

C H A P T E R

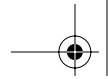
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AMERICA, YOU
HAVE A NEW
AIRLINE AND...A
NEW STANDARD
OF SERVICE



**FOR PUBLIC
RELEASE**





It was March 12, 1973. We had been working for years for this day—the first day of operations for Federal Express. We had 28 people selling in 10 cities since January 2, 1973. We had 23 executive jet airplanes (10 of which had been converted to freighters); hundreds of employees; a hub and World War II facilities in Memphis, TN; and no money.

Frederick W. Smith, the founder, had used all of his family's trust fund and incredible banking and leasing salesmanship to get us here, but that was all there was.

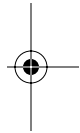
Fred Smith, myself, and others had traveled to New York and had appointments with venture capitalists all around the city the next day. Fred had seen most of these venture capitalists earlier, and they had told him to come back when we were in business. Now we were, and we were ready.

I was Senior Vice President of Sales and Customer Service. That meant setting up the pickup and delivery operation, along with the sales and service operations.

Each evening, for the past two and a half months, we had a conference call to review the results of the sales calls for the day, and we'd track the expected number of packages the first night. By mid-February, we were estimating as high as 3,000 packages for that first night.

The problem, at that level, was that our planes only held 300 packages each, and most of the 10 airplanes were contracted to the post office and other charter commitments. We could cancel contracts and deploy all 10 airplanes, but it would be very costly and risky if we didn't actually get 3,000 packages.

I decided that we'd better verify that the customer commitments were real. I started asking more specific questions and found out that sometimes salespeople lie, or at least tell you what you want to hear.





For example, one of the shippers from Memphis was a brick company that was supposed to give us 20 packages a day. I asked the salesperson why they were using an overnight service. “Are they going to ship samples to architects?” He replied, “No, they’re shipping bricks to the construction site.”

I knew we were in trouble. After nearly a week of probing, we had changed our estimate to 300 packages. This was perfect: two airplanes averaging 150 packages each at 50% capacity. We were off and running.

America, you have a new airline.

On that opening Monday night, the Memphis hub was alive with local and national TV, the *Wall Street Journal*, and local newspapers. It was the first new airline in America in 20 years, and certainly the first all-package airline ever. It was newsworthy stuff.

It was 10:00 p.m. on that Monday in March, and we had just arrived at the Yale Club in New York City. I called Memphis to get the actual package count and asked John Henry, “What’s the package count?”

“Are you sitting down?”

“Should I be?”

“Well, there’s good news and bad news,” he replied.

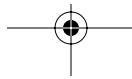
“Give me the good news.”

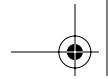
“Single digit—six packages.”

“John,” I replied, totally shocked, “what could possibly be the bad news?”

“Four were from salespeople testing the system. Only two from customers.”

Can you picture it? Dozens of people out in the middle of the night, the media, conveyors, spotlights washing WWII ramps and hangars with light. The first plane pulls up, the cargo door swings





open, and two pilots, each with a package in his hands, passes it to the awaiting throng—a throng expecting two full airplanes or at least half-full airplanes.

Back in New York, after getting the news, I walked down the hall to Fred Smith's room and knocked timidly. I told him the news, and we had a brief discussion about what we were going to do with the rest of our lives because this wasn't going to work.

The next morning Fred had recovered. As we settled into a taxi to begin our venture capital tour, he looked at each of us and said, "Fix bayonets. We're in the trenches now. Our dream is a reality. Let's make it happen."

There was such an incredible sense of commitment from Fred that we did a reasonable job of explaining why we had spent two and a half months with 28 salespeople to get two packages.

I say reasonable because we didn't get thrown out, nor did we generate any capital.

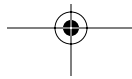
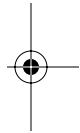
As we were riding to our first appointment, one of the attorneys said, "Take heart. The first night is always rough. You'll have dozens of packages by Friday." On Friday of that week, we had one package in the system. I calculated the cost of that package at about \$500,000 to deliver—a heck of a value to the shipper.

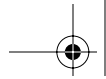
The immediate and very profound vision for all Federal Express people was spawned that first day:

GET THE PACKAGES.

This was my second experience with the power of vision. It was so crystal clear, but it was far more immediate than the "Determined people create their conditions. They are not the victims of them," which was and still is the UPS vision.

The power was the incredible motivation to do whatever was necessary on the part of hundreds of employees each with their own interpretation of what it would take to GET THE PACKAGES.





Packages meant growth, customers who bought our story, venture capitalists listening, financing, and so forth. Everything would happen with packages. Nothing would happen without them. Thousands of people would eventually have that same vision while we struggled, without money, for years to survive and finally to succeed and thrive.

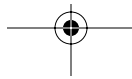
Pilots would land their planes and go make sales calls. Other pilots would run pickup and delivery stations all focused on GET THE PACKAGES. Couriers (drivers) would build relationships with shipping clerks and go through our competitors' packages, pull off their airbills, and put ours on. We called them package thieves (a good term, although we didn't direct them to do it).

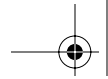
Looking back, I don't believe Federal Express would have become the industry leader that it is had we gotten the 300 packages. Without the sense of failure and the core learning that comes from failure, we would not have had the focus, nor would we have developed the service culture that still permeates the company today, nearly 30 years later.

We decided that first week that the 10 cities from Jacksonville, FL, to St. Louis, MO, didn't give shippers enough coverage. We identified 15 additional cities, including New York, Boston, Chicago, and other major cities in the east.

We put a team together with the mission to get 15 cities opened in 15 business days. The team would fly into a city with specific roles. One person took care of the Piper Cub and found a motel for everyone, another found a place for the cargo jet to unload and be serviced, another found a place for the trucks and couriers, and the fourth would go...to a bar during happy hour.

This last person was responsible for hiring. At the peak of happy hour activity, he'd stand on a chair, tap on a glass, and make the announcement that he was representing a new company in town and was hiring tonight. People would come to the table, fill out





an application, and be hired on the spot. As Tom Peters says, “Hire fast; fire fast.” And that’s what we did.

The GET THE PACKAGES vision permeated at every level of the organization. People interpreted this vision each in their own way, and this gave us the strength that eventually made us unbeatable in the marketplace.

One such example...

One of the new cities we opened during that first month was a small town in Indiana. The only reason we decided to serve it was that it had an RCA plant that shipped 20 packages a day. By the time we got the additional 15 cities opened, April 17, 1973, we had 40 packages a day, so that would mean 50% growth—exciting.

So, we sent one of our best salespeople there with instructions to GET THE PACKAGES from RCA and to call when he had received the commitment and the packages.

He called me that first day and said the traffic manager wouldn’t see him. I suggested that he get a good book and wait in the lobby all month until the guy would see him.

He called the next afternoon and said that he finally saw the traffic manager at 3:30 p.m. after waiting in the lobby all day and that the man wasn’t going to switch carriers.

I asked why.

“He claims that everyone says they have overnight service. He’s satisfied that no one delivers on the promise, and there’s nothing I could say to him to convince him otherwise. I think he’s being paid off by our competitor.”

Sometimes, salespeople say that as a last resort.

“Did you offer him free service for the week? Did you offer to ship empty boxes so he could test the system and our promise? Did you explain the hub system and that we have our own air-





planes?” I was desperately trying to figure out why people didn’t believe us. This guy wasn’t the first and, as I was learning, wouldn’t be the last.

“I did all of that and more. I’m telling you, Mike, he’s not going to use us.”

“Okay, see if you can get a plane tomorrow to Boston. We need more salespeople there.”

I’d like to say Federal Express had built a strong service ethic by design, but the reality is that we learned a number of very valuable lessons in the early days, most of which were taught to us by our employees.

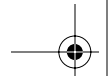
Fred Smith had started with a People–Profit ethic. The idea was to focus on employees, and they would produce the profit. He wanted to build a different kind of company. Back in the 70s, people were numbers to large companies. Companies didn’t care about their people. Fred wanted to build a people-first company. I had added the word “Service” to the mix, so the mantra had become and still is today: People—Service—Profit.

That was all well and good, but we needed PACKAGES and we needed them NOW.

One of the most valuable lessons was the power of people when they have a common vision and commitment. In this case, the vision was GET THE PACKAGES, and everyone understood it. In many cases, they understood it a lot more than I or other senior managers did, as this example demonstrates.

All kinds of things began to happen, but the biggest lesson in those early days was taught to me by a tracing clerk named Diane. Diane wasn’t very busy tracing things because we had so many people and so few packages. It was pretty hard to screw things up in those early days.





Imagine Atlanta, GA, with five drivers and three packages. The couriers would jump over one another for something to deliver and, more often than not, the package would arrive at its destination before the person receiving it. Great service. The people getting the packages loved it and told our people so, and that made our people strive even harder for the recognition.

On a Friday afternoon, about two weeks after we opened the new cities, Diane got a call from a woman from the small town in Indiana, the town with the RCA plant that wouldn't use us.

The woman was crying and through the tears managed to get out:

"I don't know who Federal Express is. All I know is that my wedding dress was in Jacksonville, FL, yesterday, and you were supposed to deliver it by noon today. It's 3:30 p.m., and it's not here! I'm getting married tomorrow, and because we're a small town, it's the social event of the season. More important, it's the event of my life. Can you help me?"

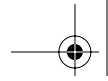
Diane related to the problem and told the woman she'd call her back. Then, she used our tracing system at the time—call each station (there were only 25) and see if one has a package that doesn't belong in its station. On the sixth call, she found the package in Detroit, more than 300 miles away.

Now, she had a problem to solve. She was going to get the package delivered that afternoon. There wasn't a doubt in Diane's mind. All of us were out trying to sell shippers or investors, so there was no one in management to ask. Looking back, I'm not sure that she would have asked permission anyway. She was committed to getting the package delivered.

She lined up a Cessna and a pilot to fly the package to Wilmington, IN, of course. Any frontline employee would do that. After all, this woman was getting married.

On Monday morning, Diane received a call from the woman who was on her honeymoon in Mexico (not an easy task in those days





to get a call placed from Mexico). The woman told Diane she had gotten her dress, described the wedding, and thanked her. Then, she asked if she could talk with a senior manager to relate the story. Diane transferred the call to me.

The woman described what had happened and what Diane had done for her. There were tears in her voice.

As she was describing Diane's actions, tears and all, all I could see was dollar signs. "How much did this cost?" I asked myself silently. As the woman went on, I scribbled a note to talk with Diane right after the call. After all, I had grown up with UPS. When a customer had a problem, you did what you could, but renting a plane wasn't on the list.

Then the woman gave me a clue that I didn't pick up until later, "Mr. Basch, it wasn't all good news. There was bad news also."

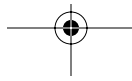
She got my attention. "Was it wrinkled?" I asked.

"Yes, but that's typical. We ironed it. The bad news was that I wasn't the center of attention at my own wedding. I had told a few people about my wedding dress having its own airplane, and the word spread. Pretty soon, the topic of discussion was this outrageous new airline for packages that had a plane per package." She laughed as she related the story.

I still wasn't laughing. I was still thinking about the cost and Diane gone astray, and then I envisioned hundreds of employees hiring planes and pilots at random. However, like all vice presidents, I was polite, thanked her for the call, and then went down the hall to find Diane.

"Why on earth would you charter a plane for a wedding dress?" I asked seriously.

"You said 'GET THE PACKAGES' and, for me, that means you give great service and solve the customer's problem. Then they talk about you, and you get more business."





Today, that makes enormous sense to me, but then it went totally over my head. “Come on Diane, if we spent \$300 for every package, we’d go bankrupt.”

After a couple of minutes of her attempting vainly to explain what GET THE PACKAGES meant to her and, in her fervent belief, what it meant to the company, she finally blurted out in total frustration:

“I figured we’re going bankrupt anyway. What’s the difference?”

There was obvious truth in that statement, so I let it go. Being people first meant honesty, and Diane was no stranger to our financial situation.

Two weeks later, RCA started giving us 20 packages a day.

A couple of their executives were at the wedding, and they went back and asked their traffic manager if he knew about Federal Express. One executive, in particular, made it plain that he should at least try our service. He did, and they began using Federal Express on a regular basis.

If I’d had a tail, it would have been between my legs as I went down to Diane’s desk to relate the news. She had a smile on her face as I arrived telling me clearly, but at least silently, that she already knew about the RCA packages.

It was an incredible lesson—one of thousands of lessons learned in those early days. The biggest lesson was that if you were clear about what you wanted as leaders and then let people give it to you without tying their hands behind their backs, you got it. Often, you got it in ways you didn’t expect, such as chartering an airplane for one package, but you got it.

The bottom line: We learned through failure, and failure is the **feedback** of a well-designed (either consciously or unconsciously) system. More important, our people had the freedom



and the focus, GET THE PACKAGES, to use that feedback to take the necessary **actions** to achieve the **goal**.

I've been involved in 13 start-ups, and it's always the same. The feedback is so tied to the customer that people do whatever is required to meet the goals and succeed. That's why I find start-ups so stimulating. The systems cycle of **goal/relevance/action/feedback** is natural and is not clouded by politically driven motivations that get in the way of success.

Some companies, such as UPS, Federal Express, Cisco, Prentice Hall, and many others, have built the success structures to take them forward into megacompanies that don't lose sight of the customer. This book is about building those success structures.

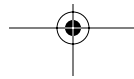
We didn't get capital until that November, but we survived because we had commitment. During the summer of 1973, 600 employees received a pay envelope with their checks and a note. "Please don't cash the check because there's no money in the bank, but hang in there. We'll succeed together."

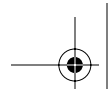
Only a handful of people left.

Many other things came with that commitment. Railway Express Agency (REA), a major competitor, went out of business, and we were able to capture the lion's share of its customers. United Airlines went on strike, leaving our air freight forwarder competitors without the ability to move freight, and our volume increased.

Fred Smith went to Las Vegas and won \$29,000 on the blackjack tables—enough to meet payroll for another week.

A pilot used his personal credit card to pay a fuel bill and get the sheriff's patrol car out from in front of the airplane. A driver hocked his watch to purchase fuel to complete his deliveries. There were hundreds of stories of employees going far beyond the call of duty to deliver absolutely positively overnight when they didn't get much support from the top.





This was because the natural system of goal/relevance/action/feedback was functioning flawlessly.

Probably the most outrageous story was a last-ditch effort in July 1973. We were out of money, our creditors were out of patience, and there was no light at the end of the tunnel. Most of us in senior management gave up once a week in those days. Then we'd run into Fred and walk away believing we were about to conquer the world.

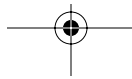
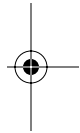
I only saw Fred give up twice in three years, and in July 1973 he had given up. His first principle of finance was no longer working: "When you borrow, borrow big. Then, when things go wrong, you have partners instead of creditors."

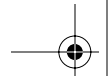
Well, things had gone wrong. Our lawyers and accountants had done all they could do to hold off the creditors, but it was all over. It was Saturday morning, and, if we didn't have \$1 million in the bank by open of business Monday morning, we were out of business. Fred had given up. He was ready to close the doors on Monday morning.

As a last-ditch effort, one of our attorneys had arranged a one-hour meeting in Chicago that afternoon with Henry Crown, the majority shareholder of General Dynamics. Henry had never heard of Fred or Federal Express. Fred had one hour to deliver a presentation and walk away with a \$1 million cashier's check, or we were done. Talk about sales pressure.

Fred sold an option to purchase 80% of the company for a down payment of \$1 million, and we stayed alive through the summer and into the fall until the venture capital came in—the first of three financing rounds that, at that time, represented the biggest venture capital start-up in American history.

Today, or at least during the .com bonanza, the \$120 million we raised is a drop in the bucket, but, during those days, it was an





enormous undertaking. Not making a profit for three years was not in the dictionary of the venture people.

When looking back, it was traumatic and, I believe, necessary.

Interestingly what would have been worse is to have gotten the 300 packages that first night. I believe we would have gotten sloppy about service and customer focus. Because we had just two customer packages, we became obsessed as a company with GETTING THE PACKAGES.

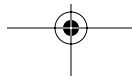
This vision didn't come in the form of a mandate from on high. It was blatantly obvious that PACKAGES were our only hope, although actions were taken by management to make it crystal clear to everyone. That obsession led to a strong service culture that has lasted decades and gets stronger all the time.

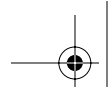
Federal Express' obsession with the conscious development of customer-focused systems and the use of technology has enabled it to maintain market share in the face of ruthless competition.

Fortunately, money or no, we had to build systems to maintain airplanes and flight rules, and that led to building systems for nearly every part of the operation.

Maintaining the spirit of the entrepreneurial company while doubling every year and moving toward bigness is a formidable task and can only be accomplished by systematizing nearly every part of the operation, from how people get to their jobs to how packages are sorted and tracked to what planes fly where and who flies them.

By systems here, we don't mean just information systems, but rather cause-and-effect systems. If this choice is made, this is the likely outcome. People are driven primarily by systems as used in this context. Well-designed systems tie choice and actions to outcome.





For example, if an organization recognizes certain behaviors, more of those behaviors will occur over time. If the recognition is for behaviors not desired, nonetheless, more of those negative behaviors will occur. If Diane were ridiculed for getting the wedding dress to the wedding, the service ethic at Federal Express would have turned into a cost focus leading to relatively poor service over time and continued dominance by UPS, even in the air business.

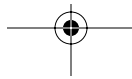
I will show some of the changes Federal Express has made through the years to remain customer focused as it continues to grow from two packages that first night to more than 4 million packages (just Federal Express express air packages) today.

The overall lesson for our current economy is that only your employees can keep you innovating and evolving constantly, or only your employees can contract the deadly disease of Customer Cancer. Only well-designed goal/relevance/action/feedback systems can optimize your employees' focus on giving power to customers.

Customer Cancer is a term I use to express organizational systems run amuck. Instead of customer focus, the cells or employees begin to focus on each other or on themselves rather than the greater good where everyone wins.

Customer Cancer is not a disease caused by competitors, by government regulation, or the economy. It is a disease of indifference, poor focus by corporate leaders, and the lack of *CustomerCulture*. Customer Cancer is a disease that is contracted only from within.

Human cancer research has shown that, "Unlike normal body cells, they [cancer cells] disregard the needs of the community of cells. They are selfish and unsociable and are only interested in their own proliferative advantage."





An example of Customer Cancer in a related organization is the United States Postal Service (USPS).

A contractor friend of mine was walking with the postmaster through a local post office preparing to bid on some construction work. He spotted a \$20 bill on the floor and began to stoop down to pick it up when the postmaster held him back and explained, “That is bait to catch thieves. The mirror you see over there is a two-way mirror, and there’s a security guard watching to see who picks it up.”

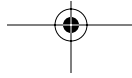
It’s no wonder postal service employees are not customer focused. It is not easy to change a culture that ingrained and that large, but, starting with one postal facility at a time, it is possible, and it must start with a degree of employee trust. Certainly both UPS and Federal Express have their share of employee theft, but there are far better ways of handling it than tempting honest employees to find \$20. That is Customer Cancer.

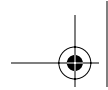
This same phenomenon happens in companies that don’t walk the talk when it comes to focusing on employee and customer well-being. I have yet to talk with or even hear about CEOs that don’t say employees and customers were their primary focus. The problem is that 95% talk about it and 5% demonstrate it through their employees’ actions and behaviors. It is those behaviors that reflect the prevailing culture, not the platitudes of senior managers.

Fred Smith had several thoughts on this subject:

“Give employees a sense of control over their own destiny, and they’ll do anything you ask—and more.” Systems must be designed to give employees and customers control of their relationship with you and their customers.

“When an employee wants a raise, only the customer can grant it. It is up to the employees to figure out how to add enough additional value to get the customer to pay for it. Customers will pay





if there is value. Stockholders won't." Systems provide the reward and the focus for employees to understand this reality and to constantly look for ways to add value to the customer's experience.

"The sun will not set on an unresolved customer or employee problem, meaning that, if the problem cannot be resolved, at least it will be dealt with and the people involved will be aware that it is being dealt with." Systems provide the sense of urgency.

On his second comment, being people first doesn't mean being the parent and entitling employees to all the benefits and rewards without accountability and performance. It doesn't mean taking care of people, but rather demanding the best from every person.

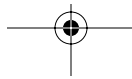
This book shows how many companies have been able to build power with customer focus. It also shows how focus on products and engineering at the expense of the customer (Customer Cancer) will gradually mean the decline of big business in favor of a more distributed model.

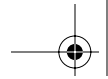
Being customer focused is a must in the new economy. Those company leaders that believe it is not will lose. The Internet just may be the asteroid that kills the dinosaur.

CustomerCulture uses the Federal Express story and other reference stories to drive home the importance of systems.

These reference stories act as springboards to creating a positive customer experience by demonstrating the power and need for the underlying systems that focus employees on customers—an experience that parallels the experience of the woman from the small town in Indiana.

It's no longer about customer service. It's about congruent and continuous customer experiences driven by culturalizing nearly every interaction. This means systematizing the routine and humanizing the exception. It means having all employees vitally





aware of the need for customer loyalty, whether they design computer screens, fly airplanes, manufacture things, or pay expense accounts.

If the experience is bad, we'll see Customer Cancers developing. If it is good, we have customer health and longevity.

The Federal Express story told in this chapter is nearly 30 years old, but the principles and the stories told in subsequent chapters underline the cultural principles that have made and are making companies throughout the world great today.

