

HARVARD BUSINESS SCHOOL PRESS

# LOYALTY RULES!

HOW TODAY'S LEADERS  
BUILD LASTING RELATIONSHIPS

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## Timeless Principles



Loyalty, the key to success in today's economy? Be serious! What relevance could such a quaint, old-fashioned notion hold for a world in which customers defect at the click of a mouse and impersonal shopping bots scour databases for ever better deals? What good is a small-town virtue amid the faceless anonymity of the Internet's global marketplace? Loyalty must be on a fast track toward extinction, right?<sup>1</sup>

Wrong. Chief executives at the cutting edge of e-commerce—from Cisco's John Chambers to eBay's Meg Whitman, from Dell Computer's Michael Dell to Intuit's Scott Cook—care as deeply about customer retention as does any top-notch bricks-and-mortar executive, and consider it vital to the success of their online operations. Whitman reports, "Loyalty is the primary ingredient in eBay's secret sauce." Web-savvy leaders know that loyalty is an economic necessity; acquiring customers on the Internet is enormously expensive, and unless those customers stick around and make lots of repeat purchases over the years, profits will remain elusive. And they know it's a competitive necessity; in every industry, some company will figure out how to harness the creative potential of the Web to create exceptional value for customers, and that company is going to lock in many profitable relationships at the expense of slow-footed rivals. Without the glue of loyalty, even the best-designed e-business model will collapse.

But that's *customer* loyalty. We all know that *employee* loyalty is another story. It takes a typical Silicon Valley firm only two years to lose half its employees. With the new economy's surge in job hopping and career surfing, how can any company hope to hold on to its workers? And how about supplier loyalty? The burgeoning Internet-based auctions, which blow apart traditional supply-chain relationships, seem to make loyalty all but irrelevant. Investor loyalty? Online trading has accelerated investor annual

churn rates toward 100 percent. Employee, supplier, and investor loyalty—all must be anachronisms of the digital economy.

Wrong, wrong, and wrong again. Customer loyalty hinges, as it always has, on committed teams of high-caliber employees and suppliers, which in turn require a core of owners committed to building an enduringly successful enterprise. The challenge of building loyalty has indeed stiffened as the new economy has blossomed and presented enticing alternatives for customers, employees, and the whole range of business partners. But along with the enormous potential of the new economy have come increased risk and volatility. In this environment, it's become clear that loyalty is an even more vital asset for success in the age of the Internet. Building loyalty has in fact become the acid test of leadership.

It's a test that most leaders are flunking. Fewer than half of all employees of U.S. companies now consider their employer to be worthy of loyalty.<sup>2</sup> Bemoaning the decline in loyalty, leaders fault the Internet, rapid changes in technology, shifting government regulation, cutthroat competition, fickle customers, and greedy, short-term investors. Some have concluded that loyalty is no longer relevant in modern society, where self-interest sets the tone for employer-employee relations. But they are kidding themselves. People yearn now more than ever for leaders and institutions worthy of their trust and commitment—to help guide and enrich both life and work. When business leaders observe diminished loyalty in the people around them, it is not because a confusing new economy has robbed loyalty of all relevance, but rather because the core principles embodied in their leadership have proven unworthy of loyalty.

## THE CASE FOR LOYALTY

Loyalty remains the hallmark of great leadership. It provides a far more exacting standard for leadership excellence than do the profits demanded today by impatient shareholders. The long-term rewards of loyalty ultimately outstrip even the most spectacular short-term profits. We are not, however, talking about a trade-off between loyalty and long-term profits. After all, what kind of customer, or supplier, or dealer, or employee would cast his or her lot with a leader who could not offer outstanding financial potential? Loyalty obviously demands superior profits, but it demands

more. It requires that those profits be earned through the success of partners, not at their expense. Loyalty can be earned only when leaders put the welfare of their customers and their partners ahead of their own self-serving interests.

Herein lies the essential paradox of business loyalty. If loyalty is really about self-sacrifice—that is, about putting principles and relationships ahead of immediate personal financial gain—what relevance can it possibly hold for business, which is in large part driven by the pursuit of self-interest?

Too few managers can answer this question coherently. They have convinced themselves that maximizing shareholder value provides the sole principle for successful business practices, and that through faithful commitment to this principle, they have fulfilled their professional and ethical obligations to partners. In reality, though, these leaders are confusing profits with purpose. Whether they know it or not, they have abandoned what I'll call the “high road” of business practice. A single-minded focus on financial results will not create the conditions for loyalty or long-term success, and it may well lead an organization down a slippery slope to the “low road.” On the low road, where money matters more than people, it becomes standard practice to take advantage of customers, employees, vendors, and a host of other business associates whenever they are vulnerable. Here, the goal of strategy is to create market power; the job of leaders, to utilize that power to strangle competitors, bully vendors, intimidate employees, and extract maximum value from customers—all in faithful duty to shareholders, whoever those shareholders happen to be this month. In this Darwinian struggle, only the toughest individuals survive, and trust is a weakness to be exploited.

Low-road strategies can generate impressive financials, for a time, and buoyant earnings and stock price provide the necessary bribes required to keep followers committed. Eventually, however, the low road leads to trouble. There will come a time when the firm gets blindsided by a competitor, or fails to anticipate a shift in market preferences, or discovers that a new technology has made its business model obsolete. And then, the true value of loyalty will become apparent. When profits inevitably get squeezed and stock price plummets, the company can no longer fund the bribes. Yet somehow, leaders must rally their partners to fight rather than switch; customers, employees, dealers, and suppliers must bind together and find a

solution. Unless leaders have built relationships based on loyalty—loyalty to something more fundamental than today’s earnings or stock price—then nothing will keep partners from jumping ship the instant a better opportunity comes along.

Many executives have confused employees, vendors, dealers—and even themselves—about the relationship between treating people right and financial success. The idea that the sole purpose of business is to generate profits, or that maximizing shareholder value matters more than treating people with dignity and respect, is absurd. Yet these common misperceptions are no more absurd than their mirror images. It is equally absurd to think that businesses can treat people right without achieving outstanding financial results, or that adhering to high standards of decency and consideration is somehow inconsistent with maximizing growth and profits.

There is indeed a high road in business, and it is the only road to lasting success. If you hope to lead others successfully or for very long, you must break through the widespread disillusionment and confusion by demonstrating that your leadership is founded on principles worthy of loyalty; principles that will inspire commitment among customers, employees, and investors; principles that cultivate partner growth and prosperity, not simply your own profits. You must show all your partners—including shareholders—how these principles create the most solid foundation for financial excellence and sustained success.

Wishful thinking? Read on, and you’ll find plenty of examples of successful loyalty leaders who can serve as practical role models for your journey along the high road. What’s their secret to building loyalty in this increasingly volatile environment of the new economy? Well, for starters, they understand the enormous value of loyalty, so they measure it.

## **MEASURING LOYALTY**

### THE LOYALTY ACID TEST

Climbing to the high road requires the right tools—in particular, tools to measure loyalty as carefully as profits. Satisfaction metrics are a good first step, but don’t stop there. Satisfaction, a fleeting attitude that lacks durable staying power, is a poor substitute for loyalty and sets far too low a standard

of excellence. Far better than satisfaction scores are measures such as customer and employee retention rates—real behaviors with real financial consequences. But even retention rates don't tell the whole story. Sometimes customers stick around simply because they aren't aware of alternatives or because they are hostage to long-term contracts. Some employees stay put only because they lack ambition or other options.

Loyalty is the gold standard for measuring the quality of a relationship. True loyalty endures through the best of times and the worst and melds mutual interests into shared goals. Are your relationships with your partners worthy of their loyalty? You have to ask them. This is precisely what many of our model loyalty leaders have done—they have taken the acid test, applying what I call the Loyalty Acid Test Survey (see appendix) to hundreds of their customers and employees.

The Loyalty Acid Test Survey is a relationship report card specifically designed to help leaders evaluate and strengthen key relationships. A handful of “loyalty leader firms” (firms that have achieved the highest level of loyalty in their segment) beta-tested this tool, with some striking results. They discovered, for example, that between 70 and 75 percent of their employees agreed with the statement “I believe this organization deserves my loyalty.” Though the firms are not satisfied with this result and are taking steps to improve, they fully appreciate their relative advantage. Exhibit 1–1 compares the plight of the average U.S. company with the initial loyalty leader results. From a representative national sample of over 2,000 employees, only 45 percent agreed that “I believe my organization deserves my loyalty,” and 32 percent were neutral. The worst news, however, is that 23 percent actively disagreed.<sup>3</sup>

Consider the predicament faced by leaders of firms on the lower end of the loyalty scale. They would like their customers to be loyal, but meanwhile, unbeknownst to the leaders, most of their own employees are not at all convinced that the company deserves loyalty. How the employees treat customers in their daily interactions will almost certainly convey their misgivings. Unless management teams measure and analyze organizational loyalty with a tool like the Loyalty Acid Test Survey, they are operating in the dark. Chances are, their energy is misdirected and resources are allocated to fix symptoms rather than root causes.

To build superior loyalty, you need an analytical framework and tools

**Exhibit 1-1**

## THE LOYALTY ACID TEST: EMPLOYEES

**“I believe this organization deserves my loyalty.”**

Agree
  Disagree

45%

22%

**U.S. Average**

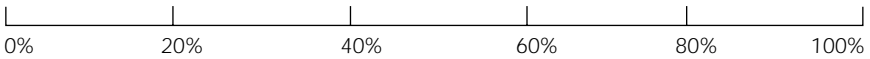
72%

9%

**Loyalty Leader Sample**

?

?

**Your Company**

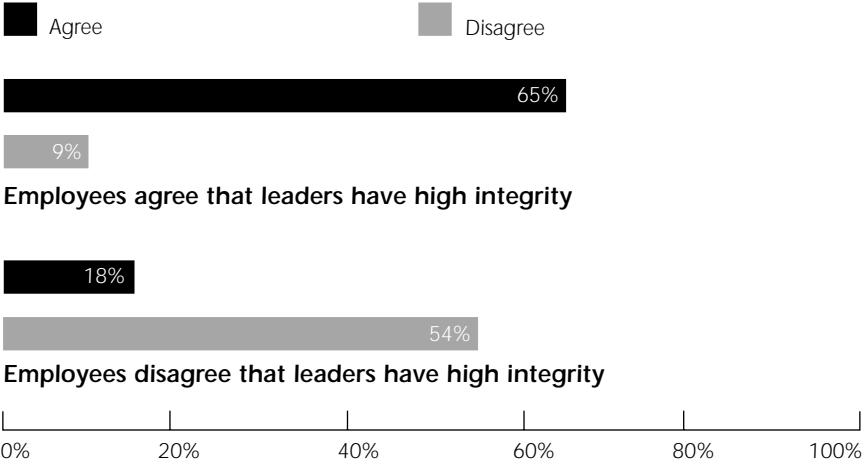
to analyze and strengthen key relationships. The Loyalty Acid Test Survey is designed to help you prioritize your challenges and create an effective game plan for maximizing the loyalty of your business partners. Adaptations for employees, customers, suppliers, dealers, and investors can be downloaded from the Web. You will also find instructions for comparing your results with the most up-to-date loyalty leader benchmarks cataloged on our Web site, [www.loyaltyrules.com](http://www.loyaltyrules.com), the unique source for this data.

So what do these numbers and the years of research tell us? How do the best companies earn such an impressive loyalty advantage? The answer begins with a single insight. The center of gravity for business loyalty—whether it be the loyalty of customers, employees, investors, suppliers, or dealers—is the personal integrity of the senior leadership team and its ability to put its principles into practice. Consider the evidence displayed in exhibit 1–2. Of the 1,057 employees surveyed who agreed that “senior leaders of this organization are people of high personal integrity,” 63 percent

### Exhibit 1-2

IMPACT OF LEADERSHIP INTEGRITY: NATIONAL SAMPLE

**“I believe this organization deserves my loyalty.”**



agreed that “I believe this organization deserves my loyalty.” Of the 444 who disagreed that their senior leaders had high integrity, only 19 percent considered their organization worthy of loyalty. As you will see in the pages ahead, the rules for building loyalty in the new economy are essentially the same rules that have always created loyalty. Timeless principles of integrity such as truth, fairness, and responsibility continue to create the gravitational core for organizational loyalty. Indeed, their validity and importance have only increased in the age of the Internet.

## THE HIGH ROAD AND THE INTERNET

Although the Internet has accelerated churn in many sectors of the economy, leaders who understand the basis of true loyalty recognize it as a powerful tool for strengthening relationships. Indeed, the electronic market space is a most hospitable environment for high-road strategies. By directly linking companies with their suppliers and customers, the Web can dramatically deepen relationships and effect enormous efficiencies. But little of this potential can be realized unless these relationships enjoy a high level of trust. For customers on the Web, where business is conducted at a distance



and risks and uncertainties are magnified, trust is more important than ever. Online customers can't look a sales clerk in the eye, can't size up the physical space of a store or an office, and can't see and touch products. They have to rely on images and promises, and if they don't trust the company presenting those images and promises, they'll shop elsewhere. In fact, when Web shoppers were asked to name the attributes of e-tailers that were most important in earning their business, the number one answer was "a Web site I know and trust."<sup>4</sup> All other attributes, including lowest cost and broadest selection, lagged far behind. Price does not rule the Web; trust does.

When customers do trust an online vendor, they are much more likely to share personal information. This information enables the company to form a more intimate relationship with customers and to offer products and services tailored to their individual preferences, which, in turn, further increases the level of trust and strengthens the bonds of loyalty. Such a virtuous circle can quickly translate into a durable advantage over competitors.

The story is much the same for integrated supply-chain relationships. Unless firms are comfortable engaging in highly transparent relationships and sharing internal information, including costs and profit budgets, with their partners, little benefit can be achieved through reduced inventory levels, coordinated scheduling, or joint planning. Open, transparent relationships work only when both sides are committed to mutual success.

In addition to rewarding trust generously, the Internet opens new opportunities to build trust. Everyone knows, for example, that communities flourish on the Web. Less understood is how the trust built up in such communities can be transferred to the companies that host them. Here, eBay provides a great example. In the past, fears about reliability and fraud prevented the exchange of used merchandise between strangers from developing into a big business. But eBay used the unique capabilities of the Web to establish and enforce the rules of engagement. Buyers and sellers rate each other after each transaction, and the ratings are posted on the site. Every member's reputation thus becomes public record. Although there are still kinks to be worked out—linking screen names to specific individuals, for example—progress to date has been astonishing. In a sense, eBay is using the Internet to bring small-town rules of trust to the most challenging of markets—a global network of strangers.

The Internet not only creates communities, but speeds the search for

truth. In the past, convenient store locations, aggressive sales forces, and a general lack of information shielded companies from the penalties of providing anything less than the best product and service quality; customer inertia was mistaken for loyalty. Thanks to the Internet, however, those shields have been dismantled. Through chat rooms and online ratings services, customers can check companies' reputations and results and share referrals instantly by copying e-mails to dozens, or thousands, of associates. They can compare supplier price and quality in real time, all the time. Winners in the new economy will welcome—and benefit from—the unprecedented level of candor characterized by the high road.

## **SUSTAINABLE ECONOMIC ADVANTAGE**

One of the greatest challenges confronting players in the new economy lies in building the kind of sustainable economic advantage necessary to deliver superior results. Not so long ago, this challenge manifested itself in the relatively straightforward goal of building structural cost advantages, which could be expected to yield a competitive edge for decades. Today, a company like IBM is displaced by Compaq, which is then leapfrogged by Dell Computer, all in the period of a few short years. Winning business models deteriorate quickly as core elements in the value chain shift and evolve. Shifting alliances and outsourcing arrangements reshuffle competitive positions. Since nearly limitless information is readily available through the Internet, competitive strategies are easier to decipher and to copy. Proprietary data and processes are more difficult to protect. Not only is information flowing more readily from company to company, so are employees. Witness the executive search business, which has mushroomed from a cottage industry to more than \$10 billion in annual fees.

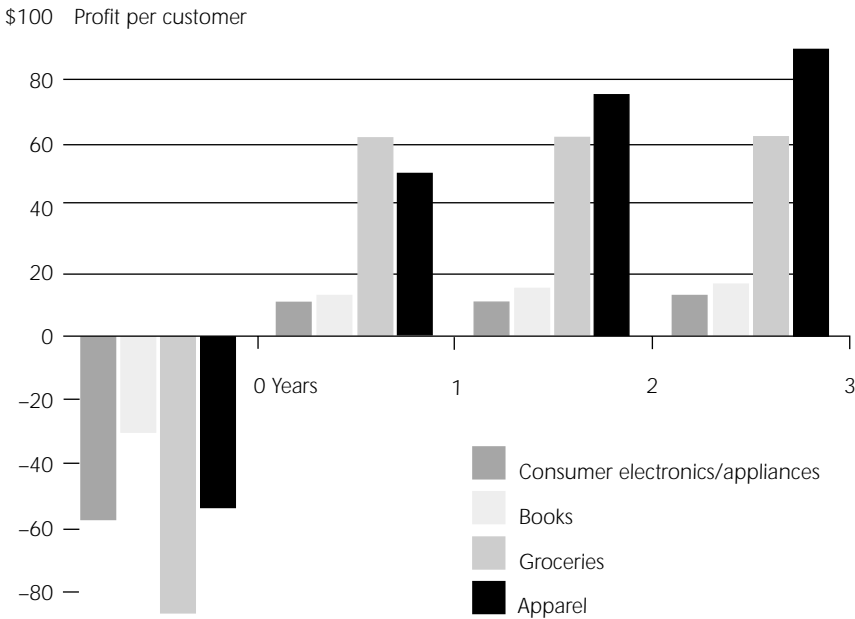
Quite likely the only possible source of sustainable competitive advantage in the new economy will be the bonds of loyalty you generate. If this strategy seems like an uphill battle in today's environment, remember that sustainable advantage means outperforming your competitors. Although defection rates across your industry may be climbing, you need to build relationships that are stronger and more enduring than your competitors'. However small the advantage, it will compound into substantial economic benefits as you grow.

In my previous book, *The Loyalty Effect*, I documented the outstanding financial results generated by leaders who can build a measurable advantage in loyalty.<sup>5</sup> By dissecting the microeconomic forces that link loyalty to profits, we explained the enormous growth and cost advantages of loyalty. We showed that in industry after industry, the high cost of acquiring customers renders many customer relationships unprofitable during their early years. Only in later years, when the cost of serving loyal customers falls and the volume of their purchases rises, do relationships generate big returns. The bottom line is this: An increase in customer retention rates of 5 percent increases profits by 25 percent to 95 percent. Those numbers startled many executives, and the book set off a rush to craft retention strategies, many of which continue to pay large dividends.

When my colleagues at Bain and I applied the same methodology to analyzing customer life-cycle economics in several e-commerce sectors—including books, apparel, groceries, and consumer electronics—we found classic loyalty economics at work. In fact, the general pattern of early losses followed by rising profits is exaggerated on the Internet (exhibit 1–3). At the beginning of a relationship, the outlays needed to acquire a customer are often considerably higher in e-commerce than in traditional retail channels. In apparel e-tailing, for example, new customers cost 20 percent to 40 percent more for pure-play Internet companies than for traditional retailers with both physical and online stores. That means that the losses in the early stages of relationships are larger.

In future years, though, profit growth accelerates at an even faster rate. In apparel e-tailing, repeat customers spend more than twice as much in months 24–30 of their relationships as they do in the first six months. And since it is relatively easy for Web stores to extend their range of products, they can sell more and more kinds of goods to loyal customers, broadening as well as deepening their relationships over time. The evidence indicates, in fact, that Web customers tend to consolidate their purchases with one primary supplier to the extent that making purchases from the supplier's site becomes part of their daily routine. This phenomenon is particularly apparent in the business-to-business sector. For example, W. W. Grainger, the largest industrial supply company in the United States, discovered that longtime customers whose volume of purchases through Grainger's traditional branches had stabilized increased their purchases

**Exhibit 1-3**  
CUSTOMER LIFE-CYCLE ECONOMICS IN E-COMMERCE



Source: Bain & Company and Mainspring data as illustrated in Frederick F. Reichheld and Phil Scheffer, "E-Loyalty: Your Secret Weapon on the Web," *Harvard Business Review* (July–August 2000): 107. Reprinted by permission.

substantially when they began using Grainger’s Web site. Sales to these customers increased at three times the rate of similar customers who used only the physical outlets.

In addition to increasing their own purchases, loyal customers also frequently refer new customers to a supplier, providing another rich source of profits. Referrals are lucrative in traditional commerce as well, but, again, the Internet amplifies the effect since word of mouse spreads even faster than word of mouth. Online customers can, for example, use e-mail to broadcast a recommendation for a favorite Web site to dozens of friends and family members. Many e-tailers are now automating the referral process, letting customers send recommendations to acquaintances while the customers are still in the e-tailers’ sites. Because referred customers cost so little to acquire, they begin to generate profits much earlier in their life cycles.

One e-commerce leader reaping the economic benefits of referrals from loyal customers is eBay. More than half its customers arrive through referrals. “If you just do the math off our quarterly financial filings,” CEO Meg Whitman has told the *Wall Street Journal*, “you see that we’re spending less than \$10 to acquire each new customer. The reason is that we are being driven by word of mouth.”<sup>6</sup> eBay has even found that the costs of supporting referred customers are considerably lower than those for customers brought in through advertising or other marketing efforts. Referred customers tend to use the people who referred them for advice and guidance rather than calling eBay’s technical support desk. In effect, loyal customers not only take over the function of advertising and sales, but even staff the company’s help desk—for free!

The combination of all these economic factors means that the value of loyalty is often even greater on the Internet than in the physical world. For any company doing business on the Web, the implication is clear: You cannot generate superior long-term profits unless you achieve superior customer loyalty. Moreover, the increased speed of change, the need for flexibility in individual roles and team structures, and the cutthroat war for talent have further intensified the need for employee loyalty. By loyal employees we mean more than those who simply show up and obediently carry out your commands. True employee loyalty includes responsibility and accountability for building successful, mutually valuable relationships. Finally, the ever-increasing need for loyal and committed suppliers, dealers, and investors increases as the Internet creates the opportunity—indeed, the competitive imperative—to build a more integrated network of relationships.

This emerging model of competitive excellence and sustainable economic advantage can be achieved only through more transparent and trustworthy partnerships within communities of mutually beneficial relationships. There has never been a more propitious time for leaders committed to the principles of loyalty.

## FINDING THE RIGHT ROLE MODELS

Where should you look for practical examples of loyalty leadership in the new economy? It might be tempting to turn to some of today’s highfliers. Isn’t their success proof of their leadership excellence? A word of caution

is in order here. Many of the Internet's putative business superstars have not yet demonstrated that they can generate profits, let alone weather the tough times that test the loyalty of customers and partners. Many digital-era savants are now closer to bankruptcy than to the billionaire status that was fleetingly theirs. Even those who survived the dot-com meltdown of the late 1990s may never live up to the lofty expectations of media pundits or the stock market.

Look instead to organizations whose exemplary track records of customer and employee retention have endured throughout the good times and the bad. Look to organizations with long track records of integrating technological innovations, including the Internet, into their core business in order to build stronger relationships. Look to organizations whose leaders have consistently put the interests of customers, employees, and their other business partners ahead of their own. Look to organizations such as the following:

- Harley-Davidson, which recovered from near bankruptcy in the 1980s by building mutually beneficial relationships, based on simple core values, with all stakeholders. Returns to investors have ranked among the top-tier returns of all public companies, and despite Milwaukee's tight employment market, a long line of applicants awaits job openings at Harley.
- Enterprise Rent-A-Car, which raced past Hertz and Avis to become the largest car rental firm in North America. It continues to grow at more than 20 percent per year in an otherwise sluggish industry. With over 45,000 employees, the company manages to hire more college graduates than does any other firm in the United States by putting the interests of customers and employees ahead of those of the owners.
- The Vanguard Group, the mutual fund industry's growth leader. The organization built its \$550 billion in assets under management by putting long-term investment returns to its customers first. With more than 40 percent of transactions now on the Web, Vanguard maintains the lowest costs and the highest customer retention rates in its industry.
- Southwest Airlines, the only consistently profitable major airline in the United States for every year since 1973. The airline has employee turnover rates of 4 to 5 percent, in an industry with rates typically double that. In the notoriously cyclical airline business, Southwest has never had a layoff. With the lowest ticket prices, the company still ranks at the top in customer service and safety.

- Dell Computer, which so effectively utilized the Internet to revolutionize the sales and production of personal computers that it has become the global market share leader. By focusing on building the most valuable customer experience, Dell has made itself the profit leader.
- Cisco Systems, whose employee turnover ran less than 10 percent during the 1990s although it is headquartered in Silicon Valley, where turnover averaged 25 to 30 percent. Not only does every employee carry an ID badge embossed with the company values, but all bonuses are dependent on meeting customer satisfaction goals.
- Northwestern Mutual, the company that has consistently focused on creating superior value for its policyholders. The “Quiet Company” has so successfully parlayed its superior customer retention into lower costs and faster growth that it can no longer be categorized as a high-end niche player; it is the industry leader in individual life insurance.
- MBNA, the only credit card company that considers customer retention so important that it reports the statistic in its annual report. The company retains 97 percent of its profitable customers.
- Chick-fil-A, whose store operator turnover runs 5 percent, compared with the competition’s 35 to 40 percent. Founder Truett Cathy has so effectively marshaled loyalty effect economics that he can afford to let his operators earn compensation double or triple industry averages, while still generating sufficient cash to grow the chain while remaining a private company.
- SAS, the leading statistical analysis (e-intelligence) software firm, whose 5 percent turnover rate among software engineers compares with the industry’s average of more than 20 percent. By hiring the right kind of people and providing them with a career and lifestyle that reinforce work-family balance (employees enjoy free health care and child care), SAS is building an institution in a notoriously fickle market space.
- USAA, the preeminent insurer of military personnel and veterans, whose customer turnover is so low that the primary root cause of defection is death. USAA’s top management believes so strongly in the importance of customer retention that the managers base their own bonuses on this metric. USAA demonstrates how customer loyalty and employee loyalty go hand in hand; the firm’s telephone staff turnover runs 9 percent, compared with more than 20 percent for the industry.

- The New York Times Company, where customer retention is tracked as carefully as profits, and where retention performance (above 90 percent) stands head and shoulders above the rest of the newspaper competition, which churns readers at rates of 25 to 50 percent.
- U.S. Marine Corps, the only branch of the U.S. military that has managed to meet its staffing targets—primarily because of superior recruiting and retention success. Rather than dropping standards to meet staffing demand, the Marines constantly raise them. The Corps' motto, *Semper Paratus*, helps convey to outsiders the central role that loyalty plays for the Marines.
- Intuit, the leader in personal financial software, whose employee turnover runs half the Silicon Valley average. Intuit has weathered several storms, including a blocked merger with Microsoft and a fundamental shift in its business model from shrink-wrapped software to the Internet by remaining loyal to its founder's values.

The list goes on, but the stories all have the same refrain. Loyalty is not dead. It rules the new economy—just as surely as it ruled the old. Leaders who grasp its true nature and economic potential understand that loyalty cannot be a one-way street. They earn people's loyalty when they treat them in a manner that inspires their trust and commitment. Model leaders understand both the short-term costs and the superior value of long-term investing in human capital, of attracting and retaining a select business team. They know that when you treat people with dignity and respect, communicate honestly, help people discover their full potential by guiding them into roles that play to their special strengths, and strive to create and nurture mutually beneficial partnerships, then you will become a leader worthy of trust and commitment and your business will thrive.

Partnerships must adhere to the rules of loyalty, or they will become nothing more than unstable, self-serving alliances. True partnerships must be driven by mutual caring, respect, responsibility, accountability, and growth. In a true partnership, each individual must willingly put the success of the relationship ahead of short-term, personal gain. And, of course, for each partner to prosper in the long term, the entire system of relationships with employees, dealers, vendors, and investors must successfully create value for the ultimate customer. Each individual must be willing not only to put the partner's interests ahead of his or her own, but also to make the interests of the final consumer the highest priority.



An impossible challenge? How can one inspire such self-sacrifice in an organization composed of ordinary mortals conditioned to follow the compass of their own self-interest? As you will see, this kind of selfless generosity is both sensible and practical, but only when leaders fulfill their responsibility. It makes sense when leaders select the right partners and guide them into roles in which they can contribute and receive real value. Leaders must also ensure that individuals are fairly rewarded for the collective success they help to create. When people trust that in the long run the success of their partners will drive their own personal success, then they can logically and wholeheartedly commit themselves to the service of others.

To earn this trust, leaders must demonstrate far more than good intentions. They must demonstrate the wisdom, discipline, courage, and commitment to ensure mutual accountability and responsibility from every partner. Only with strong leadership can relationships be restructured according to a set of principles that regularly rewards those who consistently treat others right. Leadership is indeed the key to transforming business relationships into something far greater and more powerful than the mutual pursuit of greed and self-interest. Only outstanding leadership can transform common business relationships into real partnerships truly worthy of loyalty.

The leaders profiled in this book prosper because they have built and nurtured just such a network of loyal partnerships—and they have helped those around them do the same. Because their personal integrity sets the standard, and because their own loyalty to core principles never wavers, these leaders inspire the mutual pride, trust, and commitment that bind people together even in times of turbulence and adversity. Think about it. Wouldn't you feel proud to be part of an exclusive team renowned for taking the high road? Wouldn't you remain loyal to a leader who dedicated both time and money to helping you achieve your fullest potential, and who cared more about building and maintaining loyal relationships than about his or her own bank account? Why would leaders be so generous? Out of charity?

Loyalty leaders do not act out of charity. In fact, their records show that they have prospered magnificently. Most of those profiled in this book will retire with a personal net worth in the tens or hundreds of millions; a handful have already become billionaires by devoting themselves to their partners' success and by inspiring others to follow suit. They know that their efforts to make their employees and customers worthy partners, and to align interests and share rewards, will ultimately lead to their own success and prosperity. These leaders have earned stellar loyalty credentials because they

have discovered how to create a network of mutually beneficial relationships that both build, and are sustained by, loyalty—to one another, to the firm, and, even more importantly, by commitment to a shared set of values and principles we call the *principles of loyalty*.

## THE SIX PRINCIPLES OF LOYALTY

The six principles of loyalty encompass standards of excellence, simplicity, honesty, fairness, respect, and responsibility. But they are not idealized abstractions far removed from the routine operations of the workaday world. On the contrary, they are embodied in simple, straightforward actions that drive measurement systems, compensation, organization, and strategy:

**1. Play to win/win**

Profiting at the expense of partners is a shortcut to a dead end.

**2. Be picky**

Membership is a privilege.

**3. Keep it simple**

Complexity is the enemy of speed and responsiveness.

**4. Reward the right results**

Worthy partners deserve worthy goals.

**5. Listen hard, talk straight**

Long-term relationships require honest, two-way communication and learning.

**6. Preach what you practice**

Actions often speak louder than words, but together they are unbeatable.

After extensive research and analysis, my colleagues at Bain and I are convinced of the universal nature of these six core principles of loyalty. The model leaders in this book have put them to work in a wide variety of industries and situations that range from Silicon Valley start-ups to century-old institutions, from the highest to the lowest of technologies, from manufacturing to services, from small firms to large, and from public to private—and even to mutual—ownership. The leaders' backgrounds, personalities, and management styles range just as widely, from ferociously competitive former jocks to bookish introverts, from soft-spoken, grandfatherly counselors to fire-breathing table thumpers. But underneath such

differences, these leaders demonstrate a consistent pattern for shaping their business into a network of mutually supportive partnerships.

The principles of loyalty at first glance may seem so obvious as to be self-evident truths, but don't be fooled. Although these principles are timeless, they are also revolutionary. They reflect basic inner truths as well as fundamental economic realities that all too many leaders ignore at their peril. Those who truly understand and practice them are receiving Loyalty Acid Test Survey scores that put them on the honor roll. They are building track records comparable to the masters of loyalty-based leadership discussed throughout this book. Reading their stories will help you to understand more fully how these principles work in the real world, and to diagnose and strengthen your own relationships, with potentially revolutionary results.

The executives selected to be my exemplars remain steadfastly loyal to these principles. They know that their organizations cannot exist solely to maximize shareholder value, or solely to put customer interests first, or solely to be the best place for employees to work. Because loyalty leaders recognize that all these people must be well served if their loyalty is to be earned, they are committed to providing superior value across the board, and they pare away any impediments to this goal.

You will see the six principles of loyalty in action in the case studies that follow. First, however, we must highlight the single most important lesson that the executives we will study have to teach, a lesson derived from their concept of leadership and its intrinsic responsibilities. These executives all agree that the fundamental job of a leader is to be a role model, an exemplary partner whose primary goal is to help people grow to their fullest human potential. To build loyalty, they say, you must first be loyal to others by helping them build relationships on the right principles. Then, your leadership actions must not only reinforce these principles, but embody them.

When your associates see that you are faithful to the timeless principles of loyalty, then they will be loyal in return. And when they follow your example, when they begin to restructure their own network of relationships according to your model, when they begin to place the interests of their partners and customers ahead of their own, watch out! You will have initiated a chain reaction with breathtaking consequences. You will have unleashed the loyalty effect, the spiraling economic advantages that reward those who follow the high road.