Richard Straub

The Great Transformation

In his landmark book, *Innovation and Entrepreneurship,* Peter Drucker quotes Thomas Jefferson: "Every generation needs a new revolution."[1] However, Drucker quickly makes it clear that, as much as he admires Jefferson, this comment is off the mark.

Drucker notes that most of the revolutions we have witnessed in recent history have, in fact, failed to deliver what they promised. As French philosopher and political theorist Alexis de Tocqueville pointed out, revolutions do not demolish the prisons of the old regime; they tend to enlarge them.[2]

The conditions that typically lead to revolution in the first place are oppressive leadership, bankrupt ideas and institutions, and, above all, society's failure to renew itself. Achieving large-scale social change without going through the upheaval of a revolution is obviously the better option. The term "transformation" aptly describes this preferable path.

A key question we face today is whether the Western world has the capacity to transform itself in ways that will achieve growth and prosperity, rather than to move inexorably toward social and economic decline and, quite possibly, experience the wrenching trauma of a citizens' revolt along the way.

DANGEROUS TRENDS

Evidence of the need for social change is strong, and a number of factors have converged to make the picture especially daunting. Taken together, they indicate that we are heading toward decline rather than prosperity.

- **Economic Stagnation and Financial Instability.** Even though some indicators have improved since the global financial meltdown that began in 2007, the structural problems that bogged down our economies are by no means resolved. In a recent interview, American economist Larry Summers talked about the probability of secular stagnation as a "base case" for decisionmakers.[3] Moreover,

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the debt crisis many developed economies are dealing with severely limits those governments' ability to provide further stimulus.

- **Growing Income Inequality.** French economist and academic Thomas Piketty argues in his much-discussed book, *Capital in the 21st Century,* that capital has essentially won in a contest with labor over the division of economic returns in the long term. With returns on capital growing faster than the economy overall, capital's share of economic value is increasing at the expense of labor's, resulting in widening income disparities. Piketty's profound analysis points to this as a long-term trend.[4] Henry Mintzberg, a leading management thinker, comes to a similar conclusion in a 2014 online pamphlet, *Rebalancing Society,* in which he analyzes the imbalance in society.[5]
- **Unemployment and Underemployment.** Unemployment and underemployment are at a stubbornly high level, and youth unemployment remains a particular concern. Some Western trade unions have made things worse by opposing flexibility within labor markets. However, Drucker for one believes that unions are an important "countervailing power" to large corporations and thus "modern society . . . needs an organ such as the labour union."[6]
- **An Aging Population and Low Birth Rates in Western Countries.** Demographers predict that by 2035 one billion people around the globe will be above the age of 65.[7] At the same time, falling birth rates in developed economies are reducing the number of people who will support this older population. The implications for funding retirement and social protection systems are striking, and the situation is expected to create a financial burden for the future workforce that is on course to become unbearable.
- **Untamed Leviathan.** "The state almost everywhere is big, inefficient and broke," *Economist* editor John Micklethwait remarked in 2011.[8] Since then things have only gotten worse. The suffocating bureaucracy of the state too often deprives advanced economies of the oxygen they need for innovation and growth.
- **Increasing Corporate Autism.** Since the 1980s, corporations have increasingly set aside concerns for a broad set of stakeholders—customers, employees, and communities—in favor of the supposed interests of shareholders. This trend has accelerated since the financial crisis and has led to a significant reduction in value-creating investments with a long-term horizon.

Will these steadily worsening trends become tomorrow's reality, or can we still shape a better future? How do we escape the vicious cycle we seem to be caught in? Obviously, levers need to be pulled at both the macro and the micro levels.

At the macro level, monetary and fiscal policy, labor markets, social security, tax regimes, and rules governing competition all need to be addressed. Policymakers should focus on removing obstacles and creating incentives in the right direction. This approach can be at least partly summarized as "managing by getting out of the way," which means refocusing regulations in the fields where

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they are essential and otherwise enabling productive forces to act without artificial and counterproductive burdens.

The micro level is, of course, the heart of management, where actual value is created and destroyed, and where specific decisions are taken that lead to world-changing innovations—or to a waste of productive resources.

Actual growth happens in individual organizations that are successfully managed before growth figures for a country are calculated. Meanwhile, politicians and other experts are obsessed with aggregations and ratios, and they tend to forget that the action happens in real life and not in the abstractions of economics.

Management is a real-world practice dealing with people and organizations. Managers can make a world of difference by applying their knowledge, their creativity, their emotions, and their values. Management, in this broad (and very Druckerian) sense, includes commercial players, nonprofit organizations, and public-sector bodies, each of which has a mandate to create value and achieve its mission.

American author and journalist Walter Kiechel wrote in the *Harvard Business Review* that "management has come to shape the world in which we work [amid] an era of global triumph, measured by agreement on certain key ideas, steadily improving productivity, the worldwide march of the MBA degree and a general elevation of expectations about how workers should be treated." Kiechel asserts that Drucker, a key figure in the rise of management as a discipline, "laid out a vision of the corporation as a social institution—indeed, a social network—in which the capacity and potential of everyone involved were to be respected."[9]

MANAGEMENT: A TRACK RECORD WITH BIG QUESTION MARKS

We have learned a lot about management in recent years. Once we accept the importance of good management for the economic and social well-being of today's world, it is legitimate to ask a critical question: are managers equipped—in terms of skills, competencies, and courage—to lead us toward a Great Transformation?

Management has become the focus of education, research, and practice. Extensive thinking has gone into developing the discipline of management, its tools and methodologies, and, increasingly, into specialized fields such as marketing, operations, finance, and human resources. Thousands of books proclaim the latest breakthroughs and demonstrate the progress of management thinking and research. For example, Julian Birkinshaw, a professor at London Business School, suggests in his book *Reinventing Management* four main dimensions along which management has been steadily, if slowly, evolving:[10]

- Coordinating work with a shift from bureaucracy to emergent practices
- Communicating decisions by drawing on collective wisdom
- Setting objectives that rely on the principle of obliquity rather than direct alignment
- Motivating employees by intrinsic rather than extrinsic methods

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However, a reality check shows that, despite considerable progress in making management more effective, many fundamental challenges remain. Bureaucratic hierarchies, in the form of control-oriented, top-down structures, are still highly prevalent.

In his book *What Matters Now,* American management thinker Gary Hamel argues that innovation, particularly disruptive innovation, is unlikely to flourish when a few executives have a chokehold on resource allocation.[11] The overwhelming internal complexity of large organizations creates a tendency to focus internally rather than on taking an "outside-in" perspective. This brings a loss of focus on customers and, as a result, more energy is spent on resolving internal issues than on finding new ways to delight customers.

The overemphasis on short-term gains at the expense of long-term prosperity has become the new normal, despite its negative consequences. In a recent McKinsey survey of one thousand corporate board members and "C-suite" executives, 63 percent of respondents stated that the pressure to generate strong short-term results has increased over the past five years,[12] even though 86 percent declared that using a longer term horizon to make business decisions would have a positive effect on corporate performance in a number of ways, including strengthening financial returns and increasing innovation. Regrettably, the creed of shareholder value still has a tight grip on corporate executives and their governance.

When one looks behind the gadgetry of corporate finance, the results are not nearly so impressive. The rate of return on assets and on the invested capital of U.S. firms in 2011 was only one-quarter of what it was in 1965.[13] Moreover, management's effectiveness in winning the hearts and minds of the workforce is even worse; only 13 percent of people employed worldwide say they are engaged at work, according to Gallup's 2013 study, the State of the Global Workplace. In other words, about one in eight workers—roughly 180 million employees in the countries studied—are psychologically committed to their jobs and likely to be making a positive contribution to their organization.[14]

Clayton Christensen, a Harvard Business School professor who is recognized as the number one management thinker in the Thinkers50 ranking, maintains that management's misallocation of capital is putting capitalism itself at risk.[15] With a constant drive to achieve short-term cost reductions, most corporate innovations have centered on improving efficiency. However, the capital freed up by increasing efficiencies is not being used to generate what Christensen calls "empowering innovations," which would create new businesses or even whole new industries, thus spurring growth and adding jobs. Corporations are instead hoarding cash on their balance sheets like never before, and some of the capital generated by efficiency innovation is reinvested in even more efficiency innovation.

The picture is also not rosy in the management of mega-scale initiatives initiated by political decisions. Government leaders may be good at communicating and at managing the pure political process, but when it comes to execution and the ultimate value creation for citizens, things easily get out of control. High-profile

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projects such as the German energy transition, *Energiewende,* show deep management flaws that range from governance and strategy to execution.

Everyday projects, which do not typically capture the headlines, are also mismanaged. A recent report by the GAO, for example, found that the U.S. government has 77,000 empty or underutilized buildings across the country, costing taxpayers more than $1.5 billion a year to maintain.[16] Such troubles may be related to the fact that those in the political arena have not yet embraced management skills as a factor for success in their political careers, yet the damage flawed management of such initiatives can cause is huge.

To sum up, the overall track record of managements' effectiveness and leadership is rather mixed, but there are enough bright spots to give us confidence that managers can still provide the foundation on which we will forge the Great Transformation.

A GREAT TRANSFORMATION FOR THE BETTER IS WITHIN OUR REACH

We are at an exceptional moment in history, as the developed world begins to make a series of enormous changes in society—whether for better or for worse remains to be seen. However, it is not preordained; myriad actors will shape the future, some will have more impact than others, but we know one thing for certain: during this Great Transformation, managers will be of pivotal importance.

As Drucker wrote in his 1993 book, *The Ecological Vision,* "Management and managers are the central resource, the generic, distinctive, the constitutive organ of society . . . and the very survival of society is dependent on the performance, the competence, the earnestness and the values of their managers . . . What managers are doing is therefore a public concern."[17] This seems to be the moment to take Drucker's statement seriously, to live up to our responsibility as managers and leaders. To do so will require courageous and decisive action.

The Great Transformation must begin by rebuilding trust and revisiting managers' fundamental commitment to society—namely, innovation and value creation. Of course, done well, over the long term this is also good for a company and its bottom line. Failing to invest in innovation means putting the future of a whole organization at risk, and no company that goes out of business can be a good neighbor, good employer, or a good citizen. At the same time, it must become unacceptable for a CEO to earn 300 times or more than their average employee. Even worse is that failing to keep a business viable creates significant damage, such as human suffering and society's need to address that suffering with social programs—at taxpayers' expense.

From Scalable Efficiency to Scalable Learning

Despite great new management ideas and concepts, the issue of scalability and the broad-based application of innovative management practices are far from resolved. Instead of liberating the creative and innovative energy of employees, as well as of supply-chain partners and others who are part of a corporation's ecosys-

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tem, blind processes and rigid hierarchies still hold them down. In effect, the emergence of Taylorism in non-manufacturing business operations has been enabled by digital technology. However, we can do much better than that.

Authors John Hagel III and John Seely Brown, who are co-chairmen of the Deloitte Center for the Edge, have described a shift toward a massive transformation, from institutions designed for scalable efficiency to institutions designed for scalable learning.[18] This relates not so much to formal, classroom-based learning but to learning from the ongoing experiences, projects, and initiatives that occur continually in various parts of an organization. The key is to foster learning by connecting minds to create value and share knowledge for innovation across the organization. Enterprise social media and traditional means of communication provide a new infrastructure for this type of scalable learning.

Toward a Human-Centric Paradigm

Digital technology is an unprecedented game changer, due to its continuous exponential development. As such, it can lead either further down the efficiency-enhancing and cost-cutting route, or up the innovation path. It can replace brawn with robotics or augment human brains with artificial intelligence.

Many organizations will undoubtedly be tempted to use technology to replace human beings wherever and whenever possible, but this would be a terrible mistake and almost certainly lead to a downward spiral for both society and the economy. The emphasis should instead be on empowering workers so they can leverage new technologies, with the understanding that technology is meant to serve people and enhance their capabilities.

The leader of a prominent gaming company told me that the primary task of management in his organization is to eliminate obstacles and provide tools for his workers so they can improve their access to knowledge and collaborate across their on-site functions, and even beyond the company's walls.

Management as a Liberal Art

For this kind of vision to be realized, humanists must be given equal prominence with the technologists. The grossly reductionist idea that almost any expert can be replaced by an "expert system" does not take into account profound human capabilities like intuition, creativity, and compassion. It is also naïve to assume that knowledge is objective and somehow disconnected from the human condition; in fact, the value of knowledge is largely determined by those producing and applying it. Drucker had this in mind when he called management a liberal art. It is "liberal," he explained, "because it deals with the fundamentals of knowledge, self-knowledge, wisdom and leadership; 'art' because it is practice and application."[19] Managers draw from all the knowledge and insights of the humanities and social sciences—from psychology and philosophy, economics and history, the physical sciences and ethics. But, they have to focus this knowledge on achieving results and being effective. This is something management education institutions should

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seriously consider if they do not want to become ever-more specialized engineering-type schools for management techniques.

A Second Renaissance?

In a time when technologists and technocrats dominate so much of the debate in politics, economics, and education, rediscovering the essence of being human is more important than ever. Indeed, in order to benefit from what MIT's Erik Brynjolfsson and Andrew McAfee have dubbed "the Second Machine Age," we also need a second Renaissance that is powered by the humanities and knowledge across disciplines, as Drucker posited.[20] Otherwise we run the risk of ending up in a technocracy, where technology becomes the new faith and the top technocrats are the new masters who determine the fate of those subject to their technology-driven world. What financial technocrats might do in such a world does not need further comment. The Transhumanists and Kurzweil's Singularity adepts seem to have lost the connection to the roots of human existence and uniqueness. By propagating an ideology pretending that perfect technology leaves the human being behind like a flawed outcome of evolution, it is an outrageous reduction of human condition to technology's capabilities – as advanced as they may be.

When Roger L. Martin, an academic and prolific author, writes in his book *The Design of Business* about the knowledge funnel and shows human progress from mystery to heuristics to algorithms, he does not imply that the world is going algorithmic but, as scientific progress has demonstrated, that each new discovery and each new algorithm opens up new mysteries.[21] The deeper we drill, the more mysteries we seem to unlock.

A TSUNAMI OF INNOVATION AND ENTREPRENEURSHIP

Done right, a new marriage between the human spirit and the most powerful technology humanity has ever developed, which is still in its early stages of deployment, could produce incredible results. Just think about the extensive waste in today's organization in terms of people's ideas, creativity, motivation, and engagement. Releasing just 10 percent of this latent value would mean a jump in innovation and value creation—and, in turn, in the world's prosperity. We need to get closer to what Peter Drucker called an entrepreneurial society in which innovation and entrepreneurship become an integral life-sustaining activity in our organizations, our economy, our society.[22]

With a human-centric approach, serviced by the best technology has to offer and supported by smarter government policies and regulations, our organizations can create new infrastructures that enable knowledge sharing, communication, and collaboration. In essence, we can trigger a tsunami of innovation and value creation.

There are already cases that demonstrate the tremendous potential for achieving massive and deep transformation in a short time. India's Aadhaar project led by former Infosys CEO Nandan Nilekani is one such example. The project aimed

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to provide a fake-proof ID to each of the 1.2 billion people who live in India, 500 million of them below the poverty line. Five years after its inception, 650 million people have enrolled for the unique Aadhaar biometric ID that is authenticated online, and which has the potential to give ID holders access to social benefits, bank services, and the labor market.[23]

The implications are enormous for India and rest of the developing world. It is the classic example of advanced technology serving fundamental human needs. It also shows how the application of sound management practices can bring the two streams together—leading-edge technology and a deep commitment to improving the human condition.

IN TRANSITION TOWARD THE GREAT TRANSFORMATION

The Great Transformation will not happen overnight. However, we are already in a state of transition where sound existing management knowledge can be applied. We find a lot of this in the legacy of the great management thinkers whose ideas are based on a human-centric worldview: Peter Drucker, Warren Bennis, Henry Mintzberg, Charles Handy, and C. K. Prahalad are among them. Based on these foundations, many new concepts and methods are being introduced that fit our time even more precisely.

We don't know what the future will bring, but we can determine the direction in which we want to go. We can take purposeful steps toward the Great Transformation by creating a world that embraces technology but keeps the human being at its core, conscious of our culture, our history, our spirituality, and our unending quest for self-realization.

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