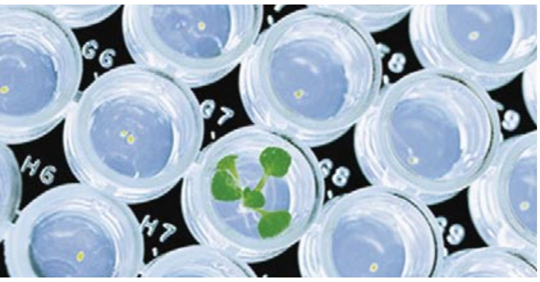
Labnotes

The newsletter of the **Management Innovation Lab**

Issue 01 | October 2006

# The challenge of management innovation



## In this issue



London Business School    Woodside Institute    aim research Advanced Institute of Management Research

Management Innovation Lab

Inventing tomorrow's best practices today

The Management Innovation Lab is a unique initiative with an equally unique and powerful perspective.

The Lab, a joint venture between London Business School and the Woodside Institute, is built around a collaborative research environment in which forward-thinking companies and distinguished scholars work together to invent the management processes and practices that will define competitive success in the 21st century.

## Why is this important?

Look back over a hundred years of industrial history, as we have done, and you will find that management innovation has frequently allowed organisations to reach new performance thresholds. In fact, management innovation, whether it is scenario planning, scientific management, lean production, just-in-time, or intellectual capital, shapes today's organisations and creates competitive advantage. Management innovation changes how managers do what they do.

The entire area of management innovation has, astonishingly, been neglected. In the rush to master the latest innovation, organisations have overlooked the potential in becoming part of the innovation process itself. The challenge is to instil management innovation into organisations. The goal of the Management Innovation Lab is to help companies become consistent management innovators so that they can identify and enact the kind of bold management innovation that drives long-term success.

Lab Notes is the Management Innovation Lab's regular newsletter. It will keep you up-to-date with the development of the Lab and give you a taste of some of the issues we are exploring and the examples of tomorrow's best management practices we are constantly uncovering throughout the world. If you want to know more about any of the stories in this issue much more can be seen at the Lab's website:

**www.managementinnovationlab.com**

If you have specific queries, would like to tell us about a management innovation or to learn more about becoming involved please contact myself or one of my colleagues, our contact details are at the end of the newsletter. Innovation is always a dialogue.

**Julian Birkinshaw**

Professor of Strategic and International Management at the London Business School and Co-founder of the Management Innovation Lab

## Jam Tomorrow

The Lab's first annual conference, Mastering the Art of Management Innovation: Making your Company Fit for the 21st Century, will be held on 16 and 17 October 2006 at the Sheraton Hotel, Park Lane, London. Led by Gary Hamel, and with presentations by Julian Birkinshaw and Nancy Snyder (Corporate VP, Whirlpool), this event will get you thinking in very practical terms about how to master the art of management innovation in your company.

For further details please visit: www.london.edu/execed/miw or contact Tim Pearson: tpearson@london.edu

### Recent publications from the Lab

The What, Why and How of Management Innovation. *Harvard Business Review*, February 2006.
Gary Hamel

How Management Innovation Happens. *Sloan Management Review*, Summer 2006.
Julian Birkinshaw and Michael Mol

For current copies of Lab publications please visit our website at:

**www.managementinnovationlab.com**

Harvard Business Review
MITSloan Management Review

### Thank you!

We would like to thank the Advanced Institute of Management Research (AIM) for their generous support in seed funding the Lab.

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# Innovation@Work: Consulting the Eden McCallum way

Julian Birkinshaw
London Business School

The London-based consulting firm Eden McCallum provides an innovative take on the nature of the firm as well as potential future scenarios for the organisation of consulting firms.

Launched in 2000 by Liann Eden and Dena McCallum, Eden McCallum is a network-based consulting firm. Rather than having a large headquarters and all the overheads associated with a conventional consulting firm, Eden McCallum retains a minimal central staff and utilises a network of freelance consultants.

Turnover is now over £10 million and the firm has delivered more than 300 projects. It has grown by more than 80 per cent per year and has 24 full-time staff and around 200 freelance consultants, making it the second biggest strategy consulting company in London after McKinsey.

As with many other businesses, Eden McCallum's evolution was based on the convergence of a number of factors. The first change was the maturing of the management consulting market, with clients seeking more control and value in their consulting spend. The dominance of the big players in the business was – and is – largely unquestioned. It has spawned an entire generation of companies and senior executives who are comfortable with the notion and value of management consulting. In the past, companies hired top consulting firms to tap into their bright, business school educated, minds. With MBA graduates and former strategy consultants now commonplace among the senior echelons of multinational firms, there is a resistance to formulaic consulting products and neatly packaged solutions. Instead, companies want consulting advice which is genuinely tailored to their situations.

The second trend Eden McCallum happily tapped was among consultants themselves. When the new economy fizzled from rocket to damp squib, many one-time consultants had reassessed what they wanted out of their careers and were loathe to re-enter the corporate world on the same terms as before. At the time when Eden McCallum began life, many experienced consultants were contemplating their next career moves.

At an operational level, too, Eden McCallum recognised an opportunity. Large consulting firms typically focused on high level board issues at FTSE 50 companies. For their part, client companies often wanted continued consulting support on specific strategic issues or implementation but were put off by continuing high costs. Eden McCallum offered a market-breaking alternative: consultants with the same high level skills and rigorous approach at approximately half the cost. After the dot-com crash, this combination of quality at lower cost was particularly alluring as many firms had scaled down their consulting budgets.

## Innovative solutions

Eden McCallum's proposition was simple: a consulting firm without any consultants on the payroll and without any proprietary methodologies. Instead, they would employ consultants on a contract-basis and would use whatever methodologies appropriate to solving their clients' problems.

To make this model work, Eden McCallum had to rethink many of the standard precepts of management thinking:

- **Tailoring the offering**
  Eden McCallum focuses on tailoring the consultants' experience, skills and personalities to the clients' needs.

The combination of quality at lower cost was particularly alluring as many firms had scaled down their consulting budgets.

The firm makes it clear that it is not in the business of creating its own distinctive intellectual capital and that it is agnostic when it comes to particular methodologies, despite the fact that novel ideas and tools are the lifeblood of most big consulting companies.

- **Outsourcing the delivery channel**
  Eden McCallum's core delivery mechanism is effectively outsourced to freelance consultants. Eden McCallum works hard to ensure the quality of these people. Only one in ten applicants makes it into the company's talent pool. The second safety element is that consulting is built on relationships rather than transactions. Relationships are between clients and Eden McCallum, and the firm endeavours to retain control and oversight over the relationship with the client.

- **Involving the competition**
  From the start, Eden and McCallum were clear that their livelihoods, and the future of their business, depended on what was ostensibly the competition: big name consulting firms. "We exist because they exist," says Liann Eden. "Companies like McKinsey, Bain and BCG create the market on both the client and consultant side."

  Before the firm was launched, Eden McCallum began a dialogue with the big players in the market. This symbiotic approach has worked. Eden McCallum has referred business to big-name consulting firms, and they have returned the compliment.

- **The process behind the network is as important as the network**
  The idea of a networked organisation is not new. Brokers and agents are commonplace. What marks out Eden McCallum is that the process behind the network is where a great deal of the value lies. Indeed, in a business without its own consultants and without its own intellectual property, this is the heart of Eden McCallum's value-added. Consequently, about half of its full-time staff are fully employed ensuring that its consultants are the right people in the right jobs. The other half of the full-time staff are totally dedicated to developing and nurturing client relationships.

- **Redefining the employment relationship**
  Eden McCallum's network of consultants are not employees in a traditional sense, nor are they entirely freelance contractors. They lie somewhere in-between: they have considerable loyalty to Eden McCallum, and they get most of their work from the company, but they define their own terms of engagement. This includes choosing which sectors they will accept projects in, how many days per week and how many months per year they work, the logistics around travel, and many other elements as well. By letting their consultants choose their own terms of employment Eden McCallum has a much more dedicated and committed workforce than would have been possible with a traditional hierarchical organisation structure.

- **Transparency**
  Eden McCallum works very hard on creating transparency in its management model. This ensures that there is a good relationship between network members, and avoids the sense that some people may be getting favourable treatment ahead of others.

Eden McCallum is very open about its fee structure. For around 100 of its consultants, the firm is their main source of income. Another 100 work on about one project a year. Initially, fees were put forward by the consultants. Then the company tried to allow clients to determine fees. Now, how much consultants are paid depends on a banding system where consultants are paid according to their seniority and consulting skills.

**In an era of outsourcing and virtual working, what are the minimum few things that the firm has to do to justify its existence?**

The answer is three things. First, the Eden McCallum brand represents a particular value proposition to its clients and its consultants, and for the founders a key part of their job is to continue to nurture and sustain that value proposition. Second, Eden McCallum is a nexus of relationships: it gains value from the social capital that builds up over time in that set of relationships. And third, it is a mechanism for structuring the work and managing projects. These are, in essence, the core competencies of Eden McCallum, and are the things the company has to sustain as it grows and evolves.

# Gary Hamel on: Management Innovation

Management Innovation Lab co-founder, Gary Hamel, is one of the world's most influential business thinkers. He talked to Georgina Peters about the work of the Lab and what management innovation means to him.

**Innovation means many things to a variety of different people so perhaps we can begin by defining terms. What do you mean by "management innovation"?**

Management innovation is innovation in management principles and processes that ultimately changes the practice of what managers do, and how they do it.

It is different from operational innovation, which is about how the work of transforming inputs into outputs gets done. It is very easy to distinguish management innovation from technology and product innovation, but not as easy to distinguish it from operational innovation.

**Can you clarify what the difference is?**

If you think of a company as a set of business processes that turn inputs into outputs, that turn labour and capital for example, into services and products, then business processes govern the workflow. This would include logistic systems, order processing, call centres, customer support, and manufacturing. Generally speaking, I'm not interested in innovation solely within this sphere.

Surrounding the work of transforming inputs to outputs, however, is everything the managers do: pulling resources together, setting priorities, building teams, nurturing relationships, and forming partnerships.

Toyota's lean manufacturing is a good example. At one level, you can say that lean manufacturing is predominately an operational innovation. But what sits a level or two above the operational changes is the radical management idea that there could be a positive return on investment from using the problem-solving skills of your employees.

Go back a few decades, and you find that if there was an efficiency or quality problem in the business, companies would send in staff experts. They would study the system, and then they would rewrite the standard operating procedures. And the employees would be asked to conform to those procedures.

The idea that a company would actually give its employees the responsibility for making those changes, that it would take people with ten or 12 years of education and then teach them statistical process control, that was just unthinkable.

So, what looks like a purely operational innovation through one lens, actually turns out to stem from a radical new management principle.

**In your research, looking back through management history, what important management innovations have you identified?**

One of the earliest was capital budgeting. I believe this started, largely in Du Pont the chemical company. As Du Pont grew, and expanded into more businesses, the question it faced was how to make rational judgements across projects for very different businesses, with very different economics, and technology, and so on.

The capital budgeting process became a way to take very disparate kind of projects, and create some common arithmetic around. While there are all kinds of limits to that because, obviously, as you summarise complex businesses in simple arithmetic, you lose a lot of the richness, I still see it as an extraordinary first.

**And you say brand management is another?**

Yes that's right. By 1929, Procter and Gamble was already codifying its brand management knowledge. It recognised that, as you moved into a mass consumer society, the mere ability to produce a product and distribute it, would become less and less important to the consumer.

‘...what looks like a purely operational innovation through one lens, actually turns out to stem from a radical new management principle.’

Before this simply making something that was 99.9 per cent pure, was a manufacturing marvel in itself. What Procter and Gamble could see was that, increasingly, competition would encompass more than the physical attributes of the product, and the ability to deliver it, but it would include intangible aspects as well.

What used to be brand management has today mushroomed into corporate image consultants, managing IP, and a host of other things. But the whole thread of how to create value out of non-physical, intangible things starts with Procter and Gamble. They were the pioneers. Although I suspect Unilever might have something to say about that.

So that is a huge innovation, because until then we lived in a physical world, we had no sense of how to create value out of things that are not physical.

**Do you think we are stifled by our preconceived management beliefs?**

I think a lot of what we believe is true, but it is not inevitable. One problem with all these books that summarise best practice is that you have to be very careful not to turn description into prescription. Otherwise soon that becomes: if it hasn’t been done, it can’t be done.

We would be stuck if most people believed that. So, I think we have to understand the historical roots of modern management practice. Understand what assumptions are baked into our management processes: change starts at the top; people work primarily for extrinsic rewards; hierarchy is the most effective means for co-ordinating the work of disparate group; the goal of strategy is to control strategic assets. And then we need to challenge and discuss them.

# The Management Innovation Lab Team

The founders of the Management Innovation Lab are Julian Birkinshaw and Gary Hamel.

**Julian** is Professor of Strategic and International Management at the London Business School and a Senior Fellow of the Advanced Institute of Management Research. His books include Sumantra Ghoshal on Management: a Force for Good (edited with Gita Piramal, 2005); Inventuring (2003); Leadership the Sven Goran Eriksson Way (2002); and Entrepreneurship and the Global Firm (2000).

**Gary** is Visiting Professor of Strategic and International Management at the London Business School, founder of Strategos and director of the Woodside Institute. He is the co-author of Competing for the Future (with CK Prahalad) and author of Leading the Revolution.

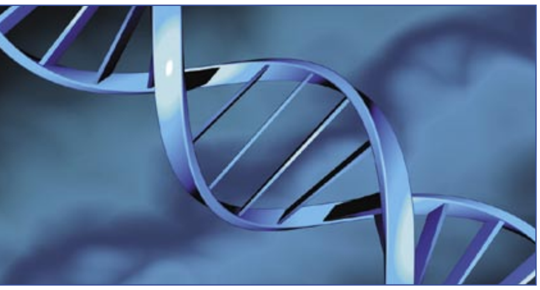
The Faculty working with the lab are **Professors Lynda Gratton**, **Michael Jacobides**, **Andrew Likierman**, **Phanish Puranam** and **Chris Voss**.

The Lab’s research fellows are **Liisa Valikangas** (above left), **Jules Goddard, Michael Mol** (above right) and **Roy Jacques**.

The lab’s associate directors are business commentators and authors **Stuart Crainer** and **Des Dearlove**, and **Mark Probert**.

# Rethinking the Assumptions of Management

**Dr Jules Goddard**
London Business School



What is the source of our Managerial DNA? What are the origins of our current models of management and organisation? These are tricky questions to answer, but most observers would agree that the principles of modern management emerged 100 to 150 years ago, at approximately the time that large industrial organisations first took off in the US, the UK and continental Europe.

Management was invented to perform a wide variety of tasks that were demanded of the large industrial organisation: Creating a sense of purpose for the enterprise as a whole, coordinating and controlling dispersed activities, accumulating and allocating financial capital, setting objectives, and so on. To conduct these tasks effectively, certain organisational principles – **the five pillars** – emerged in the early part of the twentieth century and have remained remarkably resilient since then.

| Pillar 1: | Pillar 2: | Pillar 3: | Pillar 4: | Pillar 5: |
|---|---|---|---|---|
| Hierarchy of Control, based on the assumption that someone has to take responsibility for exercising power and setting direction, and the necessary judgment to perform these difficult and onerous tasks are possessed by only a few people. | Division of Labour, based on the assumption that specialisation of tasks is the heart of good organisational design, and that specialists with complementary skills will always be more productive than generalists with overlapping areas of ignorance. | Standardisation of Process, based on the assumption that management processes coordinate the activities of many people, and that good processes become more efficient over time. | Planning of Outcomes, based on the assumptions that the future is predictable enough for planning to be a reliable, and respectable activity, and that targets bring out the best in people. | Motivation by Money, based on the assumptions that people respond to incentives, and that money is a great motivator. |

### Do these principles and assumptions still apply today?

Well, to some degree they do: picture a modern production line, a call-centre, or a mining operation, and you will see most of these five principles strongly in evidence. But of course there are large parts of our "knowledge economy" that work in spite of these traditional assumptions. There is a widespread acceptance that we need to do things differently, but these principles are analogous to biological DNA – they are so deeply ingrained in the behaviours and belief-systems of business people that we really struggle to change them.

But by unpacking these assumptions, we have a possibility to start thinking and acting differently. The evolution of management is, in my opinion, likely to take a path that challenges and subverts many of the practices and assumptions that I have listed above as intrinsic ingredients of the traditional – and dangerously obsolete – model of management. Every company needs to reflect on how their managerial practices and organisational structures can be reformed to make more skilful use of the human talent at their disposal.

### How might this be possible?

Without management – in its conventional sense – what alternative system would need to be in place for today's problems to be addressed more effectively? To give a

The evolution of management is likely to take a path that challenges and subverts many of the practices and assumptions of the traditional model of management.

flavour of what such a system could look like, the example of W.L. Gore is instructive. Gore is a $4bn manufacturer of specialised, high-tech fabrics (including Gore-Tex). It is Europe's most preferred employer, according to a recent survey by *Business Week*. These are some of the most telling characteristics of the Gore culture:

- The whole company, not simply the R&D department, is treated as an incubator for experimental ideas and initiatives
- Managers are "sponsors", not "bosses"
- No one is "assigned" to a team or to a project: each person takes responsibility for finding his or her own work assignment
- People negotiate their own commitments
- You can say no to any request
- Leaders are not "appointed": power is granted "from below"
- You are a leader in Gore "if people show up at your meetings"
- Everyone sets their own salary – and these are posted for everyone to see
- Peer pressure to deliver value are huge – and thus have the effect of bringing salaries into line with value.

W.L. Gore is an extraordinary example of a high-trust and high-performance organisation – but it can never serve as a model for any other company. Every company must invent its own future. This is in the very nature of competitive strategy – the search for greater uniqueness in the permanent battle for advantage. But we can detect 5 strands in the Gore model that presage the generic shape of the high-trust organisation of the future:

- Substituting democratic methods of decision making for hierarchical methods;
- Substituting market processes of resource allocation for strategic planning methods, by internalising competitive markets in ideas, in talent, and in funding;
- Substituting the project for the job as the building block of organisational design, thus moving beyond the traditional "one person per job" model;
- Substituting an intrinsically motivating work environment for one based on extrinsic factors such as money, thereby tapping into deeper levels of human motivation;
- Substituting personal creativity for standardised processes of operational effectiveness, thereby relying more on the natural ingenuity of people rather than their obedience or compliance.

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# **Today's classic dish:** Spaghetti organisation

**Stuart Crainer**
Associate Director - The Lab

The story of Oticon, the Danish hearing aid technology company, starts like that of many manufacturing companies. Founded in 1904, it was the first hearing instrument company in the world. By the 1970s, it was the number one manufacturer of behind the ear hearing aids in the world. But by 1974, its market share began declining as people started using in the ear models.

In the 1980s, Oticon faced increasing competition from corporate giants like Siemens, Philips, Sony, and 3M. By 1987, it had dropped from 15 to seven per cent and the company was starting to lose money. Lars Kolind took over as CEO at Oticon in 1988.

Kolind's first move was a classic cost-cutting exercise aimed at stripping out the fat that had attached itself to the company in more prosperous times. He pared the company down, shedding staff and raising efficiency. He re-focused the business on its key markets.

Oticon returned to profit, but Kolind knew that the changes were not enough. "We had to find something that we could do in a unique fashion. That led me to believe that if we could design a uniquely innovative, fast moving, efficient organisation, then this is something they [the competition] could never replicate."

In the early 1990s, Oticon developed a radical organisation model with the interaction, collaboration, and connectivity of people, customers, suppliers, and ideas at the company's heart. Kolind called it "a spaghetti organisation of rich strands in a chaotic network". ›

## Spaghetti in action

So how does the spaghetti organisation work? Any individual who comes up with a good idea is free to assemble a team and act as project leader. Each project, however, then has to compete with all the other projects trying to get off the ground at any time. In true Darwinian fashion, an employee must attract sufficient resources and support for his or her project or it will perish.

At times, there are up to 100 projects on the go, forming and disbanding as tasks are started or completed. Individuals invariably contribute to more than one project at a time. Key to freeing up the way people think and work is Oticon's mobile office system. Employees carry their office with them wherever they go at Oticon's headquarters. Desks are not allocated; instead workers use the nearest available workstation , rolling their personal rullemaries – Rolling Marys or mobile carts – around the hardwood floor to wherever they need to be in the building.

**Lars Kolind** Former CEO of Oticon

And then there's the paperless office concept. Paper is all but outlawed from the organisation. Incoming mail is scanned into the company's computer system before being shredded. Some important documents – legal documents and reports, for example – may be kept for a few days or longer, but the majority of paper is shredded within hours of arriving.

The shredder is connected to a transparent chute which passes through the company cafeteria directly below, allowing workers on breaks to watch a satisfying stream of falling paper on its way to the recycling bins. Kolind estimates that the new way of working reduced circulating paperwork by 80 per cent.

During the recession of the early 1990s, Oticon's industry experienced some of the toughest trading conditions in its history.

Oticon Delta

Oticon proved the exception. In 1995, it published figures showing revenues of $160 million and operating profits of $20 million – an increase of 100 per cent on revenue and a ten-fold increase in profits on the figures for 1990.

But, by the end of 1995, Kolind sensed that the disorganised company was becoming dangerously organised. Kolind's solution was to "explode Oticon in a new direction". Projects were re-arranged geographically within the building. He described the result as "total chaos" – precisely what he was looking for.

As he says: "To keep a company alive, one of the jobs of top management is to keep it disorganised." When Lars Kolind stepped down from Oticon in 1998 he left it in a strong competitive position.

## Contacts @ the Management Innovation Lab


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**Information on the Lab, our people, events, publications and more can also be found online at:**
**www.managementinnovationlab.com**

## Don't miss the Lab's first annual conference!

**Mastering the Art of Management Innovation: Making your Company Fit for the 21st Century**

Monday 16 and Tuesday 17 October 2006
at the Sheraton Hotel, Park Lane, London.

For details see: **www.london.edu/execed/miw**
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