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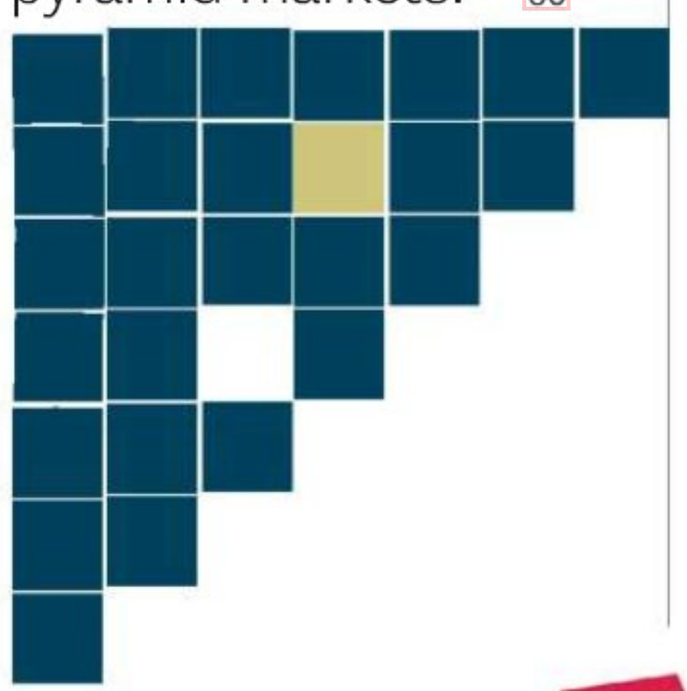

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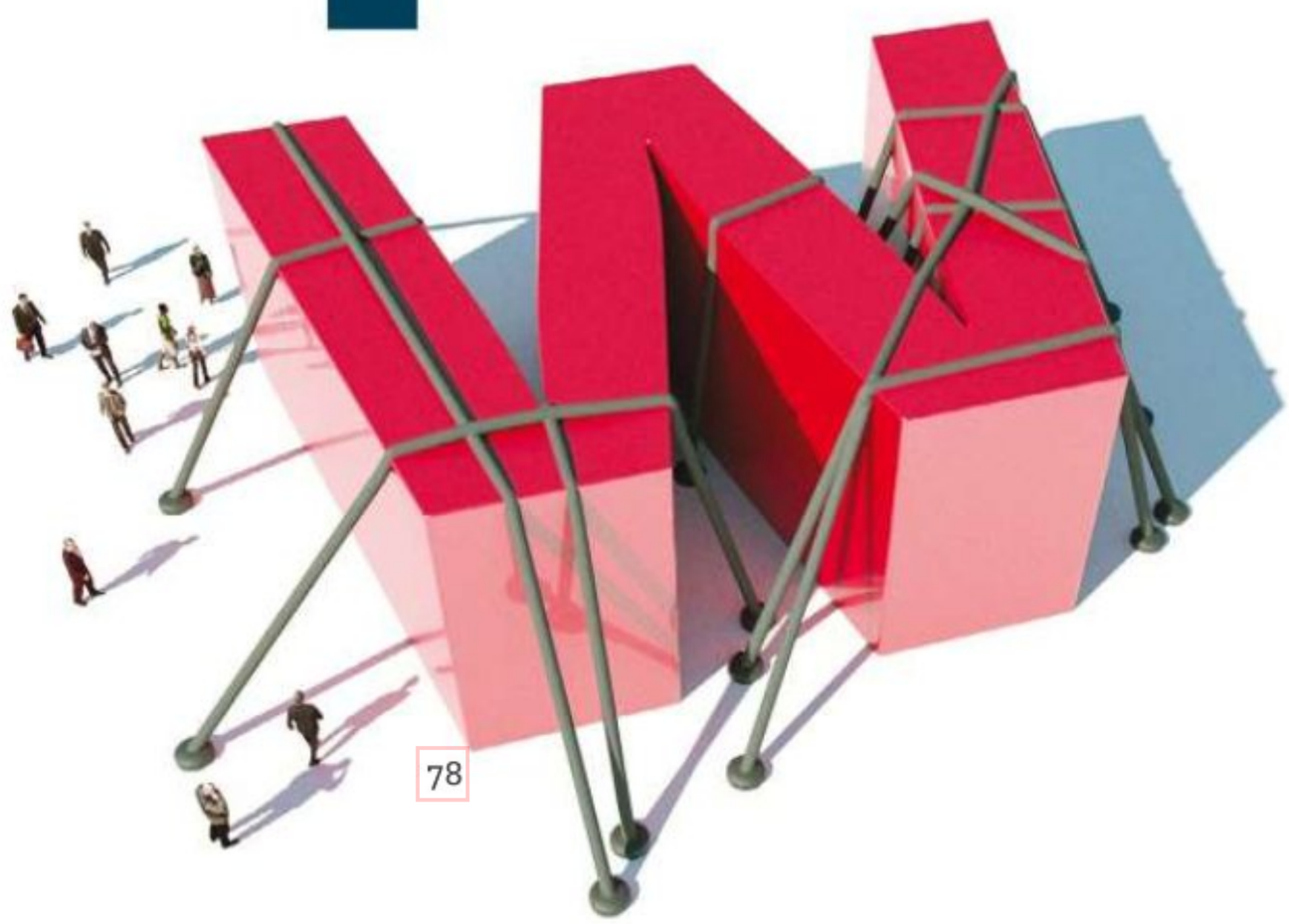

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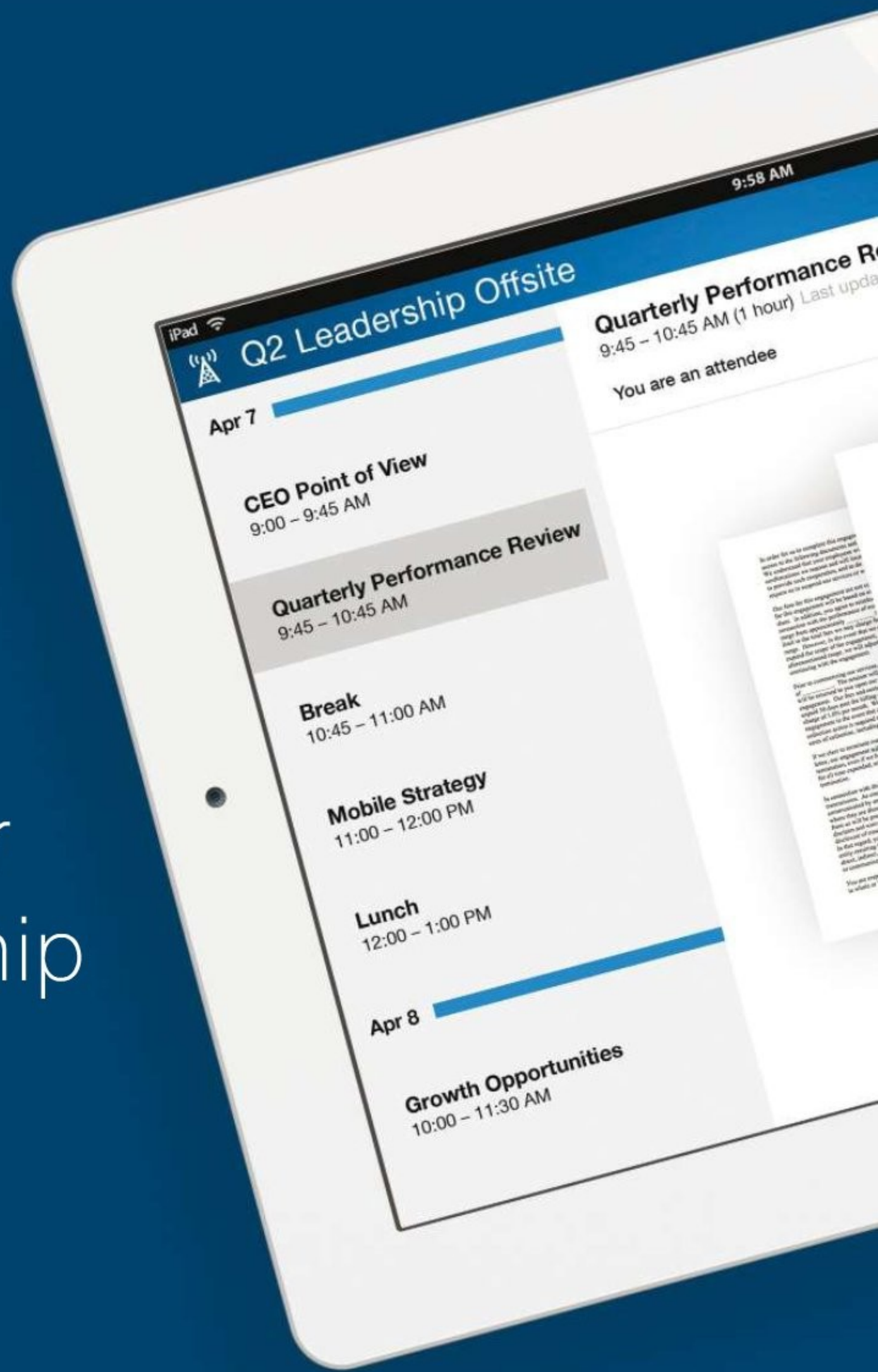

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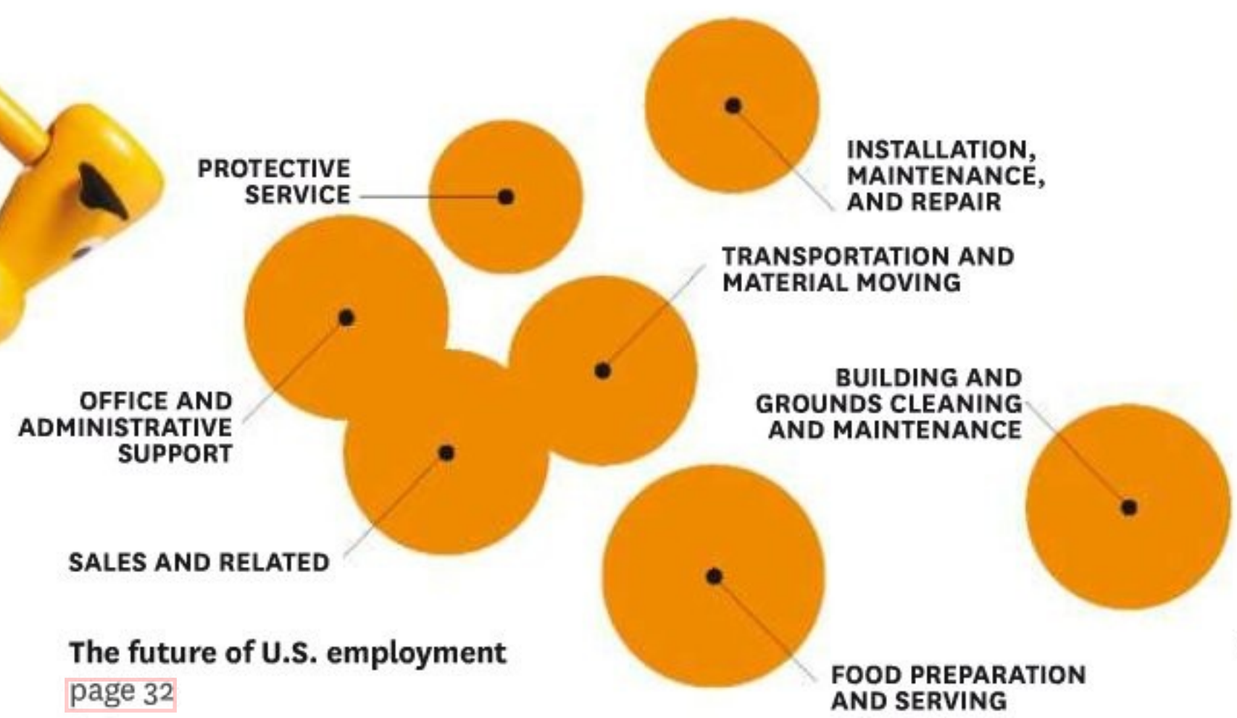

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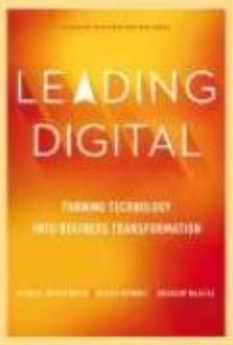

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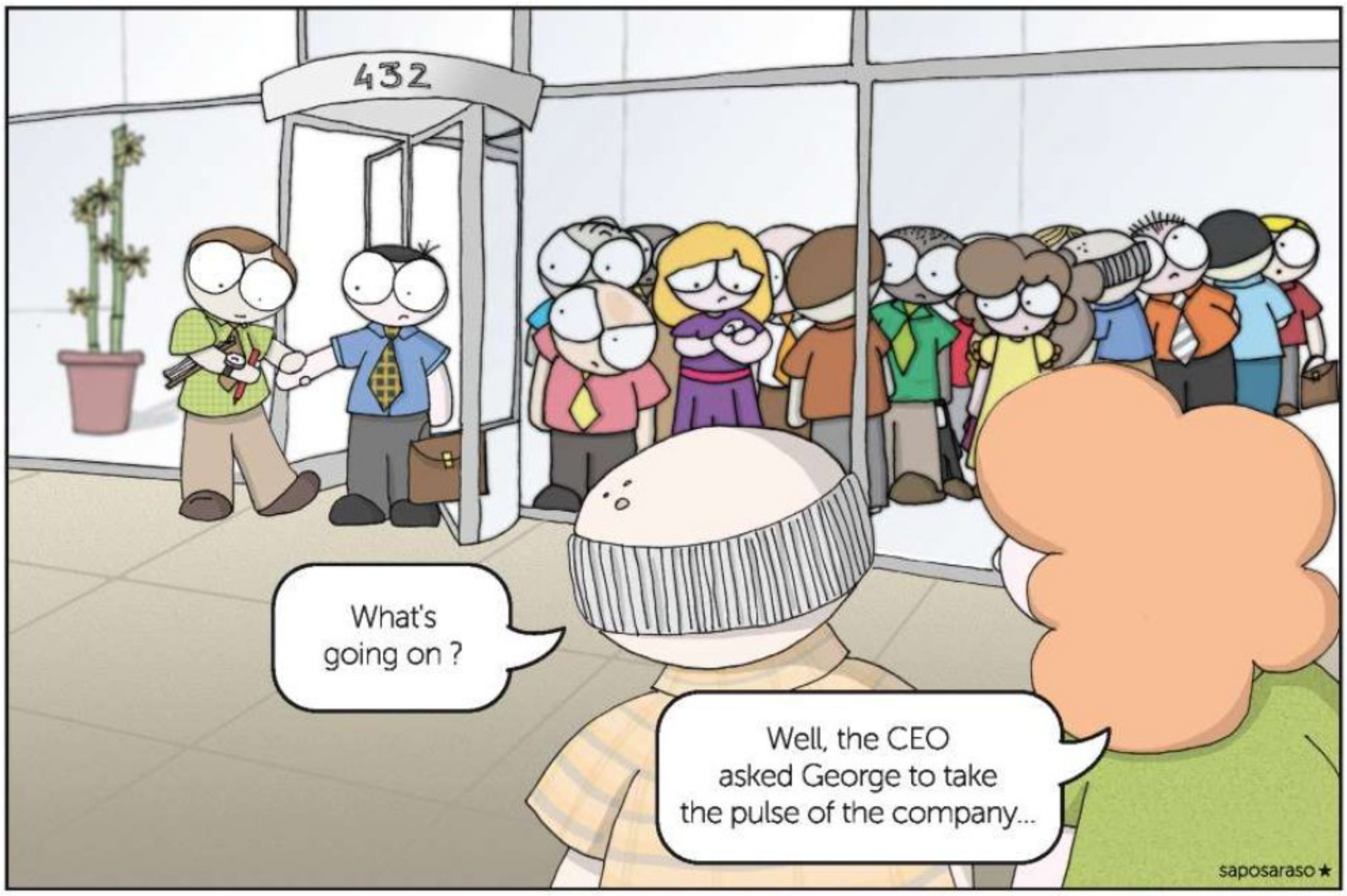

Leadership is Social

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From the Editor

Remembering Warren Bennis

Warren Bennis
(1925–2014)

How do you measure the impact of a man?

Warren Bennis, who died this summer at the age of 89, certainly ranks among the world's most influential thinkers on the topic of leadership. He explored it in more than two dozen books and in countless articles—many of them for HBR. It's not a stretch to say that he brought the study of leadership from the fringes of academia to the mainstream, always arguing that leaders need to be more democratic than autocratic. But his greatest and most enduring gift may have been his generosity of spirit. As David Wan, the CEO of Harvard Business Publishing (and a friend of Warren's), puts it: "Everyone viewed Warren as a mentor."

The list of those who would agree is indeed long and impressive, ranging from Starbucks's CEO, Howard Schultz, to the political commentator David Gergen, to the prominent psychiatrist Mark Goulston. Schultz, in his book *Pour Your Heart into It,* describes how he came to depend on Warren's advice, writing that he would call him up "late at night or early in the morning, whenever I reached a turning point and was at a loss for what to do."

Bennis spent his final 35 years teaching at the University of Southern California, and he founded the school's Leadership Institute. He kept active nearly until the end, giddily learning the art of blogging for the likes of HBR, *Bloomberg Businessweek,* and others. In 2010 he published a final book, a memoir titled *Still Surprised,* that nicely sums up his life and ideas.

I interviewed Warren when the book came out. He talked about one unfinished project: "It may come that my next book will be called...*Grace.* I think that may be just the name for a book which is going to deal with issues of generosity, respect, redemption, and sacrifice—all of which sound vaguely spiritual, but all of which I think are going to be required for leadership." As my colleague Julia Kirby wrote in a touching remembrance on our website, "*Grace* never made it to bookstore shelves. But the people who had the privilege of knowing and working with Warren got the content of that book in his presence."

Adi Ignatius, Editor in Chief

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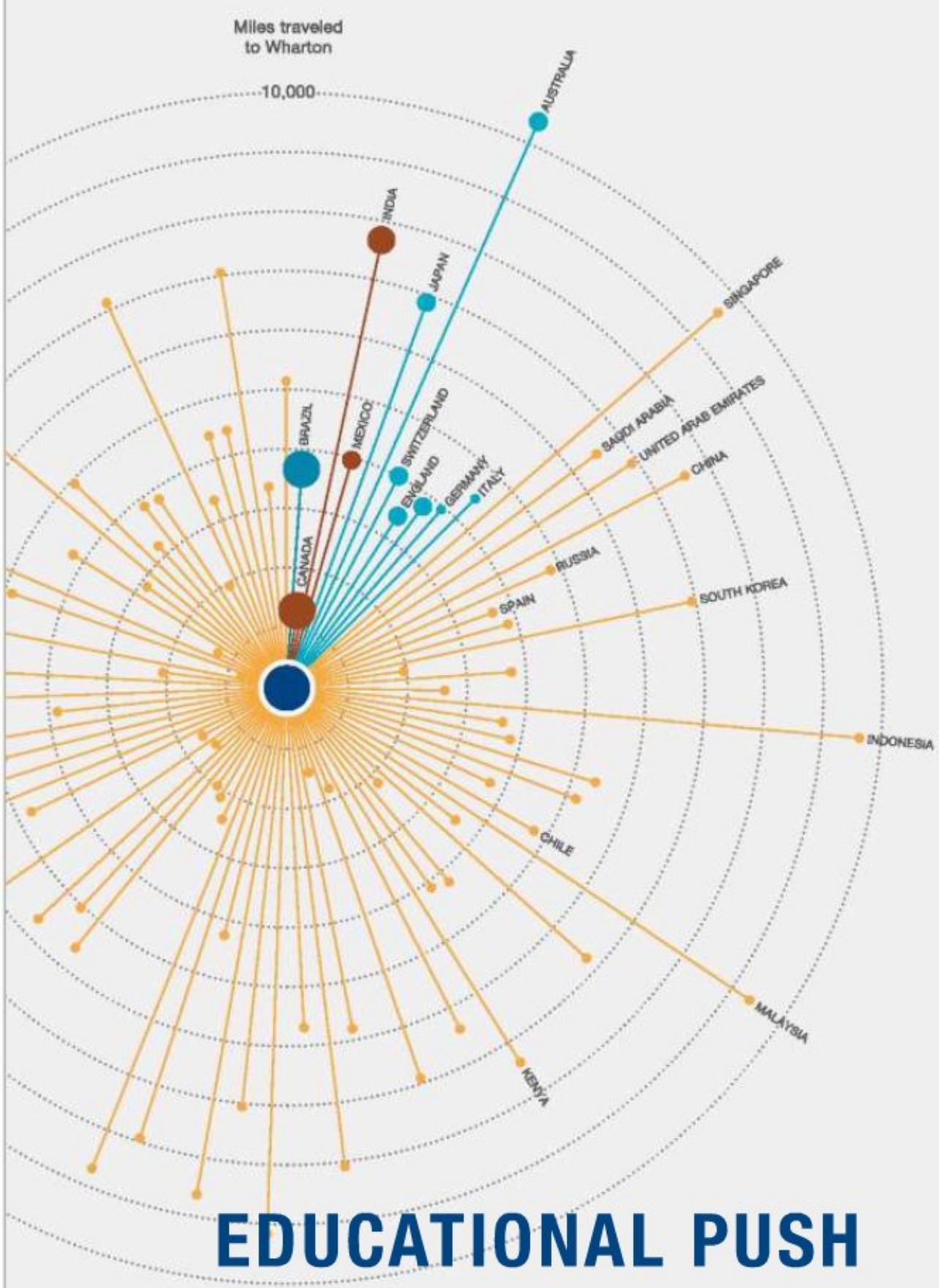

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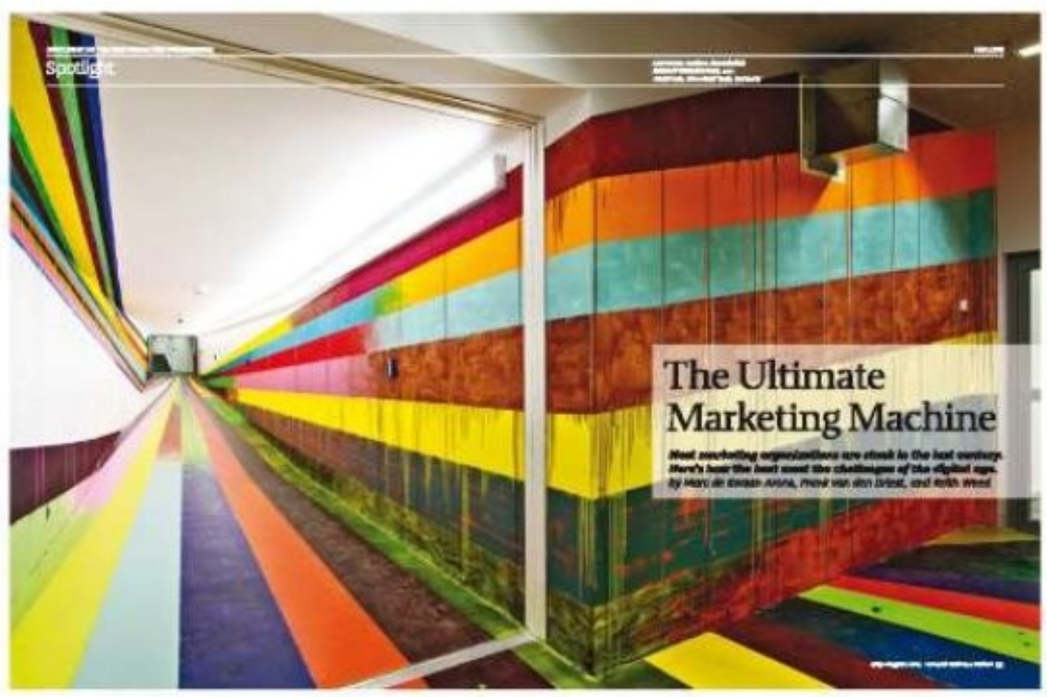
Marketing Organizations Need to Get Unstuck

HBR article by **Marc de Swaan Arons, Frank van den Driest,** and **Keith Weed,** July–August



In the digital age, new tools to engage customers surface every day, yet the structure of most marketing departments hasn't changed in 40 years. But a few organizations are ahead of the game. They've broken down silos, linked marketing strategy to business strategy, and set up nimble cross-functional teams that bring together talent with three kinds of focus: "think," "feel," and "do."

The diagram of the orchestrator model is ridiculous. For example, the idea that PR executives can provide only "feel" capabilities shortchanges the profession. And how do you know that a marketing content manager doesn't have excellent ideas in the "feel" and "do" categories? If CMOs implement this model, they will be pigeonholing people.
Adele Cehrs, CEO, Epic PR Group

The authors respond: *We believe that the way of working represented by the orchestrator model will become very important in the future. CMOs must not only make sure their organizations have bench strength in the right skills ("think," "feel," "do") but also realize that any new structure will need to flex with each project.*

Well-trained employees are empowered to contribute in ways beyond one specialty, but this model limits that contribution. It suggests that rather than having a well-rounded full-time marketing staff, it is better to have a well-rounded network of contract employees you can bring in to perform very specific tasks as needed. A better approach would be to train employees in all aspects of their vertical ("think," feel," or "do") and have them contribute in any capacity needed within it. For instance, if I'm a web analyst, I should be able to contribute to all "do" functions, not limited to one hyperspecialized job.
Tyler Cecchi, marketing associate, Digitas Health

I love the example about cable service provider Liberty Global and how its marketing team uses the think-feel-do approach to address the problem of "complex set-top box required too many on-site visits to set up." I don't see engineering mentioned in the team involved. The problem could be solved if engineers and product managers built a product made for customer

Why Marketing Needs More Introverts

HBR.org article by **Eddie Yoon,** July

As more power shifts to consumers, marketers will need to spend more time listening, reflecting, and building fewer, deeper relationships, says Yoon.

I would avoid generalizing about extroverts and introverts and ascribing skills deficiencies to either group. And, though the idea that all marketers should become better listeners is valuable, this post tells half the story. I think of marketing as a function that orchestrates interactions and communication. Because successful communication requires receiving and transmitting messages, marketers need to be both better listeners and better talkers.
John Balla, principal marketing specialist, SAS Institute

Listening is the key; it's not whether you're an introvert or an extrovert. I'm an introvert, and I can get far too caught up in my own inner dialogue to listen to the people I'm supposedly interacting with.
Cynthia Morgan, commercial credit analyst

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installation! It would be understandable if the orchestrator approach was an interim fix until engineering developed a better product, but it's not the real solution.

A flexible team approach to marketing is spot-on for today's business world, but this example seemed to miss the core problem.

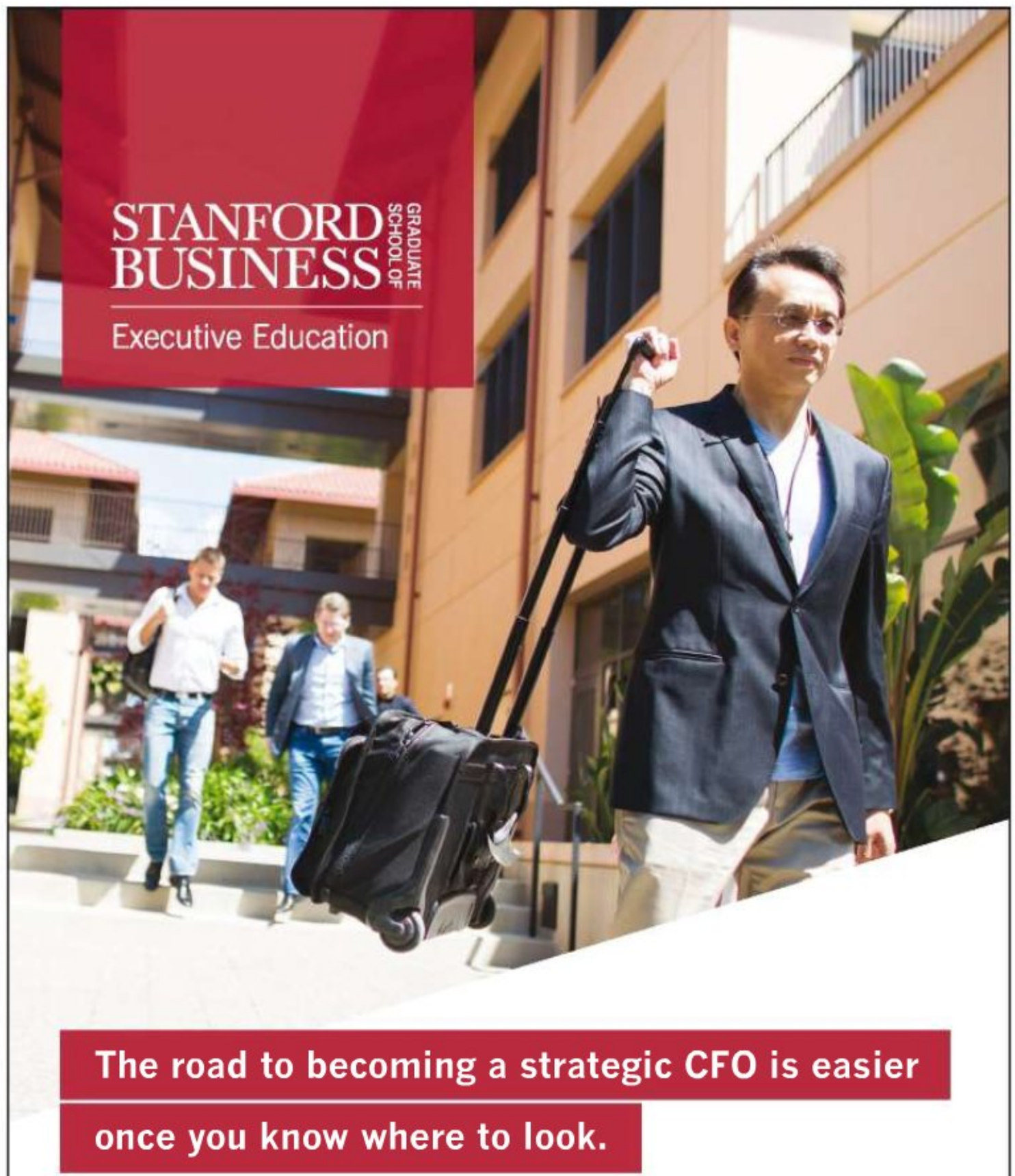
Bill Bender, partner and president, Persuasion Agent

The marketing function is not on the brink of a revolution. It should be, but I don't see it happening. The color of the chairs, how many we have on deck, and where we place them are changing—but that's about it. Better communications channels, "propensity to buy" data, and better content are not helping marketing deliver substantially more revenue to organizations—at least not in the B2B environment. We would better understand what an "ultimate marketing machine" is if we invited sales to participate in the authors' survey. Comparing the responses from stakeholders in both functions may help us understand what a 21st-century marketing organization should look like.

Adam Harmon, founder, Unstoppable Corporation

More introverted consumers are also likely to surface, and this will actually make it harder to mass-market. My prediction is that marketing will become more about consumer education and matching consumer preferences, and less about product visibility and curating preferences.

Sheila Kaur, former managing director, MS&L Dubai



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It's Time to Split HR

HBR article by **Ram Charan,** July–August

Many CEOs are disappointed with their HR departments. Charan proposes a radical solution: Eliminate the position of chief human resources officer and split HR into two functions: HR-A (administration), which would manage compensation and benefits and report to the CFO, and HR-LO (leadership and organization), which would focus on improving people capabilities and report to the CEO. Here's what our readers had to say:

The struggles that CEOs are having with their CHROs sound less like an organizational design problem and more like a selection one. With the right people in the CHRO role, firms can achieve the benefits described here without dividing up the job and asking CFOs to take on a role that doesn't come naturally to them.

Tim Bowden, director of professional services, leadership, and management, Management Concepts

It may be time to rewire HR to focus on building capabilities that support strategic initiatives, but let's not throw the design of rewards programs out with the bathwater. It is true that HR leaders must spend a lot of their time on HR fundamentals, but most of us are evolving into talent architects. There is a crucial link between compensation and the right talent, and while the author might think CFOs have reached an enlightened state where they see compensation and benefits as drivers of results rather than costs, that is not realistic. Compensation and benefits design is core to the employee value proposition and the employer brand.

Libby Sartain, board member, ManpowerGroup

The frustration that CEOs feel with HR leaders is not unique. Research has highlighted similar frustrations with finance, IT, and marketing executives. It's by no means clear that other kinds of executives would do a better job than the current crop of HR leaders or that the current group doesn't include many with operational bona fides.

Jon Younger, partner emeritus, The RBL Group; adjunct, Ross School of Business, University of Michigan, and the Indian School of Business

The strategic versus transactional divide exists in all business disciplines. To say a discipline is dysfunctional because it is too transaction-focused shows a lack of vision. Many firms are great at keeping the books but not at strategic financial planning. Yet we don't say, "Time to split up finance!" Why is this acceptable with HR?

Derrick Mickle, manager, compensation, Eddie Bauer

I agree that HR leaders must help the CEO deliver the business strategy, but I disagree that most are not doing this. Most HR leaders work to identify the employee skills needed for business success, lead talent development, design organizations to deliver results, foster a culture of agility and responsiveness, and lead change efforts. All 12 *Fortune* 100 CEOs who've attended a training for new CHROs at the National Academy of Human Resources have spoken of their partnership with their CHROs and the critical role HR leaders play in implementing business strategies. Charan's solution—splitting up HR—is not viable. The HR leader must have responsibility for the full range of HR roles to deliver the best business results.

Richard L. Antoine, president, National Academy of Human Resources; retired CHRO, Procter & Gamble

Engaging Doctors in the Health Care Revolution

HBR article by **Thomas H. Lee** and **Toby Cosgrove,** June

The transformation of health care has made many doctors anxious—and resistant. To get physicians on board with change, the authors say, we need to engage them with a shared purpose, address their economic self-interest, leverage their desire for respect from peers, and appeal to their sense of tradition.

This article is very one-sided and does not consider the opinions of the physicians. It seems to ask, "How can we manipulate professionals into doing what our organization wants them to do?" If you want physicians to buy into something, simple communication and support is what you need.

Carl Hoegerl, chair, Department of Internal Medicine, Liberty University College of Osteopathic Medicine

While financial incentives might get people in the door, they're generally insufficient. Sustained success relies on a transition from short-term motivations to long-term ones.

Jay Want, MD, chief medical officer, Center for Improving Value in Health Care

I think the key line here was that improvement efforts have to go beyond slogans, which is where many great health initiatives fall short.

Lindsay McKenzie, freelance science journalist, The Data Surgery

The professional code of nurses and doctors has always placed patients' needs first. Continued customization of care requires managerial support and understanding of the increasing demands on caregivers' time. The focus should be on caregiver-patient interaction rather than alignment with corporate conceptions of efficient delivery.

George R. Cybulski, MD, associate professor of neurological surgery, Northwestern University Feinberg School of Medicine

The Crisis in Retirement Planning

HBR article by **Robert C. Merton,** July–August

When companies switched from employer-sponsored pension plans to defined-contribution plans—epitomized by the 401(k)—they transferred risk from companies onto employees and sowed the seeds of an investment crisis. The only way to avoid catastrophe, Merton says, is to shift mind-sets and metrics from asset value to income.

The real problem with 401(k)s is the average worker's inability to get qualified investing advice. ERISA laws forbid the 401(k) custodian to give advice—a good thing. Employers can offer advice but at the risk of getting sued, so they leave employees to their own devices. And in the past 10 years, we've seen Wall Street gravitate toward "wealth management" strategies, putting qualified investment advice out of the reach of middle-class investors. This, plus the gravitational pull of defined contribution plans and a reliance on the outdated modern portfolio theory, is the reason we have a retirement crisis on our hands.

Erin Condit, head of marketing communications, SumGrowth Strategies

Even within the context of the current 401(k) paradigm, there is a huge difference in the quality of employer plans. This could be approached as an employment disclosure issue. Third-party 401(k) ratings (similar to bond ratings) could be another good option. We could require a rating for plans with, say, more than 50 employees. The rating could look at investment quality and costs, returns relative to benchmarks, contribution returns, safe harbor issues, and so on and give a single letter grade to a 401(k).

Simon Lee Karpen, technical program manager, Google

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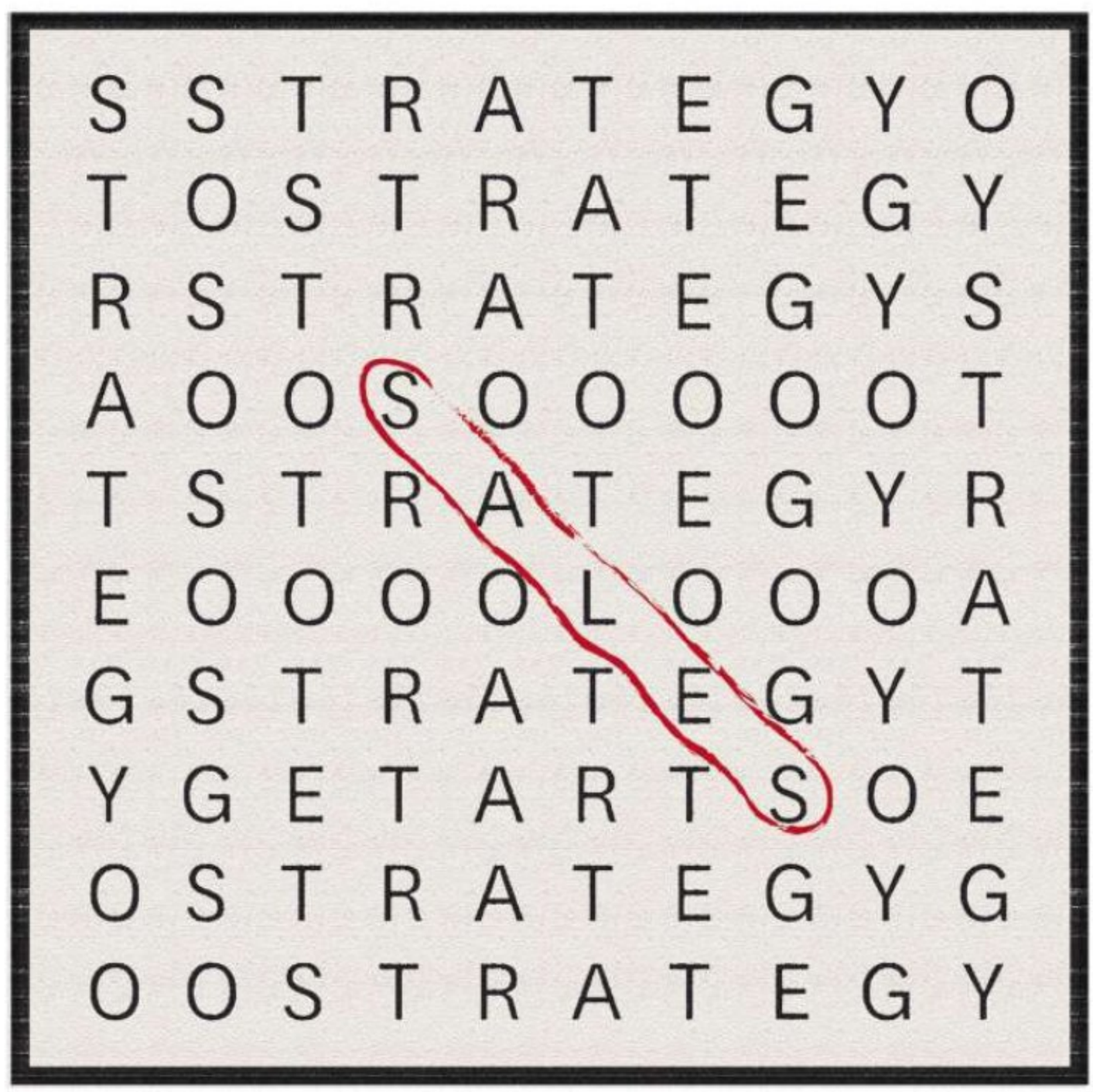
EXECUTION

Putting Sales at the Center of Strategy

How to connect the C-suite's grand plans with the field realities your salespeople face *by Frank Cespedes*

For many years Document Security Management (a pseudonym) had a thriving business in retrieving and shredding or securely storing organizations' documents. Executives and their assistants loved its one-stop-shopping value proposition, and the sales force cultivated deep relationships with them. By the early 2000s, however, it was clear that cheaper digital storage technology, especially the cloud, would disrupt the company. So DSM introduced its own cloud-based storage and directed the sales force to bundle it with traditional services.

The results were disastrous. Many of the salespeople lacked the technical knowledge to work effectively with clients' IT departments. Pricing was a problem, because the physical and digital services had very different cost structures. And in spite of being trained to bundle offerings—a key to the new strategy—reps often sold only the lower-priced, digital service. Contract renewals for traditional services fell sharply, as did profits. DSM modified its sales compensation plan, but then digital sales dipped; meanwhile, new competitors began signing clients. Ultimately DSM spun off its digital unit.



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What went wrong at DSM goes wrong at many companies: Management embarks on a strategy without considering the realities facing the people who must execute it with paying customers.

Research indicates that only a fraction—according to some studies, less than 10%—of companies' strategic plans are effectively executed and that firms deliver just 50% to 60%, on average, of the financial performance their strategies promise. One reason is that strategists, years removed from customer contact, are often blithely unaware of the embedded strategic commitments that daily field activities represent and have an obsolete vision of the company-customer interface. I describe the problem as a divide between "strategy priests" and "sales sinners," to convey that plans made in the C-suite can be "sullied" by the people who live and die by monthly quotas if those plans say nothing about how sales should allocate resources.

The sales organization should be part of every conversation about strategy. U.S. companies cumulatively spend about $900 billion annually on sales efforts—three times their spending on consumer advertising, more than 20 times their spending on online media, and more than 100 times their spending on social media. Predictions that the internet would disintermediate sales have not panned out: Although sales forces in some industries have shrunk, the overall number of salespeople in the economy is unchanged.

My research reveals four steps companies can take to improve the alignment between strategy and sales.

Communicate the Strategy

People can't implement what they don't understand. Yet few strategic plans articulate the implications for customer-contact behaviors in the field, where value is created or destroyed. Moreover, the process for introducing and reviewing plans often exacerbates the separation of the strategists from the "doers." It typically involves a kickoff sales meeting followed by a string of e-mails from headquarters and periodic reports back on results. There are too few communications, and most are one-way; the root causes of underperformance are often hidden from both groups.

Similarly, even when sales teams are trained in negotiation and selling tactics, the larger strategic context—especially the implications for target priorities—is often left out, either because the company isn't clear on its strategy or because leaders are afraid of leaks to the competition. Companies suffering from the first problem should recognize that clarifying strategy is a leadership responsibility. When the second is the issue, leaders should realize that they'll have bigger troubles than competitors' reading their big-picture strategy documents if their own people don't understand those documents.

Continually Improve Sales Productivity

Three variables drive the productivity of a sales model: customer call capacity, close rate, and profit per sale. The relative importance of each differs from company to company. Managers can boost capacity by providing better leads or giving salespeople incentives to make more calls; they can increase close rates by emphasizing the need to select the right customers and match them with optimal products or services; and they can increase profit per sale by lowering selling costs, improving the pricing or product mix, or selling more to each customer. If the sales team doesn't know how a strategic goal affects or should affect any of those variables, it will devote resources to activities that don't help, and probably hinder, execution.

Strategists, years removed from customer contact, often have an obsolete vision of the company-customer interface.

Business Processing Inc. (a pseudonym) discovered and remedied such a problem. An outsourced payroll service founded in 2000, BPI had a 75-person sales team and $40 million in revenue by 2004. But then growth stalled, and in 2008 a board member urged the CEO to analyze a question that should be central to any actionable strategy: "Who are our ideal customers?" A deep dive into the customer relationship management system yielded an answer: Clients with 15 to 50 employees, in urban locations, with at least five years of operating history. With this insight BPS shifted its selling focus. It started tracking how many calls reps placed to CPA firms in search of referrals, along with the contacts thus obtained, and paid commissions only on sales to customers of the designated type. Some salespeople hated the new system—within a year the number of reps dropped to 35. But during that time bookings increased by 25%, churn slowed, and profits and revenue jumped. Salespeople knew exactly what criteria to use to maximize productivity, and incentives encouraged behavior that supported strategy.

Improve Human Performance

Research by Jim Dickie and Barry Trailer of CSO Insights shows that the average annual turnover rate in sales organizations is 25% to 30%, which means that companies essentially replace their sales teams every four years. And individual performance differs much more than in other functions. In B2B contexts, rep performance in similar territories often varies by 300% between the top and bottom quintiles, whereas in retail selling productivity typically varies by a factor of three or four.

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LOUIS D'AMBROSIO headed IBM's software sales force before becoming the CEO of the communications firm Avaya and then of Sears Holdings; he is now the chairman of the clean-tech company Sensus. He spoke with HBR about addressing the disconnect between strategy and sales. Edited excerpts:

How dramatically does the sales process need to shift to support a new strategy?
When I was at IBM, we were accelerating growth of the software business, and the generalized tech sales reps, who'd been focused on hardware, weren't satisfactory—the product attributes varied too much. So we hired a lot of specialized software reps. We also had to think about whether you need multiple specialists calling on a customer or whether there's more synergy from having a single rep for a broad product line. At Avaya, when we shifted from traditional telephony in favor of voice over internet protocol, or VOIP, we needed reps with network and internet skills, not traditional telecom-equipment sales reps, so we brought in more than a thousand new people. Different strategies call for different approaches to go-to-market.

How should the C-suite communicate strategy to the sales team?
A great story not told doesn't count. You have to repeat something at least 10 times for an organization to fully internalize it. As CEO, I held monthly all-hands calls to keep everyone informed about strategy.

Does the compensation system have to change with a new strategy?
Yes—compensation needs to be continually evaluated. For example, if you're changing from a hardware product to a software product—moving from a traditional installation to a licensing structure—compensation has to change accordingly. Some businesses need to sell maintenance contracts, which can be very profitable, but if too much of the compensation system focuses on selling new products, it's easy to ignore the maintenance. That's a way to lose money very quickly.

Yet much of the hiring and training of salespeople is ad hoc—overly reliant on gut feelings and sales experience elsewhere. Research by my HBS colleague Boris Groysberg shows that "star talent" isn't very portable, and that's especially true in sales. Sales tasks are determined by a firm's strategy and choices, and selling behaviors are driven by the sales control systems and culture—not by a generic selling methodology or what a rep has learned at a previous firm. Companies need to understand which sales skills are most important to their particular strategy and work to upgrade them.

HubSpot, a Massachusetts-based inbound marketing firm, does this well. Its chief revenue officer, Mark Roberge, hadn't run a sales organization before joining the company, but with a degree in engineering, he had the skills to create hiring and training processes based on metrics and analysis. He devised specific job criteria and carefully scored each of the 500 candidates he interviewed in the course of a year; subsequent regression analysis at six- to 12-month intervals showed how his 20 hires performed, letting him see whether he was correctly weighting particular criteria. Instead of having new reps shadow a star, as is common practice, Roberge instituted a monthlong classroom training session, a 150-question exam, and six certification tests about HubSpot's products, sales methodology, and overall strategy.

Make Strategy Relevant

The goal of strategy is profitable growth, meaning value above the firm's cost of capital. There are basically four ways to achieve it: investing in projects that earn more than their cost of capital, increasing profits from existing capital investments, reducing the assets devoted to activities that earn less than their cost of capital, and reducing the cost of capital itself. Most C-suite executives know these value-creation levers, but too few understand and operationalize the sales factors that affect them.

In most firms, projects are driven by revenue-seeking activities with customers, so customer selection efforts directly impact which activities the firm (knowingly or unknowingly) invests in. Earning more from existing investments requires all elements of sales productivity. Reducing the assets devoted to underperforming activities requires understanding evolving customer realities and therefore depends on communication between the C-suite and the field. And financing needs are set in large part by capital on hand against the working capital needed to conduct and grow the business. The selling cycle is usually the biggest driver of cash out and cash in: Accounts payable accumulate during selling, and accounts receivable are largely determined by what's sold at what price and how fast. So increasing the close rates and accelerating the selling cycle is a strategic issue, not just a sales task.

If you and your team can't make the crucial connections between strategy and sales, then no matter how much you invest in social media or worry about disruptive innovations, you may end up pressing for better execution when you actually need a better strategy or changing strategic direction when you should be focusing on the basics in the field. As I once heard Sam Walton remind his executives, "There ain't many customers at headquarters."

HBR Reprint F1410A

Frank Cespedes is a senior lecturer at Harvard Business School and the author of *Aligning Strategy and Sales* (Harvard Business Review Press, 2014).

ILLUSTRATION: BARRY FALLS

Research Watch

START YOUR NEXT MEETING WITH A JOKE

Three-member teams with at least one person in a good mood were more than twice as likely to solve a puzzle as teams whose members were all in neutral moods, according to an experiment by **Kyle J. Emich,** of Fordham University. That's because people in good moods are more likely to share knowledge and seek information from others, which cues the rest of the group to follow suit.

PHILANTHROPY *by Michael I. Norton and Jill Avery*

Making Charity Pay

Companies are increasingly experimenting with the use of philanthropy to enhance consumer loyalty, brand awareness, and sales. But even highly creative approaches that garner a lot of buzz often fall short of sales goals, leading many companies to conclude, prematurely, that charity doesn't pay. Our research, in contrast, suggests that charity can drive engagement—when done right.

A cautionary tale: Pepsi decided to forgo advertising in the 2010 Super Bowl and instead put the money—$20 million—toward social causes through a program called the Pepsi Refresh Project. It posted consumer-generated initiatives such as school renovations and park restorations on a dedicated website and funded them according to how many votes they received. The effort made a big splash on social media—more votes were cast for Pepsi Refresh projects than in the 2008 U.S. presidential election—but sales of Pepsi products actually declined.

What went wrong? Pepsi failed to align what we call the three Cs of consumer philanthropy. Put simply, *companies* need to choose *causes* that resonate with *customers* in a way that drives sales. The lack of any connection between Pepsi Refresh causes and a product purchase meant the link between the customer and the company was missing. Lots of the people who responded to the effort were not Pepsi consumers or even likely prospects.

An experiment we recently conducted shows the importance of synergy among the three Cs. The nonprofit DonorsChoose lets public school teachers post projects—buying microscopes for their students, say—that consumers can fund directly. In collaboration with Crate and Barrel, we sent $25 gift cards that could be put toward any project on the DonorsChoose website to thousands of the retailer's customers and then compared their subsequent purchases and their attitudes about the store with those of customers who did not receive gift cards. The recipients not only came back to Crate and Barrel sooner to make another purchase but also reported more positive feelings toward the retailer.

This campaign succeeded because the three Cs were tightly linked: Crate and Barrel customers are interested in home improvement, and DonorsChoose is all about school improvement.

We suggest three strategies for managers considering consumer philanthropy. First, don't make project decisions according to causes the CEO cares about (a common practice in corporate philanthropy). Instead, consider causes your customers care about. And don't base that judgment on what they have "liked" on Facebook; look for causes to which they have already given time and money. Those are the ones that will inspire them to act.

Second, be clear about how a purchase will benefit the cause. Customers of Toms Shoes know that if they buy a pair of shoes, the company will send a pair to someone in need. So, faced with spending the same amount to get two pairs from Toms (one of which is donated) or one pair from a competitor, they see the value in the first choice.

> Don't base projects on causes the CEO cares about. Consider causes your customers care about.

Third, conduct careful experiments. Many people assumed that the Pepsi Refresh initiative caused Pepsi's poor sales. But a host of other factors, including aggressive advertising by Coca-Cola, may have been responsible. When feasible, assign some customers to the charitable promotion and others to a control condition, as we did. That will give you the best opportunity to gauge the effect of doing good.

HBR Reprint F1410B

Michael I. Norton is a professor at Harvard Business School and a coauthor of *Happy Money* (Simon & Schuster, 2013). **Jill Avery** is a senior lecturer at HBS.

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Stat Watch

In a survey 91% of university staff members said they had been ignored, avoided, shut out of conversations, or treated as invisible during the previous year, according to a study led by **Jane O'Reilly,** of the University of Ottawa. Research shows that ostracism does more psychological harm and causes higher turnover than outright harassment, which is far less common.

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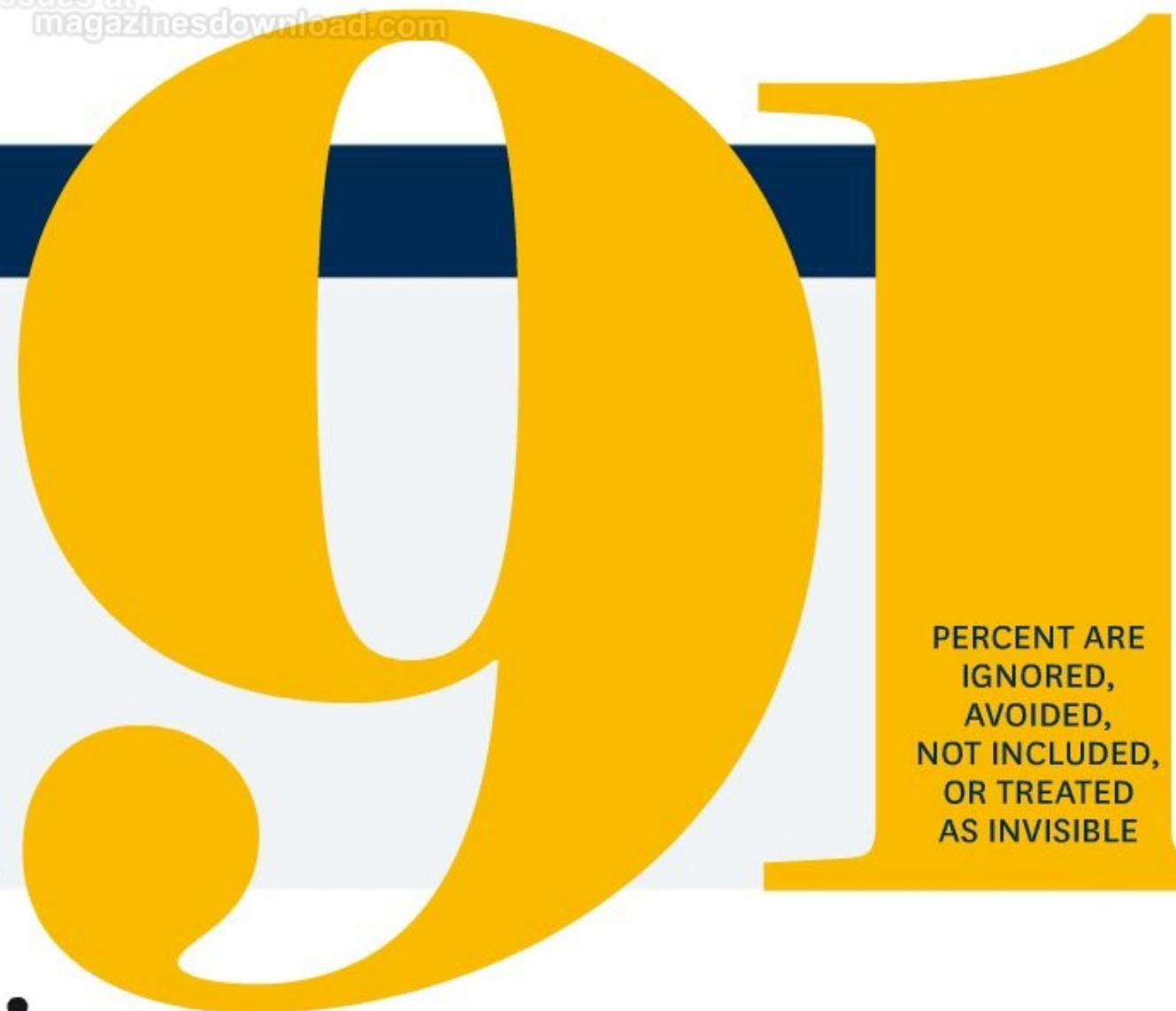

MARKETING *by Jingjing Ma and Neal J. Roese*

The Danger of Touting a Product as "the Best"

A company has a great product and naturally wants consumers to think of it as the best they can buy. So the marketing team rolls out an advertising campaign showing why the product is superior to the competition on features and price and is rewarded with robust sales. Instead of being able to bask in that success, however, the company starts to hear a lot of complaints and get a lot of returns. Clearly, the strategy backfired—but why?

It turns out that comparative ads and "Ours is the best!" product positioning activate something known as the maximizing mind-set, which leads people to regard anything that's less than perfect as a waste of money.

Our research has found that although some people are "maximizers" by nature, and others tend to be content with "good enough," those attitudes aren't fixed. The maximizing mind-set can be induced by situations that encourage people to make comparisons and to look for the very best. When marketing messages inadvertently induce it, the results may be post-purchase regret and brand switching at the slightest hint of disappointment.

In a series of experiments, we used various activities to prime university students to adopt the maximizing mind-set, in an effort to mimic the effect that "best ever" ads can have on consumers. Then we

tested how satisfied the participants were with a product.

In one experiment, for instance, we asked a group of students to determine which was the best option from among several compensation packages, mortgage deals, and the like. (A second group was simply asked whether the options differed.) We then asked all the participants to choose a snack. Half of them received the one they had selected, and half were given a substitute on the grounds that the one they wanted had run out. Finally, we asked the participants to rate their snacks on several dimensions. The students who had been primed for the maximizing mind-set and then denied their choice of snack expressed significantly more dissatisfaction than people in the other groups; this in turn reduced the amount they would have been willing to pay for the snack and increased their desire to switch to a different brand. Other experiments in our study produced similar results when consumers evaluated products while they were in a maximizing mind-set.

For marketing managers, this research provides clear guidance regarding advertising and in-store displays. Companies should think twice about comparative ads and assertions of "optimal" features, lest their products fall short in any way. And few brands are immune: Prior research has shown that just barely missing the best option can cause the most intense regret of all. Even managers who are highly confident in their products might avoid some headaches by refraining from comparisons and dialing back superlative claims.

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Jingjing Ma is a doctoral candidate at Northwestern University's Kellogg School of Management, where **Neal J. Roese** is the John L. and Helen Kellogg Professor of Marketing.

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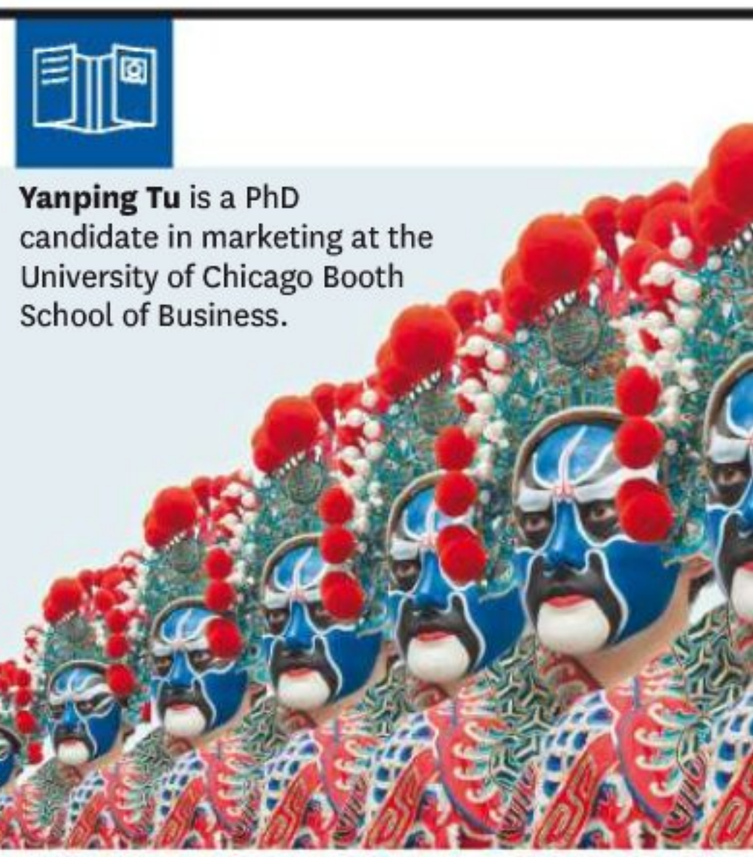

Yanping Tu is a PhD candidate in marketing at the University of Chicago Booth School of Business.

People Don't Like Anything (or Anyone) Moving Toward Them

The study: In eight experiments, doctoral student Yanping Tu and three collaborators—Christopher K. Hsee of the University of Chicago and Zoe Y. Lu and Bowen Ruan of the University of Wisconsin—found that people feel more negative toward individuals, images, and sounds if those "stimuli" are perceived to be approaching them. This aversion has cautionary implications for public speakers who like to get close to their audience as well as for marketers who zoom in on products in ads.

The challenge: Are people really repelled by anything coming toward them—even if it's a friend or a vacation? **Ms. Tu, defend your research.**

Tu: Our research shows that people feel more negative toward stimuli when the stimuli appear to be oncoming in space. Our experiments included a range of images, such as English letters, a poster from a Chinese opera, a happy-face emoticon, and a picture of a smiling man. What's more, we found the same effect with nonphysical stimuli—such as a cousin's visit or other events—that were approaching in time or increasing in likelihood.

HBR: An approaching smiley face? That sounds like a scene from a nightmare. And a smirking stranger? No wonder research subjects got the creeps when these things came at them.
First we measured people's feelings toward the images and events, so we were sure participants considered them to be positive. The happy-face emoticon was rated as 4.49, on average, on a 1-to-5 scale where 5 was "very positive." Neutral-face and frowning-face emoticons were rated 3.18 and 1.59, respectively. The responses to the images of the man were similar: When he was smiling, neutral, or frowning, he was rated 5.14, 3.86, or 2.92, respectively, on a 1-to-7 positivity scale. In the experiments all the ratings declined when the stimuli were perceived to be approaching.

But what about the approach of a person I love? Or of a welcome event?
When I first put this interview on my calendar, I thought, "How wonderful—an opportunity to share my research!" But as the date neared, I grew apprehensive. What if I got a question I couldn't answer? What if I couldn't explain myself well? Even very positive things can have negative aspects, which become more prominent in our minds as they draw close.

As for someone you love: Chances are, you feel a bit more fretful as the person approaches—you might worry that the person will ask something of you, for example—but those feelings may be overwhelmed by your happiness at being reunited. So you're experiencing layers of feelings—some negative, most positive. In our research we tried to tease apart those confusing layers by comparing people's feelings toward a gradually approaching individual with their feelings about someone who simply stayed near. We were able to show that although you may feel positive toward a loved one who approaches, you feel less positive than you would if that person were to remain near you.

My gut tells me that if I'm speaking to a group, my listeners will react more favorably if I get out from behind the podium and approach them.
Indeed they might. It's all about those layers of feelings. If you step out and get close to your listeners, they might perceive you as warm and friendly—that's one layer. But an undercurrent of negative feeling will increase as you get nearer. Without being able to articulate it, your listeners might feel intimidated or threatened. They might feel you're invading their space. Same goes for a manager walking toward an employee. The manager probably doesn't realize that with every step, the employee feels more negative about the manager. So it is one thing to stand close to people and quite another to walk closer to them.

The effect also may apply to ads showing products moving toward the viewer. If it's a beautiful new car, the viewer might

People felt increasingly negative about a poster showing a character from a Peking opera as it was wheeled toward them.

be pleased on one level that it's closer. But on another, she'll feel negative about its approach. To reduce other factors that might influence the subjects' reactions, we usually had subjects view computerized images that grew larger and therefore appeared to approach.

How do you know participants didn't perceive that *they* were approaching the stimuli? In general, people perceive an enlarging image to be coming toward them. However, when we suggested to participants that they were approaching the stimuli, rather than the reverse, the aversion disappeared. We tested this on the image of the neutral-faced man. Approaching him didn't make participants feel worse about him, as it did when subjects thought he was approaching.

What about the time aspect: Should my editors stop making such a big deal about my deadlines? The mind often treats space and time similarly. So a temporally approaching event can also be unsettling. It's quite possible that a manager can unwittingly increase an employee's negative feelings about a project by reiterating an approaching deadline. It would be especially annoying if the manager first scheduled a task, such as a meeting, for a time in the distant future and then moved it closer. Even if employees initially felt neutral about the meeting, the change would make them dread it. Increasing an event's likelihood causes similar effects.

What got you thinking about this topic? I'd love to say we had an Isaac Newton moment when we discovered the "law" of approach aversion—that we saw a beach ball rolling toward us and wondered how we felt about it—but in truth, we were talking about what it's like to be at a social event. You see someone in the crowd and think, "Hmm, that's an attractive person. I'd like to talk to that person." As he or she approaches, your feelings start to change. You worry, you fret, you feel threatened. We wondered: Why does that happen?

And why does it? It probably has to do with evolution. People evolved to understand that stimuli pose a greater danger if they're approaching, and we're still wired that way. Just as, through eons of searching for food, we evolved a belief that scarce things are good, which is why we grab the last blue dress off the rack, even if we don't need another blue dress—speaking from experience here.

How can a public speaker or a marketer apply your findings? You might be better off starting a speech near the audience—maybe a short distance from the front row—and staying there. Show your product in close-up. Beware of moving toward people, shoving a product in their direction, or moving an event up. Their evolutionary instincts will kick in, and their opinion of you, the product, or the event will start to fall.

HBR Reprint F1410D
Interview by **Andrew O'Connell**

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Vision Statement

What We'll Be Doing in 2022

A lot of health care, according to the U.S. government

When the U.S. Bureau of Labor Statistics looks into its crystal ball, it sees an aging population in need of care and a construction industry still rebounding from the Great Recession. In the decade from 2012 to 2022, the fastest growth in U.S. employment will take place in the health care, health care support, construction, and personal care fields. These four categories are expected to account for more than a third—

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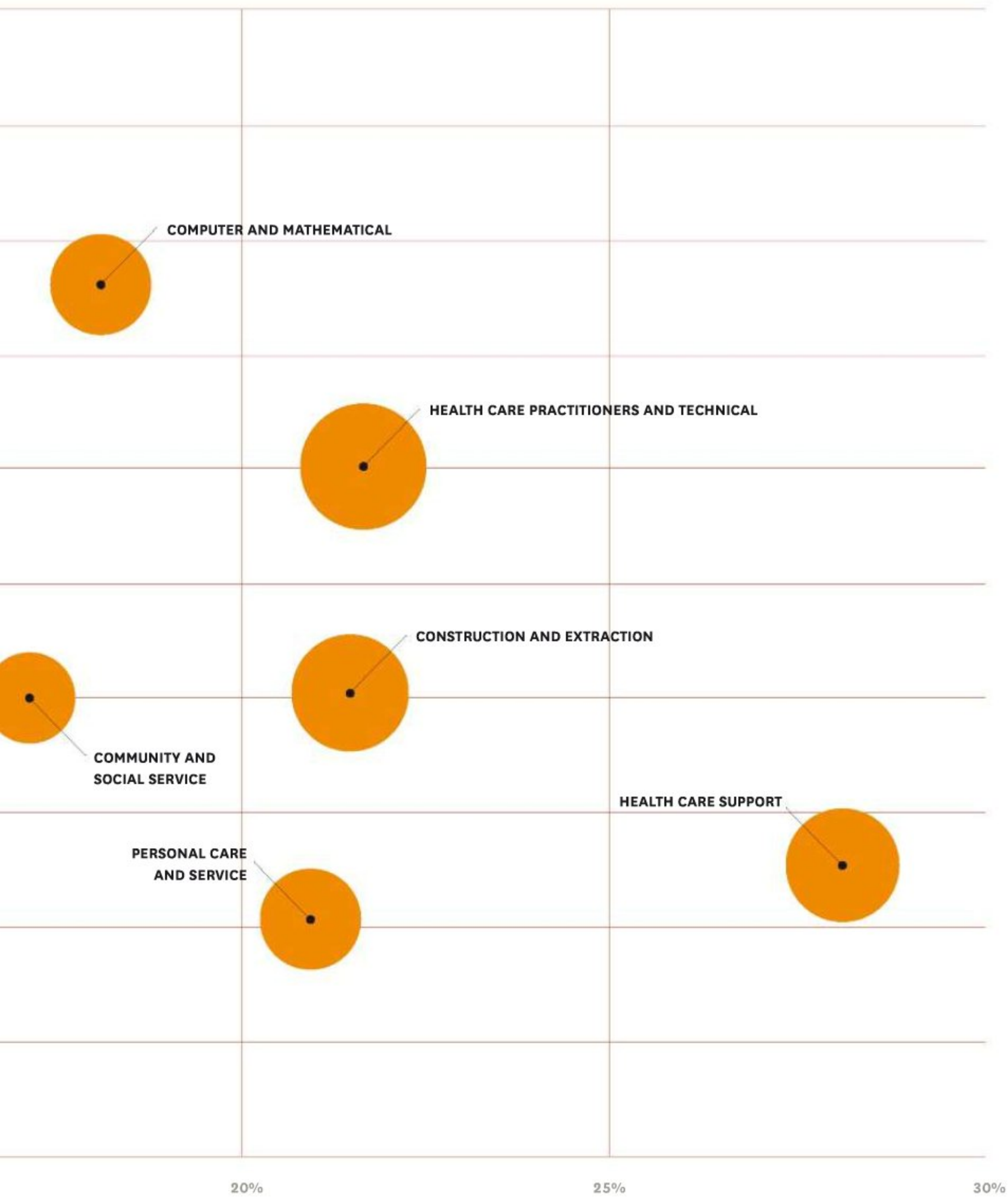
about 6.6 million—of all new jobs. Farming, fishing, and forestry is the only category expected to shrink.

Although most of the growth is expected in fields that don't require post-secondary education, jobs that demand a college degree or higher are actually growing faster (14.0% versus 9.1%). And those higher-skilled jobs will pay, on average, more than twice as much ($57,770 per year versus $27,670).

Managerial jobs are growing fastest in IT—no surprise. Also expected to show strong gains are the fields of human resources, public relations, marketing, and operations. The fastest-disappearing jobs are those in industrial production—reflecting the manufacturing sector's expected continuing decline. And CEOs? Their numbers are projected to grow by just 5.3%.

HBR Reprint F1410Z



SOURCE BUREAU OF LABOR STATISTICS, U.S. DEPARTMENT OF LABOR

*MANAGING EXPECTATIONS

Projected percentage growth by 2022 of selected management jobs

Computer and information systems	**15.3%**
Human resources	**13.2%**
Public relations and fundraising	**12.9%**
Marketing	**12.7%**
General and operations	**12.4%**
Administrative services	**12.2%**
Training and development	**11.2%**
Financial	**8.9%**
Sales	**8.3%**
Advertising and promotions	**6.9%**
Legislators	**6.4%**
Chief executives	**5.3%**
Transportation, storage, and distribution	**4.9%**
Compensation and benefits	**3.1%**
Purchasing	**2.1%**
Industrial production	**−2.4%**

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How I Did It…

Fallon's Chairman on Getting Clients to Take Creative Risks

PHOTOGRAPHY: DAVID BOWMAN

by Pat Fallon

THE IDEA

Even companies that say they want an edgy campaign often balk when it's pitched. Fallon describes how his team assesses whether clients are really open to something unconventional—and then persuades them to take the leap.

I graduated from college in 1968 with a degree in philosophy and the humanities, so I was prepared for absolutely nothing that might align with making money—and I didn't like being poor. So I took a job in the training program at Leo Burnett in Chicago. I fell into advertising, and then I fell in love with it. After a year in Chicago, I moved to Minneapolis and worked at a couple of other agencies—one for seven years, one for five.

In 1981 four partners and I founded Fallon McElligott Rice (shortened to Fallon after Nancy Rice left, in 1985, and Tom McElligott followed, in 1987). We got off to a fast start with some edgy and creative projects, and in 1984 we were named *Ad Age*'s Agency of the Year. Later on we sold the agency to a big company, bought it back, and then sold it again to Publicis, in 2000. Today we have offices in Minneapolis, London, and Tokyo; our largest clients are Škoda (for which we

have full global responsibility), H&R Block, Arby's, and Travelers insurance.

So I've worked in advertising for four and a half decades. During those years I've spent a lot of time persuading clients to run advertisements that feel risky—maybe even dangerous—the first time they see them.

Taking risks is part of our business. Often it's imperative. One of the most important things we do is assess each client's risk appetite: It's a moving target, dependent on the emotional makeup of the decision makers, the state of the company, the industry, and many other variables. We've had new clients come in like a hospital patient on a respirator: They feel they've tried everything, nothing has worked, and we're their last gasp, so they're predisposed to something unconventional. But some industries and categories, such as pharmaceuticals and airlines, are inherently more risk averse than others.

One key to persuading clients to take a risk is tightly aligning strategy with the creative approach. Although some observers think advertising comes down to crazy people sitting in a room brainstorming, strategy is the rigorous, behind-the-scenes part of our process—it's driven by research and consumer insights, and it helps to precisely define what the company is trying to accomplish with a campaign, who the campaign is meant to reach, and why it's going to trigger a specific response that drives sales. An idea that may seem risky during a presentation will look less so when it's clear that we've thought it through. The client realizes, "These guys understand my business. They understand the flow of money. They are putting my success at the forefront of decisions." That creates enough trust for the client to say, "OK, I'm going to hold my breath, hold my nose, and jump into the water with you."

"Live Richly"

When it comes to persuading clients to take risks, the first campaign I think of was for Citibank. In the late 1990s Citi's CEO, Sandy Weill, had been building the company into a "financial supermarket"—a new concept. But as a brand, Citibank had trouble differentiating itself from competitors. Retail banking is difficult in that regard. Historically, banks relied on free toasters to lure customers away from competitors; now, even if a bank creates some extraordinary new financial instrument, within 90 days all its competitors can have it too. We weren't sure we could find a way to make Citi stand out—just like its customers, we saw it as sterile and corporate.

Citi's CMO and head of advertising made a presentation that changed our minds. The bank had completely altered the way it did business internally, and now it wanted to communicate that change externally. Ordinarily, when prospective clients say they want a radical creative campaign—"Show us something that scares us" is a typical line—they don't really mean it. So despite Citi's invitation, we expected to have to work hard to persuade its executives to follow our recommendations.

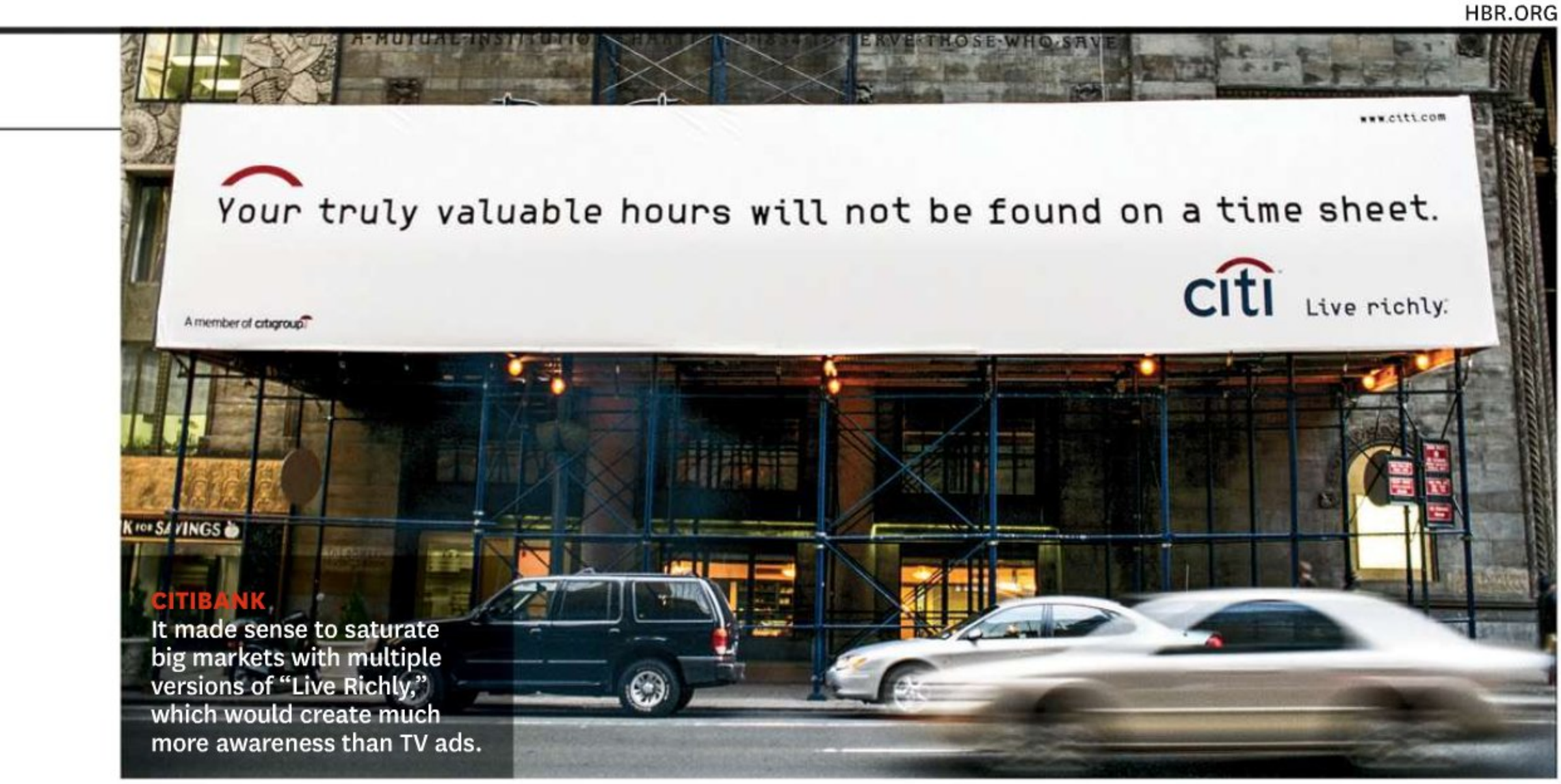
At first the Citi executives found our ideas jarring. But as we kept talking, they began to relax.

Like many large companies, Citi had done tons of research. It needed fresh eyes to discover the insights within the data. We found them by looking at the larger cultural context. The dot-com boom was in full swing, and magazines were featuring 23-year-old millionaires on their covers. Everyone seemed to be getting instantly rich. The research told us that a lot of people were skeptical—even disdainful—of that ethos. They wanted life to be rich in a holistic sense and were less concerned with financial gains. We called this segment "balance seekers." The data showed that they constituted almost 50% of banking customers.

We created a campaign to target balance seekers. Its tagline was "Live Richly." We recommended launching the campaign on outdoor billboards, and we wanted to flood the market with images and words that evoked a more realistic sense of what it means to succeed economically. "Remember, the people you are working for are at home right now," said one ad. "He who dies with the most toys is still dead," said another. We explained to Citi that we wanted its image to be unbanklike, and we suggested that it use "Live Richly" not only as an ad slogan but on all its internal branding—including employment applications.

One challenge in selling an idea like this to a large bank is dealing with the internal politics. Even if the primary decision makers like an idea, their bosses may veto it. The CMO and the advertising director brought two other senior executives to our presentation to get their buy-in, which was smart. When we first presented some of the "Live Richly" executions, I could see from their faces that they found them jarring. But as we kept talking, they began to relax. At one point, one of the executives started shaking her head no, and I stopped immediately. "What's the matter?" I asked. The problem wasn't the creative, she said; she just couldn't imagine launching a large ad campaign on billboards instead of on television. I explained that for a brand like Citi, it made strategic sense to saturate New York City and other big markets with many different versions of "Live Richly"—that would create much more awareness than TV ads. It was the right way to throw our arms around the balance seekers. As I explained the strategic rationale, she came to agree.

The campaign was extremely successful. Product differentiation is perishable, but we believed we could own a fresh, authentic attitude—one that, properly executed, could never be copied effectively.



CITIBANK
It made sense to saturate big markets with multiple versions of "Live Richly," which would create much more awareness than TV ads.

The essential truth of "Live Richly" created meaningful differentiation in a category that had defied differentiation. Citi's marketing became part of the cultural discussion. *Newsweek* picked up on it within three months of its introduction. So did *Forbes, Money,* and *BusinessWeek.*

But that was nothing compared with the consumer response. Overall interest in Citi increased, as did key brand and business measures. After a year of the "Live Richly" platform, unaided awareness increased by 20 points, brand relevance by 17 points, and differentiation from other banks by 14 points. Bank traffic and sales increased significantly, with 189% more home equity loan applications and 150% more new checking accounts. Years later, some critics said our Citi ads had played a part in the burgeoning of home equity loans that eventually led to the financial crisis, but that view totally misreads history and misunderstands the message in those ads, which were firmly based on consumer insights. We helped make Citi human, competitive, and relevant, and encouraged a healthier, more realistic approach to money.

"Just the Right Amount of Wrong"

Another risky campaign that the clients accepted was for the Cosmopolitan, a hotel that opened in Las Vegas in 2009. The Cosmopolitan hoped to attract guests who ordinarily wouldn't visit Las Vegas. The city has a reputation for being raunchy, with cheap meals and a "What happens in Vegas stays in Vegas" mentality. And the Cosmopolitan opened just a few months after *The Hangover* premiered, so this image was in everyone's mind.

In theory, these were clients who would embrace risk—they're real estate developers, so they work in an extremely volatile field. But real estate developers are beholden to their lenders, who are very conservative by nature. The Cosmopolitan was effectively owned by Deutsche Bank, which had financed the hotel. In the pitch, we succeeded in selling the top executives at the Cosmopolitan on our ideas partly because of chemistry. They reacted instantly to our people, they quickly understood what we were trying to do, and from the moment the meeting ended, we felt like we'd been hired. The bigger challenge was for Fallon, working in partnership with the Cosmopolitan, to bring the German bankers on board with the idea. The fact that our TV ad featured waiters who didn't wear pants, old ladies pinching people's butts, and a bondage scene only increased the challenge.

Traditional Las Vegas hotels appeal to the masses, whereas the Cosmopolitan would be more for a niche—as BMW is in the automotive market. We needed to find a new audience to target. We called it the "curious class"—people who like to discover new things, who like the spirit of the Strip but want something more refined. We came up with the tagline "Just the Right Amount of Wrong," which I still love. It played off the city's naughty image but tempered it and made clear how the Cosmopolitan is different. The TV spot used humor, but it also highlighted the provocative, unexpected attributes of the hotel, which has a Mexican-Chinese fusion restaurant and an incredible art collection in the lobby. The Cosmopolitan appeals to high-energy, high-taste guests; it keeps them guessing and keeps them discovering.

The campaign helped bring the Cosmopolitan some of the strongest occupancy rates and average daily rates in the category, so taking the risk paid off.

"Never Settle for Less"

A third campaign that involved a lot of risk was for H&R Block, currently our biggest client. We received a call from the company in the summer of 2010, after its CEO resigned. We'd worked with the CMO and the VP of advertising when they were at other companies, so they trusted us. They were looking for a new agency because they were facing a huge business challenge and they wanted to move quickly. They wanted to create an entire campaign for the 2011 tax season in just a few weeks, instead

PHOTOGRAPHY: COURTESY OF FALLON

of the six to eight months they'd traditionally spent developing one.

H&R Block's challenge was attracting new customers. It's a hassle to switch tax preparers, which is why 86% of filers use the same preparer (or software program) year after year. The company's share of new customers had been declining for five years straight, so H&R Block needed to do something to disrupt this inertia. The company was also frustrated because its previous campaigns had failed to get across the message that its preparers' expertise can make a real difference in the size of refunds—a key selling point. Several years earlier H&R Block had launched a free program called Second Look, in which its preparers would examine a tax return that had been prepared by a competitor (or by the filer) to identify overlooked ways to save money. But awareness of the program remained low.

Instead of doing traditional, scripted, ignorable TV ads—the kind the company had relied on for years—we wanted to do a real-life stress test of Second Look—and not just for a few strategically chosen consumers. We proposed to redo the taxes for an entire town and film the event as a documentary. We'd then turn that real-life footage into a series of commercials to run during the tax season. We would show, not tell.

The risks were huge. It was a costly undertaking with no guarantee of success. The whole idea depended on the premise that Block's preparers could find money that others had missed. If the results didn't match the claim, we'd be in big trouble.

We chose a town in Tennessee that had an apt name for the effort, Greenback, and invited all the residents to have H&R Block professionals take a free second look at their tax returns. The event was held in the high school gymnasium. In all, 97 households accepted our offer, and Block's preparers found nearly $15,000 in additional refunds. Film of the event provided the backdrop for a series of commercials carrying the tagline "Never Settle for Less." We conducted a similar event at the Nickel Diner, in downtown Los Angeles, where nearly $8,000 was found for patrons who chose to participate.

THE COSMOPOLITAN
Ads like these, from the hotel's website, hinted at Las Vegas's naughty image but emphasized the property's refined, upscale positioning.

The season's work drove Block to its best performance in more than a decade. We reversed the five-year decline and garnered 375,000 new customers. We also achieved higher retention of existing customers and increased Block's overall category share from 15.6% to 16.4%. The "Never Settle for Less" campaign continued into 2012, when nearly $250,000 in overlooked refunds was returned to the people of Detroit. In 2014 we launched "Get Your Billion Back, America," a campaign inspired by the previous work and validated by an extensive national study showing that each year a total of more than $1 billion is left on the table by inaccurate tax returns.

Risk Is Our Friend

Not every pitch goes as well as those did. We've all given presentations when we didn't really know what the hell we were doing. Sometimes we can't find a market-moving consumer insight on which to build a great campaign. Sometimes we have a great idea but we can't make the client comfortable with it. If a company takes a conceptual risk and it doesn't work, the CMO could lose his or her job. And, of course, we'd lose the work.

These risks are even more apparent now than when I started out in advertising. In the age of social media, a company is much likelier to face backlash if it chooses provocative advertisements, and the power of a single blogger can be astounding. Social media are a tremendous boon to our business when ads go viral, but they make the business much more complex than it was even five years ago. All anyone needs to communicate with the CEO is an e-mail address.

Companies have to be ready to counterpunch when ads are criticized. People are less patient for results than they used to be. And relationships tend to be more perishable. Risk management has gotten tougher, so earning clients' trust has become even more critical.

But when we're training young people in our firm, we try to teach them that risk is our friend, not something to be scared of. Our clients' end goal is not to be comfortable with their ad campaigns—it's to buy advertising that achieves their strategic aims. Sometimes we need to persuade clients that an approach that strikes them as risky is in fact safer than continuing to do what they're doing. **HBR Reprint** R1410A

Pat Fallon cofounded Fallon Worldwide in 1981 and today serves as its chairman.

PHOTOGRAPHY: COURTESY OF FALLON

Strategic Humor

CAPTION CONTEST

"So that's where they hide the silent partner."

This month's winning caption was submitted by **Tony Vance** of Millersville, Maryland.

CARTOONS: JOHN KLOSSNER, TERESA BURNS PARKHURST, CROWDEN SATZ

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The Big Idea

Roger L. Martin was the dean of the Rotman School of Management at the University of Toronto from 1998 to 2013. His most recent book is *Playing to Win: How Strategy Really Works* (Harvard Business Review Press, 2013), written with A.G. Lafley.

The Rise (and Likely Fall) of the Talent Economy

How to rein in the dynamic that enriches executives and financiers—at everyone else's expense *by Roger L. Martin*

When Roberto Goizueta died of cancer in 1997, at the age of 65, he was a billionaire. Not bad for a Cuban émigré who had come to the United States as a teenager. He was by no means the first immigrant to America to become a billionaire, but the others had made their fortunes by founding and building companies or taking them public. Goizueta made his as the CEO of Coca-Cola.

His timing was impeccable. In 1980 he became the chief executive of a company that owned no natural resources and had precious little physical capital. The talent economy had just come of age, and rewards for its key productive assets made an epochal shift—in his favor. His company was among the most valuable in the world for its iconic brand and the talent that built and maintained it. Goizueta epitomized that talent, and investors paid for it as never before.

A century ago natural resources were the most valuable assets: Standard Oil needed hydrocarbons, U.S. Steel needed iron ore and coal, the Great Atlantic & Pacific Tea Company needed real estate. As the 20th century progressed, America's leading companies grew large and prosperous by spending increasing amounts of capital to acquire and exploit oil, mineral deposits, forests, water, and land. As recently as 50 years ago, 72% of the top 50 U.S. companies by market capitalization still owed their positions to the control and exploitation of natural resources.

To be sure, those companies needed lots of labor as they continued to grow—but mainly for

PHOTOGRAPHY: PETER CROWTHER

routine-intensive jobs. Those jobs were largely fungible, and individual workers had little bargaining power; until they were enabled and motivated to unionize, suppliers of labor took a distant third place in the economic pecking order, behind natural resources and providers of capital.

The status quo began to change in 1960, with an extraordinary flowering of creative work that required substantial independent judgment and decision making. As the exhibit "The Rise of the Talent Economy" shows, creative positions accounted for a mere 16% of all jobs in 1960 (having grown by only three percentage points over the previous 50 years). That proportion doubled over the next 50 years, reaching 33% by 2010.

The top 50 market cap companies in 1963 included a relatively new breed of corporation, exemplified by IBM, which held the fourth spot. Natural resources played almost no role in IBM's success, and although capital was not trivial, anybody at the company would have argued that its intensively creative employees—its scientists and engineers, its marketers and salespeople—were at the heart of its competitive advantage and drove its success in the marketplace. The same could be said for Eastman Kodak, Procter & Gamble, and Radio Corporation of America, all businesses whose success was built on talent.

By 2013 more than half the top 50 companies were talent-based, including three of the four biggest: Apple, Microsoft, and Google. (The other was ExxonMobil.) Only 10 owed their position on the list to the ownership of resources. Over the past 50 years the U.S. economy has shifted decisively from financing the exploitation of natural resources to making the most of human talent.

From Dream Asset to Dream Deal

Through the 1970s the CEOs of large, publicly traded U.S. companies earned, on average, less than $1 million in total compensation (in current dollars)—not even a tenth of what they earn today. In fact, from 1960 to 1980 the providers of capital got an ever-improving deal from the chief executives of those companies, who earned 33% less per dollar of net company income in 1980 than they had in 1960. In that era the situation was similar across the talent classes, from professional to scientific to athletic to artistic.

> It's unsurprising that ordinary employees have long accepted this rebalancing of income—after all, it fits the American Dream.

After 1980, however, it seemingly became essential to motivate people financially to exercise their talent. Skilled leaders saw a major boost in income for two reasons:

High earners kept more money. After the Great Depression, tax policy shifted to a focus on sharing the economic pie. It was thought that a high concentration of wealth had contributed mightily to the Depression and that the rich should pay a fair share to finance the creation of secure jobs and the consumption of goods that accompanied them. Consequently, the top tax rate on high earners—a modest 25% in 1931—rose steadily to 91% by 1963, at which point someone who earned $1 million kept only $270,000 after federal taxes, and someone who earned $10 million kept a mere $1.5 million.

This started to change in the mid-1970s, when a group of economists that included Arthur Laffer and the future Nobel laureates Robert Mundell and Herbert Simon argued that above a certain tax rate on the last dollar of their earnings, the amount of work individuals supplied to the marketplace would begin to fall, and the higher the rate, the more precipitous the drop. In fact, according to Laffer's famous curve, the strength of this effect would at some point yield fewer dollars to the U.S. Treasury.

This supply-side thinking justified a major shift in tax policy. The top marginal rate plummeted from 70% in 1981, to 50% in 1982, to 38.5% in 1987, to 28% in 1988. Thus, in a mere seven years, $1 million earners saw the amount they kept after federal taxes increase from $340,000 to $725,000, while the $3.0 million that $10 million earners had been keeping grew to $7.2 million.

They were paid in stock and profits. In 1976 Michael Jensen and William Meckling published the now legendary "Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure" in the *Journal of Financial Economics*. The article, which brought agency theory to the world, argued that corporations needed to align the interests of management and shareholders—talent and capital—to keep agency costs from causing damage to shareholders and the economy in general.

For corporate executives, the alignment mechanism of choice was stock-based compensation. It has done wonders for CEO pay, which doubled in the 1980s, quadrupled in the 1990s, and has continued to grow in the 21st century

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Idea in Brief

THE PROBLEM
Talent is now the prime asset in the global economy, and in the United States it commands a hugely inflated share of the rewards for economic growth. The resulting inequality of income between top talent and routine workers is unsustainable—and the volatility that talent creates is more ominous still.

WHY IT HAPPENS
The reward structure of hedge funds and leveraged buyouts foments price volatility in asset trading, while stock-based compensation encourages corporate executives to further the interests of traders rather than those of long-term investors.

THE SOLUTION
Governmental regulation, tax reform, and the voluntary cooperation of top executives, private equity managers, and pension funds should combine to create a better mix of rewards for capital, labor, and talent.

despite increasing criticism and the devastation caused by the global financial crisis. Another, less well-known mechanism that has boosted income for the possessors of talent is the notorious "2&20 formula." Its roots lie in a 2,000-year-old practice whereby Phoenician ship captains would take 20% of the value of a cargo successfully delivered. In 1949, when a fee of 1% to 2% of assets under management was typical in the investment management field, Alfred Winslow Jones, the first acknowledged hedge fund manager, adopted the Phoenician formula. He set himself up as the general partner of what would come to be referred to as a private equity firm and charged the limited partners who invested in his fund a 20% cut of the profits that he generated ("carried interest," in industry parlance) on top of a 2% asset management fee.

When the venture capital industry, which had also started in the immediate postwar period, shifted to the private equity firm model at the end of the 1950s, it adopted this lucrative 2&20 fee structure, as did the leveraged buyout industry, which took shape in the mid-1970s. But the biggest beneficiary was the hedge fund industry, which grew to immense size and applied the 2&20 formula to ever larger and more lucrative pools of limited partner capital.

It's no surprise that talent got much richer after it was recognized as the linchpin asset in the modern economy. It's also unsurprising that ordinary employees have long accepted this rebalancing of income—after all, it fits the American Dream, in which hard work and the cultivation of talent deserve rewards. People don't mind your being rich if you made the money yourself; what they don't like is your inheriting wealth. And the evidence is clear that the vast majority of *Forbes* billionaires are self-made. But the assumptions underlying that compliance are starting to change. People increasingly ask whether talent is overcompensated—and whether it's quite the unalloyed good it has historically been made out to be.

The Downside of the Deal

Our basic grievance with today's billionaires is that relatively little of the value they've created trickles down to the rest of us. Real wages for the 62% of the U.S. workforce classified as production and nonsupervisory workers have declined since the mid-1970s. The billionaires haven't shared generously with investors either. Across the economy, the return on invested capital, which had been stable for the prior 10 years at about 5%, peaked in 1979 and has been on a steady decline ever since. It is currently below 2% and still dropping, as the minders of that capital, whether corporate executives or investment managers, extract ever more for their services.

As a consequence, since the mid-1980s inequality has rapidly increased, with the top 1% of the income distribution taking in as much as 80% (estimates vary) of the growth in GDP over the past 30 years. Serious as this is, rising inequality is not the most ominous aspect of the situation. Our current system of rewarding talent not only doesn't lead to greater overall value for society but actually makes the economy more volatile, with all but a fortunate few moving sideways or backward.

Evidence can be seen in the changing composition of the *Forbes* 400. Over the past 13 years the list's number of hedge fund managers, by far the fastest-growing category, has skyrocketed from four to 31, second only to computer hardware and software entrepreneurs (39) in possessing the greatest fortunes in America. If the LBO fund managers on the list are included, it becomes clear that far and away the best method of getting rich in America now is to manage other people's money and charge them 2&20. As Steven Kaplan, of the University of Chicago, and Joshua Rauh, of Stanford, pointed out

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in a recent paper, the top 25 hedge fund managers in 2010 raked in four times the earnings of all the CEOs of the *Fortune* 500 combined.

What are those 25 people doing?

Essentially, the business of a hedge fund is to trade. James Simons, the founder of Renaissance Technologies, ranks fourth on *Institutional Investor*'s Alpha list of top hedge fund earners for 2013, with $2.2 billion in compensation. He consistently earns at that level by using sophisticated algorithms and servers hardwired to the NYSE servers to take advantage of tiny arbitrage opportunities faster than anybody else. For Renaissance, five minutes is a long holding period for a share.

Modern market structures enable hedge funds to trade like this by borrowing stock in large amounts, which means they can take short positions as well as long ones. In fact, hedge fund managers don't care whether companies in their portfolios do well or badly—they just want stock prices to be volatile. What's more, they want volatility to be extreme: The more prices move, up or down, the greater the earning potential on their carried interest. They aren't like their investment management predecessors, long-term investors who wanted companies to succeed.

But trading doesn't directly create value for anyone other than the hedge funds. One trader's gain is simply another trader's loss. It's nothing like building a company that gives the world a better product and generates employment. Of course, hedge fund aficionados argue that the funds help corporations offload interest-rate or exchange-rate risk, thus adding economic value to the world. It's a nice rationalization, but a tiny fraction of the multitrillion-dollar industry could take care of the relatively modest task of hedging corporate financial asset risk. Besides, market volatility has increased dramatically as the hedge fund industry has grown, undermining any argument about the net risk-management benefit of hedge funds.

The shift from building value to trading value is worrisome, but the real problem for the economy is that hedge fund talent and executive talent both have an incentive to promote volatility, which works against the interests of capital and labor. Executive talent, as we saw earlier, is now rewarded primarily with stock-based compensation, which was supposed to align managers with the long-term interests of owners. But a stock price is nothing more than the shared expectations of investors as to a company's future prospects. If expectations for performance rise, the stock price rises, and vice versa. Thus stock-based compensation motivates executives to focus on managing the expectations of market participants, not on enhancing the real performance of the company.

> The top 25 hedge fund managers in 2010 raked in four times the earnings of all the CEOs of the *Fortune* 500 combined.

What's more, because stock-based compensation is generally conferred annually at the prevailing stock price, managers have an interest in volatile expectations for their company. If expectations fall during the course of a given year, the options or deferred stock granted a year later will be priced low. To reap a big reward, all managers have to do is help expectations recover to the prior level.

That's why the global financial crisis was not all bad for CEOs. Consider John Chambers, the CEO of Cisco Systems since 1995. Like Roberto Goizueta, Chambers became a billionaire by running a publicly traded company. But during his tenure Cisco shareholders have suffered through two bubbles and busts. The share price peaked at $80.06 in March 2000 and plummeted to $8.60 in October 2002. It worked its way into the $25–$33 range for most of 2007 and reached $34.08 in November of that year. In the wake of the subsequent financial crisis it collapsed to $13.62 in March 2009, climbed to $27.57 in April 2010, fell to $13.73 in August 2011, and had recovered to $24.85 by the end of June 2014.

It was a pretty wild ride for the shareholders of record as of November 2007. Those who hung in through the end of June 2014 experienced a decline of 27% in their stock price and two 60% drops along the way. But it wasn't so bad for Chambers. Those two big dips were handy for picking up attractively priced stock-based compensation—options in November 2009 at $23.40, and restricted stock units in September of 2010 through 2013 at $21.93, $16.29, $19.08, and $24.35. His $53 million in stock-based compensation from these five grants appreciated by about 18% through June 2014. If, instead of exposing shareholders to massive volatility, Chambers had overseen a steady decline from $34.08 to $24.85 during that period, his stock-based compensation would have lost about 20% of its value rather than gaining 18%.

The effect of modern stock-based compensation is to drive volatility, not appreciation. Of course, the providers of capital are constantly pressing executives to deliver better returns. What the executives do in response is fairly simple: They cut back on labor, the variable they can most easily squeeze in order to signal that they are addressing performance. Such creative destruction can be a good thing for the company and the economy—but it can also compromise the company's long-term capabilities. And managers' incentives to create large changes in the market's expectations suggest that cuts in labor are more likely to be overdone than underdone.

Increasingly, therefore, jobs disappear and usually don't return. Consequently, labor's earnings have been suppressed and real wages have stopped growing. This has exacerbated income inequality in America, especially between the very rich and everyone else: The differential between 50th percentile incomes and 90th (or 99th, or 99.9th) percentile incomes has widened dramatically since 1980 and shows no signs of stabilizing, let alone narrowing. Meanwhile, the differential between 10th percentile and 50th percentile incomes has changed very little.

The income gap between creativity-intensive talent and routine-intensive labor is bad for social cohesion. The move from building value to trading value is bad for economic growth and performance. The increased stock market volatility is bad for retirement accounts and pension funds. So although it's great that the proportion of creativity-intensive jobs is now nearly three times what it was a century ago, and terrific that the economy is so richly endowed with talent, that talent is being channeled into unproductive activities and egregious behaviors.

Saving the Talent Economy

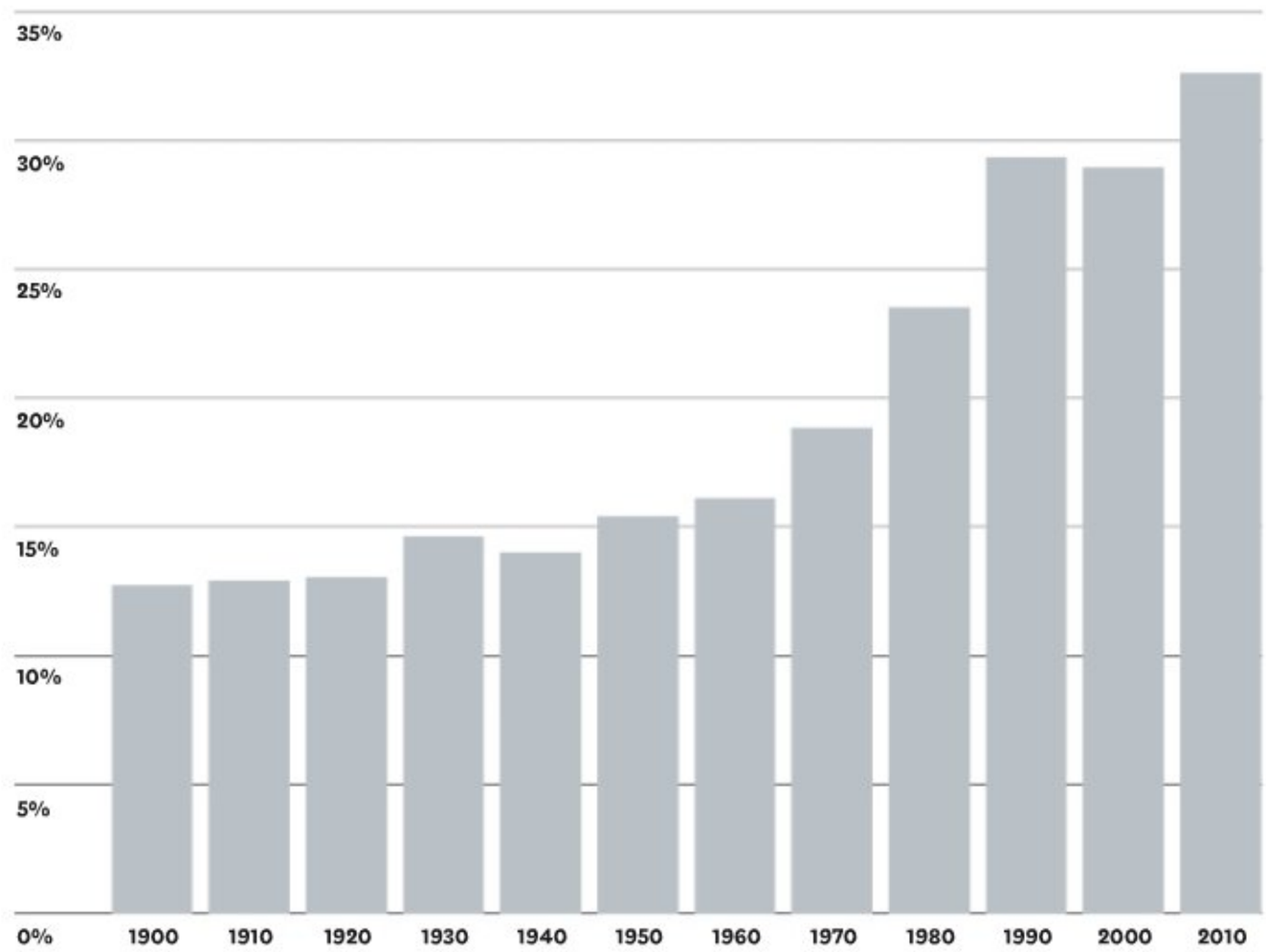
In a democratic capitalist country, it is not sustainable to leave the members of the largest voting bloc out of the economic equation. Think back to 1935, when the United States was still in the throes of the Great Depression. Real incomes were falling, and unemployment hovered around 25%. Employers had put pressure on wages both before the Depression and during it. Labor had no power whatsoever, and efforts to unionize were met with aggressive, even violent, countermeasures.

The Roosevelt administration passed sweeping pro-labor legislation—the National Labor Relations Act—that both facilitated unionization and instituted protections for the rights of unionized workers.

The Rise of the Talent Economy

My colleague Richard Florida at the Martin Prosperity Institute studies the composition of the U.S. workforce by using Department of Labor job classifications and descriptions of job content. These data make it possible to determine the proportion of jobs that are routine-intensive versus creativity-intensive. The fundamental difference is that the latter require independent judgment and decision making. Of course, the actual content of every job in America varies: Some executive assistants file and type, for example, while others are the shadow decision makers for their bosses. But a consistent measure reveals broad patterns over time.

As the chart below shows, from 1900 to 1960 the proportion of creativity-intensive jobs in the U.S. economy was stably low, starting at 13% and growing only to 16%. Today 33% of all jobs are creativity-intensive, a proportion that will continue to increase for the foreseeable future.



It also established the National Labor Relations Board to ensure that corporations adhered strictly to the letter of the act. From 1935 to their historical peak, in 1954, unionization rates rose from 8.5% to 28.3% of U.S. workers, an unimaginably high level by today's standards, and real wages for unionized employees rose faster than both nonunion wages and general economic growth.

Of course, the wages, benefits, and work-rule inflexibility for which labor successfully bargained priced it out of the market after 1960, especially as postwar Europe and Japan recovered. Also, corporations responded to labor's demands by increasing mechanization, moving to "right to work" southern states, and beginning to source internationally. By 2000 unionization was back down close to 1935 levels. But all this rebalancing took time and arguably had a negative impact on overall growth.

It seems clear that the economy is heading toward another 1935 moment. It is hard to see the Occupy Wall Street and We Are the 99 Percent

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demonstrations as anything other than a shot across the bow. Zuccotti Park may have been cleared, but the sentiment hasn't gone away. Unless the key players work together to correct what's causing the current imbalance, the 99% will vote in a rebalancing that is radically in their favor, as they did before. Frankly, it's surprising that they haven't done so already. To avert that, three things have to happen:

Talent must show self-restraint. The new generation of talent does itself few favors in terms of public image. A prime example is Steven A. Cohen—the principal formerly of SAC Capital Advisors (which pled guilty to insider trading and paid a $1.8 billion fine) and now of Point72 Asset Management—who was number two on *Institutional Investor*'s 2013 hedge fund list, with reported personal earnings of $2.4 billion. Not satisfied with the largesse of 2&20, Cohen charged 3% of assets and as much as 50% in carried interest, according to the *New York Times*. Perceived greed of this magnitude will encourage retribution. If top financiers and executives want to avoid that, they need to scale back their financial demands.

One egregious demand the hedge fund and LBO community might reconsider is its insistence on the continued treatment of carried interest as capital gains. Obviously, both asset management fees and carried interest are compensation for professional services rendered. However, the former are taxed as regular income (at a top marginal rate of 39.6%), and the latter is taxed at the preferential capital gains rate (15% from 2003 through 2012; 20% since). In 2008 that preferential rate allowed John Paulson—who famously benefited from the pain and suffering of homeowners as he aggressively shorted the mortgage market—to realize a personal tax saving of as much as $500 million on his $2 billion reported earnings.

From both a tax theory and a public interest standpoint, the favorable capital gains treatment is unjustifiable for hedge funds, because they simply trade existing stocks, creating no net benefit for society. Furthermore, many hedge fund managers are so fiscally aggressive that they negotiate the option of "fee conversion" with their limited partners. That is, they may periodically convert their asset fees to carried interest and thus reduce their taxes. By doing so, they clearly demonstrate that fees and carried interest are interchangeable in their minds—but they continue to insist that the tax authorities treat the two differently.

> It is hard to see the Occupy Wall Street and We Are the 99 Percent demonstrations as anything other than a shot across the bow. Zuccotti Park may have been cleared, but the sentiment hasn't gone away.

Investors must prioritize value creation. Those with by far the greatest opportunity to contribute positively are pension and sovereign wealth funds. As Peter Drucker correctly predicted in 1976, pension funds (and sovereign wealth funds) have become the largest owners of capital in the world. The top 50 pension and sovereign wealth funds combined invest $11.5 trillion. They currently engage in three practices that facilitate abuse by talent:

- *They supply large amounts of capital for hedge funds.* Because pension funds have ongoing obligations, they are hurt by dips in asset price levels. The often-illusory promise of high returns has caused them to channel substantial quantities of capital to hedge funds. The problem, as we've seen, is that hedge funds achieve their returns by encouraging volatility; they can and do profit whether company stocks go up or down. But pensioners want and need steady appreciation.
- *They lend stock.* Pension and sovereign wealth funds are the world's leading lenders of stock, and short-selling hedge funds are its leading borrowers. Every pension fund makes a small contribution to its annual returns through the fees it earns from lending stock, and the amount each one lends has an imperceptible impact on the market. Their lending facilitates approximately $2 trillion worth of short selling on a perpetual basis. The continual placing and unwinding of these short positions generates volatility that is great for hedge fund financial engineers but bad for the pensioners whose funds they use.
- *They support stock-based compensation.* The funds usually vote in favor of stock-based compensation for executives of the publicly traded companies

in which they invest, believing that it benefits the pensioners and citizens they serve. But if anything, broad returns on public equities have gone down while volatility has increased as stock-based compensation has increased. Thus these funds—the longest-term investors in the world—are voting against their own interests.

Even though the imbalance in favor of talent is greatest in the United States, all democratic capitalism is heading in the same direction, so a U.S. effort alone would be ineffective in correcting it. Although the notion of global collaboration might seem unrealistic, just 35 funds from 15 countries could put $10 trillion in assets behind this goal. And if those leading funds stopped funneling capital to hedge funds, lending stock, and supporting stock-based compensation, it would be hard for smaller funds to justify not following suit.

The government should intervene early. Governmental regulation to rein in the excessive appropriation of value by the top 1% is preferable to a radically anti-talent agenda that could seriously compromise America's entrepreneurial capabilities. The U.S. government's late and aggressive intervention in 1935 arguably ended up hurting labor, the constituency it aimed to rescue, more than helping it. Four actions might avert a repeat of that phenomenon:

- *Regulate the relationship between hedge funds and pension funds.* Individuals who own shares should be perfectly free to lend them to whomever they wish. However, stock lending by fiduciary institutions should be banned if pension funds don't voluntarily cease the practice. And if they don't reduce their investment in hedge funds, governments could ameliorate the effects of hedge fund behavior by banning the collection of both an asset management fee *and* carried interest. For even a small hedge fund of $1 billion, the asset management fee over the five-year life of the fund is $100 million—enough to make the fund's principals rich. With that certainty, they can take huge risks on their investments in order to win the proverbial lottery on their carried interest. Permitting only an asset management fee would discourage volatility-producing behavior, and permitting only a carried interest fee would discourage excessive risk taking. Allowing the use of one or the other while banning the use of the two in combination would be dramatically better for society than the current structure.
- *Tax carried interest as ordinary income.* This would promote tax fairness—hedge fund billionaires would no longer pay lower average income tax rates than ordinary laborers—and would reap additional billions for the Treasury.
- *Tax trades.* Government should impose on trades something like the proposed Tobin tax on international financial transactions. Anything that discourages high-frequency trading strategies is an unalloyed good.
- *Revisit the overall tax structure.* Since 1982 the U.S. taxation strategy has been unique in the developed world, and not in a good way: It features a very low personal income tax, a very high corporate income tax, and no national value-added tax (the most economically effective form of taxation in the world). Just when capital required help in battling talent, which had started earning outsize returns, the tax system flipped to side entirely with talent. Capital needs an incentive to invest in creating more jobs, and the incentive for U.S. companies is low by global standards. It is no surprise that, rather than investing, they have been accumulating record levels of cash on their balance sheets, lots of it offshore. Furthermore, no evidence suggests that this tax regime has benefited the U.S. economy, though it has clearly contributed to the dramatic rise in income inequality.

Unfortunately, political gridlock in the United States makes it unlikely that government can implement such reforms. The Republican Party seems foursquare behind hedge funds, which it sees as embodying capital—even though hedge fund managers are in fact talent, a breakaway branch of labor (their overcharged customers are the real representatives of capital). The Democratic Party, traditionally supportive of organized labor, has increasingly transferred its allegiance to capital, largely because pension funds have become the most important form of capital and their beneficiaries represent the traditional Democratic power base. Neither party represents labor directly.

ROBERTO GOIZUETA lived to see and benefited from talent's rise to become the key asset in the modern economy. But he died before the positive aspects of this phenomenon began to give way to its dark side. The trend cannot proceed unabated in the United States without provoking a political reaction. Top executives, private equity managers, and pension funds can avoid such a reaction by showing the leadership of which they are fully capable and modifying their behavior to create a better mix of rewards for capital, labor, and talent.

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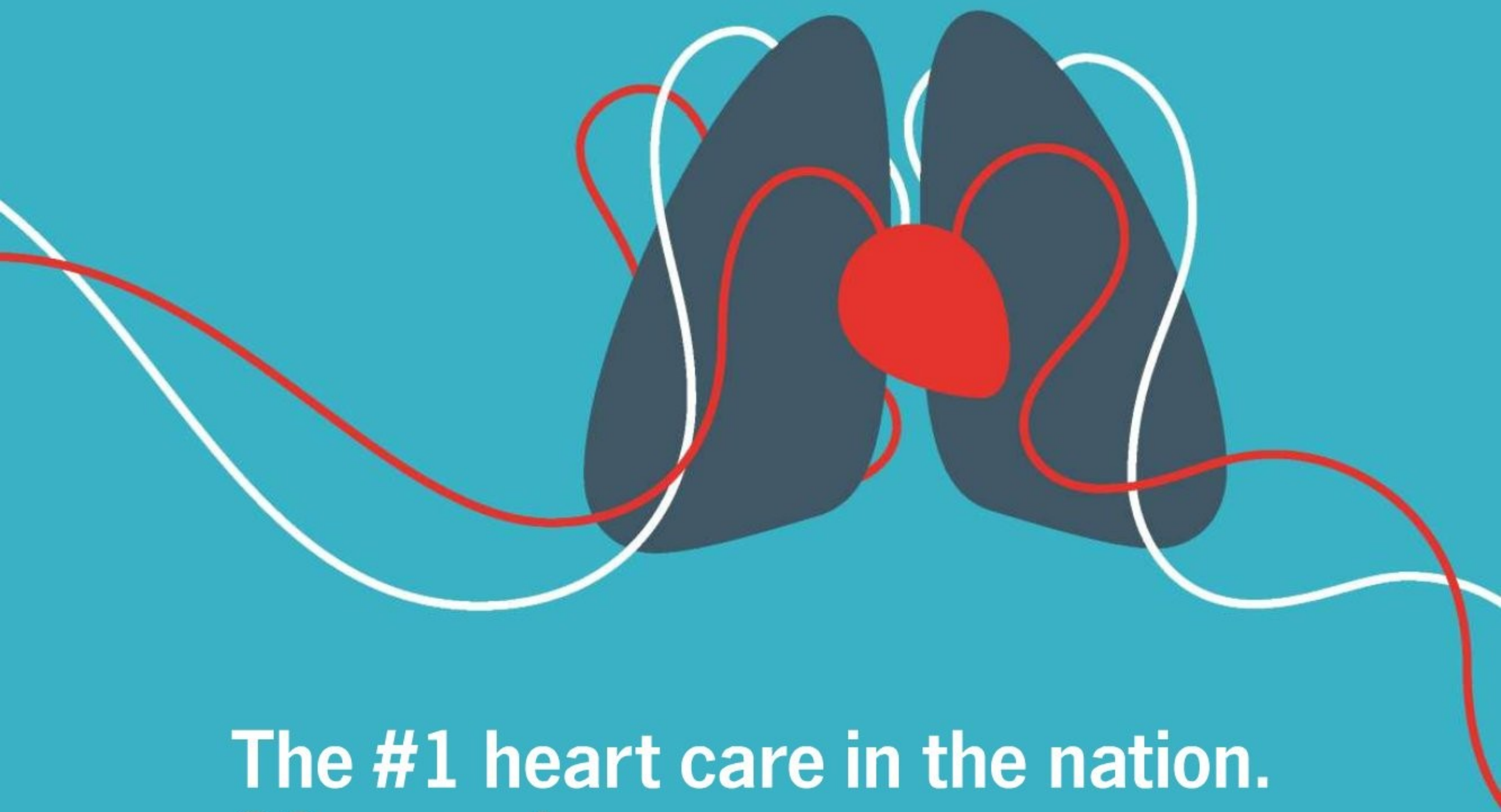

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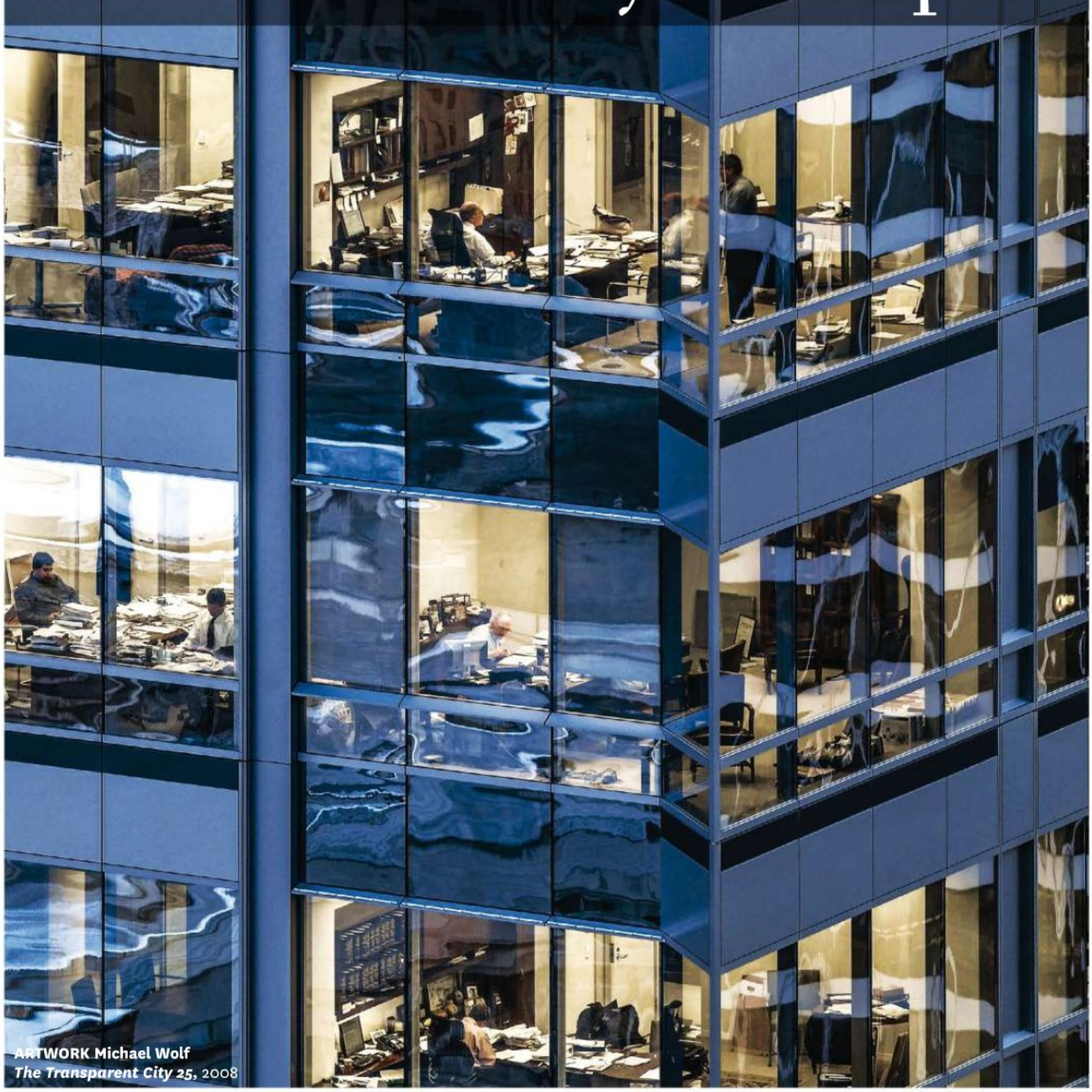

ARTWORK Michael Wolf
The Transparent City 25, 2008

Spotlight

ARTWORK Michael Wolf
The Transparent City 11, 2008

Balancing "We" and "Me"

The best collaborative spaces also support solitude.

by Christine Congdon, Donna Flynn, and Melanie Redman

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THE OPEN OFFICE

has a lot of critics these days. But it remains the dominant form of workplace design for a reason: It can foster collaboration, promote learning, and nurture a strong culture. It's the right idea; unfortunately, it's often poorly executed—even as a way to support collaboration.

There's a natural rhythm to collaboration. People need to focus alone or in pairs to generate ideas or process information; then they come together as a group to build on those ideas or develop a shared point of view; and then they break apart again to take next steps. The more demanding the collaboration task is, the more individuals need punctuating moments of private time to think or recharge.

Companies have been trying for decades to find the balance between public and private workspace that best supports collaboration. In 1980 our research found that 85% of U.S. employees said they needed places to concentrate without distractions, and 52% said they lacked such spaces. In response, thousands of high-walled cubicles took over the corporate landscape. By the late 1990s, the tide had turned, and only 23% of employees wanted more privacy; 50% said they needed more access to other people, and 40% wanted more interaction. Organizations responded by shifting their real estate allocation toward open spaces that support collaboration and shrinking areas for individual work. But the pendulum may have swung too far: Our research now suggests that once again, people feel a pressing need for more privacy, not only to do heads-down work but to cope with the intensity of how work happens today.

The open plan is just one of the culprits assaulting our privacy. The increased focus on collaborative work means we're rarely alone, and the ubiquity of mobile devices means we're always accessible. In light of these pressures, it's not surprising that the number of people who say they can't concentrate at their desk has increased by 16% since 2008, and the number of those who don't have access to quiet places to do focused work is up by 13%. Meanwhile, people are finding it harder to control who has access to their personal information, at work and elsewhere. In fact, 74% of the people we surveyed said they're more concerned about their privacy now than they were 10 years ago.

Leaving the office to work at home or in coffee shops or libraries isn't the answer—at least not for the long term. Too much remote work creates its own set of problems, such as diminished knowledge transfer, decreased engagement, cultural disconnect, and a slew of new distractions. And, of course, it makes collaboration more difficult.

Steelcase has been exploring the issue of privacy since the 1980s, and over the years we've worked with thousands of organizations in many industries to develop open office environments. Recently we conducted a study of workplaces and workers in Europe, North America, and Asia, using surveys, ethnographic research, observations, and interviews to update our understanding. Here we present new insights into the nature of privacy and offer strategies that allow employees to get away without going away.

Redefining Privacy at Work

Researchers—and architects—have traditionally defined privacy at work in physical terms: acoustical (Can we hear each other?), visual (Can we see each other?), and territorial (Do I have a place that's just for me?). But in today's workplace, we're always connected, always reachable, and to some extent always findable, in both the physical and the virtual sense. That accessibility can enhance our interactions but can also leave us feeling overexposed.

So we need to rethink our basic assumptions about privacy. At Steelcase, we believe that privacy has two distinct dimensions.

Information control. Employees today wage a constant battle to protect and manage access to their personal information. Over the course of a day, we shift constantly between revealing and concealing aspects of ourselves and our work to and from others: Who needs access to these project files? How can I keep coworkers from seeing sensitive information on my computer screen? Where can I have a confidential conversation without being overheard? Can I read an article or check my Twitter feed at my desk without fear that people will think I'm slacking?

Technology has further challenged our sense of personal sovereignty. Social media in particular have done more than any other force to compromise our ability to control our information. Facebook, for example, allows us to curate what we share about ourselves—but only up to a point. Even those who opt

About the Spotlight Artist

Each month we illustrate our Spotlight package with a series of works from an accomplished artist. The lively and cerebral creations of these photographers, painters, and installation artists are meant to infuse our pages with additional energy and intelligence to amplify what are often complex and abstract concepts.

This month we feature the work of **Michael Wolf,** a German-born photographer living in Hong Kong. Wolf's pictures examine city architecture, documenting the density and disconnection of urban life. See more of his work at **photomichaelwolf.com**.

Idea in Brief

THE CHALLENGE
Open offices are supposed to promote collaboration, but people just don't like them much. Companies have been trying for decades to find the balance between public and private workspace that best supports collaboration.

THE FINDING
Privacy has traditionally been defined in physical terms, but we need to think about it differently. Privacy is really about the individual's ability to control *information* (what information others need to know, both personal and professional) and *stimulation* (any sort of disruption).

THE SOLUTION
Privacy does not compromise collaboration but can nurture it. By improving privacy—providing spaces where employees can be by themselves and tune out distractions—you enrich and strengthen collaborative activities.

out of popular social media sites have a hard time hiding from Google. What if we really don't want coworkers to know where we live, what religion we practice, what music we listen to, or how old we are? We have to make conscious decisions about how we manage our personal information and act on those decisions vigilantly. If we don't—and most of us don't—then we're left feeling uncomfortably vulnerable.

Stimulation control. The second dimension of privacy encompasses the noises and other distractions that break concentration or inhibit the ability to focus. Stimulation control is in some ways more variable and idiosyncratic than information control. One person's distraction may be another's comforting white noise. And on any given day, our notion of distraction can change. Sometimes we might find background music soothing; other times it might be annoying. However we define them, we all need ways to manage distractions.

Fundamentally, stimulation control governs the ability to focus attention. In thinking about office design, it's helpful to understand that neuroscience research identifies three basic modes of attention. The first is *controlled attention*: working on a task that requires intense focus, such as writing or thinking deeply, while willfully avoiding unrelated thoughts and inhibiting external stimuli. When we are in this mode, interruptions and other distractions are unwelcome, and our need to control the environment around us increases.

The second mode is *stimulus-driven attention*: switching focus when something catches our attention. When we're performing routine tasks—responding to e-mails, scheduling meetings, or catching up on other administrative work—we may tolerate or even welcome interruptions or distractions. Many people choose to perform routine tasks in open, social, or active settings.

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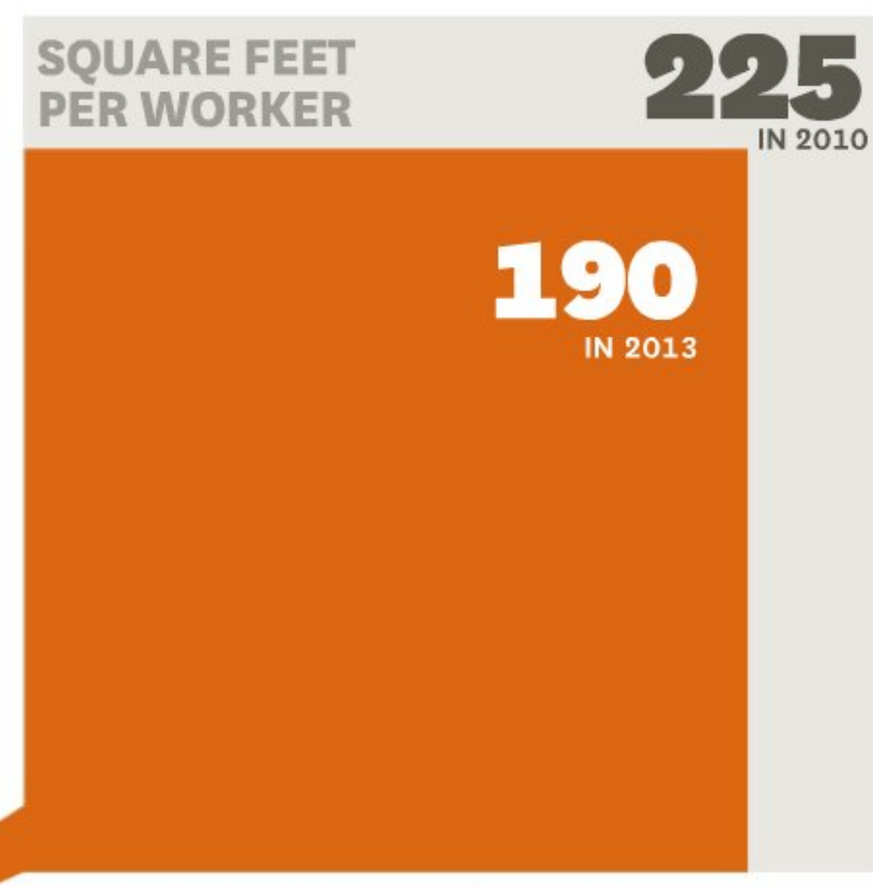
INSIDE THE U.S. WORKPLACE

Today more than **70%** of employees work in an open office environment, and the size of their individual workspaces is shrinking.



SOURCE INTERNATIONAL FACILITY MANAGEMENT ASSOCIATION AND CORENET GLOBAL

HBR.ORG For a look at workplace dynamics around the world, visit Christine Congdon's article "How Culture Shapes the Office" (HBR May 2013).

We call the third mode *rejuvenation*—the periodic respites from concentration that we take throughout the day. It's a time-out for our brains and bodies and often a chance to engage socially with others or express emotions that we've kept on a tight leash. For rejuvenation, people may seek either a highly stimulating environment or a quiet one, depending on personal preference.

The need to control stimulation as we switch among the three modes means that we require a variety of workspaces that afford more or less privacy. The challenge is to find the right balance of social and private and to provide spaces that enhance all three modes.

Privacy Across Cultures

While the need for privacy is universal, the ways it is experienced across cultures vary. To better understand the similarities and differences around the world, Steelcase partnered with the global research firm Ipsos to conduct surveys in 14 countries; we then synthesized the data with our ongoing ethnographic research. Most findings were consistent with earlier research, but a few surprised us.

Attitudes toward personal space differ greatly from country to country. Germans allocate an average of 320 square feet per employee; Americans, an average of 190. For workers in India and China, the figures are 70 and 50 square feet respectively. Yet despite their relatively dense workspaces, both Indian and Chinese workers rated their work environments highly in terms of their ability to concentrate and work without disruption.

That finding points to a significant cultural difference. In China people don't think about individual privacy in the same way that Westerners do. Chinese workers are most concerned about information control: keeping personal data private and seeking refuge from the feeling of being watched. Thus, in China, where offices are organized so that managers can easily keep tabs on workers, people tend to duck into hallways or bathrooms for a moment alone. Offices that allow workers to have their backs to the wall are considered prime real estate. In India it's not uncommon for workers to seek out pockets of privacy—in unoccupied nooks on the periphery of workspaces, in storage areas, or along walls.

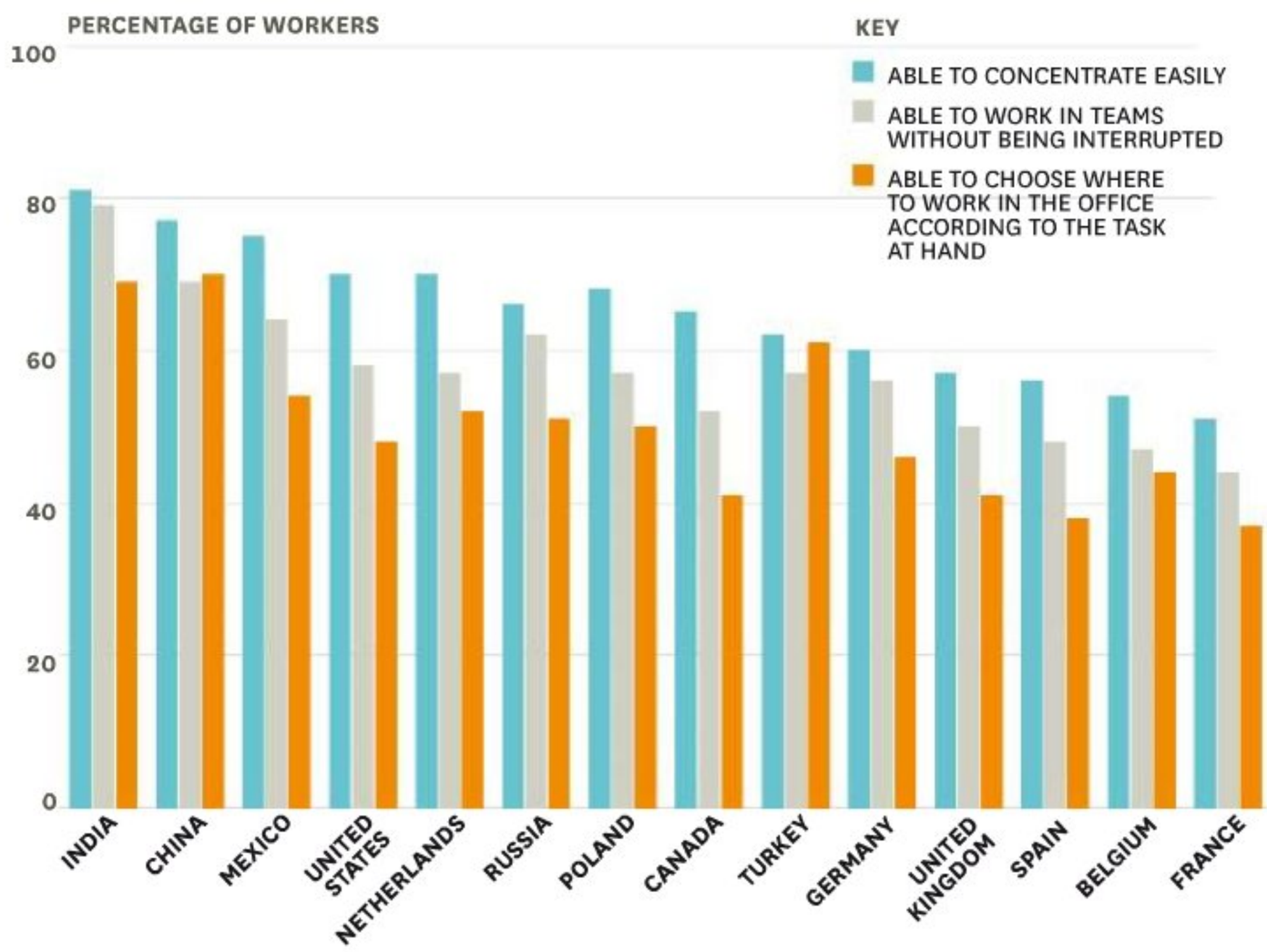
Among Western workers, by contrast, the issue of stimulation control tends to take center stage: Only 55% of the workers we surveyed said they are able to work in groups without being interrupted. Less than half say they can choose where they want to work within the office on the basis of the task at hand. In our research, the adjective Americans used most frequently to describe their workplaces was "stressful." The adjective Chinese workers used most was "calming." (Then again, it's perfectly acceptable in China to take a nap at work.)

When it comes to heads-down focus, however, American workers give their office environments relatively high marks, despite the vocal complaints heard in social media and other forums. A surprising 70% of workers in the United States say their workplace provides the ability to concentrate easily. Because cubicles still dominate the North American office landscape, and more real estate is allocated for individual workspaces than for collaboration activities, we believe that the reported frustrations are quite likely being exacerbated by factors other than the physical environment—such as the intense pace of work.

Overall, workers in European countries (except in the Netherlands) were the most dissatisfied with

HOW EMPLOYEES FEEL ABOUT THE WORKPLACE

We surveyed employees around the world on three dimensions of privacy critical to workplace satisfaction. Surprisingly, Indian and Chinese workers, who have significantly smaller individual spaces and denser office environments, ranked highest.



their ability to control their privacy and were more likely to be dissatisfied with their work environment in general. Of the workers in our survey who ranked as the most highly dissatisfied and disengaged, 53% came from France, Germany, Spain, and Belgium. The cultural norm in those countries is that work happens in the office, generally at an assigned workspace, and opportunities to seek solitude or achieve greater levels of privacy are often limited. In the Netherlands, by contrast, there's greater comfort with letting people work from a diverse range of spaces, inside and outside the office. Moreover, the Dutch are more egalitarian than their neighbors when it comes to office design. Privacy considerations are not based on status, and leaders work alongside employees of all levels in open spaces. This might explain why the Dutch accounted for almost half of satisfied and engaged employees. (For a country-by-country comparison, see the exhibit "How Employees Feel About the Workplace.")

While privacy means different things in different cultures, our study showed that workplace satisfaction and engagement are deeply connected to a sense of control over one's environment. In our study, 98% of the most highly engaged employees reported that they had "the ability to concentrate easily" in their workplace and that this attribute is a top factor in their satisfaction. They also scored high on "being able to work in teams without being disrupted" and "being able to choose where to work according to the task at hand"—other factors critical to high engagement and satisfaction. Conversely, highly disengaged and dissatisfied employees struggled with disruptions and felt they had very little control over where or how they worked. Only 15% said they could concentrate easily.

Personal Strategies for Privacy

In addition to local culture, factors such as organizational culture, the type of task one is engaged in, mood, and individual personality shape how much privacy people require and the way they achieve it. For example, introverts tend to gravitate toward places where they feel that they have the most control over stimulation. Susan Cain's recent study of introverts argues that they are not shy; rather, they are more sensitive to stimuli than extroverts are. Our research pointed to five privacy strategies that people use, sometimes unconsciously, to control both stimulation and information.

REDEFINING PRIVACY

The ubiquity of electronic devices and connectivity means that privacy in the workplace can no longer be thought of strictly in physical terms. Today privacy is about employees' need to control *information* and *stimulation* in three key realms.

	Outgoing INFORMATION	Incoming STIMULATION
SOCIAL	How much do I want colleagues to know about my personal interests? Should I connect with colleagues on social media?	How can I limit interruptions by coworkers? How can I avoid constant exposure to the noise and activity of others?
TECHNOLOGICAL	Can I opt out of giving biometric data used for security purposes? Can I shield my name from feedback to superiors?	Do I want pop-up previews of incoming e-mails? I need to focus: Is it OK to turn off instant messaging?
SPATIAL	Can people see my computer screen while I'm working? What personal photos or artifacts do I want to display?	What space configuration minimizes my exposure to flickering fluorescent lights? How can I block out my neighbor's phone conversations?

Strategic anonymity. Some of us find deep privacy in the middle of a crowd of strangers. When people go to a café to do focused work, they are often trying to inhibit the social distractions they face in their workplace. Recent research by Ravi Mehta, Rui Zhu, and Amar Cheema in the *Journal of Consumer Research* shows that working in an environment with a moderate level of ambient background noise can enhance performance on creative tasks. Many people enjoy the hum of activity in cafés or airports, where they can work, read, or relax without disruption. The key is that it's strategic: Individuals choose when and how to make themselves anonymous.

Selective exposure. In today's world, where our personal information is being shared and demanded across new channels in exponentially higher degrees, the boundaries between what is and isn't private are constantly shifting. People choose to

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reveal some information to certain people or groups, while sharing different information with others. In the physical sense, this may mean choosing whether to share a particular document with a coworker or deciding what personal artifacts to display at work. It could also be about making a decision to use the phone instead of video chat if we don't want others to be able to see us.

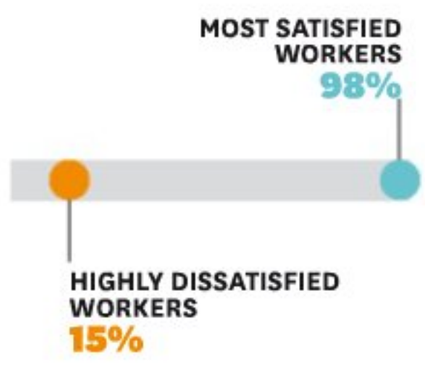
Entrusted confidence. Privacy doesn't just mean being alone. There are many contexts in the workplace where groups of individuals need to have private conversations. Some moments of entrusted confidence, such as performance reviews, may be scheduled and planned. More often, they happen spontaneously, such as when colleagues need to discuss a sensitive problem that has cropped up; and at these times it can be difficult to find an available conference room. In workplaces that are highly open, we see greater demand for dedicated conference or project rooms that teams or individuals can easily access, where they feel secure sharing confidences.

Intentional shielding. People talk about feeling "violated" when they think they're being watched or eavesdropped on. They use a variety of shielding tactics to protect themselves. We often see people go to an enclosed location to take a call, or walk in public areas where they are less likely to be overheard. Many people avoid working in spaces where they can't see coworkers approaching. Others engage in intentional shielding by keeping their own counsel, protecting their individual thoughts and ideas so that they can develop a point of view without the distracting influence of "groupthink" or peer pressure.

Purposeful solitude. Isolation is largely a matter of circumstance and state of mind: Your physical location, your habits, and your attitudes can all conspire to make you feel isolated from a group. But solitude is intentional; you make a conscious choice to separate from a group in order to concentrate, recharge, express emotion, or engage in personal activities. Some people may choose a closed space where they have visual and acoustical privacy if they need respite or to focus intently on a project. Others may choose to eat lunch in the farthest empty corner of a cafeteria. Stepping outside to sit in a quiet courtyard and taking a short walk are other ways people seek alone time.

MANAGE DISTRACTION

% of respondents who agree that their work environment allows them to concentrate easily



TAKE A BREAK

% of respondents who agree that they can socialize and have informal, relaxed conversations with their colleagues

Organizational Strategies for Privacy

As organizations come to understand the need for privacy at work, they must also recognize that privacy does not compromise collaboration. By improving privacy you can actually enrich and strengthen collaborative activities.

Organizations have a range of strategies they can implement, but the success of any of them depends on a supporting culture that gives employees control over where and how they work and how they manage their privacy. Cultures are built and reinforced when people exhibit certain behaviors over time and those behaviors are articulated, adopted, and embraced across the organization. Leaders who model the desired behaviors give implicit permission to others to follow suit and send the message "This is how we work here."

Some strategies demand an investment in new kinds of space, but others require only modest reconfigurations along with behavioral and cultural changes. Here are four effective options:

Protocols. Organizations can lay down rules that define acceptable behaviors about privacy. Protocols can be companywide or specific to certain departments, times, or places. For example, an organization might choose to designate a particular time for quiet work in one or multiple locations. Or it might decide that music or videos should be a headphones-only experience. Leaders should communicate the protocols clearly and explain the rationales behind them. Many workplace protocols have gone by the wayside when people don't understand them or forget what type of behavior is appropriate. To sustain the adoption of these practices,

Employees can use a host of props or devices to establish boundaries, but gadgets won't work unless they're backed up by a culture that respects the need for privacy.

encourage supportive but honest conversations when protocols are broken and clearly communicate the consequences for repeat offenses.

Signaling. Signals are similar to protocols, but rather than being established by the organization, they are adopted by employees themselves to communicate their privacy requirements to others. In many offices earbuds are an accepted way of signaling "do not disturb"; some people wear noise-canceling headphones to make their point even more obvious. People can also signal a desire for privacy by how they orient themselves in a room: Facing others encourages interaction; tucking behind a screen or a large plant says "I'm trying to be alone."

Employees can find a host of props or devices to help them establish privacy boundaries with their coworkers. But even the most sophisticated gadget won't work unless it's backed up by a culture that respects the individual's need for privacy. Leaders should make it clear that employees must respect privacy signals in open spaces and support individuals' efforts to control their information and stimulation.

Strategic space planning. There are two primary design approaches for accommodating privacy needs in the physical workspace: the distributed model and the zone model. In the distributed model, spaces that support stimulation control are blended into areas for both individual and group work. This model makes it easy for people to shift quickly between modes of work. For instance, a worker may need to focus deeply while preparing for a meeting, move to a nearby project room to collaborate, and afterward break away with one other person to concentrate on a task. Physical proximity of these spaces facilitates quick switching between work modes.

The zone model defines certain locations within the larger workplace as private, quiet spaces. Organizations may designate a particular area or even an entire floor or building as a sort of "library" or quiet hub. In this model, the private zones are physically separate from open areas. This approach can be especially useful in managing noise disruptions.

An ecosystem of spaces. Our studies show that the most successful work environments provide a range of spaces—an ecosystem—that allow people to choose where and how they get their jobs done.

In some situations, individuals need their own enclosed space for regular use. But design and allocation of such space needs to shift from being hierarchy-based to being needs-based. For example, many executives are granted spacious, enclosed offices that often sit empty because of travel or meeting schedules. These could be redesigned to allow other people to use them productively when their primary users are off-site. Like others in the organization, many leaders simply need access to an enclosed space for certain tasks when they are on-site.

Whether owned or shared, enclosed spaces are more effective when they allow users to control stimulation. Sound, for instance, travels like water, seeping through partitions and gaps in walls and ceilings. Enclosed spaces make it easier to avoid overhearing conversations that everyone prefers to keep private. Such spaces should also take into account visual distractions. The trend toward greater transparency has led to more glass walls, especially in spaces that are situated near windows, but they can lead to the unpleasant feeling of "working in a fishbowl." A simple band of frosted glass does a great deal to reinforce the privacy of such areas.

"Shielded" spaces can also be used to provide sufficient privacy for many tasks. These areas are generally semi-enclosed, made with partial-height walls or portable screens. When combined with appropriate protocols, the boundaries signal "Do not disturb." They are particularly effective when placed in quiet zones. They're also a low-cost solution: In one of our spaces, designers used everyday objects such as books and plants and simple configurations of the furnishings to discourage conversations. Without any explicit communication, the space clearly told people that it was intended for individual, quiet work.

OPEN OFFICES are not inherently good or bad. The key to successful workspaces is to empower individuals by giving them choices that allow control over their work environment. When they can choose where and how they work, they have more capacity to draw energy and ideas from others and be re-energized by moments of solitude. Providing the ability to move easily between group time and individual private time creates a rhythm—coming together to think about a problem and then going away to let ideas gestate—that is essential to the modern organization.

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WORK WHERE YOU WANT

% of respondents who agree that they can choose where they wish to work within the office according to the task at hand

AVOID INTERRUPTIONS

% of respondents who agree that they can work in teams without being disrupted

SOURCE 2014 WELL-BEING IN THE OFFICE STUDY, STEELCASE AND IPSOS

Spotlight

ARTWORK Michael Wolf
Transparent City 75, 2008

The Transparency Trap

Too much openness can be counterproductive. Privacy is just as important to performance.

by Ethan Bernstein

Ethan Bernstein is an assistant professor of business administration in the organizational behavior unit at Harvard Business School and the author of "The Transparency Paradox" (*Administrative Science Quarterly*, June 2012). Twitter: @ethanbernstein

"TRANSPARENCY"

is a watchword in management these days, and it's easy to understand why. After all, if people conduct their work in plain view, won't they be more open and accountable? Won't they flag and fix problems more easily, and share information and their good ideas more freely?

That's certainly what I expected to discover a few years ago, when I went in search of empirical evidence that transparency improves performance in organizations. But through rigorous field research and experiments, and observations by embedded researchers, I learned that it's not that simple. My findings, which complement various studies on open workspaces (see "Balancing 'We' and 'Me'" in this issue), suggest that more-transparent environments are not always better. *Privacy* is just as essential for performance.

Here's the paradox: For all that transparency does to drive out wasteful practices and promote collaboration and shared learning, too much of it can trigger distortions of fact and counterproductive inhibitions. Unrehearsed, experimental behaviors sometimes cease altogether. Wide-open workspaces and copious real-time data on how individuals spend their time can leave employees feeling exposed and vulnerable. Being observed changes their conduct. They start going to great lengths to keep what they're doing under wraps, even if they have nothing bad to hide. If executives pick up on signs of covert activity, they instinctively start to monitor employee behavior even more intensely. And that just aggravates the problem.

If all this seems vaguely Orwellian, so did some of the activities I saw in leading companies where intense visibility and tracking were making things worse, not better. For instance, at one of the world's largest mobile phone factories, which is in China and is owned by a global contract manufacturer, the workers on one line were hiding process *improvements* they had made—not just from managers but from their peers on other lines. Why? Because, as one experienced worker explained, "it's most efficient to hide it now and discuss it later. Everyone is happy: They see what they expect to see, and we meet our targets."

This was not an isolated example. In my research, I found that individuals and groups routinely wasted significant resources in an effort to conceal beneficial activities, because they believed that bosses, peers, and external observers who might see them would have "no idea" how to "properly understand" them. Even when everyone involved had only the best of intentions, being observed distorted behavior instead of improving it.

Some organizations, however, had found the sweet spot between privacy and transparency, getting the benefits of both. They used four types of boundaries to establish certain zones of privacy within open environments: They created boundaries around individual teams—zones of attention—to avoid exposing every little action to the scrutiny of a crowd. They drew boundaries between feedback and evaluation—delineating zones of judgment—to avoid politicking and efforts wasted on managing impressions. They set boundaries between decision rights and improvement rights—establishing zones of slack—to avoid driving out tinkering. And they put boundaries around carefully defined periods of experimentation—zones of time—to avoid both too frequent and too infrequent interruptions. Across several studies involving different industries, cultures, and types of work, the companies that had done all this were the ones that consistently got the most innovative, productive, and thoughtful work from their employees.

Type 1 Boundaries Around Teams

As social media platforms, wearable devices, and other tools for transparency become more advanced, our sense of being "onstage" is growing. And so, in keeping with the sociologist Erving Goffman's insights about interpersonal behavior, we spend more time *acting*, trying to control others' impressions and avoid embarrassment—particularly at work. We cater to our audience, doing what's expected.

That was the case at the Chinese mobile phone factory, which had 14,000 workers. When I began studying that work environment, it seemed like the epitome of transparency: Each floor—roughly the size of a football field, with no walls or other divisions—held as many as 2,000 workers across shifts.

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Idea in Brief

PROBLEM
To get people to be more creative and productive, managers increase transparency with open workspaces and access to real-time data. But too much transparency can leave employees feeling exposed. As a result, they may actively conceal what they're doing—even when making improvements—reducing productivity and, paradoxically, transparency.

SOLUTION
Employees perform better when they can try out new ideas and approaches within certain zones of privacy. Organizations allow them to do that by drawing four types of boundaries: around teams of people (zones of attention), between feedback and evaluation (zones of judgment), between decision rights and improvement rights (zones of slack), and for set periods of experimentation (zones of time).

BENEFIT
Less-transparent work environments can yield more-transparent employees. And by balancing transparency and privacy, organizations can encourage just the right amount of "deviance" to foster innovative behavior and boost productivity.

By embedding into the lines five Chinese-born Harvard undergraduate researchers—who worked, ate, and lived alongside the employees, who knew them only as coworkers—I quickly learned that the production teams hid a great deal from observers, despite the open environment. For example, to speed up assembly, workers scanned multiple bar codes into the system at once instead of scanning each one individually after applying it to a metal shield in a phone, as standard operating procedure required. And team members cross-trained on tasks during downtime—it looked like fooling around from the outside—so they could cover for one another when an operator fell behind. There was no ill intent—only a rational calculation about how to be most productive without having to waste time on explanations.

Such subterfuge is problematic for a host of reasons, though, ranging from increased risk of compliance-related defects to a lack of shared learning. To test some basic interventions that might address it, I set up a few field experiments. On one floor, where 32 production lines made similar mobile data cards, I randomly selected four lines on which to experiment, leaving 28 "controls" to work as they always had.

Because one of the experimental lines was very close to a control line, engineering put up a curtain between the two. When it was raised, one of the embedded students overheard a worker say, "Wouldn't it be nice if they hung up curtains all around the line, so we could be completely closed off? We could be so much more productive if they did that." Curious to see if that would be true, I asked engineering to fully encircle each experimental line with the equivalent of a hospital bed curtain. Over the next five months, to my surprise, the lines with curtains were 10% to 15% more productive than the rest, even when I controlled for other influences (such as the Hawthorne effect, whereby subjects improve simply in response to being studied).

By shielding employees from observation, the curtains supported local problem solving, experimentation, and focus. But within the curtains work became much more transparent. Partly for that reason, defects remained extremely low, even as

SELECTIVE SCREENING
When curtains went up around manufacturing lines at a Chinese factory, so did productivity. Lines that were enclosed in this fashion generated 10% to 15% more throughput than lines left out in the open. Within the curtains, transparency, experimentation, and camaraderie all rose.

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throughput rose. And over time the camaraderie within boundaries made the workers more likely to share—as a group—their privately worked-out solutions with other lines.

Traditionally, people in organizations expect full transparency within teams but not necessarily beyond them. Team boundaries can allow for productive, selective opacities within starkly transparent environments—as was clear at Valve Software, a top PC game developer I studied with Francesca Gino and Bradley Staats. Valve's 400-plus employees are allowed to allocate 100% of their time to projects they feel are valuable to customers. When they collaborate on new products or features, they form teams called cabals and move their desks (which are set on wheels) together into clusters. The office layout is so fluid, with some individuals rolling their desks to different cabals multiple times a week, that Valve even has an internal application to track desk location.

We've seen it happen with curtains, counters, and cabals: Even nominal team boundaries relieve the pressure of being onstage by keeping the audience small.

Valve's cabals choose their own workspaces, creating privacy by positioning themselves at a distance from others. Though transparency is high within them, it's moderate at best across the company because of the physical separation and Valve's distaste for managerial oversight. (No one has the role of keeping tabs on the cabals or shuttling information back and forth.) This gives the cabals more freedom to investigate ideas.

When one employee started a cabal to explore how Valve could get into hardware, the team was initially tiny. Had it immediately tried to rally the support of the entire organization of software engineers, the hardware concept might have been dead on arrival—it's hard to persuade lots of people at once to embrace anything new, even at Valve. But acquiring a few followers with whom to experiment and create prototypes was doable. Gradually, the hardware cabal accreted people and resources, gaining scale and momentum. To recruit more people to join it, early members eventually had to tell others what they were up to. In other words, they increased their transparency outside the group—but in their own way and when they were ready.

Is Valve providing an innovative, productive work environment? Its success suggests that it is. In its 18-year existence, Valve has produced a large share of top PC games. According to its founder, Valve has grown sales by more than 50% every year and brought in more revenue per employee than Apple or Microsoft. Its game platform consumes more bandwidth than most countries do. The cabals help the company compete in a market where creativity and rapid prototype and launch capabilities are critical.

Though Valve is an extreme case (and its success is a product of many factors), other firms are similarly fostering innovation and productivity by allowing privacy within team boundaries. For instance, Google doesn't track when and where its engineers spend the 20% of their time that they devote to projects that interest them personally—but they feel transparently accountable to others *within* the self-organized teams in which the work gets done. And that protected 20% time has been credited with the incubation of more than half of Google's current product portfolio, including Gmail, AdSense, Google Talk, Google News, Google Transit, Google Now, and the Google Transparency Report.

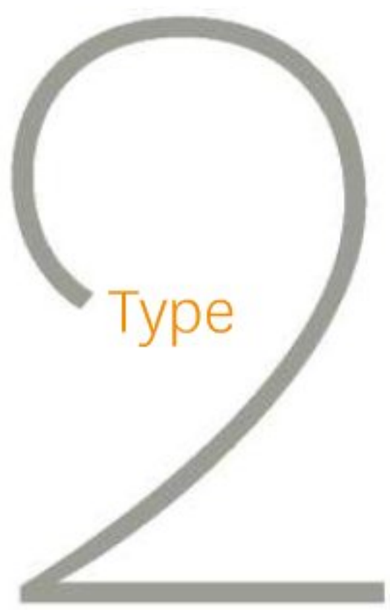
Team boundaries have a big impact on performance for service providers as well. In a recent Harvard Business School study, Melissa Valentine and Amy Edmondson show how such boundaries (in their case, counters delimiting small and very fluid groupings of nurses and physicians) improved teamwork and efficiency in a hospital's emergency department. Transparency and accountability among people working within the boundaries increased. As a result, average patient time in the department fell by more than 40%, with no decrease in quality. Remarkably, the department sustained that improvement for over a year (the length of the study) even though its daily patient volume rose by more than 25%.

Although tools for observation (see the sidebar "Tracking Every Move") and collaboration have become more powerful, making it easier for individuals to do much of their work without formal teams to support them, teams are actually proliferating rather than dying off. Longitudinal surveys show that today nearly all *Fortune* 1000 firms have formal team structures, compared with fewer than 20% in 1980.

FEEDBACK WITHOUT FEAR

At one trucking company, video cameras show drivers (but not their managers) how they can improve.

Though a number of factors are driving that trend, my research suggests it has something to do with the value of boundaries. Workers today can tackle problems in cooperation with large networks—and even crowds—of people, but as teams scholar Richard Hackman demonstrated, they frequently do it better on clearly bounded teams. Boundaries create a focus on "us" and "our work together," liberated from external noise, whether it's unproductive interference or chaotic workflow. No matter what the work is, some observers will increase productivity, but others will undermine it. Whether boundaries are spatial or psychological, they can limit observation to a zone of people. It happens with curtains, cabals, counters—even nominal team boundaries mitigate the pressures of being onstage by keeping the audience small.



Boundaries Between Feedback and Evaluation

Organizations are incorporating more and more real-time data—all those electronic bread crumbs we leave behind as we do our work—into performance assessments. In response, employees waste a lot of valuable energy managing impressions. But tools that separate data-informed feedback from the evaluation process help lower people's defenses and put the focus squarely on productivity and problem solving, where you want it.

In general, any information that goes into a formal performance review tends to put people on edge. Nevertheless, most employees are keenly interested in improving their skills. Just look at the popularity of Rypple, a social media platform created to allow members of organizations to give and gather anonymous feedback. (Salesforce.com purchased Rypple within three years of its launch for $60 million. It's now called Work.com.) "You simply had to ask, 'How am I doing at X?'" explains Rypple cofounder Daniel Debow, "and the answers were purely for you." Because only the recipients had access to their feedback, fear of repercussions was removed from the equation. Further, Debow notes, those giving the feedback submitted honest, useful appraisals—with assurance of privacy, they didn't have to worry that candid criticism might damage colleagues' reputations.

Another way of allowing employees to learn from their day-to-day actions without having every little mistake exposed to management is to deliver feedback within a protective bubble. A large U.S. trucking company did this when it installed a DriveCam at the top of each tractor cab's windshield to improve driver safety and performance. The small video camera points both outside and at the driver, gathering and wirelessly transmitting data that analysts can use to flag risky behaviors and prevent accidents. A green light tells the driver that all is well. But during a "G-force event" (any erratic driving incident that causes gravitational force, such as excessive speeding, slamming of brakes, or sudden swerving), the light blinks red and green. If the force is strong enough, the light turns red and the camera stores footage from eight seconds before and four seconds after the event. (On average, each vehicle's DriveCam stores about five minutes' worth of video a month.) The DriveCam also records key metrics, like the truck's speed and location.

A small group of coaches who oversee fleet safety review any events deemed preventable. Only in a situation involving damage or a willful breaking of the law—for instance, failing to use a seat belt or texting while driving—would the coaches share footage with management. And the supervisors who evaluate the truckers aren't privy to the coaching.

When the DriveCams were installed, drivers initially dreaded "being watched by Big Brother." Some got distracted when the red light came on, which made safety worse. But drivers have since warmed to the cams, because they now trust that management won't use the videos to evaluate or reprimand them. As one coach explains, the collaboration is helping drivers "turn bad habits into good habits" and improving their safety record. When coaches look at the footage with drivers, "it really does help," another says. "It changes people's perspectives." Sometimes it's just a simple realization: "Wow, you know, I was following a little too closely."

PHOTOGRAPHY: COURTESY OF LYTX

Type 3

Boundaries Between Decision Rights and Improvement Rights

Managers work hard to clarify decision rights, and for good reason. Spelling out who gets to make which calls helps organizations run more smoothly. It prevents duplicated effort, for example, and decision gridlock. But the empowerment of a select few can leave the other people in the organization feeling voiceless, especially if they aren't explicitly invited to improve systems, processes, roles, and tasks. Employees may withhold their ideas or implement them on the sly. When organizations don't grant improvement rights to those without decision rights, innovation by those who see solutions where others don't—known as productive, or positive, deviance—is effectively squashed in favor of conformity and compliance.

It's important to draw a line between the two kinds of rights, because the people exercising them have different needs. Holders of decision rights benefit from a transparent environment, where "every small fact becomes the subject of careful, scientific investigation," as Frederick Winslow Taylor put it more than a century ago. But while holders of decision rights want perfect visibility, which requires transparency from everyone, that kind of visibility gets in the way of employees' striving to make things better, because it curtails the experimentation necessary for improvements, as seen in the mobile phone factory and other settings.

In fact, a long stream of research tells us that in the presence of others, people do better on repetitive, practiced tasks—what psychologists call dominant responses—but worse on learning tasks that call for creative thinking. The visibility created by transparency conjures up self-consciousness and inhibitions. That's why musicians perform in front of an audience but practice without one—they need privacy to noodle and make discoveries. So, the right level of transparency—and thus oversight—depends on the activity and the observer. While musicians may practice in front of a teacher, that teacher is an invited coach, not a consumer of their work. Technology is making close scrutiny by large audiences of consumers possible to a degree that Taylor could never have imagined, and clear decision rights amplify its effects. If you're under the spotlight in front of such an audience, the last thing you want to do is to make unpracticed improvements while being held to a performance standard. All that transparency can create yearning for a closed door with a sign that says, "I'm in rehearsal!"

Organizations that understand all this are giving employees a reprieve from total transparency in order to make "slack" (excess resources) more productive rather than more scarce. Take Flextronics, a company that Willy Shih, Nina Bilimoria Angelo, and I have studied. By setting up a "moonshine shop," Flextronics has turned its factory floor in Guadalajara into a veritable Legoland for workers. The shop gives employees a place to develop tools and fixtures for their lines in periods of downtime—creative work that imparts a sense of ownership. (Manufacturing companies often facilitate improvement rights in this way.) Made of simple pipes, connectors, and recycled

PRODUCTIVE SLACK

In the "moonshine shop" at Flextronics, workers—who are encouraged to tinker with simple pipes, connectors, and recycled materials—build labor-saving devices in their downtime. Among their inventions: a lazy Susan for rotating heavy rods, a retractable chair that helps keep aisles clear, a quick gauge for the average worker's height, an easy-to-use rolling storage cart, and a heat-based process for stripping off "nonremovable" labels.

Lazy Susan

Retractable chair

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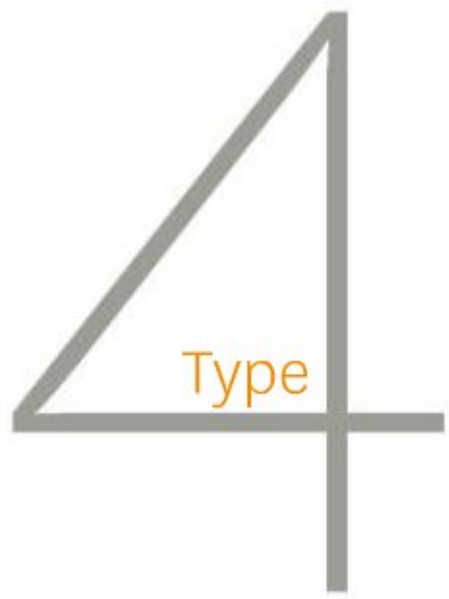
materials, the designs produced in the shop can cost a tenth of what it takes to produce the more complex, specially sourced fixtures provided by vendors. The quality makes IKEA look high-end, but the designs do the job efficiently, safely, and effectively. More important, the shop encourages continual innovation by the operators, creating efficiencies that would otherwise remain in the imagination of workers.

Manufacturers aren't the only organizations that have made slack more productive by protecting improvement rights. Saravanan Kesavan, Bradley Staats, and I saw this happen at the U.S. retailer Belk when it upgraded a mostly manual labor-scheduling system for its 24,000 employees and 300-plus department stores. Belk could have followed the lead of large retailers that have automated nearly all the scheduling task, increasing the efficiency of labor with complex algorithms based on minute-by-minute sales figures, real-time weather predictions, activity-based time studies, and other data. But Belk wanted to give its store managers and schedulers the flexibility to account for staffing variations and other local factors, since retail labor is a key driver of customer experience—and, therefore, sales. So its managers chose the simplest form of the technology and allowed local store managers and schedulers to exercise judgment, revising the schedules proposed by the system without having to seek corporate-level approval.

In the early days they revised more than 70% of the scheduling. Now that rate is below 50%—a more efficient, productive range. And while at least one of Belk's competitors recently suffered well-publicized challenges in getting a return on its new fully automated scheduling system, Belk's pilot stores showed a 2% lift in gross profit by the end of 2013, several months after implementing the version that allowed for overrides.

Which employees should be given improvement rights in order to create productive zones of slack? That depends on the organization and its leadership. In a lean environment everyone may be responsible for improvement. But other companies might treat it as an opportunity, not a mandate, perhaps vesting improvement rights in an R&D unit, a heavyweight team of senior managers, or frontline workers. Or an organization might outsource improvements to suppliers, contractors, or consultants. In any case, the assignment of improvement rights both reflects and influences strategy, so leaders must protect them by putting skunkworks activities inside zones of privacy.



Boundaries Around Time

Another way to strike the right balance between transparency and privacy is to experiment within limited blocks of time. With this approach, executives give employees more freedom for a specified period, so people can prepare for—and make the most of—their window of privacy.

This type of boundary complements the other three. A company might set up temporary teams for idea gestation, provide a onetime stream of developmental feedback (such as a 360-degree evaluation)

Height gauge

Rolling storage

Heat process

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Tracking Every Move

Many of the same companies that led the digital transformation of industries are also leading the digital transformation of work—allowing managers to observe from a distance far more than they could before.

Even knowledge work can be digitally monitored now. VoloMetrix—a Seattle-based start-up that extracts and analyzes data from company e-mails, calendars, social platforms, and line-of-business operations—provides employees with "people analytics" productivity dashboards based on their own collaboration and activity data or the data of the people they manage.

Of course, all this can feel intrusive—creepy, even—unless employers say what's in it for those being watched. That's how companies persuade consumers to give up personal information—by offering a quid pro quo. Yet for all the rhetoric about the value of utter transparency, there is scant empirical research to support it. So, what value can managers give in exchange for digitally tracking employees? Can they make the work easier or increase its impact? Can they use the data for recognition rather than coercion?

Ambition, a Y Combinator start-up, is trying to make transparency more engaging and less intrusive by reporting performance data as if employees were players on fantasy football teams (the user interface mimics fantasy football). Meanwhile, more individuals are monitoring their own activity through such devices as the Jawbone UP, the Fitbit, and the Nike+ FuelBand, to improve their behavior. Perhaps that will make them more receptive to digital tracking at work, which can yield equally beneficial self-awareness, even if the boss is watching.

SOME EXAMPLES

Amazon warehouse employees carry handheld computers that track and optimize every move.

Tesco warehouse workers wear armbands that do the same.

UPS trucks now have sensors that record nearly every action by their drivers.

Harrah's uses RFID technology to track how long it takes the waitstaff to serve drinks to customers.

that won't make its way into performance reviews, or assign improvement rights to a certain group for a quarter. Some biotech and consulting firms have borrowed the concept of the sabbatical from education and offered employees periods of relatively opaque slack. Googlers often use their 20% time on Fridays.

Tony Lo, the CEO of Giant Bicycles, granted CFO Bonnie Tu time-limited decision-making authority when he asked her to develop a business model to better meet female customers' needs. Lo saw Tu as a perfect leader for this initiative: Her seniority, reputation, and financial acumen gave her the freedom to break the usual rules. Lo—who was used to checking on important projects monthly, weekly, or even daily—left Tu alone for six months, the amount of time he thought it should take to develop and launch the idea. Tu and her team delivered brilliantly: They created a store in Taipei for women only—which reached profitability faster than any other Giant store. It has spawned a number of innovative products and serves as a model for similar stores around the globe.

In the same spirit, several major retailers have supplemented corporate planograms with "flexograms," enabling individual store managers to change how and where they display products in response to customer behavior. While some retailers, like H&M, have made flexograms a standard practice, most limit them to times of year when local customization and ingenuity are likely to maximize sales. They frequently allow experimentation during the December holiday season, for example. CVS put its sun care displays on wheels so that store managers could easily reposition them to take advantage of fast-changing weather and buying trends at specified times during key periods in the summer.

SIR ALEX FERGUSON, the former manager of the Manchester United football club, who is widely believed to be one of the greatest coaches in history, had an interesting take on transparency and its effects on performance. Though he championed the use of vests fitted with GPS sensors, which allowed analysis just 20 minutes after a training session, he said he would "never criticize a player during a training session. That's where they try the irreverent things that will, and won't, work during a match."

It's an important point: Irreverence increases our willingness to test how we do things and to deviate from the norm. But total transparency heightens the risk that our irreverence will come back to haunt us—and thus has a chilling effect on experimentation. Advanced sensing and tracking technologies make behavior highly visible in real time. How all that information should be used—by individuals, their teams, their supervisors—is a management question, not a technology question. Organizational cultures that foster psychological safety, trust, balanced power dynamics, and collaboration can help. But it's also critical for leaders to mitigate transparency with zones of privacy, enabling just the right amount of deviance to foster innovation and productivity.

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ARTWORK Michael Wolf
The Transparent City 93, 2008

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Workspaces That Move People

Today's offices don't encourage us to mingle—but that's what creativity and productivity demand.

by Ben Waber, Jennifer Magnolfi, and Greg Lindsay

IN SILICON VALLEY the tight correlation between personal interactions, performance, and innovation is an article of faith, and innovators are building cathedrals reflecting this. Google's new campus is designed to maximize chance encounters.

Facebook will soon put several thousand of its employees into a single mile-long room. Yahoo notoriously revoked mobile work privileges because, as the chief of human resources explained, "some of the best decisions and insights come from hallway and cafeteria discussions." And Samsung recently unveiled plans for a new U.S. headquarters, designed in stark contrast to its traditionally hierarchical culture. Vast outdoor areas sandwiched between floors will lure workers into public spaces, where Samsung's executives hope that engineers and salespeople will actually mingle. "The most creative ideas aren't going to come while sitting in front of your monitor," says Scott Birnbaum, a vice president of Samsung Semiconductor. The new building "is really designed to spark not just collaboration but that innovation you see when people collide."

Faith is nice, but do executives have *proof* that this works? Social space like Samsung's could be just another in a long line of fads and broken promises in workspace design: The "action office" becomes the cubicle. Cubicles are torn down for open plans, which leave introverts pining for private space. Quads. Hotel space. Couches. Rotating desk assignments. Standing desks. Treadmill desks. No desks. With apologies to Mark Twain, there's no such thing as a new office design. We just take old ideas, put them into a kind of kaleidoscope, and turn.

How do we know whether any of these approaches is effective? The key metric companies use to measure space—cost per square foot—is focused on efficiency. Few companies measure whether a space's design helps or hurts performance, but they should. They have the means. The same sensors, activity trackers, smartphones, and social networks that they eagerly foist on customers to reveal their habits and behavior can be turned inward, on employees in their work environments, to learn whether it's true that getting engineers and salespeople talking actually works.

Emerging Evidence

We've already begun to collect this kind of performance data using a variety of tools, from simple network analytics to sociometric badges that capture interaction, communication, and location information. After deploying thousands of badges in workplaces ranging from pharmaceuticals, finance, and software companies to hospitals, we've begun to unlock the

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Idea in Brief

THE CHALLENGE

Companies believe that more open space will boost productivity and creativity, but they have no evidence to prove it. They also use cost per square foot as the key metric for managing space.

THE SOLUTION

New sensor technology provides data about worker communication and its effect on group performance. It suggests how to design spaces to take advantage of digital work styles and get people bumping into one another, which leads to increased productivity and creativity.

THE FUTURE

Designs that encourage "collisions" between digital-savvy workers are being scaled beyond office buildings to improve knowledge worker performance in entire neighborhoods, pointing to a future in which the corporate office is a semipermeable public-private space woven into the urban fabric.

secrets of good office design in terms of density, proximity of people, and social nature. We've learned, for example, that face-to-face interactions are by far the most important activity in an office. Birnbaum is on to something when he talks about getting employees to "collide," because our data suggest that creating collisions—chance encounters and unplanned interactions between knowledge workers, both inside and outside the organization—improves performance.

We've also learned that spaces can even be designed to produce specific performance outcomes—productivity in one space, say, and increased innovation in another, or both in the same space but at different times. By combining the emerging data with organizational metrics such as total sales or number of new-product launches, we can demonstrate a workspace's effect on the bottom line and then engineer the space to improve it. This will lead to profound changes in how we build our future workspaces. Here are a few:

Recognize office space as not just an amortized asset but a strategic tool for growth. The consulting and design firm Strategy Plus estimates that office utilization *peaks* at 42% on any given day. By that logic, the best way to manage cost per square foot is to remove "wasted" square feet. But the data we're generating reveal that investments in re-engineering space for interactions over efficiency can increase sales or new-product launches.

Design offices to reflect how 21st-century digital work actually happens. The buildings we go to every day haven't changed as much as have the tools we use to get work done. Merging digital communication patterns with physical space can increase the probability of interactions that lead to innovation and productivity.

Re-engineer offices to weave a building, a collection of buildings, or a variety of workspaces into the urban fabric. The office of the future will most likely include highly networked,

FAR LEFT Samsung's U.S. headquarters, in San Jose, features a central atrium. **MIDDLE AND NEAR LEFT** Outdoor and large public spaces are sandwiched between floors.

Chance encounters and interactions between knowledge workers improve performance.

RIGHT Public areas can become semipublic meeting places.
FAR RIGHT Silo-busting requires spaces that draw people out of their offices.

Telenor's CEO thinks of its headquarters not as real estate but as a communication tool.

shared, multipurpose spaces that redefine boundaries between companies and improve everyone's performance.

Getting there won't be easy. It will require collecting much more data to inform new design and management principles while engaging urban planners and municipal governments. It will also transform HR, IT, and facilities management from support functions to facilitators. But if companies can change their spaces to reflect how people work, performance improvement will follow. Don't take that on faith. There are data to prove it.

Strategic Coffee Machines

Jon Fredrik Baksaas, the CEO of the Norwegian telecommunications company Telenor, credits the design of the company's Oslo headquarters with helping it shift from a state-run monopoly to a competitive multinational carrier with 150 million subscribers. That design, he says, improved communication, accelerated decision making, and even created what he calls "an attacking mind-set." It was ahead of its time in 2003, when it incorporated "hot desking" (no assigned seats) and spaces that could easily be reconfigured for different tasks and evolving teams.

The design features that make the space effective resulted from a profound shift in mind-set: Baksaas thinks of the offices not as real estate but as a communication tool. Thus strategy, features, and value become more important than cost and efficiency. You'd choose the e-mail provider with the best collaboration and file-transfer features; you can think of space investments the same way.

The improved communication Telenor achieved in its new space can be explained by Alex "Sandy" Pentland's April 2012 HBR article, "The New Science of Building Great Teams." Pentland deployed badges (the same kind now used by Ben Waber's firm) that track how people talk to one another, who talks with whom, how people move around the office, and where they spend time. (Devices were worn on an opt-in basis, and individual data were anonymous and unavailable to employers.) Pentland identified three key elements of successful communication: *exploration* (interacting with people in many other social groups), *engagement* (interacting with people within your social group, in reasonably equal doses), and *energy* (interacting with more people overall).

Spaces designed to promote these activities increase the likelihood of collisions—and the data repeatedly demonstrate that more collisions create positive outcomes. We don't measure the content of interactions, but that doesn't matter. When collisions occur, regardless of their content, improvement typically follows.

Spaces can be designed to favor exploration or engagement or energy to achieve certain outcomes. For example, if a call center wants improved productivity, the space should favor engagement—getting the team to interact more. Higher engagement is typically accomplished not with open social space but with tight, walled-off workstations and adjacent spaces for small-group collaboration and interaction. The team's break area becomes a crucial collision space. At one call center, the company expanded the break room and gave reps more time to hang out there with colleagues. Paradoxically, productivity shot up after the change. Away from their phones, the reps could circulate knowledge within the group.

Then again, for a company that—like Telenor—is trying to innovate or change, increasing engagement can be detrimental, because it takes time away from crucial exploration with other groups and outsiders. Telenor's open, public, and flexible space values exploration much more than engagement—it begs employees to meet in the open, where

they may bump into unexpected people, and allows them to claim spaces and shape them for brainstorming sessions.

Once a company has identified the pattern it's trying to achieve and how the pattern affects outcomes, it can begin to calculate the value of workspaces, not just their costs. For example, we deployed sociometric badges with about 50 executives at a pharmaceuticals company who were responsible for nearly $1 billion in annual sales. They wanted to increase sales but didn't know what behaviors would help. Even if sales went up, they couldn't necessarily say why.

The data collected over some weeks showed that when a salesperson increased interactions with coworkers on other teams—that is, increased exploration—by 10%, his or her sales also grew by 10%. An elegant correlation.

So the executives asked, How can we change our space to get the sales staff running into colleagues from other departments? In this case, the answer lay with coffee. At the time, the company had roughly one coffee machine for every six employees, and the same people used the same machines every day. The sales force commiserated with itself. Marketing people talked to marketing people.

The company invested several hundred thousand dollars to rip out the coffee stations and build fewer, bigger ones—just one for every 120 employees. It also created a large cafeteria for all employees in place of a much smaller one that few employees had used. In the quarter after the coffee-and-cafeteria switch, sales rose by 20%, or $200 million, quickly justifying the capital investment in the redesign.

Managers might be tempted to simply build big social spaces and expect great results, but it's not that simple. Companies must have an understanding of what they're trying to achieve (higher productivity? more creativity?) before changing a space.

THE ALLEN CURVE HOLDS

In his seminal 1977 book, *Managing the Flow of Technology,* Thomas J. Allen was the first to measure the strong negative correlation between physical distance and frequency of communication. The "Allen curve" estimates that we are four times as likely to communicate regularly with someone sitting six feet away from us as with someone 60 feet away, and that we almost never communicate with colleagues on separate floors or in separate buildings.

But the office is no longer just a physical place; we can enter it by logging on, attend meetings from anywhere, and collaborate on documents without ever seeing one another. It would seem that distance-shrinking technologies break the Allen curve, and that communication no longer correlates to distance.

Wrong. The Allen curve holds. In fact, as distance-shrinking technology accelerates, proximity is apparently becoming more important. Studies by Ben Waber show that both face-to-face and digital communications follow the Allen curve. In one study, engineers who shared a physical office were 20% more likely to stay in touch digitally than those who worked elsewhere. When they needed to collaborate closely, co-located coworkers e-mailed four times as frequently as colleagues in different locations, which led to 32% faster project completion times.

Out of sight, out of sync.

WHAT ABOUT THE GLOBAL COMPANY?

What happens when proximity isn't feasible? When our colleagues are not only in different buildings but in different countries?

One consumer packaged goods company we know of is trying to address these questions. It has a global real estate portfolio of more than 200 million square feet supporting 300,000 employees in 26 countries. Managing for collisions at this scale requires a two-pronged approach. First, like Telenor, the company must treat the buildings as communication tools, using more open environments and denser workspaces to promote interactions.

Second, it must link those optimized buildings in a virtual space that makes communication between them as easy and effective as possible. To achieve that, it has created a "community manager" role for workspace operations, bridging facilities management, technology, and corporate communications. The role is modeled on those found in online communities such as Yelp and Airbnb and in coworking spaces. The company's community manager tries to create virtual collisions by making it easy for people who can't interact in person to connect through online and social channels.

RIGHT AND FAR RIGHT Coworking spaces are a response to the oppressiveness of the cubicle and the loneliness of the telecommuter. Young digital workers believe that these spaces improve their performance.

By 2014, 72% of those who used coworking spaces were forecasting an increase in their income.

For example, what worked at the pharma company didn't work at a large furniture manufacturer that transformed its headquarters from classic cubicles to an open-plan office in which approximately 60% of the workforce had unassigned seating. To test the plan, we deployed badges with 65 sales and marketing team members on a single floor before and after the reconfiguration.

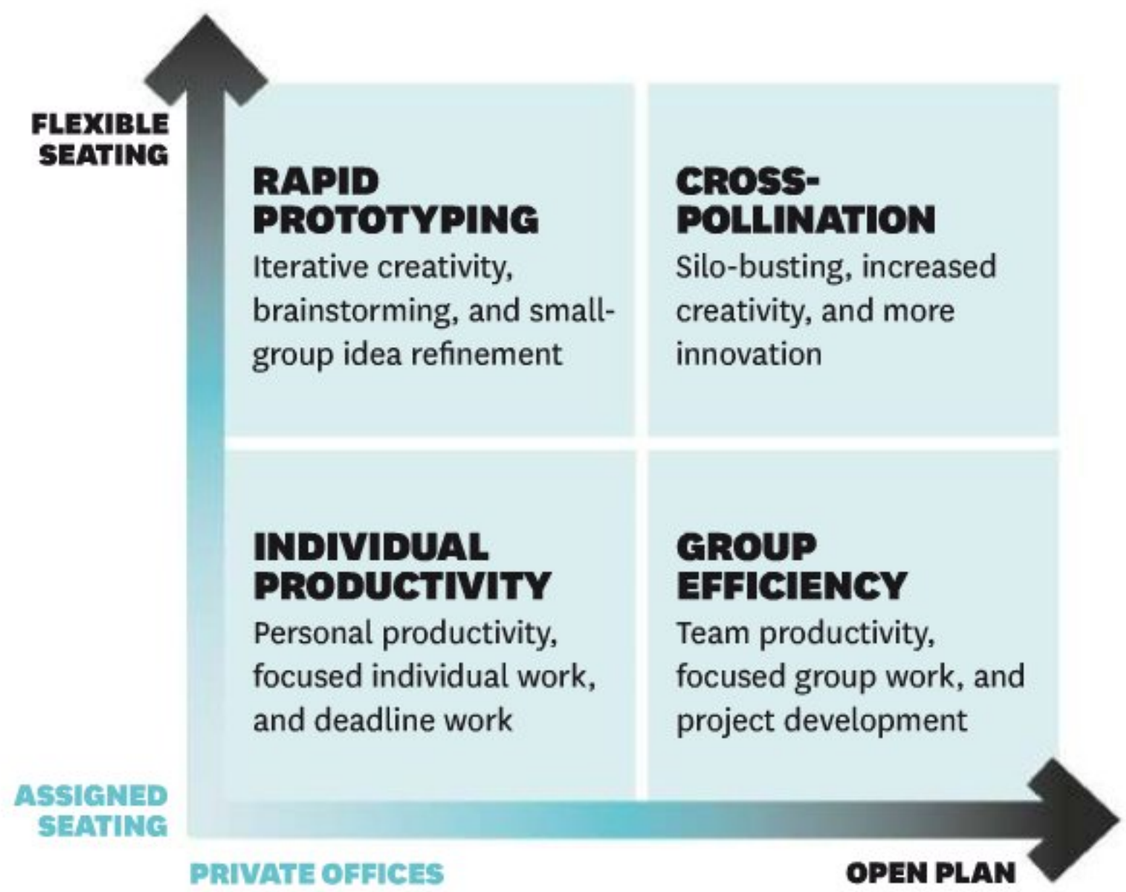
The call center's goal was to get the members of one team talking to improve productivity. Telenor and the pharma company needed space that encouraged people to collide with *other* groups. The furniture company's success required something in between: tight integration across the sales cycle, which meant some exploration and then high engagement among specific groups that needed to communicate more.

The company had hypothesized that fewer desks and a smaller footprint would move people closer together, increasing the likelihood of interaction. Unassigned seating would make interaction between people in different groups more likely. Such interaction did increase, by 17%—but energy levels (the number of individuals' encounters during the day) dropped by an average of 14%. This suggests that the space simply reshuffled stationary workers rather than creating movement. Someone from marketing might bump into new people because their temporary desks happened to be close by, but none of them were leaving their workstations once they got there. As a result, team communication dropped by 45%. The company saved money on space by reducing the number of fixed workstations, but both revenue and productivity plummeted.

The type of interaction that's most valuable changes according to goals; what doesn't change is that interaction in itself is far more valuable than we realize. Sometimes circulating, exploring, engaging,

A BEGINNER'S GUIDE TO SPACE DESIGN

If you want to reconfigure your office space to improve performance, this simple grid will help you get started. It uses two important factors in office design—relative openness and seating flexibility—to suggest what configuration will lead to one of four distinct outcomes.



and increasing the number of people's collisions is more important than individual productivity or creativity. Imagine, for example, that a worker finds a better way to do her job but never tells anyone else doing the same job what she discovered. She has improved her performance but no one else's. If she takes time out of her day to tell others about what she's learned, her productivity drops—but she has increased theirs. We've shown that in some cases even a 5% drop in personal productivity can have a positive outcome on group performance.

Think of the implications: First, most employee performance reviews are based on individual productivity and don't take into consideration how group productivity can grow through more interaction. Second, untold amounts of money are invested in tools to increase individual productivity, but the money might be better used to design a workplace that promotes collisions that will make the organization—not individuals—more successful.

Lobbies as Offices

One factor complicates all this: Office buildings are no longer the sole locations for knowledge work. In fact, research from the consulting group Emergent Research suggests that two-thirds of it now happens outside the office. Consequently, no matter how precisely we design office space to create collisions, the design is incomplete if it doesn't take into account digital work and collaboration that are independent of space and time and for which immediacy is more important.

In some ways the digital workspace enhances in-person collisions with file-sharing and communication tools such as chat, e-mail, and archiving. It can gather more ideas from more places: Research indicates that interactions and engagement decrease as the physical distance between work groups gets bigger, whereas online engagement increases with the number of users. However, data show that digital communication can't replace face-to-face interaction and may actually be enhanced by it (see the sidebar "The Allen Curve Holds"). Studies with sociometric badges confirm that remote teams don't perform as well as those in physical proximity.

Furthermore, the upgrade cycles of buildings and technology don't mesh. Telenor's state-of-the-art campus, which smartly integrated digital features such as a wireless file-sharing system—was built four years before the iPhone was introduced and before Wi-Fi became ubiquitous. Just a few years later, Telenor's then-novel proprietary wireless network would have been designed radically differently—if its features weren't obviated by cloud storage and other developments. All of which is to say that understanding how digital and physical spaces work together is crucial to improving workspace but also an incredibly complicated design challenge.

Workers themselves have been the first to take on this challenge. Just as IT has been consumerized over the past decade, digital-savvy employees are beginning to demand that their spaces adapt to how they work, rather than vice versa. This shift began in earnest in 2005, in San Francisco, London, and Berlin. Technologists, programmers, and creative professionals wanted to work outside confining office environments but also to avoid the isolation of home offices. They chose to work side by side, in what are known as coworking spaces.

Early examples were organic, built by users rather than by design professionals. They were accessible to anyone and sometimes free. People who chose to work in those spaces intentionally sought members from different organizations, thus reproducing the community, social interaction, learning, and energy typical of their online work, while adding the benefit

FAR RIGHT Workspace in the Downtown Container Park, part of the Las Vegas Downtown Project. **MIDDLE AND NEAR RIGHT** The park mixes spaces for work, living, and play, encouraging serendipitous meet-ups.

Zappos uses a new metric—"collisionable hours"—to measure a space's effectiveness.

of physical proximity to others. Unwittingly, they were engineering spaces to create the exploration that we know enhances creativity. And it worked. Studying 45 coworking spaces around the world, one of us, Jennifer Magnolfi, discovered that people had chosen them because they believed that their performance would improve more rapidly in such spaces than in an office building or at home. A 2011 *Deskmag* survey of more than 1,500 coworkers in 52 countries supported her findings:

- 75% reported an increase in productivity since joining their space
- 80% reported an increase in the size of their business network
- 92% reported an increase in the size of their social circle
- 86% reported a decrease in their sense of isolation
- 83% reported that they trusted others in their coworking space

By 2013, according to data from Emergent Research, more than 160,000 people were using several thousand coworking spaces in the United States and Europe. The organization forecasts that in five years more than one million people will be using 12,000 coworking spaces globally. Another survey showed that by 2014, 72% of participants were forecasting an increase in their income.

The growth of coworking and surveys of coworkers demonstrate that given the choice, people will choose workspaces that support their digital style while giving them access to new knowledge, exposing them to different kinds of expertise, and accelerating their learning. Coworking's success has helped some teams "graduate" out of their coworking spaces. Although the model clearly provides the exploration that independent workers and very small groups need, when teams reach a critical size, usually around 10 members, they need to up their engagement with one another. Private office space and conference rooms become necessary parts of their workday.

This has led to the scaling of coworking space. What started as small spaces for a few independent workers grew into start-up accelerators—groups of start-ups sharing some of the private collaboration space available to them. Eventually large corporations mimicked the idea by creating shared space where their employees could work with partners, researchers, and customers. The first floor of Amazon's new campus in Seattle is mostly coworking space. Ace Hotel actively markets the lobby of its New York flagship as a workspace. AT&T has created Foundry, a network of research centers in which its engineers work side by side with handpicked start-ups, corporate partners, and third-party developers to bring new products to market faster. Even bankers are doing it: ING Direct built seven cafés (now called Capital One 360 Cafés) where its workers could set up shop and interact with customers who could also use the space for work. Perhaps less surprisingly, and true to form, Airbnb has made one of the conference rooms at its new headquarters bookable (through Airbnb, of course) by anyone in San Francisco, free.

What's Happening in Vegas

Coworking is succeeding because it successfully integrates good workspace design that enhances exploration with the digital work habits of individuals and small teams. In some cases it's possible to scale the benefits of coworking—such as high collision rates and accelerated learning—to build an entire neighborhood.

The Downtown Project, in Las Vegas, is an early example of the concept. Tony Hsieh, the CEO of Zappos, is investing $350 million in the area around the company's new headquarters, which is the

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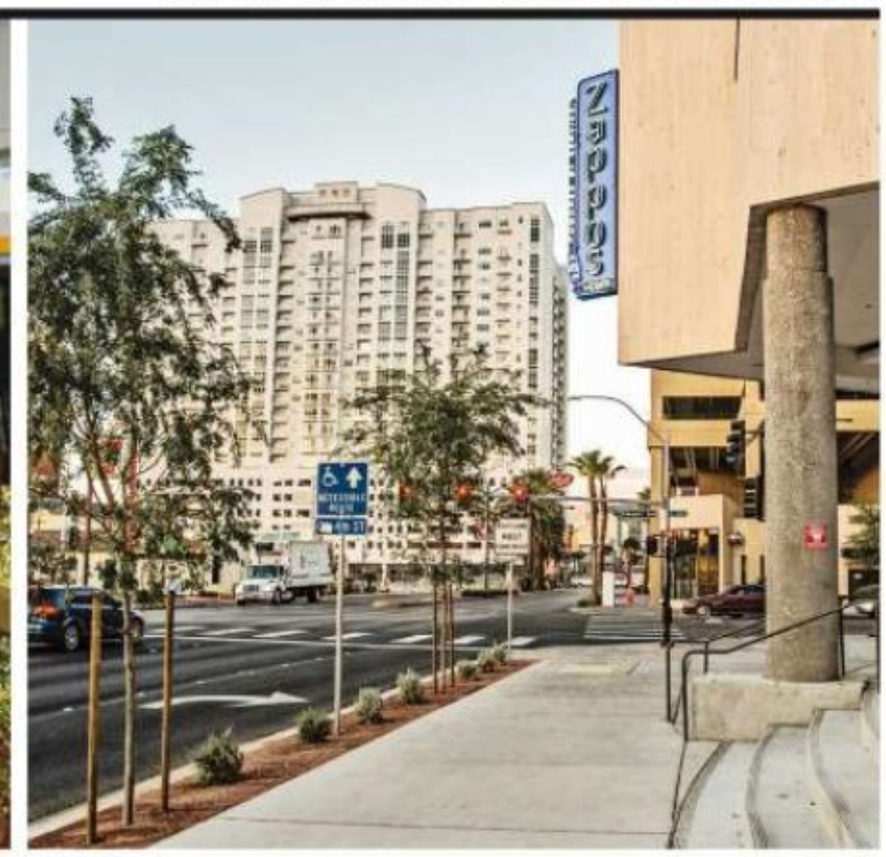

former city hall. Hsieh's goal is to grow the local start-up and entrepreneurial community in a way that will organically attract talent to the area, benefiting both Zappos employees and the neighborhood.

Jennifer Magnolfi participated in the development and analysis of coworking space inside Zappos headquarters and led a local coworking experiment that launched in early 2012 and eventually grew to include nearly 200 stakeholders, among them Zappos employees, area residents, start-ups, independent workers, and others. The spaces were improvised from a network of existing ones: a coffee shop, the courtyard of a Thai restaurant, an old church hall, the lobby of a casino, and an empty corporate apartment.

Early results show that the small, shared nature of the neighborhood fostered mobility that created collisions on a greater scale. Exploration and energy were very high. After six months, data revealed a 42% increase in face-to-face encounters, a 78% increase in participant-generated proposals to solve specific problems, and an 84% increase in the number of new leaders—participants who initiated work and collaboration and developed project scope and objectives. Ten new civic and local community projects were launched—including the Sunday Reset Project, a monthly event to promote healthful living.

Zappos and the Downtown Project have continued experimenting with the area and are using a new metric: "collisionable hours," or the number of probable interactions per hour per acre. Hsieh's goal is to reach 100,000 collisionable hours per acre in the neighborhood—about 2.3 per square foot per year.

The Downtown Project is still a controlled experiment. It doesn't capture the complexity of getting companies and civic entities to cooperate, routinely and continually, while also adapting to inevitable technological change. Nor does it address the complexity of getting a multinational to integrate coworking space when it's already managing a global office portfolio. (See the sidebar "What About the Global Company?") But it points to a new model for the corporate campus of the future that weaves together public and private spaces, employees and partners, living and working. Hsieh and others believe that companies designed on this model will be more productive and innovative—as businesses and as communities—and in the long term will gain a strategic advantage over companies that cut off their employees from the exploration that improves performance.

MORE THAN A CENTURY AGO, Frederick Winslow Taylor brought his stopwatch and principles of scientific management to the office, instilling efficiency as the highest calling in what was then a factory for processing paperwork. Today we have the means to measure the performance of modern idea factories. Even these early insights suggest a future in which we must aggressively change the definition of what workspace is, from *where* work is done to *how* it's done, and then design spaces—physical and digital—around that. The office of the past was a literal box of cubicles and desks, meeting rooms and common spaces. In the office of the future, we'll be thinking and working outside it.

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ILLUSTRATION: PETER CROWTHER

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Innovation isn't worth much if you don't get paid for it.

BY STEFAN MICHEL

When Switzerland-based Vestergaard introduced its LifeStraw technology, it proved it could innovate. LifeStraws remove 99.99999% of bacteria and 99.9% of protozoan cysts from contaminated water. The product is a favorite of aid organizations: Over the past decade, LifeStraws have been distributed after almost every disaster.

But not every place with bad drinking water is a relief zone; 780 million people in the world lack access to clean water in their daily lives. So Vestergaard saw a much larger potential market than its NGO customer base—and proved that it could innovate in another way. The challenge was LifeStraw's cost, which is beyond the means of most households in developing countries. The company found a clever means for families to fund their purchases: with carbon offset credits. Thanks to the worldwide carbon emissions trade, any documented CO_2 savings can now be monetized—and using LifeStraws means not having to burn petrol or wood to boil dirty water. Vestergaard's Carbon For Water initiative has enabled hundreds of thousands of Kenyan families to pay for its product, growing its business substantially.

Both these kinds of innovation—one in value *creation,* the other in value *capture*—are important. But most companies focus only on the first. Sometimes a business can get away with failing to think about value capture if it sells plenty of its new offerings through existing approaches. But when value capture goes unexamined, money is usually left on the table—and sometimes the only thing that can save a business is finding a way to capture value. This is the situation in which many publishing companies find themselves, as more consumers than ever are accessing content while revenue streams to producers are drying up. It can also confront young, new-economy businesses—for example, Facebook. With 1.3 billion active monthly users, Facebook has an undisputed ability to create value for customers. But as the highly volatile share price testifies, it is not at all clear that the company will figure out how to capture enough value to justify its hefty market capitalization and price-earnings ratio.

To benefit from both kinds of innovation, companies need to think about value capture more imaginatively and as a matter of course. In this article I'll present 15 ways I've seen firms capture new value, clustered under five focal points of change. Such a framework is an important step toward developing a common language around value capture—a concept that, like "business model reinvention," is hard for many executives to get a handle on. It should help managers identify value-capture twists that could work for them. (See the sidebar "A Framework for Value-Capture Innovation.")

The Innovation Blind Spot

In constant pursuit of the new, businesses maintain R&D labs, conduct pilots, crowdsource ideas, use open innovation—to top managers, it may seem that investment in innovation is enormous. Yet even avid innovators often have a blind spot when it comes to value capture. They may assume that if value is created, rewards will follow. Indeed, one reason value-capture innovation tends to be overlooked is that companies that do it well often simultaneously innovate in value creation, and the latter tends to take

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Idea in Brief

THE PROBLEM
Businesses innovate constantly to create new value for customers. But unless they also revisit how they capture value, they might not be adequately compensated for those breakthroughs.

THE SOLUTION
A new framework helps managers spot opportunities. It catalogs recent innovations in value capture and shows that they fall into five categories. Firms can profit by changing the price-setting mechanism, the payer, the price carrier, the timing of the exchange, or the segment served.

THE TOOL IN USE
In workshops at a major airline, a global professional services firm, and other businesses, cross-functional teams using the framework quickly devised new ways to capture value that boosted profits.

center stage. For example, when Netflix became a mortal threat to Blockbuster, it was easy to chalk up its victory to greater value creation. And it's true that Netflix deftly capitalized on new digital capabilities to offer personalized recommendations and could avoid presenting customers with shelves picked clean of current hits. But the death blow came from the value-capture side. The brick-and-mortar incumbent's revenue model relied heavily on late fees. Netflix introduced a subscription model that milked higher revenue from the same tendency to be tardy—without vilifying customers in the process.

Even managers who know they should worry about value capture often reduce the subject to pricing. Pricing is important, of course, and there is a rich literature devoted to managing it well. But changing a tag from $9.50 to $9.99 or running a "buy one, get one free" promotion does not constitute innovation. Value capture involves more-fundamental considerations, with greater strategic implications.

Therefore, the first step toward innovating in value capture is simply to make people conscious of it. Open managers' eyes to novel approaches like Vestergaard's and Netflix's, and the blind spots disappear. Go a step further and contemplate multiple examples, such as the ones below, and patterns emerge.

Changing the price-setting mechanism. The first group of innovations involve the mechanism or rationale by which prices are established. The most familiar of them is *value-based pricing.* This occurs when a company stops setting prices by simply marking up production costs or calibrating against competitors' prices and instead charges according to the offering's worth to the customer.

A good example involves ecosyn-lubric, a product sold by Bossard, which supplies fasteners to John Deere and other manufacturers (full disclosure: I am a member of Bossard's board). Bossard discovered that its customers' workers were spending more time manually lubricating screws than putting machines together—with messy and uneven results. So it teamed up with a chemical company to find a way to deliver fasteners with lubricant already uniformly applied. Bossard does not disclose profit margins for individual items; however, its operating margin is about twice the industry average. It's safe to say that the substantially higher price of its lubricated screws is not based on their production cost. More likely, Bossard priced ecosyn-lubric to capture a fair share of the savings its customers experience.

The other innovations in this group begin with the assumption that value-based pricing is superior and focus on two challenges: discovering customers' value perceptions (especially tricky when perceptions vary from customer to customer) and creating a structure in which different customers are charged different prices depending on their willingness to pay.

Auctioning works well for Google. The company's revenue stream comes largely from advertisers' payments to appear on search-result pages. Rather than set prices, Google has advertisers bid for the keywords with which they want to be associated. The term "mortgage," for example, is valued to different degrees depending on banks' and brokers' priorities and budgets. An auction can quickly surface its highest acceptable price (probably upwards of $5 per click—far more than the average cost of 35 cents), and Google rewards the top bidder with maximum prominence in search results.

The downside of auctioning, as many an eBay seller has learned, is that it can result in prices that don't please the seller but must be honored nonetheless. However, auctioning can also yield prices the seller would never have had the audacity to name. Imagine charging one customer 6,000 times as much as others for the same thing—and leaving him happy about the transaction. That is what a Swiss canton did when issuing license tags for cars.

Although drivers in the United States can pay a set fee for vanity plates of their own devising, the same isn't true in Switzerland, where plates are issued with consecutive numbers. However, the numbers of returned plates are reused, and occasionally the authorities get back a set so special that it seems a pity to simply hand it to the next person in line. An internet-based auction was held for the plate SG 1—the lowest number in the canton of St. Gallen—with the winner paying an astounding 135,000 francs (about $150,000). In a similar auction in Abu Dhabi, Sheikh Saeed al-Khouri paid 52 million dirhams (about $14 million) for the license tag bearing just the number 1.

Demand-driven pricing lets fluctuations in aggregate demand drive changes in price. Consider the yield-management practices of airlines, hotels, and rental car agencies. Using forecasting models based on past reservation patterns, these asset-utilization-obsessed businesses can predict peaks and valleys in demand and adjust prices to maximize profitability during both. An entertaining application of the strategy can be experienced through the Bierbörse ("beer exchange") in Germany's Berliner Republik restaurant. The fact that the price of a beer changes dynamically over the course of an evening is largely a novelty—watching the monitors update in real time gives customers something fun to talk about. But it also smooths demand and averts the slow service that often comes during peak hours.

Even avid innovators often have a blind spot when it comes to value capture, assuming that if value is created, rewards will follow.

Two forms of innovation in this group let customers set prices themselves. *Name your own price* is probably best known from Priceline, whose customers stipulate what they are willing to pay to travel from point A to point B, or for lodgings in a particular locale, within a given time frame; sellers can take or leave the deal. The arrangement is akin to an auction, but with an important distinction: The amount is not disclosed to anyone outside the transaction, so airlines and hotels can hold prices generally even as they discount for incremental sales. Taking this idea to an extreme, some companies have *pay what you want* arrangements, whereby the seller must take whatever the customer offers. Given the potential for free-rider abuse, few businesses contemplate this innovation. However, the fast-casual restaurant chain Panera Bread has shown that the model can capture value. Having implemented it in five nonprofit "community cafés" over three years, Panera reports that although 20% of customers pay less than the suggested donation (and sometimes nothing), another 20% pay more.

Changing the payer. In a straightforward world, those who consume offerings would pay for the value they receive, but in reality other arrangements often better serve consumers and producers alike. Perhaps the most familiar examples are in media businesses where content is expensive to produce and consumption is subsidized by advertisers—an arrangement known as a *two-sided market model*. Many types of businesses have relationships with consumers whom others would like to reach; they could probably succeed as two-sided markets selling access to the valuable networks they have assembled.

Any two-sided market forces a decision about how much each side pays—and the solution may be surprising. For example, the Swiss paper *20 Minuten* reaches 2 million readers—33% of the country's population between the ages of 14 and 70. Its secret? It is handed out free, mainly on public transportation. The newspaper innovated by making advertisers the sole payers. The key to the model's success is the public-transportation distribution: Advertisers are comfortable footing the bill because they know that commuters tend to be young and employed, with higher-than-average disposable incomes.

A similar innovation came from Cardea, a "meta-consultancy" that helps companies find the best consulting firms for their various managerial challenges (recommending one for, say, a cost-reduction analysis and another for a merger). The firm found that many companies resisted what they saw as a surcharge on already expensive services. Its fortunes improved when it changed its value-capture model and charged referrals to the consultants instead of their clients. Consultants accept the arrangement because Cardea's referrals reduce the acquisition costs they normally incur to gain new business.

Sometimes markets have more than two sides. In these cases it may be possible to *change the payer in the value constellation*. The U.S. market for tutoring is a case in point. With the 2001 passage of the federal No Child Left Behind Act, parents of underachieving children gained access to private tutoring services paid for by the government. Other players with a

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stake in student outcomes include state and local education departments, future employers, schools, teachers, and students themselves. With multiple diverse players, tutoring services can move among and combine several revenue streams.

A special case of changing the payer is possible in B2B settings where *internal budgeting* creates multiple (and shifting) reservoirs of cash to be tapped. When my business school, IMD, got word that a company for which it provided executive education programs was terminating its contract, it was mystified; the client had always registered very high satisfaction. The explanation soon came: Drastic cuts had been made to the firm's executive-development budget. A colleague devised a value-capture innovation that saved the account. He approached a group of the company's global functional managers and persuaded them to cover half the costs for their functions' participants out of their division budgets. When the original buyer, a human resources leader, was then offered a price cut of 50% (in terms of his own budget), he was able to say yes.

Changing the price carrier. What is the "price carrier" in your offering? In simple terms, it's the part of the experience you hang the price tag on. Someone might patronize a McDonald's restaurant because he needs a Wi-Fi connection or wants to bring the kids to a PlayPlace on a rainy day. But McDonald's doesn't charge for either of those things. The price for a visit, regardless of what one values about the experience, is carried by the food and beverage order. A strategic question many companies should ask: Is the price tag affixed to the right part of the package, and what would happen—to profits and to other players in the market—if it were moved?

Let's return to Netflix, a prime example of *changing the carrier.* The film-renting public was accustomed to discrete transactions in which customers selected DVDs and paid for each one. Many people benefited from clerks who came to know their tastes and made useful recommendations, but that service carried no price tag. Netflix changed that, moving to a membership subscription model and making personalized recommendations an explicit part of its value proposition. With customers viewing anywhere from a handful to hundreds of selections a year, the per-rental price was no longer the point; the price carrier was now the subscription service.

And consider Nespresso, which manufactures single-cup coffee makers and the capsules used in brewing. Yes, the launch of such a handy appliance is an exercise in value creation. But any innovation that allows a company to sell $19 worth of a commodity (the typical retail price for a kilo of coffee beans) for up to $137 must also be celebrated for its value capture. Nespresso accomplished this by changing the price carrier from the bag of beans to the perfectly brewed beverage.

When managers talk about *bundling and unbundling* a company's offerings, they are referring to the most common way of changing the price carrier. We see this in telecommunications, where a customer's solution typically consists of several elements, each of which could be priced separately. Bundling elements into a package with one overall price allows sellers to assemble varying solutions that appeal to different customer segments; it also staves off price wars by making comparisons between vendors more difficult. When it comes to unbundling, the best

A Framework for Value-Capture Innovation

A comprehensive survey of strategic moves to capture more value suggests that innovations come in 15 distinct forms.

INNOVATION CATEGORY	INNOVATION STRATEGY	EXAMPLES
CHANGING THE PRICE-SETTING MECHANISM	VALUE-BASED PRICING	• BOSSARD'S ECOSYN-LUBRIC FASTENERS
	AUCTIONING	• GOOGLE ADWORDS • GOVERNMENT AUCTIONS OF VANITY LICENSE PLATES
	DEMAND-DRIVEN PRICING	• AIRLINES' YIELD-MANAGEMENT SYSTEMS • THE BERLINER REPUBLIK RESTAURANT'S BEER EXCHANGE
	NAME YOUR OWN PRICE	• PRICELINE
	PAY WHAT YOU WANT	• PANERA BREAD'S COMMUNITY CAFÉS
CHANGING THE PAYER	TWO-SIDED MARKET MODEL	• *20 MINUTEN* • CARDEA
	CHANGING THE PAYER IN THE VALUE CONSTELLATION	• CARBON FOR WATER • SUBSIDIZED TUTORING SERVICES
	INTERNAL BUDGETING	• IMD'S EXECUTIVE EDUCATION PROGRAMS
CHANGING THE PRICE CARRIER	CHANGING THE CARRIER	• NETFLIX • NESPRESSO
	BUNDLING AND UNBUNDLING	• TELECOMMUNICATIONS • AIRLINE INDUSTRY
	ALL-INCLUSIVE OFFERING	• CRUISES • CHÂTEAUFORM'
CHANGING THE TIMING	INSTALLED BASE PRICING	• GILLETTE • SCHINDLER
	FUTURES CONTRACTING	• COMMODITIES PRICING • PRESOLD HOTEL ROOMS
CHANGING THE SEGMENT	TARGET COSTING	• XIAMETER
	SELF-SEGMENTED FENCING	• GROCERY COUPONS

current examples are in the airline industry. Under the International Air Transport Association's old regime, the price of a ticket included a full range of services. As the market was deregulated and price wars intensified, new carriers such as Southwest Airlines, EasyJet, and Ryanair offered lower prices and fewer services. Established carriers had a hard time competing because their offerings were inherently bundled, forcing them to charge higher ticket prices. They have recently started unbundling, charging separate fees for checked bags, seat reservations, food, and extra legroom. (Ironically, the low-cost pioneer Southwest is now known for carrying bags at no added charge.)

An *all-inclusive offering* is a variant on bundling—think of it as an "ultrabundle." A bundle offers a combined price for the sake of convenience or to induce customers to buy more elements. An all-inclusive offering combines elements that customers might not normally regard as components of one solution but that they are obliged to buy because of the time frame or setting. Cruise ships, for instance, offer all-inclusive deals that cover meals, entertainment, and sleeping quarters—purchases that are not ordinarily linked but that in the course of a cruise can hardly be made elsewhere. Another example involves the company Châteauform', whose name itself bundles parts of the French words for "castle" and "training." Châteauform' offers executive seminars in European resorts. It captures maximum value by handling room reservations and dining, subsumed under a single, fixed fee. (After a long workshop, many a manager is happy that wine and beer are included.)

One value-capture innovation, auctioning, can yield prices the seller would never have had the audacity to name.

Changing the timing. The preceding innovations all assume a fairly simultaneous exchange of value. But some famous cases of "desynchronized" exchange also suggest ways to innovate.

Installed base pricing is probably best known as the razor-and-blades model. Gillette's customers, for instance, initially buy a razor and blades together for a low price, probably receiving much more value in that transaction than they pay for. But the company effectively charges for the razor in every subsequent purchase of blades. Ink-jet printers use a similar model: The printer is cheap, but the replacement cartridges are expensive. Elevator companies apply the same logic. Schindler can install elevators at a very competitive price because the installation comes with a profitable 10-year service contract. As these examples indicate, changing the timing is usually tied to a price-carrier change; indeed, the model might be seen as a special instance of a price-carrier innovation. Certainly it requires the company to secure its future revenue stream: If printer customers started buying ink-jet cartridges from third-party suppliers, the business would not be sustainable.

A second approach to changing the timing, *futures contracting,* offers an even purer form of desynchronizing the value exchange. About 150 years ago farmers in the U.S. Midwest began selling their harvests in advance. They received cash immediately, while buyers secured a certain amount of wheat or corn for a preset price. Selling futures on commodities is now a high-volume practice. The innovation opportunity is for other sellers to adopt the approach when future needs can be anticipated. For example, a hotel chain might presell to a corporation the number of rooms it knows the firm will need; a chemical company might contract in advance for the delivery of a certain quantity of materials at a given price.

Changing the segment. The first four categories of innovation capture value within the existing customer base. The fifth captures it from customers new to the firm or the market. This path starts with two steps: Identifying customers who are unwilling or unable to pay current prices but display a need for a given offering, and then determining how to create a profitable offering for them.

The textbook marketing approach suggests conducting a market analysis to define objectives before defining strategy. It requires segmentation, targeting, and positioning to arrive at a marketing plan, including product, price, place, and promotion decisions. In contrast, *target costing* uses market analysis to gain customer insights and then determines the price at which a certain segment of the market will buy a certain product. With that price in mind, the company designs the product at a cost that ensures a sufficient margin. A prime B2B example is Xiameter. In the course of a customer-insight project, Dow Corning, one of the largest producers of industrial silicone, identified four needs-based segments of the market. Among customers seeking innovative solutions, proven solutions, or cost-effective solutions,

it was well positioned. It was much less competitive among those in the fourth segment, price seekers—customers uninterested in features and services and focused solely on obtaining the lowest price. To address that segment without weakening its value proposition to the others, Dow Corning created not just a new offering but a new brand, one with a substantially different business model. Xiameter is an internet-based platform that offers silicone without also providing consulting and other related services, thus permitting a very different pricing approach.

A second means of innovation through segmentation involves self-segmentation. Segmenting according to willingness to pay may be illegal; at the least, it is perceived as unfair. Charging different prices for similar products may lead customers who once bought a premium brand to switch to a low-cost version. Further, it is not easy to identify and group customers according to their willingness to pay. The solution, which I call *self-segmented fencing,* has two parts: First, customers self-segment by choosing either a high- or a low-priced offer. Next, the firm creates a fence in order to prohibit arbitrage, such that customers with a high willingness to pay are prevented from buying the low-priced product. Coupons are an almost perfect example of a fence. Instead of selling groceries at low prices to everyone, retailers offer coupons that discount specific products for specific periods of time. The hassle of finding a coupon, checking its validity, searching for the exact item offered, and presenting the coupon at checkout fences off customers who prioritize saving from those who are more interested in convenience.

Focusing Managers on Value Capture

The innovation pathways I've described are not mutually exclusive; often approaches can be combined. Nor are all of them applicable to every market. The point of this categorization, developed through simple pattern recognition, is to help executives innovate in value capture by suggesting new possibilities.

The process begins with top management's communicating a concern to the organization: Are our innovation efforts fairly balanced between value creation and value capture? Senior leaders must stress that fresh thinking about value capture should be integral to every strategy and innovation exercise in the firm.

A core team might then be assigned to rethink how to capture value and challenge the status quo. Having a dedicated team creates a sense of urgency and lets members develop a common language for discussing ideas. Such a team should be cross-functional, because value-capture innovations are likely to traverse lines between R&D, strategic planning, market research, IT, legal, and more. Beyond the core team, anyone in the company responsible for defining and executing strategy should be invited to join a network that is kept apprised of the team's work and routinely asked to offer ideas and feedback.

In the course of a year, the core team should devote at least one full day to envisioning value-capture innovations, perhaps using the framework presented here as a basis for brainstorming. When a large European airline staged such a workshop for its managers, the group quickly surfaced new possibilities. One participant wondered, "What if we sold contracts based not on tickets but on miles, so that a large client might buy a million miles for a fixed amount regardless of the routes?" Another idea sounded wild but provided a logical solution to a backhaul problem: "Should certain routes be offered free on certain days?" Not every idea proved to be compliant with regulations or profitable enough to pursue, but one result alone—a new approach for a specific customer segment, small and medium-sized enterprises—made the entire exercise worthwhile.

In a workshop for a services firm with more than 250,000 employees worldwide, the CEO challenged his top team to imagine how the operating margin, which had dropped to 5.5%, could be expanded—not just to 5.7%, say, but to 9.5%. Over two days the group discussed 24 value-capture innovations. The cases were presented in six batches, each followed by a two-hour exploration of how the firm might make similar changes. Several concrete follow-up actions emerged. Although none gave the firm a margin of 9.5%, the margin's decline was slightly reversed.

My work with more than 50 companies in dozens of countries has confirmed for me that businesses have spent far more time, money, and effort on value-creating innovations than on value-capturing ones—and that much can be gained by correcting the imbalance. When a driver eagerly pays 135,000 francs for a special license plate, it suggests that many sellers may not be capturing nearly as much value as they have already produced. When a coffee lover happily spends $137 for a kilo of coffee, it reminds us that new value can be created—and captured—when customers' needs are better understood. What opportunities to capture value are you missing?

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PROFITS AT THE BOTTOM OF THE PYRAMID

A TOOL FOR ASSESSING YOUR OPPORTUNITIES *BY ERIK SIMANIS AND DUNCAN DUKE*

During the past decade, many multinationals have come up short trying to make a profit by solving the pressing needs of low-income communities. Preoccupied with their social missions, companies have optimistically taken on challenging projects, only to be surprised when weak consumer demand and obstacles such as bad roads

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keep revenues low and costs high. Overstretched and disillusioned, many switch gears and reconstitute their ventures as break-even social investments that are destined to remain small.

Profits are critically important for ventures targeting the bottom of the economic pyramid—the more than 4 billion people who individually earn less than $1,500 per year. Compared with a social responsibility project, a profitable business stands a better chance of being able to increase its scale and impact. It can command resources and be sure of continued support from both the corporate headquarters and the country office.

Profitably selling to the bottom of the pyramid is difficult, but it can be done. It requires companies to focus on business fundamentals and start their ventures with a rigorous understanding of two key challenges in low-income markets: *changing consumers' behavior* and *changing the way products are made and delivered*. Companies that underestimate these hurdles miscalculate the resources, innovation capabilities, and time involved, and project teams end up poorly equipped to accomplish the task.

To help companies ensure that their ventures are built for success, we have developed an "opportunity map": a framework, drawn from our experience and research in Africa, Asia, and Latin America, that uses these two key challenges to organize bottom-of-the-pyramid opportunities by their cost and complexity. With the map, companies can design and undertake ventures that match their resources and financial expectations—and make profits, too.

Some companies may find that the map warns them away from launching headline-grabbing ventures. That's no reason for disappointment. It's smarter to aim first for smaller-scale, incremental sales opportunities that stand a better chance of success. A steady flow of profits, however modest, will then allow companies to tackle riskier growth opportunities with greater social impact. Putting profits first is the most effective and sustainable way for companies to make a positive impact on the lives of the poor.

The Hurdles in Poor Markets

Let's start by delving into the two main challenges: changing consumers' behavior and rethinking the way products are made and delivered to customers. These are not only the most common hurdles companies face in bottom-of-the-pyramid markets, they're also the most widely underestimated.

Consumer behaviors that have to change. People resist new products for a variety of reasons, but the biggest is a reluctance to alter deeply ingrained mind-sets and routines. The greater the novelty, the greater the disruption, and people with limited means and limited product experience see extreme novelty in many products.

For example, consumers in sub-Saharan Africa have responded poorly to insecticide-treated bed nets, despite the technology's simplicity and effectiveness in preventing malaria. Companies such as Sumitomo Chemical have had a tough time changing misconceptions about how malaria is transmitted and persuading consumers to hang and take down nets every day (apart from the inconvenience, the nets are hot to sleep under).

Even if a product is familiar, delivery through a new business model might pose an obstacle. Many villagers are used to taking loans from traditional moneylenders, for example, but switching to microfinance represents a big change. In most microfinance models, people must participate in borrowing groups, an activity that takes time and cooperation, and the entire group is responsible for loan repayments.

To successfully educate consumers about new or untried products, companies often have to work with them over sustained periods. Sometimes it's necessary to create consumer groups in order to harness peer pressure and build support for new behaviors. Generating widespread demand can be complex and time-consuming, driving up marketing and sales costs and increasing working-capital requirements.

Company routines that have to change. Value chains may need to be reconfigured to reach low-income buyers. Customers may require lower price points than the company can meet. They may not have access to the retail outlets where the company sells its products. They may not respond to traditional marketing strategies. Or they may live in rural areas or slums, where business units may be unable to operate at large scale because of poor infrastructure. The more far-reaching the needed changes are, the more complex, time-consuming, and costly they are to manage.

The French eyeglasses company Essilor International provides an example of the challenges posed by the need to significantly alter value chains. The company initiated a pilot program to serve some of India's 6,000 rural villages, using vans set up as

Idea in Brief

THE PROBLEM
Multinational firms' socially beneficial ventures in low-income markets need to earn profits if they're to command corporate resources, but operating in the black is harder than it looks.

THE SOLUTION
Companies can use the authors' "opportunity map" to design and undertake ventures at the bottom of the pyramid that match their capabilities and financial expectations.

THE DETAILS
The map sorts ventures according to cost and complexity by analyzing two key challenges in selling to the poor: changing consumers' behavior and changing the way products are made and delivered. The map can encourage companies to forgo overly ambitious, unsustainable projects and start with smaller ones that generate steady profits.

eye clinics. However, despite efforts to streamline sales operations and outsource production, the company has struggled to generate enough revenue to cover the costs of the vans ($50,000 each) and offset expenses such as optometrist training. Consequently, Essilor's plans for expanding the program have stalled.

SC Johnson, the household-products company behind such brands as Glade, Windex, Raid, and Ziploc, was among the first corporations to take seriously the long-term strategic potential of selling to the world's poorest people. Having operated in Kenya since the 1960s, it sought to establish a sustainable business that would improve the health and lives of residents in the slums of Nairobi. Working with researchers at Cornell University and elsewhere, the company embraced an exploratory, co-creation approach in order to ensure that its offerings would match consumer needs. (Disclosure: We were involved in the project during its first three years, starting in 2005.)

Research revealed that consumers wanted to rid their homes of insects and sanitize pit latrines. This led SC Johnson to form a home-cleaning service that used several company products, including cleaners, insecticides, and air fresheners. Sales and labor were performed by youth groups that were already providing trash collection services. However, consumers were so accustomed to their surroundings that the offer of a "clean and healthy home" didn't resonate, and local norms were a deterrent to inviting strangers inside.

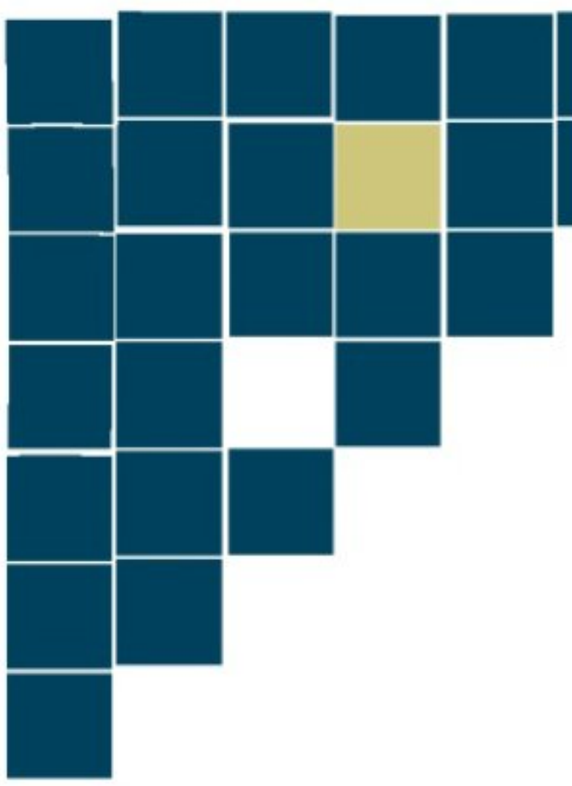
Undaunted, the team switched to providing a service cleaning toilets in schools, housing developments, and other facilities. But recruiting workers from the slums and training them to consistently do a high-quality job proved costly and time-consuming. There were complications importing SC Johnson's products in bulk and establishing a franchise agreement with the local business unit. Moreover, the company was in the process of converting its Kenya office into a lean sales outpost, which didn't match the venture's long investment time line and resource needs.

Although the cleaning business acquired a number of customers and delivered on its service promise, it did not meet its financial objectives and could not be considered a viable business investment for the company. SC Johnson ended its financial support of the effort and helped it transition into an independent nonprofit.

The lessons learned in Nairobi proved valuable when SC Johnson went on to another bottom-of-the-pyramid venture: promoting the use of insect-control products in rural Ghana, with the goal of helping prevent malaria. The company recognized two main challenges: Consumers didn't understand malaria's cause, and the villages lacked distribution channels.

In response, SC Johnson created a direct-sales model with coaches providing hands-on product demonstrations in homes and at gathering places in the community, thus building social support. Insect-control products were bundled with other items that consumers valued, such as air fresheners, which made sales more likely. In addition, buyers were given refillable containers, which reduced packaging costs. And subscription pricing, together with loyalty rewards, ensured that customers used products multiple times, thereby becoming more comfortable with the new product routines.

Changing consumers' behavior and rethinking the way products are made and delivered are the most common hurdles companies face in bottom-of-the-pyramid markets.

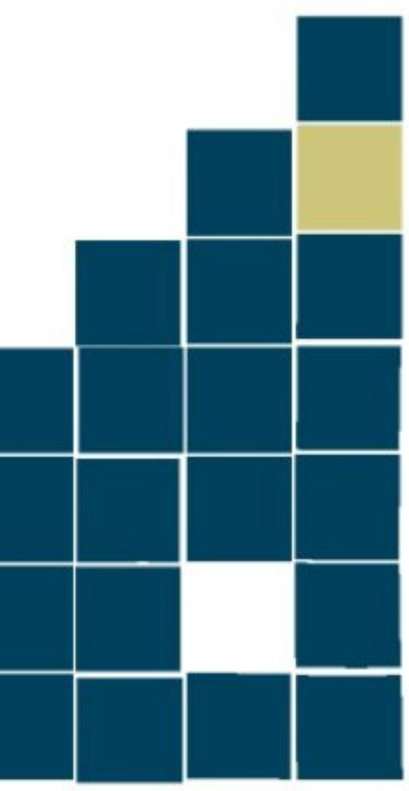


Creating this high-touch channel, and selling products in a refillable format, required new capabilities. Designers and R&D personnel worked closely with the business unit on the ground to ensure that product formulations and formats met margin requirements. The team also considered such matters as how salespeople would dispense products. The project had a strict time line for assessing proof of concept, and the field team was given a clear payback schedule in order to track the business's performance. (See "Reality Check at the Bottom of the Pyramid," HBR June 2012.) Because of all this groundwork, the Ghanaian project has so far been largely free of the tribulations that plagued the Kenyan initiative, and the pilot has made promising strides.

The Opportunity Map

Lessons learned by SC Johnson and other companies helped us create our opportunity map. We've parsed business prospects at the bottom of the pyramid into nine types (see the exhibit "Nine Kinds of Opportunities"). Below we outline a typical scenario and present an example for each, starting with the least complex and resource-consuming and ending with the most.

The objective of new channel creation is to establish a parallel means of distribution, such as Fan Milk's bike-riding vendors in West Africa.



Targeted marketing opportunity. Because of a knowledge gap, consumers are underutilizing a product that can be bought through traditional retail channels. The goal is to boost short-term consumption of that product while strengthening the company's brand in an up-and-coming mass-market demographic.

Dialog, Sri Lanka's largest provider of telecommunications services, had low sales among the rural poor, despite the fact that its mobile phones and telephone cards were readily accessible through a network of 40,000 small-scale retailers. Village dwellers couldn't relate to the always-connected lifestyle these products made possible, and they were unaware of the full range of mobile services the company offered. To increase penetration, Dialog created a network of trained women "infomediaries" who coach villagers in the use of mobile phones and help them gain the confidence and capacity to take advantage of Dialog's services.

Product redesign. Although bottom-of-the-pyramid consumers are buying a version of the product through the same channels as mainstream customers, the company could enhance the product to meet additional needs and boost the overall value proposition. The goal is to capture greater market share with a category-leading product.

In 2011, after market research revealed that poor adolescent girls in India often suffer from iron deficiency, PepsiCo worked closely with consumers in two districts in Andhra Pradesh to create a line of iron-fortified cookies and snack puffs under the brand Lehar Iron Chusti (Lehar Iron Health). To appeal to the wide variety of palates across the country, Pepsi began releasing a new flavor every month.

Distribution extension. Bottom-of-the-pyramid urban consumers with access to a company's sales channels are buying its product in an existing format, but those who live beyond the company's reach in peri-urban areas and larger market towns might also value the product. There is some modern infrastructure in the targeted areas, and a few businesses and government organizations are operating at scale. The objective is to harness existing nontraditional channels that can quickly and easily reach consumers.

In parts of rural India, Bajaj Allianz General Insurance has partnered with SKS, India's largest microfinance institution, to approach the husbands of SKS's female customers and sell them a life insurance policy that also functions as a savings instrument. In the first 10 months of 2009, Bajaj sold 1.8 million policies, generating premium income of $33 million.

New channel creation. A large rural population living beyond the reach of a company's sales outlets may be using products that provide the same core functionality as the company's offering. The objective is to build, from the ground up, a parallel distribution and sales channel that can penetrate hard-to-reach rural areas.

The Danish-owned West African dairy company Fan Milk established a street-vendor model to make its frozen dairy and juice products available in rural areas where there are no cold-storage facilities. Vendors purchase Fan Milk bicycles and pay for products before they sell them. The company provides product training and free bike repair services. Fan Milk supports approximately 25,000 vendors in West African countries, including Ghana, Ivory Coast, Nigeria, and Burkina Faso.

New product development. A company sees an unmet need that dovetails with its product-development capabilities. Consumers are using low-quality substitutes that lack key functionality or don't stand up to challenging environmental conditions. The goal is to establish a competitive advantage in a mass-market category by designing and engineering a product to be affordable and robust.

In 2009 Godrej Appliances launched the Chotukool, a revolutionary portable refrigerator for the rural Indian market, where a third of all food is lost to spoilage. By using a solid-state cooling chip and eliminating the compressor, the company reduced power requirements to a mere 62 watts and cut the price for an entry-level refrigerator in half, to just $69. The product runs on a battery, weighs less than 10 pounds, and keeps food fresh and cool at temperatures between 40 and 60 degrees Fahrenheit. Today multiple versions of the Chotukool are produced and sold through retail channels reaching consumers across socioeconomic levels.

Conquest of competitors' market. A growing industry made up of small and medium-size enterprises is serving poor consumers in an area where the company has no operations, and in order to be competitive, the company's product requires only minor modifications. The strategic objective is to use the company's economies of scale to outstrip local competitors and capture significant market share, thereby establishing a platform from which to expand to other markets.

Grupo Bimbo, the world's largest baked-goods company, expanded from its home base in Mexico to China, Brazil, and other South American countries in the early 2000s, mainly by acquiring local bakeries. As it adapted its products and brands to each market, it sought to make use of its investments in operational and distributional capabilities. While its Mexican plants are among the largest and most flexible in the industry, it has often had to upgrade the facilities acquired abroad in order to meet its standards. In China, operational changes improved productivity on some lines by 300%.

Greenfield-market expansion. The company already serves bottom-of-the-pyramid consumers in one area, but it could tailor its core offering and business model to meet the needs of similar consumers in a different area. The goal is to use the firm's operational skills to establish a market-leading position in a region of long-term interest.

When BRAC, a world leader in social and economic development, expanded from its home base in Bangladesh to East Africa, it replicated some signature innovations, such as creating large-scale microfinance programs and training promising women participants as community health entrepreneurs. In Uganda and Tanzania, BRAC's Essential Health Care program has been adapted to address the health priorities of the region, including malaria and HIV/AIDS. BRAC has since grown to become the largest development organization in Uganda, as well as one of its largest microfinance institutions.

New business-model development. The company believes the core functionality of its current product would be valued by a large rural consumer market; consumers may be using substitutes that are costly and inefficient. The company's current product, however, is priced beyond their means, even with extensive cost cutting. Furthermore, the company's business model requires infrastructure that is absent in the targeted area. The strategic goal is to establish first-mover advantage in a large, latent market by scouting and securing choice assets and limited partnerships.

Hindustan Unilever took a decade to incubate its first consumer durables, the Pureit family of water purifiers—innovative gravity-fed, tabletop devices guaranteed to kill germs. Targeting both low- and middle-income Indian customers, HUL developed four new routes to market, including an outsourced "demonstration workforce" of 10,000 people to pioneer its direct-to-home distribution and customer-education channel. After launching the Pureit brand nationally, in 2008, HUL sold more than a million units in the first year.

New market creation. The company believes there's an unmet need among a large population of low-income consumers living in hard-to-reach rural areas. There are no substitutes in the market, and consumers are largely unaware of the need for the product. The strategic objective is to nurture the creation of a new market intimately tied to the firm, placing the company's brand in a powerful position. SC Johnson's Ghana venture is a good example of this opportunity type.

A Multipronged Approach

Several of these opportunities often present themselves simultaneously. Smart companies take a portfolio approach, following up on each according to its manageability and potential for return.

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Nine Kinds of Opportunities

The nine opportunity types fall into three main investment classes: mature markets, growth markets, and frontier markets, shown in different shades below. As you move away from the bottom left corner, the opportunities become increasingly complex and resource-intensive, because they require more consumer learning and value-chain modification. New market creation is the most challenging opportunity of all.

That's the case with the French industrial giant Lafarge, the world's largest cement manufacturer. The company's long-standing commitment to sustainable economic development and to meeting the developing world's burgeoning housing needs led it to create a dedicated affordable-housing team based at its Paris headquarters. The team works closely with local offices in target countries to pilot-test ventures that complement local strategic priorities and address broader innovation objectives.

One of the company's ventures—a mature-market opportunity—is aimed at strengthening Lafarge's competitive position in retail stores, where it sells most of its bagged cement and competes aggressively for shelf space. In an effort piloted in Indonesia and Nigeria, Lafarge links retailers with microfinance organizations so that the stores can offer home-improvement loans and construction support to low-income consumers. Lafarge's primary investment is in a team of home-improvement "counselors" who market the service through channels such as information kiosks set up in stores. The counselors also connect customers to architects and other experts, provide advice on building materials, and ensure that borrowed funds are actually used for building.

In India, Lafarge is pursuing a growth-market opportunity involving the creation of a new sales and distribution channel. This venture aims to bring 15-liter bags of high-quality, ready-mixed concrete to the doorsteps of slum residents seeking to build homes. To overcome consumers' resistance to paying for the transportation and mixing of the concrete, which they could take care of themselves, Lafarge focuses on saving consumers time and reducing wasted concrete, which help them save money. The company pledges to deliver the product within 50 minutes of the time an order is called in. To meet the value-chain challenges, Lafarge has designed mini-plants that can be located near slums. Its product developers have also redesigned the product formulation and packaging so that the bags of concrete can withstand transportation in three-wheelers. This combination of strategic features presents a formidable entry barrier for competitors.

A third project for Lafarge is a greenfield-market expansion. Although the low-income consumers this venture targets live in wealthy, industrialized countries, it is every bit a frontier-market investment. It aims to drive sales by selling to developers an affordable-housing solution designed for the hard-to-build-on plots of land that represent the majority of unbuilt space in established city centers. The company has created a demonstration project in a municipality in southwestern France: a multistory concrete shell in which homes, gardens, and green spaces are attractively nested on every level. By tackling a high-profile political issue (affordable housing), the venture overcame one of the project's value-chain challenges—namely, spurring interest and awareness among municipalities and developers. Given the long time line and uncertain cash flow, project oversight extends to the company's CEO.

BOTTOM-OF-THE-PYRAMID OPPORTUNITIES come in a variety of shapes and sizes, but successes demonstrate a recurrent lesson: the value of focusing on profits. Blinded by devotion to social missions, too many companies with grand ambitions overlook profitable opportunities that match their resources and skills and jump into ventures that overwhelm their capabilities. A more realistic assessment of the challenges at the bottom of the pyramid can help companies generate the profits that will make socially beneficial businesses sustainable over the long term.

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"I thought it might help."

CARTOON: TERESA BURNS PARKHURST

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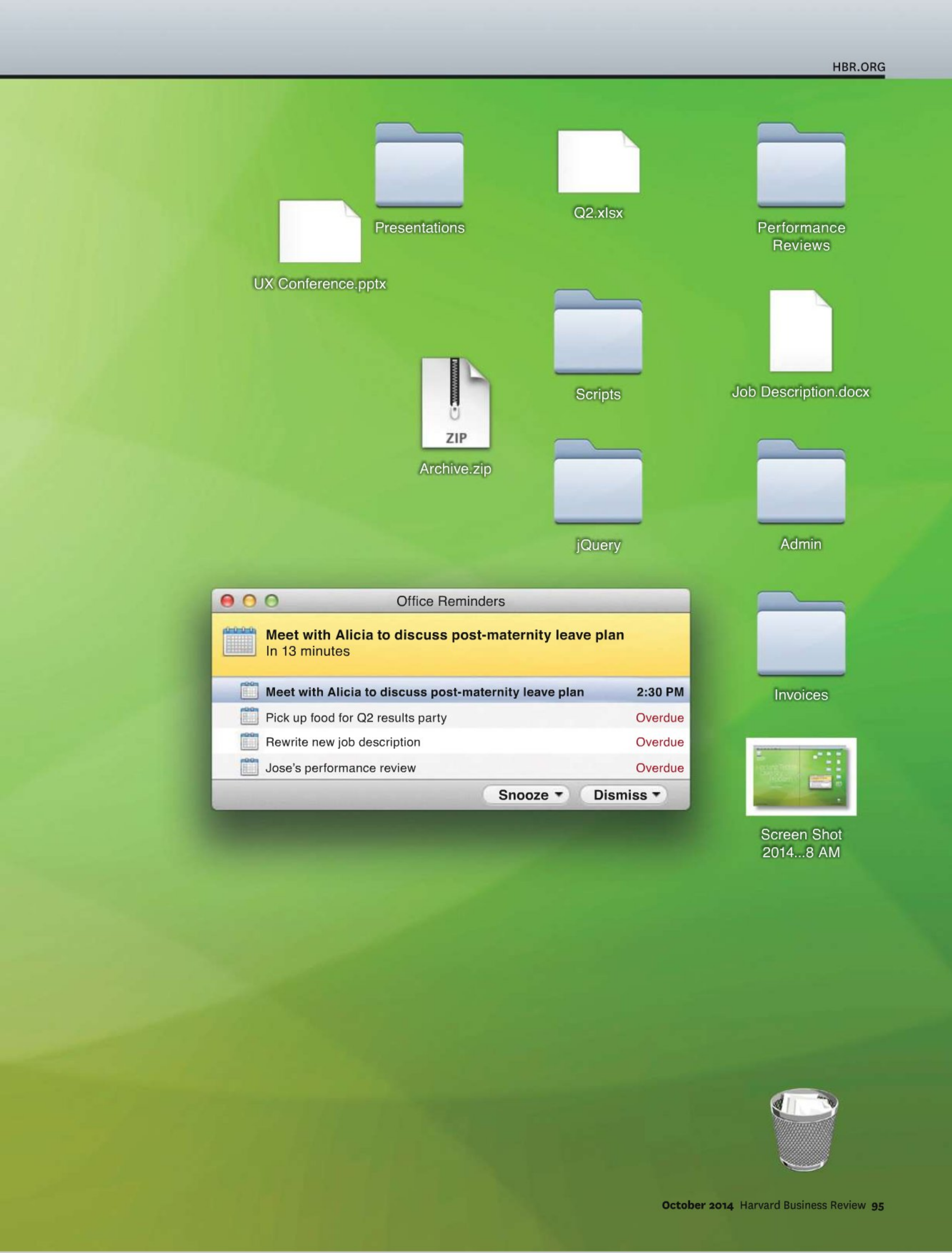
Joan C. Williams is a Distinguished Professor of Law, the Hastings Foundation Chair, and the founding director of the Center for WorkLife Law at University of California Hastings College of the Law.

Hacking Tech's Diversity Problem

To bring more women into the sector, companies should try a lean start-up approach.

by Joan C. Williams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When Google, Yahoo, LinkedIn, and Facebook disclosed their woefully low levels of female employment in the summer of 2014, admitting that they had a lot of work to do to improve them, they signaled a shift for the technology industry. It's remarkable that the sector is finally stepping up to the plate on diversity—and refreshing that its focus is on metrics rather than rhetoric.

Make no mistake: Improving those metrics will be challenging. A key feature of the tech culture—the shared belief that it's a meritocracy—may work against change. An important study by Emilio J. Castilla and Stephen Benard has shown that when an organization's core values state that raises and promotions are "based entirely on the performance of the employee"—in other words, when a company sees itself as a meritocracy—women are actually more likely to get smaller bonuses than men with equivalent performance reviews. Subtle biases against women are clearly at work here. Moreover, 40 years of social science have taught us that such biases will be perpetuated unless they're *intentionally* interrupted, and people who think they work for meritocracies are less likely to do what it takes to interrupt them.

On the other hand, if tech's senior leaders are serious about gender diversity, they could be perfectly positioned to lead change. As they so often remind us, they're not about business as usual. They're out to change the world, with corporate mottoes like "Don't be evil" and "Move fast and break things." One thing I hope they'll break with is the "diversity industrial complex": the standard approach of making token hires, offering sensitivity training, setting up mentoring networks, and introducing other incremental changes that focus on altering women's behavior to, say, make them better negotiators. When an organization lacks diversity, it's not the employees who need fixing. It's the business systems.

This article is intended to help tech companies—and others—fix those systems. It describes a new metrics-based approach that pulls from the lean start-up playbook: Collect detailed data about whether gender bias plays a role in daily workplace interactions; identify company-specific ways to measure its effect; create hypotheses about what "interrupters" might move those metrics; and then throw some spaghetti at the wall and see what sticks. Measure what happened, adjust your hypotheses, and do it all over again until you get it right.

What's a Bias Interrupter?

While much of the social science research is still devoted to "admiring the problem"—demonstrating the same patterns of gender bias over and over—some studies have begun to explore how to interrupt bias effectively. In one, researchers Andreas Leibbrandt and John A. List posted two versions of announcements for administrative assistant jobs in stereotypically masculine businesses—NASCAR, football, and basketball. One version said nothing about salary; the other said "salary negotiable." Leibbrandt and List wanted to investigate the well-documented phenomenon that women are less likely to negotiate their salaries than men, which contributes to the pay gap between the sexes. Could a simple two-word phrase interrupt that pattern?

It could. In fact, not only did the "salary negotiable" language close the negotiation gap between men and women, it closed the pay gap between the male and female hires by 45%.

This experimental approach is a classic example of a bias interrupter: It changed the basic business system in a way that stopped a pattern of bias in its tracks. And it did so without talking about bias at all (or even raising it). It also highlights three advantages that bias interrupters have over the sweeping cultural change initiatives that researchers who study organizational bias tend to recommend. Such efforts can be effective, but they're expensive—and often abandoned when a new CEO arrives with different priorities. Recently, for instance, Best Buy's new CEO eliminated the company's much-ballyhooed Results Only Work Environment, despite rigorous data documenting its business benefits.

ILLUSTRATION: ISTOCKPHOTO (BACKGROUND); PHOTOSHOPEDIA, EVERALDO COELHO, AND ALESSANDRO REI (ICONS)

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Idea in Brief

THE CHALLENGE
The technology industry has a well-documented diversity problem. But previous efforts to fix it—through sweeping cultural change initiatives or well-intentioned mentoring programs—have failed.

THE ANALYSIS
Biases that hold women back include prove-it-again!, the tightrope, the maternal wall, and the tug-of-war. Forty years of social science research have shown that biases like these will persist unless they are interrupted.

THE SOLUTION
Leaders need to design "bias interrupters"—changes to essential talent management systems that stop patterns of bias in their tracks. By redesigning how rewards and assignments are handled, managers can be sure they're retaining their best and brightest.

First, bias interrupters are based on objective metrics, whereas cultural initiatives tend to rely on earnest conversations. Second, interrupters are iterative, so they allow companies to try small interventions and then scale them up. Last, interrupters build change into the basic business systems that perpetuate bias, so they are less likely to disappear when a new CEO decides that diversity is not an imperative.

While the evidence of the effectiveness of interrupters is growing in social science literature, the effort to systematically pilot and test them in companies is just beginning. I've started to work with several companies, including Twitter and the Silicon Valley law firm Fenwick & West, on a model for building bias interrupters. With Jennifer Berdahl from the University of British Columbia, I'm also forming a working group to explore interrupters with other social scientists. It's still early days, but here's the approach I'm using to help companies identify, measure, and address diversity-related bias.

STEP #1
Determine Whether There's a Problem

The first step is to find out whether women in your organization are encountering one or more of the four basic patterns of gender bias. Here's a quick primer:

Prove-it-again! Women often have to provide more evidence of competence than men do to be seen as equally capable, a problem documented in scores of studies on double standards, attribution bias, leniency bias, recall bias, and polarized evaluations. About two-thirds of the 127 professional women that I and Erika Hall, now a professor at Emory's Goizueta Business School, interviewed for the book *What Works for Women at Work* reported prove-it-again problems. Our interviews additionally suggested that women in tech often get promoted but don't get the title or salary that typically accompanies the new job, and that women's technical expertise is dismissed the minute they are no longer in technical roles. "We're constantly asked 'if you write any code' when speaking about technical topics and giving technical presentations, despite just having given a talk on writing code," note the authors of the widely circulated "Open Letter on Feminism in Tech."

Tightrope. This is the kind of bias faced by the female salary negotiators. High-status jobs are seen as requiring stereotypically masculine qualities, while women are expected to be modest and self-effacing, so women must walk a tightrope between being seen as too feminine to be effective and too masculine to be likable. Nearly three-fourths of the women we interviewed reported tightrope issues, with twice as many reports of "too feminine" as "too masculine" problems. Classic "too feminine" problems are large loads of "office housework"—which includes fetching documents, planning parties and conferences, and cleaning up messes, literally and figuratively—and assignments to do undervalued tasks. In tech, power and prestige lie with those who "own the code"; even very talented women end up in marketing or project management roles instead. Yet a woman risks being seen as "not a team player" if she turns away work that men are rarely asked to do. (See the sidebar "'Housework' vs. 'Glamour Work.'")

In addition, when women are direct, outspoken, competitive, or assertive—rather than "nice"—they often face a backlash, including what one researcher called "the sexual harassment of uppity women" in a study showing that dominant women actually experience the most harassment. There's an avalanche of sexual harassment in tech, ranging from "angry e-mails that threaten us to leave the industry,

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because 'it doesn't need any more c***s ruining it'" to "booth babes" and networking events held in strip clubs. This "brogrammer" culture has pushed many women out of the field. In 1985, 37% of computer science degrees were awarded to women; in 2012 only 18% were. In 1991 women held 37% of all computing jobs; today they hold only 26%. Forty-one percent of women leave tech companies after 10 years, as opposed to 17% of men.

There's an avalanche of sexual harassment in tech. The "brogrammer" culture pushes many women out of the field.

Maternal wall. Bias triggered by motherhood has dramatic effects. In one famous study subjects evaluated pairs of equally qualified candidates, one of whom was a mother. The subjects received identical résumés, but the candidate who was a mother varied. The researchers found that mothers were 79% less likely to be hired, half as likely to be promoted, offered an average of $11,000 less in salary, and held to higher performance and punctuality standards. Another study looked at mothers who were considered indisputably competent and committed. Because of their dedication to the job, they were seen as bad mothers and bad people. As a result, they were disliked and held to higher performance standards.

A common take is that the long-hours culture drives mothers out of tech, but often what drives them out is sexism. As one woman told me, "Women...29, 30...were hitting the glass ceiling that I've been hitting for a long time. And if they could [afford to]..., they would just start having babies and drop out because they wanted to have kids anyway, and it's hard to show up every day and fight and fight and fight." While many women in tech have praised the industry for allowing flexible hours and remote working arrangements, mothers remain suspect. Take the recent flap when Marissa Mayer, the CEO of Yahoo, was late to a meeting. The only reason that story made the news is that it confirmed the stereotype that mothers aren't suited to be CEOs. Fifty-nine percent of the mothers Hall and I interviewed reported experiencing maternal wall bias.

Tug-of-war. This pattern, reported by 45% of the women interviewed, occurs when gender bias against women fuels conflict among women. Research shows that women who encounter discrimination early in their careers tend to distance themselves from other women, refuse to help them, or even align themselves with men at other women's expense. Distancing oneself from complaints against sexism becomes an emblem of loyalty. "I'm not a girl at Google; I'm a geek at Google," was Marissa Mayer's standard response to questions about what it was like being one of the few female programmers at the company. Today, when asked how we can encourage more women to become engineers, Mayer responds that her focus is getting more men and women to become engineers. The Open Letter protests that its authors have been "paraded around by men in the industry for how nice we've been in trying to address the social problems in tech as a way to discredit more vocal, astutely firm feminist voices. We don't like this, we've never liked it, and it needs to stop."

Organizations need to find out how, if at all, these four patterns affect women's careers internally. A good place to start is with confidential interviews or focus groups conducted by an expert in the patterns of bias. Obviously, the people in a focus group have to trust one another not to disclose who said what. One organization I'm working with has so few women that they all know one another—and already agree that there's a problem. The idea that the women in their company already discuss these issues freely with one another often surprises male senior executives—and so do the focus group results.

STEP #2
Identify Key Metrics

Your internal research will often bring to light ways to measure the problem, which you can use to identify a baseline and track the results of changes. In one organization in which internal referrals play a major role, women suggested an elegant metric: Ask both men and women if they got their last five opportunities from inside or outside the firm. In this organization and many others, senior men typically staff their teams with people they feel comfortable with—people like themselves. (It's called "in-group

favoritism.") Assumptions that "men have families to support" and that "mothers do not want stretch assignments" also play a role; examining how assignments are distributed can surface some of these.

If the problem's office housework, the metric will be different. One organization that identified this as a major issue proposed setting up a list of low-profile tasks (List A) and high-profile ones (List B). The plan was to ask men and women what percentage of their time was spent on tasks from List A versus List B.

With maternal wall bias, it's key to track how women's assignments differ before and after maternity leaves. At the Center for WorkLife Law, which I direct, we frequently hear that women returning from maternity leave get fewer or poor-quality assignments. (The result, of course, is that they quit.)

The right metrics will differ from organization to organization, depending on the types of bias uncovered and the strategic goals of the firm. But it does make sense to be systematic. Any firm undertaking this work should think carefully about four processes: how people are hired, how work is assigned, what happens during performance evaluations, and how compensation is determined. In addition, it should look for cultural markers that exclude outsiders. In tech, that's the oft-celebrated "brogrammer" culture. Companies should go beyond the classic "body counts," which simply note the number of women but don't tell you why women didn't get hired, why they don't get promoted, or why they leave sooner than you want them to (if they do).

STEP #3

Experiment, Measure Success—and Keep Trying

Once you've assessed bias and identified key metrics, the next step is to interrupt the bias, see whether the metrics improve, and then—if no improvement occurs—ratchet up to stronger interventions. The ideal interrupter is like the one in the Leibbrandt/List experiment: easy to do and not requiring training on, or even a discussion of, gender bias.

Another good example of a successful interrupter comes from Google. The company's analytics showed that women were being promoted less often than men because, to be promoted at Google, you needed to nominate yourself. Fewer women did so, presumably because modesty is so associated with femininity that women who advocated for themselves often encountered pushback, just as with negotiation. Google's response was to include female leaders at workshops on when and how to put yourself forward. This signaled to women that they were expected to self-promote. So they did, and the gender difference among Googlers nominating themselves all but disappeared.

One organization I've spoken with is concerned about whether gender bias is affecting performance evaluations. The Center for WorkLife Law proposed reading its performance evaluations to spot patterns of bias. The company's executives sensibly suggested starting off with a staff meeting explaining that they're committed to improving the quality of performance evaluations, and introducing the four patterns. Great idea: Accountability causes more people to interrupt automatic bias more often.

What happens if you find bias—how should you present it to the people involved in the relevant processes? Obviously, it's important to design feedback

"Housework" vs. "Glamour Work"

In many companies, women are expected to do disproportionate amounts of "housework," which includes both domestic tasks, like planning parties, and undervalued tasks, such as those listed below.

INDUSTRY	HOUSEWORK	GLAMOUR WORK
High tech	Managing projects	Writing the code
Law firms	Being a "service partner" who does the actual legal work	Bringing in clients
Consulting	Managing projects, delivering work, mentoring colleagues	Developing new business, managing C-suite relationships, serving as subject matter experts
Investment management firms	Handling logistics on pitches, working for low-profile clients	Making investment decisions, executing high-profile deals, managing key client relationships
Academia	Being dean of students or on the admissions committee	Publishing in prestigious journals
Architecture	Detailing bathrooms and elevators	Visiting sites, pitching to clients, being the lead in design competitions
Surgery	Managing patient care outside the operating room	Performing surgeries
Science	Organizing and executing lab work	Strategic planning of future research direction, publishing in prestigious journals

THE RESEARCH

This work grows out of the research I did for *What Works for Women at Work: Four Patterns Working Women Need to Know* (cowritten with my daughter Rachel Dempsey), which examined whether the kinds of gender bias documented in social psychology labs shows up in real workplaces. My team interviewed 127 professional women, including 63 in science, technology, math, and engineering, and 71 women of color. Our finding: Virtually all the women interviewed (96%) reported experiencing one or more of the patterns documented in experimental studies. Only five women had not, and three of them had founded their own companies.

loops very carefully, so people don't feel they are on a forced march into political correctness. Just as the metrics and the interrupters will differ from firm to firm, so will the feedback loops. But the best tone is judgment free and evidence based: "I'll bet you're not aware that there's an inconsistency in the way you're evaluating women and men; here's a study that explains why this is common."

Where should companies begin experimenting? Again, by looking at the same core processes they examined in Step 2. Though research on and experiments with interrupters are relatively new, they suggest the following brief template:

Hiring. Develop job-advertisement guidelines that advise steering clear of masculine-gendered words like "competitive," "assertive," and "ambitious." Track whether those guidelines are followed. To the extent possible, give hiring managers blinded résumés, so they can't tell whether the applicant is a man or a woman. Track whether this practice changes hiring numbers. Agree in advance on standard interview questions, watch for subtle biases, and adjust the list of questions as you learn which ones work well for all candidates. A seemingly harmless question like "Tell me about a personal or professional accomplishment that best shows your strengths" can be problematic. Since women are wary of bragging (the tightrope problem), they'll often answer this question by telling you how proud they are of their kids (women are allowed to brag about their children); men will give a work-related answer and advance their cause more effectively.

Assignments. The gentlest interrupter is one that documents that men and women are getting different kinds of projects and offers a training on how the four patterns of bias commonly affect assignments. If that doesn't work, more robust interventions are needed, up to and including a formal assignment system. As Louise Roth points out in her study of high finance, a huge problem is the channeling of women into groups with lower revenue potential. "These firms develop mathematical models for all sorts of other things," says Roth, "so why not for dividing work evenly?"

Performance evaluations. Having someone who is trained in the literature on gender bias read through all performance evaluations, which Ernst & Young has done for years, can help if your analysis shows that bias is affecting them. Be sure to track whether praise differentially translates into high overall evaluations for men but not women. Check, too, whether similar evaluations translate into greater rewards for men than for women.

Promotion and compensation. Systems that require people to brag will push women out onto the tightrope—disliked but respected if they do, and liked but not respected if they don't. In fact, any hiring, evaluation, or other process that requires self-promotion should take a hint from the Leibbrandt/List experiment and the Google example. Self-promotion should be cabined into formal contexts in which both men and women are sent the message that everyone is expected to tout his or her accomplishments.

Compensation systems based on objective metrics that are not easy to game offer a strong control on gender bias and give managers insight into who their most valuable players actually are. Roth's study of bankers confirmed what I've also found: Women fare best in jobs where performance is measured by objective metrics. Objectivity often suffers, however, when compensation is set by a powerful group of insiders. Law firm compensation systems, in which pay depends heavily on backroom negotiations over credit for bringing in clients, are a petri dish for bias. In a 2010 study about 30% of women in law firms reported being bullied out of receiving such credit.

THE PROMISE OF BIAS INTERRUPTERS IS that they allow for institutional learning and build on a critical, consistent finding: Doing anything once will not change organizational culture forever. You need to continually interrupt bias. And you need to be empirical: Keep throwing spaghetti at the wall until some sticks. Tech companies are used to spaghetti flinging, which makes them a perfect fit for an iterative process rather than one grand gesture.

What a company can't do is establish metrics, document bias, and then do nothing. That's a recipe for legal liability. But as long as companies that find bias try in good faith to remedy it, interrupters promise to be both more effective, and probably cheaper, than elaborate cultural change initiatives. And they will work a whole lot better than the other standard tools of the diversity industrial complex. Unlike women's initiatives, which often seek to fix women, and unlike stand-alone bias training, which can make diversity metrics worse, interrupters do something novel. They identify how bias is playing out in real time. And then they short-circuit it.

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Understand How to Optimize Your Fleet Operations

Can the Total Cost of Ownership Tool Help Your Bottom Line?

An Interview with John Gleason, Senior Vice President, Sales, Ryder

JOHN GLEASON

Why is the total cost of ownership equation so important?
Most companies are trying to understand the best uses for their precious capital. To make that determination, they need to know all the fleet and logistics costs associated with delivering their products to customers. You can't optimize what you don't know. That's why it's critical to understand and take a look at all the direct and indirect costs of owning and maintaining a private fleet.

Many companies overlook some accelerating costs associated with fleet ownership. For instance, new truck prices have increased by more than 40%, from the original cost of the trucks being replaced. Fuel prices are volatile. There's increasing government regulation. A driver shortage is sending costs higher. The complexity of fleet technology itself has dramatically changed. Five years ago, there were two sensors on a truck, today there are 26. At the same time, vehicle maintenance has become more complex and the industry is facing a technician shortage.

Most companies don't have the resources or capabilities to manage all these costs and provide the needed human capital. Ultimately, a company needs to determine where to invest its time and resources. And in order to do so, it has to determine: are these functions core to my business or should I outsource them to experts?

How does the Ryder Total Cost of Ownership Tool help companies get a true picture of the fleet operation?
When we developed the Total Cost of Ownership Tool in partnership with Ernst & Young, we were both very surprised to find that many companies struggle to access their own cost data. Most companies clearly understand the obvious costs, but they don't understand a range of other indirect expenses. These indirect costs, when brought to light, can radically alter the decision scenarios and assumptions that companies are using to make these important capital decisions.

Part of the problem is that the data itself is distributed across many departments, ranging from HR and legal to finance and IT. For example, it's crucial to have skilled technicians and they are in high demand, so there are real costs associated with having HR involved in recruiting, developing and training technicians, on an ongoing basis. Legal departments are devoting more time and dollars to handling increasingly complex regulations and tax issues. Companies have a very hard time identifying, capturing, and monetizing all these costs. What's more, companies often lack the specific know-how and processes needed to manage the life cycle cost of a vehicle, from initial investment in acquisition to the disposal of the truck five to seven years later.

Ryder's Total Cost of Ownership Tool pulls all that disparate data into one set of analytics, so you can compare your cost of ownership versus an outside provider, to determine where you want to invest your capital. Our benchmarking data has shown that companies were able to save, on average, 15% through outsourcing their fleets to Ryder.

THE THREE AREAS OF A TCO EVALUATION

Cash Costs: Different companies use different models to finance fleet acquisitions. Some pay cash outright or make large down payments and finance the rest. Others finance nearly the entire amount with a balloon payment at the end. Some organizations factor the cost of capital into the total cost of owning a fleet; others do not. Also consider: if cash is paid for the asset, what is the opportunity cost? Is there a better investment to make with that money? Additionally, purchasing power should be factored in; research indicates that bigger fleets find it easier to leverage their buying power as a procurement advantage.

Operations: Maintenance costs include labor, tires, parts and supplies, as well as the costs associated with accidents, repairs and temporary substitute vehicles. Maintenance costs rise with the age of the fleet and the complexity of the technology.

Beyond the costs of keeping each vehicle running, it's easy to overlook the array of people and systems that indirectly support running the fleet. Such costs may be hidden in functions such as IT, accounting and human resources. In HR, for example, costs associated with recruiting and managing technicians and drivers mount up. Procurement, contracting, driver compensation, insurance and fuel reporting take up resources in the finance and legal departments.

Asset Depreciation and Disposal: Just as companies finance their fleets differently, fleet managers use different methods to depreciate assets and estimate vehicle salvage value. Disposal costs, taxes or gains, should also be factored in, if parts of the fleet are sold.

How is Ryder able to create better savings and better service through outsourced fleet operations?
Ultimately, companies are trying to determine where to deploy their capital and, as important, how to meet customer expectations at the point of delivery.

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Once you're a Ryder customer, we deliver ongoing value through innovation. It's difficult for companies to stay innovative amid the changing technology, but when it comes to fleet management, that's all we do. For example, Ryder is a leader in using alternative fuels like natural gas, reducing greenhouse gases and providing new, unique solutions that help our customers achieve their sustainability goals. And finally, we have an extensive network of 1,000 fuel and service facilities to support customers and keep their fleets running as they enter new geographical markets. We can take care of their fleet needs, supplying trucks and service, 24/7 from coast to coast.

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MANAGING YOURSELF

Rebounding from Career Setbacks

by Mitchell Lee Marks, Philip Mirvis, and Ron Ashkenas

PHOTOGRAPHY: BRUCE PETERSON

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How well do you rebound from a career setback? To find out, visit **hbr.org/assessments/mirror-test**.

Brian was a rising star at his company. He advanced through several senior management roles and was soon tapped to head a business unit, reporting directly to the CEO. But after about two years in the job, despite his stellar financial results, his boss suddenly dismissed him. Brian was told that the company was trying to be a more open, engaged, global enterprise and that his aggressive leadership style didn't reflect those values.

Like most ambitious managers who suffer career setbacks, Brian went through a period of shock, denial, and self-doubt. After all, he'd never previously failed in a position. He had trouble accepting the reality that he wasn't as good as he'd thought he was. He also felt upset and angry that his boss hadn't given him a chance to prove himself. Eventually, however, he recognized that he couldn't reverse the decision and chose to focus on moving forward. None of the people working for him had objected to his dismissal, so he was particularly keen to figure out how to foster loyalty in future employees.

Within a few months, a large industrial parts company impressed with Brian's undisputed ability to meet financial targets recruited him to lead a division. The job was a step down from his previous role, but he decided to take it so that he could experiment with different ways of working and leading, learning to better control his emotions and rally his team around him. It paid off: Less than three years later, yet another company—this time, a *Fortune* 500 manufacturer—hired him to be its CEO. During his seven-year tenure in that job, he doubled the firm's revenue and created a culture that balanced innovation with a disciplined focus on productivity and performance.

Of course, not everyone can go from being out of a job to running a large company. But in more than 30 years of research and consulting work with executive clients, we've found that one lesson from Brian's story applies pretty universally: Even a dramatic career failure can become a springboard to success if you respond in the right way. To execute a turnaround like Brian's, you focus on a few key tasks: Determine why you lost, identify new paths, and seize the right opportunity when it's within your reach.

Figure Out Why You Lost

We've interviewed hundreds of executives who have been fired, laid off, or passed over for promotion (as a result of mergers, restructurings, competition for top jobs, or personal failings). Often, we find them working through the classic stages of loss defined by psychiatrist Elisabeth Kübler-Ross: They start with shock and denial about the events and move on to anger at the company or the boss, bargaining over their fate, and then a protracted period of licking their wounds and asking themselves whether they can ever regain the respect of their peers and team. Many of them never make it to the "acceptance" stage.

Reframing losses as opportunities involves hard thinking about who you are and what you want.

That's partly because, as social psychologists have found in decades' worth of studies, high achievers usually take too much credit for their successes and assign too much external blame for their failures. It's a type of attribution bias that protects self-esteem but also prevents learning and growth. People focus on situational factors or company politics instead of examining their own role in the problem.

Some ask others for candid feedback, but most turn to sympathetic friends, family members, and colleagues who reinforce their self-image ("You deserved that job") and feed their sense of injustice ("You have every right to be angry"). This prevents them from considering their own culpability and breaking free of the destructive behavior that derailed them in the first place. It may also lead them to ratchet back their current efforts and future expectations in the workplace.

Those who rebound from career losses take a decidedly different approach. Instead of getting stuck in grief or blame, they actively explore how they contributed to what went wrong, evaluate whether they sized up the situation correctly and reacted appropriately, and consider what they would do differently if given the chance. They also gather feedback from a wide variety of people (including superiors, peers, and subordinates), making it clear that they want honest feedback, not consolation.

Brian, for example, had to engage in frank, somewhat painful conversations with his boss, several direct reports, and a few trusted colleagues to discover that he had developed a career-limiting reputation for being difficult and not always in control of his emotions.

Also consider Stan, a senior partner at a boutique professional services firm considering global expansion. A vocal proponent of the growth plan, he had hoped to lead the company's new London office. When another partner was selected instead, Stan was outraged. He stewed for a few weeks but then resolved to take a more productive tack. He set up one-on-one meetings with members of the firm's executive committee. At the start of each session, he explained that he wasn't trying to reverse the decision; he just wanted to understand why it had been made. He

took care not to sound bitter or to bad-mouth the process or the people involved. He maintained a positive, confident tone, and he expressed a willingness to learn from his missteps.

As a result, the executive committee members gave him consistent, useful comments: They regarded his aggressiveness as an asset in the United States but worried that it would get in the way of securing new clients and running an office in the UK. His initial reaction was defensive. ("No one minded my aggressiveness when it landed key contracts," he thought.) But he kept those feelings in check—and quickly came around to appreciating the candor. "It wasn't that they were asking me to change," Stan reflected, "but they made clear to me that my style got in the way of this opportunity."

Identify New Paths

The next step is to objectively weight the potential for turning your loss into a win, whether that's a different role in your organization, a move to a new company, or a shift to a different industry or career.

Reframing losses as opportunities involves hard thinking about who you are and what you want. Research shows that escapism is a common reaction to career derailment—people may take trips to get away from their troubles, immerse themselves in busywork, drink or eat excessively, or avoid discussing their thoughts and plans with family and friends. While these behaviors can give you mental space to sort things out, they rarely lead to a productive transition. It's more effective to engage in a focused exploration of all the options available.

New opportunities don't usually present themselves right away, of course, and it can be hard to spot them through the fog of anger and disappointment in the early days after a setback. Studies by change management expert William Bridges highlight the tension people feel when they're torn between hanging onto their current identities and expectations and letting go. Leaders we've counseled describe entering a "twilight zone": The status quo has been fatally disrupted, but it's not clear yet what success will look like in the future.

That's why it's useful to take time to test out some ideas for what to do next. One option is to speak with a career counselor or engage in therapy, both to clarify goals and to work on personal development. Another is to take a temporary leave from your job to go back to school or test-drive a career interest at a start-up or a nonprofit. Pausing a bit can allow you to find new meaning in your setback.

Recall how Brian reacted when he was fired from his unit-head job: He began to consider lower-level positions that would give him room to tinker with his leadership style. Or look at Paula, whom we met while studying the resiliency of online advertising executives involved in restructurings. When her high-tech company's new CEO launched a corporate makeover, Paula felt relatively safe because the European business unit she led had met or exceeded its targets for 11 straight quarters, and she had been promoted three times in five years. But then she discovered that her position would be eliminated.

At first Paula blamed everything from company politics to her boss's failure to protect her and her team. Then, three months after the announcement, her last day arrived. She had no plans and didn't want to make any right away. Instead she spent time examining her life and her career. She reached out to friends and business associates—"not to network" (her words) but to gain perspective and advice in thinking through her goals. She reflected on each conversation, made notes, and eventually developed what she dubbed "four themes for my next job": She wanted to bring new products to market (rather than relaunching U.S. offerings in other regions), to interact more directly with clients, to work for a company with a unique value proposition, and to have colleagues she liked and trusted. Paula then tailored her job search to achieve those goals.

Seize the Right Opportunity

After you identify possible next steps, it's time to pick one. Admittedly, this can be a little frightening, especially if you're venturing into unknown career territory. Reimagining your professional identity

is one thing; bringing it to life is another. Remember, though, that you haven't left your skills and experience behind with your last job, and you'll also bring with you the lessons learned from the setback. You may also have productively revised your definition of success.

Research we've conducted, along with career specialist Douglas (Tim) Hall, shows that needs and priorities can change dramatically over time—as children are born or grow up and move out, after a divorce or a parent's death, when early dreams fade in midlife and new ones emerge, and when perspectives and skills become outdated and new growth challenges beckon. So choosing the right opportunity has a lot to do with the moment when you happen to be looking.

Paula's story is a case in point. Her list of "must haves" led her to interview for and accept a more senior position, as VP of international sales, at a smaller firm in the same industry. The job was located in the European city where she already lived and wanted to stay.

Brian, by contrast, took a significant step down, but he took advantage of the opportunity to learn to become a better manager. He developed an understanding of the triggers that had caused him to behave unproductively in the past and devised coping strategies. For example, instead of immediately pouncing on subordinates for performance "misses," he learned to have off-line discussions with the relevant managers. After some practice, the measured approach began to feel more natural to him.

Bruce, a senior IT manager at a New York bank that went through a merger, is another example. He kept his job in the deal's aftermath but was devastated to lose out in his bid to become the chief technology officer of the merged company. He stayed on through the integration, but after a year of rethinking his personal and career goals—and considering a variety of jobs—he moved with his family to Austin, Texas, and joined a small technology firm that became wildly successful. Just as important, he also found time to coach his two children's soccer teams and pursue his passion for music as a guitarist for a local band.

Like Paula and Brian, Bruce did serious discovery work after his setback—and then acted with conviction. He moved to a new city, industry, and job that would allow him to recover and thrive.

For executives who decide to stay with their employers, the biggest change may be in mind-set or psychological commitment. That's what happened with Stan at the professional services firm: Having gained a clearer sense of how his colleagues viewed him, he embraced his role as rainmaker, better appreciating the income, status, and perks that came with it. He also found a new source of satisfaction and accomplishment: mentoring the next generation of talent on how to win new business.

Shifting perspective like this takes just as much energy as switching companies or jobs. If you're not able to dig into your current work with renewed gusto, as Stan did, you might decide to put more discretionary effort into family life, volunteering, or hobbies, recognizing that having a rich personal life can compensate for not being number one on your team or in your organization.

WE ALL KNOW the importance of resilience and adaptability when it comes to career success. But these qualities don't come easily or naturally to everyone, which is why it's so useful to have clear steps to follow after a setback. The approach laid out here can help transform the anger and self-doubt associated with failure into excitement about new possibilities.

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Taking Control in a Constantly Changing Regulatory World

In an increasingly globalized economy, it can be difficult to keep track of the constantly changing tax and insurance laws as well as regulatory requirements in every country where your company operates. But it's critical to have comprehensive information to help you protect your foreign assets and exposures. Lawrence Boyk, Head of International Programs Casualty, recently talked about the Zurich Multinational Insurance Application, one of the most comprehensive online tools providing a regularly updated view of laws and regulations around the world.

Why is it challenging to build an effective global risk mitigation program?

Each customer is unique, and each operates in a different set of countries. Each country has different insurance regulations, and what applies in one is not necessarily true in another, so a program must be tailored to the unique characteristics of each line of business. One of the purposes of insurance is to facilitate commerce to help the company work in the local business and legal environments. So there are many moving parts that customers must take into account as they expand to different countries. Zurich built the Multinational Insurance Application to be a global compliance tool, to make sure our customers structure a program that will work in each jurisdiction.

How can the Zurich MIA tool help companies effectively tailor their insurance programs globally?

The tool is designed to give customers detailed information about insurance regulatory requirements across more than 180 countries and to address the viability of insurance-related activities such as claim payment, risk engineering services, and loss adjustment activities in those countries. For example, when you buy insurance in the U.S., it typically has a worldwide territory, but that doesn't mean it will be recognized in every country. The Zurich MIA tool helps customers understand what is and is not allowed in different countries with regard to non-admitted insurance, as well as what activities the insurer can perform. For instance: Who is permitted to go into a country to handle a claim? Can you pay the claim directly? With the answers, your organization is better prepared and has confidence it can meet the needs that arise. We map each country, and then we tailor a program for customers with the right policies that support compliance and business continuity. The tool helps them understand the tax implications of policies too.

How does the Zurich tool support international growth while protecting assets?

Zurich MIA puts at your fingertips the answers to key questions that can affect business development and expansion, enabling you to make better-informed decisions. It gives the customer essential insights into a variety of potential business scenarios related to their risk in each country, with updated information on relevant insurance and tax requirements. It helps us make the right recommendations, so the customers get the right policies to protect their assets and in the end their reputation.

LEARN MORE ABOUT THE ZURICH MIA TOOL:
zurich.com/internationalprograms

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Case Study

Should a Female Director "Tone It Down"?

by Boris Groysberg and Deborah Bell

ILLUSTRATION: BARRY FALLS

HBR fictionalized case studies present dilemmas faced by leaders in real companies and offer solutions from experts.

Finally, Sarah thought. J.P. Offutt, the CEO, had named a time when they could meet.

Sarah was a director of the company that J.P. ran, a Florida-based shopping-center-development group, and she was devoted to both him and his firm. But board meetings had been tense recently, and J.P. had grown distant.

In Sarah's opinion, the problem was obvious: Sid Yerby, the CFO. Despite Sarah's repeated requests for comprehensive financial statements, he continued to come to board meetings with a mere two pages of analysis that lacked any explanation. How could she or any of the other directors provide fiscal oversight without access to details of the company's operations or accounting?

Increasingly, however, hers seemed to be the minority view, and she was starting to feel isolated. Some months back, J.P. had told her privately that he appreciated her persistence with Sid. The young and inexperienced CEO confessed that he often felt uncomfortable asking tough questions of the CFO, an industry veteran who was 10 years his senior. It didn't help that J.P.'s father, Bill Offutt, who had founded the company and remained its chairman, didn't seem bothered by the lack of documentation.

Sarah, an experienced real estate consultant, had always been happy to help. But the clamor against her from Sid and the other board members was growing uncomfortably strong. In fact, one of her fellow directors had accused her of having

a private agenda that included taking the CFO down a couple of pegs. Another said to her face that she talked too much, just like his teenage daughter. Outwardly Sarah balked at this, but inwardly she was intimidated, especially because she was the only woman on the board. Even Bill, who had recruited her as a director and praised her stick-to-itiveness and gumption, had commented that others considered her "pushy." It was high time, she thought, that J.P. sprang to her defense.

The Previous Quarter

As Sid clicked through to a liquidity projection slide, Sarah allowed herself a small smile. It was a minor victory, but a victory nonetheless. Two weeks earlier, J.P. had pulled her aside and asked her to stop arguing with the CFO. Initially she was taken aback. Arguing? She was just asking questions. Besides, she'd been under the impression that J.P. wanted her to question and challenge Sid. Nevertheless, she decided to try a new approach: Before the board meeting she had called Sid and suggested that his presentation include certain essential details, such as the liquidity projections.

Still, he had to know that the inclusion of a single additional slide wasn't enough. After he finished, Sarah raised her hand. She could hear the sighs around the table. "Sid," she said, "I want to commend you for the additional information you've provided. But as I mentioned when we spoke a few weeks ago, it would be helpful to have even more information. For example, how do our financial ratios compare with the rest of the industry's? And what about best-, base-, and worst-case scenario projections?"

Everyone started talking at once. Sid turned to Bill with a shrug, as if to say, "You see what I have to deal with?" Bill quieted the room by tapping his pen on the table. "We simply can't fight over every financial report," he said. "Everyone here is an experienced business leader." Using the pen as a pointer, he continued, "Avery is the CEO of a trucking company, Louis runs a bank, et cetera. They're very comfortable reading financial summaries, and they don't want to waste their time getting into the weeds."

"But it's our fiduciary duty to get into the weeds," Sarah said. "Even though we've had a steady rise in our stock price, we've been relying more and more on buying underperforming assets using floating-rate debt, assuming that the assets will stabilize and we can refinance at lower rates. But that's a big assumption, and the board deserves more detail about why that's our strategy."

Rather than address those issues, Bill ended the discussion and moved on. It burned Sarah up. Fine—she would be quiet for now, but that night she wrote J.P. a letter that pulled no punches, for the first time formally documenting her concerns about the company's strategy and Sid's reporting standards, which she felt were far too casual for a big real estate investment trust, or REIT. The letter also asked J.P. for a one-on-one meeting in the week after she came back from a vacation with her husband and their four children.

> When Sarah raised her hand, she could hear the sighs around the table. The chairman quieted the room and said, "We simply can't fight over every financial report."

Sisterly Advice

Before leaving for vacation, Sarah had her monthly dinner with her sister Betsy, a biotech entrepreneur. Although they both juggled work and large families, they remained close and engaged in each other's lives.

It was while Sarah waited for her sister at their favorite restaurant that she received the affirmative response from J.P. She was relieved he'd agreed to meet, but there was a nervous twinge in her gut that wouldn't go away. J.P.'s e-mail was terse, and she found it unsettling.

As Sarah greeted Betsy, she tried but failed to wipe the worry off her face. "What's wrong?" Betsy asked immediately.

"It's that board I'm on—the real estate company." Sarah exhaled loudly. "Did you know we're now the second-biggest REIT in the country? We own hundreds of properties, and we're making tons of money. But the management team still wants the company to function like the small family business it was years ago. I can't tolerate that. And I especially can't tolerate our CFO Sid Yerby's casual approach to the numbers."

"I know—you've talked about him," Betsy said.

"He's like an overconfident cardsharp who bets high on a pair of deuces. Nobody calls him on it except me. By the way, many times when I've grilled Sid over his numbers, it's been because J.P. asked me to do it. J.P. once told me he couldn't run the company without me. But now it seems like he's giving me the cold shoulder and giving Sid free rein."

"What exactly is Sid doing wrong?" Betsy asked.

"Well, back in 2011, we made a few big acquisitions that gave us a lot of great properties but also stuck us with billions

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in debt, most of which had to be financed with short-term paper. The company is now highly leveraged—much more so than any of our competitors. Sid says property values have stabilized, the consumer is back in the saddle, and there's nothing to worry about. But what if we hit another downturn? No one else seems concerned."

She sighed. "All the other directors hate it when I grill him. They think I have some private agenda. But I don't, except the interests of the company."

"In all your grilling, have you ever uncovered anything nefarious or illegal?" Betsy asked.

"No," Sarah replied.

"Incompetent, boneheaded, sloppy?"

"No, but—"

"Misguided, rash, questionable?"

"Well, I do think many of his choices are questionable, especially around our leverage," Sarah said.

"But he did get your company through the mortgage crisis and the recession in good shape, right?" Betsy countered.

"Yes."

"Well, rightly or wrongly, that may be one reason why you don't have a single ally on the board."

In J.P.'s Office

Sarah and J.P. sat opposite each other on the short leather sofas in his office. He looked nervous.

"Sarah, you know my own capabilities are limited," he began. "I don't know everything there is to know about business, and I never will. And as I've said to you before, that's why I can't run this company without—" he hesitated.

Sarah filled in the rest. "Without me. I know. And I appreciate that."

"No—sorry. Without Sid."

She stared at him, unsure what to say.

"Sarah, your intellect is very powerful," he continued. "And your questioning, especially on financial matters, is very informed and insightful. What you have to say is always important."

"But?"

"But Sid has expressed his frustration with the situation on the board, and in fact, he's prepared to tender his resignation."

"Really?" This was exciting news, Sarah thought.

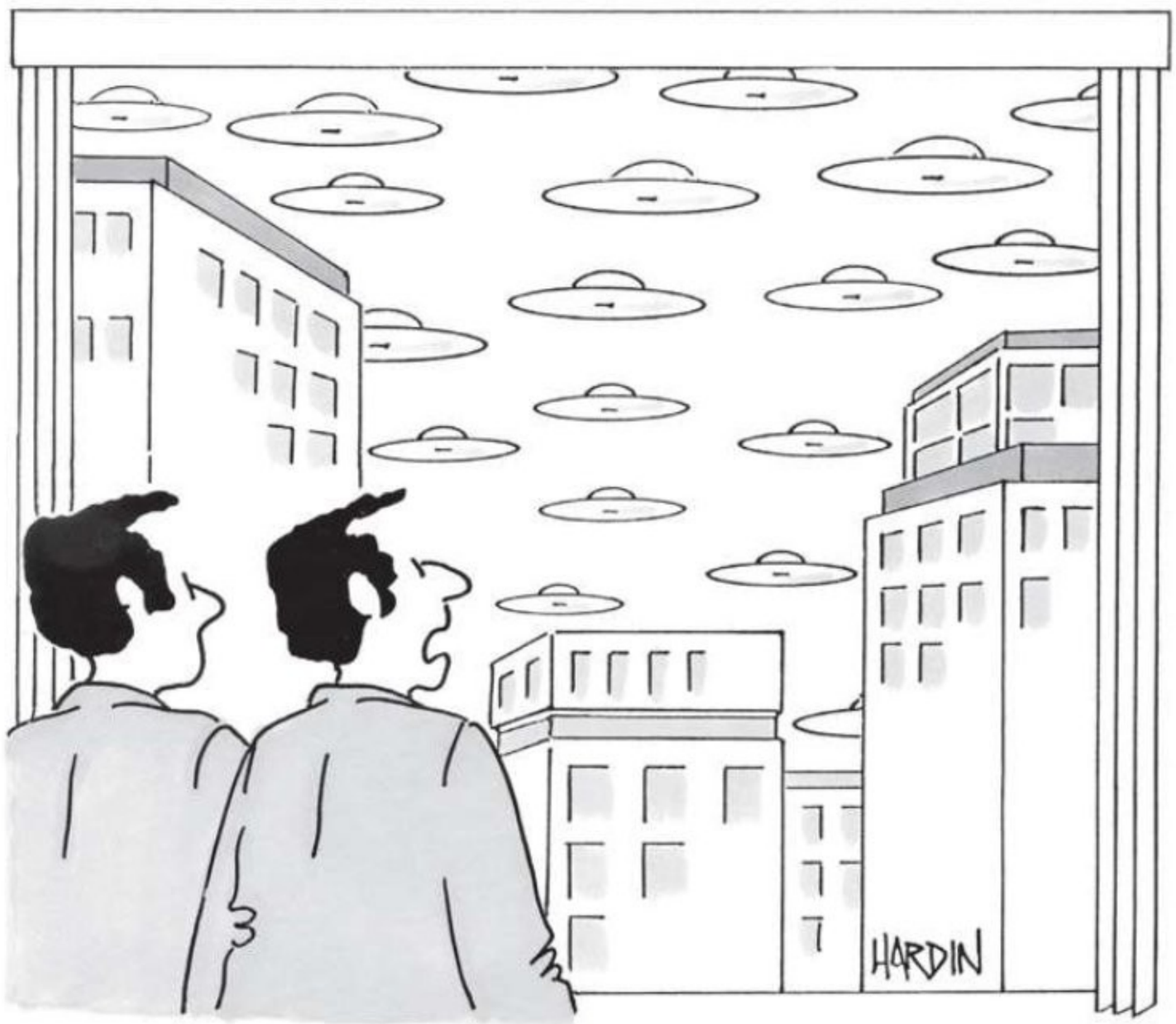
"He'll stay if you, well, as he put it, 'tone it down and back off.'"

Sarah was stunned—so much so that she had to exert considerable effort to bring herself back into the conversation. She realized then that J.P.'s expression showed more resolve than she was used to seeing in him. Was he truly giving her an ultimatum: Shut up or leave the board?

Boris Groysberg is a professor of business administration at Harvard Business School and a coauthor of *Talk, Inc.* (Harvard Business Review Press, 2012). **Deborah Bell** is a researcher of organizational behavior whose work focuses on organizational dynamics and effectiveness.

How should Sarah respond to J.P.?

See commentaries on the next page.



"Good heavens! What if they've come seeking market share?"

CARTOON: PATRICK HARDIN

The Experts Respond

Ilene S. Gordon is the president, CEO, and chairman of Ingredion, a global supplier of ingredients to numerous industries, including food and pharmaceuticals. She also serves on the boards of International Paper and several nonprofits.

SARAH'S RELATIONSHIP with her fellow directors has clearly gone off the rails, but she might be able to retain her position and become more effective in it.

She is absolutely right that a board needs more than two pages of summarized financial information at each meeting. In a public company, directors are supposed to represent independent shareholders' interests and provide a strategic sounding board for management. They shouldn't rubber-stamp whatever the CEO and the CFO present. They need to understand how the company makes its money and where competitive threats are lurking. They should want—and, in my experience, most do want—to dig into the numbers and understand data such as profitability and financial ratios.

So at first blush, Sarah appears to be succeeding admirably in her role as director. In fact, she seems to be the only one who's treating the job seriously. But take a step back and you can see that she's failing miserably. She isn't contributing constructively to the team, so her attempts to represent independent shareholders are ineffective.

Sarah might argue that the other directors are the problem. I wonder if many of them are longtime associates of the founding family whose loyalty to Bill and J.P. may outweigh other concerns. Even so, Sarah can become a better team player. She should do her homework and find out about her fellow board members' backgrounds and viewpoints—who has what expertise, who feels the same way she does about the issues facing the company. I seriously doubt she's the only one who wants more financial information. It's a good bet that a few other directors would welcome a conversation with her if she approached them with an open mind. Once she has established common ground, she should use those areas of alignment to build relationships. She should have done more research before officially becoming a director—that's what I always do—but I don't think it's too late.

If, as I suspect, Sarah has a few potential allies around the table, and if she's able to forge relationships with them, she should make it her priority to build an alliance that can diplomatically yet forcefully insist on getting more-detailed financial information and engage management in thoughtful discussions about such things as debt and how expansion should be funded. That's the way to represent independent shareholders.

The chairman and the governance and nominating committees have roles to play, too, of course: They should coach Sarah and the other directors on how to listen and how to present opinions so that the board's discussions become more fruitful and people's time isn't wasted. As the chairman of Ingredion's board, I often seek out discussions with board members between meetings. I've worked with several directors who feel strongly about certain issues, and, yes, sometimes people do bump heads. A chairman shouldn't try to eliminate conflict—it's important to have a diversity of opinion on a board, and I like it when people speak up and become change agents. When managed appropriately, conflict can be productive. I try to bring out the best in each director so that he or she is operating effectively, both individually and as a team member.

> Other directors would welcome a conversation with Sarah if she approached them with an open mind.

It's possible, of course, that the chairman and the head of the governance committee wouldn't want to help Sarah. She also might not find any potential allies or be able to engage more constructively. Under any of those circumstances, Sarah and the board should probably part ways—everyone would be the better for it.

But this board faces another, deeper issue. The leadership abilities of the company's CEO are questionable, to say the least. It's a big red flag that J.P. has been deputizing Sarah to grill Sid at board meetings. He's the one who's supposed to ask the tough questions. If J.P. can't face up to Sid, this company has a much bigger problem than the conflict around Sarah.

WHAT WOULD YOU DO?
SOME ADVICE FROM THE HBR.ORG COMMUNITY

THE LACK of financial detail is hampering Sarah's ability to discharge her fiduciary duty. I don't think it would be prudent for her to back down. If the CFO is unwilling to provide detailed financial information, she must inform the CEO that she will have to resign from the board with a letter to shareholders.
Carrie Mantha,
CEO, Indira

SARAH SHOULD immediately stop pursuing financial information in board meetings, promising instead to secure information privately, quietly, and offline. She should apologize to each board member for using a public forum to aid her personal understanding. And she should take ownership of her role in the misunderstanding. This way, Sarah would be both complying with the "tone it down or leave" ultimatum and securing additional information on the organization's financials.
Christine R. Valeriann,
marketing consultant and professional faculty member, Johns Hopkins Carey Business School

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Sue Decker is a former president of Yahoo and a former entrepreneur-in-residence at Harvard Business School. She is a member of the boards of directors of Berkshire Hathaway, Intel, and Costco Wholesale.

WHEN A BOARD develops a culture as dysfunctional as this, no individual director other than the chairman can alter it without support from other members. So although her concerns are valid and her requests are quite reasonable, Sarah has lost her power to drive change, and she now has to decide whether she can live with this culture. I don't think she can—I know I couldn't—so I would advise her to state her concerns publicly and resign.

But to avoid finding herself in a similarly polarizing and ineffective position in the future, she must learn as much as she can from this experience.

The next time Sarah joins a board, she should think about how she can better use her power. She should adopt a communication style that reflects an appreciation of the roles of her fellow board members, and she should observe important communication boundaries.

A well-functioning board has committees that take on specific roles, some of which are required by law. In fact, most of a board's real work happens in committee meetings and one-on-one interactions, not in the general meetings. The audit committee's role, for example, is to understand and monitor the company's financials, including its liabilities, and it is often responsible for risk-management oversight. So the concerns Sarah is raising in the general board meetings should have been raised first with the audit committee and the company's outside auditors. Had the committee and the auditors shared her concerns, she could have reached a consensus with fellow board members or outside experts. Sarah doesn't appear to understand the committees' roles and functions—which brings me to the issue of boundaries.

> If a director told me that I was like his teenage daughter, I would ask him to explain on the spot.

By repeatedly trying to get into detailed discussions of the financials in general board meetings, Sarah transgressed personal boundaries. In effect, she chastised Sid Yerby, the CFO, in front of his peers and his boss. As a result, she and Sid ended up in an attack-and-defend mode, which prevented them from empathizing with or validating each other and from finding common ground. The style of communication hijacked the content of the issue.

The board obviously has its own boundary issues: The comment that Sarah is like a director's teenage daughter was completely inappropriate. Sarah should have immediately addressed that comment with the director to understand what he meant and to communicate that it was inappropriate. If someone had made a remark like that to me, I would have asked him to explain on the spot and put him in a position to retract and apologize. Sarah then should have followed up in a one-on-one meeting with the director.

Sarah should have been holding one-on-one meetings with other directors all along, in order to express her views and find out how the others thought about various issues. She should have used those meetings to try to put herself in their shoes. For example, a critical question is why Sid doesn't want to provide more-detailed financial information. Is it because the chairman and the CEO don't want him to? Or is he hiding something? Once Sarah had come to understand the others' viewpoints and motivations, she might have been able to resolve her issues. Or—who knows?—she might have discovered a cover-up that would need to be reported to shareholders and outside auditors.

As the only woman on the board, Sarah is in a tough position. The other directors may not be overtly sexist, but their choice of language suggests that at least some of them view her through that lens. This makes her choices about when and how to communicate her concerns even more delicate and sensitive, and her personal style may have gotten in the way of effective communication. She seems quick to go on the offensive and equally quick to get defensive. She may not realize that her personal power could be much greater if she were disarming and nondefensive rather than abrasively forceful.

Had she been more successful in gaining information and establishing boundaries in the way she communicated her concerns, Sarah might have been able to win support from her fellow board members for her requests. If the CFO continued to resist, despite board support for Sarah, a decision to resign from the board would have had a powerful impact on shareholders, because it would have raised troubling questions about the top management team's motivations.

SARAH IS in a "moment of power" in which she could agree with the CEO's request and ask for a concession in return. She might say, "Let's commission an independent audit from an external auditor, just to have peace of mind, for all of us—you, me, the board, and even Sid."
Alen Gojceta,
technical sales manager, IBM Croatia

AN OUTLOOK that would be considered direct or assertive in a man is often seen as pushy or emotional in a woman. That is a problem for Sarah's fellow directors, but it should not dissuade her from doing the right thing.
Liz Mellon,
editorial chair, Dialogue, *a journal at Duke Corporate Education*

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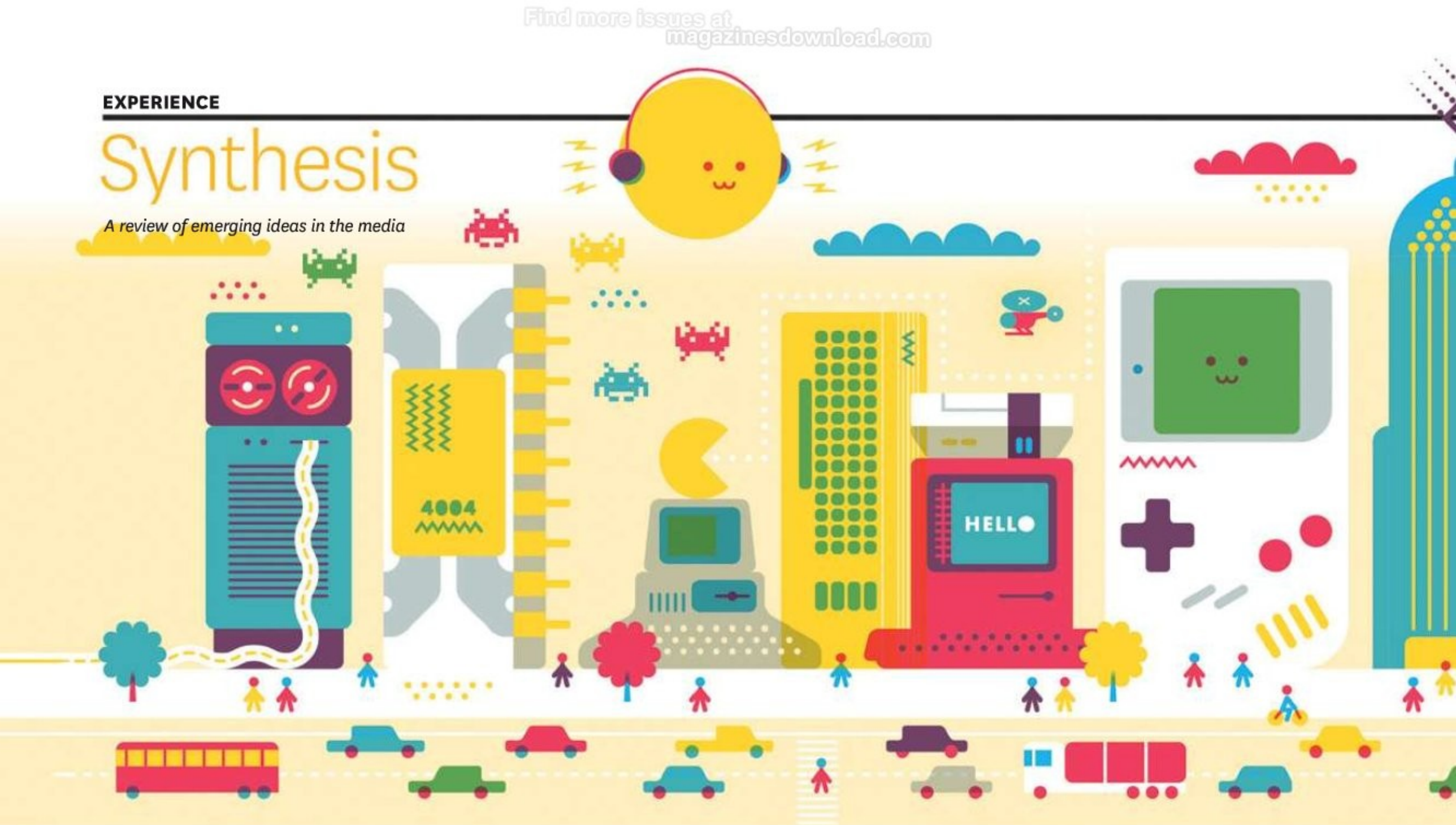
Synthesis

A review of emerging ideas in the media



Innovation, Then and Now

Why do we lionize the tech industry's past and mock its present? *by Walter Frick*

In the second episode of *Halt and Catch Fire,* AMC's new show about the birth of personal computing, the protagonist encourages his two recruits—a hardware engineer and a coder—to ignore a recent setback and keep working to build a new kind of PC. "I thought that maybe we could do this precisely because we're all unreasonable people," he tells them, borrowing from George Bernard Shaw. "And progress depends on our changing the world to fit us—not the other way around."

That line perfectly sums up how we regard technology's past. Looking through the rearview mirror, we see only iconoclasts and geniuses. But flip the channel and fast-forward 30 years to HBO's *Silicon Valley,* and present-day tech entrepreneurship is portrayed in a very different light. These characters care more about ideas they can code in a weekend than they do about truly world-changing innovation: As one says, after selling his company to Google for $200 million, "We're making the world a better place through constructing elegant hierarchies for maximum code reuse and extensibility."

The triviality is emphasized in another scene when a woman chatting up the show's protagonists admits that she's an actress who owns a start-up that "sources actors to parties to liven things up and get in conversations with guests."

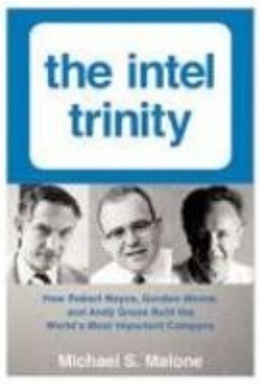
These are fictional shows, yes, and *Silicon Valley* aims at parody. But the gulf between the high esteem we have for historical innovation and the disdain we feel for many of the tech world's offerings today is real. And it's on ample display in several recent nonfiction books as well.

Consider *The Intel Trinity,* Michael Malone's new history of the company, and *The Innovators,* Walter Isaacson's look at the pioneers who "set the world afire" by creating the computing industry. These are heroic tales, exemplified by a story that both authors tell about Intel's Robert Noyce. In October 1971 the legendary engineer and entrepreneur invited his relatives to California for a reunion and, on a bus tour of the Bay Area, offered them a bold prediction concerning the impact of his company's work. Holding up Intel's new 4004 microprocessor, he said, "This is going to change the world. It's going to revolutionize your home....you'll all have computers. You will have access to all sorts of information....Everything will happen electronically."

Of course he was right. Noyce, his Intel cofounder Gordon Moore, and all the others profiled by Malone and Isaacson did invent our future, so it's no surprise that we want to gaze back at them in admiration.

Halt and Catch Fire
AMC, 2014

Silicon Valley
HBO, 2014



The Intel Trinity: How Robert Noyce, Gordon Moore, and Andy Grove Built the World's Most Important Company
Michael S. Malone
HarperBusiness, 2014

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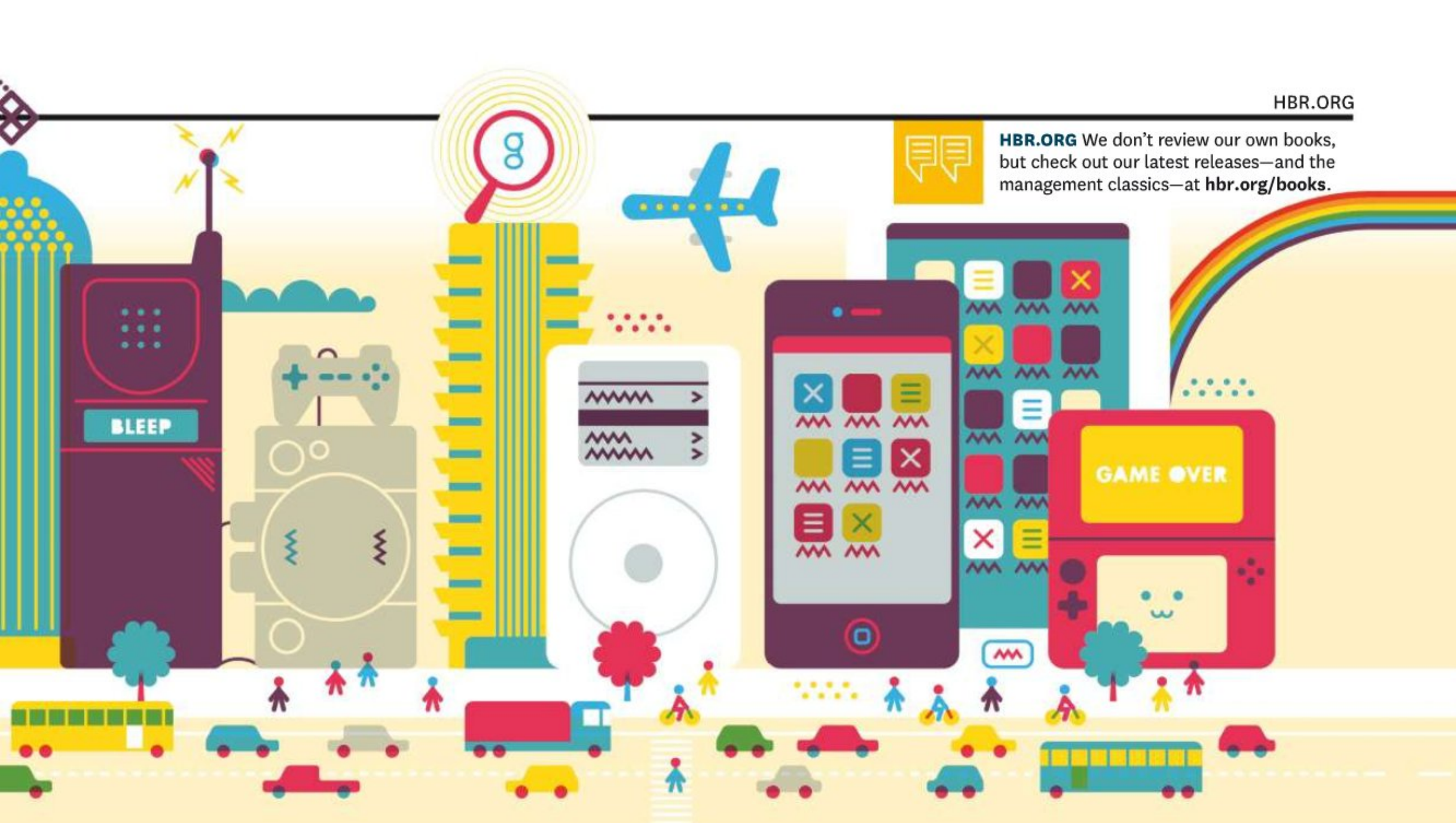


No Exit, a new e-book by Gideon Lewis-Kraus that expertly captures the mundane grind of start-up life in today's Silicon Valley, offers a decidedly less inspiring narrative. It centers on Boomtrain, a fledgling video discovery site that, when that idea didn't work, morphed into a media recommendation engine for businesses. The founders are earnest and capable, pitching and pivoting their way against the long odds of their industry. But there's nothing spectacular about them or their company, and that's precisely the point. They came from a start-up incubator, not a lab or a garage. They focus on viable business models, not scientific research and development. And they're obviously not setting anything afire.

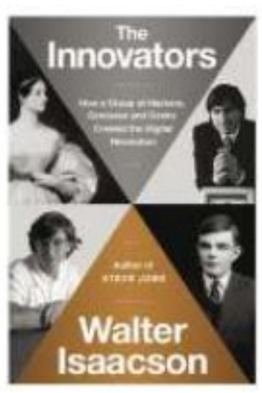
Why the contrast? Why do we increasingly glorify the tech industry's past while mocking or dismissing its present? One answer is that history has a way of filtering out the also-rans and focusing on the greats. That may be part of the explanation, but there's more to it.

Despite the current pace of technological change, it's hard to shake the feeling that today's new products and services are somehow smaller than the innovation we saw 20 or 30 years ago. The companies have fewer employees and rarely push the boundaries of basic or even applied science. The ideas that get hatched and funded are apps masquerading as platforms, platforms masquerading as breakthroughs.

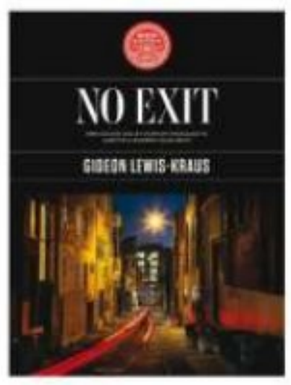
A big reason for that is the much-heralded democratization of entrepreneurship. Today anyone can start a technology business. It's cheaper than ever, and—thanks to the booming VC industry, a glut of angel investors, and crowdfunding websites like Kickstarter—it has perhaps never been easier to get bankrolled.

> "The $5 million that went to one company of 10 people in 1999 is now going to 10 companies of two people."
>
> Gideon Lewis-Kraus, *No Exit*

Whether that's a good or a bad thing remains to be seen. A few decades from now we may look back on this era as one in which the tech world, notably Silicon Valley, mostly just spun its wheels, producing many more trivial or even laughable ventures than truly disruptive technologies. Or we may find that all those bites at the entrepreneurial apple resulted in innovation on a par with the microchip and the personal computer. The heroes of our day—people such as Elon Musk, Peter Thiel, Larry Page, and Sergey Brin—might one day rank up there with Noyce and Moore. The difference is that they're surrounded by waves of imitators who won't change the world and, in fact, aren't even trying.



The Innovators: How a Group of Hackers, Geniuses, and Geeks Created the Digital Revolution
Walter Isaacson
Simon & Schuster, 2014



No Exit: Struggling to Survive a Modern Gold Rush
Gideon Lewis-Kraus
Wired Extra, 2014

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Walter Frick is an associate editor at *Harvard Business Review.*

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THE GREAT TRANS-FORMATION

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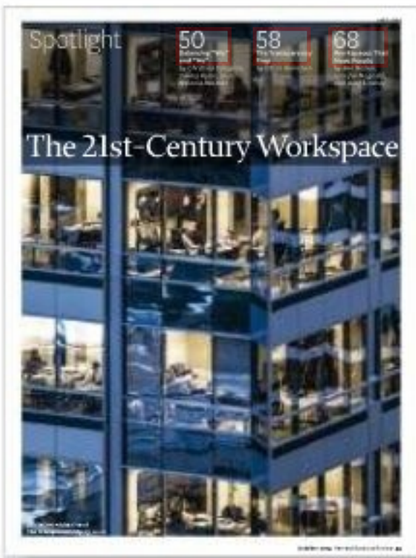
SPOTLIGHT ON THE 21ST-CENTURY WORKSPACE



It's now possible to measure productivity—and also collaboration—no matter where work gets done, and that has numerous ramifications for workspace design. But one thing hasn't changed: It's incredibly difficult to create space that works for everyone.

OPERATIONS

Balancing "We" and "Me"

Christine Congdon, Donna Flynn, and Melanie Redman | page 50

The open office is the dominant form of workspace design for good reason: It fosters collaboration, promotes learning, and nurtures strong culture. But what most companies fail to realize is that collaboration has a natural rhythm that requires both interaction and private contemplation.

Companies have been trying for decades to find the balance between public and private workspace that best supports collaboration. In 1980 52% of U.S. employees lacked workspaces where they could concentrate without distraction. In response, high-walled cubicles took over the corporate landscape. By the late 1990s, the tide had turned, and only 23% of employees wanted more privacy, and 50% wanted more access to other people. Ever since, firms have been beefing up spaces that support collaboration and shrinking areas for individual work. But the pendulum seems to have swung too far: Once again, people feel a pressing need for privacy, not only to do heads-down work but to cope with the intensity of work today.

To address these needs, according to the authors, we have to rethink our assumptions about privacy. Traditionally defined in physical terms, privacy is now about the individual's ability to control *information* and *stimulation*. In this article, the authors examine workspace design through the new lens of privacy and offer insights on how to foster teamwork and solitude.

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ORGANIZATION & CULTURE

The Transparency Trap

Ethan Bernstein | page 58

To promote accountability, productivity, and shared learning, many organizations create open work environments and gather reams of data on how individuals spend their time. A few years ago, HBS professor Ethan Bernstein set out to find empirical evidence that such approaches improve organizational performance. What he discovered is that this kind of transparency often has an unintended consequence: It can leave employees feeling vulnerable and exposed. When that happens, they conceal any conduct that deviates from the norm so that they won't have to explain it. Unrehearsed, experimental behaviors sometimes stop altogether.

But Bernstein also discovered organizations that had established zones of privacy within open environments by setting four types of boundaries: around teams, between feedback and evaluation, between decision rights and improvement rights, and around periods of experimentation. Moreover, across several studies, the companies that had done all this were the ones that consistently got the most creative, efficient, and thoughtful work from their employees.

Bernstein's conclusion? By balancing transparency and privacy, organizations can capture the benefits of both, and encourage just the right amount of "positive deviance" needed to increase innovation and productivity.

HBR Reprint R1410D

INNOVATION & CREATIVITY

Workspaces That Move People

Ben Waber, Jennifer Magnolfi, and Greg Lindsay | page 68

Few companies measure whether the design of their workspaces helps or hurts performance, but they should. The authors have collected data that capture individuals' interactions, communications, and location information. They've learned that face-to-face interactions are by far the most important activity in an office; creating chance encounters between knowledge workers, both inside and outside the organization, improves performance.

The Norwegian telecom company Telenor was ahead of its time in 2003, when it incorporated "hot desking" (no assigned seats) and spaces that could easily be reconfigured for different tasks and evolving teams. The CEO credits the design of the offices with helping Telenor shift from a state-run monopoly to a competitive multinational carrier with 150 million subscribers.

In another example, data collected at one pharmaceuticals company showed that when a salesperson increased interactions with coworkers on other teams by 10%, his or her sales increased by 10%. To get the sales staff running into colleagues from other departments, management shifted from one coffee machine for every six employees to one for every 120 and created a new large cafeteria for everyone. Sales rose by 20%, or $200 million, after just one quarter, quickly justifying the capital investment in the redesign.

HBR Reprint R1410E

Features

THE BIG IDEA

POLITICAL ECONOMY

The Rise (and Likely Fall) of the Talent Economy

Roger L. Martin | page 40

Since 1960 the U.S. economy has moved from largely financing the exploitation of natural resources to making the most of talent. The rewards to executives and financiers have skyrocketed as a result. But over the past two decades or so, the author argues, it has become increasingly clear that much of this talent is trading value rather than creating it: The fastest-growing group on the *Forbes* 400 list is hedge fund managers. What's more, stock-based incentives, which were intended to align the interests of top executives with those of long-term shareholders, are actually encouraging CEOs to serve the interests of short-term traders. The losers in this game are employees engaged in routine work, whose rewards are shrinking or whose jobs are disappearing.

This state of affairs has created a growing—and unsustainable—inequality of income. Martin suggests that three things must happen if we are to avoid radical and talent-hostile steps imposed through the ballot box: (1) Talent must exert some self-discipline and lower its expectations. (2) Investors—primarily pension and sovereign wealth funds—must prioritize value creation. That means not voting in support of stock-based compensation and no longer supplying hedge funds with large amounts of capital or lending them stock. (3) Government should regulate the relationship between hedge funds and pension funds (if the latter don't do so voluntarily), tax "carried interest" as ordinary income, tax trades, and revisit the overall tax structure.

HBR Reprint R1410B

STRATEGY & COMPETITION

Capture More Value

Stefan Michel | page 78

Sometimes the only thing that can save a business is a new way to capture value.

Businesses constantly innovate to create new value—but unless they also focus on how they *capture* value, they won't realize maximum benefit from their breakthroughs. And even avid innovators often have a blind spot when it comes to value capture. Managers need to think about value capture more imaginatively and as a matter of course. A new framework developed by IMD business school's Stefan Michel can help them do so.

Michel details 15 value-capture innovations, which fall under five broad categories. Firms can profit by changing the *price-setting mechanism* (think of Priceline), the *payer* (media businesses where advertisers subsidize content consumption), the *price carrier* (Netflix), the *timing of the exchange* (commodities futures), or the *segment served* (grocery coupons, which "fence off" customers who prioritize savings).

The practical applications of the framework are proven: In workshops at a major airline and a global professional services firm, for instance, cross-functional teams using this tool quickly devised new ways to capture value that boosted their company's profits.

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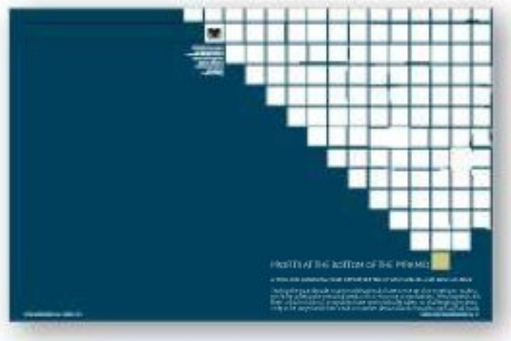
GLOBALIZATION

Profits at the Bottom of the Pyramid

Erik Simanis and Duncan Duke
page 86



The best way for companies to improve the lives of the world's poorest people—those at the bottom of the pyramid—is to focus first on doing good business, not just on doing good. That's the contention of the authors, who say that a steady flow of profits from manageable ventures will pave the way for later investments in more-ambitious socially beneficial projects.

The authors cite two main challenges in selling profitably to the bottom of the pyramid: changing consumers' behavior and changing the way products are made and delivered. To help companies see how these challenges affect various business prospects, they have developed an "opportunity map" that classifies opportunities along a spectrum from the least complex and resource-intensive to the most. At the simplest end are targeted marketing opportunities in mature markets. In the middle are opportunities in growth markets: efforts to redesign products, extend distribution channels, or create new ones. At the other end of the spectrum are frontier-market ventures to develop new products, conquer competitors' markets, expand into greenfield markets, develop new business models, or create altogether new markets.

The authors present examples of each type and explain that companies can pursue multiple opportunities simultaneously. If they choose wisely, they can make profits and advance their social missions at the same time.

HBR Reprint R1410G

DIVERSITY

Hacking Tech's Diversity Problem

Joan C. Williams | page 94

The technology industry has a big problem with diversity, one that seems to be getting worse: In 1991 women held 37% of computing jobs; today they hold only 26%. But if tech firms want to get serious about hiring, retaining, and promoting more women, they'll need something more effective than sensitivity or mentoring programs that "fix" individual behavior, and longer lasting than cultural change programs. The author suggests an approach that borrows from tech's own playbook on experimentation: Collect detailed data on bias in your organization, identify company-specific ways to measure its effect, create hypotheses about how to move those metrics, and then throw some spaghetti at the wall and see what sticks.

Working women face four kinds of bias: prove-it-again (continually being asked to prove their competence), tightrope (backlash for being too assertive or too nice), maternal wall (erroneous assumptions about mothers), and tug-of-war (pressure to distance themselves from other women). All four affect hiring, work assignments, evaluations, and promotion and compensation. Companies need to understand how, and then thwart these biases with "interrupters," small changes to business systems that stop patterns of bias. They can be as simple as adding "salary negotiable" to want ads—which closed the pay gap between men and women by 45% in one study.

Doing anything once will not change organizational culture. Bias needs to be disrupted constantly, and the iterative interrupter approach may well be the way to do that.

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How I Did It

LEADERSHIP

Fallon's Chairman on Getting Clients to Take Creative Risks

Pat Fallon | page 35

The author has worked in advertising for four and a half decades, and during those years he has spent a lot of time persuading clients to run ads that feel risky—maybe even dangerous—when they're first pitched. A client's risk appetite depends on the emotional makeup of the decision makers, the state of the company, the industry it's in, and many other variables. Strategy is the rigorous, behind-the-scenes part of Fallon's process: Driven by research and consumer insights, it helps to precisely define what the company is trying to accomplish with a campaign. Realizing that the agency has thought it through, the client becomes more comfortable taking the leap.

The author describes three highly successful campaigns: "Live Richly" saturated New York City and other big markets with provocative signs that proved much more powerful than TV ads and created meaningful differentiation for Citibank in a category that had defied differentiation. "Just the Right Amount of Wrong" developed a niche market for the Cosmopolitan hotel of Las Vegas—people who like the spirit of the Strip but want something more refined. "Never Settle for Less" helped H&R Block expand its customer base by offering a free second look at tax returns in various locations. The company's professionals discovered thousands of dollars in additional refunds, and ads created from film footage of the event raised consumer awareness of a key selling point.

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Managing Yourself

Rebounding from Career Setbacks

Mitchell Lee Marks, Philip Mirvis, and Ron Ashkenas | page 105

It's not easy to recover from a big career disappointment such as getting fired or being passed over for a promotion. Many people sink into anger or denial, blaming situational factors or company politics. Though that's a natural response, it can also prevent them from breaking free of the destructive behaviors that may have derailed them in the first place.

People who successfully rebound from career losses take a different approach: They do the hard work of figuring out why they lost, identifying which new paths they could take, and then seizing the right opportunity—whether that's a different role in the same organization, a move to a new company, or a shift to a new industry or career.

Drawing on in-depth research and the authors' consulting experience, this article offers practical guidance for transforming anger and self-doubt over what seems like a failure into focused exploration and excitement about the fresh possibilities the situation presents.

To gauge your ability to rebound from career setbacks, take the self-assessment at hbr.org/assessments/mirror-test.

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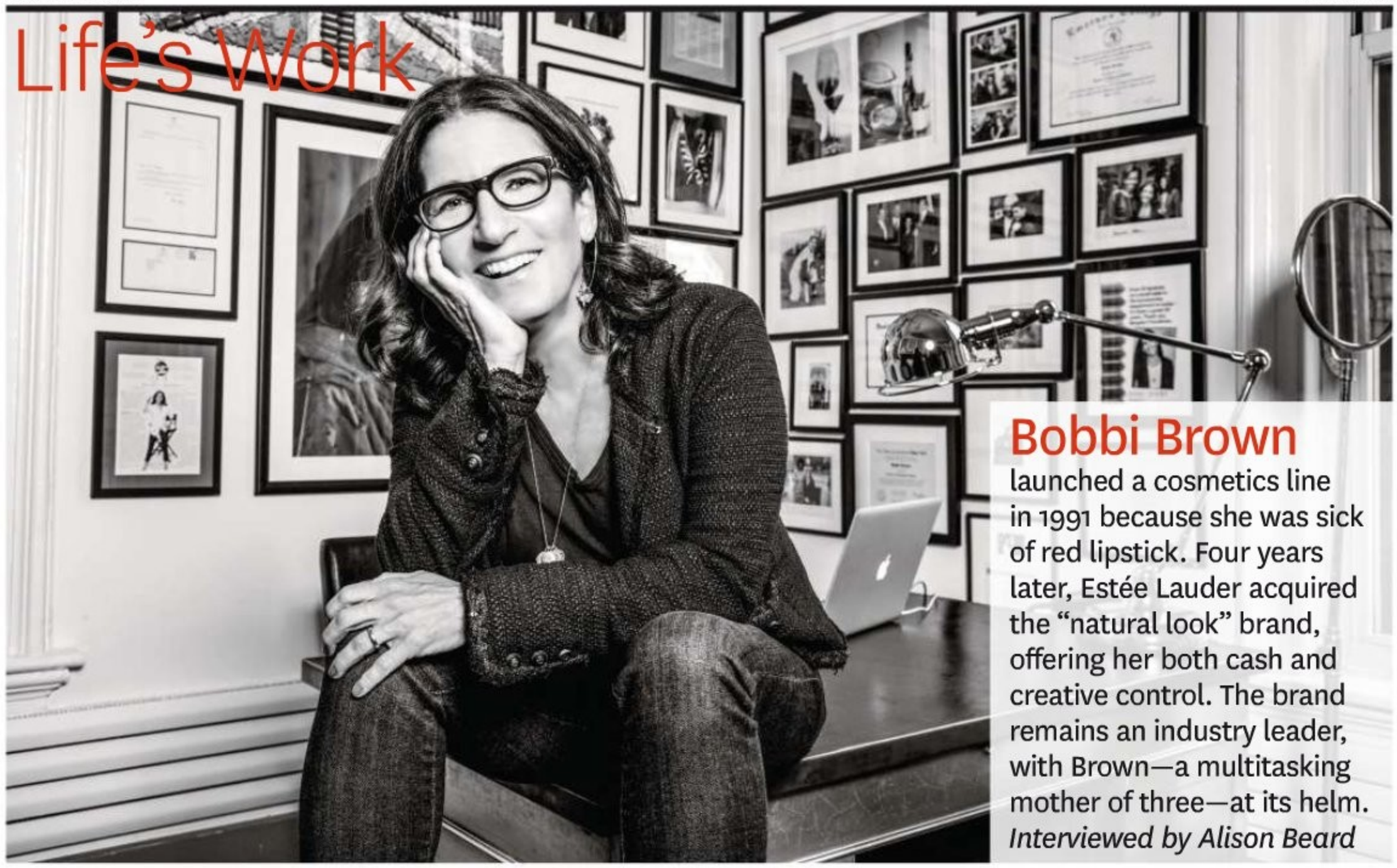
Life's Work



Bobbi Brown

launched a cosmetics line in 1991 because she was sick of red lipstick. Four years later, Estée Lauder acquired the "natural look" brand, offering her both cash and creative control. The brand remains an industry leader, with Brown—a multitasking mother of three—at its helm. *Interviewed by Alison Beard*

HBR: Your title is chief creative officer. What does that role entail? **Brown:** Everything that touches my artists and the consumer: developing products and marketing them. I rarely have a finance or operations meeting. I wave to those guys and give them a thumbs-up, but I do all the things that I'm good at and I love.

Is it hard to run your own brand within a big organization? There are hurdles—things you have to get over or around. When people give you their opinion, you just tell them, "It's a really great idea. Thank you." Then you go back and do what you think is right. Usually in big companies, there's so much to do that no one really dwells on everything that's discussed. And because the brand is growing, they don't come back to me. They don't insist; they suggest.

But you moved out of headquarters a while back. Yes, I was in the corporate environment, I think on the 45th floor, and I dressed like a corporate employee, wearing uncomfortable suits and high heels. I went to work and looked out the window that didn't open, and it just never felt right. At one point when our business was flat, I said to the CEO, "I'm not able to do what I want to do." He said, "What would you do?" I said, "I'd move downtown. I'd allow people to wear jeans. I'd have a creative, open atmosphere." I did those things, and it worked.

What kind of boss are you? I'm incredibly busy, so I tell people the truth. One of my employees laughs at me because when I don't like something, I say, "No offense, but..." But I'm also the first to hug someone when they come up with a great color or formula. I absolutely give credit, because there's nothing I do by myself except an interview. So I have good relationships with my people. You either work for me a long time or you don't last.

What do you look for in new hires? I need people with good energy who share my aesthetic and are fun, talented, and truthful. I cannot work with someone who says one thing and does another. It's hard to know a person's creative process from an interview, so I first try to work with people on a freelance basis.

Where do you do your best work? I commute via car service, so twice a day I have an hour to do anything. I come up with ideas. I've written all eight of my books in the backseat. Working with a team is one thing, but I find it difficult to focus in the office.

What happens when you miss a cosmetics trend? I listen to the market, but if I don't like the current form of a product, I won't just put my name on it. I figure out why people want something and re-create it. I don't need to be first; I just need to be best.

Why should executive women care about makeup? Success requires experience, of course, but also confidence. You want to feel your best. If you can do that with no makeup, you're really lucky.

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For Brown's tips on work/life balance, go to **hbr.org/brown**.

PHOTOGRAPHY: SPENCER HEYFRON

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