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Why Some Companies
Make the Leap...
and Others Don't

GOOD TO GREAT

JIM COLLINS

Coauthor of the bestselling
BUILT TO LAST

GOOD TO GREAT

Why Some Companies Make the Leap ... and Others Don't

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Dedication

This book is dedicated to the Chimps.
I love you all, each and every one.

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MEMBERS OF THE *GOOD - TO - GREAT* RESEARCH TEAM

ASSEMBLED FOR TEAM MEETING, JANUARY 2000

First row: Vicki Mosur Osgood, Alyson Sinclair, Stefanie A. Judd, Christine Jones

Second row: Eric Hagen, Duane C. Duffy, Paul Weissman, Scott Jones, Weijia (Eve) Li

Third row: Nicholas M. Osgood, Jenni Cooper, Leigh Wilbanks, Anthony J. Chirikos

Fourth row: Brian J. Bagley, Jim Collins, Brian C. Larsen, Peter Van Genderen, Lane Hornung

Not pictured: Scott Cederberg, Morten T. Hansen, Amber L. Young

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Preface

As I was finishing this manuscript, I went for a run up a steep, rocky trail in Eldorado Springs Canyon, just south of my home in Boulder, Colorado. I had stopped on top at one of my favorite sitting places with a view of the high country still covered in its winter coat of snow, when an odd question popped into my mind: How much would someone have to pay me *not* to publish *Good to Great?*

It was an interesting thought experiment, given that I'd just spent the previous five years working on the research project and writing this book. Not that there isn't *some* number that might entice me to bury it, but by the time I crossed the hundred-million-dollar threshold, it was time to head back down the trail. Even that much couldn't convince me to abandon the project. I am a teacher at heart. As such, it is impossible for me to imagine not sharing what we've learned with students around the world. And it is in the spirit of learning and teaching that I bring forth this work.

After many months of hiding away like a hermit in what I call monk mode, I would very much enjoy hearing from people about what works for them and what does not. I hope you will find much of value in these pages and will commit to applying what you learn to whatever you do, if not to your company, then to your social sector work, and if not there, then at least to your own life.

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Boulder, Colorado
March 27, 2001

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Chapter 1
Good is the Enemy of Great

That's what makes death so hard—unsatisfied curiosity.

—BERYL MARKHAM,

West with the Night[1]

Good is the enemy of great.

And that is one of the key reasons why we have so little that becomes great.

We don't have great schools, principally because we have good schools. We don't have great government, principally because we have good government. Few people attain great lives, in large part because it is just so easy to settle for a good life. The vast majority of companies never become great, precisely because the vast majority become quite good—and that is their main problem.

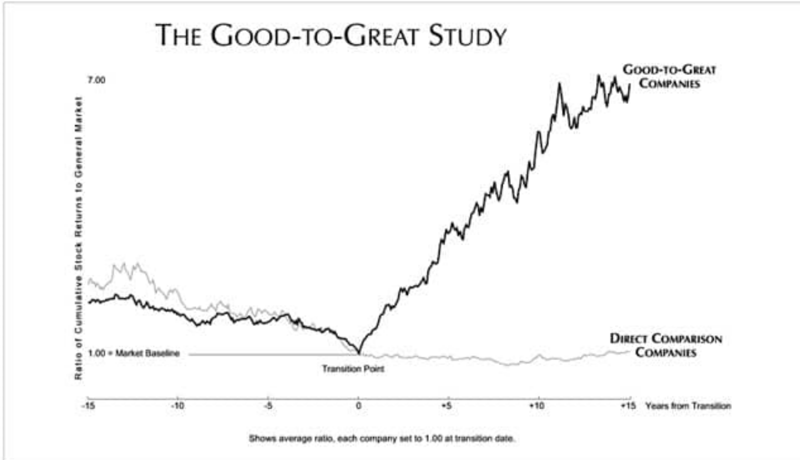
This point became piercingly clear to me in 1996, when I was having dinner with a group of thought leaders gathered for a discussion about organizational performance. Bill Meehan, the managing director of the San

Francisco office of McKinsey & Company, leaned over and casually confided, “You know, Jim, we love *Built to Last* around here. You and your coauthor did a very fine job on the research and writing. Unfortunately, it’s useless.”

Curious, I asked him to explain.

“The companies you wrote about were, for the most part, always great,” he said. “They never had to turn themselves from good companies into great companies. They had parents like David Packard and George Merck, who shaped the character of greatness from early on. But what about the vast majority of companies that wake up partway through life and realize that they’re good, but not great?”

I now realize that Meehan was exaggerating for effect with his “useless” comment, but his essential observation was correct—that truly great companies, for the most part, have always been great. And the vast majority of good companies remain just that—good, but not great. Indeed, Meehan’s comment proved to be an invaluable gift, as it planted the seed of a question that became the basis of this entire book—namely, Can a good company become a great company and, if so, how? Or is the disease of “just being good” incurable?



Five years after that fateful dinner we can now say, without question, that good to great *does* happen, and we've learned much about the underlying variables that make it happen. Inspired by Bill Meehan's challenge, my research team and I embarked on a five-year research effort, a journey to explore the inner workings of good to great.

To quickly grasp the concept of the project, look at the chart on page 2.[*] In essence, we identified companies that made the leap from good results to great results and sustained those results for at least fifteen years. We compared these companies to a carefully selected control group of comparison companies that failed to make the leap, or if they did, failed to sustain it. We then compared the good-to-great companies to the comparison companies to discover the essential and distinguishing factors at work.

The good-to-great examples that made the final cut into the study attained extraordinary results, averaging cumulative stock returns 6.9 times the general market in the fifteen years following their transition points.[2] To put that in perspective, General Electric (considered by many to be the best-led company in America at the end of the twentieth century) outperformed the market by 2.8 times over the fifteen years 1985 to 2000.[3] Furthermore, if you invested $1 in a mutual fund of the good-to-great companies in 1965, holding each company at the general market rate until the date of transition, and simultaneously invested $1 in a general market stock fund, your $1 in the good-to-great fund taken out on January 1, 2000, would have multiplied 471 times, compared to a 56 fold increase in the market.[4]

These are remarkable numbers, made all the more remarkable when you consider the fact that they came from companies that had previously been so utterly *un*remarkable. Consider just one case, Walgreens. For over forty years, Walgreens had bumped along as a very average company, more or less tracking the general market. Then in 1975, seemingly out of nowhere—bang!—Walgreens began to climb... and climb...and climb... and climb... and it just kept climbing. From December 31, 1975, to January 1, 2000, $1 invested in Walgreens beat $1 invested in technology superstar Intel by nearly two times, General Electric by nearly five times, Coca-Cola by nearly eight times, and the general stock market (including the NASDAQ stock run-up at the end of 1999) by over *fifteen* times.[*]

Notes:

1. $1 divided evenly across companies in each set, January 1, 1965.

2. Each company held at market rate of return, until transition date.

3. Cumulative value of each fund shown as of January 1, 2000.

4. Dividends reinvested, adjusted for all stock splits.

How on earth did a company with such a long history of being nothing special transform itself into an enterprise that outperformed some of the best-led organizations in the world? And why was Walgreens able to make the leap when other companies in the same industry with the same opportunities and similar resources, such as Eckerd, did *not* make the leap? This single case captures the essence of our quest.

This book is not about Walgreens per se, or any of the specific companies we studied. It is about *the question*–Can a good company become a great company and, if so, how?—and our search for timeless, universal answers that can be applied by any organization.

> Our five-year quest yielded many insights, a number of them surprising and quite contrary to conventional wisdom, but one giant conclusion stands above the others: We believe that almost *any* organization can substantially improve its stature and performance, perhaps even become great, if it conscientiously applies the framework of ideas we've uncovered.

This book is dedicated to teaching what we've learned. The remainder of this introductory chapter tells the story of our journey, outlines our research method, and previews the key findings. In chapter 2, we launch headlong into the findings themselves, beginning with one of the most provocative of the whole study: Level 5 leadership.

UNDAUNTED CURIOSITY

People often ask, "What motivates you to undertake these huge research projects?" It's a good question. The answer is, "Curiosity." There is nothing I find more exciting than picking a question that I don't know the answer to and embarking on a quest for answers. It's deeply satisfying to climb into the boat, like Lewis and Clark, and head west, saying, "We don't know what we'll find when we get there, but we'll be sure to let you know when we get back."

Here is the abbreviated story of this particular odyssey of curiosity.

Phase 1: The Search

With the question in hand, I began to assemble a team of researchers. (When I use "we" throughout this book, I am referring to the research team. In all, twenty-one people worked on the project at key points, usually in teams of four to six at a time.)

Our first task was to find companies that showed the good-to-great pattern exemplified in the chart on page 2. We launched a six-month "death march of financial analysis," looking for companies that showed the following basic pattern: fifteen-year cumulative stock returns at or below the general stock market, punctuated by a transition point, then cumulative returns at least three times the market over the next fifteen years. We picked fifteen years because it would transcend one-hit wonders and lucky breaks (you can't just be lucky for fifteen years) and would exceed the average tenure of most chief executive officers (helping us to separate great companies from companies that just happened to have a single great leader). We picked three times the market because it exceeds the performance of most widely acknowledged great companies. For perspective, a mutual fund of the following "marquis set" of companies beat the market by only 2.5 times over the years 1985 to 2000: 3M, Boeing, Coca-Cola, GE, Hewlett-Packard, Intel, Johnson & Johnson, Merck, Motorola, Pepsi, Procter & Gamble, Wal-Mart, and Walt Disney. Not a bad set to beat.

From an initial universe of companies that appeared on the Fortune 500 in the years 1965 to 1995, we systematically searched and sifted, eventually finding eleven good-to-great examples. (I've put a detailed description of our search in Appendix 1.A.) However, a couple of points deserve brief mention here. First, a company had to demonstrate the good-to-great pattern *independent of its industry*; if the whole industry showed the same pattern, we dropped the company. Second, we debated whether we should use additional selection criteria beyond cumulative stock returns, such as impact on society and employee welfare. We eventually decided to limit our selection to the good-to-great *results* pattern, as we could not conceive of any legitimate and consistent method for selecting on these other variables without introducing our own biases. In the last chapter, however, I address the relationship between corporate values and *enduring* great companies, but the focus of this particular research effort is on the very specific question of how to turn a good organization into one that produces sustained great results.

At first glance, we were surprised by the list. Who would have thought that Fannie Mae would beat companies like GE and Coca-Cola? Or that Walgreens could beat Intel? The surprising list—a dowdier group would be hard to find—taught us a key lesson right up front. It is possible to turn good into great in the most unlikely of situations. This became the first of many surprises that led us to reevaluate our thinking about corporate greatness.

GOOD-TO-GREAT CASES

Company	Results from Transition Point to 15 Years beyond Transition Point*	T Year to T Year + 15
Abbott	3.98 times the market	1974–1989
Circuit City	18.50 times the market	1982–1997
Fannie Mae	7.56 times the market	1984–1999
Gillette	7.39 times the market	1980–1995
Kimberly-Clark	3.42 times the market	1972–1987
Kroger	4.17 times the market	1973–1988
Nucor	5.16 times the market	1975–1990
Philip Morris	7.06 times the market	1964–1979
Pitney Bowes	7.16 times the market	1973–1988
Walgreens	7.34 times the market	1975–1990
Wells Fargo	3.99 times the market	1983–1998

*Ratio of cumulative stock returns relative to the general stock market.

Phase 2: Compared to What?

Next, we took perhaps the most important step in the entire research effort: contrasting the good-to-great companies to a carefully selected set of "comparison companies." The crucial question in our study is *not*, What did the good-to-great companies share in common? Rather, the crucial question is, What did the good-to-great companies share in common that *distinguished* them from the comparison companies? Think of it this way: Suppose you wanted to study what makes gold medal winners in the Olympic Games. If you only studied the gold medal winners by themselves, you'd find that they all had coaches. But if you looked at the athletes that made the Olympic team, but never won a medal, you'd find that they *also* had coaches! The key question is, What systematically *distinguishes* gold medal winners from those who never won a medal?

We selected two sets of comparison companies. The first set consisted of "direct comparisons"—companies that were in the same industry as the good-to-great companies with the same opportunities and similar resources at the time of transition, but that showed no leap from good to great. (See Appendix 1.B for details of our selection process.) The second consisted of "unsustained comparisons"—companies that made a short-term shift from good to great but failed to maintain the trajectory—to address the question of sustainability. (See Appendix 1.C.) In all, this gave us a total study set of twenty-eight companies: eleven good-to-great companies, eleven direct comparisons, and six unsustained comparisons.

THE ENTIRE STUDY SET

Good-to-Great Companies	*Direct Comparisons*
Abbott	Upjohn
Circuit City	Silo
Fannie Mae	Great Western
Gillette	Warner-Lambert
Kimberly-Clark	Scott Paper
Kroger	A&P
Nucor	Bethlehem Steel
Philip Morris	R. J. Reynolds
Pitney Bowes	Addressograph
Walgreens	Eckerd
Wells Fargo	Bank of America

Unsustained Comparisons

Burroughs
Chrysler
Harris
Hasbro
Rubbermaid
Teledyne

Phase 3: Inside the Black Box

We then turned our attention to a deep analysis of each case. We collected all articles published on the twenty-eight companies, dating back fifty years or more. We systematically coded all the material into categories, such as strategy, technology, leadership, and so forth. Then we interviewed most of