Improving the way organizations run through participative planning and management.
The Ritz-Carlton Hotel Company
1992 and 1999 Malcolm Baldrige Quality Award Winner

Introduction

Horst Schulze—Most people think that the Ritz-Carlton is an old company in the hotel business. It is not. When I joined the company in 1983, as its first employee, it did not yet own a single hotel. Later that year we purchased the Ritz-Carlton Hotel in Boston, Massachusetts, together with exclusive rights to the Ritz-Carlton trademark for North America, the foremost name in luxury hotels. We knew that although we didn’t have to build a great reputation, we did have to live up to one.

With our purchase of the Boston Ritz-Carlton, and two new hotels under construction, 1983 was the beginning of our company and our dream to create something exceptional. In 1984 we opened our first hotel in Atlanta, Georgia, and the second hotel soon after, also in Atlanta. By the following year we had added hotels in Laguna Niguel, California, and Naples, Florida, to our holdings in Atlanta and Boston—none of them in what could be considered a strategic location. The prevailing wisdom was that if you wish to start a hotel chain, you should begin in New York City, Chicago, or San Francisco. That way you will be assured the strategic advantage of high visibility within the travelling community.

Nevertheless, we persevered, and we were named “Best Hotel Company” by several consumer groups and travel agencies in 1986. Our guests didn’t always agree. It became clear to us that being “best” in this case meant only that we were the best of a poor lot. Our need to achieve higher standards, coupled with the demands of a rapidly growing portfolio of hotels under construction, led the leadership team to personally take charge of managing for quality and to adopt the Malcolm Baldrige National Quality Award Program Criteria.

Adoption of the Baldrige Criteria

The Baldrige Criteria provided the comprehensive structure we needed to optimize our performance. In 1989 we started to organize the company around the Criteria. We began to learn the language of quality. Although there were times we thought that the Criteria weren’t for us, we soon learned that we were only at the beginning of our journey. Today we have 36 operating hotels and 30 more under construction worldwide—all of which use the Baldrige Criteria. In 1992 we received...
Adoption of the Baldrige Criteria, continued

our first Malcolm Baldrige National Quality Award. In the following years we continued to apply the principles of the Baldrige Criteria, and we increased leadership's role in our structured approach to business excellence. We are pleased to have won the award again in 1999.

Quality starts with leadership

At the Ritz-Carlton Hotel Company, quality starts with leadership. Leadership creates the vision and sets the standards in all areas. It makes sure that the entire organization is aligned. Leadership must be committed to everyone it serves: customers, employees, the communities in which we operate, and investors. The most important of these commitments is safety. Our customers and employees must be safe at all times. Safety is designed into our processes and technology. All of our food and beverage employees are trained and certified in food safety principles and alcohol beverage service. Employees are trained, and personal safety instructions are given to all of our guests. We have emergency action teams and monthly safety drills. We even have a special program to protect our youngest guests. A wholehearted commitment such as this has to come from the leadership.

The pyramid

Leadership, of course, has to have a plan. At the Ritz-Carlton we depict our strategic plan as a pyramid (Figure 1). At the top is our 10-year vision: to be the...
The pyramid, continued

premier worldwide provider of luxury travel and hospitality products and services. Beneath that is our five-year mission. Every Ritz-Carlton Hotel, wherever it is located, is expected to achieve product and profit dominance. Our objectives, tactics, strategy, method, and foundation support the five-year mission. The foundation of the Ritz-Carlton Company is built upon our values and philosophy, and Credo. Everyone has to feel it, understand it, and be able to know how to measure it. Without that foundation, everything else would falter.

The Gold Standards

The Credo is the heart of our leadership (Figure 2). It says that the Ritz-Carlton Hotel is a place of genuine caring and comfort to its guests. Note that it doesn’t say “highest occupancy rate,” although we do want to achieve a high occupancy. Our highest mission is to genuinely care about our guests. We don’t just give them a bedroom; the whole experience is the product we provide. The Ritz-Carlton is a place where we want to instill a sense of well-being in our guests. The real measure of the quality of our product is whether we instill that sense.

Figure 2. The Ritz-Carlton Credo and Motto.

<table>
<thead>
<tr>
<th>Credo</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Ritz-Carlton Hotel is a place where the genuine care and comfort of our guests is our highest mission.</td>
</tr>
<tr>
<td>We pledge to provide the finest personal service and facilities for our guests who will always enjoy a warm, relaxed yet refined ambience.</td>
</tr>
<tr>
<td>The Ritz-Carlton experience enlivens the senses, instills well-being, and fulfills even the unexpressed wishes and needs of our guests.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Motto</th>
</tr>
</thead>
<tbody>
<tr>
<td>“We are Ladies and Gentlemen serving Ladies and Gentlemen.”</td>
</tr>
</tbody>
</table>

Our values are represented in our Motto. It says, “We are Ladies and Gentleman serving Ladies and Gentlemen.” The message is clear: employees are to respect every guest as a lady or gentleman, and at the same time the organization is to respect every employee as a lady or gentlemen. We serve, but we are not servants.

Most organizations talk about the importance of service today. Because service is the foundation of our company, we realized that the term must be clearly defined as well. Service at the Ritz-Carlton has three steps (Figure 3 on the following page). We also have a promise that we make to the Ladies and Gentlemen we employ. Our Credo, Motto, and the Three Steps of Service are discussed in the Ritz-Carlton Basics. The Basics are our 20 fundamental expectations about job performance and responsibility for quality, which we continually share with our employees. The Credo, the Three Steps of Service, the Promise, and the Basics together make up our Gold Standards, which have an incredible empowering effect on the Ritz-Carlton.
The Ritz-Carlton Hotel Company: 1992 and 1999 Malcolm Baldrige Quality Award Winner

CASE STUDY

The Gold Standards, continued

The specific actions our senior leaders take to deploy our approach consist of three major processes:

1. Working with the Ladies and Gentlemen, using a combination of hands-on behavior modeling and reinforcement, during the seven-day countdown to the opening of new hotels. The president and chief operating officer personally demonstrate the guest/employee interface image. They also facilitate the development of the vision statement for each newly formed department.

2. The decisions from the strategic planning process are arranged in a "Pyramid Concept" and distributed throughout the organization.

3. The Gold Standards are reinforced daily by new employee orientation, training, meetings, displays, discussion of the mission statement and Credo, and peer pressure.

Leadership effectiveness is evaluated by our semiannual employee satisfaction results, which measure whether or not the leader has gained the full support of the Ladies and Gentlemen in achieving our Gold Standards. Figure 4 on the following page shows the satisfaction results. Our effectiveness is also measured by audits on areas of public responsibility, such as safety systems, and food and beverage preparations.

Gaps in leadership effectiveness are addressed with development/training plans.
If there is a widespread deficiency, the corporate human resource function develops or improves courses, processes, or facilities. In addition, we also make use of developmental job assignments.

We are often asked by many people outside our company, “What does quality do?” My answer is “Quality produces results.” We know that without a commitment to quality we would not be the premier provider, dominant in product and profit in each one of our locations.

**Strategic Planning**

Patrick Mene, James Schultenover—Strategic planning at the Ritz-Carlton is the way we set direction for business excellence. After 10 years of Baldrige implementation, we have come to realize that we must fully understand the larger environment in which we operate before we begin our annual strategic planning.

We have improved our strategic planning process by using what we call a Macro-Environmental Analysis, which looks at the wider business environment now and into the future. This analysis addresses changes such as sociological trends, supply and demand, requirements of our owners, and our employees. (There are some business analysts who believe that the room stock is a larger factor in a hotel’s success than quality; we do not necessarily agree, but we do look at that factor.) Customer and Market Focus is an intricate part of this analysis. We use this information to try to understand the worldwide economic outlook.

Horst Schulze, the 12 senior leaders who report to him, and I are responsible for collecting the data for the Macro-Environmental Analysis. Our parent company (Marriott Corporation) has an organization of specialists in strategic planning who also work with us to collect this data. We use this Macro-Environmental Analy-
Macro-Environmental Analysis, continued

The planning process begins in March and runs through June. (Step 1) Using the Macro-Environmental Analysis, the senior leaders either confirm the 10-year vision, the five-year mission, strategy, and the methods and foundation, or they make changes to them. (Step 2) Using the Macro-Environmental Analysis, strategic mandates are identified along with gaps in performance. (Step 3) The strategic mandates and gaps are used to create the Vital-Few Objectives for the next three years. The objectives are designed to address the projected gaps identified in the Macro-Environmental Analysis and to maintain or enlarge any advantage we have over our competitors.

Vital-Few Objectives are separated into multiple categories to respond to the strategic mandates, and to represent all who are affected by the Ritz-Carlton. The output of this step becomes our Pyramid. One of the Vital-Few Objectives is our employees' pride and joy, and satisfaction. We have found that there is a strong relationship between the creative spirit we want our people to have, and the pride and joy that they can take in their work. Other Vital-Few Objectives are customer loyalty, reducing customer difficulties, enlarging sales income, and increasing profitability.

Deployment of the plan

During the months of July through September, the senior management begins deployment of the Vital-Few Objectives (Figure 6 on the following page).

(Step 1) Key production processes are identified by three criteria: very important, of increasing importance, or work that is poor in comparison to competitors. This ranking is done by process owners at the corporate level. (Step 2) Support processes are deployed to the support functions of the organization. These processes indirectly affect our products and enable us to reach our Vital-Few Objectives. (Steps 3 and 4) We involve the Ladies and Gentlemen of the Ritz-Carlton to learn what resources we require to reach our Vital-Few Objectives. We communicate the measures and targets of our Vital-Few Objectives to the lower levels of the organiza-
Deployment of the plan, continued

Figure 6. The Deployment Process.

Deployment Process

1. Develop Production Process
2. Deploy Support Processes
3. Develop Preliminary Plans/Budget for L.L.C. and Hotels
4. Finalize Ritz-Carlton Pyramid Plan, Budgets for L.L.C. and Hotels
5. Reinforce Pyramid Concept/Plans/Budget
6. Communicate Pyramid Concept to the Ladies and Gentlemen
7. Execute Plans
8. Daily Line-Up Reinforcement, Ongoing Throughout the Year
9. Evaluate/Improve Planning Process

July - September
October - February

They identify the tasks that, if done, will meet the objectives. The lower levels then submit the “bill” to perform these tasks. Activities that have been agreed upon are then incorporated into our financial planning and budget process.

Even though we are a two-time Baldrige winner, we’ve had to learn some hard lessons. While we understood our customers and had a great planning process, sometimes we could not get the resource allocations right. It took us a long time to learn how to make sure that people had the right resources for each one of our processes. Too often at planning time, we’d find out that while an overhead process had more than enough resources, there weren’t enough basic items, such as coffee cups, to serve customers.

(Steps 5 through 7) In the early fall the pyramid concept is reinforced during our semiannual general managers’ meeting. Then the pyramid is communicated to the Ladies and Gentlemen of the Ritz-Carlton, who then execute the plan.

Publishing the pyramid, or any plan, does not create automatic results. To deploy the plan we subdivide the goals and assign responsibility at the process level. For example, the lodging people own the housekeeping and check-in processes, the conference service people own meeting planning, food and beverage people own restaurant services. We use what we call the Greenbook, our logic process and tools, to improve our products and processes. Everyone is involved in choosing measurements.
Deployment of the plan, continued

(Step 8) Throughout the year, in every work area, on every shift, a brief line-up meeting is held. During these formative sessions, the Pyramid concept is reviewed, the Gold Standards are reinforced, and good ideas are shared. (Step 9) Every year the vice president of quality evaluates and improves the planning process.

The review process

Corporate and hotel upper management reviews performance of the strategic plan monthly. The framework of a typical review is shown in Figure 7. The opportunities for improvement are decided upon by process owners with assistance from the directors of quality. The findings and actions are communicated through the hierarchy, process owners, and our quality newsletters. We ensure performance against these objectives by our Service Quality Indicators (SQIs), the 12 most serious concerns in the eyes of the customers.

![Figure 7. Framework for Typical Performance Review.](image)

Planning for customer priorities

I am, as many of my colleagues at the Ritz-Carlton are, a classically trained hotelier. We are very visually oriented people. During our implementation of the Baldrige Criteria, I've learned that although the sparkle of the chandeliers is important, it is not the only priority of our guests. It doesn't matter that the petunias are perfect, if the valet dents your car or your bill is wrong. We've learned to make our customers' priorities, our priorities.

Ordering these customer priorities is also crucial. We found that we cannot have employees dealing with trivial priorities daily, without the needed resources for crucial ones. When employees cannot serve coffee because we haven't ordered enough cups, or they can't put guests in the right room, and they have spent the better part of their day saying “Please forgive me” to our guests, their pride and joy in their work evaporates. Pride is a very powerful emotion; once it is gone, futility or anger sets in. The accountants may disagree, but I have found that there is nothing more valuable to us than a loyal guest and our employees' pride and joy in their work.
Customer and Market Focus

James Schultenover, Patrick Mene—The hotel industry has a long history and, unfortunately, so have many of its practices. The industry has been slow to adapt and quick to copy. We were the last industry to adopt technology to improve business processes. In the 1980s, hotels raced to copy one another in providing bigger soaps or imported chocolates. We are also traditional in how we prosper: when the times are good, we raise prices, and when times are bad, the soaps get smaller and the chocolates disappear.

The Baldrige Criteria changed all that at the Ritz-Carlton, and it has provided us a powerful competitive advantage. We’ve shifted from looking “out” from our own perspective to looking “in” from the customer’s. We learned that customer research has to be integrated, comprehensive, and systematic, and it should be driven by customer criteria.

We also realized that good customer satisfaction ratings weren’t enough— we need customer loyalty. A satisfied customer may decide to try another hotel; a loyal customer will instruct his travel agent to always book him at the Ritz-Carlton. We want to look at the “top box” rating, not the roll-up of all the satisfaction numbers (Figure 8 below and Figure 9 on the following page). A fact of life in the hotel industry is that 95% of the customers who switch vendors rated themselves as being satisfied before the switch—that is a number that makes us very nervous. The strategic value of a loyal customer base is very high—the companies that will last are the ones with a solid base of loyal customers.

<table>
<thead>
<tr>
<th>Source: Nationwide Surveys</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Figure 8. Frequent Leisure Traveler 1999 Key Comparisons.</strong></td>
</tr>
<tr>
<td><strong>Top 2 Boxes</strong></td>
</tr>
<tr>
<td>Ritz-Carlton</td>
</tr>
<tr>
<td>Overall Satisfaction</td>
</tr>
<tr>
<td>Cleanliness of Room &amp; Facilities</td>
</tr>
<tr>
<td>Adequate Security</td>
</tr>
<tr>
<td>Value for the Money</td>
</tr>
<tr>
<td>Staff Knowledgeable &amp; Helpful</td>
</tr>
</tbody>
</table>

Sources of data

We have many sources of customer research at the Ritz-Carlton. A noteworthy tool that we use is CLASS, an automated “memory system” that links returning guests to their preferences. The Ladies and Gentlemen and our suppliers are then apprised of what is new and different about each individual customer or event, enabling them to better serve that customer. This practice creates lasting relation-
Realizing the value of customer loyalty, continued

The 6P’s Concept

We benchmarked Procter & Gamble Company, and from them learned the 6P’s Concept, which lays the groundwork for our product and process design. After we develop a full understanding of our market segments, customers, and their priorities, we develop and distribute internally a 6P’s Concept. This consists of the:

1. **Problem** (customer problem or need). It is no longer sufficient for us to depend upon our brand name. That may conjure up a positive image in the customers’ minds in San Francisco or Singapore, but we have competitors in every market. Unless we identify a need or problem for a customer and meet it, we are just another pretty hotel that competes on price.

2. **Product** (what it is). This is the product definition statement.

3. **Promise** (what it can do for the customer; or what can the customer do or enjoy because of this product). We used to say that we provide the finest personal service, but that may mean very little. We have found that we have to be very specific about the services we provide.

4. **Personal Advantage** (what the whole value is to the customer).

5. **Positioning** (what can the customer latch onto in their mind as a differentiation). For example, BMW is the “ultimate driving machine.” That slogan creates a very clear picture in the customer’s mind about how the car will perform, drive, and sound. We have a hotel on the San Francisco peninsula, halfway between the city and Silicon Valley, whose position is “You’re as connected or as far away as you want to be.”

6. **Price/Value** (what customers must give up in time or money to get it).

We have found that the problem, the promise, and the position statement are the most difficult to write because they must be the most specific. We develop a 6P’s
The 6P’s Concept, continued

concept for every new hotel, and once a year we reevaluate it for all existing hotels. We then take it a step further by defining the 6P’s for each major customer segment. The 6P’s equal relevancv; without it, we do not have a unique position with which we can provide a market-by-market solution.

Figure 10 lists the major measures in our Sales and Marketing Performance Management System. Advance Bookings is a leading indicator; the rest are lagging indicators (the longest lags by 45 days). The effectiveness of our Customer and Market Focus is evaluated through reviews of our standard performance measures daily, monthly, and annually. Service Quality Indicators (SQIs), the 12 most serious defects, and RevPAR (revenue per available room) by market segment are reviewed daily at each hotel. Advance bookings, customer satisfaction, RevPAR by market segment, and the P&L statement are reviewed monthly. Incidentally, we've performed a number of analyses and found that every time we increase customer satisfaction by one percentage point, our profitability goes up by two to five percent. The annual reviews at the corporate level are contained in our strategic planning pre-work, and Macro-Environmental Analysis. The daily and monthly reviews identify performance gaps to be corrected. An extensive review of the Macro-Environmental Analysis confirms or drives changes in our marketing strategy, objectives, and plans.

**Figure 10. Sales and Marketing Performance Measures.**

<table>
<thead>
<tr>
<th>Subject</th>
<th>Precede/Lag Operations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advance Bookings</td>
<td>Precedes up to Several Years</td>
</tr>
<tr>
<td>Service Quality Indicators (SQI)</td>
<td>Lags by 1 Day</td>
</tr>
<tr>
<td>(Measure the Gold Standards)</td>
<td></td>
</tr>
<tr>
<td>RevPAR</td>
<td>Lags by 1 Day</td>
</tr>
<tr>
<td>(Revenue Per Available Room)</td>
<td></td>
</tr>
<tr>
<td>Customer Satisfaction Determination</td>
<td>Lags by 45 Days</td>
</tr>
<tr>
<td>The P&amp;L Statement</td>
<td>Lags by 40 Days</td>
</tr>
</tbody>
</table>

**Information and Analysis**

Bob Warman, Pam Angelucci, John Timmerman—There are two basic types of measurements used at the Ritz-Carlton: organizational measures for upper managers at the both the hotel and corporate level, and operational (process) measures for planning, assessing, and improving daily operations at the hotel level. The organizational measures assess employee and customer satisfaction and RevPAR growth, sometimes owner satisfaction (profit) measures are included. Employees are surveyed quarterly, and customers are surveyed after they have had a period of time to reflect
Organizational measures, continued

upon their stay. We use J.D. Power and Associates to administer the surveys. Not only does increased employee satisfaction drive customer satisfaction, increased customer satisfaction drives increased RevPAR growth as well.

Operational measures are used in daily operations and for process management. We also make an additional distinction as to whether the measure provides information before, during, or after operations (Figure 11).

**Figure 11. Operations Measures.**

<table>
<thead>
<tr>
<th>Subject</th>
<th>Unit of Measure</th>
<th>Use</th>
</tr>
</thead>
<tbody>
<tr>
<td>Before Operations Measures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject</td>
<td>Unit of Measure</td>
<td>Use</td>
</tr>
<tr>
<td>Macro-Environmental Analysis</td>
<td>Summaries of Performance, Money, Ratios, Indexes</td>
<td>Annual input for senior leaders to reset organizational and operational measures</td>
</tr>
<tr>
<td>New hotel development</td>
<td>Defect Points (i.e., PQI)</td>
<td>Measures for senior leaders to plan, assess, and improve each new hotel development</td>
</tr>
<tr>
<td>Daily variable demand</td>
<td>Production/Hours Worked Ratio</td>
<td>Plan daily operations and pricing</td>
</tr>
<tr>
<td>During Operations Measures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject</td>
<td>Unit of Measure</td>
<td>Use</td>
</tr>
<tr>
<td>The Gold Standards</td>
<td>Taste, Sight, Smell, Sound, Touch</td>
<td>Operational measures for the individual employee to plan, assess, and improve their work</td>
</tr>
<tr>
<td>After Operations Measures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subject</td>
<td>Unit of Measure</td>
<td>Use</td>
</tr>
<tr>
<td>Vital-Few Objectives</td>
<td>Organizational Performance Indicators, Money, 1 – 5 Scale, Percentages</td>
<td>Improve Organizational Performance</td>
</tr>
<tr>
<td>Key Production and Support Processes</td>
<td>Weighted Defect Points (SQI)</td>
<td>Improve Daily Operations</td>
</tr>
<tr>
<td></td>
<td>Production/Hours Worked Ratio</td>
<td></td>
</tr>
<tr>
<td></td>
<td>RevPAR</td>
<td>Improve Pricing Policies</td>
</tr>
</tbody>
</table>

Before Operations Measures assess the development of new hotels. We've identified 10 critical aspects of developing a new hotel, from the day we sign the contract to the day the hotel opens. We know that based on the success of the
Before Operations Measures, continued

contract through opening day, we can gauge the success rate of the hotel, and the number of years it will take us to recover from serious defects. We evaluate those 10 measures, the Product Quality Indicators (PQI), in our corporate office.

The first PQI, Sub-Standard Management Contract, measures the contract. We know that if there are articles and clauses in the contract that will restrict us from providing the right environment and product for our guest, this will affect our business results. Areas addressed include such things as a late feasibility study or a wrong concept. If we have to make detailed design changes or miss a construction start, that will have a negative impact on our profitability, especially if we must cancel advance reservations.

During Operations Measures

We rely on our Gold Standards to measure quality during operations because many of our customer requirements extend beyond the functional to the sensory, which is subjective and difficult to measure. It took us two Baldrige Applications and site visits for us to feel comfortable with this approach. We spend a lot of time and energy training our employees about the Gold Standards, and the foundations, and values of the organization through our process of selection, orientation, and recertification. We ask individual employees to step back and make a judgement as they deal with each individual customer as to how well we are performing. They are trained to stop the line, correct the problem, and move on. It is the interaction between the individual customer and the hotel employee that determines how well we perform.

After Operations Measures

There are several After Operations Measures employees track at the Ritz-Carlton. The Service Quality Indicators (SQI) are the 12 most serious defects that can occur during regular operation of the hotel (Figure 12 on the following page). Note that there are many factors included under each single evaluation. For example, there are a possible 3,000 defects, each worth one point, that are subsumed under the Inadequate Guestroom Housekeeping defect category.

The scale is weighted because on a per-incident basis, a missing bottle of conditioner in the guest room is of less importance to the guest than a missing jacket in the coat check. The weightings were determined through both quantitative and qualitative feedback from customers. J.D. Power surveyed customers as to whether there was a very strong, strong, or moderate degree of correlation between each defect and their overall satisfaction. The staff has given feedback as to the degree of concern shown by our guests regarding each type of problem. The total number of occurrences is multiplied by the weight, totaled, and then divided by the number of working days to obtain the average daily point value. The result is then communicated to the work force daily. This self-assessment allows our Ladies and Gentlemen to evaluate how well they are performing in advance of the J.D. Power survey, so that problem areas can be corrected.
We use three types of comparative data at the Ritz-Carlton: (1) comparison to industry and our foremost competitor, (2) benchmarking outside our industry, and (3) benchmarking within our own company. Benchmarking has been very useful over the years to propel us to higher levels of achievement. We use various sources of information such as other Baldrige winners, consulting companies, and benchmarking groups as sources of comparative data. Each one of our key or business processes has an owner; at the corporate level this is a functional vice-president, at the hotel level this is an individual manager. A process owner is assigned to each metric associated with the key production and support processes. Because the process owners are heavily involved with designing the architecture of the data, rarely do they see a fact or figure that they don't understand.

For example, we tap travel advisory groups and focus groups of meeting planners and individual travelers. We use the Mayflower Group to compare our performance not only within our industry, but also against the best major companies in America. Regional vice-presidents oversee groups of hotels and ensure that best practices and improvements are shared. When we open a hotel, we use experienced management staff from other hotels to train the new staff; this allows sharing of best practices. We also use the company Intranet to share best practices and benchmarking information.

We manage our business by fact, so the reliability of our data is crucial. We rely in part on our highly trained Ladies and Gentlemen, who are trained in statistics, to gather accurate data. On a daily basis, the Ladies and Gentlemen identify and implement improvements in performance measures. Whenever process owners or consulting specialists indicate a change of plans is needed, plans are rewritten, re-budgeted, and re-approved.
Process Management

Bob Warman—Our first Baldrige feedback report said that our process management wasn’t very strong, nor did we have a systematic approach to improving it. Today, we are a process-focused company with many standard procedures. We realized that our processes must be thoroughly planned so that we can give our Ladies and Gentlemen the means to meet our standards, create a market, and generate income.

Our key production processes are those we have identified to be the most critical to the customer in service delivery. They are—

General Manager
- Anticipation of Guest Needs
- Handling of Requests/Difficulties

Room Function
- Housekeeping Detail
- Club
- Warm Welcome

Meeting Event
- Primary Event Numerics
- Event Planning Responsibilities
- CSM Availability Responsibilities
- Function Space Management
- Pre-Event Conversation/Internal Review
- Event Improvement

Food and Beverage Function
- Room Service Timeliness
- Lounge
- Audio/Visual
- Restaurants
- Banquet Food/Beverage Timeliness
- Pool and Beach (Resorts Only)

At the corporate level, we define measurements and goals for each process area. Process owners at both the hotel and corporate level share information up and down. Once we determine the minimum standards, we ask each hotel to determine the resources they need to meet these standards. These SQI budgets are approved or modified, then sent back to the employees to spend the money necessary to make it happen. We work to improve the things the customer requires, and eliminate waste.

One of the responses we’ve received from our guests is their desire for us to know them and to remember them. We’ve created a process to make this happen. The CLASS database tracks the preferences of our guests and is accessible from every Ritz-Carlton Hotel so that we can anticipate guests’ needs. We’ve learned from our surveys that it is important to not only track what customers want, but what they don’t want as well.

For example, if we put fresh flowers in each hotel room and you as a guest have
an allergy to flowers, that would be just as bad as not meeting one of your anticipated needs. We try to gather as much information about our guests' personal preferences as possible, so that we can make their stays absolutely perfect. This is a system that is “fed upwards” from the employees, who are trained to be perceptive and to interact with guests on a more personal level to gather preferences. Each employee carries what we call a Preference Pad to jot down notes about our guests' preferences; the information is then entered into the CLASS database.

We are now developing a leisure reservation system to integrate ancillary services within the hotel, including transportation and spa services. This system is being developed in response to guest feedback and requests. Our process management approach was to form a cross-functional team to identify the work processes necessary to deliver those ancillary services in a more integrated way. We will then overlay technology if it is appropriate.

The most important customer requirement is guestroom housekeeping. A Ritz-Carlton guestroom is immaculate and fully functional because of a group of employees called CARE, which stands for Clean and Repair Everything. When this process improvement group started three years ago, defects ranged from 50 to 60 per million opportunities. This year we rated 18 defects per million opportunities— and we are on course to achieve a rate of well below four defects per million. CARE has analyzed data so thoroughly that they have calculated how often the light bulbs and the batteries in the remote controls should be replaced before they fail.

We have identified 13 key business processes at the corporate and hotel level; these are—

- New Hotel Development (Corporate Only)
- Sales and Marketing
- Rooms Function
- Engineering
- Purchasing
- Retail
- Human Resources
- Revenue Management
- Sales and Marketing
- Food and Beverage
- Loss Prevention
- Information Technology
- Accounting/Operations
- Quality

One of our biggest challenges is meeting the needs of the customer as we open new hotels. Our hotels are dramatically different, so corporate can only give basic understanding of what is critical to the customer. Each individual hotel must design their processes to meet the needs of the customer in the part of the world in which they are located. The design and support of processes is modified for each new hotel based on market research, facility design, and operating conditions. The processes are transferred to our Ladies and Gentlemen during the countdown process. We bring the senior management of the hotel together with the corporate office and go through the nine-step improvement process for each one of the key processes.
There are defects in our processes: we recognize them, we fix them, and we refine the processes so we can prevent future defects. The Greenbook is our handbook to process improvement; it features a nine-step quality improvement process to the design, control, and improvement of all processes. Standing cross-functional teams at all levels use measures and customer input to improve key processes. Improvements are institutionalized by the traditional hierarchy and the executive process owners. Each hotel has a quality improvement team made up of employees that are involved in the departments that affect the process. They have weekly meetings to go through the process improvement process in each one of the 25 sub areas.

We try to solicit and share good ideas from among our employees. Several years ago we had a formal system in place called the “Good Ideas System,” which was created after benchmarking other companies. We have found that a decentralized system is much better approach. Employees have over 260 opportunities to provide feedback and become involved in the planning of the work through daily line-ups, departmental meetings, project team meetings, and Town Hall sessions. We have tried to create an environment of open communication; then it is the responsibility of the leadership to help employees to test and implement those ideas. The quality office is always a resource for the development and advancement of good ideas within the operation.

Human Resources

Leonardo Inghilleri—The Baldrige Criteria Human Resource Focus is critical to a service organization such as ours. What we do and who we are as a company is determined by the point of contact between a guest and our employees. If that moment of contact is pleasant and memorable for customers, that customer will decide our company is a great one. If we have disgruntled employee “terrorists,” who alienate guests at every chance, then our customers’ experiences will not be positive. Therefore we need to concentrate a significant amount of resources and efforts to attracting, training, and keeping good employees.

We do not look at human resources as a freestanding line of business; it is an integrated business process woven into the fabric of the corporation. Our vision, to be the premier provider of luxury services and products, drives the process that will ultimately provide the results. Human resources is one of those processes; it is a critical factor for the success of the company.

We believe that unless employees have pride and joy in their work they cannot be a successful contributor to the enterprise. There are a number of corporations that regard their employees as “FTE’s” (Full Time Equivalence)—as eight hours of labor. We think that attitude is a mistake and, moreover, immoral. People don’t fulfill functions—they have a purpose. It is essential to engage the heart, the soul, and the brain of each one of our employees. The employee who comes to work because he
wants to and believes he is part of something great will do a better job than someone who comes to work because he must. Unlocking the discretionary efforts of each employee is a critical success factor for any corporation. The question is “How do you do that?”

We do that by creating a work environment that is supportive and engaging, so that our people are proud of being associated with the company. They are fulfilled and satisfied. People have asked us, “What are the deliverables of human resources?” The usual answer is, “Hiring the right people and training them.” But those are just operational processes. They happen to be regulated by human resource professionals, but they are really part of the business’s daily operational life. The deliverables of Human Resources are to create a skilled and empowered work force that operates with pride and joy. To do this, we need to create a work environment that is supportive, engaging, that allows people to take pride in their work, and that creates opportunities for growth.

We operate in an industry where many of our workers are in the lower income tier. We don’t necessarily employ people at the minimum wage, but these are hourly jobs that don’t pay tremendous amounts of money. A number of our employees come from socially limited environments, so our job is to create an environment in which they feel like ladies and gentlemen. We try to encourage a great sense of affiliation and belonging, so that they feel part of the corporation and can take pride and joy in their work.

We create the Ritz-Carlton work environment beginning with the selection process. Most employers today believe that there is a tight labor market. Not true. There are many, many millions of workers out there—they just happen to work somewhere else. Our job is to get those outstanding workers to work for us. Our best advertisers and recruiters are our own employees.

We have partnered with Talent Plus, located in Lincoln, Nebraska, to create a scientific selection process. We studied the needs of the customers to learn what they expect from each job category. For example, we learned that customers expect a doorman to be attentive, friendly, and welcoming, rather than someone who just saunters over to open the door. Customers expect housekeepers who are attentive and neat, so that the rooms are immaculate with everything in its place.

With this input from our customers we have defined the talents needed to perform each job. Then we interviewed our best performers with the assistance of occupational psychologists to determine the intensity of those talents present in the best performers. From this information we created the Talent Intensity Index profile—a profile of the ideal candidate. Then we created an interviewing process that allows us to determine the intensity of those talents present in each candidate, and we hire accordingly.

A tight labor market means that we must move quickly to hire new employees to maintain our service standards. We have reduced the time it takes to process...
The Ritz-Carlton selection process, continued

Hire the best performers

We do not allow managers or recruiting officers to hire individuals that do not meet the requirements of the job. We created this rule because when management allows mediocrity to penetrate the organization, all those who are willing and able to do the job will be frustrated. The best performers will eventually leave the organization because although mediocre people sometimes like to be associated with successful people, the reverse is not true. Every single time that you, as a manager, tolerate mediocrity and make a wrong hiring decision, you are in effect pushing your best performers out of your organization. You cannot accomplish anything exceptional if you tolerate mediocrity. In short, our motto is “We are Ladies and Gentlemen serving Ladies and Gentlemen”: if an employee cannot identify with this, they usually leave the company.

Compensation must be in alignment with vision

Companies cannot attract and retain exceptional employees if they do not pay them competitive wages. A functional company has alignment between its systems and processes with its vision. In other words, the company does what it says it will do. Our goal is to delight the customer so therefore we must have the processes in place that enable this, including our compensation strategy. We look not only at our own industry but every other company that pulls employees from the same pool.

For example, a few years ago at the front office of one of our hotels we were experiencing a turnover rate of 200%, even though we paid the highest wages in the hotel industry. This turnover rate was devastating because a stable front desk is essential to guest satisfaction and problem resolution, and we were forced to post a supervisor at the desk to ensure proper service. We found out that an airline was expanding their hub in the area, and they were using the Ritz-Carlton as a “training school” for their check-in agents. We matched the wages the airline was offering, and our turnover rate dropped dramatically. We were then able to move the supervisor off the desk, and lower our overall costs.

We have identified a number of jobs that can be filled by developmentally disabled, handicapped, or semi-handicapped individuals. We make every effort to work with institutions and centers to identify those candidates who are able to fulfill the requirements of the job. One disabled worker, a lobby attendant, has won the employee of the year award several times. We are very proud of that. Hiring the disabled is the moral thing to do, and that is very important in any business.

New employee orientation must be done at once

The next step in developing a successful work force is orientation. Imagine the following scenario: After a great deal of time and money is spent hiring her, it is Allison’s first day and she is very excited about her new job. The manager welcomes her, then introduces her to Joe, and says, “Why don’t you follow Joe, he’ll take you
New employee orientation must be done at once, continued

to the kitchen, and show you what you need to do." As the two of them walk to the kitchen, Joe (who had a little problem with the manager the night before) says to Allison, “You know, this company s...!” All too often this is the new employee orientation.

The new employee orientation pulls a newly hired employee into the cultural fabric of the company. It serves the purpose of changing the employee’s behavior to fulfill the company’s vision. Adults only change their behavior as a result of a significant emotional experience, such as a death, a wedding—or being hired. During that short interval, the barriers that have been built up over a lifetime are down, and that is when employers have the opportunity to mold the behavior of the employee. If you allow Allison to follow Joe to the kitchen, then that opportunity is lost forever. You will never be able to convince Allison that yours is a great company: that you care about customers, you are quality-oriented, ethical, and strive for success.

The executive committee of each hotel runs our orientation programs, so that the first person the new employee meets is the general manager. We have found that if we hold an orientation program three, four, or five days after the new hire's first day, it is already too late. Those first hours are critical; they need to be focused on the emotional and social side of the company, so that the new concepts will sink in. Later on, when the employee is more comfortable, it is time to do the paper work.

Day 21 class follow up

We designed our Day 21 class based on a study that was done of college students and their satisfaction rate. Researchers found it took three weeks for the organizational norms to affect those students. So the purpose of our Day 21 class is to provide us with a timely “weather report” of the success of our orientation and technical training certification. We then follow up with a satisfaction study that is done twice yearly.

Technical training a must

A strong foundation of technical skills is essential for the success of the company. An employee cannot make intelligent decisions for the company and the benefit of the customer if they don't know what they are doing. After the new employee orientation, we address the issue of technical skills in Training Certification. Each employee is coupled with a departmental trainer. This is another hourly employee who has the responsibility to ensure that the new hire has the technical knowledge necessary to do their job. For example, they will instruct the new hire on how to perform housekeeping tasks over the next 21 days, using a checklist. Eighty-five percent of our training and development is created internally. Last year we updated our training certification program; we selected the most talented employees in our hotels to write the training certification for us.

Our training programs are linked to our business strategy: they are not a “flavor of the month.” An example of this is a class called GLOW, which was created to address guest problem resolution. Our feedback from customers and guests...
We also use the “line-up,” for continuous teaching. Many companies spend a lot of time selecting and training people, then they abandon them to their own destiny. Large advertisers understand why this is a mistake. Companies such as Coca-Cola spend about 10 percent of their revenue— an enormous amount of money— on advertising because unless people are reminded, they tend to forget. Repeating the same message to consumers enables them to sell more beverages. We do the same thing from an organizational standpoint. At the beginning of every shift in every one of our hotels, we meet with our employees for 10 or 15 minutes. This just-in-time training creates a moment of alignment. We discuss why we are in business, the purpose and importance of customer focus and teamwork. This creates a moment to refresh their minds about telephone etiquette, how to carry a tray, or make a bed. It also creates a moment to celebrate accomplishment, recognize birthdays, or other special events.

Employees are subject to an examination/audit at the end of their initial training period to demonstrate mastery of their job. Annual Performance Appraisal information is evaluated to identify weaknesses in our training and development approach.

A business such as ours is very “transactional.” The check-in counter clerk...
Empowerment process, continued

The Ritz-Carlton Hotel Company performs dozens of check-ins per day, a housekeeper cleans 16 rooms a day. It would be a tragedy if we allowed them to think that their jobs were “check-ins” and room cleaning. Their job at the Ritz-Carlton is to make our guests’ stays memorable, and to fulfill our mission. Empowerment is very important in our business because anything in a hotel can go wrong too often will. When this happens, we expect our employees to stay focused on our mission and vision, and to create genuine care and comfort for our guests.

For example, an engineer is up on a ladder changing a light bulb, and he sees a guest returning from the beach loaded down with bags and pool toys. We expect that engineer to come down from the ladder, open the door for the customer, and welcome the customer, then go back to his job. We train our employees to break away from their routine, fulfill the customers’ needs, then return to their job—this is one of the key principles of empowerment. Figure 14 shows our empowerment process.

Many companies say their employees are empowered, yet when an employee spends money to fulfill a customer need, that employee is often subject to an interrogation the next day. That is not empowerment. We give our employees a $2,000 spending authority to rectify customer problems. Up to that limit, we don’t ask questions. We’ve found that they rarely spend the money, but they do satisfy our customers. Empowerment is one of the key deliverables of Human Resources.

Figure 14. The Basic Empowerment Process.

Employee involvement

We have found from our employee satisfaction surveys that in order to take pride and joy, employees want a work environment where they have the tools, resources, supplies, and time to get the job done properly. We would never change working conditions without first involving the worker. In traditional companies, the budget is normally decided by corporate, then it is scattered down through the organization. Any discussion on the budget is, of course, dictated by corporate, so it is all rather dysfunctional. We ask employees what they need in order to reach the desired scores in customer satisfaction, profitability, growth rate, etc. Then we negotiate. For example, if they ask for $1.5 million to deliver a 97% customer
Employee involvement, continued

Employee turnover

We have benchmarked the employee turnover rates within the hotel industry and the service industry in general. The hotel industry has a rate of 100%, the service industry twice that. Our turnover rate is 20%. When we started, our rate was in the 70–80% range, and we have worked meticulously to lower it (Figure 15). We created a number of initiatives to increase a sense of affiliation, and pride and joy. Top wage will attract workers, but it will not keep them. We’ve found that the genuine care and comfort for our guests must be mirrored in care and regard for our employees. Employee involvement in the decisions that affect their work has helped to dramatically lower our turnover rate. Top performers are placed on accelerated training programs, including leadership programs, and accelerated career paths.

Figure 15. Percentage of Employee Turnover.

Journey to Performance Excellence

The Ritz mystique was born in attention to quality

Patrick Mene—The mystique that surrounds the Ritz-Carlton trademark was born in fin de siècle Europe when the legendary Caesar Ritz created the two great hotels in London and Paris that bear his name. The Ritz Hotels electrified the world and defined the standards for luxury hotels. Their food and beverages were exquisite. And until then it was rare for a guestroom to have its own private bath. Caesar Ritz ensured the highest quality in service by continuing the craft concept. As in the small inns of earlier years, apprentices were hired, trained, and subject to inspection and audit by the master himself.

Other large hotels were also being built at this time, and the industry began to change dramatically. These great hotels needed some form of delegation, so the innkeeper position became one of general manager, and departments were created. The general manager became progressively removed from managing the daily activities that determine quality. In the early 20th century it became fashionable for
The Ritz mystique was born in attention to quality, continued

The Baldrige Criteria provides the structure to continue the mystique

Business results

The Ritz-Carlton Hotel Company: 1992 and 1999 Malcolm Baldrige Quality Award Winner

The Ritz-Carlton Hotel Company: 1992 and 1999 Malcolm Baldrige Quality Award Winner

When we purchased the Ritz-Carlton Hotel in Boston, Horst Schulze made the decision that the upper managers of the hotel would be extensively involved in the management of quality. He said, "[We are] responsible not just for cooking, cleaning rooms, delivering products and services, [we] are responsible for anticipating the wishes and needs of the guests." He then provided every conceivable tool for the work force to do that, including an automated memory system so that our 17,000 employees could remember the likes and dislikes of 800,000 guests. Many senior managers choose not to delegate certain areas, such as banking relations or pricing; Horst Schulze realized he could not delegate the management of quality as a start-up company and achieve business excellence. When we open a new hotel, Horst does not come in to examine the advance bookings or the contracts, he is there to personally train every employee on the Gold Standards.

In the late 1980s Horst Schulze said, "Even though we are considered to be at the top of our game, I think on a scale of one to ten, we are a six; we are just lucky that our competitors are a five." He felt the Malcolm Baldrige Award Criteria would provide us with the structure we needed to improve. When I read the Criteria for the first time, I thought it was irrelevant. Then John Timmerman said, "We know how to pack 500 cars into a garage designed for 250. We are always searching for the next amenity for the guest room and redoing the restaurant for the fifth time. Perhaps by using the Criteria we can learn how to be more scientific in our approach: learn how to design the garage better, how to choose the right amenity, and, maybe, we really don't need to redo the restaurant again—just get guests into the room that they expected."

On our quality journey we realized that although our business was a very refined one, we were like a job shop in that every one of our customers wants something new and different. By using the job-shop model we were able to understand how to create that "newness and difference." We also came to understand that within such a large and complex organization, quality was essentially the communication of the customer's requirement to all concerned, then designing the responsive action. Our goal is 100% employee pride and joy, zero customer difficulties, and 100% customer loyalty.

The Ritz-Carlton would not have achieved what it has today if not for the Malcolm Baldrige Criteria. We have achieved tremendous improvement in our...
financial results: in 1995 our Pre-Tax Return on Investment was 5.3%, in 2000 it is 17.6%, and we project that it will increase even more in 2002. Our Gross Profits are shown below in Figure 16.

Our organizational effectiveness has improved as well. Figure 17 shows total revenue per hours worked, an important measure of operational effectiveness in a service industry such as ours. And Figure 18 (on the following page) shows a repair and maintenance cost comparison.

Figure 16. Gross Profit vs. Main Competitor.
Source: PKF Consulting (Note: No 1999 data available for other than Ritz-Carlton.)

Figure 17. Total Revenue Per Hours Worked.
Source: Ritz-Carlton Hotel data.

Allison Frantz is corporate director of training for the Ritz-Carlton Hotel Company, L.L.C. In this position she directs the employee training and career development efforts of all 36 hotels and resorts worldwide.

Allison joined the Ritz-Carlton in 1988 as a front office agent. After completing a management training program, she was transferred to the Ritz-Carlton, Washington, D.C. as a sales manager and then moved to the position of training manager. Allison was
Leonardo Inghilleri joined the Ritz-Carlton Hotel Company in April of 1994 as vice president of human resources and member of its Corporate Steering Committee. In this capacity, he is responsible for all strategic aspects of human resources development and administration. Because of the fast-paced growth of Ritz-Carlton, Mr. Inghilleri’s priorities are currently centered on organizational development and the conceptualization of innovative business practices. These initiatives will ensure the core values, philosophy, and progressive approach that have positioned Ritz-Carlton as a leader in the service world are constantly strengthened and leveraged for greater shareholder value. Mr. Inghilleri comes to the Ritz-Carlton from the Walt Disney Company where he was director of human resources for Euro Disney Resort Hotels. As part of the opening team, he was also instrumental in introducing and establishing the Quality Process at Euro Disney. Before joining Euro Disney, he was responsible for Human Resources of the North American division of Alitalia Airlines; prior to that he held several positions in the travel industry in Italy, England, and the United States. Born in Rome, Italy, he holds a degree in Economics and Business Administration from the University of Rome.

Patrick Mene is vice president of quality at the Ritz-Carlton Hotel Company. He joined the company to lead its Total Quality Management efforts and was a part of both the 1992 and 1999 Malcolm Baldrige Award-winning teams. He was a contributor to the Juran Handbook, fifth edition. Before joining the Ritz-Carlton Hotel Company, he worked at the L’Hermitage Hotel, Hyatt Hotels, Westin, and Omni Hotels.

James Schultenover is vice president of sales and marketing, responsible for directing the sales, marketing, and public relations efforts of all 36 hotels, resorts, and sales offices.
He also oversees the strategic planning of hotels under construction and development worldwide. Before joining the Ritz-Carlton, he held various positions at Omni Hotels and Marriott Hotels.

Horst Schulze became president and chief operating officer of the Ritz-Carlton Hotel Company in 1988, after serving as vice president of operations and general manager. Previously, he was with the Hyatt Hotels Corporation where he was corporate vice president in charge of food and beverage operations. In 1991 he was named “Corporate Hotelier of the World” by Hotels Magazine. He received several quality awards including the 1995 ASQC Ishikawa Medal and the 1995 Educational Institute’s Arthur Landstreet Award. He was named one of Business Travel News’ 25 Most Influential Executives of 1999.

Bob Warman was named vice president of operations in February 1999, overseeing the hotel operations, including rooms, and food and beverage functions. He began his career as front office manager of the Buckhead property. Previously, as executive vice president of real estate for the company, he was responsible for overseeing worldwide expansion for the company.

Editorial assistance was provided by Carolyn Field.
Foresight 2020:
The Future of Quality in the Age of Technology

Author
Gregory H. Watson, President, American Society for Quality, Milwaukee, Wisconsin

An uncertain future
There is confusion today about the future of the quality movement. Business is changing its emphasis on quality, and ownership of quality practices is also changing. Business professionals, not just quality professionals, are now using the quality tools. Many people also believe that there is a difference between Six Sigma and the quality principles. As leaders of the American Society for Quality (ASQ), we’ve had to ask ourselves: “What is the status of ASQ and the quality movement?”

The first future study: 1995
Back in 1995, ASQ conducted its first study in which we looked forward to the year 2010 and our place in it. But a funny thing happened in the meantime: the future arrived much faster than we expected. We had grossly underestimated the rapid advancements in technology, such as the Internet, and how much these changes would alter the business landscape. The technical forecasts we made were achieved almost five years ahead of our expectations. We also overestimated Japan’s economic influence and underestimated China’s. But the study did help us prepare for the years to come, and led us to initiate important strategic changes for the organization, including a $2-million systems upgrade, a name change, a new organization structure, and a new research strategy. Those changes have served us well, but they are not enough. We realized that we have to look again at the forces that will shape our future, so that we can continue to play a vital role in it.

The Foresight 2020 study identifies critical assumptions
In August 1999 we convened a future study team, many of whom were also members of our strategic planning committee, to conduct Foresight 2020, a look ahead to that year. This study increased our understanding of our entire business environment, our customers, and ourselves. More importantly, the results of this study yielded insight into the critical assumptions we have about the quality movement and our society.

This study identified some key demographic, economic, cultural, and technical trends that will continue. We also identified eight forces that will shape our future, and from these trends and forces we created four possible scenarios. Our aim is then to develop recommendations for action plans for ourselves, our constituents, and our customers based on these scenarios. ASQ has reached an inflection point: the future growth of our organization can move in any number of directions (Figure 1 on the following page). In the ‘80s and early ‘90s interest in quality bloomed—and mem-
The Foresight 2020 study identifies critical assumptions, continued

Figure 1. The American Society for Quality (ASQ) Growth Inflection Point

(1) Demographic forecasts. There are two peaks in population caused by increases in immigration and birthrates: the so-called Baby Boom Generation and Generation-X. During the baby boom, birthrates increased in the 1940s, peaked in the late ’50s, and then bottomed out in the ’70s. The second increase, Generation-X, began in the late ’70s, peaked in the early ’90s, and is now tailing off. These two cycles indicate there is a 40-year pattern of growth—that fact allows us to anticipate the beginning of another new cycle in the year 2010.

We all have spending, saving, and investing habits that are a function of our age. Therefore around 2010, we can anticipate a slowing of spending as many of the Baby Boomers start to conserve their incomes and increase their savings in preparation for retirement. That money then becomes the investment capital needed to create innovation in our children’s generation, the fruits of which will come to market sometime later when our children have established themselves in their careers, and we have retired.

We identified this cycle time for innovation as one of our critical assumptions: the time to market for new inventions will remain constant and cyclical.

(2) Technological forecasts. There are several technical areas that we believe will come into fruition by the year 2020. One is nanotechnology: the manipulation and manufacture of materials and devices at the molecular scale. Computer-aided customization will become routine, as we see in the Lexus automobile with its...
programmable seat control. Fuel cell technology will come into its own: automobiles (consider the technology linkage that has been established between Ballard Technologies, Ford, and DaimlerChrysler) and homes (look at the work of Plug Technologies) will be able to use alternative fuel sources. High definition TV will become commonplace, and be incorporated into our cellular phones, smart maps (these will interactively define the direction required based on feedback loops from geographic satellites that track your real-time movement), and handheld computers. People will carry an electronic wallet, a smart card really, that will replace the keys to your house, your driver’s license, credit cards, medical records. A company in France called GemPlus has already begun marketing products. Many of these technologies have been around for some time, but we will now see integration of computing power and information access into new products and services.

We make a couple of critical assumptions regarding technology: first, is the continuity of technological growth: Moore’s Law* will continue to hold true (or even accelerate). A second related critical assumption is: the health of the economy and distribution of money will continue to be significant in determining the speed of commercialization for new technology. In developed retail markets, the more people with discretionary funds to spend on new technology products (these are the early adopters), the faster a product, such as HDTV, can move to mass market, because their critical mass provides a rapid payback for the inventor’s investment, allowing a more rapid price reduction. Another critical assumption is that the existing investment in production capacity for a mass market creates its own inertia, slowing down the investment and development of new technology. This explains part of the phenomenal growth of the Internet: it didn’t have to displace another technology.

Critical to the shift in the technological force is that once we thought that it was only important to own the patents. Now the speed of technical diffusion, the time it takes for technology to be commercialized, is accelerating, as we become more sophisticated in turning intellectual knowledge into commercial applications. This means that the time to obsolete patents is becoming more rapid and their enduring value is less important, but their significance as “business trading cards” is becoming a more significant aspect of future business alliances and technological partnerships.

(3) Social forecasts. We made a number of social forecasts:

• **Electronic immigrants and telecommuters.** Electronic immigrants from other cultures and economic conditions will continue to displace workers in more favored economies. Many companies now hire computer programmers in India or Eastern Europe who then telecommute. The labor costs of these telecommuters are about 10% of a programmer in the U.S. or Western Europe. The flip side of this coin

---

*In 1965 Gordon M oore, co-founder of Intel Corporation, observed that the number of transistors on (and the power of) integrated circuits doubles roughly every 18 to 24 months, while the price remains relatively constant. This observation has become known as M oore’s Law.
PERSPECTIVE

Inputs for our scenario planning, continued

is that telecommuting will have a positive impact on family life, as more people have more time available to spend building their personal relationships.

- **Virtual reality.** The virtual reality created by the Internet and computer games will have a growing negative impact as a new form of addiction. People will become addicted to this artificial world that they can control, becoming more physically and emotionally disconnected from their families and communities.

- **Information warfare.** Computer viruses, worms, and other forms of technical sabotage will become an increasing threat to computer and web-based organizations.

- **Lingua franca.** English, already the dominant language of business, aviation, and science, will become the dominant language of the web. Toshiba of Japan, declared in January of 2000 that English will be their corporate language.

- **Knowledge entrepreneurs.** We'll see the development of the “gold collar” worker; this is someone who sells his or her knowledge to the highest bidder to improve business performance. Author John Naisbitt, in his book *Megatrends*, said that information was becoming the most precious resource companies own.

- **Intelligent tutoring systems.** Schools will be transformed from classrooms into intelligent tutoring systems by the application of interactive media. This technology will adjust instruction to the needs and interests of each individual student to make learning more effective and fun. This innovation may reverse the current trend towards more teamwork and heterogeneous grouping in public schools.

- **Digital revolution.** The digital revolution will focus society on its value system: how it works together effectively and behaviors that facilitate efficient work both within and across organizational structures. Attention will be focused on trends that decentralize, globalize, harmonize, and empower work.

- **Values.** A return to “family values” will also occur, as the home becomes a center for both work and family.

---

**What do we really know about the future?**

We identified eight driving forces that will shape our future:

(1) **Partnering.** Superior products and services will be delivered through partnerships, ranging from strategic alliances to mergers and acquisitions. Companies will become more adept at choosing the right partner to accelerate the application of knowledge—the fundamental reason for partnership.

(2) **Learning systems.** The use of advanced technologies will speed knowledge transfer in education.

(3) **Adaptability and flexibility.** The velocity of change is increasing in society; so adaptability, flexibility, and the ability to manage change are becoming increasingly important. We will have to discover simpler solutions to deal with the increasing complexities of an ever-changing environment.

(4) **Environmental stability.** We will start to act on a truly global basis to stabilize and preserve the natural environment, as we realize that the actions of local groups are insufficient to preserve the ecosystem as a whole.
(5) **Globalization.** The shrinking globe will continue to shape our economic, political, and social environment. There will be continuing growth of trade unions, such as NAFTA and the European Union, as nations realize that they will have to band together to have the economic strength needed to compete. The electronic transfer of money across international borders obviates the local governments’ role in taxation. A more global perspective is going to be required to prevent sub-optimization. Whether real or virtual, the battles of the future will be fought not over land borders, but over electronic ones.

(6) **Knowledge focus.** Knowledge will become the prime competitive and wealth creation factor. The Internet explosion has underscored the significance of an organization’s knowledge and the value of intellectual assets as a commercial property. Peter Drucker and other management guru’s have heralded the next business age as the “age of knowledge.” Knowledge begets knowledge as each organization finds ways to grow its knowledge base and capitalize on its internal intellectual assets. As manufacturing grows less important and is pushed off-shore to “developing nations,” the developed world finds more of its business emphasis placed upon service industries and knowledge creation industries (research and development). A critical assumption related to knowledge is that the manufacturing base of a country is the best indicator of its development. The future emphasis will shift toward service, and manufacturing will no longer be a valid indicator of wealth generation capability.

(7) **Customization and differentiation.** These will continue to grow in importance, as Tom Peters said, “We’ll...be building in lot sizes of one for all customers.” This level of product differentiation is going to become even more important to growing sales, so we’ll have to find ways to deal with this potential dilemma by learning to both customize products and mass produce them at the same time so that we can operate most efficiently. Product specialization will be delivered in what we call the “soft side” of the product, rather than the “hard side.” An example of this is what is called a software radio: all of the features are located in a microchip that can be programmed to perform any radio telecommunications function.

(8) **Shifting demographics.** The social values and ethnic makeup of our society will continue to change. This driving force will create a leveling effect across national boundaries as nations compete via e-commerce across national boundaries. The shift in values and ideals will span across generations and around the world (age groups are not normally distributed by country). Many times the transition between two generations results in a social rift that separates parent from child and leads to alienation of one or both parties. (I hope that this change will occur more smoothly than it did from my father’s generation to mine.)

When we began to construct our scenarios, we realized that no amount of “futuring” would allow us to see the road ahead clearly. What matters though is that they are a helpful way to consider what could happen. We wanted to look at the second and third order implications of coming changes, so that we could build...
The “base case” scenario

The Fruits of Knowledge (Scenario One)

This is a “base case”: the linear extrapolation from the status quo to the year 2020. The fundamental elements of quality management, (such as basic problem solving and the methods of total quality management) have been instrumental in realizing the benefits promised by the new knowledge society. Yet there are companies, countries, regions that have still “not got religion.” The economic boom of the ‘90s never led to a crash as many feared; instead information technology and the rise of the new knowledge economy “rewrote economic textbooks.” The quality principles were applied to these new realities to devise new theories by a new group of economics. The heightened awareness of the quality principles spurred many companies to deep-seated reforms and more sustainable economic health. Global organizations, such as the International Monetary Fund, took the cue and began requiring the adoption of the quality principles as a condition of economic assistance.

Technology remains the driver of change. In 2013 e-commerce eclipsed all other forms of commerce combined. The quality movement contributed to the runaway growth of e-commerce by helping to devise international protocols and standards that are used to facilitate, regulate, and safeguard commercial transactions.

Convergence of information technologies and the propagation, integration and cross-referencing of knowledge bases have lifted many vocational specialties to new heights of achievement. The human genome project, for example, has been combined with longitudinal data (cross-society trend analysis) and holistic approaches...
The “base case” scenario, continued

(Using both traditional and nontraditional medicine) to yield customized, prevention-oriented health care.

Information technology has finally fulfilled its social promise. Machine knowledge now exceeds human knowledge: more appliances than people are now on-line, and some expert systems outperform human logic.

Technology has intensified human strife, bringing many new voices to the table, and introduced many new thorny ethical questions, such as gene splitting. While these dialogs began during the early 1990s, they were engaged on the fringe of society. At this time however, these issues have moved into the mainstream and have become issues that divide political parties and create ethical and moral problems in large segments of society. More and more people have become loners, relating to the larger world only electronically as technology becomes a source of solace and alternate reality.

Globalization has sidelined many organizations; the remaining leading organizations are learning organizations. Knowledge management is considered an essential subset of quality, systematizing the capture and just-in-time transformation of knowledge into bottom-line value.

Mergers and alliances have completely transformed the business landscape. Today’s companies are so modular that they are more aptly termed “value chains.” Each consists of a major brand-holder supported by thousands of niche partners and micro-enterprises. This organizational structure was created to maximize the intellectual property and contribution of the members of the “value partnership.”

Quality practices have enabled the production of “customized experiences” for history’s most demanding customer base. Aging Baby Boomers, the day’s largest and wealthiest demographic group, expect sellers to provide “systematic delight” geared towards their personal values, tastes, and goals. Much production is now done in lots of one; other products are released in beta and customized for their specific buyer.

Companies are now expected to be exemplary citizens of their communities; the quality principles have been used to develop social responsibility measures. Workers fall into two categories: those who are free to work where they like, and those that are tied to a location. In either case loyalty between the two is nearly nil. Quality professionals are fewer in number but higher in status. The Global Society for Performance Excellence (formerly ASQ) is at the crest of this wave, helping professionals and nonprofessionals carry quality’s message throughout society.

The quality movement dwindles with unhappy results

Back to the Past (Scenario Two)

The world of 2020 is one where economic and environmental disruptions, ineffective leadership, and social fragmentation have created a vicious circle. The quality movement has diminished, due partly to institutional cost cutting, disenchantment with its outcomes, and the profession’s own failure to grasp the seriousness of the situation. The profession has dwindled to near extinction; ASQ has closed its doors.
This sorry outcome began back in the stock market crash of 2003, when the high tech bubble finally burst, sapped by persistent recessions in Japan, Indonesia, and Brazil. Many middle class investors found themselves bankrupt—and unemployed. The inequities between small numbers of wealthy and increasingly large and desperate masses triggered breakdowns in cooperation and communication across all social dimensions.

The Internet, defenseless against organized terror, has become a playground for hackers and hate groups, and a vibrant black market in personal and security data. Most individuals, and increasingly most utilities, have moved “off ‘Net.” A coalition of governments has declared war against the information pirates, and people have rallied to “take back the ‘Net.”

Technology research and development has spun out of control, with labs and companies ignoring ethical and quality standards in their pursuit of quick profit. Although quality professionals could not have averted all these trends, they could have injected a critical note of sanity. The quality movement could have framed the debate on crime’s root causes and their elimination. More broadly, they could have applied the quality principles to the new knowledge economy and financial institutions.

Ecological disasters have piled up like other disasters. Thousands of companies began ignoring EPA regulations since funding cuts forced the agency to curtail regulation.

The lid blew off a brewing backlash against globalization. Alliances among nations, customers, and suppliers have begun to break down. In global companies, knowledge management has been replaced by knowledge hoarding, organizational pyramids, and functional silos.

Forced to cut corners, most organizations have frozen quality efforts wherever they could. Most governments have become increasingly bureaucratic and hard to do business with. Not surprisingly, quality in every sector has slid drastically. Although centers of excellence remain, they are islands in a sea of mediocrity.

Marshalling the quality movement

The Sustainability Show (Scenario Three)

This scenario shows a paradigm shift in progress: sustainability is the central organizing principle for society. Quality is recognized as the best tool kit for achieving sustainability, and its principles, tools, and techniques are ubiquitous. However, much of this progress has been achieved at the price of stronger, larger government. There is a foreboding rise in paternalism and authoritarianism.

Two decades of worldwide turbulence have pushed global society to a search for sustainability. At the turn of the century, all the bad habits of the Industrial Age seemed to bear rotten fruit at once. Years of rolling environmental crises, economic meltdowns, social violence, and economic terrorism finally led citizens to turn en masse to government.

The United Nations has effectively become our world government; national
governments are stronger too. Public order is tighter, crime has declined, and social networks have strengthened.

Accompanying this has been a worrying decline in civil liberties and freedom of information. The wild west days of the Internet are over—taxes, access charges, and cyberporn censorship have won the day.

Baby Boomers have begun to exit the world stage; Generation-Xers are bringing a shrewd realism and a preoccupation with civic order to the public realm. Generation-Yers, now in their 20s and 30s, are vigorous advocates of teamwork, rationalism, and institution building. So far the effects are largely positive.

Many governments have applied quality internally, becoming more globally oriented, agile, customer focused, and technology capable. An entire body of knowledge is emerging around the application of the quality principles to governance in a knowledge-based society. In the U.S. and European Union, public companies include quality in their shareholder reports, and the U.S. appointed its first secretary of quality.

Quality's mandate has been extended to include quality of life in the broad context of community and the environment. In organizations, Six Sigma has become standard practice in all sectors.

The technical tide has turned away from R&D for profit's sake, towards "appropriate" technologies that support social and environmental wellness. Capitalism now aims for "good growth." Free markets are guided by win-win principles, enforced by rules and regulations. A universal currency devised by quality professionals, issued and administered by the new global treasury, has eliminated currency trading while still allowing local markets to set value. The electronic wallet, cryptocurrency and Internet-based access accelerated this ability to shift to the universal currency.

Global society is mobile; employment is managed globally through the Internet, which some view as dangerously "big-brotherish." Corporations and governments share an uneasy alliance. Government regulation is significant, but it is addressed to the ends rather than the means. Companies that fully reshape themselves for sustainability become inherently agile and knowledge-enabled.

The Garden of Quality (Scenario Four)

In this scenario we have progressed from allowing technology and business to drive society, to subordinating technology to human and biospheric well-being. Quality has been the key to this transformation. The quality movement has shifted from inspection, to control of work processes, to a new focus on measurement and Six Sigma. The emphasis has moved up the value-added chain from operations (doing things the right way), to strategy and vision (doing the right things the right way). Quality has been embraced throughout our lives, radically reshaping society at every level by the use and application of the analytical tools and humanistic quality methods to integrate all of society's elements into a cohesive effort to better all
The quality movement fulfills its promise, continued

The techniques of quality improvement have been applied solving the ecological legacies of the 20th century. Technology has been integrated into virtually every aspect of life, connecting generations and cultures. Values and vision statements guide the processes and identities of most organizations. Once organizations felt, “We are interdependent and should cooperate.” Now they feel, “We are one and should co-create.” Large organizations use quality measurements and reporting systems (later generations of SA 9000, Natural Step, and ISO 14000) to manage change. Knowledge of quality improvement tools is expected of all knowledge workers, and everyone is considered a knowledge worker.

Most individuals enjoy strong self-esteem and respect, and self-actualization is seen as one of society’s chief purposes. Society is more pluralistic than ever as it fragments peacefully along affiance lines. Government institutions are minimal and nimble, and are focused on common services. Governments have learned to watch their step, as today’s citizens aren’t tolerant of inefficiency, dogmatism, or high-handedness.

Of the four scenarios I’ve just described, the “Fruits of Knowledge,” an extrapolation of today’s status quo, was voted the most likely; while the “Garden of Quality” scenario was voted the most desirable. Common to all four scenarios was the recognized need for basic and advanced quality and statistical methods. What was uncommon was the degree of use and acceptance of the tools.

We looked at the implications of this study for quality professionals and for other users of quality improvement techniques. The pursuit of quality is changing, and must change. It has to become more innovative, flexible, and faster, while the requirement for quality professionals is diminishing. For example, out of 20,000 Six Sigma Black Belts trained since 1995, most are not quality professionals— they are people from line organizations. There is a projected 45,000 Black Belts to be trained over the next two years— again most will not be quality professionals. This represents a massive transfer of knowledge from inside the quality community to the world at large. The implication for quality professionals is that to stay viable we must become coaches for these new practitioners. Quality professionals will become a kind of process technologist who train others in the latest technology or cutting edge quality tools. This means we will have to become better educated, more collaborative coaches, able to work in situations where we don’t have authority.

Quality professionals will need to expand their levels of competency: we need to be able to explain the basic lessons of statistics to executives and the details of the design of experiments to an engineer. We must master the fundamentals and learn how to apply them in diverse applications. We must not only know what a flowchart is, but also how to relate a block diagram into a probability map, and how to teach an organization to do statistical modeling based on flowcharting principles. This requires more “bandwidth”— and lifelong learning.
Implications for society

The implications of this study for society are that as the population continues to grow, the strain of providing the increasing amounts of basic water, transportation, energy, and communication services will increase. We hope that the tools and methods of process management and quality improvement will be applied to solve these problems. All types of organizations will come to value continuing growth, and they will provide opportunities for continuing learning and challenges for all people.

Society will also have to learn to think systematically and act globally. Currently, I live in the Tampa Bay area where none of the three local communities of Clearwater, Tampa, and St. Petersburg plan or talk together. That is not a model for success in any area. Quality methods can play a role in helping organizations improve communication and manage by fact, enabling them to create better solutions.

Implications for organizations

There are several implications for organizations. Today we see that leading firms adopt the quality tools more readily than many other firms. Indeed, with Six Sigma, we can see documented proof that better bottom-line performance is delivered and documented through objective means. We see that the shared knowledge of quality is going to be the culture and operating language of companies, producing better business results and healthier communities.

Organizations are starting to think systematically, although different functional groups may refer to it by different names. In human resources it is called organizational development; in the information technology group, systems analysis; and in finance, internal auditing. But all of them use the same principles and tool sets. Over the last three years we've seen business processes—the support services in organizations—being subsumed under one individual called the Chief Administrative Officer.

We will see all business managers taking personal responsibility and being held accountable for quality, not just holding quality organizations as responsible. DuPont Corporation embraced Six Sigma 16 months ago; at that point they had four core values in their organization—none of which focused on measurement or accountability. Now personal accountability has been emphasized so that “the way people work together” is not just hiding decisions behind the veneer of a team, but each individual taking the personal responsibility for their actions and contributions to decisions.

A “unified theory” of the quality field

We know that we need to become customer sensitive and market-driven, responsive, agile, flexible, and adaptable, carrying with us a sense of urgency. In the past we declared that the quality community was our customer, but we didn't know what to do with that customer. Now we know we need to research them, ask them questions, figure out how to partner with them. We need to diversify our membership and our approach to quality. We need to be more relevant, significant, and accountable to our members. We need to stay at the leading edge of our profession.
A “unified theory” of the quality field, continued

Above all we have to realize that we have to be altruistic, public minded, and ethical in everything we do. If we succeed, we might achieve what eluded Dr. Einstein—a “unified field” theory. This unified field will have no more warring factions or leading gurus. We need to become a caring community, not a dysfunctional profession.

There is only one obstacle to our success, and Pogo said it best, “I met the enemy and they is us.” The reason for this is that too often people tend to hold onto their pasts more dearly than they should. We tend to build a collaborative fence around our profession’s status quo. The only way to change that is to become more inclusive and to become better listeners—that change will mold the future of ASQ and the quality movement.

Author information

Gregory H. Watson is president of the American Society for Quality (ASQ) for 2000-2001 (ASQ headquarters is located in Milwaukee, Wisconsin). He is also the managing partner and president of Business Systems Solutions, Inc., an Academician with the International Academy of Quality, and a Six Sigma certified Master Black Belt. Previously he served as vice president for quality at Xerox Corporation, corporate director of quality at Compaq, and manager of the Quality Leadership Development Program at Hewlett-Packard. Mr. Watson has served as a judge for the Texas and New York State Quality Award Programs, the Florida Sterling Award, and the Air Force Quality Award. He has been a member of the board of examiners for the Malcolm Baldrige National Quality Award, and a corporate representative to the GOAL/QPC Research Committee.

Editorial assistance was provided by Carolyn Field.
Improving Process Efficiency to Increase Customer Satisfaction

Authors
Tracy Peacock, Associate Vice President, Change Management, and Deanise Hemmer, Senior Specialist, Strategic Business Planning, Merrill Lynch Credit Corporation, Jacksonville, Florida

Total balance sheet management
Merrill Lynch Credit Corporation (MLCC) is a wholly owned subsidiary of one of the largest financial institutions in the world, Merrill Lynch and Co. Our purpose is to provide Merrill Lynch clients with the same innovation in credit management that the cash management account provides for their assets.

We began by pioneering the home equity line of credit, as the first step in meeting some of the liability needs of our clients. We realized that managing what you owe is just as important, if not more so at times, as managing what you own. Over time, we’ve created a myriad of credit solutions to address what we anticipated as our future client needs. Ultimately, this strategy has become known as total balance sheet management, and was adopted and embraced by our parent company.

Managing rapid growth
In 1981, MLCC opened its doors with only eight employees; today, MLCC employs over 900 individuals. Through product expansion, development, and further penetration of the Merrill Lynch client base, our loan originations have also increased significantly over time. In 1999, we originated $6.5 billion in first mortgages and credit lines, and we expect to have similar, if not better results in the year 2000. As our mortgage volume has increased, so has our servicing portfolio. We currently service over $8.5 billion in first mortgages and home equity lines of credit on-site and we have formed a strategic alliance to service $14 billion.

By embracing quality, focusing on solid business planning, using a systematic process-management approach for continuous business improvement, and getting employee involvement, we’ve been able to effectively manage this rapid growth.

Strategy starts with vision
At MLCC, our business strategy starts with our vision: to be the preeminent provider of planning-based liability management solutions. Our vision supports our parent company’s value proposition, namely to build client net worth by planning for and managing both sides of the balance sheet.

The cultural transformation begins
In 1993, we began to direct our energies toward a cultural transformation to redefine the way that we do business. Our business transitioned from a transaction-oriented type of business to a more client-focused approach. We took a very complicated assembly-line process and established a single point of contact that was totally
commitment to meeting client needs. The process changed from a functional process to a relationship-driven process, which was unheard of in our industry at the time. We recognized the need for change, not as a crisis of survival, but as an opportunity to manage growth and improvement.

As part of the cultural transformation, we also aligned our terminology to the new client-focused philosophy (see Figure 1). Those changes were much more significant than just a change in terminology; they were about defining our culture and value as an organization. Once we had redefined our cultural philosophy, we then truly aligned the organization with the values and principles (see Figure 2) that guide our actions and behaviors, and fuel our passion for excellence.

The cultural transformation begins, continued

Redefining our philosophy and aligning the organization
A covenant with our partners

At MLCC, our partners are our most valued asset. They make us who we are today, they build on who we were yesterday, and they shape who we will be tomorrow. Our values and principles reinforce the fact that we all work as a team for a common goal. To bind this partnership, we’ve established a covenant with our partners (see Figure 3). The covenant was devised and created to encompass everyone, from a front-line partner all the way up to the boardroom.

Figure 3. What It Means to Be an MLCC Partner.

- You have a stake in your company’s success.
- You have accountability for your role.
- You are committed to the mission, goals, and objectives of the company.
- You share in and constantly practice the company’s values.
- You believe the company’s success is your success.
- Doing the job right is more important than getting the job done.
- Your performance will be measured. You will be accountable. You will be recognized.

It’s not the strongest that survives; it’s the one most adaptable to change

We understand that to be a championship team we have to be willing to work together, be open to new ideas, and be adaptable to change. Charles Darwin once said that it’s not the strongest of the species that survives, nor the most intelligent; it’s the one that’s most adaptable to change. And although natural evolution may change slowly, business changes quite rapidly.

Using the Sterling Award criteria for self-assessment

In 1994, we embraced the criteria of the Florida Governor’s Sterling Award to help us manage change better. We used the Sterling Award criteria to conduct a self-assessment and to validate the changes that we had made or were considering for the future. Over the next three years, we would use the Sterling Award criteria as a management tool to better manage our growth and change.

Developing the business planning process

In 1995, we applied for the Sterling Award, and although we did not win the award, we did receive some very valuable feedback on our key strengths and key opportunities for improvement. Because of the Sterling feedback, we created and implemented our business planning process. The business planning process allowed...
Developing the business planning process, continued

Developing the business planning process, continued

MLCC to take the corporate directives from our parent company and set internal strategic objectives to accomplish those directives. It also provided the foundation to align key activities in every operational area as drivers of the strategic objectives.

Identifying proactive opportunities for change

Identifying proactive opportunities for change

The business planning process starts with a strategic evaluation of our strengths, weaknesses, opportunities, and environmental threats (SWOT) as an organization. Based on the corporate strategy, we next define areas that we feel are key to focus on. This information becomes the foundation of our business planning process. Based on this foundation, “critical few objectives” are defined, with drivers for the organization overall to support the corporate strategy. Once the business plan for the company is determined, functional group managers determine how their individual area can influence the key objectives and drivers of the organization. Each department will come up with: (1) key activities or drivers to support the objectives set for the firm, (2) metrics to evaluate how they are currently doing in achieving those objectives, and (3) stretch targets, not only for the current year but for the following year as well. The budget process is simultaneously going on to ensure business plans and budget are in alignment.

Client feedback helps improve the process

Client feedback helps improve the process

Each time we close a mortgage, we ask our clients for feedback. At the mortgage closing, clients receive a survey that asks them to evaluate MLCC based on our overall process, and provide feedback. The feedback provides an opportunity for recommendations on how to improve our process by asking clients what their specific needs are. We also ask if they would refer a friend or relative, which is a good indicator of customer retention and loyalty.

The financial consultant as a client

The financial consultant as a client

In our business, the external client isn’t our only client. Being that we are a wholly owned subsidiary that was developed to meet the needs of the Merrill Lynch client base, one of our key clients is the financial consultant (FC). The financial consultant is an internal partner who represents the Merrill Lynch–client relationship. In the past, the consultant has been known as a “stock broker” or “financial counselor.” But to align with the Merrill Lynch strategy, the financial consultant has become an advisor for all client financial needs, including assets, estate planning, mortgages, and insurance. So whenever we close a mortgage for an external client, the financial consultant as an internal client is also surveyed to capture their feedback relative to our process. We use the feedback from the customer surveys and financial consultant surveys to evaluate our client-focus and determine areas for potential improvements.

Evaluating progress in a monthly meeting

Evaluating progress in a monthly meeting

Once the business planning process has been completed and the final budget has been aligned to it, the objectives become part of a monthly managers’ meeting. This meeting provides an opportunity to evaluate, on a monthly basis, how the company and individual partners are doing toward achieving the targets that have
Improving Process Efficiency to Increase Customer Satisfaction

been set forth in the planning process. Anything that is not on target becomes a gap. If those items remain gaps over a consistent time period without resolution, then they become an improvement initiative to be managed by the change management team.

While devising this business planning process was a major breakthrough for MLCC, the biggest impact on the firm was that it let every partner from the executive level to the front line understand exactly how they impacted the overall process and what their key contribution was to the future success of the firm. This process allows all of our partners to be involved in setting our future direction. It literally takes planning from the boardroom to the boulevard.

At any given time, partners are able to submit suggestions for improvement to the business planning process. The business planning process not only links the business unit to the corporate office, but each individual partner's performance objectives are tied to how they contribute to meeting the key objectives for the firm. This motivates partners to suggest ideas on where improvements can be made because it makes their day-to-day job more efficient. In addition, knowing and understanding organizational objectives makes meeting the individual's own performance objectives more attainable.

Once we began implementing the strategic business planning process, we discovered that the plans helped us identify the need for clearly defined processes, as well as the need for a systematic approach to business improvement. We therefore developed our 7-Step Process Management Model (see Figure 4). The model helps us to systematically identify and document business processes, and implement needed improvement initiatives identified as part of a monthly gap analysis.

The 7-Step Process Management Model begins with mapping and measuring clearly defined business processes. The key and often most challenging part of the model is choosing metrics that accurately reflect what is important to the organization and that are relevant to early detection of potential shortfalls so that these items can be addressed during the process as leading indicators rather than after-the-fact as lagging indicators.
The seven steps

The 7-Step Process Management Model begins with identifying key processes and prioritizing them according to the stakeholder impact and the need for improvement. One way processes needing improvement are identified is through the evaluation of the strategic planning process. Critical few objectives not met in the current year roll over to the following year as strategic improvement objectives and metrics.

The second step is to construct a process flowchart for the key processes within the organization so that we can see very clearly where one process ends and the next process begins. It also helps us to better identify our internal customers and suppliers, and really leads to breakthrough improvements, because on paper we are able to clearly see any inefficiencies and loops indicating rework in the process.

Step three is to identify indicators. Once the process flowcharts have been constructed, it becomes necessary to identify the most appropriate indicators and set stretch targets to monitor the progress of each.

The fourth step, implementing the quality control system, is a combination of the process mappings and designated in-process and end-of-process indicators with specific targets.

Monitoring the quality of the control system is step five. Once we've implemented the quality control system, we monitor each indicator's performance. We do so on a monthly basis as part of the monthly managers' meeting to see which indicators are performing at or above target. Those that are out of target are drilled down for the root causes and addressed going forward.

Step six is to improve processes. Generally, improvements are made during the initial implementation of processes and/or are identified as part of the monthly indicator performance evaluation (or gap analysis), but improvement initiatives can take place any time throughout the year.

The final step is to standardize processes. Once processes have been formalized and documented, they are communicated throughout the organization via an Intranet and e-mail. We also hold quarterly partnership meetings with everyone in the organization to communicate/reiterate any recent changes that have taken place.

Any time a major process improvement is required, its impact on other functional areas must be evaluated. If the process change meets specific criteria guidelines, then it must go through a formalized change management process. All process owners have an opportunity during this process to identify any concerns they have and obtain resolution prior to rollout.

A committee of senior vice presidents evaluates all business cases that have been submitted for review and approval as part of the formalized change management process. Each case is evaluated based on the impact to the customer, the financial bottom line, and internal partners. The senior VP committee ultimately decides if the case warrants further consideration, resources, and research, based on the predicted benefit to the firm.
The benefits of process management

Process management provides us with a road map to get where we want to go (Figure 5). Anyone can use it to understand the landscape before them. Whether new partners are trying to understand their jobs or one department is trying to understand how to work better with another department, process management can provide the tools necessary for better navigation.

Process management can also lead to improvements such as streamlining of processes to better serve the customer. Process management can really help when faced with new internal challenges or in finding new ways to remain competitive in the ever-changing business environment.

We used the process management model to organize the company. We mapped out the organization to more clearly see the internal customer-supplier relationships and ultimately better meet the current and future needs of our stakeholders—our clients, partners, and shareholders.

Positive change

At MLCC, our slogan, “Change is debilitating when done to us, but exhilarating when done by us,” is a way of life. Our focus on quality and improving world-class customer service enables us to manage rapid growth and change over the years. We embrace quality and partner involvement, again not as a crisis of survival, but as an opportunity to effectively manage our growth and change.

Growth-driven organizational structure

We recognized that operating in functions was not the most effective way to do things, so we asked ourselves what processes we absolutely needed to stay in business. The answers (Figure 6 on the next page) became our “core processes”: (1) Develop/Market, (2) Sales/Production, (3) Funding, and (4) Servicing.

We then asked what support was needed to get the essential business practices and core processes done. Those answers became our “support processes”: (1) Systems Technology, (2) Business Services, (3) Finance, Accounting, and Underwriting, and (4) Legal Compliance.
For this new structure to work, our leaders had to clearly understand what their roles needed to be. At MLCC, we believe leaders should be “champions for change.” By change, we mean constant business improvements to meet stakeholders’ needs. We also believe that leaders are “champions for all that must not change,” namely our core values and principles.

Leadership

The Seven Leadership Activities

It is critical as an organization that we have a system to provide and further develop the leadership needed to manage change. When we developed our Seven Leadership Activities (see Figure 7), we kept them simple so that all of our partners could understand and be part of these activities. While the Seven Leadership Activities were originally designed for current leaders, ultimately, the activities became a tool to help partners in their own career planning because the activities very clearly defined the competencies of a good leader.

An annual partner survey helps develop leadership abilities

We use the feedback from an annual partner survey to provide constructive feedback and counseling to our leaders regarding areas that they may need to improve.
Improving Process Efficiency to Increase Customer Satisfaction

An annual partner survey ..., continued

improve. The survey results help to evaluate the competency of our leaders and provide a very clear definition of what partners expect from their leadership team.

360° reviews

We have initiated 360° reviews with all of our leaders to identify growth opportunities. The process includes being reviewed by five coworkers (generally one direct report, a leader, a peer, someone they have worked closely with, and one additional person) chosen by our corporate human resources area in conjunction with the leader being reviewed. The review provides feedback from three or four different levels throughout the organization. That really helps to drive the behaviors that we need in our leaders, and to help identify gaps. After a 360° review, the leaders develop personal action plans designed to close any gaps identified, using a variety of leadership tools and programs available.

360° reviews at the departmental level

Although our leadership model and leadership activities are geared toward leaders, they can be translated to anybody in the organization. In some pockets of the organization, 360° reviews are used on teams at the departmental level to help build and drive competencies.

Connecting service and process to win the Sterling Award

The development and implementation of the business planning process, the 7-Step Process Management Model, and the Seven Leadership Activities kept us very busy in 1995. By taking our service-oriented culture and putting systematic processes in place, we ensured consistency, strategic focus, and commitment throughout the organization.

In 1996, all of our hard work paid off. By addressing the issues that the initial Sterling assessment provided, we were able to make significant improvements in the organization. When we applied for the Sterling Award in 1996, we won.

Raising the bar

Winning the Sterling Award was a major accomplishment for MLCC. However, it was only a milestone in our never-ending quest for excellence. As a management tool, it helped us to continuously improve our business with a focus on our stakeholders. But at MLCC we are constantly changing and raising the bar. In 1997, immediately after receiving the Sterling Award, we set our sights on the Malcolm Baldrige National Quality Award, applied for it, and won. While winning the Baldrige, like winning the Sterling, was a major accomplishment for MLCC, we see it as another milestone along our journey in the never-ending quest for excellence.

Being world-class is not a fixed state

We have learned— as Ron Strauss, President of ML Japan Securities says— that “Being world-class is not a fixed state. It’s a mentality of growing constantly, getting better and better at what you do, and realizing that you are never finished. And also being invigorated— not exhausted— by knowing there is always more to learn.” We have always believed in continuous business improvement, and we’ve believed that all aspects of business should go through constant improvement cycles.
Room to grow

When you are in a continuous business improvement mode, you’re always looking for ways to get better. So in 1998, we once more raised the bar and began an internal assessment of our business design and processes, using the 7-Step Process Management Model as our approach to discover areas where our immediate attention could offer the most benefit to our stakeholders.

We didn’t reassess our design and processes because anything was particularly wrong; we were a very successful business. But through our survey feedback, we knew our customers and partners wanted a faster, friendlier process. We weren’t running as efficiently as we could have been. So we began an improvement process by interviewing, examining, and re-mapping our processes.

We knew that our process as it existed had several opportunities for improvement. Although we seemed to work harder and harder, year after year, our focus really needed to be on working smarter. We had outgrown a process that might have worked well at one point in time, but now it was time to change our business design to meet the changing needs of our environment.

Improving processes without looking at the big picture

Several key factors led to our need for reinvention. We had really embraced process management so individuals were improving processes without looking at the bigger picture. A group in one area would be streamlining and getting things done as quickly as possible, without thinking about what was happening in the process down the line. Partners were sending more work to the partners in the next area without taking into consideration any problems that it might have been causing.

Quick fixes can cause problems, too

Teams were creating quick fixes to solve problems in their own area, but a quick fix made by one team wasn’t necessarily shared with other teams that were doing the exact same job. This was causing issues for the receivers of the output, who were getting output one way from one team and another way from a different team responsible for the same job.

A good example of the issues associated with quick fixes involved our post-closing area. The post-closing area was a department of approximately 30 people correcting errors that were made on files because of an increased volume and limited capacity. So when we reengineered the process, we built pre-audits into the process before the loan closed. That change enabled us to look at and correct documents and files prior to a loan’s closing, instead of after closing, resulting in a happier client.

More work, but not more profit

The finance industry experienced a refinancing boom in 1998. We had more business than we’d ever had before. We processed more loans than we ever had, yet we were the least profitable that we ever had been relative to the number of origina-tions we brought in. We were working very hard, yet we had to turn customers away because we couldn’t handle the capacity. Our processes weren’t streamlined as effectively as they could have been.
Reinvention through internal process assessment

To create a faster, friendlier process, we reinvented the organization’s core loan origination process to better meet stakeholder needs. We expanded step six of the Process Management Model and implemented an improvement methodology that was a systematic approach to defining and implementing firm-wide business enhancements.

During our internal process assessment, we created a cross-functional team of five individuals to interview partners at various levels throughout the organization to see how business was getting done. We interviewed multiple partners in each position to ensure that the message we received was consistent. To assess how our business design and current processes were working, we asked partners: (1) how they did their job on a daily basis, (2) what specifically they did in their job, (3) what would make their jobs easier, and (4) what specific things slowed them down or made it harder to do their jobs. We wrapped up the interview by asking what one improvement suggestion they would recommend to make the greatest impact on their job efficiency.

To our surprise, after interviewing people with completely different job functions, we found that the themes regarding improvement opportunities were consistent (see Figure 8). We reviewed and discussed the recurring themes with our senior leadership group, focusing on the things that caused the most significant problems. We used the feedback from all the interviews and the discussions with middle and upper management to redesign a more efficient process.

Mapping the process firm-wide shows the need for improvement

We used this information to create a firm-wide process flowchart, which actually spanned three walls in a large conference room. We presented and discussed the flowchart with our senior leadership team and CEO at an off-site meeting. What we found was a mess. The exercise helped the organization realize that it was the overall process that needed improvement, not any particular area.

We used rework loops to show areas where unnecessary work was being done. Some loops were six feet long, which is a powerful statement of where our inefficiencies were located. Each of the five members of the reinvent team had a representative icon on the process flowchart that indicated a key theme that we had identified. As each of us explained our part of the presentation, we would show every point in the process where that theme was an issue, placing the representative icon on the wall map.

We also did a technology map underneath the process map. For example, the technology map would show that to do one part of the process, you needed to use six software applications. When you moved to the next section of the process, none of those six applications were being used anymore, but there were eight new software applications to recapture the same information. By visually representing the inefficient process, the map made quite an impact on the management team.
We shared the conceptual framework for the new process with the entire organization. Then partners and leaders throughout the organization used this information to design a more efficient, streamlined process for MLCC. This involved refining processes that existed, determining the infrastructure needed to support the new process, developing definitions of key roles, developing transition and implementation plans on how we were going to get there, and developing the basis for our long-term and short-term technology strategy.

To successfully implement the new process, we had to align our resources with the new needs of the organization. Our intent was to match partner skill-sets with newly created position descriptions. We asked partners in affected areas to pick their top three areas of interest based on the new position descriptions. Their current leaders and the leaders of the new areas then convened to determine the best fit for the new organization.

Notably, over 95% of the partners were assigned to either their first or second choice, so it worked out well from a partner motivation and satisfaction perspective.

As a trial run, the core reinvent team brought line partners from each of the areas prior to the reinvented process, into a computer training room. The line partners then tested the newly defined process in a mock environment, to see how it was going to work out. They worked through some of the issues that could occur once we implemented the process, and documented resolutions.

After several tests in this environment, each person representing a specific position in the new process defined, down to excruciating detail, exactly what steps would be performed in the new job. The output was an extremely comprehensive manual that included each new position with a high-level summary of what the position would entail, all the way down to specific keystrokes required on various systems. The output from that group was a very beneficial educational resource for transitioning.

What did we gain from the reinvent process? We gained improved service for our clients. One of the key goals of the reinvent process was to increase up-front approvals. We wanted to be able to say “yes” faster in the process. And we made significant progress, in that roughly 30% of clients are being conditionally approved on the very first phone call, and we're constantly making new strides. We increased efficiency and profitability for MLCC, by being able to do more with less. And we provided a better quality of life for our internal partners, being able to give them manageable workloads to allow for a better work/life balance.

We conducted “reinvent reality-checks,” to ask our partners what was really going on, how the process was working for them. We went back to the same partners that we had interviewed previously and asked them if they liked the way the new...
Improving Process Efficiency to Increase Customer Satisfaction

Reinvent reality-checks, continued

process was working, what changes they would make at this time, and if they were seeing any new inefficiencies created because of the new changes.

Basically, we confirmed several things. First and foremost, reinvent was an overwhelming success, as shown by our ability to approve more clients up-front on the first telephone call. We also realized that we needed to revisit the leadership model because it hadn’t been revised since 1995. With all the rapid changes that were occurring, we needed to determine if there were some elements of the leadership model that needed to be enhanced as well. We also determined that we now had the right process and it was time to refine the metrics and the technology to support it.

Process first, then technology

We had purposely waited to address the technology issues. We wanted to create a process that made sense and was as efficient as possible without depending on technology. In our interviews with partners, we had heard repeatedly about technology-related issues. We assured them that we would be addressing the technology issues if they could just help us get the process right first.

Now that the process is confirmed a success, we are looking at correcting the technology-related issues, in the form of a new Loan Origination System (LOS), with expected implementation in December 2000.

The reporting project

While developing the business requirements for the technology initiative, we are focusing on making sure that we have the right metrics to drive the right behaviors, through a firm-wide reporting project being conducted simultaneously with our LOS implementation.

Like most organizations, MLCC has access to huge amounts of data. We didn’t know which data were most important to the organization. Our goal with the reporting project is to identify and collect the current metrics and reports being used across the organization. For example, we were asking the supervisor of a loan processing team what reports are being used, how often the reports are used, what metrics are being collected from those reports, and how the metrics are calculated. We’re evaluating the validity and determining what the best metrics are, for each position. And again, we’re going back to make sure that the same types of reports are being used consistently.

Questions for the leadership team

We’ve also asked the 13 members of our senior leadership team a series of questions that started very high level (such as what does business success look like to them) and drilled down to very specific detail (such as what key 5-7 metrics would show them the health of the organization). We asked a lot of strategic questions and potential business enhancement questions, about everything from our business planning process to our reward and recognition system. We will use the consolidated data from these interviews as part of our SWOT process and strategic module review for 2001.
A dashboard mentality

We are identifying the critical information needs from the bottom up and the top down relative to our business strategy. We’re going to establish recommended key metrics using a dashboard mentality.

Right now, we have our monthly management report, which is a representation of all of the critical few objectives, key activities, and metrics broken down by each senior leader. However, we determined we really don’t need to see all of that information on a monthly basis. All we need to see is a very simplistic, one-page deliverable that shows which objectives/indicators are performing on target, and why others are not performing, with drill-down data to support why. We’re streamlining our entire reporting process.

Correcting out-of-target performance

Once the linkage is clearly defined and the reporting format has been established, value is added by being able to diagnose, evaluate, and attack out-of-target performance. The dashboard (the product of the firm-wide reporting initiative) will allow our leaders to better monitor performance relative to targets and focus in only on those objectives/indicators not meeting target. By means of a drill-down approach that directly ties the drivers of strategic objectives from the front-line partners all the way up to the executive level, any indicator not meeting target within stated variances will clearly stand out as an area for potential future improvement, especially if it is consistently not meeting target. Again, partners at all levels will know how and where they can potentially contribute when improvements are needed.

Key strengths and challenges

All of this information and analysis has to boil down to business results and how well we achieve them. Like everything in a continuous improvement culture, our measures have some key strengths and some key challenges (see Figure 9). We’re

Figure 9. The Measurement System.

<table>
<thead>
<tr>
<th>Key Strengths</th>
<th>Key Challenges</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Many, many measures to cover all areas of the business</td>
<td>• Identifying the indicators that have the greatest impact on the business</td>
</tr>
<tr>
<td>• Positive trends, with favorable performance relative to industry standards/averages</td>
<td>• Difficulty in producing consistent, competitive/comparative data</td>
</tr>
<tr>
<td>• Systematic improvement process in place to address unfavorable trends</td>
<td>• Rolling-up measures with different underlying metrics</td>
</tr>
<tr>
<td>• Complete understanding of linkage to overall measurement system</td>
<td>• Availability of historical data on newer measures</td>
</tr>
<tr>
<td>• Linkage</td>
<td>• Linkage</td>
</tr>
</tbody>
</table>
very fortunate to be guided by standardized review and improvement processes that focus on being fact-based. For us, linkage is the key element. Our metrics link from the individual partner-level performance metrics to the strategic company-wide drivers and metrics. This linkage allows partners to easily see how their contribution impacts the company, which often translates into instant gratification.

Process management is really about stopping, getting back to basics, and focusing on the path that MLCC wants to take for the future. This path has to be based on doing what's right for the organization as a whole while meeting the needs of our three key stakeholders — the client, the partner, and the shareholder.

When you put all the pieces together, there's one recurring theme throughout MLCC, and that's teamwork. We focus together on common goals and objectives to do what's right for our stakeholders while never losing sight of the fact that business improvement is constant.

Tracy Peacock serves as a member of the Executive Management Team responsible for the coordination and facilitation of all enterprise-wide formalized change initiatives, planning, quality, and business improvement initiatives. She joined MLCC in 1993 and has held various positions within MLCC, with a focus on organization-wide process, operational, and technological enhancements. She earned a Professional Blue Belt certification in 1997 that designates her as an internal quality consultant for the organization. She holds a B.A. degree in marketing from the University of North Florida, an A.S. degree in Business Administration from Middle Georgia College, and holds her Series 7 and Series 63 Securities Registrations under NASD.

Deanise Hemmer joined MLCC in 1995, and has been instrumental in the design and development of MLCC's strategic and business planning process. In her current role, she facilitates the annual planning process, which provides the structure and support needed to assist MLCC in achieving its long-term and short-term goals and objectives. Deanise develops and coordinates corporate communications with the firm, keeping MLCC employees abreast of organizational initiatives and activities. Her role also includes public relations for MLCC's continuous quest for excellence by coordinating, facilitating, and fulfilling public speaking requests, tours, benchmarking studies, quality conferences, and information requests with organizations across the country.

Editorial assistance for this article was provided by Charles Putney and Daniel Picard.
Without Quality You’ll Drive Out Trust and Increase Fear

by Laurence R. Smith, Editor

We’ve all heard people say, “Total Quality Management is dead,” or “I’m sick of hearing about quality; it was a fad; stop talking about it.” But have we really thought about what that means in practice? If management is not clear about what it means to say quality is dead, it might unknowingly trap itself inside a self-destructive paradigm, with everyone getting more frustrated, fearful, and angry all the time. It could be, to use a familiar warning, “throwing the baby out with the bathwater.”

What really is the story about “quality?” On the surface, it seems to be a “mixed bag.” Some had bad experiences and sought other management models. Some have done well with it and just don’t use the term anymore; they’ve gone on to develop customized systems that more fully serve their organization’s needs. Others have adopted the steadily evolving criteria of the Baldrige National Quality Award Program. (The Baldrige terminology has shifted in recent years to “performance excellence” rather than “quality.”) Some never tried any of the quality management programs, preferring to operate under traditional, authoritarian command-and-control models. Some call it yet another fad in management culture and advocate their own “better way.” The result: a lot of noise in the system.

These are, of course, turbulent times. Change may seem to be accelerated today, but it is useful to remember that the 1970s and 1980s were turbulent, too. Many organizations successfully navigated through the turbulence using “new” philosophies and practices that were termed quality management; they were management-focused, customer-focused, and employee-focused. They achieved dramatically positive results, and attracted millions of customers.

They also made money. The U.S. Commerce Department’s National Institute of Standards and Technology found that Baldrige National Quality Award-winning companies outperformed the Standard & Poor’s 500 this year by 4.8 to 1. They achieved a 1,101% return on investment, compared to a 222% return for the S&P 500. This is one of the highest returns since NIST began to track Baldrige winners in 1995. (For more information, see www.nist.gov/public_affairs/releases/g00-26.htm.)

In choosing a management model that avoids including quality, it is vital to be sure that the organization can perform well without it. There might be a danger, perhaps a subtle one, in declaring the quality movement prematurely dead, calling it a fad, and adopting a more politically popular alternative. The danger, besides the obvious one of replacing one unsatisfying fad with another, is one of throwing the baby out with the bathwater. The subtlety is that in our haste and preoccupation with the “really important” things, such as a single-minded obsession with making money and more money and only money, we don’t even see that there was “a baby in the bath.” (And if we did see it, maybe we just called it an acceptable casualty in our ongoing hot and cold war for survival and growing bigger in what some believe is an inherently dangerous, fiercely competitive world.)

The “baby” in this case is trust. Now you may think trust is something nice to have in an ideal world, but it isn’t that important in these tough economic times. What are really important are the behaviors and results you want. That kind of thinking, of course, would make it easy to throw this baby out with the bathwater without even caring about it. But if it’s business results that we really care about, it is important to see those results with both eyes. Focus one eye on the product or service results, and the other eye on the people who produce and buy the product or service being sold.

To see the importance of trust (and its relationship to quality management) more clearly, think about our lives as we have grown up. We were born into this world totally dependent on the quality of care that we received from others for our human existence. It was, in hindsight, our first experience
Our company, at first, included parents, doctors, nurses, family, friends, healthcare institutions, air, water, food, and clothing. It expanded steadily to include housing, shopping, entertainment, neighborhoods, police, government, business, church, school, media, and the environment.

Our learning began immediately at birth and continues as long as we live, both consciously and subconsciously. Early in life we also began to be trained and educated. That education included the notion that we were to grow from childhood dependence to adult independence. Americans pride themselves on becoming rugged individualists. While becoming ourselves and “being me” is an important part of growing up, it is only one side of maturity. The other side is interdependence.

The simple truth that we can ignore or take for granted is that we have learned to cooperate and depend on each other. If we didn’t, we would still be living as hunter-gatherers in the forests and jungles of the world. As individuals, we don’t grow our own food, make our own clothes, build our own transportation, roads, cities, etc. We depend on others for much of what we need for survival and everyday life. We will never outgrow this dependence on others, and that’s not bad. It is also true that a mature person achieves an optimal degree of independence. So the interdependence we can happily or unhappily (and unavoidably) enjoy is to be shareholders and stakeholders with other people in the various communities we associate with in life, and with our living planet.

As we grow up, we learn that when people band together in families, communities, and nations, they agree to learn and perform various functions that build individual and common wealth and well-being. I think we all recognize this intuitively. As we mature emotionally, intellectually, physically, and spiritually we recognize deep within us that to achieve a good life we need good quality. We need to receive and give good quality. We need quality that we can rely on in all things and in all relationships. We learn that when we are able to rely on good quality, the producers of it earn our trust. We learn to know who and what we can trust in order to continually have our physical, emotional, intellectual, and spiritual needs met. What does trust do? Trust permits us to live in less fearful ways. Trust facilitates the pursuit of happiness.

As time goes on we learn how to act and interact with others by how they treat us. So much of what we become as human beings, workers, and citizens is initiated by our thoughts about who and what we can trust. Those thoughts are instantly followed by our feelings, which we then turn into actions. Our actions produce a result. We evaluate that result with more thoughts and feelings, which lead to more behaviors, more results, more thoughts, and more feelings in a continuous cycle. It’s like using the familiar Plan-Do-Check-Act (PDCA) Cycle popularized in the Quality Movement, with a special recognition that our motivations and intentions in the Check and Act phases are driven by our thoughts and feelings about what we think happened to us in the Do phase. I emphasize what we think happened here because, as we all know, our thoughts are sometimes mistaken and lead us into places we would not have gone had we verified our thoughts before acting on them. This is one of the main features of coaching, which has become a popular and important management skill. Coaches are taught to ask questions, rather than tell. The job is to enable clear and accurate thinking as much as possible, to improve decision making and reduce costly errors.

Getting back to quality, it is useful to recognize that quality is a reciprocal phenomenon, involving what we give and what we receive. One of the things that we all want to have is a sense of value. We want to feel and be valuable. We want to receive things that are of value to us. And we do, and should, want to give to others that which is of value to them. That is what produces a high quality of life.

We live our lives, sometimes floating, sometimes swimming, in a seemingly chaotic sea of interrelationships and interdependencies, seen and unseen, local and global. This is a kind of corporate life, but the boundaries are so large that we generally don’t see that we are a part of this company. Our very citizenship actually means we are legally a part of a corporation, a national corporation, with rights and responsibilities, freedoms and liberties. We also join other companies
of people in our lives, being members of several communities at the same time. The quality of our life emerges as a complex composite in a nested system of interdependent interactions that produce what we need to live well. This includes what we receive from others in our environments and relationships, the goods and services we consume, and what we contribute to life, our own and to others. One of the things we need to learn how to do well, to improve the quality of community life, is manage those interactions. That requires systems thinking.

When we enter the world of work, after learning from two or more decades of life's experiences, we arrive with a fair amount of conditioning in quality and trust. We add to this knowledge the new work systems and processes we're expected to use, the politics and management relationships, the customer expectations, coworker requirements, supplier inputs, and other environmental relationships.

In the 1980s there was a kind of global earthquake that shook the world. A crisis loomed in the U.S. economy. It was actually building for 30 years but was virtually ignored until 1980. At that time the top management of U.S. manufacturers noticed that they were not making as much money as expected. Where had all the customers gone? They looked and found the cause. U.S. consumers discovered they had a choice in what to buy. U.S. consumers were buying products made by Japanese manufacturers because they were cheaper and were of better quality at the same time.

Economic competition was hurting American corporations badly in the late 1970s and early 1980s. The consumer discovered and embraced the alternative to expensive, poor quality products and unresponsive manufacturers that resulted from badly managed corporate America. What was going on, everyone wondered? An investigation into the cause of the Japanese “economic miracle” and its negative impact on American manufacturing companies led to the discovery of an American academic living in Washington, D.C. Nobody in “official” Washington knew of him in 1979, yet he had spearheaded the industrial growth of Japan, starting in 1950. This American teacher, Dr. W. Edwards Deming, became suddenly famous in 1980 as the person who first taught Japanese industrialists about quality. He, and others who followed (like Joseph Juran and Peter Drucker), advised management to create and manage processes and systems to build in high quality at lower costs and showed them how to do it.

They taught that quality, cost, and delivery begin with the attitudes and thinking of top management and cascade downward from there. In subsequent decades we saw that this philosophy, and the methodologies that enabled it, slowly and steadily produced innovative products, high quality, and lower costs. The problem, for the most part, was not with the worker. Most workers in the various institutions want to do the right things and do them well. Yet the institutions do the wrong things and when they try to fix them they make them worse. As Dr. Deming pointed out in 1980, 80 percent of the problems are in the systems, and management controls the systems, so the major problem is management. Yet management tends to blame the worker.

Management paradigms began to change in the 1980s when U.S. leaders visited Japanese corporations and learned how those organizations were led and managed. Alarmed and threatened, leading American manufacturers discovered they had to change their management philosophies and methods. Western manufacturers adopted these ideas in the 1980s and achieved great results in the next 10 years.

American observers noticed that there was more participative planning and management in the Japanese firms, which facilitated innovation, speed, better quality, and lower costs. Consequently, American firms eliminated many levels of management to get decision making closer to the front lines. The traditional American style was that managers were paid to think and workers were paid, not to think, but do as they were told, creating an adversarial relationship between labor and management that was widespread. Management now enlisted the brainpower of their workers, as well as their workers’ hands. Organizational planning and management was pushed down into lower levels of the organization, and spread horizontally, instead of remaining centralized at the top. That
change resulted in management becoming closer to the customer. It produced a quicker, more responsive, and more innovative organization. It also began to restore consumer trust and loyalty.

Then, when the Japanese economy suffered in the 1990s, for reasons other than “quality,” Western management seized on the notion of declaring quality dead. They tried to go back to command-and-control management, giving the consumer the least quality they could get away with, paying workers the least they could get away with, while maximizing their own incomes and the corporate profits. Is it any wonder that trust is hard to find?

The point of all of the foregoing material is to make apparent the connection between quality and trust. It is that when we don’t get the quality we expect or want in any of our relationships, involving either individuals or public or private enterprises, we think our trust has been violated, and we feel violated. When the source of our violated trust denies our claim, or refuses to restore the quality of the relationship we wanted, a crisis point is produced. At that point we can easily and quickly get angry and move into an aggressive fight mode. Or we can feel hurt and take a flight response, withdrawing into apathy. In both cases our freedoms can be at stake. Violence can lead to a loss of freedom through more laws and greater regulation. Apathy can lead to a loss of freedom through inertia of the masses and from political power grasped by activist special interests. Conversely, when trust exists, we gain the freedom to be more positive, creative, and innovative.

We can, however, adopt a more mature response, one in which our freedoms grow. We can choose, and keep choosing, higher quality. We begin to accomplish this by seeking to balance the initially narrow and hardheaded thinking of the mind with the broader, caring, emotional intelligence of the heart. In this way we avoid destructive anger or apathy in favor of creative improvements in quality that build trust and a better way of life. This kind of thinking is new in our culture because Western society has placed overwhelming developmental emphasis on the intellect. We have been led to believe that the IQ is what is really important in selecting people.

We now know that there are multiple intelligences that need to be used to achieve performance excellence. We now know that it is unwise to expect management to be mental and do “hard stuff,” and not be bothered with emotions or matters of the heart, the “soft stuff.” Emotional intelligence is real. It is connected to health and well-being and is a major indicator of performance excellence in managers and leaders. As some corporate leaders have learned from successfully facing hard competitive times, the soft stuff is the hard stuff.

Now, you may be thinking that all of this is wishful or intellectual thinking, okay in a perfect world but we have to live in the real world, one that calls for tough thinking and tough decision making in a dog-eat-dog world of intense, cutthroat economic competition. My response to that is that it is true that we have to live in the real world but that world is ours to create. The world that we are creating now, through our actions and inactions, will be the world that we and our children will be living in tomorrow. This, of course, is not a new thought. An unknown ancient Chinese philosopher said, “One generation plants the trees, another gathers the shade.”

And that brings us back to where we began, the link between quality and trust. If we, through ignorance or single-minded pursuit of some short-term political or monetary gain, make quality a scapegoat for the errors of management along the way, we send ourselves down a path of decline. We will never solve our problems if, when things go wrong, we send a scapegoat out into the wilderness, with such sentiment as: Quality is dead! We will begin to solve our problems when we recognize that quality and trust go hand in hand. We will begin to solve our problems when we ask ourselves the right questions.

The major impact of quality in our lives is trust. That includes a trust that people all over the planet are asking the right questions, questions that enable us to produce a good quality of life on earth. That’s what interdependence is all about. The major impact of such trust will be less fear, a healthier quality of life, greater freedom to innovate, and the ability to create a better life for our children and ourselves.
Using Performance Excellence Programs to Create a Strategic Revolution in the Firm

Authors
James Hunt, Elaine Landry, and Jay Rao, Assistant Professors, Babson College, Babson Park, Massachusetts

Abstract
Experience with performance excellence initiatives (formerly known as Total Quality Management, or "TQM") has left some firms disillusioned. We propose that this disappointment is due in part to the fact that firms have too often viewed those programs solely as a tactical "program" rather than as a strategy that can fundamentally change the firm and how it competes. This article first explores the dangers that lurk in such a limited view of performance excellence efforts. As counterpoint, we describe the experiences of one firm, KomTek, Inc. of Worcester, Massachusetts, to illuminate the potential for a strategic revolution that is possible through comprehensive—both tactical and strategic—TQM efforts.

In the late 1980s and early 1990s, numerous U.S. manufacturing firms implemented performance excellence programs, with the goal of increasing customer satisfaction by increasing quality and lowering costs. Some firms in fiercely competitive industries managed to enhance their viability through the use of TQM methods and programs, and survive. By the late 1990s, however, the ability of quality programs—by themselves—to deliver sustainable competitive advantage had severely eroded. Having achieved product quality, the competitive battle shifted to a race for lower and lower costs. Labor costs, in particular, were targeted as a major problem, in relation to a now very global marketplace.

Many firms have been confronted with the dilemma of whether to build upon, or abandon, the tactical successes of their quality programs. We argue that the true value of quality efforts may lie ultimately in their ability to serve as a foundation for a strategic revolution for the firm, as the benefits of management and labor's shared attention to broader organizational capabilities are leveraged. While competition in the 1980s and 1990s may have been around quality and cost, competition in the next decade is more likely to be around the ability of a firm to learn, adapt, and innovate, just the kinds of capabilities that can be the outcome of a commitment to performance excellence programs and all that they entail. We argue that such a view requires a change in the mindset about and perceptions of performance excellence programs on the part of a firm's (business and labor) leadership. This view is distinctly at odds with one that holds that the key to global competitive success is to cut cost solely through shipping work to low labor cost areas of the globe.

KomTek, a forging and casting company, is an example of how the outcomes of a long-term quality effort, and a responsible, adaptable, innovative, and learning-
oriented work force, can serve as valuable strategic resources. In 1989, this small forging plant created a competitive operational strategy built around their TQM program. They fueled their initiative with an innovative labor-management partnership. And, they did more than survive. They emerged from the turbulent decade of the 1990s as a learning-oriented, adaptive, flexible, and innovative organization. In this article, we will use the KomTek story to illustrate how an operational strategy grounded in quality principles, far from being limited to the task of process improvement, can evolve into a strategic force that will fundamentally enhance an organization's capacity to adapt to, and compete within, the global economy.

This case offers important lessons for other firms struggling to survive. Our discussion aims to be of particular use to those organizations that may be—paradoxically—considering the diminution of their quality efforts and the competitive advantage they may confer.

Developments in TQM practice

In the early to mid-1980s, several Japanese firms made significant inroads into the U.S. markets primarily due to superior product quality and lower prices in such product areas as automobiles, semiconductors, audio-video, and home appliances. Many U.S. firms tried to emulate the quality efforts of the Japanese firms and worked to improve product quality and profitability, reduce costs, and increase customer satisfaction. TQM became a “hot” business model and was embraced by thousands of organizations.

Unfortunately, by the mid-1990s, a number of firms started reporting lackluster economic returns on their TQM investments. Peter Senge, in a keynote address to the 1993 American Society of Quality Control (ASQC) conference, summarized surveys on TQM conducted by the Arthur D. Little and McKinsey corporations. Senge reported that of the 500 TQM firms surveyed, less than a third were accomplishing anything and two-thirds of the programs had ground to a halt (Ahire et al., 1996). The media quickly jumped on several such reports and declared the TQM movement “dead.”

Researchers have recently begun to analyze what really happened during this period. Hendricks and Singhal (1999) empirically demonstrated that quality initiatives dramatically improved the financial performance of the firm when—and if—TQM, with all of its components, was implemented effectively. Studies reveal that successful implementation of a comprehensive performance excellence program involves planning, effort, patience, and tolerance for setbacks and pitfalls. Ineffective examples appear to result from a “quick fix” mentality. Specifically, hopes of instant gratification have led some firms to ignore well-established fundamentals of the TQM approach: a demonstrated and ongoing management commitment, realistic expectations about the time frame required to achieve success, caution about over-reliance on statistical methods, and a sustained quality-oriented culture.

Too often, TQM was viewed as a tactical program oriented to short-term operational effectiveness goals. Although even these TQM efforts often produced a
Developments in TQM practice, continued

high quality and well-controlled process, it was one with results that competitors could easily replicate. To effect sustainable shifts in the competitive dynamics of a firm within a particular industry, changes to both organizational culture and organizational capability must also be achieved. In order to do so, the organization had to develop a highly empowered and capable work force in full partnership with the firm’s managers and owners. As this was normally a fundamental challenge to the organization’s existing culture, it was one of the most daunting, and often ignored, components of quality programs.

In the 1990s, most firms had instituted some form of quality program as a response to external pressures on product quality and costs. Today, in the global environment of 2000, competitive pressures also demand that a firm has the ability to source work from one continent to another while simultaneously upgrading and adjusting domestic manufacturing processes. The concept of speed no longer refers solely to time to market, but also to how quickly a firm can deal with such demands. Further, firms routinely face cost pressures from multinational companies that locate facilities in underdeveloped countries with significantly lower labor costs. The quality programs implemented by most firms did not adequately meet these challenges (Niven, 1993). The survivors have had to be aggressive in expanding their quality strategy to address a broader set of business demands over and above the traditional concerns of flexibility, speed, and service.

Alternative views of TQM

TQM entails an effort at “managing the entire organization so that it excels on all dimensions of products and services that are important to the customer” (Chase et al., 1998). This view of TQM is codified as performance excellence criteria set forth by the Malcolm Baldrige National Quality Award (NIST, 2000). The Baldrige program stipulates a comprehensive approach to quality, specifying seven areas that need to be addressed to achieve performance excellence: visionary leadership, strategic planning, customer and market focus, information and analysis, human resource focus, process management, and business results. Such a view of the requirements of performance excellence was advocated by the early works of the quality gurus Crosby (1978) and Deming (1986), and demonstrated by many Japanese firms in the 1980s.

Some of the early models of TQM stipulated that increasing levels of quality could be obtained while reducing costs through operational effectiveness. As noted previously, many companies embraced the TQM approach in the last two decades, viewing it as a tool to quickly improve quality while simultaneously decreasing costs. Often, however, the companies did so without a true appreciation of performance excellence and all of the required processes as advocated by these thought-leaders.

While improvements in operational effectiveness at these firms might have contributed to superior profitability in the short run, such innovations by themselves were not sufficient to sustain this strategy long term. Easily replicable management techniques and support from consultants facilitated rapid diffusion of best practices.
Alternative views of TQM, continued

within many industries. It became very difficult for firms to compete successfully solely on the basis of operational effectiveness over an extended period of time (Porter, 1996). As competitors imitated the quality achievements of a firm, the firm would once again find itself competing purely on cost. And, when firms began to seek major costs to attack, labor was an obvious target.

Once labor costs became a renewed focus, many firms opted to source manufacturing to low-wage areas. The adjustment also meant an attempt to transplant TQM to the new locale. This process often resulted in the effective end of the firm in its domestic location and the discharge of now highly competent workers. In these cases, both the investment in people and the transformation of the firm into an organization that could compete around knowledge are often completely lost. Frustration with these experiences caused many to express their disappointment in the investments they had made in their quality programs (Niven, 1993).

This failure to value human capital is extraordinarily ironic given that in the twenty-first century most businesses will have to compete on knowledge if they are to survive (Ireland and Hitt, 1998). Currently, the push to cut costs, regardless of the long-term impact of doing so, may be forcing many firms to destroy their future competitiveness. Further, the loss of manufacturing capability in a community also will mean loss of jobs, and other social benefits that spring from the firm’s existence.

Commitment to a broader strategic view of performance excellence initiatives becomes untenable when the scenarios described above are analyzed. Deming’s view was that TQM could be viewed more holistically, and more productively, from the intersection of organizational behavior and strategic management. This perspective pushes the organization to consider the firm’s entire value chain (i.e., partnerships with suppliers, customers, and society). Such a view of a total quality program can lead to surprising results even in the most competitive industries. It does, however, require continual learning and change, and a sustained focus on all that this holistic view implies: employee teamwork initiatives, motivational programs, training in job-specific and human relations skills, and introduction of policies that lead to increased employee empowerment.

KomTek and the forging industry

KomTek, a division of Kerick Enterprises, is a privately held forging and casting company that specializes in high technology custom products for the aerospace, nuclear, and medical industries. Currently, the Worcester, Massachusetts-based company has 150 employees and revenues of $30 million. The KomTek story, from 1968 to 2000, reflects a constant struggle, and need for adaptability, within the brutally competitive and shrinking forging industry.

The forging industry includes three major segments: custom forging, captive forging, and catalog or commodity forging. Over the last 20 years, this industry has undergone a painful contraction due to overcapacity and pressures from world markets. In the early 1980s, a deep recession shrunk end-user markets, weakening many operations. The reduced competitiveness of the U.S. forging industry was
KomTek and the forging industry, continued

compounded by import penetration. Between 1979 and 1990, an estimated 25% of the firms were forced out of business. And, the closing of more than 100 forging facilities caused a loss of more than 16,000 jobs (Forging, 2000).

Custom forging operations, such as KomTek, make parts to order for customers. This segment of the industry shows revenues of approximately $5 billion annually. At this time, 250 companies in approximately 300 plants in the U.S. and Canada perform forging. North American and Western European businesses in this segment are now typically competing for very high quality, specialized markets in areas such as aerospace and medical devices (Forging Industry Association, 1999).

Competing in the custom-forging high-quality markets requires high quality products and on-time delivery, while at the same time keeping prices and margins low. Forging is a capital-intensive industry. New, more sophisticated, and more expensive equipment is continually being developed, as the manufacturing process is refined. Salaries for skilled workers are also high, particularly in Europe and North America. Direct labor salaries at a unionized plant such as KomTek typically begin around $15 per hour, plus benefits.

As the 1980s were drawing to a close, KomTek’s goal was to become a world-class manufacturer of closed-die forging and castings. The owners—CEO Robert Kervick and his father Paul—reviewed the company’s viability, with respect to achieving this objective. Revenues in 1989 stood at approximately $25 million, up from $950,000 two decades earlier. Employment at the plant was at its highest level, growing from 35 workers in 1968, to 200 by 1989. The company had good relationships with its customers. And the business had an excellent reputation as a good corporate citizen in its home city of Worcester, Massachusetts. The executive team was committed to retaining jobs in a community that had experienced continual erosion of its industrial base. KomTek was also aggressively re-investing in the company in the form of upgraded technology.

By the late 1980s, the pursuit of the custom forgings market was the only viable business strategy available to KomTek. The commodity forging market was closed off because of the high costs of domestic production. Custom forging customers demanded even higher levels of quality. However, they also had concerns about costs and were liable to vertically integrate and in-source work if they could do it more cheaply, while retaining quality.

Under these circumstances, TQM appeared to offer a logical competitive operations strategy to the firm. TQM could help KomTek supply products that could be used in situations requiring very high levels of reliability, such as airline engines and hip prosthetics. In addition, TQM promised to provide a means to address cost issues through waste control and other inefficiencies in development and manufacturing.

When CEO Kervick and his strategy team evaluated the company alongside these new realities, they came to the disturbing conclusion that neither the manage-
The evolution of the KomTek strategic model, continued

Readiness for survival—building a foundation through total quality

...ment team nor the work force was capable of undertaking a significant quality effort. They made the commitment to address major issues in the areas of labor-management, leadership style, and employee training.

Although labor-management problems at KomTek were not an overriding concern in the 1980s, there was a fundamental distance between the two sides. Workers, though highly skilled forge hammer operators, focused solely on their own work. They were not encouraged by supervisors to think about process problems or improvements. Collaboration, in general, between labor and management was rare. Collaboration across departments was nearly non-existent. Over the years, a predictable level of mistrust occurred. Working on a problem meant blaming and punishment, not learning. Labor viewed management as out to get the most profit from each transaction rather than working for the long-term good of the work force. Management viewed labor as taking advantage of their own situation with unnecessary rules and bargaining tactics.

CEO Kervick and several members of the bargaining unit leaders became convinced that it would be necessary to bridge the gap between the various groups in the firm if any movement toward collaborative problem solving were to take place. Both labor and management confronted the problem of “lack of trust.” At one point early in the process, one of the Union representatives suggested that if management was serious about making fundamental changes and sharing power with the bargaining unit, then they ought to put the union’s name on the building next to KomTek’s logo. Much to their surprise, “United Steel Workers of America, Local 2936,” was immediately added to the outside of the company’s two plant buildings. This symbolic act sent the message that management was ready to listen, and to make changes. Over the two-year period between 1989 and 1991, management and labor continued formal and informal discussions, shared training experiences, and—with some external consulting support—began to create the conditions by which a sense of shared responsibility could emerge.

Throughout this strategic change process, it was necessary to pay vigilant attention to the issue of management style. A particularly gifted plant manager showed a willingness to challenge the hierarchical management style customary at KomTek to that time. His ability to communicate effectively with all parties, acknowledge the problems of management, and address issues with a high level of perceived fairness gave him a great deal of credibility. He found himself siding at times with the workers, against a supervisor. This was an unheard of action for a manager at KomTek prior to the TQM change process. Still with the company, his role has changed over time to a more strategic one. Importantly, in their efforts to replace this plant manager, the company has twice recruited individuals with significant industry experience. Over time, however, both individuals managed with an autocratic style that threatened regression and the consequent loss of the labor-management partnership. In both instances, those individuals were replaced.
During this period, KomTek invested in extensive company-wide training. The result was that work was redesigned to incorporate an aggressive use of highly empowered self-managed teams. The labor-management contracting process was reworked (with the help of representatives from the International Office of the Steel Workers Union). Collaboration between shop-level workers and customers was commonplace.

Over the course of the early 1990s these efforts generated important tactical results for the company, including improved employee morale, significant decreases in waste and scrap, greatly reduced workers compensation claims through an improved safety record, and a variety of other process improvements.

By 1997, employees at KomTek had assumed significant and almost unprecedented responsibility for running most aspects of the plant. Workers were involved in a variety of joint union and management planning innovations around new technology, marketing, and customer satisfaction. These changes dramatically altered the culture of the firm. For example, on plant visitations, members of the bargaining unit, not management, conducted the tours. Union guides were equally likely to discuss business issues such as global competition and market positioning as traditional wage and benefit concerns. On their own initiative, several members of Local 2936 made themselves available to other USWA Locals interested in learning about the training process and problem-solving teams in place at KomTek. Except for firing or disciplining other members of the bargaining unit, self-managed work teams absorbed almost all the responsibilities associated with traditional supervisory positions. The number of shop-floor supervisors required to run the day-to-day operations of the plant decreased from 12 to three over seven years.

Although this significant investment of commitment, trust, training, and money stabilized KomTek, it did not serve to fundamentally protect the company from the vicissitudes of its market. KomTek remained profitable and independent throughout most of the 1990s, while a number of KomTek’s competitors lost their independence and were forced to dissolve or accept acquisition by other firms. By the end of the 1990s, two large manufacturers controlled nearly $2.5 billion of the $3-billion marketplace in the U.S. alone. The remaining $500-million market was a bargaining zone for the remaining 150 shops. The decade of the 1990s was fought over both quality and cost. By 2000, most firms had met the product quality challenge and had turned their attention to the issue of costs.

Like others in their industry, KomTek began to face enormous pressure to outsource work to other areas around the globe. Large customers now expected that supplier firms would phase out U.S.-based operations and manufacture in low-wage countries alone. Specific industry pressures also had a challenging impact on KomTek’s margins. In the aircraft industry, for instance, KomTek was a first- and second-tier supplier of new engine parts. KomTek also supplied after-market spare parts to other large suppliers who, in turn, provided these products to the aircraft engine manufacturers. In this particular business, the aircraft engine manufacturers usually “give
Responding to challenges within the global marketplace, continued

away the engine at cost to airline companies and rely upon after-sales parts and service, for profitability. First-tier suppliers were increasingly squeezed by alliances between their ultimate customers and other large suppliers that tended to erode first-tier suppliers’ bargaining position. Threats on the part of large customers to vertically re-integrate (i.e., make the parts themselves, often abroad) continued as well. The sum of these competitive challenges threatened the very existence of the firm.

Not surprisingly, the survival response for many firms was to end their investment in the people in their domestic plants and take unilateral action (rather than collaborating with employees), by selling the business, or moving the operations out of the United States. In contrast, KomTek responded with a different plan for survival. The firm redeveloped partnership agreements with large customers in which low margin work will be sourced to collaborative off-shore ventures while growing the high-margin business and new business partnerships at their existing plant. KomTek will expand both domestically and internationally using as foundation the significant organizational capabilities that resulted from investments in total quality and the related shifts in the organization’s culture.

This new survival strategy came with the participation and involvement of the company’s Union members. As they had in the late 1980s, and as had now become a habit, labor and management confronted these competitive threats jointly, rather than individually. In doing so, the business leadership was now working with a group of bargaining unit leaders who not only understood quality but also in this case more importantly understood the business and the strategic realities that the firm was facing. CEO Kervick charged a joint management and union working group with the task of assessing ways for selective projects to migrate to an offshore operation. The charge included the directive that any overseas work complement rather than compete with the long-term interests of the Worcester facility and its workers. The teams at KomTek have reached the conclusion demonstrated in research (Heckscher, 1988) on firms that have undergone similar pressures— mutual respect and active partnership is the only route to surviving economic battles.

The 1999 contract negotiations discussions resulted in a decision to codify management and labor’s interdependence. Specific language was written into the labor-management agreement to reflect the value the organization places on partnership. The contract agreement states that, “The Union and the Company share responsibility for the long-term viability of the Company and, therefore, must share in the decision making with respect to the employment security of its employees” (KomTek Cooperative Partnership Agreement, 1999.) Subsequently, joint labor-management decisions were made regarding work-force reductions at the plant (approximately 30 employees), changes in the structure of employee compensation (lowering base pay and placing more compensation at risk based on company performance) and changes in healthcare benefits. There has been very little turnover in the plant since the early 1990s. The vast majority of KomTek’s work force and therefore the skills and habits of organizational learning that have evolved over the past decade, remains intact.
Responding to challenges within the global marketplace, continued

Currently, a KomTek plant is being developed in Tunisia to handle the low-end, highly labor-intensive work. Employees at KomTek in Worcester will lead the training efforts to prepare management and workers for the Tunisia plant operations. In addition to performing high margin manufacturing, workers in Worcester will continue to be engaged in research and development efforts involving the introduction of new technologies, new alloys, and new manufacturing processes. The now highly educated and extremely collaborative work force can then continue to represent a strategic asset for the company. There is agreement within the Worcester plant that this new venture would not have been possible without a shared labor-management collaboration in the decision-making process and a shared world view of KomTek's business realities.

In 2000, KomTek views itself as a highly energized, focused organization ready to leverage the knowledge and capabilities that evolved from a sustained performance excellence program effort. They have relied on the well-established values of their quality program to preserve and strengthen their industry position. The changes in the difficult and demanding market served by KomTek and its competitors illuminate just how critical it has been to make appropriate choices at each strategic crossroad. In KomTek's case, these decisions have included layoffs, hiring and firing of senior-level managers, developing work-force flexibility, union concessions, and ultimately the decision to source some work in low labor cost areas while expanding and retaining high margin work at home.

The KomTek story suggests that the human capital that develops through a total quality effort can potentially provide a foundation for a firm's survival and should not be ignored. It would appear that KomTek's investment in total quality has improved its ability to compete on resources in a sustained fashion. The actual activities in which the KomTek work force engages at both the strategic and tactical levels now go quite far beyond the use of the tools of TQM. Employees have more understanding of the need to be flexible in the face of competition and are prepared to commit their full intellectual energies to dealing with business issues. The ongoing organizational transformation does not rely on the existence of performance excellence teams, but rather on the joint use made of these principles by individuals representing both labor and management.

How can other firms secure their own survival strategy? Research (Collis and Montgomery, 1995) on the resource-based competition school of strategy suggests that it isn't enough for a firm to have resources, such as a highly educated work force. Rather, that work force must be doing something that is valuable in the marketplace and relatively difficult to replicate.

A tactical definition of TQM emphasizes the use of quality tools in a business process. This view can confuse the tools for the actual substance. Similar conceptual confusion occurs when managers and scholars try to define “high performance work organizations” (HIPOs). In fact, HIPOs typically utilize many tools familiar to
Lessons from a global market survivor, continued

students of TQM, such as self-managed teams, lean manufacturing, and tools for studying work processes. An alternative is to define the concept by what it does, not by its tools. The high performance work organization might then better be described as one in which “the organizational system continually aligns its strategy, goals, objectives, and internal operations with the demands of its external environment in order to maximize organizational performance” (Kirkman et al., 2000).

This, of course, sounds much like a description of the evolution of KomTek. Those firms that abandoned quality programs after extensive investment may have been making the mistake of confusing tools, a resource that perhaps didn't seem to be of value, with a learning-oriented culture, a highly valuable resource.

Conclusion

The economic context and challenges faced by KomTek are not unusual. Many firms that invested significantly in their TQM efforts now find themselves under intensive competitive threat, particularly around the question of costs. Clearly, experience at KomTek strongly suggests that management and, where appropriate, labor leaders consider the potential strategic value of the comprehensive efforts illustrated in the KomTek case. We suggest that there are several lessons that can be learned from the KomTek experience and from this analysis:

- If the strategic value of the firm's investment in total quality is a learning-oriented, adaptable, and innovative work force, then it is necessary to maintain a steadfast commitment to the partnership between labor and management. This will result in a truly shared sense of responsibility for the firm's survival. There can be no compromises here.

  Regressive management styles, such as a reversion to top-down autocratic leadership in the face of declining economic performance, can inhibit the maintenance of this sense of shared responsibility. Shared responsibility requires a shared commitment to common goals. The failure to maintain that commitment on the part of management, through actions that show management's intention to gain at the expense of labor and without regard to the long-term interests of the firm, may undermine the strategic potential of a total quality effort (Pfeffer, 1998). Managers may not even notice that they have subtly destroyed something of significant value to the firm.

- Efforts to share power and responsibility are critical— even with respect to business strategy and even during a company's most difficult periods. As noted in the previous point, total quality efforts have typically involved shared decision making at the shop-floor level. If total quality is to be leveraged for strategic purposes, it follows logically that employees must be involved in strategic decisions as well. This means, of course, that they need to be prepared to actively participate in such strategic decision making. Interestingly, at KomTek, experience suggests that the union representatives will be much more likely to consider concessions on their part if they have full participation in the business decisions that require those concessions.
Conclusion, continued

- If your firm is seeking to compete around knowledge, innovation, and flexibility, persist in educational efforts and the development of leadership throughout the firm. This will result in a deep and learned sense of the business issues and strategic options that the firm confronts. At KomTek, managers found that, over time, they tended to hold fewer of the "whole company" meetings that often began when the quality programs was initiated. In retrospect, they now see that as a mistake. Working to upgrade the knowledge and the skills of the work force must be continuous, as one can never know when or how that knowledge will be needed, particularly in a global and turbulent business environment.

- Integrate all your efforts. Take care to make sure that using a total quality and labor-management partnership as a foundation for strategic change is integrated with other strategic efforts of the business, such as those related to marketing, global partnerships, and investment in technology. KomTek was not working only on labor-management partnership issues as this case progressed. They continued to invest in new technology, they searched the world for appropriate business partners, and they constantly considered alternative business and marketing tactics. Most important, this vigilance has produced a plan that continues to be the road map to business survival.

Author information

James Hunt, DBA, is an Assistant Professor of Management and holder of the Charles E. McCarthy Family Term Chair at Babson College. James teaches management, strategic human resource management, and leadership. James is also the co-faculty director of the Coaching for Leadership and Teamwork Experience. James’ research is in the area of leadership development.

Elaine Landry is an Assistant Professor of Management and holder of the Wilson Payne Term Chair at Babson College. Her principal research interests are negotiation in employment relations and the theory and pedagogy of negotiation. She has received grants from the U.S. Department of Labor and the National Institute for Dispute Resolution, and has taught and published works on managerial negotiations, mutual gains bargaining, civil rights and community conflict, and cooperation in the labor-management relationship.

Jay Rao is an Assistant Professor of Operations Management and holder of the Gupta Term Chair at Babson College. His research areas include Service Operations & Management, Service Quality and Consumer Satisfaction/Dissatisfaction in Services. He has published several articles in the Production and Operations Management Journal and Quality Management in Health Care. He is the co-author of nearly 10 business cases, some of which have received national and international awards.

References


References, continued