

Why management matters for productivity

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While government policy will play a key role, the actions of managers and their organizations will decisively influence the realization of global productivity potential in the years ahead.

Achieving the productivity “catch-up” and “frontier expansion” noted in the previous article ultimately will depend on the actions of individual firms and their management teams—influenced, of course, by the government policy context in which they operate. How does the view from the trenches in those firms compare with the McKinsey Global Institute’s country- and sector-level one? It’s quite consistent, according to research on the relationship between management practices and firm-level productivity. McKinsey conducted that research over more than a dozen years, in conjunction with the Centre for Economic Performance at the London School of Economics and partners from Stanford and Harvard universities.

Our study now spans roughly 14,000 organizations in more than 30 countries.¹ It shows that the core elements of management can be assessed and scored and that well-managed firms have higher productivity, market value, and growth, as well as a greater ability to survive adverse conditions, such as global financial recessions. Our research further indicates that more than 80 percent of all productivity variation occurs within a given sector for a given country

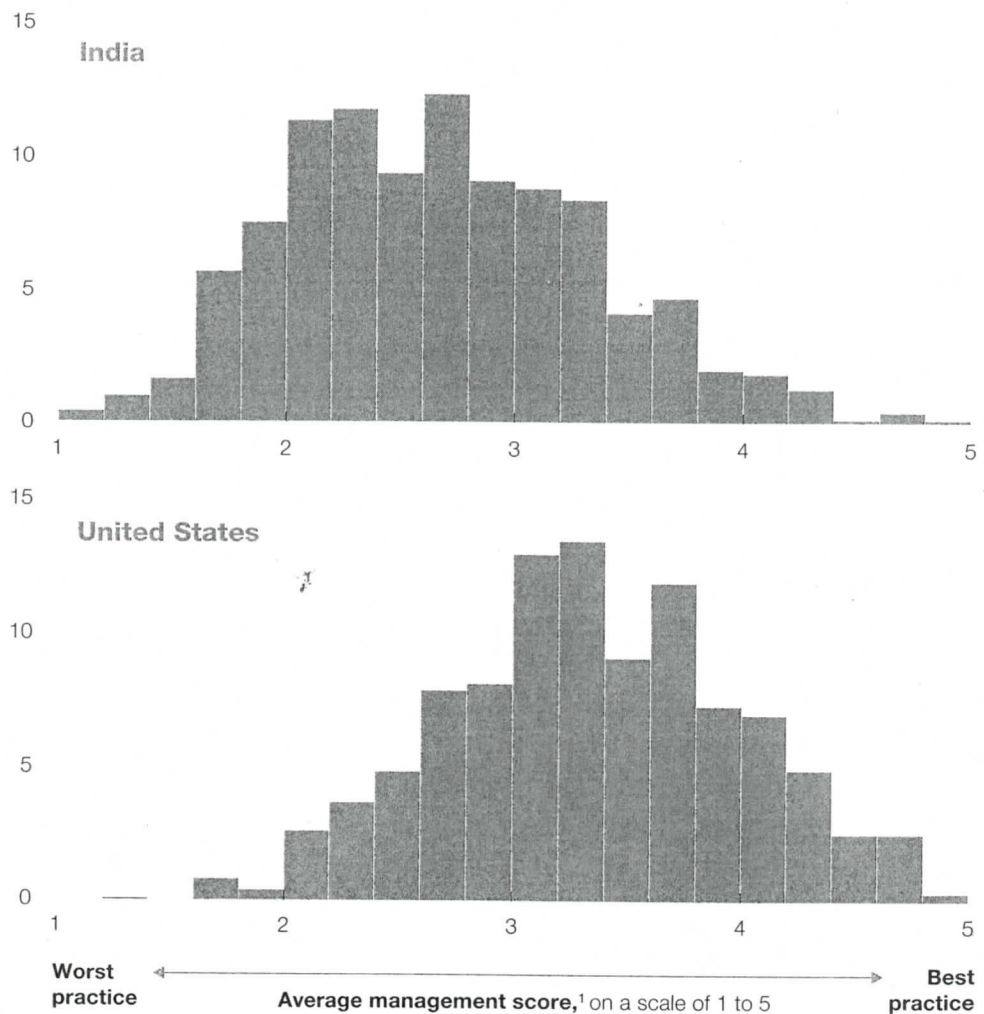
¹ The data collected are updated from our original report: *Management practice and productivity: Why they matter*, July 2007, Centre for Economic Performance, London School of Economics, cep.lse.ac.uk/management.

and that there's a "long tail" of persistently badly managed firms in all countries and across all sectors. These findings suggest a significant potential for management-led productivity improvements in every country on Earth. Of course, the tail of poorly managed firms is much bigger in some countries, such as India, than in others, such as the United States (Exhibit 1).

Exhibit 1

The long tail of poorly managed firms is much bigger in some countries than others—for example, in India compared with the United States.

% of companies with given score



¹Sample of 1,225 manufacturing companies in the United States and 729 in India.

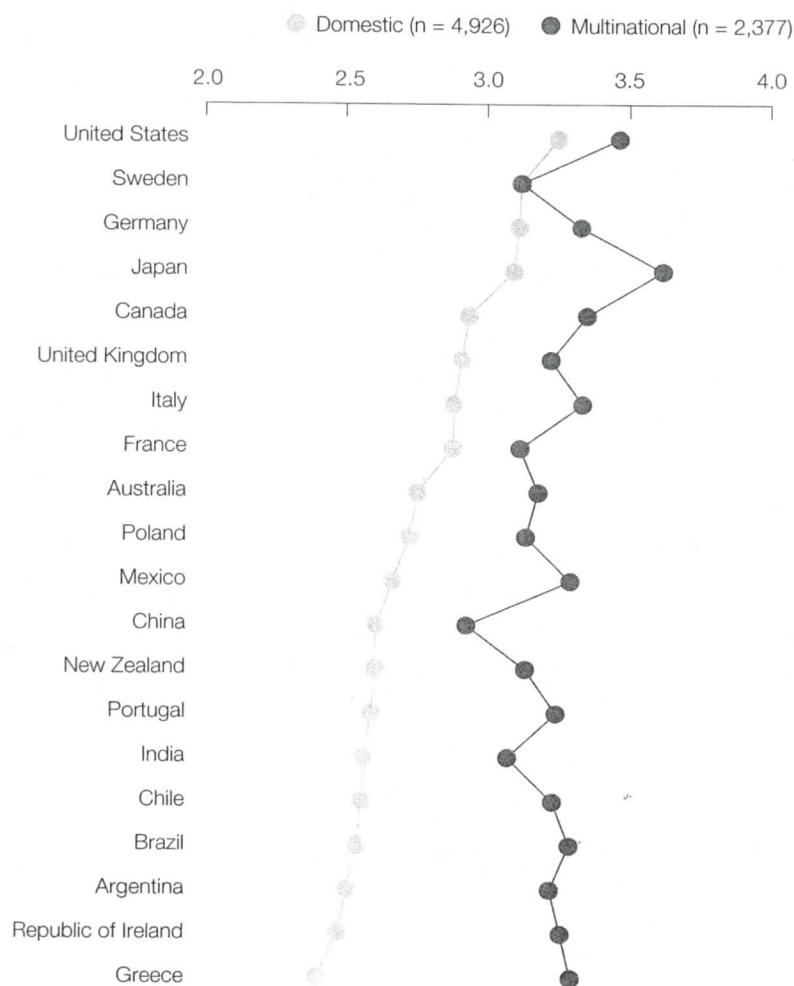
Source: Updated data from original report: *Management practice and productivity: Why they matter*, July 2007, Centre for Economic Performance, London School of Economics; McKinsey analysis

Historically, multinationals have played an important role in seizing this potential because they have been the most productive companies, on average, no matter what their country of origin or where they operate (Exhibit 2). As multinationals based in emerging markets grow in prominence in the years ahead, we are likely to see

Exhibit 2

Historically, foreign multinationals have been the most productive companies, no matter where they operated.

Average management scores for domestic companies and foreign multinationals,¹
on a scale of 1 to 5, where 1 = worst practice and 5 = best practice



¹ Sample of 7,303 manufacturing companies; domestic subsidiaries of multinational companies—eg, a Toyota subsidiary in Japan—are excluded.

Source: Updated data from original report: *Management practice and productivity: Why they matter*, July 2007, Centre for Economic Performance, London School of Economics; McKinsey analysis

new “flavors” of the powerful market dynamics that help these companies stimulate productivity by bringing technology and know-how, which spill over into the broader economy. Multinationals invest in raising their employees’ skills, which also diffuse into the broader economy as people move around and set up their own businesses. Finally, the increased competition that multinationals bring (and are exposed to) forces domestic players to improve their own productivity—driving down prices, increasing demand, and creating more choice for customers.

Interestingly, there’s an almost complete lack of self-awareness among managers about the productivity or management effectiveness of their own companies: we found virtually no correlation between their independent rankings of the management practices of their companies and our own assessment, conducted as a double-blind study. The possible solutions our research suggests include transplanting superior management practices between countries by rotating key managers, both inside companies and outside them. Rotation boosts productivity performance over time by ensuring that a larger number of operations benefit from the leadership of more productive managers—provided, of course, that companies weed out weak ones rather than cycle them elsewhere in their operations. ◻

The authors would like to thank their collaborators in this work, especially Nicholas Bloom, Stephen Dorgan, Dennis Layton, and Raffaella Sadun.

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