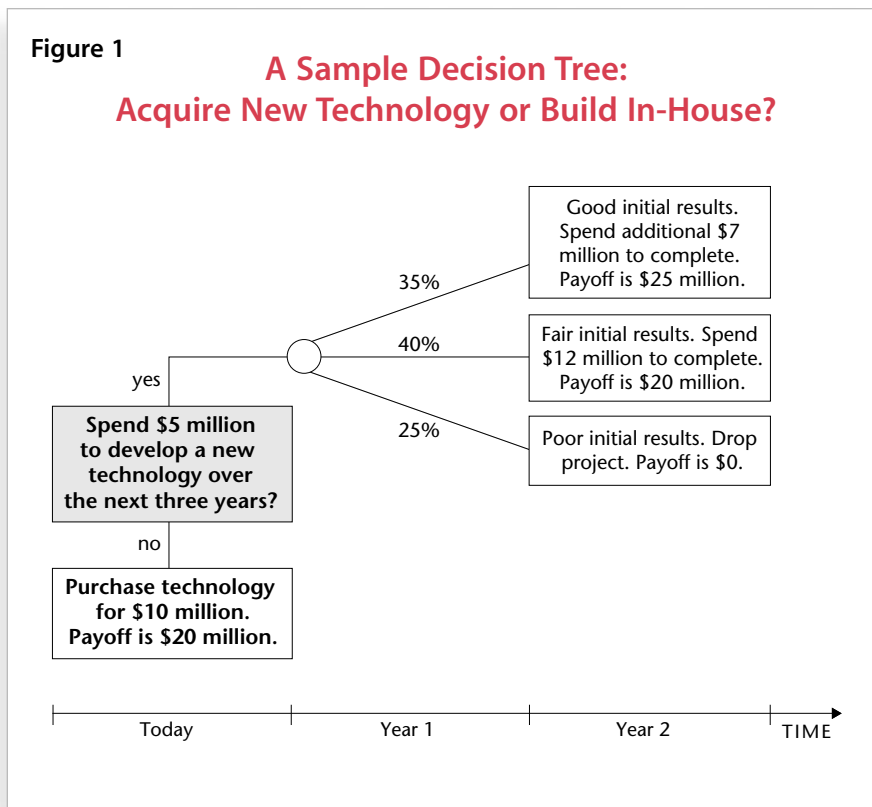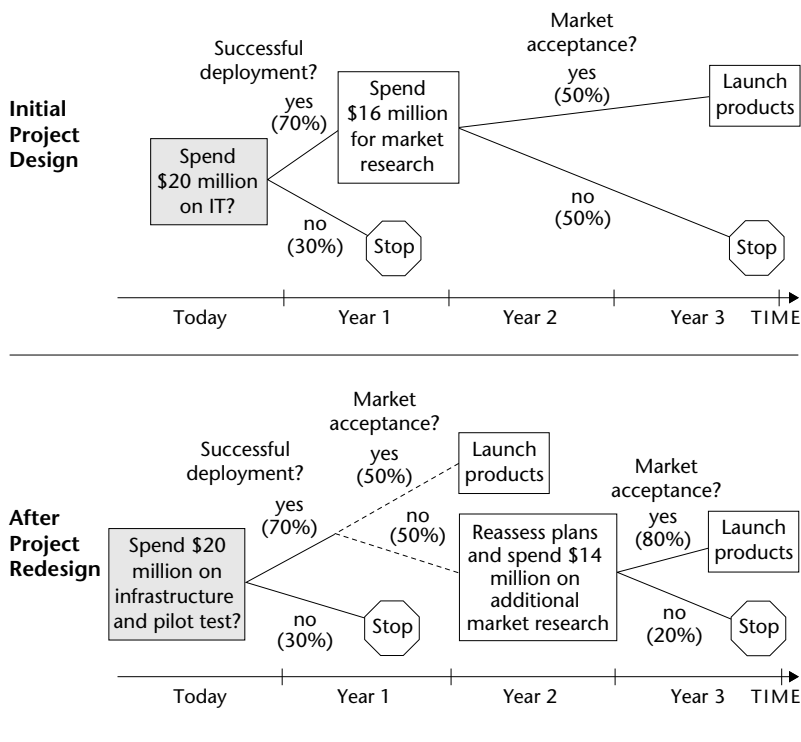

The redesign enables the value of the launch and revised marketing plan to be folded back into the initial investment decision. The result, when you do the calculations, is an increase in the value of the project from a negative $3.3 million to a positive $5.5 million. In addition, with the redesign there is only a 37% chance that the project will be terminated, whereas the original design had a 65% chance of being scrapped.

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http://hmurealoptions.harvardbusinessonline.org

Redesigning the project enables managers to learn more about the market at an earlier stage, thereby creating an opportunity to modify the marketing plan and increase the chance of market success. Under the revised plan, the project value increases because the follow-on investment is deter-

mined *after* some of the uncertainty has been resolved. The beauty of this decision-tree approach to ROV, therefore, is that it takes advantage of risk and uncertainty by tying expenditures more closely to the maturation of the opportunity. Breaking up the one market-research investment bet into two smaller investment bets enables the project manager to use options to improve his allocation of resources to the project as new information becomes available.

Process concerns

Decision analysis is not without its implementation problems. For example, it can be difficult to get the relevant scientific and technical personnel to agree on the probabilities of failure or success for each stage of the project. In particular, managers who are invested in the success of the project often believe that the probability of success is close to 100%. Moreover,

when a project is up and running, teams are frequently unwilling to discuss potential exit scenarios. This problem is particularly acute when managers have incentives to meet deadlines and milestones at any cost. The result is that midstream discussions about project closure are often biased.

To avoid these difficulties, make sure that you involve both business managers and technical personnel in creating the decision-tree diagrams. This will improve the buy-in that the project receives from both groups and will also make it easier to discuss plans for exiting the project if the outcomes are unsuccessful. Make sure that the two groups' incentives are aligned so that they are jointly accountable for the profitability of the project and the overall ROI of the portfolio of projects under way in your group. For instance, by giving rewards to project members for killing unsuccessful projects sooner rather than later, you increase the likelihood that even team members who have a strong personal investment in a particular project will agree to pull the plug if it's failing.

With these structural fixes in place, you're much better positioned to reap the chief benefit of the decision-tree approach to ROV: the improved coordination of spending with the potential outcomes of active learning. ❖

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RESOURCES

Value Sweep: Mapping Growth Opportunities Across Assets
by Martha Amram
Harvard Business School Press • 2002

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How to Build Organizational IQ

*On the other side of a change initiative,
you need to be sure that your company is
not just different, but smarter too.*

TODAY'S leading companies can't be accused of being unaware of the need for continual change—they launch change initiatives all the time. But often the efforts amount to running in place: the company maintains its relative competitive position, but it doesn't really learn anything that will help it respond better to the next unanticipated development. It doesn't get smarter, nimbler, or more resilient.

One software vendor we know tried to boost its competitiveness by overhauling its pricing system. But it failed to address the fundamental problem: the lack of an effective feedback process connecting the sales and product-marketing functions. Barely three months later, this new pricing system was rendered obsolete by a competitor's innovative scheme for bundling products—but only after the lost revenue reached into the tens of millions of dollars did the software vendor realize what was happening. Even then, its response to its competitor's move was hobbled by sluggish information flows and decision-making processes.

Judged on the basis of its original objective—removing barriers to sales by introducing a new pricing structure—the project was a success. But most of the benefits quickly vanished and the status quo reemerged. In too many companies, the results are similar. The change effort doesn't go deep enough: although the company changes, its organizational IQ doesn't grow.

A high organizational IQ is akin to a high individual IQ. It increases the organization's ability to discern what's significant in often unexpected events and then craft quick and effective responses. As with individual IQ, organizational IQ can be quantified. In a mid-1990s Stanford University study of 164 high-tech firms, the ones with higher IQ scores significantly outperformed their lower-IQ competitors in terms of profitability, growth, and shareholder value because they were consistently able to make better decisions in shorter time frames. But unlike individual IQ, organizational IQ can be systematically improved, especially along five key dimensions.

1 External information awareness. This dimension has to do with an organization's ability to capture and quickly distill key information about customers, competitors, and market opportunities. In 1996, Richard Archuleta, now senior vice president of operations at Hewlett-Packard's personal systems group, was charged with turning around the laptop division. The division's low external information awareness score indicated that it had lost touch with the market. Archuleta's first step was to open up communication channels to customers. He gave unfiltered customer letters and analyst reports wide distribution. He initiated open dialogues with customers and even included *lost* customers so that criticisms that had been suppressed could be recaptured and analyzed.

When Dorman Followwill became vice president of the health care practice of Frost & Sullivan, a San Antonio, Tex.–based marketing consulting company, the practice was hemorrhaging cash, primarily because there was no effective process for prioritizing research efforts according to customer needs. Followwill made customer councils mandatory: "No research report will be produced without an explicit audit trail back to a client request," he insisted. Three quarters later, the practice had held 60 of these information-gathering sessions; not surprisingly, its external information awareness had improved considerably.

2 Internal knowledge dissemination. If you want everyone making smarter decisions that contribute to the overall strategy, then you must streamline the information flows in the organization. Communications from the top down, from the bottom up, and between functions must provide the right information to the right person. Moreover, the amount of information that has only marginal value to the recipient must be reduced. Says HP's Archuleta: "We communicated constantly to share the strategy and current performance to help employees understand the changes we made and why we were doing it. This communication process was as important as the decisions made in moving the organization toward business success."

3 Effective decision architecture. The goal here is to ensure that decisions are made by the appropriate functions and at the appropriate levels. This enables the managers with the best information and perspective to react quickly to changes without having to wait for either higher-level approval or consensus among peers.

In HP's laptop division, the decision architecture led to delays and poor decisions from both a customer-need and cost perspective. "R&D held the keys to all major decisions, which left

marketing and manufacturing without the tools to contribute effectively to the business," recalls Archuleta. By assigning certain responsibilities to other areas—for example, handing over the selection of design and manufacturing partners to the manufacturing department—he was able to streamline the decision making.

Improving the decision architecture can also increase external information awareness. "A bad decision architecture locks your senior management team in the office," says Followwill. "A good decision architecture frees up senior managers to visit clients and drive strategic initiatives."

4 **Organizational focus.** By doing less—concentrating only on activities that are essential to achieving its strategic goals—a company often finds that it performs better. HP's Archuleta canceled a number of projects once he had sized up the situation. Even after "the organization thought it had cut down to a minimum set of activities, we forced ourselves to take out another product program," he says. "Cutting deeper than we initially thought possible allowed the organization to execute dramatically better." By 2001, HP had become the number-one brand in the U.S. consumer laptop market. By making small operational improvements, companies with high organizational IQs often generate market breakthroughs. An operational focus on "lessons learned" at the weekly review meetings of Frost & Sullivan's health care practice helped management realize that it could dramatically cut costs and increase customer value by providing Web-based access to its research reports. Breakthrough insights like this enabled Followwill and his team to make the practice highly profitable within a year.

5 **Information-age business networks.** To realize the full value of high-IQ management, you must look beyond your own company's bound-

aries. How can the strategic focus, decision architecture, knowledge dissemination, and external information awareness of your entire supply chain and distribution network be enhanced? Even well-managed companies have great room for improvement here.

According to Harald Hudak, a director at DaimlerChrysler's Japan operations who has led numerous successful change initiatives, "managers need to make sure organizational IQ is managed and tracked with the same rigor as financial and operational metrics." After all, a fundamental goal of management must be the improvement of the organization's ability to recog-

nize shifts in the environment, proactively decide what to do about them, and execute the decisions thoroughly and with dispatch. Absent the rigorous tracking of organizational IQ, a change initiative will end up addressing only today's problems. ❖

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FROM THE EDITOR'S DESK ■ BY LOREN GARY

Pinpointing Organizational Deficiencies

ORGANIZATIONAL IQ is more than just a metaphor for a company's ability to learn from its experiences, says Johannes Ziegler, CEO of the professional services firm Synesis (Mountain View, Calif.). It's a measure that can be quantified by surveying a cross-section of a company's employees to answer questions about each of the five dimensions of organizational IQ, calculating aggregate scores for each dimension, and then comparing the scores with best practices and averages from a database of more than 100 organizations worldwide. The views of the company's customers and business partners are also factored in.

In *Survival of the Smartest: Managing Information for Rapid Action and World-Class Performance* (John Wiley & Sons, 1999), Ziegler and his coauthor, Stanford Business School professor Haim Mendelson, outline a cheaper and faster version of this process, which relies on employee surveys and one-on-one discussions of the aggregate responses to generate an IQ profile for the organization. The purpose of such an "IQ Quick Scan" is not simply to document what is going wrong, but to understand why.

An IQ Quick Scan of modem-producer Modex revealed that a poor decision architecture and insufficient external information awareness were creating bottlenecks that prevented the company from reaching its full potential. Specifically, the root causes of the underperformance were micromanagement by senior executives, which made middle- and lower-level managers feel that they weren't empowered to make decisions, and engineers' and product managers' separation from the market (they had little understanding of what core customers cared about). By identifying these underlying causalities, the company was able to systematically address the most important issues. A second IQ Quick Scan, conducted six months after the changes had been implemented, revealed that Modex's scores for decision architecture and external information awareness had doubled. ❖

Quick Scans

Ideas and insights from other management publications…

The Role of Charisma in the Early Stages of Groups

STUDIES HAVE ALREADY highlighted the importance of charismatic leadership in times of crisis. The findings in **"The Antecedents and Consequences of Group Potency: A Longitudinal Investigation of Newly Formed Work Groups"** underscore the importance of charismatic leadership in the formation and early life of a new work group. Specifically, write authors Scott W. Lester, Bruce M. Meglino, and M. Audrey Korsgaard, the persuasive skills of a charismatic leader help increase the *group potency,* "the collective belief of a group that it can be effective." By serving as a role model and providing relevant task cues, the charismatic leader enhances the group's performance on initial tasks, which, in turn, increases group potency. Even if short-term goals are not achieved, charismatic leadership can "affect potency by creating confidence in long-term outcomes."

The Academy of Management Journal, Vol. 45, No. 2, April 2002
For a reprint, call 914-923-2607

Improving Informal Networks

ENHANCING THE WEBS of personal relationships that employees use to find information and do their jobs is not "simply a matter of more and better communication," write Rob Cross, Nitin Nohria, and Andrew Parker in **"Six Myths About Informal Networks—and How to Overcome Them."** Nor do more connections necessarily mean a more valuable network. Instead of asking, "Who is currently obtaining information from whom?" ask, "Who knows what?" This will help you identify areas in which the network is sparse. Possible remedies include changing your staffing practices—for example, having people work on a project in a different department at least once a year—and developing a searchable skill-profiling database in which employees record their expertise and experience as they learn new skills and knowledge.

MIT Sloan Management Review, Vol. 43, No. 3, Spring 2002
For a reprint, go to www.mit-smr.com

Giving an Acquisition the Gimlet Eye

GORE TECHNOLOGY GROUP (GTG) of Los Angeles has developed a reputation for buying distressed divisions of tech giants and breathing new life back into them, writes Adam Lashinsky in **"Five Secrets of a Turn-around Ace."** What makes GTG so successful? It takes advantage of the transition to reacquaint the acquired company with its customers and establish new rules. But perhaps most important, GTG is rigorous about asking the question, "What is this company good at?" Says president James Bailey: "All we do is open up the box and dump it out on the table. I don't have any feelings about what's in the box." GTG brings this kind of dispassionate analysis to the acquired company's overall business plan, aggressively renegotiating deals and deep-sixing plans that rely too much on blue-sky projections.

Business 2.0, Vol. 3, No. 2, February 2002
For a reprint, go to
www.business2.com/articles/mag/0,1640,36744,00.html

Boosting an Innovation's Chances

THE MORE THAT an innovation takes root in disruption—targeting "customers in markets that are unattractive to the [industry's] leaders"—the more likely it is to succeed, writes Harvard Business School professor Clayton Christensen in **"The Rules of Innovation."** In markets where "product functionality is not yet good enough," companies must compete by making better products," which typically means making components that fit together "in ever more efficient ways in order to wring the best possible performance out of the available technology." But when "the functionality of products has overshot what mainstream customers can use," firms must compete "through improvements in speed to market, simplicity and convenience, and the ability to customize products to the needs of customers in ever smaller market niches." In addition, if an innovation "helps customers do things they are already trying to do more simply and conveniently, it has a higher probability of success."

Technology Review, Vol. 105, No. 5, June 2002
For a reprint, go to
www.technologyreview.com/articles/christensen0602.asp