UNLIMITED MAGAZINE
Monday, 1 July, 2002

“The gospel according to McKinsey”

McKinsey & Company is the global god of management consulting. But as Rebecca Macfie found out, not everyone in this part of the world is genuflecting

By Rebecca Macfie

Andrew Grant flings himself through the elegant curved doors of the McKinsey and Company boardroom, profusely apologetic that he's 10 minutes late for our interview. With his clear blue eyes, eyebrows raised in an expression of constant amazement and beaming gap-toothed grin, he looks more like an excitable boy trying hard not to jump on the furniture than a hot-shot management consultant. He rapidly makes up for lost time, talking 90 to the dozen about the McKinsey brand, about how the firm can help save the ailing New Zealand economy from oblivion, and about the hard calls that sometimes have to be made in the tough world of management consulting.

As principal of the New Zealand office of McKinsey, 34-year-old Grant is the local face of a global firm with offices in 44 countries and revenue of $US3.4 billion in 2000. Since setting up the New Zealand office in 1998, Grant has ingratiated McKinsey into the top echelons of the New Zealand corporate sector and carved out a place for himself as one of the nation's new breed of power brokers, alongside the likes of Fonterra chief executive Craig Norgate, Carter Holt's Chris Liddell and the Knowledge Wave Trust's Bridget Wickham. McKinsey's New Zealand office consults to most of the nation's top 10 companies, it's been intimately involved in the evolution of Fonterra, it's written a new road map for the wool industry, and it was a key player in the "Catching the knowledge wave" conference held in August 2001. Grant has had the ear of the prime minister in drawing up the government's innovation strategy, thrown his weight behind the controversial upgrade of Auckland University's Business School, and associated himself with the country's first business high school at Onehunga High.

It seems like you can scarcely walk to the corner shop these days without brushing up against the McKinsey influence somewhere along the way. So, what is the McKinsey promise?

The silken-tongued Grant has a clutch of neat phrases to sum up the McKinsey brand. The firm, he says, is renowned for "serving the most important companies on the most important issues." It's prepared to take "the hard right over the easy wrong … We teach people from day one that their greatest obligation is the obligation to dissent". It stands on a "track record of impeccable work". It measures its success not in fees, but by the extent to which it brings about "lasting and positive change" in its clients. It hires only the smartest graduates (five out of the 15 consultants in the New Zealand office were Rhodes Scholars) and has a rigorous " up or out" policy to weed out stragglers. It takes a "global perspective": all McKinsey clients benefit from the firm's international expertise and extensive database of knowledge.

According to the McKinsey marketing machine, it's prepared to walk away from lucrative clients if these goals are being compromised. In one story peddled by the firm, Marvin Bower, managing director from 1950 to 1967 and regarded as the godfather of McKinsey, bellowed at a client, "The problem with this company, Mr Little, is you". The comment, apparently, was accurate. It was also the end of McKinsey's work with that client, but that didn't bother Bower. That's integrity for you.

It seems that New Zealand clients are prepared to pay top dollar for access to this brand. The Wool Board paid McKinsey $3.5 million for its June 2000 report on industry restructuring — a document that took just eight months from commissioning to publication. The Dairy Board coughed up $3 million for McKinsey's help in putting together the strategic framework that led to the first mega-merger proposal, which failed when the industry was unable to settle its historic rivalries, and later re-emerged as Fonterra. McKinsey's bill for work with Fletcher Challenge ran into several million dollars.

Wool over their eyes

Value for money? To find out, Unlimited poked through the entrails of McKinsey's work in the wool and dairy sectors. It didn't take long to find well-informed sceptics who were prepared to question the contribution made by the global doyens of management consulting to their troubled industries.

Take Murray Taggart, for example. Taggart is chair of the meat and fibre division of Federated Farmers and was a member of the Independent Stakeholders Group, put together to watch over McKinsey's wool industry work and ensure that the firm remained independent of the Wool Board's influence. The very existence of this group was testament to the long history of mistrust and division in the wool industry — a background that was always going to make McKinsey's task of charting a more prosperous future extremely difficult. Indeed, some 19 reports on the wool industry had been done in the decades before McKinsey was called in, and most had been left to gather dust. In October 1999, when the decision was made to commission McKinsey, the board was facing open farmer dissent.

That said, Taggart was deeply underwhelmed by the McKinsey work. "Frankly it amazed me how superficial some of their analysis was. I remember coming along to one meeting of the stakeholders group and they said that research and development should be directed 30% on-farm and 70% off-farm. I challenged them on that and said experience indicated that the further away from the farm you spend the money, the less benefit comes back to the farm. The next meeting they had changed it completely around to 70/30 the other way. To me, that indicated a superficial analysis. They should have challenged me and had the background to knock me over. I wasn't impressed by the fact that they didn't.

"Was it worth $3 million? No."

What was the McKinsey prescription, and was it able to be implemented?

McKinsey's 168-page wool report recommended the creation of a complex new structure for the industry, in which the Wool Board would be scrapped and its assets and brands transferred into new vertically integrated companies to market strong wool (dubbed StrongWools NZ) and fine wool (FineWools NZ). McKinsey said mid-micron wool growers faced a bleak future and should consider doing something else with their land. It recommended that the board's electronic wool trading platform, Woolnet, be commercialised to hasten the development of e-trading. Wool and meat research and development should be collapsed into a single levy-funded company (SheepCo) and a chunk of grower reserves should fund the creation of a sheep genetics company (Ovita).

Alongside these detailed prescriptions, McKinsey threw in an entire chapter on the need to lift farm productivity, which included the insightful observation that some farmers were more efficient than others. "From the results that are being achieved on comparable land, there is clearly a difference in the way top performers go about their farming ... Every farm has its own special circumstances." Wow.

Two years on, have the McKinsey recommendations been implemented? Did McKinsey bring about the lasting change that Grant talks about? Judge for yourself.
The proposal to develop a company to market strong wool — which accounts for around 75% of the national clip — didn't get off the ground. Taggart believes StrongWools NZ was never a goer, and its existence in the report was a political sop to those in the industry desperate to retain some kind of centralised structure. According to Mike Andrews, former Fletcher Challenge chief executive and head of the team charged with implementing McKinsey's wool reforms, it just couldn't be translated into an economically viable company. Instead, a joint venture combining the board's strong wool brands and the Wool Research Organisation's carpet-related intellectual property has been created, dubbed Wool Interiors.

McKinsey's fine wools formula was followed, with the creation of a new company owned 65/35 by growers and Wrightson. But industry insiders say the well-performing merino sector was moving down this track before McKinsey came on the scene.

Mid-micron farmers, told by McKinsey to pack away the shears and try something else, have seen the price for their wool go through the roof because of changes to the way the Chinese manage their quota system.

The board hasn't been able to sell Woolnet, and e-trading has not proved to be the silver bullet McKinsey hoped. However, SheepCo and Ovita have been formed. The Wool Board is in the throes of disestablishing itself, but in its place there will be a new grower-owned holding company, Wool Equities, which will own the remainder of the board's assets. Will it work? Who knows?

Peter Crone, managing director of wool exporter John Marshall and Co and former chair of the Wool Exporters Council, doubts it. He describes the McKinsey report as a "blatant" misuse of wool gro-wers' money.

Wrightson managing director Allan Freeth gives McKinsey a "D" in terms of the investment that went into the report and the results produced. He suspects McKinsey oversold itself to the farmer community, which had high expectations of what could be achieved from the 2000 report. He says one of the key concepts underpinning the report — the idea of an integrated supply chain, to match what growers and processors produce with what customers want — had been under development at Wrightson for two years before McKinsey came on the scene. "Effectively they have done what a lot of consultants do, which is borrow your watch to tell you the time."

As it turns out, Wrightson is now pushing ahead with its own version of an integrated strong wools marketing company, but Freeth says that owes little to the McKinsey report. Even when the merino joint venture was put together, he says no one involved in the process referred to the McKinsey report. "Have they created value? Probably, you would say no. However, they have put a sharp end on things and they have been something of a catalyst for change."

Another source who was intimately involved in the wool report puts it another way. "You effectively pay a franchise fee to have the McKinsey name on a report like this. You could do it yourself, but the bank or the stakeholders wouldn't necessarily wear it."

And it seems that McKinsey itself is happy with the notion that its report served more as a circuit breaker than a detailed and accurate prescription for the industry. Grant says the firm had some "really tough, hard-nosed conversations about whether we should get involved [in the wool sector], and whether we could succeed ... We know how expensive our fees are and we would only get involved if we did actually believe the chemistry for change was right.

"I'm happy it's kick-started that process of reform. It's taken some twists and turns that we didn't necessarily foresee. Am I disappointed some things haven't happened? Yes, I am. Have there been a few positive surprises? Absolutely. Has the report been followed to a T? No. it hasn't. But I also think that's unrealistic, because there's a real world out there."

Udderly intriguing

According to McKinsey's dairy industry sceptics, the real world got the better of it there, too. Malcolm Bailey, former Federated Farmers president, member of the anti-mega-merger group Farmers for a Better Dairy Deal and now a member of Fonterra's shareholders council, doesn't mince his words when he assesses McKinsey's performance in his sector: "The quality of their advice was hugely compromised."

Bailey's gripe with McKinsey goes back to the late 1990s, when the firm was brought in to advise the dairy industry on a new structure, in response to a dictate from the then-National government that producer boards would be deregulated. At the time, the industry was deeply divided, with the two big co-ops, Kiwi and NZ Dairy Group, in a battle for control of the board and most farmers still clinging steadfastly to the notion of the single desk.

McKinsey's task was to map out a new structure that would set the industry up for a prosperous future. Two options were shortlisted by McKinsey. One was a structure based around two cooperatives, each competing on the milk processing and commodity trading fronts, but with just one pursuing the industry's added-value agenda. The other option was to collapse the industry into just one mega-cooperative. In the end, McKinsey went with the mega-cooperative option — which became known as MergeCo — but only on the proviso that a set of strict pre-conditions were met, designed to mitigate the potential for such a beast to become lazy and uncompetitive.

According to a confidential 1999 strategy paper under the McKinsey byline, the pre-conditions were to "minimise performance inefficiency". It warned that "failure to implement any one of these measures would put at risk all of the value-creation potential of this structure". Among those pre-conditions were a "large proportion" (at least 40%) of independent directors, and an independently administered milk price with 4% productivity improvements built in. Integral to the proposed structure was a plan to split out the value-added businesses into a separate company, owned by the cooperative but able to bring in outside capital and with tradable shares.

According to one very senior industry source, who was closely involved during the 1999 MergeCo period, McKinsey said it would walk away if the pre-conditions weren't met. As it turned out, the industry failed to convince the Commerce Commission that the bene-fits of a mega-merger would outweigh the anti-competitive risks (instead of the claimed benefits of over $310 million from the new structure, the commission's 1999 draft determination cited the potential for economic efficiency losses of between $138 million and $527 million, when compared with the status quo or complete deregulation), and the industry dissolved into further internecine warfare.

Out of the ashes rose the GlobalCo concept in late 2000 (eventually to become Fonterra), a very similar idea to MergeCo. We never got to find out what the Commerce Commission thought of this idea because the Labour/Alliance coalition allowed it to go ahead without commission approval. And what happened to the McKinsey pre-conditions? According to Bailey and others, they were seriously watered down. Notably, Fonterra was formed with only three independent directors on a board of 13. With Mike Smith's resignation early this year, the number of independents now sits at two. There's no sign of the value-added businesses being put into a separate company with tradable shares, nor of the mandatory 4% annual productivity gain.

Did McKinsey walk away? No, and Grant refutes any suggestion of a sell-out. "I publicly said we gave the industry eight out of 10 [on compliance with the pre-conditions]. It wasn't perfect, but in terms of whether we were confident that enough had been done and whether they were on a pathway to put them in place, we said yes. Would we hold up the merger on the basis of the small print that hadn't been met? We just didn't think that was responsible." He says in some areas the industry bettered the pre-conditions, such as the proposal to have an annual Standard and Poors valuation of what an efficient commodity producer would pay for milk, against which shareholders will be able to benchmark the efficiency of Fonterra.

According to Fonterra chief executive Craig Norgate, McKinsey wasn't involved in putting together GlobalCo and only came back on the scene after the shareholder vote in mid-2001. Nevertheless, Grant publicly championed the GlobalCo model, recommending to farmers that they vote yes to the merger.

Since the merger, McKinsey has been consulting to the dairy giant on Project Galileo, a long-term strategic planning project. In addition, and somewhat ironically, it's been called in to help out with governance issues following the shock resignation of Mike Smith.

One person who takes a dim view of McKinsey's involvement in the mega-merger is Tony Baldwin, leader of the Producer Board Reform Team set up in 1999 following National's decision to deregulate the boards, and a member of Farmers for Better Dairy Deal. Having worked at close quarters with the producer board leadership, he says they are ripe for the plucking by smart consultancies like McKinsey.

"Organisations like McKinsey do well out of organisations that have weak leadership and are politically paralysed. The general level of commercial and intellectual nous in the producer board leadership is quite low, so they are vulnerable — and they also have deep pockets." Baldwin believes the mega-merger was a lowest common denominator option for a divided and commercially naïve industry that was afraid to lose its traditional single-seller security blanket. He says McKinsey was willing to act as a high priest to "validate and fortify" the merger decision.

Agree with Bailey and Baldwin or not, their comments raise two intriguing points about the McKinsey role: at what point does a highly paid consultant bite the hand that feeds it (as Marvin Bower did); and at what point has the line between independent think tank and advocate been crossed?

Grant reckons, "It's about being a positive influence and a discipline inside, versus when you make that call [to quit]. We have these sorts of conversations all the time about all our clients, in terms of whether we are adding value by staying involved, whether we are being tough enough. Situations are often painted black and white. But there is also the [decision] of to what extent are we better to stay involved and be the performance coach from the inside, versus stepping out and not being involved. These are tough calls ...

"New Zealand can't succeed without Fonterra. The commitment to seeing Fonterra succeed and seeing farmers benefit as a result is deeply and sincerely felt. We also recognise the obligation around being objective and independent and delivering tough messages."

Expert evangelists?

As for advisers crossing the line into advocacy and corporate evangelism? Being part of a global organisation tends to keep you objective, Grant says. "People looking at a client from Oslo or Bejing bring a very different perspective to people looking at them from Auckland."

According to McKinsey's clients, this global view generates real value. Fonterra's Norgate says, "They have real competence in terms of accessing the best knowledge that exists on certain topics internationally ... Often if you have your own people working on a strategy project, they believe what they've always believed, so by bringing in someone external they really test the rigour of that thinking. It's intellectual honesty that we're looking for."

Carter Holt Harvey's Chris Liddell, who has used McKinsey for several projects over the past few years, has similarly found the firm's depth of international expertise valuable. As one of the core group of "Catching the knowledge wave" conference organisers, Liddell also worked closely with McKinsey staffers who were made available to help organise and run the conference on a pro bono basis. The McKinsey people "had incredibly good process disciplines. They were very good at helping you get your thoughts together in workshop sessions, and putting them into a digestible form for the conference."

Stuart Parker also got a close-up view of the McKinsey style when he was hired to research and write a theme paper on entrepreneurship for the conference — one of five discussion papers prepared by senior post-graduate students. These days, Parker is getting on with his own entrepreneurial project, electronic wine-trading site CellarSoft.com. But his experience has left him with a somewhat jaded view of the McKinsey style. Despite being given what he thought was a clean slate for his research, when he presented his draft he discovered it didn't fit the agenda of the powers that be and the McKinsey people were brought in to rewrite it.

"The McKinsey guys have a bizarre way of working. They can't think without a whiteboard in front of them. They just write down the issues and draw their little trees and at the end of the day they come up with a list of bullet points. That's how they distil big ideas and present information. It's very formulaic. It really irritated us that no matter what kind of original take we had on something, every time the McKinsey guys walked into the room it would be, okay, let's get a white board and distil it down. You lose a lot in that sort of process.

"Everyone goes, 'Oh the McKinsey guys are here, our problems will soon be over'. But realistically, if you put any bunch of smart people in a room with a whiteboard you'll come up with some good ideas. It doesn't matter what brand they've got on their heads."

Pot of Kiwis?

Andrew Grant reckons that if your dreams don't scare you they're not big enough. He's certainly got a big scary dream for himself and the staff of McKinsey and Company's New Zealand office. "If New Zealand business doesn't really pull itself to the next level, that's a huge reflection on McKinsey," he says.

He's worried that in New Zealand's incremental slide down the OECD, we'll go the way of British broadcaster Malcolm Muggeridge's "pot of frogs" fable. When witless frogs are subjected to tiny increases in water temperature, although they are able to escape the heat, they acclimatise to the warmth and stay put. Eventually they will be boiled alive. In other words, the deterioration in New Zealand's economic performance is happening so slowly we scarcely notice how dangerous our predicament is.

Grant is on a mission to help save us from ourselves. That's why he's come back to his homeland, and isn't pursuing bigger clients and tougher challenges elsewhere in the McKinsey empire. After working for the firm in Australia, Chile, Japan and the UK, the former Rhodes Scholar in moral philosophy and industrial economics was made a McKinsey partner at the age of 28 and given the go ahead to set up the New Zealand office.

"McKinsey would never have set up a New Zealand office, but there were a number of committed individuals who were really proud of what McKinsey stands for but also desperately cared for our nation. We worry that it's not performing like it should be ... We have this noble purpose that McKinsey can be a really positive influence on the economy."

Evangelising talk like this comes easy to Grant. It's in the DNA. His dad, Ian Grant, used to push the Christian message to teenage audiences through a TV programme called The Herd. Ian and his wife Mary also ran a programme for street kids in South Auckland before setting up Parenting with Confidence, a organisation they believed would help get to the root cause of society's ills. The concept of duty clearly runs deep in the blood. "I was a simple kid from Onehunga and my Rhodes scholarship was a big break. I feel an acute sense of service that I do have to give back."

The road to economic and social salvation, according to Grant, is through growth, innovation and aspirations. He's a fan of public/private sector partnerships, of good dialogue between academia, politicians and business, and of the balanced scorecard. "To me, the notion of exceptionally successful business is entirely consistent with having the best-nourished, best-looked-after employees and making a positive contribution to the community. I just don't agree that there have to be trade-offs between those things."

Too many Kiwis have modest, comfortable dreams, he believes. "When you talk to a lot of entrepreneurs there's a glass ceiling around $4 million. They only want to create a $4 million business because that's what buys the boat and the beach house. In the US people ask, 'Okay, now I've been successful, how am I going to be significant?'"

As a nation, we need to think big. "We shouldn't be setting a 4% growth rate, it should be 5% or 6% if we're going to create the sort of health and education system that's going to compete with Australia and other places. "I worry that too often in New Zealand we set the bar too low."

McKinsey facts

- Founded in 1926 by James McKinsey, a former accountancy professor at the University of Chicago
- Marvin Bower, who drove the firm after McKinsey's death in 1937, believed the firm should only take on engagements when the value to the client exceeded the fee
- Annual revenue in 2000 was $US 3.4 billion
- It has 84 offices in 44 countries
- It consults to two-thirds of the Fortune 1000
- It rates as the preferred employer among MBA graduates from the world's top 35 business schools
- The New Zealand office was established in 1998.