

Producing sustainable competitive advantage through the effective management of people*

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Executive Overview

Achieving competitive success through people involves fundamentally altering how we think about the workforce and the employment relationship. It means achieving success by working with people, not by replacing them or limiting the scope of their activities. It entails seeing the workforce as a source of strategic advantage, not just as a cost to be minimized or avoided. Firms that take this different perspective are often able to successfully outmaneuver and outperform their rivals.

Suppose that in 1972, someone asked you to pick the five companies that would provide the greatest return to stockholders over the next 20 years. And suppose that you had access to books on competitive success that were not even written. How would you approach your assignment? In order to earn tremendous economic returns, the companies you picked should have some sustainable competitive advantage, something that 1) distinguishes them from their competitors, 2) provides positive economic benefits, and 3) is not readily duplicated.

Conventional wisdom then (and even now) would have you begin by selecting the right industries. After all, "not all industries offer equal opportunity for sustained profitability, and the inherent profitability of its industry is one essential ingredient in determining the profitability of a firm."¹ According to Michael Porter's now famous framework, the five fundamental competitive forces that determine the ability of firms in an industry to earn above-normal returns are "the entry of new competitors, the threat of substitutes, the bargaining power of buyers, the bargaining power of suppliers, and the rivalry among existing competitors."² You should find industries with barriers to entry, low supplier and buyer bargaining power,

few ready substitutes, and a limited threat of new entrants to compete away economic returns. Within such industries, other conventional analyses would urge you to select firms with the largest market share, which can realize the cost benefits of economies of scale. In short you would probably look to industries in which patent protection of important product or service technology could be achieved and select the dominant firms in those industries.

You would have been very successful in selecting the five top performing firms from 1972 to 1992 if you took this conventional wisdom and turned it on its head. The top five stocks, and their percentage returns, were (in reverse order): Plenum Publishing (with a return of 15,689%), Circuit City (a video and appliance retailer; 16,410%), Tyson Foods (a poultry producer; 18,118%), Wal-Mart (a discount chain; 19,807%), and Southwest Airlines (21,775%).³ Yet during this period, these industries (retailing, airlines, publishing, and food processing) were characterized by massive competition and horrendous losses, widespread bankruptcy, virtually no barriers to entry (for airlines after 1978), little unique or proprietary technology, and many substitute products or services. And in 1972, none of these firms was (and some still are not) the market-share leader, enjoying economies of scale or moving down the learning curve.

*Adapted from Jeffrey Pfeffer, *Competitive Advantage through People*, Harvard Business School Press, Boston, 1994.

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The point here is not to throw out conventional strategic analysis based on industrial economics but simply to note that the source of competitive advantage has always shifted over time. What these five successful firms tend to have in common is that for their sustained advantage, they rely not on technology, patents, or strategic position, but on how they manage their workforce.

The Importance of the Workforce and How It is Managed

As other sources of competitive success have become less important, what remains as a crucial, differentiating factor is the organization, its employees, and how they work. Consider, for instance, Southwest Airlines, whose stock had the best return from 1972 to 1992. It certainly did not achieve that success from economies of scale. In 1992, Southwest had revenues of \$1.31 billion and a mere 2.6% of the U.S. passenger market.⁴ People Express, by contrast, achieved \$1 billion in revenues after only 3 years of operation, not the almost 20 it took Southwest. Southwest exists not because of regulated or protected markets but in spite of them. "During the first three years of its history, no Southwest planes were flown."⁵ Southwest waged a battle for its very existence with competitors who sought to keep it from flying at all and, failing that, made sure it did not fly out of the newly constructed Dallas-Fort Worth international airport. Instead, it was restricted to operating out of the close-in Love Field, and thus was born its first advertising slogan, "Make Love, Not War." Southwest became the "love" airline out of necessity, not choice.

In 1978, competitors sought to bar flights from Love Field to anywhere outside Texas. The compromise Southwest wrangled permitted it to fly from Love to the four states contiguous to Texas.⁶ Its competitive strategy of short-haul, point-to-point flights to close-in airports (it now flies into Chicago's Midway and Houston's Hobby airports) was more a product of its need to adapt to what it was being permitted to do than a conscious, planned move—although, in retrospect, the strategy has succeeded brilliantly. Nor has Southwest succeeded because it has had more access

to lower-cost capital—indeed, it is one of the least leveraged airlines in the United States. Southwest's planes, Boeing 737s, are obviously available to all its competitors. It isn't a member of any of the big computerized reservation systems; it uses no unique process technology and sells essentially a commodity product—low-cost, low-frills airline service at prices its competitors have difficulty matching.

Much of its cost advantage comes from its very productive, very motivated, and by the way, unionized workforce. Compared to the U.S. airline industry, according to 1991 statistics, Southwest has fewer employees per aircraft (79 versus 131), flies more passengers per employee (2,318 versus 848), and has more available seat miles per employee (1,891,082 versus 1,339,995).⁷ It turns around some 80% of its flights in 15 minutes or less, while other airlines on average need 45 minutes, giving it an enormous productivity advantage in terms of equipment utilization.⁸ It also provides an exceptional level of passenger service. Southwest has won the airlines' so-called triple crown (best on-time performance, fewest lost bags, and fewest passenger complaints—in the same month) *nine* times. No competitor has achieved that even once.⁹

What is important to recognize is why success, such as that achieved at Southwest, can be sustained and cannot readily be imitated by competitors. There are two fundamental reasons. First, the success that comes from managing people effectively is often not as visible or transparent as to its source. We can see a computerized information system, a particular semiconductor, a numerically controlled machine tool. The culture and practices that enable Southwest to achieve its success are less obvious. Even when they are described, as they have been in numerous newspaper articles and even a segment on "60 Minutes," they are difficult to really understand. Culture, how people are managed, and the effects of this on their behavior and skills are sometimes seen as the "soft" side of business, occasionally dismissed. Even when they are not dismissed, it is often hard to comprehend the dynamics of a particular company and how it operates because the way people are managed often fits together in a system. It is easy to copy one thing but much more difficult to copy numerous things. This is because the change needs to be more comprehensive and also because the ability to understand the system of management practices is hindered by its very extensiveness.

Thus, for example, Nordstrom, the department store chain, has enjoyed substantial success both in customer service and in sales and profitability

growth over the years. Nordstrom compensates its employees in part with commissions. Not surprisingly, many of its competitors, after finally acknowledging Nordstrom's success, and the fact that it was attributable to the behavior of its employees, instituted commission systems. By itself, changing the compensation system did not fully capture what Nordstrom had done, nor did it provide many benefits to the competition. Indeed, in some cases, changing the compensation system produced employee grievances and attempts to unionize when the new system was viewed as unfair or arbitrary.

Thirteen Practices for Managing People

Contrary to some academic writing and to popular belief, there is little evidence that effective management practices are 1) particularly faddish (although their implementation may well be), 2) difficult to understand or to comprehend why they work, or 3) necessarily contingent on an organization's particular competitive strategy. There are interrelated practices—I enumerate 13, but the exact number and how they are defined are somewhat arbitrary—that seem to characterize companies that are effective in achieving competitive success through how they manage people.

The following policies and practices emerge from extensive reading of both the popular and academic literature, talking to numerous people in firms in a variety of industries, and the application of some simple common sense. The particular way of subdividing the terrain is less important than considering the entire landscape, so the reader should realize that the division into categories is somewhat arbitrary. The themes, however, recur repeatedly in studies of organizations. It is important to recognize that the practices are interrelated—it is difficult to do one thing by itself with much positive result.

Employment Security

Security of employment signals a long-standing commitment by the organization to its workforce. Norms of reciprocity tend to guarantee that this commitment is repaid. However, conversely, an employer that signals through word and deed that its employees are dispensable is not likely to generate much loyalty, commitment, or willingness to expend extra effort for the organization's benefit. New United Motor Manufacturing (NUMMI), the Toyota-GM joint venture in California, guaranteed workers' jobs as part of the formal labor contract in return for a reduction in the number of job

classifications and an agreement not to strike over work standards. This commitment was met even in the face of temporarily slow demand, and many observers believe that as a result, trust between employees and the organization increased substantially.

Taking on people not readily eliminated exerts pressure to be careful and selective in hiring. Moreover, "employment security enhances employee involvement because employees are more willing to contribute to the work process when they need not fear losing their own or their coworkers' jobs. Employment security contributes to training as both employer and employee have greater incentives to invest in training,"¹⁰ because there is some assurance that the employment relationship will be of sufficient duration to earn a return on the time and resources expended in skill development.

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Selectivity in Recruiting

Security in employment and reliance on the workforce for competitive success mean that one must be careful to choose the right people, in the right way. Studies covering populations ranging from machine operators, typists, and welders to assembly workers—all in self-paced jobs so that individual differences mattered—indicate that the most productive employees were about twice as good as the least productive.¹¹ Southwest Airlines worries a lot about hiring the right people. In fact, it flies some of its best customers to Dallas and involves them in the flight attendant hiring process, believing that those who are in contact with the front-line employees probably know best what makes a good employee. At Lincoln Electric, hiring is done very carefully based on the desire to succeed and the capacity for growth.¹²

One of the practices of many of the Japanese automobile-manufacturing plants opened in the United States that proved especially newsworthy was their extensive screening of employees. Some of this was undoubtedly done to weed out those who were likely to be pro-union, but much of the screening was to find those people who could work best in the new environment, could learn and develop, and needed less supervision. There was little screening for particular skills, under the assumption that these could be readily learned. Nordstrom, the very effective specialty retailer

whose sales per square foot are about double the industry average, tends to recruit sales clerks who are young and college-educated, seeking a career in retailing.¹³

Besides getting the right people in the door, recruiting has an important symbolic aspect. If someone goes through a rigorous selection process, the person feels that he or she is joining an elite organization. High expectations for performance are created, and the message sent is that people matter.

High Wages

If you want to recruit outstanding people, and want them to stay with the organization, paying more is helpful, although not absolutely necessary. High wages tend to attract more applicants, permitting the organization to be more selective in finding people who are going to be trainable and who will be committed to the organization. Perhaps most important, higher wages send a message that the organization values its people. Particularly if these wages are higher than required by the market, employees can perceive the extra income as a gift and work more diligently as a result.¹⁴ Nordstrom typically pays its people an hourly wage higher than the prevailing rate for retail clerks at comparable stores. Coupled with incentive pay for outstanding work, Nordstrom salespeople often earn twice the average retail income.

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Companies sometimes believe that lowering labor costs is essential for competitive success. This is not invariably the case, even in cost-competitive businesses, because in many organizations, labor costs are a small fraction of the total costs. Furthermore, even if labor costs (let alone labor rates) are higher, it may be that enhanced service, skill, and innovation more than compensate by increasing the level of overall profit. For instance, the CEO of Wendy's, facing declining company profitability, decided that the best way to become the customer's restaurant of choice was to become the employer of choice.¹⁵ This entailed improving both benefits and base compensation, instituting a quarterly bonus, and creating an employee stock option plan. The results were dramatic: "Our turnover rate for general managers fell to 20% in 1991

from 39% in 1989, while turnover among co- and assistant managers dropped to 37% from 60%—among the lowest in the business. With a stable—and able—workforce, sales began to pick up as well."¹⁶

Incentive Pay

There has been a tendency to overuse money in an effort to solve myriad organizational problems. People are motivated by more than money—things like recognition, security, and fair treatment matter a great deal. Nevertheless, if people are responsible for enhanced levels of performance and profitability, they will want to share in the benefits. Consider the alternative—if all the gains from extra ingenuity and effort go just to top management or to shareholders (unless these are also employees), people will soon view the situation as unfair, become discouraged, and abandon their efforts. Thus, many organizations seek to reward performance with some form of contingent compensation.

Lincoln Electric is deservedly famous for its piecework and incentive bonus plan. Contrary to first impressions, the plan does much more than merely reward individual productivity. Although the factory workforce is paid on a piecework basis, it is paid only for good pieces—workers correct quality problems on their own time. Moreover, defects can be traced to the individual who produced them. Quality is emphasized as well as productivity. Additionally, piecework is only a part of the employee's compensation. Bonuses, which often constitute 100% of regular salary, are based on the company's profitability—encouraging employees to identify with the whole firm. They are also based on the individual's merit rating, and that rating is, in turn, based on four equally important aspects of performance: dependability, quality, output, and ideas and cooperation.¹⁷ This broader evaluation mitigates the pernicious tendencies of simplistic incentive systems to go awry.

Employee Ownership

Employee ownership offers two advantages. Employees who have ownership interests in the organizations for which they work have less conflict between capital and labor—to some degree they are both capital and labor. Employee ownership, effectively implemented, can align the interests of employees with those of shareholders by making employees shareholders, too. Second, employee ownership puts stock in the hands of people, employees, who are more inclined to take a long-term

view of the organization, its strategy, and its investment policies and less likely to support hostile takeovers, leveraged buyouts, and other financial maneuvers. Of course, to the extent that one believes this reduced risk of capital market discipline inhibits efficiency, significant employee shareholding is a disadvantage. However, the existing evidence largely contradicts this negative view.

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It is probably no coincidence that all five of the companies mentioned as providing the best shareholder returns from 1972 to 1992 appear on The Employee Ownership 1000, a listing of "1000 companies in which employees own more than 4% of the stock of a corporation" traded on the New York or American stock exchanges or the over-the-counter market.¹⁸ Although employee ownership is no panacea, and its effects depend largely on how it is implemented, the existing evidence is consistent with the view that employee ownership has positive effects on firm performance.¹⁹

Information Sharing

If people are to be a source of competitive advantage, clearly they must have the information necessary to do what is required to be successful. At the Advanced Micro Devices submicron development center, there are computer terminals throughout the plant that every employee has been trained to use in order to obtain information about product yields, development progress, production rates, or any other aspect of the operation. One reason sometimes given for not disclosing information to large numbers of employees is that it may leak to competitors. When Robert Beck was head of human resources for the Bank of America, he perceptively told the management committee, reluctant to disclose the bank's strategy and other information to its employees, that the competitors almost certainly knew the information already; typically, the only people in the dark are the firm's own employees.

Participation and Empowerment

Sharing information is a necessary precondition to another important feature found in many success-

ful work systems: encouraging the decentralization of decision making and broader worker participation and empowerment in controlling their own work process. At Nordstrom, the written philosophy states:

We also encourage you to present your own ideas. Your buyers have a great deal of autonomy, and are encouraged to seek out and promote new fashion directions at all times. . . . Nordstrom has a strong open-door policy and we encourage you to share your concerns, suggestions and ideas. . . .

Nordstrom Rules:

Rule #1: Use your good judgment in all situations. There will be no additional rules.²⁰

The evidence is that participation increases both satisfaction and employee productivity.²¹ Autonomy is one of the most important dimensions of jobs and was the focus of many job-redesign efforts undertaken as part of the quality of working life movement in the 1960s and 1970s.²² The fundamental change involves moving from a system of hierarchical control and coordination of activity to one in which lower-level employees, who may have more or better information, are permitted to do things to enhance performance. At a Levi Strauss jeans factory, when it was time to purchase new forklift trucks, the drivers themselves got involved. They determined specifications, negotiated with suppliers, and made the final purchase decision, in the process saving the company money as well as obtaining equipment more appropriate for that plant. At Eaton, a unionized manufacturer, workers tired of fixing equipment that broke down and suggested that they build two new automated machines themselves. They did it for less than a third of what outside vendors would have charged and doubled the output of the department in the first year.²³

Self-Managed Teams

Organizations that have tapped the power of teams have often experienced excellent results. Monsanto, a large chemical company, implemented work organization based on self-managed teams at its chemical and nylon complex near Pensacola, Florida. Teams of workers were responsible for hiring, purchasing, job assignments, and production.²⁴ Management was reduced from seven levels to four, and the plant experienced increases in both profitability and safety. At a 318-person submarine systems plant owned by AT&T,

costs were reduced more than 30% through the use of teams.²⁵ Federal Express uses teams in its back-office operation with great success—service problems fell 13% in 1989 after the company's 1,000 clerical workers were organized in teams and given additional training and authority.²⁶ One of the more dramatic examples of the benefits of using teams occurred at Johnsonville Sausage. In 1986, a manufacturer asked Johnsonville to produce private-label sausage. The president was about to decline the new business, because he believed that the plant was already at capacity and could not handle the additional workload. However,

before deciding, he assembled his 200 production workers, who are organized in teams of five to 20, and asked them to decide. . . . After . . . ten days, they came back with an answer: "We can do it." . . . The teams decided how much new machinery they would need and how many new people; they also made a schedule of how much to produce per day. Since Johnsonville took on the new project, productivity has risen over 50% in the factory.²⁷

Teams work because of the peer monitoring and expectations of coworkers that are brought to bear to both coordinate and monitor work. Indeed, even critics of the team concept often argue that the problem with teams as a substitute for hierarchy is not that this approach doesn't work but that it works too well. Thus, a dissident union leader in the NUMMI plant noted: "[W]hen the team's under pressure, people try to meet the team's expectations and under peer pressure, they end up pushing themselves too hard. . . . The team concept is a nice idea, but when you put the teams under pressure, it becomes a damn effective way to divide workers."²⁸

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Training and Skill Development

An integral part of most new work systems is a greater commitment to training and skill development. Note, however, that this training will produce positive returns only if the trained workers are then permitted to employ their skills. One mistake many organizations make is to upgrade the

skills of both managers and workers but not change the structure for work in ways that permit people to do anything different. Under such circumstances, it is little wonder that training has no apparent effect.

At Advanced Micro Devices' submicron development facility, some 70% of the technicians came from older facilities at AMD. In keeping with AMD's emphasis on employment stability, as old facilities were closed, people were evaluated with respect to their basic skills. If accepted, they were put through a seven-month program at Mission College—at full pay and at company expense—and then went to work in the new facility. This training not only demonstrated the firm's commitment to its employees, which was then reciprocated, but also ensured that the facility would be staffed with highly qualified people who had been specifically trained for their new jobs.

At a Collins and Aikman carpet plant in Georgia, more than a third of the employees were high school dropouts, and some could neither read nor write. When the firm introduced computers to increase productive efficiency, however, it chose not to replace its existing workforce but to upgrade its skills. After spending about \$1,200 per employee on training, including lost job time, the company found that the amount of carpet stitched increased 10%. Moreover, quality problems declined by half. The employees, with more skills and better morale, submitted some 1,230 suggestions, and absenteeism fell by almost half.²⁹

Cross-Utilization and Cross-Training

Having people do multiple jobs has a number of potential benefits. The most obvious is that doing more things can make work more interesting—variety is one of the core job dimensions that affect how people respond to their work. Variety in jobs permits a change in pace, a change in activity, and potentially even a change in the people with whom one comes in contact, and each of these forms of variety can make work life more challenging. Beyond its motivational effects, having people do multiple jobs has other important benefits. One is keeping the work process both transparent and as simple as possible. If people are expected to shift to new tasks readily, the design of those tasks has to be straightforward enough so they can be learned quickly. A second, somewhat related benefit is the potential for newcomers to a job to see things that can be improved that experienced people don't see, simply because they have come to take the work process so much for granted.

Multiskilling is also a useful adjunct to policies

that promise employment security. After all, it is easier to keep people at work if they have multiple skills and can do different things. By the same token, maintaining employment levels sometimes compels organizations to find new tasks for people, often with surprising results. When Mazda, the Japanese automobile manufacturer, suffered a decline in business in the 1980s, rather than laying off factory workers, it put them to work selling cars, which, in Japan, are often sold door to door. At the end of the year, when awards were presented to the best salespeople, the company discovered that the top ten were all former factory workers. They could explain the product effectively, and of course, when business picked up, the fact that factory workers had experience talking to customers yielded useful ideas about product characteristics.

At Lechmere, a retail chain owned by Dayton-Hudson, the company experimented with cross-training and utilization of employees at a new store in Sarasota, Florida. The store offered the workers raises based on the number of jobs they learned to perform, a variant of a pay-for-skill plan. The workforce, composed of 60% full-time employees rather than the 30% typical for the chain, was substantially more productive than in other stores. "Cashiers are encouraged to sell records and tapes. Sporting goods salesmen get tutoring in forklifts. That way Lechmere can quickly adjust to changes in staffing needs simply by redeploying existing workers. The pay incentives, along with the prospect of a more varied and interesting workday, proved valuable lures in recruiting."³⁰

Symbolic Egalitarianism

One important barrier to decentralizing decision making, using self-managed teams, and eliciting employee commitment and cooperation is the symbols that separate people from each other. Consequently, it is not surprising that many of the firms that are known for achieving competitive advantage through people have various forms of symbolic egalitarianism—ways of signaling to both insiders and outsiders that there is comparative equality and it is not the case that some think and others do. At NUMMI, the executive dining room was eliminated, and everyone eats in the same cafeteria. Everyone wears a blue smock. There are no reserved places in the employee parking lot.

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Communication across levels is greatly enhanced by the opportunity to interact and meet in less formal settings. This means that senior management is more likely to know what is actually going on and be able to communicate its ideas more directly to everyone in the facility. The reduction in the number of social categories tends to decrease the salience of various subdivisions in the organization, diminishes "us" versus "them" thinking, and provides more of a sense of everyone working toward a common goal. This egalitarianism makes cross-movement easier because there are fewer status distinctions to be overcome. At NUMMI, there is only one classification for Division 1 personnel compared to more than 80 previously. The number of skilled trades classifications shrank from 18 under the old General Motors systems to 2.³¹

Egalitarian symbols come in many forms. In some organizations, it is dress—few who have worked in a manufacturing facility have not heard the phrase "the suits are coming" when people from headquarters, typically more formally dressed, arrive. Physical space is another way in which common fate can be signaled, or not. The CEO of Solectron, a contract manufacturer that won the Malcolm Baldrige award, does not have a private office, and neither does the chairman. In contrast, John DeLorean's graphic description of the fourteenth-floor headquarters for General Motors is one of hushed, quiet offices reached by a private elevator that was secured—in other words, executives cut off from the rest of the organization.³²

Although symbolic egalitarianism would seem easy to implement, the elimination of status symbols is often one of the most difficult things for a company to do. A friend bemoaned the fact that just as he had reached a managerial level that entitled him to use a private dining room, have preferential parking, and occupy a larger office, his employer embarked on a total quality movement and eliminated all of these perquisites.

Wage Compression

Although issues of wage compression are most often considered in terms of hierarchical compression, and particularly CEO pay relative to that of others, there is a horizontal aspect to wage compression as well. It can have a number of efficiency-enhancing properties for organizations.

It is important to remember that wage compression is distinct from incentive pay. Incentive pay simply means that people are rewarded, either individually or in groups, for their performance.

These rewards can be large, producing wide variation in salaries, or small, producing substantially less variation. It is also important to recognize that incentive pay—particularly when applied to larger units such as work groups, departments, or the entire organization—can either reduce or increase the wage dispersion that would otherwise exist. Most gain-sharing and profit-sharing programs actually reduce pay dispersion, although they need not do so.

When tasks are somewhat interdependent and cooperation is helpful for accomplishing work, pay compression, by reducing interpersonal competition and enhancing cooperation, can lead to efficiency gains.³³ Furthermore, large differences in the allocation of organizational rewards can motivate people to achieve these rewards. Although increased motivation can produce greater efforts, large differences in rewards can as readily result in excessive time and energy spent on ingratiating oneself with one's supervisor or trying to affect the criteria for reward allocation.³⁴ By this reasoning, a more compressed distribution of salaries can actually produce higher overall performance, as there is less incentive for individuals to waste their time on gaming the system.

To the extent that wages are compressed, pay is likely to be deemphasized in the reward system and in the organization's culture. This has some obvious economic benefits—people are not constantly worrying about whether they are compensated appropriately and attempting to rebargain their salaries. A de-emphasis on pay can also focus attention on the other advantages of organizational membership such as good colleagues and work that is interesting and meaningful. There is a literature in psychology that suggests we attempt to figure out why we are doing what we are by looking at ourselves as an outside observer would.³⁵ If we see we are very well paid, perhaps on a contingent basis, for what we do, we are likely to attribute our behavior to the economic rewards. If, however, we are not particularly well paid, or if pay is less salient, and if it is distributed on a less contingent basis (which will make it less salient), then we are likely to attribute our behavior to other, more intrinsic factors such as the inherent enjoyment of the work. In other words, being paid in a contingent fashion for what we do can actually undermine our intrinsic interest in and satisfaction with that activity.³⁶ Thus, pay compression, by helping to de-emphasize pay, can enhance other bases of satisfaction with work and build a culture that is less calculative in nature.

Promotion from Within

Promotion from within is a useful adjunct to many of the practices described. It encourages training and skill development because the availability of promotion opportunities within the firm binds workers to employers and vice versa. It facilitates decentralization, participation, and delegation because it helps promote trust across hierarchical levels; promotion from within means that supervisors are responsible for coordinating the efforts of people whom they probably know quite well. By the same token, those being coordinated personally know managers in higher positions. This contact provides social bases of influence so that formal position can loom less important. Promotion from within also offers an incentive for performing well, and although tied to monetary rewards, promotion is a reward that also has a status-based, nonmonetary component. Perhaps most important, it provides a sense of fairness and justice in the workplace. If people do an outstanding job but outsiders are being brought in over them, there will be a sense of alienation from the organization. One other advantage of promotion from within is that it tends to ensure that people in management positions actually know something about the business, the technology, and the operations they are managing. There are numerous tales of firms managed by those with little understanding of the basic operations, often with miserable results. David Halberstam's history of Ford Motor tells how finance took control of the company. Not only were these people not "car men," they knew little about automobiles, technology, production processes, or the market—anything that could not be conveyed via statistics—and had little interest in learning.³⁷ The problem with managing only through statistics is that without some understanding of the underlying processes that produce the measures, it is likely that managers will either focus on inappropriate measures or fail to fully comprehend what they mean.

By contrast, at Lincoln Electric, almost everyone who joins the company learns to weld—Lincoln's main product is, after all, arc welding equipment. Graduation from the welding program requires coming up with some innovation to the product. At Nordstrom, even those with advanced degrees start on the sales floor. Promotion is strictly from within, and when Nordstrom opens a new store, its key people are recruited from other stores around the country. This helps perpetuate the Nordstrom culture and values but also provides assurance that those running the store know what they are

doing and have experience doing it the Nordstrom way.

Taking the Long View

The bad news about achieving some competitive advantage through the workforce is that it inevitably takes time to accomplish. By contrast, a new piece of equipment can be quickly installed; a new product technology can be acquired through a licensing agreement in the time it takes to negotiate the agreement; and acquiring capital only requires the successful conclusion of negotiations. The good news, however, is that once achieved, competitive advantage obtained through employment practices is likely to be substantially more enduring and more difficult to duplicate. Nevertheless, the time required to implement these practices and start seeing results means that a long-term perspective is needed. It also takes a long time horizon to execute many of these approaches. In the short term, laying off people is probably more profitable compared to trying to maintain employment security; cutting training is a quick way to maintain short-term profits; and cross-training and cross-utilization may provide insights and innovation in time, but initially, the organization foregoes the advantages of more narrow specialization and the immediate proficiency achieved thereby.

What determines an organization's time horizon is an important issue, but one outside the scope of this article. In general, however, there is some evidence that family ownership, employee ownership, or other forms of organization that lessen the immediate pressures for quick earnings to please the securities market are probably helpful. Lincoln Electric is closely held, and the Nordstrom family retains a substantial fraction of the ownership of that retailer. NUMMI has Toyota as one of the joint venture partners, and Toyota's own plans for the facility virtually dictate that it take a long-term view, which is consistent with its culture and tradition. Again, the Walton family's ownership position in Wal-Mart helps ensure that the organization takes a long view of its business processes.

It is almost inconceivable that a firm facing immediate short-term pressure would embark on activities that are apparently necessary to achieve some competitive advantage through people. This provides one explanation for the limited diffusion of these practices. If the organization is doing well, it may feel no need to worry about its competitive position. By the same token, if the organization is in financial distress, the immediate pressures may be too severe to embark on activities that provide

productivity and profit advantages, but only after a longer, and unknown period of time.

Measurement of the Practices

Measurement is a critical component in any management process, and this is true for the process of managing the organization's workforce. Measurement serves several functions. First, it provides feedback as to how well the organization is implementing various policies. For example, many organizations espouse a promotion from within policy but don't fulfill this objective. Often, this is because there is no systematic collection and reporting of information such as what percentage of the positions at given levels have been filled internally. A commitment to a high-wage policy obviously requires information as to where in the relevant labor market the organization's wages fall. A commitment to training is more likely to be fulfilled if data are collected, not only on the total amount spent on training but also on what types of employees have received training and what sorts of training are being delivered.

Second, measurement ensures that what is measured will be noticed. "Out of sight, out of mind" is a principle that applies to organizational goals and practices as well as to people. One of the most consistent findings in the organizational literature is that measures affect behavior.³⁸ Most people will try to succeed on the measures even if there are no direct, immediate consequences. Things that are measured get talked about, and things that are not don't.

It is no accident that companies seriously committed to achieving competitive advantage through people make measurement of their efforts a critical component of the overall process. Thus, for example, at Advanced Micro Devices' submicron development facility, management made how people were managed a priority and measured employee attitudes regularly to see whether they were "achieving the vision." One survey asked questions such as: How many teams are you on in your own department and with members of other departments? How many hours per week do you spend receiving training and training others? The survey also asked the extent to which people agreed or disagreed with statements such as: there is problem solving at all levels in my work group; people in my work group are encouraged to take the initiative; a spirit of teamwork exists in our work group.

It is no accident that companies seriously committed to achieving competitive advantage through people make measurement of their efforts a critical component of the overall process.

In a world in which financial results are measured, a failure to measure human resource policy and practice implementation dooms this to second-class status, oversight, neglect, and potential failure. The feedback from the measurements is essential to refine and further develop implementation ideas as well as to learn how well the practices are actually achieving their intended results.

Overarching Philosophy

Having an overarching philosophy or view of management is essential. It provides a way of connecting the various individual practices into a coherent whole and also enables people in the organization to persist and experiment when things don't work out immediately. Moreover, such a philosophy makes it easier to explain what the organization is doing, justify it, and mobilize support from internal and external constituencies. Most simply put, it is hard to get somewhere if you don't know where you are going. In a similar fashion, practices adopted without a deeper understanding of what they represent and why they are important to the organization may not add up to much, may be unable to survive internal or external problems, and are likely to produce less than stellar results.

Many companies that seek competitive success through their people and practice a number of approaches really began with some underlying principles or else developed them early in the process. Levi Strauss's quality enhancement process began with the understanding that "manufacturing for

quality and speed meant breaking the old paradigms," turning the culture upside down and completely reorienting the parameters of the business.³⁹ The company and its manufacturing senior vice president explicitly articulated the underlying assumptions of the old way of thinking and the new, as illustrated in Table 1.

Some Words of Caution

It would be difficult to find a single company that does all of these things or that does them all equally well. Some successful firms have tended to do a higher percentage, and it is useful to grade one's own company against the overall list. Nevertheless, there are few companies that do everything. Which practice is most critical does depend in part on the company's particular technology and market strategy.

A second important caution is to recognize that it is possible for a company to do all of these things and be unprofitable and unsuccessful, or to do few or none of them and be quite successful. How? These factors are almost certainly related to a company's ability to achieve competitive success through its workforce. But although that may be an important basis of success, and one that is even increasing in importance, it is clearly not the *only* basis of success.

IBM, for instance, has done many of these things and has built a skilled and dedicated workforce. That in and of itself, however, could not overcome a product strategy that overemphasized large, mainframe computers. People Express, now defunct, also built a strong culture, selectively recruited, and used innovative compensation and work organization strategies to build flexibility and productivity in its operations. Indeed, it was one of the lowest-cost providers of airline services. But this cost advantage could not overcome other problems, such as the founder's edifice complex,

Table 1
New versus Old Paradigms at Levi Strauss

Old Paradigm	New Paradigm
Economy of <i>scale</i> as basis for improvement logic	Economy of <i>time</i> as basis for improvement logic
Quality involves trade-offs	Quality is a "religion;" no compromise
Doers are separate from thinkers	Doers must also be thinkers
Assets are things	Assets are people
Profit is the primary business goal	Customer satisfaction is the primary business goal
Hierarchical organization; goal is to please the boss	Problem-solving network organization; goal is to please the internal or external customer
Measure to judge operational results	Measure to help people make operational improvements

Source: Presentation by Peter Thigpen at the Stanford School of Business, February 26, 1991.

which resulted in too-rapid expansion, acquisition of Frontier Airlines and becoming seriously financially overleveraged, and a growth rate that was not sustainable given the firm's fundamental human resource policies. In focusing on managing the workforce, I highlight only one dimension of the several that determine corporate performance.

By the same token, it is possible to be successful, particularly for a while, doing none of these things or even their opposite. Frank Lorenzo took over Continental Airlines and put it into bankruptcy in 1983 to break its union contracts. To say he played hardball with his employees was an understatement. Lorenzo's strategy was founded on financial and negotiating skills, not on his workforce. For a while, these strategies worked—although Continental lost \$161 million in 1983, by 1985 it earned about \$60 million, a very rapid turnaround. Similarly, Carl Icahn at Trans World Airlines made money, for a while, taking strikes and fighting with his workforce, seeking success through financial strategies. Neither airline succeeded in the long run, but in the short run, cutting wages and benefits, cutting employment levels, and managing through fear can produce temporary results.

A third word of caution is that these practices have potential downsides as well as benefits and are not necessarily easy to implement, particularly in a one-at-a-time fashion. One obvious problem is that they all necessarily entail more involvement and responsibility on the part of the workforce. There are many employees who would rather work only with their bodies and check their minds at the door—particularly if that is what they have become accustomed to—and instituting work practices that entail more effort and involvement may force turnover. These practices may be resisted by others in the company as well. The reader is cautioned that implementation issues loom large, regardless of how sensible the practices may be.

Endnotes

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Executive Commentary

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The author points to thirteen practices for managing people, some of which are coincidental with Japanese management practices. These include employment security, employee ownership, cross-utilization and cross-training, training and skill development, wage compression, and promotion from within. The remaining practices are not widely accepted by Japanese companies but should not be considered insignificant. In my opinion, we need to consider two questions when applying Pfeffer's framework to Japanese corporations. First, what are the environmental and cultural factors that have enabled Japanese firms to adopt the six practices I listed above? Second, how are Japanese companies altering their overall human resource practices and why?

Environmental and Cultural Factors

Japanese corporations have, for some time, believed in "growth" and "maximizing market share." Their management strategy has generally focused on imitating and improving the products and services invented in Europe or the United States, often at lower costs. The competitive advantage most significant to them during this period has been their efficiency-oriented technologies and the use of the collective wisdom of a homogeneous and highly-educated work force. The shared mindset of Japanese workers can be attributed to the country's uniformity of race, culture, and national educational system. Organizational cultures shared the sense that decisions could be made and problems resolved with non-verbal or "belly-to-belly" communications even between superiors and subordinates. It is not unusual to find ambiguity in job descriptions, mission statements, definitions of authority and responsibility, and evaluation criteria of personnel in Japanese organizations. The Japanese management style has been one which relies on controlling people through norms based on long-standing

customs. The lines between society, family and work are not rigidly drawn. In fact, they are quite blurred. As a result, the traditional management style has been dependent on linking cultural and work norms and values which has been quite effective in past years of rapid growth and the employment of "me-too" strategies.

New Directions in Human Resource Management

Now Japan and its companies are facing many challenges. Not every company can or will survive if it adheres to the old paradigms of strategy and management. They must think through how they develop and deploy human resources, particularly if there is little opportunity for favorable growth.

The values of the younger generation of workers are also prompting change. Younger workers tend to be reluctant to argue with their superiors in business situations; they prefer to be rewarded now, not at some future point; and they are comfortable switching jobs or companies if they feel their talents are being underutilized.

Leading Japanese firms have come to realize the significance of these changes and are working at altering their human resource systems. Some Japanese companies have been involved with restructuring in recent years. They are trying to improve their competitiveness through business process engineering. In these cases, they inevitably find that such an initiative requires the destruction of the company hierarchy and the downsizing of the organization. They are faced with the challenge of helping managers to cope with the unfamiliar environment and develop their skills as leaders. Unless they are successful in getting managers to change their traditional management style, employing some of the practices described by Pfeffer (information sharing, empowerment, and self-managed teams), they may not succeed. To this end, more companies are considering

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