

February 6 2009

# Managing in a downturn

A weekly four-part series



## In this issue

### Part three Looking beyond the crisis

- 2 Keeping a keen eye on consumer behaviour** Marketers must respond to the radical shifts in consumers' spending habits brought on by the downturn but also ready themselves for recovery, write **John A. Quelch** and **Katherine E. Jocz**
- 4 Tasting the fruits of effective innovation** **Ranjay Gulati** and **Nitin Nohria** on how judicious R&D cuts can free up funds for more deserving projects and spur more imaginative use of external partnerships for long-term innovation
- 5 Sure way to tackle uncertainty in tough times** In a world of widespread insecurity, company leaders must develop crisis response plans and display behaviour that restores trust among stakeholders, writes **Neal A. Hartman**
- 6 Plugging in to transformation** Companies must maintain their investment in information technology infrastructure and Web 2.0 technologies to ensure long-term survival and growth, argue **Vasant Dhar** calls **Arun Sundararajan**
- 8 Does your M&A add value?** With deal activity slowing to a crawl, managers must look beyond indicators and focus on whether potential mergers and acquisitions add value for shareholders, say **Laurence Capron** and **Kevin Kaiser**
- 10 The time is ripe for fresh ideas** **Lynda Gratton** argues that recession represents an opportunity to abandon outdated management practices and experiment with innovations such as virtual working and wider distribution of leadership
- 11 Play fair with workers to reap rich rewards** Tough decisions and cost cuts are inevitable, but if properly executed they can avoid damage to employee morale and even clarify company identity and purpose. By **Batia Mishan Wiesenfeld**

## On FT.com

### The downturn in depth

**Video:** Sir Archie Norman, former Asda chairman, on how to rejuvenate a company that is facing difficulties

**Audio:** Henry Mintzberg of McGill University on why the prevailing management model is wrong – and how it needs to change

**Exclusive articles:** Willem Burgers asks if cutting marketing budgets in a downturn is the right decision; Jan-Benedict E.M. Steenkamp and Marnik G. Dekimpe look at how fast-moving consumer goods are marketed in a recession; and Campbell Harvey, John Graham and Murillo Campello consider how businesses are managing liquidity in the current context

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# Keeping a keen eye on consumer behaviour

Marketers must respond to the radical change in consumers' priorities but also ready themselves for recovery. By **John A. Quelch** and **Katherine E. Jocz**

**W**hat promises to be the longest and deepest global recession since the 1930s took many marketers by surprise. What appeared first as a crisis affecting the US home mortgage market soon morphed into a global financial meltdown and the evaporation of consumer credit.

Given an average household debt in the US of 130 per cent of annual household income, it was inevitable that a downturn in consumer confidence would follow, along with a substantial reduction in consumer spending, which accounts for 72 per cent of US gross domestic product. How should marketers, few of whom are experts in macroeconomics, respond to these conditions?

It is important is to understand how customers are reacting to the new reality, how their attitudes and

behaviours are changing, how easy it is for them to switch suppliers or stop buying your products and services, and whether the shifts that are evident today are going to continue once the economic recovery kicks in.

What is certain is that the market segmentation scheme you were using to plan your marketing budget and programmes this time last year is obsolete. You need to listen to your customers and possibly develop a new segmentation approach. We have identified six segments of consumers based on their response patterns to the current crisis.

We have found that the consumer mix varies across categories and across brands within categories, with stronger, trusted brands being less vulnerable to downward pressure on prices and margins:

■ **Naysayers** are frightened consumers who have stopped buying any

discretionary purchases and are trimming their daily purchases. They are, for example, trading down from fresh to frozen vegetables, sharing a single tube of toothpaste among family members and switching from single-purpose, specialised cosmetics to multipurpose products. They are either out of work, in fear of being laid off or know people who have been.

■ **Short termers** are younger, urban consumers with few savings who have, therefore, lost little in the financial meltdown. They will carry on as normal unless and until they lose their jobs. They will then have to adjust their consumption behaviour almost overnight, as they have no savings cushion.

■ **Long termers** are consumers who see the reduction in their retirement accounts as an unfortunate bump in the road. They are worried but not panicked. They are adjusting their purchasing behaviour by searching out the best deals, emphasising functional over emotional benefits, trading down to simpler versions of products they need, making fewer impulse purchases and foregoing some luxuries. However, they remain broadly optimistic and are not shutting down their consumption.

■ **Simplifiers** are baby boomers who have lost a significant percentage of their savings, and, as a result, have become more risk averse and are reassessing their values. Some will conclude that they must postpone retirement to recover their net worth. Others will decide that they can make do with less, reduce their consumption and simplify their lives.

■ **Sympathisers** are savvy consumers who switched into cash ahead of the crash but who know others who did not. They could afford to buy a new car but they do not want to appear ostentatious. They are continuing to spend at near-normal levels but more discreetly.

■ **Permabulls** are relentlessly optimistic. Their "here today, gone tomorrow" attitude has them looking for opportunities to make up for lost ground and find the next million dollar idea or stock pick. Their appetite for consumption remains constrained only by the availability of credit.

Marketers must understand how these six segments overlay their existing customer mix. They must understand the shifting price sensitivity of their current and potential customers and how it is affecting where and how often they shop. They must adjust accordingly the mix of marketing devoted to brand franchise building versus short-term promotions, such as coupons and rebates, that can sell products quickly, albeit at lower margins. In this recession, for example, the BMW 5 series may

gain relative share at the expense of the pricier 7 series. Sports car sales may decline but demand for hybrid vehicles may hold up better than the rest of the car market.

## Hope and change

Marketers must not be glum. They must balance an empathy for the financially distressed consumer with a resilient, perhaps even defiant, spirit of hope and optimism. The appropriate blend varies from one product category to another.

In general, consumers in a recession will screen out advertising messages that are based on fear appeals. There is enough uncertainty in the environment already. More appropriate are advertisements that emphasise the reasons, especially the functional features, to trust in a brand, evidence that a brand delivers value, and an emphasis on core benefits that relate to family values, friendships and relationships. Gillette's ads for its top-of-the-line Fusion shaving system justified the premium price by stressing its high-tech features, comparing the product's performance to Nascar race cars.

In the face of doom and gloom, we all need to be uplifted. Many brands in the US, for example, are attempting to piggyback on the enthusiasm for Barack Obama, US president. Ikea has called on consumers to change their furniture to mark the new president in the White House. Pepsi launched a new logo and ushered in 2009 with a celebration of "Optimismmm". Under the umbrella of a new slogan "Refresh Everything", the company's website invites consumers to submit their thoughts to "the man who is about to refresh America".

When consumer spending power is limited, marketers are not just competing to maintain or build share in their own stagnant or shrinking product categories. They are competing against all forms of substitutes and, in a real sense, competing against all other expenditures for their share of the consumer's wallet. Brands such as Pepsi and Coca-Cola that depend for volume on millions of consumers choosing them every day must continue to project positive messages in their advertising while ensuring that their pack sizes and retail price points are adjusted to cater for a more frugal consumer.

The best antidote to margin degradation, in good times or bad, is innovation. Some companies fear launching new products in recessions – with good reason if the product is merely a superficial line extension that adds little value. But an exciting new product that offers functional value as well as emotional appeal should

## Your guide to Managing in a downturn

### Week 1 January 23

- Introduction
- The roots of the downturn
- Scandinavia's banking crisis
- Japan's hubris
- Seizing golden opportunities

### Week 2 January 30

- Re-assessing risk
- Managing people
- Leadership
- Communicating the plan
- Rethinking the supply chain

### Week 3 February 6

- The nature of M&As
- Marketing in tough times
- Sustainable business
- Understanding customers
- Innovation

### Week 4 February 13

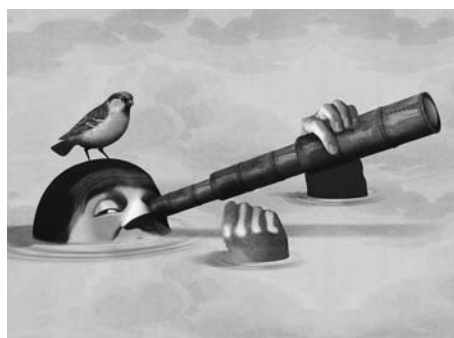
- A new business environment
- Is economic power shifting?
- Sovereign wealth funds
- Collaboration
- Banking and transactions

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not be held back. For one thing, the clutter of new products competing for consumers' attention will be less than normal. Second, if you delay until the recovery comes, you will join a backlog of new products all trying to secure shelf space at the same time. Third, delaying today's product launch may delay launches of additional products you have in the pipeline, permanently undercutting your competitive edge. Rather than delaying a new product launch, shape the value proposition to address the information and reassurance needs of today's target consumers while retaining the flexibility to tweak the positioning as necessary when economic recovery arrives.

**Change or die**

A recession is no time to hunker down. It is a time to question the strategic rationale for non-core assets and the fundamental assumptions of your business model. Monster.com, a recruitment website, generates almost all its revenues from job posters, not job seekers. This business model works well when times are good but not when employers are firing rather than hiring. Perhaps the model should be re-evaluated to diversify Monster's revenue streams.

More important, recessions often accelerate rather than decelerate underlying trends in consumer behaviour. Take use of the internet. With consumers spending more time at home rather than going out, internet use promises to increase. At the same time, consumers anxious about current and future job opportunities are more keen than ever to develop the networks that can help them with advice and job leads. Look for professional network sites such as LinkedIn

of the communications budget on search ads, banner ads and building brand community websites. Indeed, the major packaged goods companies, including Unilever and Procter & Gamble that do not sell their products directly to consumers online, typically spend a mere 2 per cent.

However, savvy marketers are accelerating their investment in and experimentation with digital media during the downturn. Kraft Foods, for example, is experimenting with the downloading of recipes to iPhones when consumers are shopping for groceries.

Many brands are running contests on their websites to encourage the creation of user-generated videos that are voted on by visitors to their websites. The goal is to build enthusiasm for the brand among a loyal cadre of consumers who will become the electronic spokespeople for the brand.

Of course, the recession demands adjustments in the communications mix to enable penny-pinching marketers to stretch their marketing dollars. These include substituting 15- for 30-second television ads; using less expensive radio ads instead of television to maintain advertising frequency to

**Marketers must balance an empathy for the financially distressed consumer with a resilient, even defiant, spirit of hope**

target customers; reducing outdoor advertising if fewer people are driving to jobs each day and others switch to public transport. But what is most important is to understand that the trend to digital is here to stay and to embrace it.

**Planning for recovery**

Conventional wisdom suggests that consumers return eagerly to their old attitudes and behaviours once a recession abates. Indeed, the theory is that pent-up demand during a recession is unleashed once consumer confidence rebounds and credit becomes more readily available.

This may well be true for durable goods such as cars and home appliances, which demand ever-increasing servicing costs the longer consumers hold on to them. It is, therefore, essential that manufacturers plan ahead to have the capacity available – whether internal or outsourced – to ramp up production and dealer inventories quickly. It is also predictable that, in emerging economies, consumers who were looking forward to owning their first television set or buying their first car will still want to do so once economic circumstances permit.

What is not so clear is whether all consumers in developed economies will revert to past behaviours. If the recession is long, as appears likely, new attitudes and behaviours are more likely to become ingrained. For example, preparing meals at home rather than eating out or buying in bulk are just two behaviours born of economic necessity that may continue after the recession ends. Coping mechanisms often involve collaborations with family, friends and neighbours that become a satisfying part

that we may find more pleasure in experiences than owning things, that less is more, these are questions that we are more likely to ask during an economic recession. In much the same way that life-changing events such as marriage or divorce may prompt us to reappraise our basic values and goals, so an economic shock can provoke a similar response.

In no industry will the challenge of understanding customer behaviour and market segmentation be greater than in retail financial services. Consumer trust has been severely shaken as the share prices and integrity of hitherto stalwart institutions have been undermined.

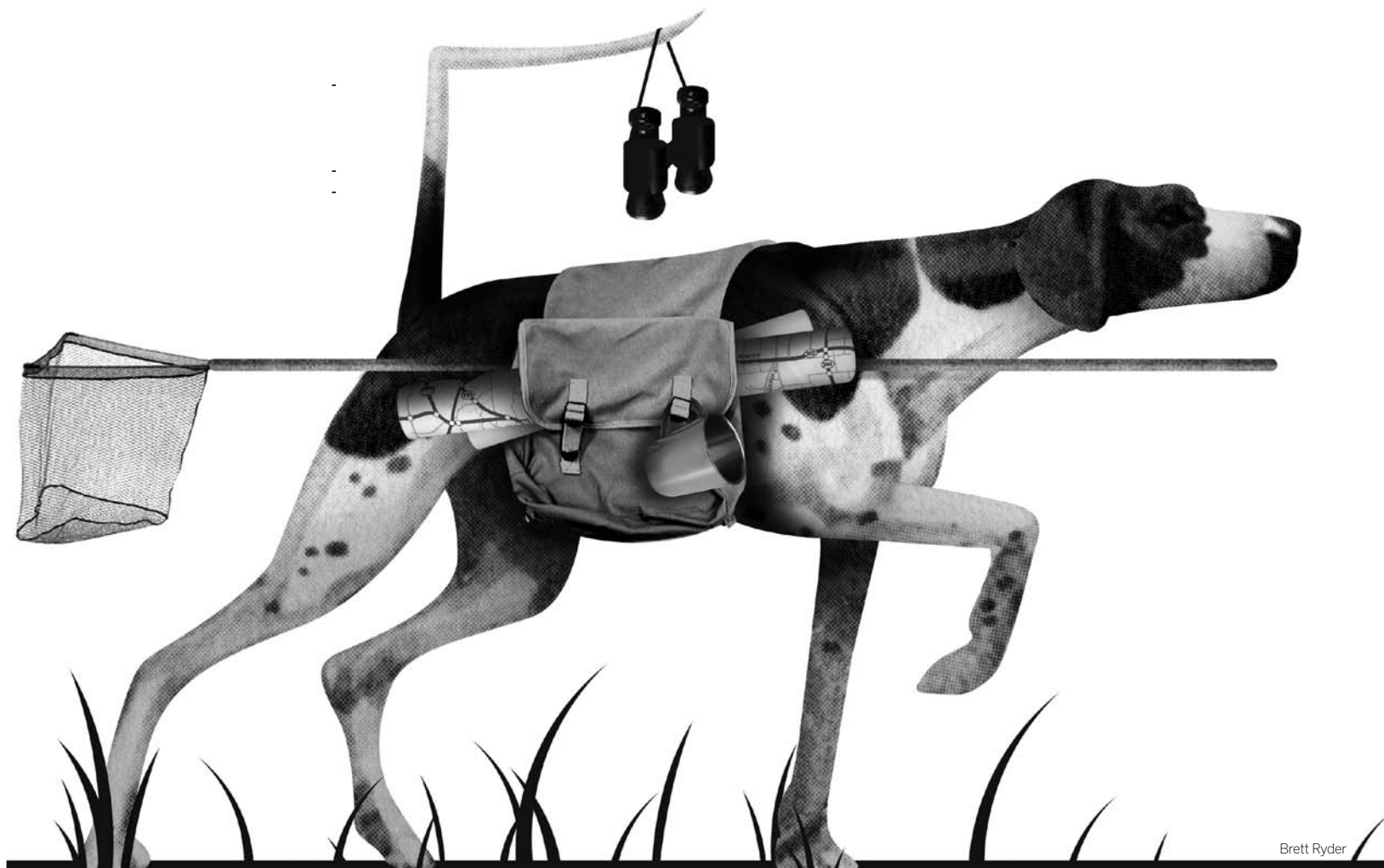
Millions of investors have seen their assets slashed. Many feel cheated. How will they respond to an economic recovery? Many will remain more cautious in their investment portfolios than they should be. A second group, probably smaller in number, will be more aggressive than they should be, feeling the need to make up lost ground.

Yet opportunities will emerge from the crisis. It was no accident that John Bogle launched Vanguard, the investment management group, and Charles Schwab founded his brokerage in the wake of the recession of the early 1970s. These companies introduced new value propositions that resonated with consumers. In the same way, new value propositions will emerge from the deficit of trust induced by the current recession. Existing companies need to watch out for the flank attack from such innovative newcomers.

Finally, in planning for recovery, every marketer must understand the leading indicators that will signal a turnaround in their industry and com-

**Further reading**

On FT.com, two pieces look in greater detail at marketing in a downturn: Willem Burgers asks if cutting marketing budgets is the correct response; and Jan-Benedict E.M. Steenkamp and Marnik G. Dekimpe consider strategies for marketing fast-moving consumer good brands. To read both articles, visit [www.ft.com/managingdownturn](http://www.ft.com/managingdownturn)



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# Tasting the fruits of effective innovation

Judicious cutting of redundant R&D projects can free up funds for more deserving projects and spur more imaginative use of external partnerships for long-term innovation. By **Ranjay Gulati** and **Nitin Nohria**

**R**ecessions bring cuts in the size of the labour force, in capital expenditures, in advertising budgets, in travel, even in the loss of coffee and donuts from our meetings. Sadly, investments in research and development and innovation, the seed-corns of our future, are not insulated from these realities either. Over the past four quarters, the total R&D expenditures of S&P 500 companies (based on the approximately 200 companies that report them quarterly) declined 13 per cent – from a total of \$43.1bn in the fourth quarter of 2007 to \$37.4bn in the third quarter of 2008 – with more cuts almost certain in the near future.

Companies wanting to innovate will have to do more with less. But how? The process boils down to three issues: determining the overall magnitude of cuts that need to be made; deciding which projects to cut and which to maintain; and reconsidering the locus of innovation, including whether it can be done outside the traditional boundaries of the company.

## The magnitude of cuts

Some reduction in R&D investments might not necessarily hurt an organisation's innovative capacity. During good times, companies tend to become lax in choosing which R&D projects to support. In a study of large multinational corporations, we found that the relationship between innovation success and resources deployed was curvilinear.

Too few resources stymied innovation, but so did too many resources, by breeding a lack of discipline and by diminishing the incentive to bring innovation projects to fruition. As with downsizing, some degree of R&D cuts can actually be productive, but going too far risks permanently shrinking the bottom line.

## Where to cut

Managers must be judicious about which innovation projects they support. The example of one big US electronics manufacturer during the 1990-92 recession is instructive. Told to trim his spending by 30 per cent, the head of R&D called a meeting of

everyone involved in leading the approximately 300 R&D projects then ongoing in the company. (The exact number took more than a month to pin down.) Over the course of an entire day, he forced the group to go through a series of exercises designed to slash the R&D budget by 50 per cent, well beyond the target. The process was painful, but by the end of the day about 200 projects to be axed had been identified.

He then asked managers to identify which of the 100 projects that remained could most benefit from additional spending. About 30 projects were identified, with some of their budgets increased by as much as 100 per cent. The results were stunning. More new products were brought to market that year than ever before, and the company felt it had finished the year with an even healthier innovation pipeline than it had started with. The moral of the story: do not think just about the innovation projects you can cut. Think also of how you can free up resources to give a boost to the projects with the best pay-off.

We label this the “4-4-2 Approach” – cut four, maintain four and double-up on two – but it comes with a caveat: beware that you do not overuse the approach to privilege what organisational theorist James March calls “exploitation”-oriented innovation – projects that can generate revenues most quickly or have the best short-term pay-off – over “exploration”-oriented innovation with more distant pay-offs that nonetheless might be vital to the company's long-term prospects.

The key lies in the mix. In the example discussed above, the company was careful to continue to invest in

**Too few resources stymied innovation, but so did too many resources, by breeding a lack of discipline**

both, which is why it was able to strengthen its innovation pipeline while increasing the immediate flow of what came through the pipe into the market.

In cutting R&D budgets and projects, globally distributed companies must also be careful not to privilege ideas championed by the centre – those closest to the company headquarters and the traditional seats of power – at the expense of ideas championed by those who work in the company's international locations.

Projects at the centre are often marquee initiatives that the company can benefit from across the globe, what our colleagues Chris Bartlett and Sumantra Ghoshal have called “global-for-global innovations”. But local-for-local innovations can sometimes grow into local-for-global blockbusters. Consider, for example, the small, rugged portable electrocardiogram monitor that GE Healthcare developed in India to serve local rural markets but which ultimately found markets in many other countries. In a world where the emerging markets of today may become the most important markets of tomorrow, protecting and nurturing such local innovations through the current downturn is essential.

## The locus of innovation

The current turbulent R&D environment is also leading many companies to relocate the locus of innovation beyond their own boundaries. Increasingly, companies are discovering the advantages of collaborating with a range of external entities, from suppliers to universities to customers, for novel ideas. In some instances, they rely upon these external entities to autonomously produce innovation and in others they actively collaborate with them. Procter & Gamble, for example, has famously made this strategy an enterprise-wide mantra that it loosely describes as “connect and develop”.

The benefits of externalising innovation are obvious, ranging from cost sharing to leveraging potential economies of scale. Outsourcing innovation can allow companies to both contract and expand their own footprint at the same time. As they move to aggressively reapportion R&D, companies increasingly shrink what they might consider to be “core” activities. At the same time, they also become adept at entering into collaborative ventures in areas that allow them to expand their domain of innovation.

This simultaneous contraction and expansion can play a key role in enabling both top-line and bottom-line growth, but there are several roadblocks to get round. The first is

“core confusion”. Some companies hesitate because they are unwilling or unable to reconceptualise what they consider to be core activities and end up clinging to more than they should under the mistaken assumption that certain domains are of necessity core.

The key distinction here is between “core” and “critical”. Critical tasks are things such as clinical trials which, while vital to the business, do not necessarily provide much advantage in the marketplace. Core tasks, on the other hand, are those that provide companies with a unique advantage in the marketplace. Elements of innovation that are critical but not core can easily be externalised in ways that ensure reliable delivery from an external entity without in any way compromising marketplace advantage.

## Apple's shrinking core

Perhaps no company has shrunk its core and expanded its periphery more adeptly and to greater advantage than Apple, and no Apple product better illustrates this than the company's iPhone. In creating its first mobile phone, the company leveraged the engineering capabilities of its partners, thus allowing Apple to design and deliver innovative products in record time and in a much more cost-effective way than it could have done on its own. So, while Apple created its own operating system, it partnered with developers such as Google to preload applications such as Google Maps on to the device.

Similarly, most of the hardware in the iPhone and all of the manufacturing of it have been outsourced. Apple carefully guards information on its supplier partners because it views this as a key source of strategic advantage, but shortly after the device was launched in June 2007, iSuppli, a third party, took the handset apart and found a global representation of third-party companies.

Much of the phone's core communication capability came from German semiconductor supplier Infineon. Balda, another German group, provided the display module. The touch screen itself was provided by multiple sources including Japanese groups Epson Imaging Devices, Sharp and Toshiba Matsushita Display Technology. South Korean company Samsung provided the applications processor and the technology for the phone's memory. iSuppli added up the estimated cost of the entire set of inputs, and calculated that the margins for Apple were likely in excess of 50 per cent.

Apple's partnership with AT&T, the sole carrier compatible with the



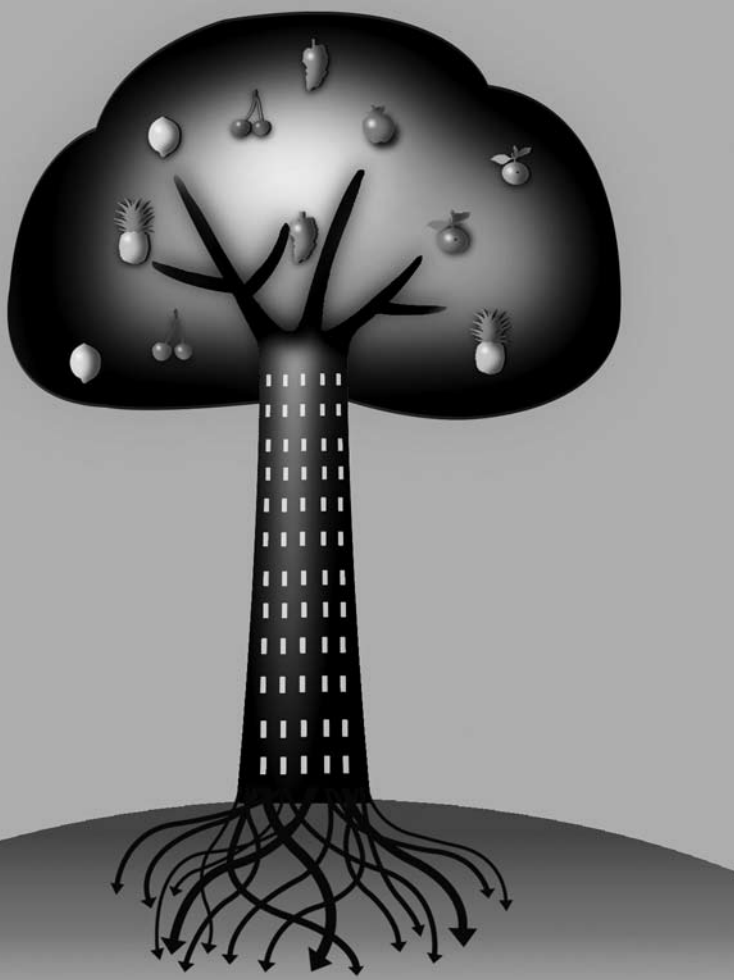
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# Sure ways to tackle uncertainty in tough times

Company leaders must develop crisis plans and display behaviour that restores trust among stakeholders. By **Neal A. Hartman**



Nick Lowndes/Eastwing

iPhone in the US, allowed Apple to expand its periphery while also giving its partner a significant upside, including five years of exclusivity, approximately 10 per cent of iPhone sales in AT&T stores, and a small piece of Apple's iTunes revenues. In return, Apple persuaded AT&T to spend considerable time and resources to develop a new feature called "visual voicemail" and to streamline the in-store sign-up process.

Perhaps the most vivid example of Apple's periphery-expanding alliances has been the array of partnerships it has formed to develop applications and peripherals that are sold to customers in the growing numbers of Apple stores or via its online store.

## The perils of open innovation

Despite the obvious lure of open innovation, especially in perilous budget times such as these, two issues need to be tackled to fully leverage the potential advantages this has to offer. First, skilful companies recognise that a shift towards open innovation must be balanced with a strong anchor around their customers. It is tempting in an open-innovation model to be a technology-push company where countless ideas emerging from a large partner-base are funnelled through to customers in a dizzying array of offerings.

But companies must understand how to balance this push model with

**By choosing which projects to cut, protect or even expand, companies can do more with less**

a customer-driven pull model as well. They need to find ways to funnel customer insight to their partner base while at the same time allowing partners to open up new frontiers that might go beyond customer imagination.

Apple has succeeded in finding a balance between what it thinks customers want and what they might need. The company directs its partners on key input requirements while allowing them considerable freedom to develop what they consider to be desirable for customers.

As collaborative innovation moves to centre stage for companies and permeates their core, they also have to recognise the importance of developing expertise in managing their growing array of partnerships. Collaboration does not come naturally to most companies.

However, the pioneers in this movement understand the importance of building a relational capability within the company. They not only embrace a set of routines and processes to become better at identifying partners and negotiating agreements, they also embed a collaborative mindset into their culture. These shifts require concerted and systematic effort.

## Conclusion

Reductions in R&D budgets may be inevitable for most companies in the present context. But if made intelligently, these cuts do not have to hurt innovation. By choosing which projects to cut, protect or even expand, companies can do more with less.

Moreover, by becoming more adept at shrinking what they consider core while leveraging partners who can help them innovate in ways that are genuinely customer-centric, companies can embrace a more open approach to innovation that may pay lasting dividends, even when the economy recovers. ■

**A**s the global economy slows, managers face a more uncertain business environment than they have probably ever known. Successful executives will shape the future by developing a strategic plan. Uncertainty can be seen as a threat, or it can be viewed as creating possibilities.

We do not know how governments will respond or how global financial systems will behave, but managers need to examine their company and industry and consider the overall economic trends.

## Challenges in a downturn

How can companies attract and keep talented employees? How can leaders reduce the amount of uncertainty surrounding their organisation? And how do managers create a company culture that can thrive in uncertainty?

Communicating clearly, consistently and honestly is key. Consider recent developments at Apple. When photographs appeared in the press showing a much thinner Steve Jobs, investors worried. Mr Jobs, the company's chairman and CEO, issued a statement to put rumours about his health to rest and this helped ease investors' concerns. Shares in Apple fell again, however, with the news that Mr Jobs' health problems were more complex than previously thought and that he was taking leave, although he would continue to be involved with key decisions. Now Apple must work hard to alleviate the uncertainty that investors perceive.

Managers need to deal with uncertainty directly. It is important to understand that people perceive uncertainty in different ways and managers should nurture the idea among stakeholders that uncertainty brings possibilities, rather than seeing it just as a threat. Managers must also share information; it is generally assumed that the more input people have into change, the more they buy into company goals.

Managers who consistently display their values and beliefs through their behaviour have a significant impact on the culture of the organisation. If employees understand that the company leaders view uncertainty as something that offers opportunities, this will be embraced throughout the organisation.

## The value of planning

Although no company can develop a strategy that addresses every uncertainty, having a crisis plan in place will help, regardless of the situation that arises. It is doubtful that before September 11 2001 any of the organi-

sations housed in New York's World Trade Center would have considered the possibility that aircraft would be flown into the buildings. Yet those companies that had a crisis plan in place dealt more effectively with the crisis and uncertainty following the event than those that had no plan.

Managers developing a plan should begin with research, using internal resources as well as outside consultants. Managers should look broadly at ideas, borrowing from other companies where appropriate. Companies should perform scenario analyses by predicting potential uncertainties, identifying relevant risks and simulating events. A team needs to be in place to deal with the events and address stakeholders; this ensures clear and consistent messages. Plans, once devised, must be constantly reviewed and revised.

Organisations must also be flexible and have the ability to quickly and efficiently try new methods in the face of changed circumstances. Developing this organisational flexibility should be a central objective of any company.

## Mastering uncertainty

Managers must also pay close attention to their own actions during uncertain times. Because many people perceive uncertainty as frightening, leaders need to display behaviour that brings about a sense of trust and credibility. Uncertainty is often a source of stress, but it is how people react to this stress that determines the kind of decision-making that occurs. Effective managers are those who develop the emotional maturity to behave rationally and confidently in stressful and uncertain situations and they must nurture this ability in their employees as well.

Managers should also build social support systems, both inside and outside the organisation. Managers who work with effective teams can share experiences and gain new insights, enabling them to deal more effectively with uncertainty and sudden change.

Because uncertainty is stressful, it is important that managers learn how to manage stress. A person's ability to deal with uncertainty is better if they exercise, maintain a healthy diet, sleep well and talk about the issues. If one considers uncertainty as a vehicle of possibilities rather than a threat to current norms, the attitude is much more positive.

Managers in the 21st century must be ready to deal with the threats uncertainty brings and to think boldly and creatively about the possibilities it offers. Organisations with managers who are able to do so will prosper for years to come.



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# Plugging in to transformation

Maintaining IT investment is even more vital for survival than it was in past downturns. By **Vasant Dhar** and **Arun Sundararajan**

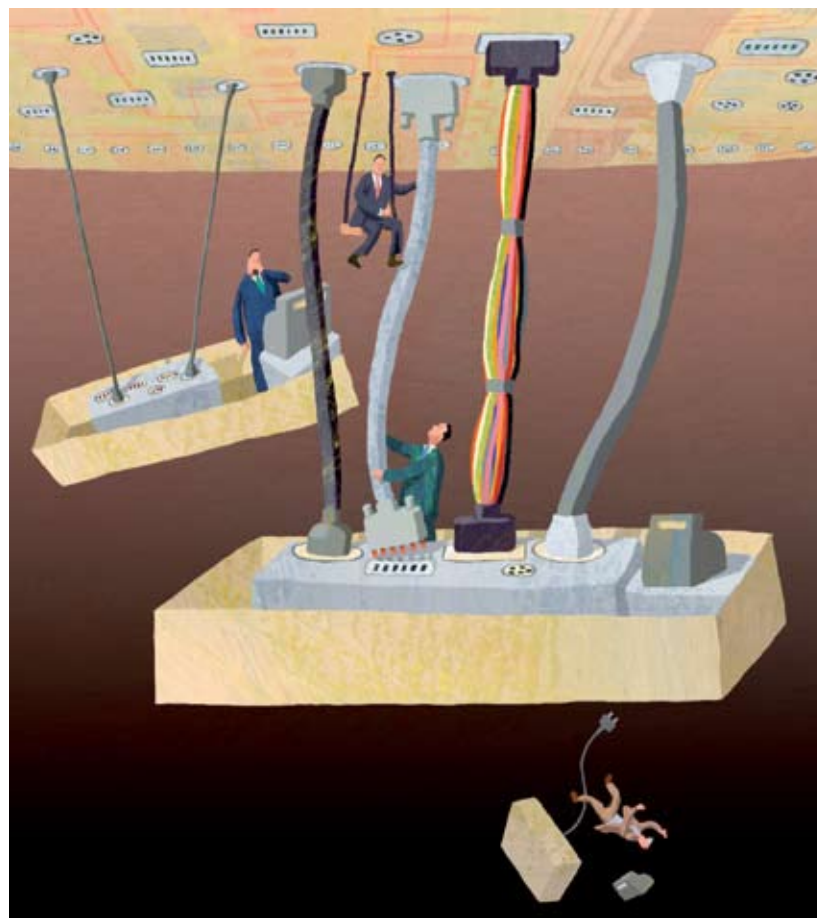
**T**he current downturn is unique because it is happening in the midst of a rapid transformation of business by information technologies. This transformation has been driven most recently by the widespread adoption of broadband and Web 2.0 technologies, mobility enabled by increasingly powerful wireless devices, technological platforms of unprecedented functionality, and the emergence of commercially viable computing clouds and software services.

These turbulent economic times present new opportunities for companies that invest wisely in information technologies, and new threats for those without a sufficiently forward-looking IT investment strategy. Opportunities arise because downturns can change consumer preferences, making people experiment with new lower-cost products or modes of consumption that were not pursued seriously during more prosperous times. Dangers arise if IT spending is conducted without careful assessment of the long-term impact. This is more likely when executive attention is devoted excessively towards short-term earnings management and cost control.

## IT investment strategies

So, what is the right IT investment strategy during this economic downturn? Our academic research frames three kinds of IT-related business decisions: those that react to or cause “industry transformation”, where business models are fundamentally altered by progress in information technologies; those that increase operating efficiency or productivity through the use of IT infrastructures, enterprise systems or transactional systems that enable economies of scale or complexity; and those that lead to acquiring and leveraging various kinds of “customer intelligence” enabled by technological systems that better connect customers to products and companies to consumers.

Viewing IT investment strategy through this lens requires varying one’s recessionary reaction based on which kind of IT-related decisions one is contemplating. First, IT investments associated with pending or ongoing business model transformation should be continued or ramped up. The recession will not change the fact that the basic business models of numerous industries have been and will continue to be changed by IT over the coming years. Furthermore, such transformation persists in both good and bad times. For example, the financial brokerage industry was transformed by the widespread adop-



Alastair Taylor/Inkshed

tion of online consumer trading systems during the build-up to the dotcom boom of the mid to late 1990s.

In contrast, the wrenching digital transformation of the music business over the past few years was affected most critically by decisions made soon after the dotcom bust in 2000. While the roots of change were evident in the emergence of the MP3 digital music format and peer-to-peer file sharing, record labels failed to make intelligent decisions about their IT strategy, shifting market power dramatically to newer intermediaries such as Apple, which exploited emerging technology platforms and changing user preferences to become the world’s largest music retailer.

In industries characterised by business model transformation during downturns, it is especially important not to focus excessively on short-term IT cost control. Downturns can accelerate the pace of transformation, making it critical to think about the opportunities and threats engendered by the combination of changing preferences and technological change.

An example is video entertainment. Increasingly, consumers of conventional television and film content are also turning to alternative forms of video entertainment that are exclusively internet-based. The recession is likely to reduce spending on cinema tickets and DVDs, prompt consumers to reassess expensive cable subscriptions and shift consumption towards lower-cost online video content.

As more consumers make this switch, it is essential that film studios and TV networks invent a viable business model, rights management strategy and delivery infrastructure that supports revenue-generating digital consumption. Withdrawing their IT investments and business model

development as a cost-cutting measure could have a disastrous long-term effect on the current market leaders.

Decisions about investments in infrastructures and systems that contribute towards operating efficiency can be made more conservatively. Returns from IT infrastructure investments tend to take years rather than months to materialise. Further, they do not show up unless augmented by substantial organisational and employee behaviour re-engineering, which may be hard to implement during a period of widespread hiring freezes.

## Downturns induce innovative investments

In parallel, cost reduction pressures will catalyse the transition from proprietary to shared infrastructures that tap into cloud computing platforms and software as a service. These new models of corporate computing are likely to replace self-owned IT systems for non-mission-critical processes and applications. The current downturn may provide the impetus organisations need to invest in the assessment and transition planning necessary for successful migration to these lower-cost IT infrastructures.

## Withdrawing IT investments as a cost-cutting measure could have a disastrous effect on current market leaders

Decisions relating to the use of information technologies to acquire and use customer intelligence are affected in various ways by the downturn. In a recessionary economy, customer retention is critical to a company’s survival.

At the same time, the internet has enabled an explosion in access to electronic data, which is becoming increasingly important to truly “understanding” people through their data trails. User-generated content is widely prevalent as people become increasingly connected and spread information about even the most obscure of topics.

Businesses can access this data relatively cheaply, thus creating the potential for IT investments that increase customer intelligence and improve the business intimacy of consumer contact. For companies that do not currently leverage electronic customer data as an asset, now might be the time to carefully assess how this could support current and future business strategy.

This assessment needs to recognise that the basic model of customer contact and marketing is being transformed by online advertising and Web 2.0 technologies, whereby companies move away from directly influencing their customers and towards either reacting to their customers’ electronic intent, or mediating the influence that consumers have on one another.

At the same time, companies are now positioned to use “crowdsourcing” technologies to obtain more complex intelligence from their customers. The richness of this intelligence is expanding substantially through the use of interactive product design that involves frequent and active electronic consumer input; from open research and innovation through the use of development contests; and from superior forecasting and business intelligence acquisition through the use of prediction markets. As customer preferences evolve in reaction to the recession, acquiring intelligence through aggressive Web 2.0 investment strategy is critical. The simple user-generated content we have seen substitute company-generated messages is just the tip of the iceberg.

## Conclusion

We are analysing a unique point in history. Previous downturns occurred during times when our IT infrastructure was primitive relative to what exists today. Information has become plentiful and relatively cheap as a torrent of content flows from users to an increasingly interactive web while people simultaneously leave richer electronic data trails of their behaviour. Against this backdrop, missing the IT investment boat could set companies back more than it has done in the past.

Decisions about these investments need to be forward-looking in a way that includes an assessment of relevance to both current and anticipated future business models. Curbing spending with a short-term focus will eventually cost more than it saves, while IT investments based on an intelligent framework could generate long-term gain.

## Further reading

To find out more on how Prof Dhar and Prof Sundararajan think managers can engage with new technologies, visit <http://w4.stern.nyu.edu/emplibary/techstrategy.pdf>

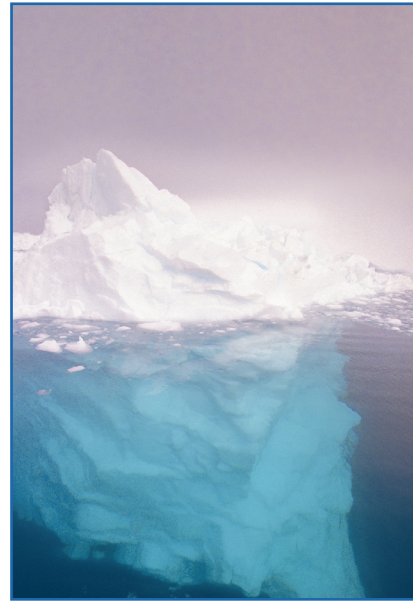


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# What lurks beneath the surface can sink your reputation.



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# Does your M&A add value?

With deal activity slowing to a crawl, managers must look beyond indicators and focus on delivering shareholder value. By **Laurence Capron** and **Kevin Kaiser**

**T**he market for corporate control is facing a downturn. Thanks to tough borrowing conditions, depressed stock values and the slumping global economy, the value of merger and acquisitions transactions cancelled since the beginning of October almost equals the value of deals that have been completed, according to data compiled by Thomson Reuters. Those figures do not, however, include withdrawn deals for which values were never publicly disclosed. Notable withdrawn deals include the \$147bn bid for Rio Tinto, the Anglo-Brazilian mining group, by BHP Billiton, the Australian mining giant; and the failed \$48.5bn buy-out of Canada's BCE telecoms by a consortium of private equity groups. The total volume of worldwide M&A deals globally fell 29 per cent in 2008 compared with 2007, with the US (down 32 per cent) and Japan (down 45 per cent) particularly hard hit.

The reduced activity in the market of corporate control, along with the collapse of iconic companies in the advisory community (investment banks, rating agencies, commercial lenders, consultants, lawyers, accountants) could be perceived as a big blow to many companies for whom acquisitions have been the preferred growth strategy in past decades. When carefully chosen, priced and executed, M&As help companies create value by providing access to new technological or human resources, exploiting learning opportunities, meeting customers' needs, exploiting economies of scale or restructuring industry capacity.

However, the current slowdown in M&A activity, notably for large transactions, could provide an opportunity for companies to think more carefully about their M&A strategy and the process they have been using to buy companies. Indeed, M&As in past decades have, on average, destroyed value for the acquirer's shareholders. It is therefore timely to step back and better understand the functioning of the market for corporate control in which companies operate.

## Failures in the market for corporate control

Whereas acquisitions have been touted as a value-creating tool, most companies have failed to add value through acquisitions, at least in terms of shareholder value. Beyond the oft-cited reasons (failure to deliver on synergy potential, paying too high a price and integration issues), the root cause of most failures is the incentive system that encourages managers to ask the wrong questions.

Managers should ask how a potential acquisition might improve their company's ability to meet customer needs in ways that cannot be easily matched by its competitors. They should value this using expected future cash flows to ensure that the pur-



Nick Lowndes/Eastwing

chase price does not exceed this future value. However, most managers ask very different questions, such as: how will this impact on our earnings per share?; how will this impact on our growth rate?; how will this help us to reach market share targets?; and how will this impact on our share price and my options pay-offs?

All targets on such indicators can be achieved by one of two methods: creating value or destroying value. The difference hinges on the expected value of the benefit realised relative to the price paid to obtain it. Whenever a manager delivers on an indicator, the question should be: "What is the value of delivering on the target and what will I have to pay to do so?"

It is important to distinguish between the overriding objective for companies, which is value creation, and the indicators that measure how well they are delivering on this objective which include, share price, EPS, market share, growth in any given indicator, customer satisfaction, etc. Most managers pursue incentives based on these indicators. The result is that managers knowingly destroy value in the pursuit of promotions/bonuses/option scheme pay-offs.

One symptom of these incentive compensation schemes is an undue focus on company size rather than value creation, due in part to the practice of benchmarking CEO compensation across companies of similar size – bigger being better. The result is that managements are willing to overpay for acquisitions and are encouraged to do so by advisers whose primary interest is often ensuring that the transaction takes place rather than ensuring that the acquirer creates value in the process.

## Misaligned incentives and the current crisis

This combination of misaligned incentives and a focus on indicators rather than value contributed to the decisions made by bankers and mortgage brokers, among others, that led to the current financial crisis.

Finance and strategy scholars have found evidence of incentives misalignment between investment banks and their clients that arise when banks put their own fees and brokerage commissions ahead of client interests. Within the M&A context, powerful incentives within M&A advisory banking – such as the advisory teams' bonus pool and the bank's desire to advance in the M&A league tables by increasing deal numbers and volumes – may conflict with the interests shareholders.

The M&A advisory community has played a significant role in the failures in the market for corporate control. This community, from investment bankers to corporate lawyers, uses incentive systems that push for aggressive transaction execution. Certification agencies have failed to provide reliable estimation of company quality and viability. This violation of

**Reliable advisers with the skills to assess and advise on the value impact of M&A opportunities will gain importance**

shareholder trust has seriously damaged the M&A advisory community's credibility and this is likely to impact on the role in future. We believe that reliable advisers with the skills to assess and advise on the value impact of M&A opportunities will gain in importance.

## Navigating the current M&A market

In the current situation, companies will need to resourceful and creative to navigate through frictions in the M&A market. Solutions include using internally generated cash, more aggressive use of shares as acquisition currency, delayed payment schemes or other forms of vendor financing, or even using non-equity securities as acquisition currency, which essentially turns the selling company's shareholders into lenders of acquisition debt financing. These sources will be more difficult for financial buyers to access than for strategic buyers. For this reason, private equity-led acquisitions will need to be more creative still, with recent trends towards higher equity percentages, aggressive vendor financing, and "growth-equity" investments where the returns will be driven by growth of the acquired business rather than cheap leverage.

In every case, it will remain critical that in addition to simply tapping creative financing schemes, the acquirer provides compelling arguments for value creation. Another important skill will be persistence. There will be even fewer "quick and easy" acquisition opportunities than in the past.

This additional pressure will further reinforce the focus on the right questions, such as how could this opportunity enhance our competitive advantage or its sustainability? It will also drive development of internal skills for better identifying, screening, valuing, negotiating, structuring and integrating the right targets at the right price. All of this will help companies to get through what will be a difficult short term, and simultaneously position them to be among the first to capture the opportunities that will arise as economies rebound.

In summary, while the crisis will impose many hurdles to financing and closing transactions in the market for corporate control, it will drive home the critical need to identify and capture value from any and all opportunities. This should strengthen the skills, internally and externally, that are required to deliver on this value-creation imperative as well as the corporate governance terms between shareholders, management and advisers. More than ever, it will be crucial for managers not to manage the short-term cash positions of their companies to ensure their survival, but also prepare for and build long-term value-creating strategies for their companies.



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# Risk Management in Turbulent Times



**Mike Nolan**, Global Head of Internal Audit,  
Risk & Compliance Services  
for KPMG

A global market post-mortem has begun, giving rise to questions about how the credit crisis and its repercussions could have become so severe before decisive action was taken.

It's tempting to simply attribute the financial services meltdown to the heedless pursuit of exponential revenue growth in a world of easy credit. The reality is, of course, more complex, pointing to insufficient transparency, accountability and regulatory oversight.

Also coming into focus are indications of significant failures on the part of some financial services organizations to effectively manage risk. In a recent KPMG survey\* of almost 500 global banking executives, 76 percent reported that risk management remains stigmatized as a support function at their banks. Only 48 percent of the respondents said risk management was understood to be the responsibility of everyone in the organization, and 45 percent said their boards lacked risk experience. Furthermore, 64 percent of respondents said that their Chief Risk Officer needs to hold greater influence over strategy development.

Mike Nolan, Global Head of Internal Audit, Risk & Compliance Services for KPMG and partner in the US firm, says that all companies, regardless of industry or size, should reevaluate their views and attitudes toward risk management. "Senior leadership should strive to create a risk culture within the organization, which starts by setting an appropriate tone at the top, reassessing the risk management practices across the organization and cultivating the requisite risk management skills."

**"Risk management should be elevated within organizations, moving from a back-office function to become a strategic partner that has the ear of senior leadership."**

## Cultivating a Risk Culture

Although the credit crisis has claimed some high-profile companies, others weathered the storm with less damage. The reason, says Nolan, is that many companies took decisive action to try to manage and hedge their risks in advance of the crisis and were able to adapt their risk model to address market conditions as they worsened. In strong performers, Nolan says, the risk management

\* KPMG International Survey: Never again? Risk management in banking beyond the credit crisis

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function is fully integrated in the business, enabling insights and best practices to be shared. Key senior managers are both experienced and fully involved in the process of managing risk. Risk management responsibilities are also likely to be streamlined so that risk can be owned and managed within the business unit where it occurs, but quickly escalated through the risk management function to senior leadership and the board of directors when necessary.

Weak performers, by contrast, may have allowed their risk management initiatives to splinter into silos, where vital information can be delayed, distorted or buried. The risk function also tends to be held at arm's length from business operations and senior management.

"Risk management processes are most effective when they are linked to company strategy and embedded in the operations of the business," he adds. "The leadership team should establish an enterprise-wide framework within which risk can be measured, reported and managed."

Setting the appropriate "tone at the top" is the first priority. Signaling commitment at the senior level provides the foundation for effective risk management, affecting an organization's governance, risk appetite, limits, compliance and control. It is clear from the experience of the last year that these areas are where problems of risk management most often start. When asked to rank the leading contributors to the credit crisis, the banking executives polled in the KPMG survey\* cited risk governance and risk culture among the top factors.

"Risk management should be elevated within organizations, moving from a back-office function to become a strategic partner that has the ear of senior leadership," says Nolan.

## Declaring Independence

While it may seem obvious in retrospect, a common risk management failure was the reporting structure. In one organization, the Chief Risk Officer's reporting relationship to a senior officer made it impossible for him to effectively challenge his boss regarding inappropriate risks. In another instance, a global chief executive who traded on behalf of his bank, exempted his trading portfolio from the limits and controls structure that applied to other portfolios.

Companies should ensure that the risk management function is independent—free from organizational pressure or influence, says Nolan. In some companies, this may require a change in reporting structure.

"Risk officers should have direct access to the board without influence from the CEO," Nolan says. "And, they need to know their jobs won't be jeopardized if they raise a red flag about potential risks."

Fortunately, there are signs that improving risk management will move to the top of the corporate agenda.

According to the KPMG survey\*, 85 percent of respondents said that they have already reviewed, or are in the process of reviewing, their risk management procedures, with another 7 percent of respondents saying that they are planning a review. Further, 62 percent of those surveyed reported that acquiring or developing risk management skills will be a top priority, which should help senior management and other employees to make educated risk judgments.

"Ultimately, it's not about eliminating risk, but managing and optimizing it," Nolan says. "CEOs and CFOs should become stewards of risk; they must be able to understand, articulate and manage risk and its impact on the organization. When the organization is under severe stress, the risk culture can help ensure that 'doing the right thing' doesn't give way to 'doing whatever it takes.'"

For more information on succeeding in turbulent times, visit: [kpmg.com/succeeding](http://kpmg.com/succeeding)



# The time is ripe for fresh ideas

Recessions are a chance for companies to abandon outdated management practices and experiment with innovations such as virtual working and group leadership. By **Lynda Gratton**

**F**orget business workshops and cases studies – recessions provide real-time opportunities for executive learning as old myths are brought into question and management innovations emerge.

Historically a downturn has been a time when business models, organisational structures, labour markets and employee contracts come under immense strain. Accepted wisdoms are challenged and this break in thinking can result in the adoption of new practices and the adoption of new habits and skills. These pressures and fissures – while difficult at the time – can yield fresh ideas, engaging experiments and interesting adaptations in the long run.

This is important because while many managers are adept at innovating products and services, few have been adept at innovating the practice of management itself. As a consequence, businesses are often cluttered with increasingly outdated ways of managing: performance management processes that were invented in the 1950s; notions of leadership that go back to the command control of the second world war; and meeting protocols that have not changed for decades. At the same time, potential innovations such as virtual team technology are left unheeded.

## Lessons of past recessions

To understand this better, let us look at two recessions the business world has experienced in the past 30 years. The 1981-82 recession heralded the end of the notion of a “job for life” and marked the rise of what would eventually be called the “free agent”. With the greater autonomy of workers came experiments in flexible working and project-based work. These nascent attitudes received further impetus as technology was able to support flexibility and enabled the move of some work from the office to the home.

The 1990-92 recession accelerated these changes while adding another important dimension: globalisation. The slashing of costs that came with this recession encouraged manufacturers and, later, service providers to move work out of the developed

economies to the labour markets of the emerging economies such as India and eastern Europe. What began simply as the exodus of low-cost work to emerging markets accelerated during the following 10 years and evolved into the highly sophisticated globalisation of the talent markets in sectors such as information technology and research, resulting in the rise of what has been called the “creative class”.

## The current downturn

If recessions are times that enable accelerated change in management practices, then to make the most of this acceleration managers must identify where the fissures and tensions are likely to emerge. There are two points of tension emerging in this recession that may allow for innovation in management practices.

### ■ Wider distribution of leadership

This recession has brought into stark perspective the role of the leader. Up to this point, the dominant norm has been the “command and control” leadership style. In this model, the organisation is viewed as a hierarchy in which decisions are escalated to the top, where a CEO makes the decisions.

But many people are now questioning the wisdom of placing so much power in the hands of so few. At the same time, insights from research in decision sciences and technological advances have shown that often the best decisions are made by an “intelligent crowd”, rather than one all-powerful individual.

This is a fissure in the norms of organisational life that could well lead to the acceleration of a more democratic and distributed decision-making process and the idea that leadership can be held by a wider group of people. The wise executive takes this as an opportunity to think more profoundly about the selection and development of leaders and the means of strategic decision making.

Senior leadership cadres have traditionally been essentially homogenous – middle-aged men with similar backgrounds. While research on innovative teams has shown that such groups are likely to be less competent in decision making than diverse



Nick Lowndes/Eastwing

teams – little change has taken place. With the dominant model under question, this is a good time to bring diversity back on to the agenda. Businesses should be looking more closely at the experiences of the Norwegian government, which passed legislation requiring that women must comprise 40 percent of boards of listed companies.

Every six months, a number of important questions about the future of the company, its markets and its technologies are posed by the senior team to the whole company with the assumption that anyone can volunteer their insight and ideas on these questions. The views of these grass-root strategists are then brought together in a series of virtual and real-time meetings in which the ideas are discussed and debated. The outcomes of this collective thinking play a crucial role in the creation of the company's strategic planning and a platform on which resource allocation decisions can be made.

### ■ Creating flexible virtual teams

Past recessions have often served

**With companies freezing travel budgets, many executives will have to do more work virtually**

to accelerate the adoption of management practices and processes that already had some popularity pre-recession. The same is true of the technology and mindset that supports virtual working. Assembling teams to work on projects and task forces has become more viable in the past decade, often hastened by the pressures of globalisation. Yet while virtual working is emerging as a trend, there is still an assumption that face-to-face working trumps virtual working. At the same time, research I have conducted with my colleagues on teams across the world has shown that many fail to utilise the technologies available to them.

As a result, every Sunday night thousands of executives board aircraft and trains to get to Monday morning meetings. With many companies freezing travel budgets, this is likely to change and many executives will have to do more work virtually.

At the same time, the entry and exit roads of the world's big cities are clogged from early dawn with commuters hurrying to and from work. This movement of people has been based on two assumptions: that people need to meet every day to get their work done; and that when at home, they are likely to slack and they, therefore, need the discipline of an office to ensure they perform.

Both assumptions are wrong. First, people do not need to meet every day to get their work done. Our research has shown that virtual teams – where members rarely meet – can be highly productive. What is important in these teams is that they are all inspired by a meaningful task, fascinating question or compelling vision. So, while it is indeed important for people to establish a working relationship, we have discovered that more productive and innovative teams focus on completing a shared task rather than meeting each other face to face.

For example, the vast majority of the many thousands of volunteers across the world who every night build and repair the Linux open-source software platform have never met each other in real life. Theirs is a community built exclusively in the virtual world, powered by a compelling vision and shaped by individual commitment.

The second assumption – that peo-



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# Play fair with workers to reap rich rewards

Tough decisions and cost cuts are inevitable, but if properly executed they can clarify company identity and purpose. By **Batia Mishan Wiesenfeld**

ple need the discipline of an office to ensure they perform – is also a myth that is well past its sell-by date. During the past decade, much research and practical examples have shown that when people have the opportunity to work on engaging, well-planned tasks at home they are significantly more productive and committed than those who toil through the commuter traffic every day.

I predict that we will see a sharp rise in the number of virtual teams that include home-based members. This will require us to abandon some old team habits and learn some new ones. It will also require us to build a much deeper understanding of which factors drive the performance of virtual teams and how these teams can be actively developed.

## Opportunities in a downturn

So how can executives respond to the opportunities this recession will provide for innovation in management? It is a two-stage process. First, create space by jettisoning what is not needed, and second, begin to experiment with new practices.

What can be jettisoned? One of the worst predominant management practices has been the preponderance of face-to-face meetings. In highly skilled hands, these meetings can be a dynamic activity and a crucial decision-making platform, but too often they decay into something much less productive. Now is a good time to question the number of face-to-face meetings. And, if some of these meetings are crucial, then take a leaf out of BP's book and train even the most senior executives in facilitation and dialogue skills.

Next, consider which experiments can be conducted immediately that would enable the business to develop new and innovative management practices. Here are some candidates for challenging experimentation that can work well in a recession:

- Follow the lead of the Norwegian government and rapidly increase gender diversity at senior levels by putting in place quotas for the proportion of women short-listed and appointed in roles.

- Question the existing logic that determines how decisions are made by following Nokia's lead and experimenting with strategy formation from the bottom up – rather than always going for the top down.

- Restrict travel to encourage virtual teams. Take a closer look at how they work and experiment with ways of supporting them.

- Put group-ware technologies at the top of the performance agenda. Experiment with video conferencing, webcasts and group decision-making tools.

Not all of these experiments will flourish and some will die out over time. I would expect, for example, that while we will see more virtual teams and greater use of the technologies that support them, once cost cutting is relaxed, some people will return to airports. Others, however, will have fundamentally changed their habits and begun to build working communities that are virtual and highly productive.

Recessions are a time of destruction of the old order, a time when assumptions are questioned and nascent practices and ideas are given space to flourish. That is little cheer for now but, in the longer term, an enormous stimulus for change. ■

**T**he economic downturn has brought millions of lay-offs, leaving most companies populated by employees who could be best characterised as “survivors”. As the recession continues, some companies will use this period to establish a platform on which to shape growth and success when the economy turns round. For others, declining performance will lead to wave after wave of redundancies in a seemingly inexorable downward spiral.

What differentiates the companies that will weather this downturn from

of research studying thousands of lay-off survivors across organisations and industries, my colleagues and I have found that when lay-off procedures are fair, remaining employees are more committed, more motivated, more creative, report a more positive and co-operative work group climate, and are more confident and less likely to leave the company.

For example, in one large non-profit organisation, managers role-played breaking the bad news to lay-off victims in order to prepare themselves to be sensitive, rather than formal and abrupt. An employee survey showed

that morale did not decline after the lay-offs because of how the redundancies were handled. In a large bank that was previously riven by political factions and infighting, using consistent and transparent procedures to allocate jobs and cut staff after a merger actually enhanced *esprit de corps* and helped to facilitate co-ordination across units.

What do fair procedures require? One common misconception is that, in order to be fair, managers should ensure organisational survival while avoiding tough decisions or cost cuts. However, being fair is not about straying from hard choices. Fairness is not defined

Alastair Taylor/Inkshed

by the *what* that must be done, but rather *how* it is done.

Fair procedures reassure employees that they will get their share of desired outcomes in the long run and can help to convey a company's positive character and identity. Unfair procedures, by contrast, tell employees that the organisation's values are undesirable and that employees are not valued. My research has found that employees who are treated unfairly are more likely to prioritise their own self-interest, focus on the short term, micro-manage subordinates and projects, and protect themselves through methods such as deflecting responsibility and avoiding risk.

For example, in a supermarket chain, employee theft increased significantly after a poorly managed cost-cutting initiative. In stark contrast, employees who are treated fairly are more likely to act in the organisation's interests, take a long-term view, empower and help other employees and invest themselves in their jobs and companies, such as through innovative ideas and actions.

## Focus on remaining staff

While the global downturn poses a host of threats, it also provides an opportunity for savvy managers. Employees are attempting to make sense of their circumstances and to establish a new set of expectations. They are, therefore, especially open to words and signals from management that define the company's identity and purpose. Although employees may exude negativity and cynicism in difficult times, most are looking for something to believe in. Managers must, therefore, refocus employee attention on goals, missions and purpose. When employees perceive that purpose as valuable, they are more likely to accept the organisation's identity and work hard to align their goals with those of the company. When their assessment is negative, they are more likely to withdraw.

For example, in a large European public hospital, staff interpreted cost-cutting as evidence that management was willing to sacrifice patient care. This occurred because managers failed to draw a link between the cuts and the aim to remain a local hospital that could best serve the immediate community. This failure to connect managerial decisions with organisational identity led to increases in employee turnover and absenteeism.

## How to make fairness clear

Clarifying what the organisation stands for requires well thought out ideas and consistent communication, but relatively few resources. It is essential that managers articulate why decisions are made and why the organisation has set particular goals.

This helps employees to see the link between their own roles and the larger whole. An added benefit is that such discussions prompt reflection, which can expose erroneous assumptions and allow them to be corrected.

Employee attention should be directed outward to combat the tendency for resource scarcity to provoke unproductive internal competition. For example, employees and departments can evaluate themselves in relation to the value they deliver to customers, rather than the return they deliver to shareholders. Serving the customer is personally rewarding and builds employees' sense of competence. Customer feedback directs employee effort without managerial intervention. To take advantage of this, managers must help staff to understand who their customers are, and the factors that shape their satisfaction.

Building organisational identity and implementing change in a fair manner requires managerial commitment, but it can be accomplished without additional expenditure. For managers forced to downsize during the downturn, this could prove to be beneficial for business growth and sustainability in the long term.



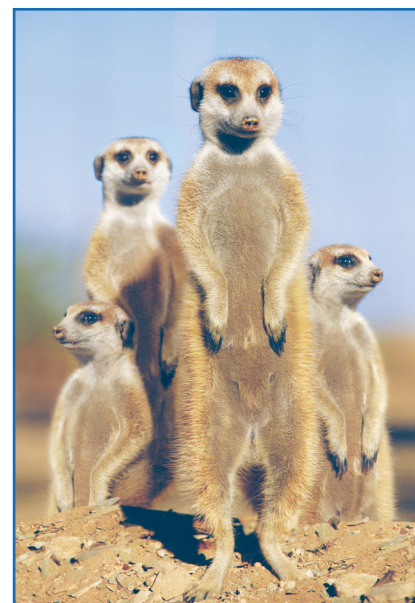
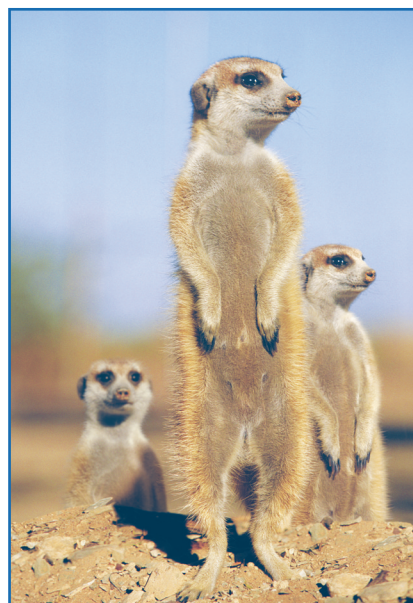
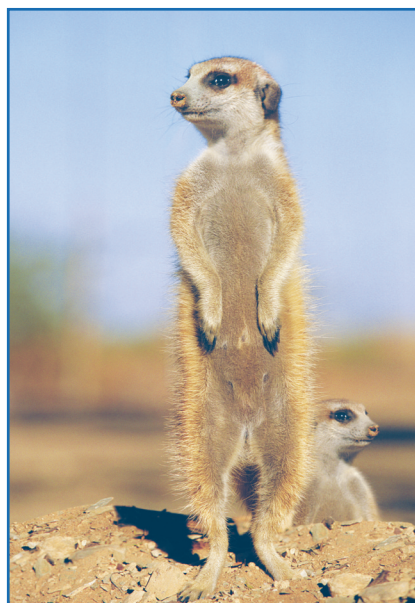
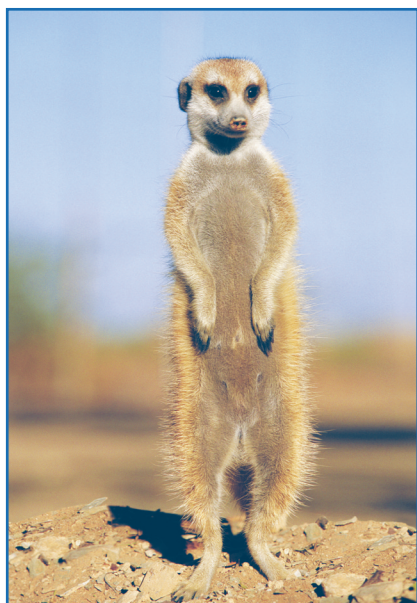
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the ones that will fail? The ones that succeed will be those that recognise that their lifeblood is the motivation and commitment of their remaining employees. While the traditional rewards that managers use to motivate employees, such as promotions, pay increases and bonuses are in scarce supply in difficult times, there are other steps managers can take, for free or at little cost, to strengthen morale.

The single most important thing managers can do is to plan and implement decisions in a manner that is fair – especially those related to downsizing. What do we mean by fair? Decisions are perceived as fair when they are implemented consistently and without bias, are based on thoughtful analysis rather than politics or whim, and when they are explained. Employees sense fairness when they are given advance notice of changes and an opportunity to provide input, wherever appropriate, and are treated with dignity and respect.

Fair procedures reduce the likelihood that employees who are made redundant will file a wrongful termination lawsuit. Furthermore, in years

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