McKinsey on **Organization**

An in-depth look at the challenges facing senior managers | Published by *The McKinsey Quarterly* | July 2005

Studio/Lab, Chicago

Leading change:
An interview with the CEO of P&G

Alan G. Lafley discusses how to stretch a company's aspirations without overpromising. Second in a series of interviews with leading executives on change management.

Article at a glance

In this interview, Alan G. Lafley, CEO and longtime insider, recounts how he orchestrated recent change at P&G.

Lafley describes his role helping managers to make strategic choices by challenging their deeply held assumptions. Aspirations, he insists, should involve stretching but still be achieveable.

One danger during a turnaround is that managers and employees can become so overwhelmed by the breadth of change that the organization freezes. Reaffirming the positives can help.

While many companies assume that outsiders are needed to shake things up, Lafley argues his 25 years in operations give him a depth of understanding that allows for 'more intelligent' risk taking.

Leading change: An interview with the CEO of P&G

Rajat Gupta and Jim Wendler

Outrageously high targets for revenues, earnings, and market share; a bold vision based on a striking new business model or groundbreaking technology; major strategic moves, such as acquisitions or partnerships, that change the game in an industry; a new CEO, freshly arrived from the outside and committed to shaking things up. Such shocks to the corporate system are widely assumed to be necessary for transforming a company's performance.

Yet Alan G. Lafley's first five years as CEO of P&G show that none of these things is strictly necessary for achieving this sort of change. A large global company that has stumbled and lost some of its confidence can be led to new levels of performance through a more subtle form of leadership exercised by a long-term insider. Lafley's experience sheds particular light on two of the biggest challenges facing CEOs in this situation: the pace of change and the need for 'stretch' aspirations.

Lafley recalls vividly the market's initial disappointment when he took the helm, in June 2000. "I remember being in the basement of the television studio here in Cincinnati at 6 PM on the day [my appointment] was announced. I was the deer in the headlights, being grilled about the company and about why it was doing so badly. And the stock price had gone down a few bucks that day because I was a total unknown." The appointment of a prominent outsider, such as Robert Nardelli of Home Depot or James McNerney of 3M, might have pushed up the company's shares because the market assumed that an insider wouldn't drive the level of change required. Under his predecessor, the hard-driving insider Durk Jager, the company had issued three profit warnings in four months. On one momentous day, its shares fell by a full 30 percent. No wonder investors thought a more dramatic gesture was needed.

Five years later, the markets are looking at Lafley and P&G very differently. From fiscal years 2000 to 2004, the giant company's profits jumped by almost 70 percent, to $9.8 billion, and revenues increased by almost 30 percent, to $51 billion. Investors have embraced P&G's future thanks to new products ranging from Swiffer (a sweeper offering for hard floor surfaces) to Actonel (a prescription medication for osteoporosis), as well as innovations in a wide range of established brands. Lafley's announcement of the $54 billion acquisition of Gillette, in January 2005—by far the largest in P&G's history—has been well received by investors and analysts, who are generally skeptical about major deals.

Executing with excellence

The full story of P&G's turnaround is packed with complex, interlocking decisions about brands, personnel, technology, markets, facilities, and much else. One of the strongest patterns is Lafley's approach to raising aspirations: he agrees with Lou Gerstner that strategic visions can be a distraction, so he has never offered one. Lafley also seconds Lawrence Bossidy's belief that companies should aim to achieve great execution but insists that the real challenge is to "unpack" this idea. "Bossidy's right—in the end, it's about executing with excellence. But you can exhort all you want about excellent execution; you're not going to get it unless you have disciplined strategic choices, a structure that supports the strategy, systems that enable large organizations to work and execute together, a winning culture, and leadership that's inspirational. If you have all that, you'll get excellent execution."

Lafley emphasizes the key difference between a true transformation and incremental business building by describing the role he played during his first 15 years with the company: "That wasn't transformation. No, the game then was: take another half a share point and another half a margin point, build to a 50 percent market share, and take 85 percent of the profits and returns that are outsized in that industry. It was very much like classical military strategy, where you just keep putting on pressure, you just keep extending the lines, you just keep rolling up the weakest competitors, and so on."

Over time, however, the desire to compete in this way can erode into complacency, which Lafley has consciously tried to avoid. "You can get used to being a player without being a winner. There's a big difference between the two. So I became interested in transforming players into winners." Once a company's culture has changed so much that being a mere player is acceptable, Lafley argues, the culture must be transformed. At that stage, just trying to improve the numbers isn't enough. Deeper change is required.

Sometimes the need for a change is obvious from a company's competitive position. Lafley recalls his years heading P&G's Asian operations: "We were the last into Asia. We were a small player there in comparison with Unilever, which had been there at the time of the Raj, and Nestlé, which had been there since 1900." In such an environment, P&G had to transform its performance just to become a serious player. But in other parts of the company—such as beauty care, which Lafley ran during the year before he became CEO—P&G's performance, though lagging, was still thought to be respectable. Lafley set out to change that view.

Achievable aspirations

Lafley argues that although aspirations should stretch a company, it is counter-productive to overpromise. "As a new CEO, I took P&G company goals down to 4 to 6 percent top-line growth, which still required us to innovate to the tune of one to two points of new sales growth a year," as well as some market share growth and, on average, a point of growth from acquisitions. "And then I committed to stretching but achievable double-digit earnings-per-share growth." The share price went down again "because the first thing I did was to set lower, more realistic goals."

Nonetheless, these were indeed stretch goals, Lafley believes, because he had still publicly committed the company to growing faster than it had in recent years and faster than the industry as well. Moreover, he and his leadership team set internal goals higher than those announced externally.

Lafley reined in the company's aspirations in a second, more subtle way: he defined what he calls "the core"—core markets, categories, brands,

Alan G. Lafley

Vital statistics
- Born on June 13, 1947, in Keene, New Hampshire

Education
- Graduated in 1969 with BA in history from Hamilton College
- Graduated in 1977 with MBA from Harvard Business School

Career highlights
- P&G (1977–present)
  - Chairman of the board, president, and chief executive (2002–present)
  - President and chief executive (2000–02)
  - President, global beauty care and North American market development (1999–2000)
  - Executive vice president, P&G; president, P&G North America (1998–99)
  - Executive vice president, P&G; president, P&G Asia (1995–98)
  - Group vice president, P&G; president, P&G Far East (1994–95)
  - Group vice president, P&G; president, laundry and cleaning products, P&G USA (1992–94)

Fast facts
- Served in the US Navy (1970–75)
- Serves on board of directors of numerous institutions and companies, including GE, United Negro College Fund, Hamilton College, Business Council, Business Roundtable
- Served on board of directors of GM
- Member of Harvard Club of Cincinnati

technologies, and capabilities—and focused his near-term efforts entirely on that. P&G's markets and operations, he determined, were too vast and diverse to be turned around all at once. This decision meant, among other things, that only a fraction of the more than 100 countries where P&G operates would receive significant attention initially. "So we called out ten priority countries, and people said, 'Oh, I'm not on the list.' I just told them, 'Just keep doing a good job where you are.'"

While management literature has emphasized the necessity of defining the core, Lafley underscores the importance of actually communicating the definition clearly. Indeed, he says that the need to communicate at a Sesame Street level of simplicity was one of his most important discoveries as CEO:

"So if I'd stopped at 'We're going to refocus on the company's core businesses,' that wouldn't have been good enough. The core businesses are one, two, three, four. Fabric care, baby care, feminine care, and hair care. And then you get questions: 'Well, I'm in home care. Is that a core business?' 'No.' 'What does it have to do to become a core business?' 'It has to be global leader in its industry. It has to have the best structural economics in its industry. It has to be able to grow consistently at a certain rate. It has to be able to deliver a certain cash flow return on investment.' So then business leaders understand what it takes to become a core business."

Why is such excruciating repetition and clarity required? After all, as Lafley proudly notes, P&G attracts the best and brightest from the world's finest universities. One obvious reason is the sheer scale and diversity of the workforce. The company's 100,000 people come from more than 100 cultures, and for many of them English is a second language.

Another reason is the need to unclutter the thinking of employees so they can focus on the critical business of problem solving that Lafley can't do for them. "They have so many things going on in the operation of their daily businesses that they don't always take the time to stop, think, and internalize. They have to figure out what it all really means because I cannot call out the strategy for a business. I want them to use the same basic model and the same discipline to make the right choices for, say, the Philippines," where P&G has a half-billion-dollar business—a sizable operation but only 1 percent of the whole. "I want the manager there to think very consciously about what kind of culture is going to be a winner, what kind of capabilities are needed, and so on."

Coaching and coaxing

So Lafley insists that he can't babysit the businesses: to a large degree they must define their own future, while he plays the role of coach. But coaching at P&G doesn't mean coddling. On the contrary, Lafley demands that his managers take on the responsibility of making tough strategic choices. "Most human beings and most companies don't like to make choices. And they particularly don't like to make a few choices that they really have to live with. They argue, 'It's much better to have lots of options, right?'"

Those extraneous options have a way of reappearing on the table after they have been dismissed. Lafley therefore insists on a "not-do list" as an end product of the strategy process. "For example, when we chose our corporate-innovation programs, we cleared the deck of a lot of other stuff that we were then doing. So we'd have a list of all the things that we're not going to do. And if we caught people doing stuff that we said we were not going to do, we would pull the budget and the people and get them refocused on what we said we were going to do."

To help managers make these strategic choices, leaders must sometimes challenge deeply held assumptions. Lafley recalls a first meeting with his cosmetics managers in Japan after he took over Asian operations. He was known around the company for his work with the Tide brand, "so this guy said, 'You know, this is nothing like laundry detergent,' and smiled." Lafley spent much of the next month talking with consumers at sales counters and in their homes and then reported back to his team, "Do you know what I've learned after 30 days? Cosmetics is everything like laundry detergent! You need to know who your consumers are—intimately. You need to understand not just their habits and practices but their needs and wants, including those they can't articulate. Then you've got to delight them with your brands and your products." Lafley was determined not to allow the mystique of cosmetics to prevent the team from adopting classic P&G practices that had built the company and were fully applicable. A significant result of this process was the decision to promote the SK-II skin care line, which became one of the company's most successful in recent years.

Act as a role model

Being a role model is of course especially important when a CEO makes tough demands on managers. P&G's managers expect Lafley not only to make the same kinds of strategic choices he requires of them but also to act consistently on those choices. Lafley therefore recognizes that he must be ready for moments of truth that can alert the organization to his own deep commitment to P&G's aspirations.

Such moments came early in Lafley's tenure. He had to decide whether to go ahead with strong marketing support for the launch of several new brands (Actonel and Torengos in the United States, and Iams in Europe). "Profit pressure was severe. We had just missed earnings two quarters in a row, and the new brands would need strong, sustained support because they were going up against market-leading competitors. But innovation is P&G's lifeblood, and the businesses believed in their products—all of which tested better than those of competitors— and in their brands. So we locked arms and we went ahead. When I look back now on those early weeks, it's clear that I had to make choices like these to convince P&G managers we were going to go for winning."

One of the classic problems facing any CEO during a turnaround is the possibility that managers and employees become so overwhelmed by the breadth of the changes facing them that they can't achieve any change at all. The organization freezes, as though in shock. Lafley, after all, had taken over a 163-year-old company that was accustomed to leadership in most of its markets and had been famous for its cultural pride and self-confidence. "Then all of a sudden," he notes, "all that had been shattered." Although this slump wasn't P&G's worst in living memory—that came in 1984–85, when the company's earnings dipped below those of the previous 12 months for the first time in many years—it was perceived by outsiders as the worst. "Because of the role of the press, it was a more public failure."

Yet Lafley realized that P&G, though struggling, was in better shape than press reports suggested. In particular, he recognized that the company's culture, far from being a hindrance, was an asset that could be leveraged in a transformation. So he reversed his predecessor's sharp critique of the culture and affirmed its competitive value in discussions with managers and employees across the company.

"I started with P&G values and said, 'Here's what's not going to change. This is our purpose: to improve the everyday lives of people around the world with P&G brands and products that deliver better performance, quality, and value. That's not going to change. The value system—integrity, trust, ownership, leadership, and a passion for service and winning: not going to change. The six guiding principles, respect for the individual, and so on: not going to change. OK, so here's the stuff that will change. Any business that doesn't have a strategy is going to develop one; any business that has a strategy that's not winning in the marketplace is either going to change its strategy or improve its execution.' And so on. So I was very clear about what was safe and what wasn't."

This reassurance, like the intensive coaching about strategic choice and its consequences, was certainly a positive factor. Both helped the company raise its sights again.

Keep innovating

Ultimately, aspirations are energizing only when they are grounded in new ideas that can help a company win in the marketplace. Successful transformations always have a strong content dimension—particularly, of course, at companies like P&G, where constant product innovation is a central element of strategy. Lafley, however, believed that the pendulum had swung too far toward technology during the heady new-economy years. At one point, the annual budget for "skunk works" technology—experimental projects outside the mainstream businesses—had reached $200 million. "We were spending more than tech companies were on this kind of stuff," he observes. Thus P&G, which business schools treated as the classic example of a company that builds all of its processes around consumer "pull," was now "pushing" technology into the market. This was certainly one way to develop new ideas, but not necessarily winning ideas.

Durk Jager had excited P&G people with these investments. Lafley describes that approach as "forward to the future," which he contrasts with his own "back to the future" mind-set: "I wanted to put consumers front and center and get back to asking, 'Who are they and what do they want?' Find out what they want and give it to them. Delight them with P&G products. So I have this incredibly simple saying: 'The consumer is the boss.' And there are two moments of truth—when consumers make their purchase decision, and when they use the product. If they're delighted at the second moment of truth, they'll repurchase our brands and hopefully begin to use our products regularly."

When Jager left the company, news accounts cited his global reorganization as a major contributor to his departure. Lafley, however, not only supported the reorganization but had also served on the team that designed it. Rather than abandon Jager's new organizational structure, Lafley used it to support his own theme of returning to a stronger consumer orientation. The new market-development operations were charged with winning the first moment of truth, the new global business units with winning the second. The new structure, says Lafley, then "had a simple reason for being," and another apparent liability became an asset for the transformation.

More generally, Lafley strongly credits Jager with moving P&G toward a more external focus. Jager had begun to promote what the company calls "connect and develop"—that is, the pursuit of more externally sourced innovation. Currently, 25 percent of new products and technologies come from outside the company, but Lafley wants to raise that to 50 percent, so that "half would come out of P&G labs and half would come *through* P&G labs, from the outside."

Lafley is pushing for more exposure to the outside world in other ways as well—for example, by establishing strong relationships with external designers, distributing product development around the world to increase what P&G calls "consumer sensing," and even bringing John Osher, who invented the Crest SpinBrush electric rotating toothbrush, inside the company for a period to help make it more innovative. All of these moves have increased the flow of new ideas.

That flow should surge again with P&G's acquisition of Gillette. Like most major deals, this one is intended to create value in a number of ways, including relatively straightforward cost efficiencies. Lafley has concrete ideas for strengthening Gillette's brands too. He believes that increased innovation will be the most significant factor in the longer run, though he concedes that it is difficult to predict, at this early stage, exactly what form innovation will take:

"My aspiration is that this deal will accelerate the growth and development of our company by a decade or two. It's clear that Gillette and P&G are two of the strongest innovators in consumer products. Gillette's a company, like us, built on innovation in their core businesses. So I'm hopeful that we'll learn a lot from each other. They're mechanical engineers, we're chemical engineers. I'm very hopeful that this combination will open up new businesses to us. If you put mechanical and chemical engineers together, they're going to see things that we don't see today, because our view of the world is bounded."

Lafley clearly has strong faith in the transformative power of learning—a faith evident not only in his aspirations for the Gillette deal but also in the coaching role he regularly assumes with managers. It is clear, as well, in his initiatives to expand P&G's formal management and leadership training: for example, he founded the company's college for general managers and teaches leadership.

His coaching role has also shown him the importance of his own learning experiences. The first months after Lafley's appointment as CEO were particularly difficult in this respect: although he had experience selling the full range of P&G products during his stint as leader of the North American market-development operation, he lacked a deep understanding of about half of the company's businesses. Some things he learned during this period were bracing: "I discovered that the cupboard was bare on the technology side in one business, that we didn't have the leadership we needed in another business, and that we didn't know what the strategy was going to be in a third business." He was learning, in effect, what was needed to coach the organization.

Although Lafley needed a period of crash learning as CEO despite his 25 years as a P&G operating manager, he credits his experience with giving him insights into ways of transforming the company. "You need to understand how to enroll a leadership team and then an organization, how to operationalize the strategy, how to get the accountability that you want all the way down the organization. The more deeply you understand something, the more willing you are to take risks and the more intelligent those risks are." His deep knowledge of the company, he says, "meant I knew how and when we could take risks and stretch ourselves to go for peak performance—without breaking down."

Does a radical change agent lie behind the cultural conservatism? Lafley paused at the "radical" label because, at least until the Gillette deal, the transformation had been the cumulative effect of a series of small, interlocking changes. No single dramatic event during the past five years defines the period, just as no evocative vision statement served as its road map. "I guess I'm a serial change agent," Lafley says.

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