

Change and Leadership at Semco

Semco is one of the most interesting companies on the planet. There are no job titles and no personal assistants. People set their own salaries. Everybody shares in the profits.

That sounds like a recipe for disaster, or at least chaos, but Semco has grown consistently for the last twenty years despite being located in one of the most volatile economies in the world. The story of Semco and its majority shareholder, Ricardo Semler, is often told something like this.

"... his father handed him control of the family's small Brazilian company, Semco, a maker of industrial machinery. Faced with disastrous performance, Semler (at age 22) responded radically. He fired most of the top managers and got rid of most management layers; there are now three. He eliminated nearly all job titles. There's still a CEO, but a half-dozen senior managers trade the title every six months, in March and September. Executives set their own pay, and everyone in the company knows what everyone else makes. All workers set their own hours. Every employee receives the company's financial statements, and the labour union holds classes on how to read them. Workers choose their managers by vote and evaluate them regularly, with the results posted publicly." (*Fortune*, 26 November 2001)

That makes it seem like what Semco did was based on a clear change strategy, and that managers can follow a similar change strategy with similar results. However, upon deeper reflection and a closer look at what actually happened perhaps the story is more complex.

Ricardo Semler's father, Antonio Curt Semler, an Austrian-born engineer, founded Semco in 1953. The company he founded was a fairly typical South American company for the time. It was rigidly hierarchical and patriarchal and it had a rule and a policy for just about everything. The company manufactured several products, but was known for its marine pumps. Ninety percent of the sales were to the Brazilian shipbuilding industry.

Ricardo joined the company at age 19. He thought the company was too reliant on one industry. So Ricardo recommended diversification. His father refused. Ricardo thought the company was too rigid. His father disagreed. Ricardo thought the company needed better financial practices. His father thought otherwise.

That's where things might have stood for some time, except that recession came to Brazil in the early 80s. It hit Semco especially hard. Ricardo threatened to quit unless he got his way. His father gave in and young Ricardo became Semco's CEO. One of his first official acts was to fire two-thirds of the top management, many of whom were his father's friends.

Ricardo set to work designing and implementing a diversification strategy and changing the way business and planning were done. In the beginning this was done in the traditional way. Reports and manuals and controls replaced management discretion. He wanted to re-organise Semco into something resembling a matrix structure. None of this was easy as these were major changes and people argued about why they were necessary. Finding cash

and business to keep the company afloat during the process was also difficult. Ricardo was soon working the kind of schedule he'd told his father he didn't want. There was nothing but business, all day, every day. Something had to give and it turned out to be Semler's health.

He began having fainting spells and other problems. A doctor told him that he had the highest level of stress the doctor had ever seen in a twenty-five year old. Semler decided to change. He started by leaving the office at seven PM every evening, no matter what.

In 1985 one of his managers suggested to Semler that he should create self-managed teams of six to eight production workers who would be entirely in charge of all aspects of production. They set their own budgets and production goals. Compensation was then tied to budget and production performance. Costs went down. Productivity and profits went up.

Semler liked that. Many production workers liked that. Others were leery of taking on what they saw as "management" responsibility. It was the middle managers that didn't like the new concepts. They felt they were losing their power and prerogatives. In a little over a year, one third of them quit.

Now Semler added profit sharing, but with a twist. In Semco's system, workers received about a quarter of the net profits from their division. The twist involved how the profits were distributed. At Semco a democratically elected committee was responsible for designing the program and for allocating the profit-sharing funds. Things looked like they were stabilising, but then Brazil's President Collor instituted regulations that limited access to liquid capital. A severe recession was the result and Semco was in trouble again.

The company cut costs in just about every area until there was no alternative than to either layoff staff or impose salary cuts. The problem with layoffs was that Brazil's labour law required that every dismissed worker receive two years' worth of severance pay, something Semco could not afford.

Then a worker's committee approached Semler with a proposal. They'd take a pay cut, but with three conditions. First, the profit-sharing percentage would be increased until salaries could be restored. Second, management would take a forty percent cut in salary. And, third, the workers would get the right to approve all expenditure. Semler agreed.

In the plants, workers started handling multiple job duties and using their knowledge of how the factory worked to come up with new procedures that saved time and money. At one factory they divided themselves into three manufacturing units of about 150 people each. Each unit had complete responsibility for manufacturing, sales, and financial management. The new Semco was being born.

The autonomous team idea was adopted throughout the company. As it evolved the teams began hiring and firing both workers and supervisors by democratic vote. Policy manuals disappeared to be replaced by a policy of common sense. However, there is an actual

manual. It runs about twenty pages and is filled with cartoons and brief statements of principle.

One more change had to be completed in order to create the Semco of the 21st Century. In the late 80s a group of engineers had received permission to become what was called the Nucleus of Technological Innovation. The idea was that they, and a group of workers, would become fully autonomous. In effect they were seeking to extend the autonomous team concept to a larger group.

Effectively the group would operate entirely on its own, though with the same culture as Semco. Their performance would be reviewed every six months. They took a percentage of sales as compensation. That model, essentially extending the autonomous teams, eventually became the model for all of Semco. Today's Semco doesn't have a traditional management hierarchy or typical organisational chart, or even a matrix or lattice management structure. The company is effectively made up of autonomous, democratically run units. The model of organisation is that of concentric circles.

At the centre are the Counsellors, including Ricardo Semler. There are six of them and a different one takes the CEO job every six months. They deal with general policy and strategy, overall financial results, and work to inspire the Partners who make up the second circle. Partners are six or seven leaders from each of Semco's divisions. Everyone else is an Associate. Some Associates also work as team leaders. Semco has no receptionists, secretaries or any personal assistants. Associates set their own salaries, which are publicly posted and worked into the budgets. All meetings are open to any Associate who wants to attend. Financial information is available to anyone who wants to see it and courses are available to help them understand what they see.

The story of Semco and Ricardo Semler is one about how change happens, how to adapt to changing environments and what a truly living company looks like.

There have been two kinds of change at Semco. The major organisational changes took twenty years to become reality and not one was the result of any sort of master plan. Instead, the big changes were driven by crisis such as financial hard times or Semler's stress-related illness. With very few exceptions most of the dramatic ideas came from someone other than Ricardo Semler. His genius has been in holding to a general concept of empowerment and allowing and supporting changes that could easily have been viewed as taking away his power.

There are two models for the kind of changes we have seen at Semco. One is the biological model of punctuated equilibrium. Things go along fairly smoothly with minor changes, then there is a sudden burst of change and things settle down again. The other model comes from chaos theory. In chaos theory major change happens when an organism faces a threat that moves it away from equilibrium and stability, and out toward the edge of chaos.

The major changes at Semco over the last two decades of the twentieth century created a company that remains a confederation of small, freestanding units. That "structure" is part of why Semco can adapt so quickly today to deal with threats or to seize opportunities.

Semco's units are limited to 150-200 people, the magic number in sociological, management and anthropological studies. It's the largest group that a human being can feel a part of and that can create a social context that affects behaviour. Having a small group makes it easy to spot a threat or opportunity, figure out what to do, and swing into action. Above this size you need formal processes to get this done, below this size it becomes a natural function. It's those processes that slow down big businesses and make smaller businesses nimble. Semco is really less a single large company with more than a thousand employees than it is a bunch of smaller companies who can see, process and react quickly to changes in the environment. And who all operate with the same values, philosophy and culture.

Ricardo Semler noted that "Semco's ongoing transformation is a product of a very simple business philosophy: give people the freedom to do what they want, and over the long haul their successes will outnumber their failures. It's a system that puts a lot of weight on leaders because then can no longer simply protect themselves with symbols of power like closed offices or special parking places. They have to rely exclusively on their ability to generate respect."