

McKinsey on Organization Health

BY DAVID CREELMAN

It is always a pleasure when a leading consultancy like McKinsey does research in the HR space because they bring credibility and a fresh perspective. Their recent book, *Beyond Performance: How great organizations build ultimate competitive advantage* by Scott Keller and Colin Price outlines their take on organizational health—what it is, how to measure it and how to improve it.

This work is of importance to the HR profession because:

- It's one of the biggest studies ever done and conclusively demonstrates the connection between people management practices and business results.
- They come at it from a business perspective, not an HR perspective. Their conclusions are not so different from what HR has been saying, but they bring new clarity.
- They are focused on helping managers take action, not just doing a diagnostic.
- McKinsey has credibility at the CEO and Board level

I spoke to Scott Keller about the book.

Creelman: What led you to this concept of “organizational health”?

Keller: When you look at their performance over time, most organizations seem to be wired for mediocrity. It's a big problem—and not just for leaders, but for society too. We set out to find an approach that would enable organizations to reliably achieve high performance and sustain that.

We started with the notion that we needed to measure how well an organization aligns itself, how well it executes what it is trying to do, and how well it is able to renew itself over time. We built and refined our measurement tool over 10 years; we call it the organizational health index (OHI).

We focused not only on measuring alignment, execution and renewal but also on identifying the management practices that drive those three areas. We ended up with 37 different practices (such as knowledge sharing) that are very tangible in terms of how you run the business day-to-day. We are able to say these are the management practices, scientifically speaking, that are correlated with high performance.

Creelman: I think it is self-evident there is reciprocal causality: good management practices lead to good results and at the same time good results make it easier to implement good practices. Still, everyone is going to ask “Is it causality or just correlation?” Tell me what you found.

Keller: I would say that we have the strongest argument in the history of the field that these practices do cause improved performance. I'd hesitate to say we proved it beyond doubt, but the results are convincing. We looked at 19 different business outcomes, such as enterprise to book value, market growth and sales.



We worked with over 100 clients actually using the measurement tool, and had the luxury of doing this over roughly 10 years to see the extent to which it was working. We concluded organizational health truly is a leading indicator.

A fascinating example occurred in 2005 when our research team looked at Toyota's health data and concluded that in five years or so Toyota would have some real quality issues. That was preposterous at the time. But our researchers had looked into how Toyota was building their capabilities and saw that the way they were ramping up the number of senior engineers who could monitor suppliers was divorced from what you would have expected for sustainable growth. Sure enough, five years later we saw the quality issues surface. That is just an anecdotal example of how health is a leading indicator.

Creelman: The OHI is based for the main part on what we in HR would call an employee opinion survey. How is the OHI different from the employee surveys that we are familiar with?

Keller: Yes, it is an opinion survey; it asks about those 37 management practices and to what extent they are used. It also asks about outcomes of such things: do the practices give clarity and direction, and do they help you innovate.

Opinion surveys are a very helpful tool and we have done the analytics to determine how closely perceptions match reality. As an example, if you ask someone if performance is rewarded you are going to get different people filling out different opinions on a survey. Then as a test you can actually go into the HR systems and see how much people get paid versus their performance rating and whether there is a big distribution or not. There are a number of those types of analytics that can be done with respect to innovation, performance management and so on. When we have done those analytics we found that because the questions are about the management practices employees experience day to day, the opinions tend to be a good read. We are at the point where we can suggest at minimum a company should do the OHI to get a look at their organizational health: the tool is designed so we know with a reasonable degree of certainty that it is going to give you at least an 80-20 read on what your real health is.

However the survey is not the totality of how you assess health and depending on their situation clients may want to have the full diagnostic.

Creelman: How do senior teams react to results of an OHI study?

Keller: Usually there is a combination of relief and alarm. The relief comes from the fact we finally have a language that allows us to talk about these issues in a concrete way and can speak about it through data. The alarm side of it is that now we as leaders do need to do something about it. We can no longer talk about it behind closed doors. The time has come that we have a choice to make. Are we going to go forward into something which we have not done before? Will we be able to pull this off?

That is where our recommendations on what management practices improve results is appreciated. The feedback we get from clients is that it's guidance on the practical steps that is the most helpful part of the equation.

Creelman: Do you get any push back from managers on this approach?



Keller: Every organization is different, but by and large we have received less pushback towards the OHI than with any other HR tool used in organizational life. Part of the reason is that managers know it is based on one of the biggest research projects in the history of organizational effectiveness: 600,000 people have been involved, 500 organizations, 900 academic articles and books were reviewed in depth and more than 100 companies involved with what is much like a clinical trial of the approach. That helps inoculate some of the harder nosed people who would say “Oh no, here comes the soft stuff.” They know we have put the whole weight on McKinsey’s R&D capabilities behind the OHI and as a result it feels aligned with business manager’s needs.

Beyond Performance is available at:

<http://www.amazon.com/Beyond-Performance-Organizations-Competitive-Advantage/dp/1118024621>

David Creelman writes and speaks on human capital management (www.creelmanresearch.com)