Building a Professional Services Firm for the 21st century: Why firms need a lifestyle change, not a crash diet

Keith Dugdale, February 2014

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Some firms will soar in these economic times, some will get by and some may well disappear. Those who fly will be those who lead their way through the period and don't just manage their way. Firms with leaders who actively embrace the strategic changes that are needed and take the rest of the firm along with them for the ride.

Sadly many will convince themselves, and others, that this current economic climate is a blip, that a short term crash diet will suffice and that there is no need for a more permanent change in lifestyle. The diet is usually the easier decision for leaders, but often the most painful for others and for the long term. As 1960s author Upton Sinclair put it "It is difficult to get a man to understand something, when his salary depends upon his not understanding it."

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As recently as the 1980s and 1990s, many professional services firms tightened their belts, offloaded staff with low utilisation and in some cases reduced executive income. Largely these approaches worked as economies picked up and the driving forces behind the downturn evaporated. Over the next 10 to 30 years firms made hay whilst the sun shone.

When the Global Financial Crisis (GFC) rolled around the Northern Hemisphere in 2008 many firms believed this was another blip and went on another crash diet. Akin to the myth that one can boil a frog alive by raising the water temperature gradually, many firms in the US, Europe and Asia felt a gradual increase in discomfort. With the lack of sudden pain few firms took a big leap. Over the following four to five years many saw revenues per hour worked drop by more than 40%.

> *Since the GFC in 2008 some professional services firms in Europe have seen recoverable revenues drop 40%*

The Financial Times 2012 report (http://ftcorporate.ft.com/professional-services/) on Effective Client-Adviser Relationships identified many of the issues and what professional services clients are looking for – however few firms have adapted as radically as the report would indicate they need to. "Although clients' businesses have become more agile and innovative, there is frustration that many advisory businesses have not implemented the same degree of change". The report has one particularly damning finding: "While 51% of consultants consider that they offer excellent value for money only 2% of clients agree."

What is needed is strategic change not operational tinkering. However lessons appear not to have been learned from what has happened post GFC and the failings are being repeated. Maybe one of the reasons is the mindset of the people in charge.

In 2012 the tap was significantly tightened on Australia by China reducing its mineral needs. Many firms believed this was another blip and so squeezed their operations. Every month since things have continued to tighten with some firms now losing up to 40% of staff and some now 30% off the previous year's revenue.

> *Some firms have made up to 40% of their staff redundant but have made few changes to strategy*

Often short term profit is maintained by reducing costs such as advertising, training or staff. This can be essential, but once there is no direction or support the firm is directly compromising its ability in its core business. Performance is further compromised by cutting front-line staff too deeply.

The financial impact on the business is raised further without the hunger and discipline which is needed when times are tough. Many people expect the 'beast' to keep feeding them. They do not realise they are a vital organ in the beast.

This economy is not a blip - it is the new reality. China holds the power over Australia; clients around the world are more educated and have more power over providers; and expertise is increasingly commoditised with cheaper advice coming in from overseas.

One large firm in Asia called in 2008 because "after 20 years of boom times our partners have forgotten how to pick up the phone and call their clients"

Before the downturn many firms and their people had become fat, happy and lazy. Those who will shine going forward are those with the right attitude and aptitude. The firms who will be leaders in their field in 10 to 20 years will be those brave enough to realise that in order to succeed they need to change.

Of the Fortune 500 companies listed in 1955, 87% are no longer in that list. 50 years ago the average lifespan of a company on the fortune 500 list was 75 years, now it is less than 15 years. Why does this happen? Mainly because leaders find it harder to change than just do the same thing, slightly differently.

The average life of a company on the Fortune 500 list has dropped from 75 years to 15 years

As Einstein famously stated, insanity is "doing the same thing over and over and expecting a different result."

Fortunately some firms have felt the heat sufficiently and are reacting to position themselves for the next decade and not just for the next reporting period or next time sheet. In Australia some law firms in particular are making radical changes, however many are doing little more than moving the chairs around the deck of the Titanic.

Firms need to look at structure, rewards, systems and people in the way many firms in the Northern Hemisphere wish they had five years ago. The way this is approached will be largely determined by the leaders who are in place at the time.

Structure and responsibilities of leaders

Many firms are currently 'led' by operations roles and people whose expertise and mind-set is operational. Their skill and enjoyment comes from focussing on efficiency and who are naturally more comfortable considering the past and current situation than they are in looking to the future.

What is needed is a structure with a strategic leadership team above the operational leaders. This is critical if the firm is to achieve its existing or new vision.

There then has to be a strategy aligned to that vision which is agreed to by leadership and pursued with rigour.

Many firms are unfortunately driven by operational decisions made by people with impressive job titles. However a job title does not determine whether someone is a leader; their behaviour does.

Operations should support strategy not drive it. To make this shift a different structure is needed, with potentially significantly different types of people within the top echelons of that structure.

The CEO is responsible for driving the construction of the vision and for motivating the organisation to live and breathe it. They also must determine their personal legacy, which aligns with the vision. They must be inspirational, a visionary and a future thinker. It is more important that the CEO understands the world in which their industry operates than it is that they understand the ins and outs of their own business. They do not need to come from within their own industry. Their role is positioning the firm externally and leading it internally.

The strategic leadership team is responsible for development of the strategy to achieve the vision and for the execution of that strategy. This is the key team to run the organisation as all decisions made must align with the strategy and vision. If circumstances change then the vision and strategy need to change before operational changes are made. There is healthy tension between the three strategies of operations, client and product as discussed below. For example there cannot be blind adherence to client intimacy without consideration of operational excellence.

Like the cart and the horse, strategy must lead operations

The operational leadership team should be responsible for making sure that operations support and drive the strategy. For example the head of IT needs to make sure that all technology acquired supports the client centric, operational excellence and thought leadership strategies. The head of HR needs to be responsible for implementing KPIs which drive client centric behaviour, thought leadership and operational excellence.

Core attributes of executives, partners and staff

Traditionally firms have focussed on being the expert. They recruit people with expert university results, they train them to be even deeper experts and reward and promote the best experts. This leads to two potential issues, which generally only become concerns when times are tight.

Unfortunately the skills and mindset of an expert do not necessarily correlate to those of a visionary leader.

Many legal firms addressed this a decade ago by bringing in a lateral hire CEO or Head of Operations who was not from their industry. That approach is however not common resulting in too many leaders who are experts but neither visionaries nor strategic thinkers.

CEOs from outside the industry are rare in professional service firms but could be critical

Research also shows that expertise is no longer enough. To be truly successful the professional services provider needs several core attributes, all linking to the strategy below:

- The ability and drive to build trust with economic buyers – not just provide technical solutions to technical buyers
- The ability to influence clients and all levels of government in their decisions – as opposed to reacting to their needs
- The drive and intellectual capacity to create new ideas, methodologies, services etc. – rather than entrench themselves in a safe, comfortable area
- The commitment to build a firm based on trust – rather than one driven by structure and process
- The discipline to agree goals and then address non-performance – rather than accepting mediocrity

To develop these attributes in their staff, professional services firms need to make several critical changes:

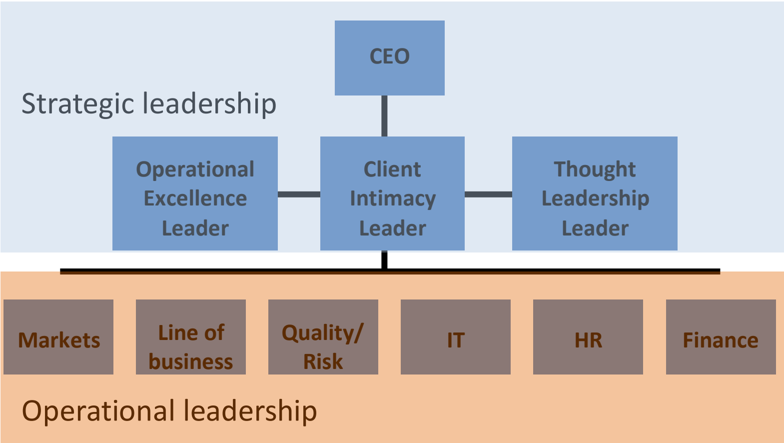
- Redefine core recruitment criteria
- Revisit KPIs for rewards and promotions
- Re-engineer the skills that are trained
- Establish proper technology that measures and predicts performance
- Redesign the organisational structure and people/responsibilities within that structure

Strategic options

One widely used strategic management model is Treacy & Wiersema who talk about three factors that determine whether an organisation is to be successful:

1. Operational excellence
2. Product (thought) leadership
3. Customer / Client intimacy

Their hypothesis is that to succeed, any organisation should be market leader in one of these three, and on a par with their competition in the other two. Hence the structure suggested to the right.



1 Operational excellence

This involves two elements: internal operations (how to increase utilisation of staff, minimise non-use of workspace etc.) and external (how to deliver projects on time). Many firms have focused only on internal operational efficiency which can have a negative impact on the external aspect. If too much focus is on efficiency, e.g. utilisation, one risks compromising on-time delivery as people are too stretched. Safety, technical correctness and all the other core values of professional services firms are at risk if efficiency is driven as the key KPI.

The difference between operational efficiency and operational excellence needs to be understood

KPIs and skill development need to reward the right behaviour at all levels. Similarly firms need to have the commitment to discipline the less diligent regardless of any other attributes they may have. Systems need to map the internal and external operations simultaneously.

A useful way to look at this is through the Project Management Institute's *Project Management Body Of Knowledge* approach. They focus on 10 areas which could be directly linked to operating excellence when running a business:

- Integration Management
- Scope Management
- Time Management
- Cost Management
- Quality Management
- Human Resource Management
- Communications Management
- Risk Management
- Procurement Management
- Stakeholders Management

2 Product (thought) leadership

The OECD defines innovation as *“the implementation of a new or significantly improved good or service, process, new marketing method or a new organisational method in business practices, workplace organisation or external relations.”*

Creating an idea is invention, implementing it and commercialising it is innovation. Many firms have KPIs and systems which inadvertently stymie ideas. Should an idea surface they are then too inert and risk averse to do anything with it. What is needed is a knowledge management model which drives innovation.

To drive the right behaviour, people who have great imagination need to be given time and rewards for that attribute even more than they get recognised for short term measurable activities. Leadership need to have mechanisms for testing ideas, refining them and commercialising them. Even at the level of sharing ideas many firms fall over. A major challenge many staff cite is knowing where and how to share ideas and where and how to borrow other people’s ideas.

One widely accepted knowledge management (KM) model is Wiig and the American Productivity and Quality Center which identified six emerging KM strategies in a study of leading organisations:

- Knowledge Strategy as Business Strategy
- Intellectual Asset Management Strategy
- Personal Knowledge Asset Responsibility Strategy
- Knowledge Creation Strategy
- Knowledge Transfer Strategy
- Customer-Focused Knowledge Strategy

Many firms focus on the knowledge strategy as business strategy. That leads to a focus of taking what they know - their expertise - and selling it. If innovation or product leadership is to become a successful strategic driver then a knowledge creation strategy needs to be driven.

For people to be brave enough to create a great idea they need support when an idea fails. People who are not risk-averse need to be celebrated not castigated. As Sean Temlett the CIO from iCampus in South Africa puts it: “Two words that kill innovation – Prove it.”

Two words that kill innovation – “Prove it”

3 Customer / Client intimacy

Most firms proudly state that “client relationships are key.” However if one digs under the surface, the understanding of a client relationship is fairly superficial. Rarely are systems or measures in place which drive and support people to build the right relationships. Many drive a project based relationship. Customer Relationship Management systems rarely measure anything other than revenue potential. Rarely do firms have chargeable codes for relationship building.

The key is that people in the firm have the right relationship with the right people in the market place. People with power and influence not just those responsible for an opportunity.

The strength of relationship is about quality not quantity. Social media is an excellent way of increasing numbers of relationships but few social media or CRMs measure how much two people trust each other. David Maister’s trust equation below is a good simple way to consider strength of relationship:

$$\text{Trustworthiness} = \frac{\text{Credibility + Reliability + Intimacy}}{\text{Self-orientation}}$$

Credibility is expertise, reliability is doing what you said you would do, intimacy is the extent to which you show you care about the other person and self-orientation is how much you focus on you, your firm and your needs.

As mentioned, most firms excel in credibility. Many clients tell me that recently reliability has dipped. Intimacy is generally the key missing ingredient, however self-orientation is also a major issue in many firms.

Most web sites, brochures and proposals say how great a firm is, how many people they have and how widespread they are. When people meet clients or targets the time they spend talking about themselves and their services is astonishing. It makes the firm very proud of themselves but it is of minimal value to the client and does little to build trust.

Most professionals acknowledge this language is wrong, however it has become so entrenched it is extremely hard to change. The onus should be on the provider to understand what the client is trying to achieve. Until the advisor understands that there is no value in citing all aspects of their firm as they may well be irrelevant.

When it comes to intimacy there are a few tests you can try:

1. Do you know the personal vision and strategy of the person you are speaking to; do you know the departmental and even organisational vision and strategy?

2. Test Maister's formula out with your client relationships. Allow a score of between 1 and 10 against each of the elements. The maximum score possible is 30. A score over nine is generally good. Most score below five.

3. When your client looks at their diary and sees your name, is that the meeting they look forward to more than any other meeting that week - every time you are in the diary. If so then you are probably trusted and valued.

   As Dov Seidman says in his seminal book *How* "*The aim is to out behave*". You need to out-behave everyone else who wants your client's time and money. Every time the client has met you they should walk away having received significant value from the meeting – even if they have no need for your technical offering. You have somehow managed to understand their world and provide value in the meeting in their world.

   "The key is to out-behave the competition"

4. Would your client put their career on the line for you. Would they be prepared to recommend you to other people of power and influence?

Many firms use client feedback processes and sometimes these are excellent. However it is critical these processes are ongoing, not just at the end of a project or year, they are done in-person and are conducted by someone independent and objective who will be asking the right questions. It is rare that all these basic rules are followed as it is deemed too expensive and time consuming by leadership and too threatening by the team themselves. Ironically those points in themselves prove that the client is not the most important thing to the firm.

People need to be rewarded for building trust and have charge codes, KPIs etc. which drive that behaviour. People who are great at relationships should have the same career opportunities as the more technically minded. The systems need to measure relationship strength as well as pipeline. A global CFO recently made a suggestion to their advisor which is sound advice for many *"Get different people and people who are different."*

"Get different people and people who are different"

Skill development programmes for all levels of staff need to ensure all staff understand that clients are at the centre of the firm, and that it is everyone's job to build deep trusted relationships across the marketplace as much is it is their job to be technically proficient.

The key to intimacy is whether the firm has the determination to prove that it cares about its clients and is prepared to do what it takes to out-behave the competition. That it is prepared to move from being a technical firm with clients to a relationships firm with technical expertise.

Conclusion

Some of the ideas suggested here are fairly simple to implement. However, making the small tactical changes becomes pointless if the critical aspects around leadership and strategy are not in place. If these more significant changes were easy to implement then everyone would be enthusiastically re-designing their firm. However most are not – and for very understandable reasons:

- For many firms the platform is not yet burning
- These changes are more akin to changing a spouse than changing an outfit
- To quote indigenous leader Pat Dodson *"In a climate of uncertainty and fear, without strong and visionary leadership, people panic"*