Organizational transparency drives company performance

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Abstract

Purpose – To explain the logic of value creation through increased organizational transparency of human capital.

Design/methodology/approach – The authors compare the status of today's organizations with other areas of life where transparency has been a fundamental driver of efficiency. Further, the authors break transparency down into logical steps of value creation. Insight is based on hands-on experience working with several companies on these issues as well as designing software to support the logic.

Findings – Modern companies are taking steps to drive company performance through increased efficiency delivered by increased transparency but few take it all the way. No universal model is prescribed but a clear sequence of foundations that need to be in place is discovered.

Research limitations/implications – The paper is based on the authors' research and learning from working in this field. Further research in the field of organizational transparency as a means to drive company performance is suggested.

Originality/value – This paper takes a different angle than the traditional view.

Keywords Organizations, Strategic alignment, Human capital, Company performance

Paper type Viewpoint

This article focuses on the execution of strategy in organizations and the transparency of those strategies within organizational structures. Business strategy is distinct from the process of breaking down the strategy into definitive and meaningful components upon which individual employees can act. Employee understanding of those components is critical to the successful execution of the organization's strategy. We illustrate this point with what we call "strategy transparency".

What level of transparency optimizes the operational efficiency of an organization? How much transparency and frictionless matching of supply and demand of human talent is optimal in order to effectively execute a strategy?

The observations that follow in this paper have been gained from our vantage point at SuccessFactors, a Silicon Valley software firm serving more than 1000 customer organizations in 139 countries and 18 languages, with over two million employee/users of our performance and talent management solution. To protect confidentiality, examples have been modified and cited without identifying the organizations involved, but such examples are current and real world.

Strategy transparency

Execution of strategy is the key driver of an organization's financial performance (Bossidy *et al.*, 2002). Execution has an impact on financial performance that is six times higher than the impact of a strong strategy itself (Huselid *et al.*, 2005). Employees represent the most valuable, and thus most costly, variable in the execution of business

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strategy. Therefore, maintaining motivated and engaged employees is essential to the successful execution of business strategy.

Many of our customers are progressive high-tech organizations in which employees represent a critical component of strategic capability, so much so that the strategic focus of organizations, and major investment decisions, are becoming more dependent on the capabilities of people than other market driven factors. There is a complex interplay of factors at work in such resource allocation and investment decisions, but the specific capabilities of individual people are critical for companies dependent on talent to drive strategy execution. In such companies, strategy development and the issue of what can be accomplished with current and future talent pools based on the ability to attract and develop key talent are interdependent.

Strategy can be broken down into definitive components, or goals, upon which individual employees can act. When these goals are made relevant and achievable for individual employees, they can be aligned to promote successful execution of strategy (Kaplan and Norton, 2006). However, the absence of a well defined strategy and a breakdown of individual objectives create a condition for weaker performance. The levels of transparency at which strategy can be communicated to employees will impact the organization's performance.

At the first level of transparency, an organization does not reveal its strategy to its own employees. Non-transparency is an extreme precautionary measure used to prevent competitors from obtaining strategic information from internal sources. It may be that when employees are intentionally left unaware of business strategy, organizations manage to succeed only in the absence of competitive market conditions. These include monopolies and oligopolies, which enjoy regulatory protections that do not promote strategy transparency in their organizations.

The second level of transparency is defined by ambiguous strategy that is interpreted liberally by organizational executives. Executives understand the organization's strategy primarily in the context of how it directly affects his or her area of accountability. As such, overall business strategy is not coherent across the organizational hierarchy. This level of transparency is typical of large, multi-national companies with different lines of business, where disparate strategies are housed in their own silos.

One example of this could be a consulting company, with its bulk of revenue in the low margin IT development and outsourcing business, that decides to acquire a high margin low volume management consulting service firm without a clear strategy on how to marry the two models into something greater for the owners. With no clear strategy, individual managers might continue to optimize the single business model they understood, and upon which accountability had been based until that point, instead of focusing on the greater potential of the combined organization – the reason for the acquisition.

Another example might be a manufacturing company that has grown into a product line where its own brands are competing with one another. Imagine a merger between two companies in the warehouse equipment business where the European division promotes one brand and the US division promotes another one. How is this company going to drive any synergies from that merger if a transparent strategy broken down into goals for individual managers, including which product lines should be marketed to which market and customer, does not exist? The risk for sub-optimized decisions in marketing and sales, as well as development and manufacturing, is high without a clear understanding of the business strategy broken down into individual goals.

The third level of transparency is evident in organizations that have developed a clear strategy, but have not made it clear at the lower levels of the organizational hierarchy. This is common among large businesses with employees on the frontline who provide customer service. Companies in the retail and airline industries, for example, have large workforces that frequently interact with customers. The challenge, then, is for executives to execute the organization's strategy through the contributions of employees at lower levels of the hierarchy. However, customers are often more educated and informed of a company's products and services than the actual employees, who are sometimes viewed as obstacles in the way of completing transactions.

The evolution of information technology has reduced the value customers perceive in some traditional channels of customer service. Frontline employees are often not given the authority to make decisions and use their own judgment to create value for the customer and the organization. An "efficiency paradox" exists, whereby companies view employees as components of machinery, rather than as a motivated workforce that can make the difference in successful execution of the organization's strategy. Consequently, this broken model creates opportunities for competitors to seize. Electronic retailers, such as amazon.com, have succeeded by enabling customers with information and self-services that have traditionally been provided by customer service representatives. Today, consumers can bypass these traditional channels altogether. Astute traditional brick and mortar retailers have responded by integrating the web channel into its physical stores, for example where items on display can be immediately ordered and sent home to the customer if there is a shortage. Another way traditional retailers have responded has been to sell over the web and offer hassle-free returns through the stores, thus reducing the customers' perceived fear and pain factor for online shopping. Irrespective of how the design of the process will be carried out to support the selected strategy, the frontline people must be focused on goals that support the very customer experience desired. Lack of understanding, authority or motivation from the employees to do so will hurt the organization.

At the fourth level of transparency, a company has a strategy that is clearly communicated and broken down into actionable goals for each employee. Individual goals are defined throughout the employee lifecycle, from requisition and on-boarding of new employees, to managing their ongoing development, performance, and potential succession. In our experience at SuccessFactors, this fourth level of transparency is growing in importance as a source of competitive advantage.

An example of where we see the fourth level of transparency becoming more important is in the context of the strategic shift many firms are making from hardware manufacturing, increasingly commoditized and competitive, towards value added services and software. Numerous high tech organizations have undergone or are undergoing this strategic shift today. Without a clear understanding of their current talent pool and their ability to attract and develop the needed skills, execution of the new strategy is at risk. The companies with which we work undergo a tremendous amount of change with layoffs and new hires in parallel. The successful organizations are the ones that can find the potential on an individual basis and act upon that information (Berggren and Fitz-Enz, 2006).

Transparency and employee motivation

On average, organizations lose forty percent of the potential financial value of their strategies due to poor performance and talent management of their employees (Mankins and Steele, 2005). A clear understanding and alignment of individual goals with an organization's over-arching strategy is fundamental to driving execution of that strategy, but it certainly is not enough. Unless employees are motivated, the alignment of organizational and individual goals will not optimize the organization's overall performance (Sirota *et al.*, 2005). It is critical, then to understand what will motivate an individual to achieve the goals that contribute to the execution of the organization's strategy.

As organizations evolve in the economic ecosystem, those who drive the execution of organizational strategies are being influenced by factors that previous generations did not face**.** There has always been change, but now it happens at an even faster pace. Globalization of markets and access to information through technology in general and Internet in particular has propelled change at a dramatic speed.

Most people in the developed world today take food and shelter for granted, and the job has become something more than simply a means to put food on the table. Many people in developed countries do not view their jobs solely as a means to support their basic needs and lifestyles, but are looking at work as a means to fulfill needs that are higher up in the Maslow Hierarchy Of Needs pyramid. Based on our experience in the field, this appears to be even more true of the so called Generation X. Their attitudes towards work and what motivates them appear to be dramatically different than some of their older colleagues.

Preferences, attitudes towards work, and motivation change over time in the cycle of each individual working life. A recent college graduate will have different priorities and preferences for work today than he or she will/would ten years from now with work experience and a family to support. With increasing demands for talent and a shortage of individuals, this is becoming more critical for organizations to understand and take into account in its strategic planning and utilization of human capital.

We know that it is costly to retain poorly performing employees, but organizations also pay a significant cost when talented employees voluntarily leave. This talent drain results in costly sourcing and development of new talent, but often hurts more in terms of productivity losses and inability to grow. Employee preferences and what they look for from work are determined not just at an individual level, but also over time. An organization that fails to recognize and meet those changing needs over time will underutilize its talent.

To mitigate this talent drain, organizations can build a job description that is based on the strengths of an individual who fills a particular position, rather than mold an employee to fit a job role that is rigidly defined. The benefits of this intriguing approach will become increasingly apparent for organizations that are highly dependent on talent for their success. The authors will continue to monitor this area of human capital management and gauge its impact on organizational performance.

Paying employees equally or differentiating compensation on demographic parameters is a concept that the authors describe as the "worse than average" paradox. An employee who often implicitly advocates this system of equal pay recognizes that his or her own performance is already worse than the average performance of other employees. Thus, he or she is being over-paid relative to the salary that would be paid in an organization with a pay-for-performance culture. If a majority of employees in an organization approach their work with this "worse than average" mentality, the ability to change and successfully execute strategy is less likely to occur. The authors believe that this is one reason to why people are often reluctant to adopt any change before they clearly see what and how this change will affect them personally and financially.

Organizations that become mired in this system of equal pay explain that it is difficult to overcome and that it is a fair system of compensation, relative to all other alternatives. A recent study, where stronger and weaker companies are compared in terms of financial performance, shows the connection between pay and performance. 67 percent of the stronger performing group has a holistic pay-for-performance system in place and 28 percent of the weaker performers do (Berggren and Fitz-Enz, 2006). The key to being successful with this approach is to be able to make it right. A shift to a pay-for-performance model where the perception that performance is arbitrarily assessed is doomed to fail. As Stanford Professor Jeffrey Pfeffer discusses in his recent book about evidence-based management, pay for performance is a complex issue (Pfeffer and Sutton, 2006). Financial incentives have a motivational, informational and a selection effect. All are very powerful if designed correctly, but become a risky approach if not based on real data on performance. What we see from working with successful organizations, from our growing customer base of more than 1000 companies, is that those that are implementing or reinforcing a pay-for-performance model integrate goal setting, with performance reviews that relate to those goals, and where career opportunities and compensation are directly linked to the outcome from the performance assessments. This was also a finding from a recent research effort investigating the linkage of pay-for-performance and financial performance (Berggren and Fitz-Enz, 2006).

In many developed countries, especially in Europe, strong unions have been enforcing a system of equality pay that makes it hard to change. With increasing competition for employee talent and high performers, the system of equal pay will ultimately reduce the organization's overall performance and ability to successfully execute on strategy. Continually over-compensating employees in a system of equal pay will raise an organization's average compensation above the market average. This will negatively impact the organization's financial agility and its ability to invest in areas of the business targeted for growth. Organizations that fail to correct this pattern will continue to retain under-performers and lose high-performing talent.

Pay-for-performance is optimally effective when that performance is fairly assessed, and the results are used as a basis for determining employee compensation. Logically, an organization's most valuable employees must be motivated by incentives that are fair and directly related to their contributions. Although there is no universal pay-for-performance model, there are some common models that have proven to be unsuccessful. Compensating employees with the same salary or pay rate, regardless of individual performance levels and their impact on strategy execution, is increasingly being recognized as a sub-optimal model (Fitz-enz, 1997). In this case, employees are being paid for their time, rather than any significant contribution to the organization. Research shows that recognizing individuals for strong performance has a significant effect on increasing employee motivation (The Jackson Organization, 2005).

Establishing an organizational culture that rewards performance should be promoted by continually motivating employees. In addition to recognizing individual employee performance, two other major factors that motivate employees exist. First, the relationship that an employee has with his or her manager can foster communication about all aspects of the employee's job performance. Second, the success of the organization as a whole can be used as a motivating factor when an individual's goals and performance are aligned with those of the organization. When the organization succeeds, the individual should also feel that he or she has succeeded.

Another interesting phenomenon in relation to organizational transparency is the openness and comfort in which employees can express frustration with their own organization's inability to execute strategy and make critical decisions. Recently, for example, employees at Capitol Records publicly aired their discontent with the CEO's management style, and brought their concerns directly to EMI, which owns Capitol Records (Johnson, 2006). To encourage this form of complete transparency, alignment of goals and strategy should be understood at all levels of the company.

Organizational transparency at the forefront

In working with some of the most progressive companies in Silicon Valley, we have found that organizations are increasingly making goals transparent, rather than keeping them undisclosed. With greater transparency, individual performance and contributions to the organization become more evident. Transparent goals are critical for an employee to understand how his or her own goals and performance relate to those of other employees. An organization cannot attempt to replace broken business models, reform management, or restructure the organization without replacing them with a new solution or system that will succeed.

An organization cannot develop a transparent organization without first ensuring that fundamental conditions are in place. As discussed in this paper, an organization must possess a clearly defined strategy that is possible to execute with the human capital that the organization nurtures. That strategy must then be broken down into individual goals that support the over-arching strategy. To achieve this, information technology must be leveraged, especially as organizations' operations, employees, and customers become more global in nature. Another indicator of the rapidly-evolving direction of organizational strategy and structure is the trend in the tenure of CEOs. The average tenure of a CEO has dropped from approximately ten to five years over the past decade with a 126 percent increase in turnover since 2000 (Gaines-Ross, 2005).

Openly communicating goals within an organization is a step in the direction of driving efficiencies through information transparency. A benefit of transparent goals and the linkage between them within an organization is to drive collaboration between employees directly, and not exclusively through direct managers. Another potential benefit from this is to drive efficiency through reducing redundant work efforts that might not otherwise be known. What is less common in practice, though, is making employee compensation levels transparent. Few, if any, organizations reveal information about individual compensation as it relates to employee performance over time.

Conclusion

Though there is no universal model that can be applied to every organization, there are fundamental conditions that need to be in place to foster organizational transparency and, therefore, drive company performance. A clearly defined strategy that is broken down into individual actionable goals is essential to making employee contributions relevant and purposeful. Further, relentless execution through integrated pay-for-performance relies on fair assessments of employee performance.

The authors' hypothesis is that transparency within an organization reduces inefficiencies in strategy execution, and is a key factor in attracting and retaining high performers in the labor market. Further research into this area is suggested.

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