October 2001

Good to Great

Fast Company

by Jim Collins

Start with 1,435 good companies. Examine their performance over 40 years. Find the 11 companies that became great. Now here's how you can do it too. Lessons on eggs, flywheels, hedgehogs, buses, and other essentials of business that can help you transform your company.

I want to give you a lobotomy about change. I want you to forget everything you've ever learned about what it takes to create great results. I want you to realize that nearly all operating prescriptions for creating large-scale corporate change are nothing but myths.

The Myth of the Change Program: This approach comes with the launch event, the tag line, and the cascading activities.

The Myth of the Burning Platform: This one says that change starts only when there's a crisis that persuades "unmotivated" employees to accept the need for change.

The Myth of Stock Options: Stock options, high salaries, and bonuses are incentives that grease the wheels of change.

The Myth of Fear-Driven Change: The fear of being left behind, the fear of watching others win, the fear of presiding over monumental failure—all are drivers of change, we're told.

The Myth of Acquisitions: You can buy your way to growth, so it figures that you can buy your way to greatness.

The Myth of Technology-Driven Change: The breakthrough that you're looking for can be achieved by using technology to leapfrog the competition.

The Myth of Revolution: Big change has to be wrenching, extreme, painful—one big, discontinuous, shattering break.

Wrong. Wrong. Wrong. Wrong. Wrong. Wrong. Totally wrong.

Here are the facts of life about these and other change myths. Companies that make the change from good to great have no name for their transformation—and absolutely no program. They neither rant nor rave about a crisis—and they don't manufacture one where none exists. They don't "motivate" people—their people are self-motivated. There's no evidence of a connection between money and change mastery. And fear doesn't drive change—but it does perpetuate mediocrity. Nor can acquisitions provide a stimulus for greatness: Two mediocrities never make one great company. Technology is certainly important—but it comes into play only after change has already begun. And as for the final myth, dramatic results do not come from dramatic process—not if you want them to last, anyway. A serious revolution, one that feels like a revolution to those going through it, is highly unlikely to bring about a sustainable leap from being good to being great.

These myths became clear as my research team and I completed a five-year project to determine what it takes to change a good company into a great one. We systematically scoured a list of 1,435 established companies to find every extraordinary case that made a leap from no-better-than-average results to great results. How great? After the leap, a company had to generate cumulative stock returns that exceeded the general stock market by at least three times over 15 years—and it had to be a leap independent of its industry. In fact, the 11 good-to-great companies that we found averaged returns 6.9 times greater than the market's—more than twice the performance rate of General Electric under the legendary Jack Welch.

The surprising good-to-great list included such unheralded companies as Abbott Laboratories (3.98 times the market), Fannie Mae (7.56 times the market), Kimberly-Clark Corp.(3.42 times the market), Nucor Corp. (5.16 times the market), and Wells Fargo (3.99 times the market). One such surprise, the Kroger Co.—a grocery chain—bumped along as a totally average performer for 80 years and then somehow broke free of its mediocrity to beat the stock market by 4.16 times over the next 15 years. And it didn't stop there. From 1973 to 1998, Kroger outperformed the market by 10 times.

In each of these dramatic, remarkable, good-to-great corporate transformations, we found the same thing: There was no miracle moment. Instead, a down-to-earth, pragmatic, committed-to-excellence process—a framework—kept each company, its leaders, and its people on track for the long haul. In each case, it was the triumph of the Flywheel Effect over the Doom Loop, the victory of steadfast discipline over the quick fix. And the real kicker: The comparison companies in our study—firms with virtually identical opportunities during the pivotal years—did buy into the change myths described above—and failed to make the leap from good to great.

How change doesn't happen

Picture an egg. Day after day, it sits there. No one pays attention to it. No one notices it. Certainly no one takes a picture of it or puts it on the cover of a celebrity-focused business magazine. Then one day, the shell cracks and out jumps a chicken.

All of a sudden, the major magazines and newspapers jump on the story: "Stunning Turnaround at Egg!" and "The Chick Who Led the Breakthrough at Egg!" From the outside, the story always reads like an overnight sensation—as if the egg had suddenly and radically altered itself into a chicken.

Now picture the egg from the chicken's point of view.

While the outside world was ignoring this seemingly dormant egg, the chicken within was evolving, growing, developing—changing. From the chicken's point of view, the moment of breakthrough, of cracking the egg, was simply one more step in a long chain of steps that had led to that moment. Granted, it was a big step—but it was hardly the radical transformation that it looked like from the outside.

It's a silly analogy, but then our conventional way of looking at change is no less silly. Everyone looks for the "miracle moment" when "change happens." But ask the good-to-great executives when change happened. They cannot pinpoint a single key event that exemplified their successful transition.

Take Walgreens. For more than 40 years, Walgreens was no more than an average company, tracking the general market. Then in 1975 (out of the blue!) Walgreens began to climb. And climb. And climb. It just kept climbing. From December 31, 1975, to January 1, 2000, $1 invested in Walgreens beat $1 invested in Intel by nearly two times, General Electric by nearly five times, and Coca-Cola by nearly eight times. It beat the general stock market by more than 15 times.

I asked a key Walgreens executive to pinpoint when the good-to-great transformation happened.

His answer: “Sometime between 1971 and 1980.” (Well, that certainly narrows it down!)

Walgreens’s experience is the norm for good-to-great performers. Leaders at Abbott said, “It wasn't a blinding flash or sudden revelation from above.” From Kimberly-Clark: “These things don't happen overnight. They grow.” From Wells Fargo: “It wasn't a single switch that was thrown at one time.”

We keep looking for change in the wrong places, asking the wrong questions, and making the wrong assumptions. There’s even a tendency to blame Wall Street for the “instant results” approach to change. But the companies that made the jump from good to great did so using Wall Street's own tough metric of success: a sustained leap in their stock-market performance. Wall Street turns out to be just another myth—an excuse for not doing what really works. The data doesn’t lie.

How change does happen

Now picture a huge, heavy flywheel. It’s a massive, metal disk mounted horizontally on an axle. It's about 100 feet in diameter, 10 feet thick, and it weighs about 25 tons. That flywheel is your company. Your job is to get that flywheel to move as fast as possible, because momentum—mass times velocity—is what will generate superior economic results over time.

Right now, the flywheel is at a standstill. To get it moving, you make a tremendous effort. You push with all your might, and finally you get the flywheel to inch forward. After two or three days of sustained effort, you get the flywheel to complete one entire turn. You keep pushing, and the flywheel begins to move a bit faster. It takes a lot of work, but at last the flywheel makes a second rotation. You keep pushing steadily. It makes three turns, four turns, five, six. With each turn, it moves faster, and then—at some point, you can''t say exactly when—you break through. The momentum of the heavy wheel kicks in your favor. It spins faster and faster, with its own weight propelling it. You aren't pushing any harder, but the flywheel is accelerating, its momentum building, its speed increasing.

This is the Flywheel Effect. It's what it feels like when you’re inside a company that makes the transition from good to great. Take Kroger, for example. How do you get a company with more than 50,000 people to embrace a new strategy that will eventually change every aspect of every grocery store? You don’t. At least not with one big change program.

Instead, you put your shoulder to the flywheel. That’s what Jim Herring, the leader who initiated the transformation of Kroger, told us. He stayed away from change programs and motivational stunts. He and his team began turning the flywheel gradually, consistently—building tangible evidence that their plans made sense and would deliver results.

“We presented what we were doing in such a way that people saw our accomplishments,”Herring says. “We tried to bring our plans to successful conclusions step by step, so that the mass of people would gain confidence from the successes, not just the words.”

Think about it for one minute. Why do most overhyped change programs ultimately fail? Because they lack accountability, they fail to achieve credibility, and they have no authenticity. It’s the opposite of the Flywheel Effect; it's the Doom Loop.

Companies that fall into the Doom Loop genuinely want to effect change—but they lack the quiet discipline that produces the Flywheel Effect. Instead, they launch change programs with huge fanfare, hoping to “enlist the troops.” They start down one path, only to change direction. After years of lurching back and forth, these companies discover that they’ve failed to build any sustained momentum. Instead of turning the flywheel, they've fallen into a Doom Loop: Disappointing results lead to reaction without understanding, which leads to a new direction—a new leader, a new program—which leads to no momentum, which leads to disappointing results. It's a steady, downward spiral. Those who have experienced a Doom Loop know how it drains the spirit right out of a company.

Consider the Warner-Lambert Co.—the company that we compared directly with Gillette—in the early 1980s. In 1979, Warner-Lambert told *Business Week* that it aimed to be a leading consumer-products company. One year later, it did an abrupt about-face and turned its sights on healthcare. In 1981, the company reversed course again and returned to diversification and consumer goods. Then in 1987, Warner-Lambert made another U-turn, away from consumer goods, and announced that it wanted to compete with Merck. Then in the early 1990s, the company responded to government announcements of pending healthcare reform and reembraced diversification and consumer brands.

Between 1979 and 1998, Warner-Lambert underwent three major restructurings—one per CEO. Each new CEO arrived with his own program; each CEO halted the momentum of his predecessor. With each turn of the Doom Loop, the company spiraled further downward, until it was swallowed by Pfizer in 2000.

In contrast, why does the Flywheel Effect work? Because more than anything else, real people in real companies want to be part of a winning team. They want to contribute to producing real results. They want to feel the excitement and the satisfaction of being part of something that just flat-out works. When people begin to feel the magic of momentum—when they begin to see tangible results and can feel the flywheel start to build speed—that's when they line up, throw their shoulders to the wheel, and push.

And that's how change really happens.

Disciplined people: "Who" before "what"

You are a bus driver. The bus, your company, is at a standstill, and it's your job to get it going. You have to decide where you're going, how you're going to get there, and who's going with you.

Most people assume that great bus drivers (read: business leaders) immediately start the journey by announcing to the people on the bus where they're going—by setting a new direction or by articulating a fresh corporate vision.

In fact, leaders of companies that go from good to great start not with "where" but with "who." They start by getting the right people on the bus, the wrong people off the bus, and the right people in the right seats. And they stick with that discipline—first the people, then the direction—no matter how dire the circumstances. Take David Maxwell's bus ride. When he became CEO of Fannie Mae in 1981, the company was losing $1 million every business day, with $56 billion worth of mortgage loans underwater. The board desperately wanted to know what Maxwell was going to do to rescue the company.

Maxwell responded to the "what" question the same way that all good-to-great leaders do: He told them, That's the wrong first question. To decide where to drive the bus before you have the right people on the bus, and the wrong people off the bus, is absolutely the wrong approach.

Maxwell told his management team that there would only be seats on the bus for A-level people who were willing to put out A-plus effort. He interviewed every member of the team. He told them all the same thing: It was going to be a tough ride, a very demanding trip. If they didn't want to go, fine; just say so. Now's the time to get off the bus, he said. No questions asked, no recriminations. In all, 14 of 26 executives got off the bus. They were replaced by some of the best, smartest, and hardest-working executives in the world of finance.

With the right people on the bus, in the right seats, Maxwell then turned his full attention to the “what” question. He and his team took Fannie Mae from losing $1 million a day at the start of his tenure to earning $4 million a day at the end. Even after Maxwell left in 1991, his great team continued to drive the flywheel—turn upon turn—and Fannie Mae generated cumulative stock returns nearly eight times better than the general market from 1984 to 1999.

When it comes to getting started, good-to-great leaders understand three simple truths. First, if you begin with “who,” you can more easily adapt to a fast-changing world. If people get on your bus because of where they think it’s going, you'll be in trouble when you get 10 miles down the road and discover that you need to change direction because the world has changed. But if people board the bus principally because of all the other great people on the bus, you’ll be much faster and smarter in responding to changing conditions. Second, if you have the right people on your bus, you don’t need to worry about motivating them. The right people are self-motivated: Nothing beats being part of a team that is expected to produce great results. And third, if you have the wrong people on the bus, nothing else matters. You may be headed in the right direction, but you still won’t achieve greatness. Great vision with mediocre people still produces mediocre results.

Disciplined thought: Fox or hedgehog?

Picture two animals: a fox and a hedgehog. Which are you? An ancient Greek parable distinguishes between foxes, which know many small things, and hedgehogs, which know one big thing. All good-to-great leaders, it turns out, are hedgehogs. They know how to simplify a complex world into a single, organizing idea—the kind of basic principle that unifies, organizes, and guides all decisions. That’s not to say hedgehogs are simplistic. Like great thinkers, who take complexities and boil them down into simple, yet profound, ideas (Adam Smith and the invisible hand, Darwin and evolution), leaders of good-to-great companies develop a Hedgehog Concept that is simple but that reflects penetrating insight and deep understanding.

What does it take to come up with a Hedgehog Concept for your company? Start by confronting the brutal facts. One good-to-great CEO began by asking, “Why have we sucked for 100 years?” That's brutal—and it's precisely the type of disciplined question necessary to ignite a transformation. The management climate during a leap from good to great is like a searing scientific debate—with smart, tough-minded people examining hard facts and debating what those facts mean. The point isn’t to win the debate, but rather to come up with the best answers—and, ultimately, to lock onto a Hedgehog Concept that works.

You’ll know that you’re getting closer to your Hedgehog Concept when you align three intersecting circles that represent three pivotal questions: What can we be the best in the world at? (And equally important—what can we not be the best at?) What is the economic denominator that best drives our economic engine (profit or cash flow per “x”)? And what are our core people deeply passionate about? Answer those three questions honestly, facing the brutal facts without blinking, and you’ll begin to see your Hedgehog Concept emerge.

For example, before Wells Fargo understood its Hedgehog Concept, its leaders had tried to make it a global bank: It operated like a mini-Citicorp—and a mediocre one at that.

Then the Wells Fargo team asked itself, “What can we potentially do better than any other company?” The brutal fact was that Wells Fargo would never be the best global bank in the world—and so the leadership team pulled the plug on the vast majority of the bank’s international operations. When the team asked the question about the bank’s economic engine, Wells Fargo’s leaders confronted a second brutal fact: In a deregulated world, commercial banking would be a commodity. The essential economic driver would no longer be profit per loan, but profit per employee. The bank switched its operations to become a pioneering leader in electronic banking and to open utilitarian branches run by small crews of superb people. Profit per employee skyrocketed. Finally, when it came to passion, members of the Wells Fargo team all agreed: The mindless waste and self-awarded perks of traditional banking culture were revolting. They proudly saw themselves as stoic Spartans in an industry that had been dominated by the wasteful, elitist culture of banking. The Wells Fargo team eventually translated the three circles into a simple, crystalline Hedgehog Concept: Run a bank like a business, with a focus on the western United States, and consistently increase profit per employee. “Run it like a business” and “run it like you own it” became mantras; simplicity and focus made all the difference. With fanatical adherence to that simple idea, Wells Fargo made the leap from good results to superior results.

In the journey from good to great, defining your Hedgehog Concept is an essential element. But insight and understanding don’t happen overnight—or after one off-site. On average, it took four years for the good-to-great companies to crystallize their Hedgehog Concepts. It was an inherently iterative process—consisting of piercing questions, vigorous debate, resolute action, and autopsies without blame—a cycle repeated over and over by the right people, infused with the brutal facts, and guided by the three circles. This is the chicken inside the egg.

Disciplined action: The “stop doing” list

Take a look at your desk. If you’re like most hard-charging leaders, you’ve got a well-articulated to-do list. Now take another look: Where’s your stop-doing list? We've all been told that leaders make things happen—and that's true: Pushing that flywheel takes a lot of concerted effort. But it’s also true that good-to-great leaders distinguish themselves by their unyielding discipline to stop doing anything and everything that doesn't fit tightly within their Hedgehog Concept.

When Darwin Smith and his management team crystallized the Hedgehog Concept for Kimberly-Clark, they faced a dilemma. On one hand, they understood that the best path to greatness lay in the consumer business, where the company had demonstrated a best-in-the-world capability in its building of the Kleenex brand. On the other hand, the vast majority of Kimberly-Clark’s revenue lay in traditional coated-paper mills, turning out paper for magazines and writing pads—which had been the core business of the company for 100 years. Even the company's namesake town—Kimberly, Wisconsin—was built around a Kimberly-Clark paper mill.

Yet the brutal truth remained: The consumer business was the one arena that best met the three-circle test. If Kimberly-Clark remained principally a paper-mill business, it would retain a secure position as a good company. But its only shot at becoming a great company was to become the best paper-based consumer company—if it could take on such companies as Procter & Gamble and Scott Paper Co. and beat them. That meant it would have to “stop doing” paper mills.

So, in what one director called “the gutsiest decision I've ever seen a CEO make,” Darwin Smith sold the mills. He even sold the mill in Kimberly, Wisconsin. Then he threw all the money into a war chest for an epic battle with Procter & Gamble and Scott Paper. Wall Street analysts derided the move, and the business press called it stupid. But Smith did not waver.

Twenty-five years later, Kimberly-Clark emerged from the fray as the number-one paper-based consumer-products company in the world, beating P&G in six of eight categories and owning its former archrival Scott Paper outright. For the shareholder, Kimberly-Clark under Darwin Smith beat the market by four times, easily outperforming such great companies as Coca-Cola, General Electric, Hewlett-Packard, and 3M.

In deciding what not to do, Smith gave the flywheel a gigantic push—but it was only one push. After selling the mills, Kimberly-Clark’s full transformation required thousands of additional pushes, big and small, accumulated one after another. It took years to gain enough momentum for the press to herald Kimberly-Clark’s shift from good to great. One magazine wrote, “When ... Kimberly-Clark decided to go head to head against P&G ... this magazine predicted disaster. What a dumb idea. As it turns out, it wasn't a dumb idea. It was a smart idea.” The amount of time between the two articles: 21 years.

Now it begins

Our study of what it takes to turn good into great required five years—and 10.5 person-years—and amounted to our own flywheel effort. Looking back on our research, what's most striking to me about our findings is the absence of a magic moment in any of the good-to-great companies—or in our own journey to understanding. The real path to greatness, it turns out, requires simplicity and diligence. It requires clarity, not instant illumination. It demands each of us to focus on what is vital—and to eliminate all of the extraneous distractions.

After five years of research, I'm absolutely convinced that if we just focus our attention on the right things—and stop doing the senseless things that consume so much time and energy—we can create a powerful Flywheel Effect without increasing the number of hours we work.

I'm also convinced that the good-to-great findings apply broadly—not just to CEOs but also to you and me in whatever work we're engaged in, including the work of our own lives. For many people, the first question that occurs is, "But how do I persuade my CEO to get it?" My answer: Don't worry about that. Focus instead on results—on subverting mediocrity by creating a Flywheel Effect within your own span of responsibility. So long as we can choose the people we want to put on our own minibus, each of us can create a pocket of greatness. Each of us can take our own area of work and influence and can concentrate on moving it from good to great. It doesn't really matter whether all the CEOs get it. It only matters that you and I do. Now, it's time to get to work.

Jim Collins (jimcollins@aol.com) wrote the essay "Built to Flip" in the March 2000 issue of *Fast Company*. His new book, *Good to Great: Why Some Companies Make the Leap ... And Others Don't,* will be available in October.

Sidebar: Separating the good from the great

Can a good company become a great company? How? It took Jim Collins and his team of researchers five years to come up with the answers: 11 companies made the leap from good to great and then sustained those results for at least 15 years. How great was great? The good-to-great companies averaged cumulative stock returns 6.9 times the general market in the 15 years after their transition points. The actual screening-and-selection process was a rigorous one. The criteria were:

1. The company had to show a pattern of good performance, punctuated by a transition point, after which it shifted to great performance. "Great performance" was defined as a cumulative total stock return of at least three times the general market for the period from the transition point through 15 years.

2. The transition from good to great had to be company specific, not an industrywide event.

3. The company had to be an established and ongoing enterprise—not a startup. It had to have been in business for at least 25 years prior to its transition, and it had to have been publicly traded with stock-return data available for at least 10 years prior to its transition.

4. The transition point had to occur before 1985 to give the team enough data to assess the sustainability of the transition.

5. Whatever the year of transition, the company had to be a significant, ongoing, stand-alone company.

6. At the time of its selection, the company still had to show an upward trend.

The study began with a field of 1,435 companies and emerged with a list of 11 good-to-great companies: Abbott Laboratories, Circuit City, Fannie Mae, Gillette Co., Kimberly-Clark Corp., the

Kroger Co., Nucor Corp., Philip Morris Cos. Inc., Pitney Bowes Inc., Walgreens, and Wells Fargo.

The next step in the study was to isolate what it took to make the change. At this point, each of the 11 good-to-great companies was paired with a comparison company—a company with similar attributes that could have made the transition, but didn't.

Then the research began. Collins and his team reviewed books, articles, case studies, and annual reports covering each company; examined financial analyses for each company, totaling 980 combined years of data; conducted 84 interviews with senior managers and board members of the companies; scrutinized the personal and professional records of 56 CEOs; analyzed compensation plans for the companies; and reviewed layoffs, corporate ownership, "media hype," and the role of technology for the companies. The findings are contained in *Good to Great: Why Some Companies Make the Leap ... And Others Don't* (HarperBusiness, 2001).

Sidebar: Great answers to good questions

Fast Company: The CEOs who took their companies from good to great were largely anonymous. Is that an accident?

Jim Collins: There is a direct relationship between the absence of celebrity and the presence of good-to-great results. Why? First, when you have a celebrity, the company turns into "the one genius with 1,000 helpers." It creates a sense that the whole thing is really about the CEO. At a deeper level, we found that for leaders to make something great, their ambition has to be for the greatness of the work and the company, rather than for themselves. That doesn't mean that they don't have an ego. It means that at each decision point—at each of the critical junctures when Choice A would favor their ego and Choice B would favor the company and the work—time and again the good-to-great leaders pick Choice B. Celebrity CEOs, at those same decision points, are more likely to favor self and ego over company and work.

FC: Like the anonymous CEOs, most of the good-to-great companies are unheralded. What does that tell us?

JC: The truth is, few people are working on the most glamorous things in the world. Most of them are doing real work—which means that most of the time they're doing a heck of a lot of drudgery with only a few moments of excitement. The real work of the economy gets done by people who make cars, who sell real estate, and who run grocery stores or banks. One of the great findings of this study is that you can be in a great company and be doing it in steel, in drug stores, or in grocery stores. No one has the right to whine about their company, their industry, or the kind of business that they're in—ever again.

FC: Let's say that I'm not running a company. How do the good-to-great lessons apply to me?

JC: The basic message is this: Build your own flywheel. You can do it. You can start to build momentum in something for which you've got responsibility. You can build a great department. You can build a great church community. You can take every one of these ideas and apply them to your own work or your own life.

FC: What does your research suggest about the best way to respond to the current economic slowdown?

JC: If I were running a company today, I would have one priority above all others: to acquire as many of the best people as I could. I'd put off everything else to fill my bus. Because things are going to come back. My flywheel is going to start to turn. And the single biggest constraint on the success of my organization is the ability to get and to hang on to enough of the right people.