Problems with the Silicon Valley Style of Management

By A V Vedpuriswar
Naveen Das

What makes a region globally competitive? Answers to this question can be found by understanding the reasons behind the spectacular growth of what is today the world's most famous industrial hub, Silicon Valley. In a 50 mile long corridor stretching from San Jose to San Francisco, companies are demonstrating how knowledge can be effectively utilized to generate wealth at a rate which other regions cannot even dream of. Over the years, the Valley has given birth to several world class hardware and software companies including Intel, Hewlett Packard, Sun Microsystems, Oracle Corporation, Apple Computer and Cisco.

The transformation of the Valley from a region of apricot and prune orchards into a global innovation centre has indeed been remarkable. The Valley has become famous today for its risk-taking culture that facilitates the incorporation of a company within hours. Its ability to transform a concept into a company in no time is unmatched. Sun Microsystems CEO Scott McNealy recalled the ease with which his company started operations: "We were able to open a checking account on our word. We were able to rent a building without showing an ID. We were able to get phone lines and Wilson Sonsini (a law firm in Palo Alto) filled a huge boardroom table full of documents for us to sign. Actually, on their word processor, they just changed a previous name to our name."

The growth of Silicon Valley: A brief history	
1931	David Packard and William Hewlett, founders of Hewlett Packard begin a long and rewarding partnership. In 1938, they obtain a loan from a Stanford professor, Fred Terman, to make an audio oscillator.
1955	William Shockley sets up Shockley Labs in Palo Alto. Two years later, Gordon Moore and Robert Noyce set up Fairchild Semiconductor, the first company to work exclusively in Silicon Valley.
1959	Noyce files a patent for the integrated circuit. Five years later, Moore predicts that the number of transistors that fit into a chip will double every two years.
1968	Noyce and Moore quit Fairchild and pool $250,000 to set up Intel, which introduces its first microprocessor, 4004 in 1971.
1976	Apple computer is set up by Steve Jobs and Steve Wozniak.
1977	Larry Ellison sets up Software Development Laboratories, the forerunner of Oracle.
1980	Apple makes the biggest public offering since Ford in 1956.
1982	Sun Microsystems is founded by Stanford University students, Vinod Khosla, Scott Mc Nealy and Andy Bechtolsheim.
1984	Leonard Bosack and Sandra Lerner set up Cisco Systems to develop networking technology.
1993	Intel unveils the Pentium Microprocessor.
1994	Jim Clark and Mark Andreassen set up Netscape. A year later, Netscape goes public.
1997	Steve Jobs returns to Apple.
1998	The Valley's growth continues, fuelled by Internet start-ups.
2000	Growth slows down in the Valley. Companies announce they are retrenching staff as the technology sector slows down. Cisco is among the companies affected badly. Many Valley residents realise that they are unable to maintain their lavish lifestyle.

The Valley has fostered a culture where penalties exist not for failures, but for not trying. Failure is considered a badge of merit. The business environment has bred a class of entrepreneurs called 'repeaters' who often fail in a new venture, but learn the lessons well and come back to tie up venture capital and run a successful business. The Valley's strong belief seems to be that an entrepreneur who has good ideas and stumbles, comes away with enough lessons to get it right the next time.

Due to its phenomenal capability to innovate and fuel start-ups, the Valley's style of doing business has been well researched and documented. Companies in the Valley are known to be lean and mean. Many of them like Cisco depend heavily on outsourcing. Valley companies are also known to give generous stock options to their employees. At the same time, employees are aware that they can lose their jobs if things turn sour. Does all this mean that the Valley's management style should be replicated in other parts of the world? Jeffrey Pfeffer, in a recent article in the Sloan Management Review (Spring 2001) argues that all is not well with the Silicon Valley management style. He feels the style is suitable for creating start-ups but not for sustaining and building an organization in the long run.

Pfeffer argues that the Valley culture, which encourages employees to move on to greener pastures, has led to heavy turnover. Valley companies do not do enough to retain people. Many good people leave and often emerge as formidable competitors. Recruiting and training costs have gone up significantly. A more stable and steady work culture, that is needed to build organizations, is clearly lacking in the Valley. Pfeffer's views are shared by Christopher Klaus, founder of Atlanta based Internet Security Systems, "The start-ups just suck people out of your company." ISS had a turnover of 1 to 2% annually, against the Valley's 25% during early 2000.

Use of contract labour and outsourcing, while adding flexibility, has also meant lost opportunities. Many employees do not share their knowledge freely when they know their contracts will be terminated at the end of the year. Pfeffer argues that performance of important activities outside the company has led to diminished customer retention, reduced productivity and fewer opportunities for developing intellectual capital within the organisation. Jason Krantz, an American entrepreneur who decided not to shift the operations of his internet start-up, Infineta Inc to the Valley, has supported Pfeffer's argument: "If you're going to build a sustainable business, you really need the knowledge to stay in your company."

The Valley's compensation practices, such as providing signing bonuses and stock options, have proved counterproductive, by encouraging people to take too many risks. People go for broke. If they win, they continue and if they lose, they move on. In other words, stock options have not made employers feel like owners, or created any long term orientation. Of course, in the wake of the recent technology meltdown, most of these options are worthless. This has proved traumatic for people used to a lavish style of living.

The Valley's culture of working long hours is also having its impact. It is causing burnouts and breakdown of family life. Pfeffer argues that these long hours, far from reflecting loyalty to the company, are actually used by employees in building networks and preparing resumes, i.e. for personal gains.

As Pfeffer concludes: "In the short run, with enough venture money and enough product demand, any business model may appear feasible. In the long run, those companies that actually run their businesses efficiently and produce sustainable results will be the ones you keep reading about."

References

1. Michael J Mandel, "Taking its place in the pantheon," August 25, 1997, www.businessweek.com

2. Jim Kerstetter, etal, "The dark side of the Valley," *Business Week*, July 17, 2000, pp. 44-45.

3. Jeffrey Pfeffer, "What's wrong with management practices in Silicon Valley? A lot," Sloan Management Review, pp 101-102.