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What witch doctors?

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Maybe management theory is not hocus pocus after all

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ONCE again, scepticism about management theory—at least as business schools teach it—is growing. In his latest book, “The Future of Management”, Gary Hamel notes that several top executives—including Sergey Brin and Larry Page (the “Google Guys”) and John Mackey of Whole Foods Market—did not go to business school. Donald Trump is a Wharton alumni, but you would not guess it from his new bestseller, “Think Big and Kick Ass in Business and Life”, with its street-fighter’s advice to always get even and never marry without a prenuptial agreement. Rakesh Khurana’s new book about business schools, “From Higher Aims to Hired Hands”, charts how management science declined from a serious intellectual endeavour to a slapdash set of potted theories.



It does matter

All of this seems in keeping with the sceptical title of a book about management theorists written a decade ago by two journalists at *The Economist* (one now its editor-in-chief) called “The Witch Doctors”.

A new study begs to differ, arguing that firms implementing sound management practice have higher labour productivity, sales growth and return on capital. “Improved management practice is one of the most effective ways for a firm to outperform its peers,” concludes the study,

"Management Practice and Productivity: Why They Matter". That this is at all controversial shows how far management theory has fallen from its peak early in the 20th century, when it seemed that the science of running firms would be as rigorous as, say, applied physics.

To prove their case, the study's authors, including Nick Bloom of Stanford University and John Van Reenen of the London School of Economics, have interviewed managers at some 4,000 companies in America, Europe and Asia. (This advances an earlier study of 700 firms in America, Britain, France and Germany.)

Using the interviews, the authors rated management practices on a scale of one to five (with one being worst and five best) across 18 categories within three broad areas: shop-floor operations, performance management and talent management. There seems to be no magic bullet: a firm's average score across all 18 dimensions was the best guide to whether it would outperform its peers.

Many of the detailed findings are more surprising. In every part of the world, the spread between the best and worst run firms is wide. American firms tend to be best run, with an average score of 3.3, and Indian firms worst, with an average score of 2.62. But the best 20% of firms in India performed better than the average American firm, and the best 10% of Indian firms outscored 75% of American firms.

In every country surveyed, businesses owned by multinationals tend to be better run than their locally owned peers. Multinational firms in India scored better than any other businesses except American multinationals operating in America. When a local firm is acquired by a multinational, the quality of its management tends to rise.

Multinationals have an edge, the authors argue, because they "have been forced to take a systematic approach to management. Only by having strong, effective management practices in place have they been able to replicate the same standards of performance across different regions, cultures and markets."

Another driver of better management practice is competition, which has the strongest effects on the worst managed companies. In many countries, weak competition allows too many underperforming, poorly managed firms to survive. When firms with a score of 2 or less are excluded, the average score across the board rises from 2.62 to 2.88 in India and from 2.64 to 2.91 in Greece, compared with a small rise from 3 to 3.09 in more competitive Britain and from 3.3 to 3.33 in super competitive America.

One other notable finding: firms with dispersed ownership scored best and performed best, whilst those owned and run by their founders or members of the founder's family performed relatively poorly. Worst of all were family-owned firms run by the founder's eldest son, with an average management score of 2.53. Further proof of the wisdom of Warren Buffett's opposition to the hereditary principle, which he calls the "lucky sperm club", and describes as akin to "choosing the 2020 Olympic team by picking the eldest sons of the gold-medal winners in the 2000 Olympics."