Managing Human Resources Risks

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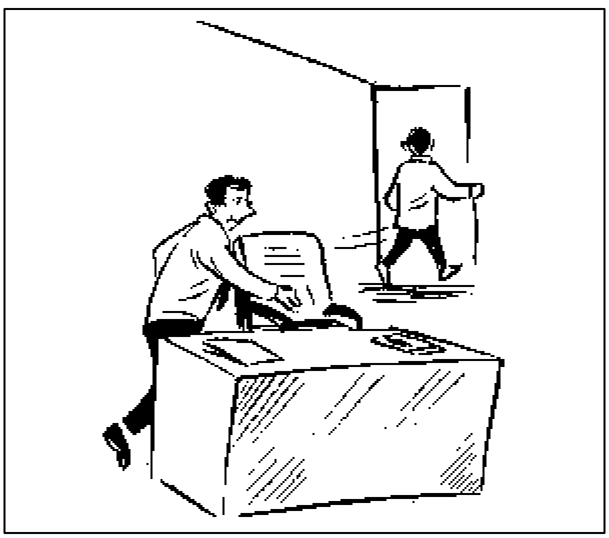
In today's knowledge driven business environment it is the quality of people that ultimately determines the competitiveness of an organization. Great companies attract good people and have mechanisms for retaining and nurturing them. In such companies, there is never a leadership vacuum. On the other hand, in poorly managed companies, good people hesitate to join. Those who do join, lose motivation, get frustrated quickly and leave. Due to a shortage of talented managers, such companies find it difficult to grow fast and exploit the opportunities in the market place. Over a period of time, they lose their competitive edge. In short, human resources management has become more critical than ever before. This article examines some of the important risks associated with Human Resources (HR) and how they can be managed.



Succession Planning

At a strategic level, succession planning is probably the most important Human Resources (HR) risk. The consequences of appointing the wrong successor can be disastrous. Take the case of Westinghouse. A series of wrong CEOs virtually drove the company which was once rated on par with General Electric, into bankruptcy.

Though all CEOs want to avoid a wrong successor, their track record, in this regard is disappointing. Consider the legendary CEO, of Coke, Roberto Goizueta. The aristocratic Cuban had trained his successor, Doug Ivester well and had nominated him as his successor well before his death. When Goizueta died of cancer, Ivester took charge in what the markets perceived to be one of the smoothest transitions ever in a Fortune 500 company.

Yet, a couple of years later, Ivester was found unfit for the task and had to resign. An accountant by training, Ivester had a flair for numbers and had the reputation of a street fighter, unlike Goizueta, who had been a charismatic leader, strategic thinker and delegator. When they were together, Ivester complemented Goizueta well. But after becoming the CEO, Ivester found it difficult to manage some sensitive issues. Towards the end of 1999, he announced his resignation.

Looking back, Ivester's number crunching, financial engineering and technical skills were exceptional but his people orientation and leadership skills were inadequate. Following an incident in Belgium, when

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hundreds of people became sick after drinking Coke, Ivester did not go there for a week. This reflected his inability to appreciate the magnitude of the crisis. Similarly, Coke's failed merger deal with Orangina was mostly due to Ivester's failure in dealing with anti-American sentiments in France. Ivester also seemed somewhat out of place while handling a racial discrimination suit. Quite clearly, Goizueta had trained his successor well but had chosen the wrong successor in the first place.

The problems associated with succession planning are particularly acute in India, where family managed businesses proliferate. Such companies throw discretion to the winds and often spend more time on dividing the family silver among the next generation than in grooming the right person to take over the top job. Family managed companies would do well to remember that the chosen successor should have the necessary education, skills and grooming to appreciate the privileges, responsibilities and challenges involved. They should also be bold enough to appoint a professional manager from outside the family, when there is no suitable candidate within. Some of the more progressive Indian business houses like Ranbaxy, the Murugappa group and the Eicher group have demonstrated a high degree of professionalism in this regard.

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Many Indian companies are now beginning to take succession planning more seriously. At Larsen & Toubro (L&T), one of India's leading engineering companies, many of the company's senior managers are expected to retire in the first few years of the new millennium. CEO AM Naik has named the top 10% of his executives as stars and chalked out a fast track career path for them. This is an attempt to make sure that talented managers are around when positions fall vacant in the coming years. Naik hopes that by 2005[1], "L&T will be in strong hands." Before initiating the program, L&T employed the services of an HR consulting firm to list the positions falling vacant and the required competencies. L&T now fills vacant posts with internal candidates, wherever possible. In some cases, however, it compares the internal candidate with an external applicant to judge the internal candidate's readiness to move into the new job.

What the Board Needs to Do

The board should play an active role in the succession planning exercise. Indeed, choosing the CEO is probably the most important decision the board makes. Unfortunately, many boards do not take succession planning seriously. The directors either due to their cosy relations with the incumbent CEO, lack of concern or simply inertia, are reluctant to broach the subject. It is not simply a matter of chance that many CEOs in major US companies have failed to last even 3 years in recent times. These include Douglas Ivester of Coke, Durk Jaeger of Procter & Gamble, Dale Morrison of Campbell Soup and Jill Barad of Mattel. In India, companies like Thermax have faced crises because of poor succession planning.

Identifying and specifying the attributes the next CEO should have, are challenging tasks. But many boards do not invest sufficient time and effort in this regard. They confine themselves to generalities such as team-building skills or the ability to manage change. Other boards concentrate on technical capabilities to the point of completely overlooking leadership skills. In many cases, future CEOs are judged by their past track record in delivering measurable performance like increase in market capitalization. Quite clearly, a balanced approach, which takes into account the different dimensions of the job in a holistic manner, is necessary.

Leadership is something which is difficult to quantify. But, boards should still identify some parameters for measuring the leadership qualities of a potential CEO. According to Bennis and O'Toole[2], the Board should assess the soft qualities of the future CEO by asking the candidate's peers, subordinates and superiors a series of questions to get an idea about following :

[1] *Business Today, September 21, 2000.*

[2] *Harvard Business Review, May-June, 2000.*

- Consistency in the way the candidate inspires trust in others.
- Ability to introduce a high degree of accountability.
- Ability to delegate.
- Amount of time and effort the candidate spends in developing others.
- Amount of time the candidate spends in communicating the company's purpose and values down the line.
- Comfort level in sharing information, resources, praise and credit.
- Ability to energise others.
- Demonstration of respect for followers.
- Listening skills.

A crucial decision boards have to make is whether to choose an insider or an outsider. Firms in trouble often look for fresh blood. On the other hand, when things are going smoothly, the board is more likely to appoint an experienced insider. According to a study by Nitin Nohria and Rakesh Khurana[3] , an outsider replacing a CEO, who has been fired, tends to do well. But an outsider, who takes over as CEO when the company is doing quite well, often fails miserably. In the absence of a crisis, an outsider may find it difficult to carry the insiders along. So, in the case of an outsider, it helps if the board sends clear signals that there are major areas of concern and the new CEO has been brought in to address them.

Pepsi Co., India recently decided to appoint Rajeev Bakshi, a Cadbury veteran, as its new country head. The search for the successor took almost 3 years. Pepsi Co., headquarted in New York was closely involved in the appointment of the new CEO, though a head-hunter was used to prepare the short-list. Pepsi Co., has a tradition of taking outsiders. In fact, most of the senior managers in its Indian operations have been poached from Hindustan Lever. He is expected to work with current CEO, PM Sinha for about 9 months before Sinha retires. He will also spend 3 months at Pepsi Co's New York headquarters. The general feeling is that Sinha has done a good job of stabilizing Pepsi Co's Indian operations. According to insiders,[4] the appointment of Bakshi may lead to a churn in the top management ranks. Only time will tell whether Bakshi can hold the team, painstakingly put in place by Sinha, together.

Being the designated successor of a powerful incumbent CEO is very often not a happy experience. The power and influence of the CEO tends to upset the succession planning exercise. The incumbent CEO is usually aware that allowing the process to go ahead smoothly gives him a chance to perpetuate his legacy. But he still hesitates and fails to come to grips with the situation. So, when the CEO is powerful and has been around for a long time, the Board's involvement in the succession planning exercise should be greater.

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What the CEO Needs to Do

Many CEOs fail to handle succession planning effectively for a variety of reasons:

- They are so involved with the present that they do not think about the future.
- They forget the big picture and stay focussed on day-to-day operations.
- They have an exaggerated sense of self-importance and begin to think that they are indispensable.
- They are poor in building a second layer of management because of an unwillingness to tolerate good people or to delegate.
- They try to avoid conflict and hesitate to send a clear message to senior managers, who the successor is going to be.
- They continue to play a role in the company even after the new CEO has been put in place.

[3] *Harvard Business School, Working paper, August 1997.*

[4] *Business India, May 28 - June 10, 2001.*

To avoid these pitfalls, CEOs must periodically ask themselves the following questions:

- Is leadership growth keeping pace with business growth?
- Is an adequate member of managers being groomed to keep pace with the strategic needs of the organization?
- Are vacancies in senior management positions being filled up smoothly through internal promotions?
- Are objective plans in place to identify and develop future leaders?

CEOs would do well to be proactive and take care of the following:

- Identify the key leadership criteria and provide support to potential leaders to meet these criteria.
- Select a few high potential leaders and concentrate the resources available on their development.
- Monitor the results of the succession planning process at all levels of the organization regularly.

In short, succession planning is a key strategic issue that needs the time and attention of top management on an ongoing basis. A pro-active approach is far more desirable

The Successor's Dilemma

Some CEOs appoint successors well in advance of their retirement but only to see them leaving prematurely. John Walter, who became the president of AT&T in October 1996 left in just 9 months. Disney's Michael Ovitz had lasted just over a year as president when a souring relationship with CEO Michael Eisner forced him to leave. In Citigroup, heir apparent Jamie Dimon quit in 1998, following differences of opinion with his mentor, Sanford Weill. Merrill Lynch COO Herb Allison, who was strongly tipped to become the next CEO, met with the same fate.

So, a successor needs to be coached well on handling the transition. He should be encouraged to stay in constant touch with the CEO, remain focused and be made to understand that his stakes are much higher than those of anyone else in the company, including the incumbent CEO. The successor must be motivated to seize the initiative and rise to the occasion, displaying the highest possible level of emotional maturity. He should also be made to realize in a subtle way that if he quits, he would harm his own chances of becoming a CEO elsewhere.

The successor should be counselled to put himself into the shoes of the CEO and understand what is going on in his mind. Typically, the CEO goes through 3 phases after the successor has been appointed. In the first phase, he feels good that he has initiated the process and maintains a good relationship with the successor. Then, the CEO starts feeling uneasy as the successor takes charge and begins to shake things up. The CEO realizes that he is losing control and is now having to share his power and authority with the heir apparent. The prospect of leading a sedentary retired life, also starts causing anxiety. Finally, the CEO unless he is a person of extraordinary mettle, develops friction with the heir apparent. At this juncture, an open conflict may develop and the CEO might marshal support from his trusted lieutenants and even encourage people to come to him directly, bypassing the heir apparent. The successor often responds by being even more aggressive and result oriented. If he succeeds, the CEO feels even more threatened. Ironically enough, when the successor is just ready to move into the corner office, he becomes frustrated by the confusing signals sent by the CEO and decides to quit.

In short, succession planning is a key strategic issue that needs the time and attention of top management on an ongoing basis. A pro-active approach is far more desirable than an ad hoc, knee jerk one. It is heartening to note that some Indian companies are taking succession planning very seriously. Some MNC subsidiaries are clear trendsetters in this regard. Hindustan Lever (Lever) spends quite a bit of time and effort on succession planning. Transition from one CEO to another has generally been smooth and there has been no case of any CEO miserably failing in the top job. Succession planning at ITC has also been generally smooth, though one CEO, KL Chugh was probably a wrong choice. A fixed five-year-term for the CEO has lent an air of credibility to the whole process at ITC. In contrast, Coca-Cola India has seen CEOs changing at regular intervals, a clear sign that succession planning has not been very effective. Another Indian company which has been praised for succession planning is Ranbaxy. When Parvender Singh died, his successor, DS Brar, a professional manager, took over the reins without much loss of continuity.

In general, Indian companies still have a long way to go in the area of succession planning. Especially in Public Sector Units (PSUs), succession planning has been a disaster. CEOs have changed frequently and not been allowed to settle down in their jobs. Many of the appointments have been guided by political considerations. The fact that quite a few of the top jobs at PSUs are either unfilled or manned by acting CEOs is a clear indication of the lack of importance attached to succession planning. The crisis at Unit Trust of India (UTI) in recent times has much to do with a totally ad hoc approach towards CEO succession planning. In many Indian companies, CEOs spend more time protecting their turfs than in developing the next line of leadership. Unless this attitude changes, they may find themselves facing crises from time to time.

> ***The increasingly knowledge intensive nature of many businesses creates serious problems when talented employees leave***

Attracting and Retaining Employees

Turnover of key employees is another big HR risk that companies face today. The increasingly knowledge intensive nature of many businesses creates serious problems when talented employees leave. So, companies must do what is necessary to retain their best managers. Attracting and retaining talent is not just a matter of higher salaries and more perks. It involves shaping the whole organization, its vision, values, strategy, leadership, rewards and recognition. Thus, companies must look at retention as an exercise that ensures long-term employee commitment rather than as a knee jerk response to hold back employees after they resign.

An effective retention strategy must be built around the following:

- Taking note of the company's culture, designing and building the ideal culture.
- Assessing potential candidates for hiring, following careful hiring practices.
- Measuring and understanding the issues driving retention.
- Putting in place well designed career-development plans.
- Designing an attractive and transparent reward system.

Building the right culture is an important step in improving employee loyalty. It involves understanding the existing values, clarifying business goals and strategy, defining the desired culture and introducing change management initiatives, wherever necessary to correct the state of affairs. Fostering the ideal work culture involves various steps:

- Hiring people with leadership potential rather than just managerial potential.
- Articulating a strong corporate purpose that makes people believe that they are making a positive impact on society.
- Treating people with dignity and respect.
- Interacting regularly with employees talking to them to understand the problems they are facing and giving them the additional resources they may need to discharge their responsibilities efficiently.
- Attempting to influence rather than control employees.

Hiring the right candidate is a challenging and difficult task. Yet, hiring practices in most companies leave a lot to be desired. Often, the process is reactive and aimed at filling up vacant positions. Very often, managers get impressed by resumes. Later, the performance of the selected candidate falls short of expectations. As Jack Welch has put it[5] , "In the hands of the inexperienced, resumes are dangerous weapons. Eventually, I learned that I was really

[5] *In his autobiography, "Jack, Straight from the gut."*

looking for people who were filled with passion and a desire to get things done. A resume didn't tell me much about that inner hunger. I had to 'feel' it." Interviews are conducted by untrained managers, who do not appreciate that most candidates are good at projecting themselves well during interviews. Questions are often predictable and candidates come well prepared to answer them. Examples include: What are your strengths and weaknesses? Where do you see yourself 5 years from now? Candidates are taken at face value and the answers they give during interviews are not probed further. Another mistake made by recruiters is stereotyping based on race, gender, and nationality. Being carried away by one good attribute and totally ignoring other attributes is another pitfall. Consequently, companies fail miserably in predicting a candidate's performance on the job.

Leaders, who believe in treating employees fairly, build employee loyalty. Those who fire employees indiscriminately erode loyalty

Many companies insist on references but do not understand their limitations. In most cases, referees usually mention only the good things about the candidate as they care more about their personal relationship (with the candidate) rather than contributing towards making a good hiring decision. Another common mistake made by managers is delegation of important jobs such as job description and initial screening to junior employees who are not trained or properly briefed. Hidden agendas, like the desire to put close friends or trusted lieutenants in the vacant job also lead to wrong hiring decisions. Many job searchers focus on the boss's requirements and/or the interests of the candidate's subordinates. Yet, it is also important to look at the traits valued by peers. Competencies should be defined clearly. Otherwise, the same term may mean different things to different people. Many companies spend far too much time unproductively using open advertisements for filling positions. Personal contacts, which can quickly throw up a list of potential candidates, are more cost effective. Well-managed companies encourage their employees to "refer" competent candidates. Cisco is a good example.

Above all, retaining employees is a matter of building loyalty. More often than not, the ability to develop loyalty is linked to the credibility of the top management. CEOs must demonstrate leadership by practising what they preach. For example, CEOs, who have the courage to recall defective products, even when heavy expenses are involved, send the right signals to employees. Those who simply pay lip service to customer care end up confusing employees. Leaders, who believe in treating employees fairly, build employee loyalty. Those who fire employees indiscriminately erode loyalty.

Complex organizations create bureaucracies and slow down decision-making processes. Using small teams facilitates faster and entrepreneurial decision-making. It also increases accountability and makes it easier to recognize achievers. High achievers relish such a work environment. So, to retain talented employees, bureaucracy must be killed ruthlessly. There is no better example of a CEO, who doggedly fought bureaucracy, than Jack Welch of GE.

Long-term relationships can be nurtured only in an environment of trust. This demands two way communication. Meeting employees regularly, listening to their problems and taking appropriate action where necessary go a long way towards building employee loyalty.

Frederick F Reichheld [6] makes a distinction between "low-road" and "high-road" companies. He argues that low-road companies, which have a single-minded focus on financial results, take a big risk. Such companies take advantage of customers, employees, vendors and other business associates whenever they are vulnerable. He adds "The goal of strategy at those companies is to create market power; The job of leaders is to use that power to strangle competitors, bully vendors, intimidate employees and extract maximum value from customers... In this

[6] *Harvard Business Review, July-August, 2001.*

Darwinian struggle, only the toughest individuals survive. Trust and loyalty are weaknesses to be exploited." As long as there is status quo, things are fine but once a new technology or competitor emerges or there is a serious crisis, such companies are overwhelmed by the turn of events with few committed employees around to handle the situation. High-road companies on the other hand try to create win-win situations and invest in building long-term employee loyalty.

To sum up, talented employees like to continue their association with an organization when the following conditions hold good:

- The company is able to inspire the employees through its vision.
- Employees find a greater meaning in the work they do.
- The company is focused on getting results.
- Employees are convinced that rewards and recognition are linked to contribution and performance.
- Employees are rewarded for their innovation and creativity.
- The organization supports the growth of the employees and their development.
- Employees are convinced they can trust the top management.
- Employees feel that they are valued by the organization.
- The organization shares information in a transparent manner.
- The company encourages prudent risk-taking.
- The top management takes feedback from employees regularly.
- The employees perceive the compensation they get to be fair in relation to the work they do and in comparison to similar organizations.

One final point needs to be made here. Just as it is important to hire and retain good people, so is it necessary to remove the non-performers and misfits to protect a performance-oriented culture. GE uses the vitality curve, (a type of normal distribution) to identify the bottom 10% of the people who are asked to leave every year. Welch has explained the importance of dealing with such people decisively[7] : "Some think it's cruel or brutal to remove the bottom 10% of our people. It isn't. It's just the opposite. What I think is brutal and false kindness is keeping people around who aren't going to grow and prosper. There's no cruelty like waiting and telling people late in their careers that they don't belong, just when their job options are limited."

Good managers clarify the job responsibilities and ask employees to define their personal priorities

Aligning Individual Aspirations with Organizational Goals

Many talented employees leave their organization not because they are unsuccessful in their jobs but because they become fatigued and burnt out, due to long hours on the job. Managers have to help employees find the balance between work and their personal life. Good managers clarify the job responsibilities and ask employees to define their personal priorities. By defining goals very clearly and by being focused on the results than the process, they succeed in giving employees a lot of autonomy. Good managers also recognize and support the full range of the people's life roles. This deep interest strengthens the bond with the employees who learn how to establish boundaries and stay focused on the job.

In good companies, managers regularly examine whether conflicts between work and personal priorities are due to work place inefficiencies. They regularly experiment with work processes to improve the organization's performance and the lives of its people. They question basic assumptions and develop innovative workplace processes, to facilitate the achievement of goals without in any way compromising the personal interests and priorities of employees. They have an open mind towards modern day work practices such as flexi working hours and allowing employees to work from their

[7] *"Jack, Straight from the gut."*

homes or from the location of their choice. Consulting and computer software companies tend to fall in this category.

Today's knowledge oriented business environment is characterized by ever rising employee aspirations. Employees are ambitious and want to achieve a lot in very little time. At the same time, they want to maintain a balance between work life and family life. Innovative techniques are hence needed to understand the inner motivations of employees and manage them intelligently. Many people leave their organizations because of a wrong assumption on the part of senior managers that people who are doing well in their current jobs are also happy. According to Timothy Butler and James Waldroop [8], the best way to retain the star performers is to ensure that the jobs they do match their embedded life interests, which are "long held, emotionally driven passions, intricately entwined with personality and thus born of an indeterminate mix of nature and nurture." The activities that make people happy are determined by their deeply embedded life interests. Such interests are displayed during childhood and remain stable thereafter but manifest themselves in different ways at different points in a person's life. Butler and Waldroop use the term job sculpting to describe the art of matching people to jobs consistent with their embedded life interests. The main problem with *job sculpting* is that not too many people are aware of their deeply embedded life interests. Indeed, many people do not know at least till they are midway through their career, the kind of work that will make them happy.

The process of filling up vacancies and the role of the HR department need to be changed to help people pursue their embedded life interests. People are often promoted either because a vacancy has to be filled up quickly or because they complain about inadequate growth opportunities. HR departments often use standardized methods based on personality to determine the type of jobs, employees should handle. Butler and Waldroop argue that job sculpting requires an ongoing dialogue between the employee and the boss and cannot be delegated to the HR department. To become good job sculptors, managers need to improve their listening skills. When employees describe what they like or do not like about their jobs, managers must pick up cues. In the performance appraisal form, employees can be asked to write about the kind of work they love or what they most like about their current job. This could be an excellent starting point for employees to open up and start articulating what they would really like to do. Based on these inputs, the next assignment can be suitably selected. As Butler and Waldroop put it: "In the knowledge economy, a company's most important asset is the energy and loyalty of its people—the intellectual capital that unlike machines and factories, can quit and go to work for your competition… To turbocharge retention, you must first know the hearts and minds of your employees and then undertake the tough and rewarding task of sculpting careers that bring joy to both."

Concluding Notes

The way an organization hires and develops people, to create the leaders of tomorrow has tremendous implications for its long-term competitiveness. Ultimately, it is the quality of people that separates an excellent organization from an average one. So, companies have to pay special attention to the HR risks they face and handle them in a systematic, proactive and coordinated manner. This in turn calls for a detailed examination of specific areas such as leadership development and recruitment and taking suitable steps to revamp the organizational mechanisms and processes, wherever necessary. In short, HR risks deserve far more attention than they have received till now. They also need a more active involvement of the top management.■

Reference # 15-02-09-03

[8] *Harvard Business Review, September-October, 1999.*