How Productivity Killed American Enterprise

by Henry Mintzberg

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Looking back on the great depression that began in 2008, economists have their ready explanations. The American trade imbalance had been disastrous for years; the Bush administration was piling up massive budget deficits; Americans were not saving—indeed many were re-mortgaging their homes to maintain spending—while investors from abroad, particularly the government of China, were being relied upon to cover the shortfalls. It couldn't last, the economists agreed in retrospect, and in 2008 the tipping point was reached.

One thing, however, continues to puzzle these economists. The American economy looked so good back then: corporate profits were robust, and American business seemed amazingly efficient. "Productivity rises in the U.S.," ran a headline in the *International Herald Tribune* in December of 2005, with the subhead, "Labor costs decrease as output increases." It sounded so encouraging. How could this have happened?

Productivity Gains as Losses The answer lies beneath the statistics of those macroeconomists, indeed beneath the theories of the microeconomists, who have always seen the corporation as an individual, whether the founding entrepreneur or some subsequent chief executive who maximized “Shareholder Value.” Underneath its chiefs, beyond its productivity, much of American business was rotting from within. Productivity was destroying not only America’s great enterprises, but also its legendary enterprise.

Many of these productivity gains were in fact productivity losses. To understand this, imagine yourself as the head of a large American corporation back in 2008 who wishes to make the quickest possible bundle of cash for your company, not to mention yourself, while contributing to those productivity figures. What’s the best strategy?

Fire everybody and ship from stock. Working hours disappear while sales continue, indeed can increase, since you have every incentive to cut prices in order to clear out that stock. Hence productivity soars while you are cashing in—until, of course, the company runs out of stock. This, almost literally, is what was happening in American business. In 2008, it ran out of stock.

Shareholder Value in those strange times had nothing to do with the value of a company, let alone with any human value. It was a euphemism for driving up the price of a company’s shares as quickly as possible. That had become a virtual craze in the 2000 decade, with market analysts exerting enormous pressure on chief executives to keep pumping up their stock market stock. While it may be difficult to believe now, in those days publicly-traded companies were expected to report performance every three months, as if anyone could discern the change in the fortune of a large enterprise from October to December. A ridiculous idea indeed. It did, however, do its job, namely keep the senior management firmly focused on measurable performance, instead of on products and services and customers—in other words, on results today, not sustenance tomorrow.

Leadership as Heroic But how were the employees of these companies to focus their undivided attention on maximizing Shareholder Value when most of them had never even met the shareholders, many of whom were day traders who bought the stock in the morning and sold it in the afternoon? What incentive did the employees have to serve such people, especially when Shareholder Value expressly dismissed any claim they themselves might have had on the results of their labor?

Consistent with the economic view of the corporation mentioned earlier, the answer was (a) to hold one person, the chief executive officer, responsible for the performance of the entire company, (b) to motivate that person through stock options and the like, and (c) to provide him or her with virtual carte blanche to act at will—and quickly. Of course, there was no letup in the rhetoric about building company cultures for the long run and encouraging the teamwork of knowledge workers, etc. But the reality was exactly the opposite: companies centralized power around their chief executives to an extent that had not been seen for decades.

Never mind the terrible injustice this did to a corporation's ability to function as a cooperative entity. Never mind that a new CEO with barely any knowledge of the company, the culture, and the customers could ride in on a great white horse and play havoc with everything the company had built for years. The financial markets had to be served, and that meant ushering in the age of heroic leadership, so that one person could relentlessly drive everyone else to raise short-term measurable performance, no matter how.

Legal Corruption But how exactly? How did these heroic leaders manage to push up those share prices so quickly? Some, as we know, simply cheated, cooking the books to make things look good. But this was the tip of the iceberg, the illegal corruption that, once revealed, could be dealt with in courts of law. Far more pervasive, and insidious, was the legal corruption underneath, which amounted to cashing in the "goodwill" that many corporations had nurtured so carefully over so many years.

Accountants had trouble measuring that, so it did not count. But they could certainly measure short-term profits, much as the economists could measure productivity. So the CEOs managed this narrow kind of performance very carefully, often more carefully than they managed the business itself. The object was to con the financial analysts, or at least those people convinced by these analysts to buy the stock. So all kinds of employees were distracted making useless plans to impress outside investors. One person I knew laughed about the great debates over obscure PowerPoints for plans that everyone in his company knew would never be executed.

Other popular strategies included trashing the brand (little Mercedes, as Daimler's quality diminished) and exploiting the customers (squeeze what the company could get immediately, forgetting about repeat business), always, of course, in the name of product "quality" and customer "service."

So-called "mergers" (namely takeovers) were also popular: do the deal and dump the consequences of making it work on everyone else. The trick was to become bigger than your competitors, not better. Better took time, and effort. Indeed, by getting rid of some of these competitors altogether, you didn't have to work so hard at becoming better. Sure most of those mergers failed, often miserably. But by that time most of the CEOs were gone, in the meantime having basked in the publicity.

Most popular of all—and closest to shipping from stock—was the so-called "downsizing," a euphemism for firing operating workers and middle managers left and right. At the drop of a share price, even as the company remained profitable, out the door went all kinds of people—bones thrown to distract the hungry dogs of the financial establishment.

Human Resources in place of Human Beings Unfortunately, however, these bones—or to use the actual, but no less demeaning, vocabulary of the time, "human resources"--belonged to flesh and blood human beings. Resources are things; they don't mind being dispensed with. Human beings are people; they do. Moreover, in their heads, on their way out the door, these human beings carried the data banks of their organizations. Sure there was useful information in the computers—explicit information. But far more important was the tacit information contained in the heads of the experienced people, and no corporation had a program to download that.

These people also carried out the hearts and souls of their enterprises. For it was not this "heroic" leadership that built America into a great economic powerhouse, but the committed efforts of all kinds of trusted workers, engineers, and middle managers, as well as senior executives who cared deeply about products, services, and customers.

By 2008, such people were increasingly difficult to find in the publicly traded companies, even among those "human resources" left behind, waiting their turn to be downsized.

And that turn often came. For no sooner did the initial firings put a company into trouble, than the howls went up to do something more dramatic, namely fire more people—that is, throw more oil on the burning enterprise.

Macro-Managing by Deeming It was as if a dark cloud had descended over corporate America, separating those involved with what companies really did—designing, producing, selling—from those who controlled them, and were not so involved. Instead they announced their grand strategies and negotiated their great mergers from on high, followed by the pronouncement of performance standards for everyone else to attain. Up there, it was "management by deeming." How interesting that "micro-managing" was being so roundly condemned at the very same time that "macro-managing"--people in positions of authority who did not know what was going on—was destroying American enterprise.

Thus we had, in the run-up up to 2008, the Enrons, the AOL-Time Warners, and the AT&Ts. Then came BP: while spending fortunes extolling its environmental credentials publicly, privately the company was cutting costs with consequential disasters in Texas (a refinery fire that killed 15 people) and in Alaska (a major pipeline leak). At Hewlett Packard, a new chief executive arrived with the announcement that she had her strategy all worked out—before she had spent a single day in the company, let alone the industry. Such was the level of hubris that had taken over corporate America. Never before had there been so much hype about leadership, and never before had there been less evidence of it.

This chief executive, by the way, like many others, saw herself as a great gambler. Some gamblers these were: they played with other people's money; they cashed in whether they won—with stock options—or lost—with their golden parachutes (for "taking risks," they claimed!). And sometimes they collected just for drawing cards, as when bonuses were paid for completing a merger, before its consequences could even be known. Crazy years indeed!

Productivity on the Backs of Workers and Managers Returning to that "downsizing," how was it that so many people in so many companies could suddenly have become redundant? Had these companies previously been so bloated? Or did their new chief executives have startlingly fresh insights into how to make a company more efficient?

Given that some of these companies were performing just fine before the downsizings, the more likely explanation is that these new chief executives simply discovered the benefits of shipping from stock. That was certainly easier than improving the real value of a company. Why bother to focus on service, quality, even—dare it be said?—their own failures to manage? That takes work. Instead, they shifted the bottom line to the top, deemed profits, and then managed costs, largely by firing people

Not everyone, of course, could be fired—some people had to stay and move that stock out the door. So more of this "efficiency" was ushered in as the chief executives dumped their failures to improve real performance on the backs of the workers and middle managers left behind, who had to work that much harder. And this in turn led to a great deal of "burning out"—which became the catchphrase of the time—accompanied by a significant rise in angst among so many people in corporate America. A great fuss was being make about "hyper-competition" and "turbulent environments," etc., but much of this was a smokescreen to hide the confusion of senior managements. Competently-run companies, with interesting strategies and engaged workers--fewer and fewer among the publicly-traded, it should be noted--simply got on with their business.

This extra workload might have been a fair deal if these people were compensated for their efforts. But they were not. In his *New York Times* column of December 5, 2005, economist Paul Krugman discussed "a remarkable disconnect between overall economic growth and the economic fortunes of most American families." Real medium household income "fell for the fifth year in a row," while the number of "Americans without health insurance continued to rise," despite "spectacular" growth in corporate profits since 2001. Not since the great trusts of the late nineteenth century had those in control of large American companies so ripped off the rest of society. Sure employment rates were high, as measured by the economists of the time. But what kind of employment was that?

And where were the unions, which had so painstakingly developed their role as protectors of American labor? By the year 2000, they had been emasculated, thanks to the actions of the Reagan administration in the 1980s and later to the collapse of communism, which made every collective effort seem suspect and every form of individualism seem grand (including, curiously enough, "free enterprises"--collective entities masquerading as individuals, “persons” in the eyes of the law: the corporations had become persons while the persons had become resources!).

Stories beyond the Statistics In the column mentioned above, Krugman labeled as a “mystery” the “joylessness of the economic expansion for most Americans.” Had he been an anthropologist instead of an economist, more attuned to the inner workings of corporate cultures than the outer statistics they generated, he might not have been mystified at all.

I’m not an anthropologist, but in those years, I spoke with many people in large American corporations—in all parts of large American corporations. And I was getting the same story, time and time again. “Henry, you can’t believe what is happening here,” said an editor in a publishing house with which I dealt. “I took a year off; I couldn’t take it any more,” claimed an ex-student of mine who had attained senior positions in the telecommunication industry. “It’s a joke around here,” a middle manager in a high technology company told me. “All they care about is the merger. No one in senior management gives a damn about the customers.” A senior sales manager I met on an airplane said he was having trouble selling his American machinery abroad because the quality and service had so deteriorated.

The Lean and Mean Icon None of these stories showed up in the statistics of the economists. But anyone could have known—anyone, for instance, who read about Wal-Mart becoming the icon of American business at the time. It inherited this mantle from, to go way back, companies like DuPont and Ford (in their earliest years), later Hewlett

Packard, IBM, and 3M, in more recent years, Intel and General Electric. All had been renowned for their innovative capabilities; all had been significantly responsible for creating the American economic powerhouse. And then came Wal-Mart, famous for what, besides greeting retail customers with a smile: low-wages, union busting, scrimping on health insurance. The business icon of the day! “Lean and mean”—with a vengeance. What does this so admired phrase tell us about the times?

On the other side of the same coin, an OECD report in 2005 noted a “significant decline” in the intensity of American research and development. America built its economy on its capacity to innovate—to explore. American engineers had been admired throughout the world. By 2008, when the MBAs and financial types and lawyers had taken control of corporate America, so much of that exploration had metamorphosed into exploitation.

The Desperate Efforts to Sell “Shareholder Value” Corporations are social institutions--communities. They function best when committed human beings work in cooperative relationships, under conditions of respect and trust. Destroy this and the whole institution of business collapses.

Unless, of course, your competitors are doing no better than you. Accordingly, in those years American politicians, economists, and business people embarked on a desperate campaign to promote this notion of Shareholder Value around the world. They called it “globalization,” but it was just an effort to sell a model of managing that was failing in the United States. Exporting misery you might say—letting others share in that “joylessness” Krugman wrote about.

Some companies in other countries got drawn in—with no small number of them eventually collapsing. But there was also much resistance, particularly in countries with strong business traditions of their own, such as Japan, Germany, and France (whose resistance earned the particular invective of the American media—it might have been a sane place to live, but it was just not “productive”).

Japan, with its relatively egalitarian corporate cultures and long-term perspectives, was especially noteworthy. The Japanese style of management was all the rage in the America of the 1980s. But that waned as Shareholder Value took hold, while problems arose in the Japanese economy. Look at how efficient we have become, extolled the American business pundits as they disparaged the Japanese style of managing. But was that the problem in Japan, or might it have been other economic factors, including the banking system? The answer was evident in what continued to be the Japanese icon, and what a different icon it was, this epitome of the Japanese style of managing: Toyota was soaring, while General Motors was sinking.

Other Possibilities Back Then? Could all of this have been stopped before the fall? There were certainly steps that could have been taken before 2008. Getting the financial analysts off the backs of the corporations, for example. It was almost as if companies were being managed from the offices of such people, who insisted on major changes with barely any knowledge of what really went on in these massive enterprises, let alone caring about their long-term future. More companies could have come off the stock exchanges, or never have gone on to them in the first place. There were other, more patient and sensible ways to finance enterprises.

Companies could also have taken "corporate governance" seriously. Instead of rearranging the deck chairs in the boardrooms, they could have opened these places up to the people who cared most deeply about the sustained strength of the enterprise, because they had the most at stake, namely the employees.

Above all, there could have been moves to keep the mercenaries out of the executive suites. A simple test would have worked: anyone who demanded a massive personal compensation package that set him or her apart from everyone else, including protections available to no-one else, should have been dismissed as having no claim on the word "leadership." How many of the CEOs of the publicly-traded enterprises of 2008—those "leaders"-- would have passed that test?

What Now? But none of this happened. Not by 2008, when the unholy coalition of financial greed and economic dogma had gained such a stranglehold on America. Chief executives would have had to be selected differently, and remunerated differently, to reflect the fact that teamwork and long-term corporate health really did matter, and that human beings really were the corporations' "greatest assets." Most importantly, there would have had to be some real corporate leadership—concerned, engaged, modest--alongside equal attention to corporate "community-ship."

What, then, might be done now? For starters, question everything that has brought the American economy to its knees: naïve economists and superficial analysts; Shareholder Value that undermines enterprise value as well as human values; "governance" as an excuse for status quo centralization; "leadership" that amounts to hubris; the enterprise viewed as a collection of disconnected "agents" instead of a community of engaged members; and an obsession with measurement that inevitably puts quantity ahead of quality.

Even in those strange days of 2008, we had what could have been models of good business sense: a publishing house in San Francisco that sold its stock to its authors, who knew the place and cared about its real values (Berrett-Koehler); companies whose founders or founding families sustained a spirit of solid performance (Costco, IKEA, BMW); large business cooperatives with engaged worker ownership (Mondragon in the Spanish Basque region); countries where capitalism took other forms (Japan); even one prominent U.S.-headquartered multinational whose chief executive was elected in a closed ballot by its senior managers (McKinsey & Company—did it recommend this to any of its clients?).

Not until we appreciate how companies work as communities to attain greatness, and how societies combine social needs with economic ones to attain balance, will we begin to climb out of the abyss into which we have fallen.

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