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Lessons from the Industrial Excellence Award

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Foreword

“He who stops getting better has stopped being good.”

Hans Schneider, General Manager of the Siemens Amberg Electronics Factory, Industrial Excellence Award overall winner 2007

There is a general perception that inflexible labor markets and high labor costs are contributing to a massive displacement of manufacturing jobs and investment from Western Europe to Eastern Europe and Asia. The debate in Western Europe is highly charged, but sometimes ill-informed.

It is true that some low-skilled jobs are moving into low labor cost countries. On the other hand, many more highly skilled jobs are actually being created in the highly developed countries. The total impact on Western economies is much more complicated, and there is some evidence of important benefits.

In this book, we showcase examples of excellent industrial management that has managed to create substantial job growth in manufacturing. This book is based on 14 years’ observation of the Industrial Excellence Award (IEA) in Germany and France, the first ten years of which we summarized in our previous book, *Industrial Excellence (Springer 2003)*, and on an additional five years of observation between 2002 and 2007. We have seen that *management’s first and noble responsibility to society is to achieve competitiveness*. Competitive organizations create growth and jobs, even in Western Europe. Competitiveness requires clearly articulated strategic positioning, together with excellent execution, and mobilization of all employees to apply their abilities and to pull in one direction. The combination of a clearly understood and shared strategy with mobilization of the organization and execution enables a company to increase productivity substantially. It is total productivity that underlies wealth.

This book offers lessons for managers of industrial firms. It offers a framework of management quality coupled with strategic positioning that together lead to competitiveness. We describe a number of examples of excellent management in Germany and France that can serve as role models. The achievements of the winning organizations have been no less than breathtaking. They have shown us that with intelligence, discipline and drive, the sky is the limit. Success and recognition provide motivatation and good management encourages abilities and energy in the organization and allows it to thrive. Such organizations do not destroy employment, they create it, and contribute to the surrounding communities. Figure 1 shows the employees of the IEA overall winner in 2007, the Siemens Amberg Electronics factory, after they won the award. They are a role model for what is possible.

We conclude by suggesting lessons managers in Western European economies should draw. The current debate is sometimes confused – even senior managers suggest that successful plants that have managed to increase productivity

Fig. 1. Award celebration at the Siemens Amberg Electronics Factory

somehow prosper at the expense of the economy: "Yes, you are successful, but only by stealing business from your competitors and thus, overall, shrinking the labor pool in our country!"

The lesson is that, it is management's responsibility to ensure the competitiveness of the organization. Competitiveness leads to growth and job creation. It is not a zero sum game; it benefits the organization and the economy in which the organization operates. This includes, in addition to management quality and sound strategy, the ability of the organization to collaborate with the stakeholders in the community. We have to move away from the labor cost discussion and the fight over who retains which piece of a limited and shrinking pie. The future lies in innovation and structural change, allowing differentiated strategic positions and generating new sources of value. In some cases, this requires giving up low-skilled work for more customized and productive work that can continue to support economic wealth. The political system must support and re-train the people who are displaced in the process, offering them other opportunities. Businesses must support the political system in this endeavor: businesses cannot thrive in an impoverished surrounding. We outline some of the responsibilities of the partners, government and unions in Chap. 10, although a complete discussion of their roles is beyond the scope of this book. Our emphasis is that businesses must be good citizens in their own long-term interests.

This book, like our first book *Industrial Excellence*, is about management quality. Management must lead the way in finding new sources of value (and thus total productivity) through innovation in products and services as well as supply chain structures, potentially with partners. The three key parties – businesses, politicians, and unions – have to stop blocking innovation by fighting for their own piece of the pie, and support the change. We are all sitting in the same boat.

We argue that business management, in particular, should stop complaining about the other parties and roll up its sleeves to ensure the competitiveness of its organization. That is management's responsibility.

We show excellent examples of how ensuring competitiveness is possible in Germany and France. We thank the managers of these companies for generously giving their time to be interviewed. And we thank all participants in the Industrial Excellence Award for their efforts. We have learned from all of them.

We also thank our colleagues at INSEAD, particularly Ludo Van der Heyden and Luk Van Wassenhove, for their generous collaboration. We are indebted to Andreas Enders, Fabian Sting, and Delphine Delafontaine for their efforts and high quality work in managing the Industrial Excellence Award and giving insightful input into the content and design of the book. We also thank our journalist partners, Dieter Dürand from *Wirtschaftswoche*, and Thibaut de Jaegher from *L'Usine Nouvelle* for their collaboration.

We like to extend our thanks to Sally Simmons and the Cambridge Editorial Partnership, who conscientiously accompanied us during the work on this book, and helped us convert our many notes and ideas into several of the chapters. Her writing and editorial skills are appreciated. Mistakes, of course, remain our own. Finally, we acknowledge the support of the INSEAD Alumni Fund, which helped to facilitate the award competition for the years when our site visits to these and other outstanding firms were taking place.

Fontainebleau and Vallendar Christoph Loch

January 2008 Stephen Chick

Arnd Huchzermeier

Contents

Part I: The Challenge

Part II: Management Quality, Innovation, and Services

Part III: Networked Strategy

Part IV: What Does this Mean? Implications of the Industrial Excellence Examples

PART I

The Challenge

Chapter 1

Management Quality and Strategic Positioning

1.1 The Challenge

In 2002, two managers from organizations that had won the INSEAD/WHU Industrial Excellence Award gave presentations to INSEAD's International Council, an annual discussion forum for senior managers. The topic was "High Performance Organizations," and the two winning companies presented their action programs and reported on their successes, including impressive productivity gains. A participant in the audience, a senior German manager, raised his hand and said: "It is impressive how you are making this succeed, and you are certainly doing very well for yourself, but you are aware that you are stealing jobs? Your clients save costs and become more profitable, you make money, people in India get jobs, but you are using your productivity gains to win against your competition, and so you are destroying jobs in Europe, just shifting those jobs out of Europe and contributing to the flow of jobs to low-cost countries. Companies become profitable, but at the cost of the home population who are losing their livelihoods. How do you feel about doing your country and its economy such a disservice?" His challenge was the start of a fiercely contested debate.

This remark is symptomatic of the direction the public debate in Europe has taken on outsourcing or off-shoring (or "*délocalisation*," as it is referred to in France). This senior manager had accepted the fallacious idea that there is a fixed amount of labor sloshing around in the industry, and that by raising productivity, and by shifting jobs into low-cost countries, that amount is reduced, leading to unemployment.

This thinking is now recognized as erroneous but, worryingly, many people still adhere to it. In our daily lives most of us understand and accept that if something becomes more expensive, we will buy less of it – if the price of beer in bars goes up, people buy and drink less, and if the price goes down, people buy more. If beer is much cheaper in the bar next door some people will prefer to drink there (unless the first bar provides some other added value, such as a more pleasant atmosphere).

The same holds for labor (as well as for capital) in economic activity – if the price goes up, firms will buy less of it, replacing labor with capital (for example, investing in automation). Labor is a purchased production factor, and if workers in other countries can provide labor of the same quality for less cost, there will necessarily be a trend to purchase it there, again, unless some other value is provided (such as proximity to customers and higher responsiveness).

Increasing productivity does not reduce the overall demand for labor. It may do so in the very short term (if, for example, buying a machine releases a worker). However, for the economy as a whole, productivity enhancements reduce the effective cost of labor by increasing the output that can be produced per labor hour. Therefore, higher productivity increases the demand for labor. Productivity does *not* destroy labor. On the contrary, it makes labor more attractive for the economy.

Indeed, economists agree that productivity growth is probably the single most important indicator of an economy's health: it drives real incomes, inflation, interest rates, profits, and share prices. Productivity in the economy as a whole closely tracks growth, wealth, and job creation. Figure 1.1 illustrates this connection through the most widely used wealth measure, Gross Domestic Product (GDP),[1] and labor productivity (the GDP per hour worked).

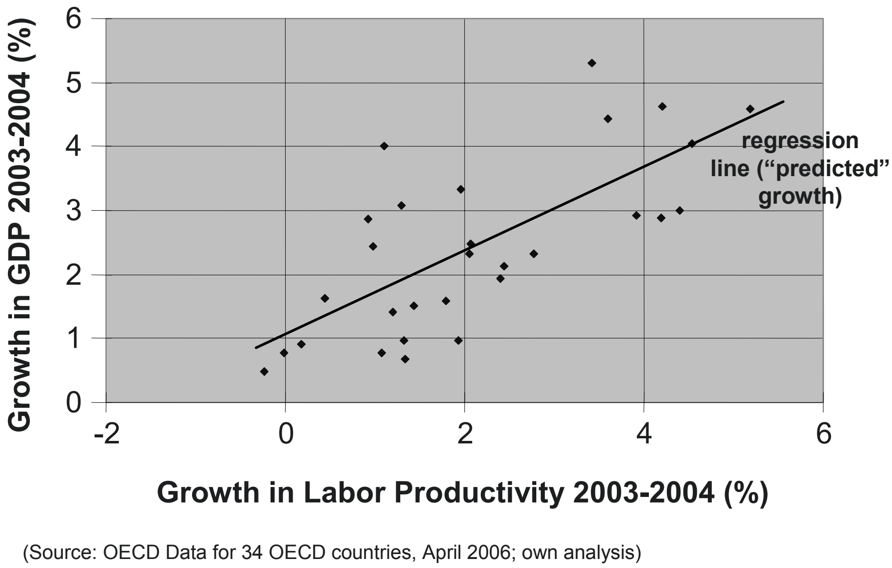

Fig. 1.1. Connection between GDP growth and labor productivity growth

[1] GDP (gross domestic product) is one of the most widely used measures of a country's wealth. It is defined as the market value of all final goods and services produced within a country in a given period of time. It can be formally written as: GDP = consumption + investment + government spending + (exports – imports). "Gross" means that depreciation of capital stock is not deducted (without depreciation, with net instead of gross investment, it is the net domestic product). Consumption and investment in this equation are the expenditure on final goods and services. The exports minus imports part of the equation then adjusts this by subtracting the part of this expenditure not produced domestically (imports), and adding back in domestic production not consumed at home (exports).

The chart shows 2003–2004 GDP growth and growth in labor productivity. A clear connection is evident: countries with higher labor productivity growth simply grow more.[2] And this is true despite the fact that at least two other important drivers of growth are missing: capital productivity (the value produced per unit of capital employed), and labor mobilization (the percentage of the population that actively participates in the workforce). In other words, labor productivity is one of the key drivers of economic growth.

In order to connect this discussion to management, we need to broaden it. An economy creates wealth and growth if it is *competitive*. That means that the economy is able either to create *value* (whether this is through higher quality products and services, or different products and services, or delivering them faster, and so on – anything that is valued by paying customers), or to deliver the same value at *low cost*. Competitiveness can be driven by the output side (revenues) or by the input side (cost). A competitive organization can grow because it is able to offer customers value for their money. An industrial sector that contains competitive organizations will grow. An economy with a significant number of competitive sectors will grow. And growth means job creation.

This has an important implication: who is responsible for the competitive ness of organizations? The answer to this is *management*. It is management's responsibility to produce a strategy for an organization that allows it to compete successfully, to be profitable, and to grow. If certain inputs become more expensive, the strategy must be adjusted in order to get more value out of those inputs, to use fewer of them, or to replace the products that use them by other products that use fewer. Organizations that are not successful in instituting a flexible strategy like this are not successful in the market, either.

A successful strategy cannot consist exclusively of managing the cost side. On the value side, it must define unique or attractive services to be offered to customers.

This leads us to one of the major premises of this book: economic growth and job opportunities within a country are heavily driven by growth in productivity (of both labor and capital). Productivity growth is, in turn, closely related to the competitiveness of industrial sectors, a key driver of which is the management of private companies. Economic growth is, to a significant extent, the result of management at myriad enterprises in the economy. Therefore, economic growth is partially the responsibility of managers.

The reader might well object to all the responsibility being placed on the management of individual companies, and point out that governments are responsible for creating conditions under which companies can be successful. This is, of course, true. Many external influences are important for the competitiveness of companies within a country. The government (through regulation, social charges and taxation, the provision of infrastructure and safeguarding property rights), the social system (through the educational system), and the unions (through bargaining of

[2] The regression is highly statistically significant and explains 50% of the variance.