



# the ACTION LAB

## Creating a Greenhouse for Organizational Change

*How do you mobilize your company for rapid change?*

*The Action Lab catalyzes “out of the box” thinking — and empowers the company to act.*

By Richard T. Pascale and Anne H. Miller

**In** THE MID-1990's, Royal Dutch/Shell, like many other large companies, was nagged by a sense of unfulfilled ambition. At every level its traditional change-management approach — painstaking analysis and planning followed by careful consensus building and sequential implementation — was powerless to move

it from where it was to anywhere it wanted to be.

Take, for example, Shell Malaysia, where the chairman, Chris Knight, needed to create a whole new direction for the downstream marketing and distribution part of its \$6 billion, 6,000-person business. For the first time in memory, Shell was contem-

plating a decline in its gasoline market share in the face of aggressive competition. An initial cost management drive had improved financial returns but not the allure of its gas stations, whose unappealing exterior was turning off increasingly picky and affluent customers. Meanwhile, prime sites for new service stations were becom-

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**Richard T. Pascale** is an associate fellow of Oxford University and a visiting scholar of the Santa Fe Institute. A faculty member at Stanford's Graduate School of Business for 20 years, he is a consultant to leading companies worldwide. Dr. Pascale is co-author of "The Art of Japanese Management" (Simon & Schuster, 1981), a New York Times best seller, and author of "Managing on the Edge" (Simon & Schuster, 1990) and numerous Harvard Business Review articles. He is completing "Surfing the Edge of Chaos" (with Mark Millemann and Linda Gioja, Random House, 2000), applying recent scientific insights into the nature of living systems to achieve discontinuous organizational change. **Anne H. Miller** is a partner at Applied Value, where she leads efforts for combining strategy and organizational skills to deliver large-scale change in major corporations worldwide. Ms. Miller specializes in the issues facing leaders who seek to renew and sustain organizational capability for innovation. She has been responsible for large-scale change efforts across a variety of industries and national cultures, including Southeast Asia, South Africa, South America, Europe and the United States.



ing harder to win.

The newly privatized downstream portion of Malaysia's national oil company, Petronas, posed a particularly tricky problem. On the one hand, Petronas competed against Shell's downstream business. On the other, as the national oil company, Petronas owned all the underground assets and mineral rights in the nation, so Shell was obliged to partner with it in negotiating upstream exploration and production contracts. Effectively, Petronas held the key to Shell's success in Malaysia. Finding a way of managing this delicate relationship creatively — balancing

competition and cooperation — was crucial.

Mr. Knight needed to achieve a change in both levels of service and strategic ambition — and in real time rather than the 24 or 30 months any major change would have taken the company in the past. He turned to a radically new approach for Shell — a series of Action Labs. The Action Lab (see accompanying article, page 69) is a short, extremely intense collective effort to telescope time frames and promote radical new behaviors that companies may have talked about for years but never been able to achieve. For instance, Shell Malaysia's

first lab was charged with reversing the erosion of market share by transforming customer service to Shell's 1,000 service station dealers and 12,000 commercial customers. A second lab was commissioned to explore the idea of a joint rationalization of storage depots with Petronas as a possible entree to a broader logistics partnership. But instead of two years to analyze and plan, Mr. Knight gave the labs just 60 days to produce results.

In effect, Mr. Knight had to create a "greenhouse" for extraordinary innovation that was insulated from the day-to-day "jungle" of running the

business and its cultural norms. Composed of cross-functional and multi-level participants reflecting the stakeholder groups that would implement the solutions, the labs were headed by informal leaders and assisted by facilitators who helped clarify the labs' charters and break through ingrained mind-sets and assumptions that had hindered previous attempts

accept that no one else has the answer — the team itself must generate it. Management really does need help! Participants often need coaching to get through the eye of this emotional needle and gain the confidence to pursue bold and original ideas.

All this points to a paradoxical rule of thumb: When an Action Lab is not experiencing upsets or failures, it

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to change. Outsiders, such as dealers or officials from Petronas, were invited in or enrolled in the experiments that followed. Finally, Mr. Knight and two members of his team served as executive sponsors to protect and to review the lab's progress. Often, they found themselves rolling up their sleeves to help participants negotiate around the organizational land mines.

#### SHIFTING THE LOCUS OF ACTION

Now comes the hard part. It is one thing to put people in fresh surroundings, give them a blank sheet of paper and assure them it is safe to fail. But lab participants invariably begin by asking: "Do they really mean it?" or "What's the hidden agenda?" As the lab team interviews sponsors and others outside for the answer, the members typically encounter all the conflicting views that have held problems in place for years. Stress intensifies. Ultimately, the lab is forced to

is probably not pushing the envelope hard enough. Because of the human tendency to postpone trauma, most of the lab's real work happens in the pressure of the last weeks. Until then, the lab is building strength by gathering a base of facts, strengthening cohesion and dealing with occasional failure. Regular debriefings foster the daily mixture of hardship and insight. Developing an initial team point of view is the jumping-off point for action. Generally, the faster the lab gets into action, the faster it learns.

While the executive sponsors may regard the lab as a "safe haven," for participants it is a pretty uncomfortable place to be. They usually feel they are walking a tightrope between results that are too timid or overly bold: either way their career prospects are on the line. Nine times out of 10 the Action Lab takes the courageous route.

Consider the aviation lab of Shell

Brazil, which targeted fuel sales to corporate jets. Emerging from a regulated environment, jet fuel in Brazil was historically sold at a fixed rate for major airlines and private aircraft alike. Consequently, pilots of private aircraft were at the bottom of the food chain, serviced only after the big airlines had been taken care of. The result was a chronic scheduling problem for these pilots, who often found themselves bearing the frustration of their V.I.P. clients. When the pilots were invited into the lab for some online research, the findings pointed to a significant opportunity not only for a premium-priced prompt fueling service, but also for add-on services for the V.I.P.'s.

Sponsors and other stakeholders outside the lab were initially lukewarm about the proposal. What was so exciting about a market analysis that showed a revenue opportunity of only a few million dollars, based on a few pilot testimonials? But the lab persisted, knowing that what it planned for aviation would set a precedent for other market segments, and indeed for the whole organization. Finally, it hit on the idea of acting out the strategy in cooperation with an airport—and inviting senior management to take part. Having struck a deal with a major airport in São Paulo, the lab spent an exhausting and exhilarating week packaging its menu of services, notifying parties of the offering and setting up a prefabricated V.I.P. facility for private pilots, complete with business services and refreshments. Senior managers were invited to the airport at 5:30 one morning to see the

idea put to the test. On the appointed day Shell sold double the normal amount of fuel at a premium price, waiting times were slashed from hours to minutes, and the planes were cleaned and restocked while being refueled.



Hardly surprisingly, once pilots had a taste of the V.I.P. service, they wanted more, prompting Shell to roll out the service throughout the country. The executive segment now contributes 10 times more to total aviation net income than it did two years ago — and the delivery team is known for its innovation and responsiveness. Shell has expanded its specialty fuels concept to include motorcyclists and commercial accounts. The former chief executive of Shell Brazil, Wim Goebel, commented, “It makes me shudder at what else is possible if we put this kind of effort into everything we do.”

From their joint experience, both lab participants and senior management learned a crucial lesson: Success on the commercial battlefield has as much to do with commitment as a team as with the brilliance of ideas. As they got the hang of “acting their way” into the new strategy, each took full accountability for pulling off the experiment. One lab participant said: “We were not following orders or a predetermined plan — we were making it up in the field. This is not the normal way of taking strategic ini-

tatives at Shell.”

The Cummins Engine Company, the world’s largest diesel-engine manufacturer, also experienced the power of acting its way into a new strategy. By mid-1997, the company had lost its engine leadership and was seeking new competitive advantage in “lifetime customer value,” emphasizing the owner cost of a superior-quality engine over its full service life, versus cheaper (but more expensive to maintain) rivals. To make the proposition work, Cummins needed not only to reduce prices by 20 percent but also to embed the service life concept throughout the engineering, manufacturing and dealer repair activities of a 20,000-person organization.

One of the lab teams, including union stewards, manufacturing supervisors and plant managers, challenged the company’s most sacred assumption — that everything must be made in-house to meet Cummins’s stringent quality standards. In just four weeks the lab pioneered alliances that entailed turning over whole plants to supplier collectives. Cummins would become the “focused assembler” for key components and the

quality watchdog for the whole process. The lab also came up with imaginative ways of moving toward flexible manufacturing while protecting jobs. Early results indicate that the new strategy has opened up new areas of market potential and avenues for market leadership. It has also restored Cummins’s competitive edge in cost and productivity.

#### EVOKING NEW BEHAVIOR PATTERNS

Social psychologists tell us that new social structures and behaviors take shape only when the rigid patterns and assumptions of the past are unfrozen. Unfreezing takes place when people are stressed emotionally, physically and intellectually to the point where the familiar framework fails. The lab’s constrained deadline and unconstrained aspiration — delivering a demonstrable and unanticipated business result in four to six weeks — is deliberately imposed to force participants out of conventional methods and hierarchical patterns, which limit the solution space. Stressed and bereft of familiar supports, all labs pass through a period

of panic and despondence before, typically, rescuing themselves by getting precise about goals, resolving to break through traditional solution constraints and rallying around their determination to generate action.

Choosing to move ahead within this new context often leaves traditional positions behind and starts a brand new kind of conversation in which, uncomfortably at first, no one

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feels really competent. Indeed, people begin to realize that positional authority and traditional patterns of “camaraderie” are often the factors that got the company into the impasse in the first place.

Shell Malaysia’s logistics lab was chartered to pilot a partnership for a gasoline distribution depot with the recently privatized marketing and distribution arm of Petronas. This was seen as a precursor to a full network rationalization of both companies and ultimately to a total logistics partnership. Success in depot operations had historically been defined by unit-cost efficiency. That is where the lab conversation started — and stalled. At the time, Petronas was a less efficient operator than Shell. So where was the gain?

The breakthrough came when the lab was prompted to reframe both

question and answer. What if Shell and Petronas sought the larger prize of becoming dominant in downstream logistics in Malaysia? Focusing on unit cost per ton of gasoline transported by truck from depots to service stations had blinded the lab from assessing the possibilities of jointly financing a pipeline that Petronas was planning to build that would slash the cost of throughput from refinery to customer.

Over time the lab laid the groundwork for a new relationship with Petronas. Not only did the subsequent logistics partnership realize cost savings that surpassed Shell’s most optimistic forecasts, it changed a vulnerable downstream supply and distribution business into a strategic and operational partnership with one of the powerhouses of Southeast Asia. By an ingenious blend of competing and collaborating — not just at the top of the organization, but at all levels — both companies gained on all other competitors. Shell generated \$5 billion in investment opportunities, while the industry as a whole avoided the waste and oversupply problems that plagued neighboring Thailand. Shell Malaysia added a new strategic capability — the ability to form joint ventures with erstwhile competitors — which has subsequently become a pivotal element of Shell’s downstream strategy worldwide.

#### CHARTERING THE LAB

Framing a lab effort is often difficult — if it is too narrow, its contributions become trivial; too broad and the charter is unmanageable. The pipe-

line subsidiary of British Gas, Transco, confronted this dilemma when it instituted a strategy lab in the middle of an industry and company restructuring. The lab was challenged to map a course of action that would spin off its various components and enable them to be stand-alone, commercially viable entities within six to 12 months. The inquiry was driven by the likelihood that regulated income would disappear at some point in the future. The problem was, the charter proved to be unmanageable given the regulatory uncertainties beyond the control of British Gas. The lab foundered, with great frustrations for both participants and sponsors.

In contrast, British Gas simultaneously began a second Action Lab, which focused on Transco’s \$1.6 billion annual capital budget, covering everything from massive pipeline infrastructure projects to routine replacement of off-the-shelf hardware, such as gas meters. On the one hand, stiffening regulatory scrutiny was turning the screws on the capital investment program. On the other, investment was difficult to control because two-thirds of the investments occurred through tens of thousands of expenditures under \$100,000. The lab’s charter was to create transparency with a new process that was more manageable and demonstrated integrity to the regulatory body and the public at large.

The lab spent the first weeks mapping a “day in the life” of an investment decision. It was a revealing exercise. The map uncovered the extent to which each geographical

*continued on page 70*



## The Action Lab in Action

**The** Action Lab is based on a simple, profound and paradoxical truth about most deep learning in adulthood: We are much more likely to act our way into a new way of thinking than think our way into a new way of acting. Three corporations in different corners of the world have translated theory into action guided by four design principles:

**1. Create an environment that is safe enough to promote experimentation and learning but intense enough to foster discontinuous change.** The trick involves keeping group attention focused on the difficult challenge, regulating distress so that the group does not become dysfunctional and handling the conflicts that arise as participants grasp avoidance mechanisms, such as scapegoating and looking to authority for the answers.

**2. Evoke new behavior patterns using a compelling real-life challenge facing the business that stresses the social order of the team.** The situation must be relevant and intense enough to “unfreeze” the social norms and force members outside their com-

fort zone into ambiguous and uncharted territory.

**3. Get to the bottom of the assigned task by uncovering the “ground truth” — the real business issues and expectations that exist when all the obscuring layers are peeled away.** This base of facts is the anvil against which straight talk occurs and new responses are forged.

**4. Foster a discontinuity in how a team is “led” as a prerequisite for achieving discontinuity in performance.** The traditional repertoire of leaders (relying on authority, having “the answers” or exercising detailed levels of control) typically fails in the lab setting. Radical solutions often emerge from unlikely sources in the organization. This frequently makes leaders feel threatened and uncomfortable. Keeping leaders in the hot seat requires enormous commitment on their part to stay the course.

Zoom in on a lab in session. The door leading into an open workspace displays a sign: “Leave your position outside and enter.” Within, a team of 10 individuals — including representatives from operations, marketing, H.R.,

finance, I.T. and from time to time customers or suppliers — sit in a circle. Dress is casual. Shop-floor workers and fast-track managers are indistinguishable from customers and vendors. Small tables with untidy piles of paper occupy the room’s perimeter. Flip charts adorn the walls, providing a chronicle of what the lab is up to and what it has accomplished from day one. One has a big square of “possibilities” with sections X’d out as feasibility analysis and organizational constraints have narrowed choices toward a likely course of action. A shoebox on one table accumulates \$1 donations as a celebration fund that grows each time anyone makes limiting statements such as “we tried it before and it didn’t work” or “they’ll never let us do that” or breaks a punctuality commitment by showing up late.


The lab participants are tired. They have spent the day trying to engage sponsors in bold propositions. Each sponsor, viewing the proposals through a different lens of experience, has found some flaw. One of the quieter lab participants speaks up: “We seem



to give up on our grand ideas every time an executive finds something to criticize. If this keeps up, we won't have anything left. Maybe this pattern of avoiding conflicts is the problem." The lab realizes that it has unconsciously been drawn into the company's hierarchical and consensual management style,

thereby limiting itself to safe territory. As one lab participant sums it up: "The lab is the company. Everything that blocks this company's ability to invent a new future is right here in this room."

Such insights are compelling. Instead of selling an idea, participants are drawn to look deeper at "why the disagreement?"

They uncover how their solution is being interpreted and what their colleagues, sponsors and other stakeholders think the company's interests really are. Armed with this understanding, the lab can create joint work that helps others outside the lab become enrolled in a bold solution. 

*continued from page 68*

manager could pursue his or her own view of where the best investment interests of the company lay. Naturally, many views conflicted, and overall corporate priorities were ignored.

To help senior management change the rules of the unspoken and self-defeating game, the lab set up investment review groups containing cross-functional teams of managers whose job was to provide a peer review of all expenditures and to surface conflicting views. At the same time, the lab seized on an ongoing reorganization to restructure local work groups by giving them profit and loss accountability. One of the chief revelations of the lab was that with the investment review groups and new work group accountability, commercial behavior was unavoidable, even in a regulated environment. The results are already notable. In less than a year, Transco's capital expenditure requirement for enhancement of the infrastructure has been reduced by 40 percent. Straight talk about investment permeates the company. One investment review group member said,

"Our test of a good question during a peer review is to ask the question that we are afraid the regulator might ask."

#### THE NEW REALITY FOR LEADERS

Top management alignment has a crucial bearing on the success of Action Labs. At Shell, Cummins Engine and British Gas, senior executives have learned that combining strategy and execution in the lab quickly confronts the company with the "political" constraints to its espoused strategy. In particular, it exposes how many consensual management practices lead to compromise solutions, which everyone can accept but no one really wants. The lab disrupts the givens of "who defers to whom," and disturbing questions about organizational policy and turf frequently shake up the surface agreements among the senior group.

Throughout the journey senior executives find themselves in the hot seat. The façade of espoused strategy cracks under the tension when lab action reveals that it is at variance with the enacted reality. What the top team thinks it stands for is revealed in all its

ambiguity as the interpretations cascade through the organization. For instance, top management at Cummins knew that the link between its statement of "lifetime customer value" and what employees actually did to put it into operation was open to infinitely broad interpretation. It took the labs to help managers become more articulate about what the vision really meant.

In another example, British Gas set up a lab to demonstrate what it would take to establish a pipeline-to-home Connections Business that could compete with outside providers. The company had analyzed and discussed the possibility for more than a year, but nothing concrete had materialized. It took the lab just a week to grasp that what was preventing action was not difficulty of execution but crippling hidden strategic disagreements at board level. Instead of setting up the business unit, the lab's first action was to help reveal (with dignity) the misalignment at senior levels. Then the lab's objective could be talked about openly and acted on with an ambition that grew as the

work progressed.

As the glare of lab attention peels away the difference between intentions and execution, executives are often led to change the way they lead. Rather than feeling obliged to have all the answers, they learn to create an environment for radical solutions to emerge from unexpected places. If things seem out of control, they are, to an extent. This is the price of breaking up patterns that keep an organization in an unwitting conspiracy to maintain the status quo. Chris Knight at Shell observed: “When we started this, there were two surprises. We didn’t expect the lab participants to be nearly as thoughtful and imaginative as they were. And even though we were forewarned, we didn’t expect that the breakthroughs they were asked to address were actually hidden in the disagreements we had concealed among ourselves for many years.”

Breakthroughs such as those at Shell, British Gas and Cummins Engine were possible only because senior management allowed lab participants to “own” a part of the business. They had to recognize that a successful lab would come up with its own results, not their answer as senior managers. This is a critical point. When they subconsciously expect the lab to come up with their answer, the very leaders who sanctioned the lab in the first place

can end up thwarting its work.

#### FROM THE GREENHOUSE TO THE JUNGLE

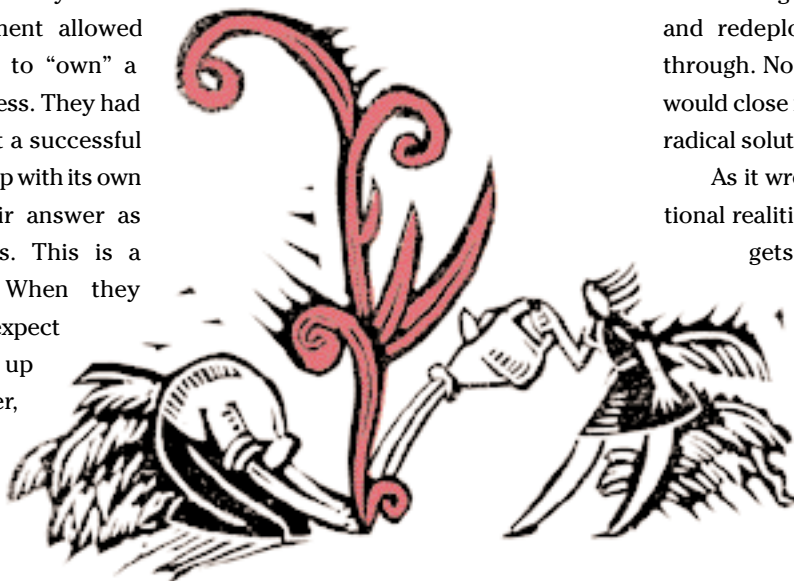
If the Action Lab is a greenhouse to nurture new growth, establishing the seedlings so that they can grow to potential in the jungle of the organizational environment is a delicate and critical task. One lab on its own can disturb the soil and nourish new ways of working. But it cannot compete with the institutional undergrowth that defines how employees really get promoted, paid and recognized. Often, the durability of the status quo becomes evident only when it is threatened.

For example, Shell Brazil chartered a lab to find ways to make its key industrial customers more successful through the use of Shell lubricants. In short order, the lab team found ways to achieve substantial savings in one major customer’s manufacturing processes, at the same time drastically increasing the sales of

one lower-margin lubricant at the expense of short-term sales of a higher-margin product. Everyone celebrated the early win, and the lab turned its attention to negotiating a profitable long-term customer contract. Work stalled, however, when the participants found that the new focus on the customer’s lifetime value conflicted with the sales reward systems that favored high product margins. The lab could not legitimize the value of the new way of working without jeopardizing sales compensation. In the end, the institutional context defeated the new initiative.

On the other hand, Shell Malaysia’s customer services lab managed to cut through huge institutional inertia to bring its solution to fruition. It was easy enough to hire and train a team of operators to staff a new 24-hour service center to provide customers with a single point of contact. It was quite another thing to shift organizational power to empower customer service representatives rather than managers to break the logjams and redeploy resources to follow through. Normally, the organization would close ranks to insure that such radical solutions were frozen out.

As it wrestled with the organizational realities of departmental budgets and attitudes, the lab could see that the quality and therefore success of its initiative was ultimately dependent on the service center’s relationships with the sales force, distribution





schedulers and dealers. As lab members, some of them had had a voice in creating the aspiration. But what about their colleagues? For instance, sales workers would no longer be responsible for administration and order-taking, a major part of their everyday work. Their new role looked more like business consulting. Deliberately using its ambiguous hierarchical status, the lab acted like a Trojan horse in steadily incorporating more employees into its experiment. New yardsticks of success were negotiated (rather than imposed) by the teams and tested in the lab by delivering early results together. Each issue was dealt with “on line” with real data and real customers. The customer service center was acting its way into its new role, becoming a demonstration model of what the rest of the organization could be. One behavioral barrier at a time was removed, as the center worked to instill a competitive customer service discipline throughout the downstream business using live commercial issues.

Enrolling a critical mass of employees behind the widespread change is a first lesson in jungle survival. As of this writing, British Gas and Cummins had conducted more than 10 labs each in 10 months. Shell Malaysia conducted more than 40 labs in an 18-month period. The work of protecting these vehicles and progressing fell to Results Councils established to insure that the company did not settle for less than the ambitious results committed to in the labs. Mr. Knight said: “The seedling trans-


plant structure we created in Malaysia was about building capability and developing new ways of working in action. By [our] binding the managers together in the Results Councils, they were compelled to participate and could not hide.”

By grounding its work in the reality of action, the lab generates not just an improvement but a fundamental shift in the business “ground truth” — underpinning expectations and assumptions — that can roll through an organization like an attitudinal tidal wave. More than 100 pacesetter labs within Shell’s worldwide manufacturing organization have shaved \$400 million from refining operating costs during the period 1996-98 and are regarded as instrumental in transforming the 2,000-person research and development organization from a cost center to a commercially viable technical consultancy. Through Action Labs, British Gas has not only found ways of reducing its capital expenditure requirement by 40 percent but has also made strong inroads into replacing the complacency that accompanied a long history of regulation with a commercially oriented sense of enterprise. While labs are early in the rollout at Cummins Engine, results of the new ways of working with suppliers and customers open the way for radical improvement.

#### **AN AGENT OF TRANSFORMATION**

As these pioneering organizations show, successful labs can produce extraordinary results. By engineering a

breakdown of the existing order, they open up a new space of possibilities; by instilling the disciplines of accountability in action, treating setbacks as opportunities and aligning around new operational yardsticks of business success, they translate that possibility into action. As a bonus, the lab environment has the benefit of identifying and developing new generations of leaders who would otherwise be unrecognized in normal reporting and recognition structures. By underwriting new leaders as well as new processes in lab experiments, these corporations are increasing their chances for sustained success.

Increasingly, corporate leaders are coming to realize that the technology of the Action Lab can help them to create breakthroughs, not just in their current ways of doing business, but in rethinking what their businesses could be. That is, as corporations internalize the disciplines of the lab, they become not simply more successful by today’s criteria but more capable as organizations, able to respond proactively to new opportunities by redefining in practical terms what success means — for themselves, for their industries and for the societies in which they operate. Although not sufficient on its own to achieve transformational change, the Action Lab is nonetheless an essential means of breaking the gridlock that prevents executives from being powerful and of banishing the entropy that over time slows down even the best of corporations. 

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