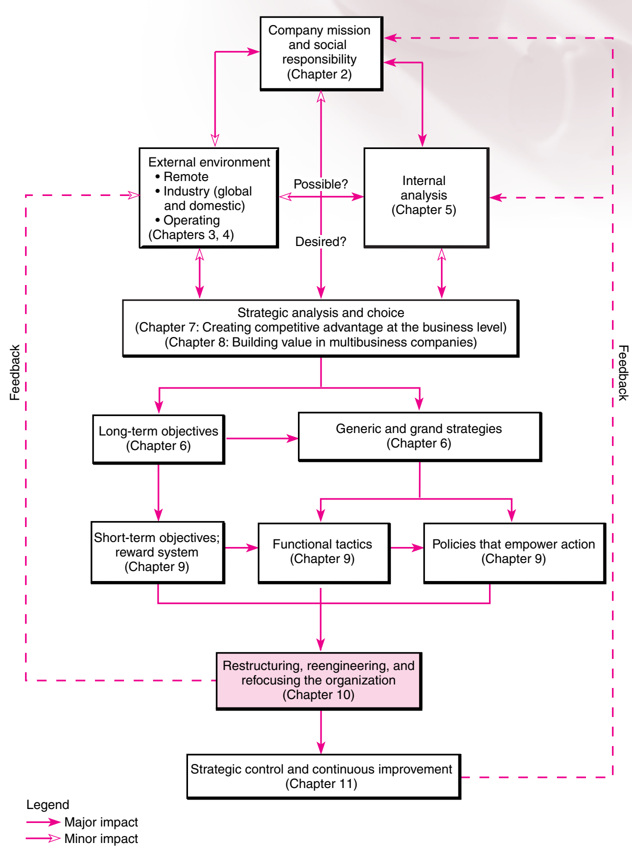
Chapter Ten

Implementing Strategy: Structure, Leadership, and Culture



Until this point in the strategic management process, managers have maintained a decidedly market-oriented focus as they formulate strategies and begin implementation through action plans detailing the tactics and actions that will be taken in each functional activity. Now the process takes an organizational focus—getting the work of the business done efficiently and effectively so as to make the strategy work. What is the best way to organize ourselves to accomplish the mission? Where should leadership come from? What values should guide our activities each day? What should this organization and its people be like? These are some of the fundamental issues managers face as they turn to the heart of strategy implementation.

While the focus is internal, the firm must still consider external factors as well. The intense competition in today's global marketplace has led most companies to consider their structure, or how the activities within their business are conducted, with an unprecedented attentiveness to what that marketplace—customers, competitors, suppliers, distribution partners—suggests or needs from the "internal" organization. This chapter explores three basic "levers" through which managers can implement strategy. The first lever is structure—the basic way the firm's different activities are organized. Second is leadership, encompassing the need to establish direction, embrace change and build a team to execute the strategy. The third lever is culture—the shared values that create the norms of individual behavior and the tone of the organization.

Consider the situation new CEO Carly Fiorina faced at Hewlett Packard in the midst of a global recession. The unfortunate reality for her: HP's lumbering organization was losing touch with its global customers. Her response: As illustrated in Exhibit 10–1, Strategy in Action, Fiorina immediately dismantled the decentralized structure honed throughout HP's 64-year history. Pre-Fiorina, HP was a collection of 83 independently run units, each focused on a product such as scanners or security software. Fiorina collapsed those into four sprawling organizations. One so-called back-end unit develops and builds computers, and another focuses on printers and imaging equipment. The back-end divisions hand products off to two "front-end" sales and marketing groups that peddle the wares—one to consumers, the other to corporations. The theory: The new structure would boost collaboration, giving sales and marketing execs a direct pipeline to engineers so products are developed from the ground up to solve customer problems. This was the first time a company with thousands of product lines and scores of businesses attempted a front-back approach, a structure that requires laser focus and superb coordination.

Fiorina believed she had little choice lest the company experience a near-death experience like Xerox or, ten years earlier, IBM. The conundrum: how to put the full force of the company behind winning in its immediate fiercely competitive technology business when they must also cook up brand-new megamarkets? It's a riddle Fiorina said she could solve only by sweeping structural change that would ready HP for the next stage of the technology revolution, when companies latch on to the Internet to transform their operations. At its core lay a conviction that HP must become "ambidextrous" excelling at short-term execution while pursuing long-term visions that create new markets. In addition to changing HP's structure, Fiorina also sought to revamp its culture of creativity. Her plan for unleashing a new culture of creativity was what she called "inventing at the intersection." Until 2001, HP made stand-alone products and innovations from $20 ink cartridges to $3 million servers. To revolutionize HP's culture and approach, she launched three "cross-company initiatives"—wireless services, digital imaging, and printing—the first formal effort to get all of HP's separate and sometimes warring "tribes" working together.

Will it work? You are in the position of using hindsight to find out. Regardless, she earned high marks for zeroing in on HP's core problems and for having the courage to tackle them head-on. And, if it did, the then 46-year-old CEO would become a twenty-first century management hero for a reinvigorated HP becoming a blueprint for others trying to transform major technology companies into twenty-first century dynamos. Said Stanford

Strategy in Action
Fiorina's Way at Hewlett Packard

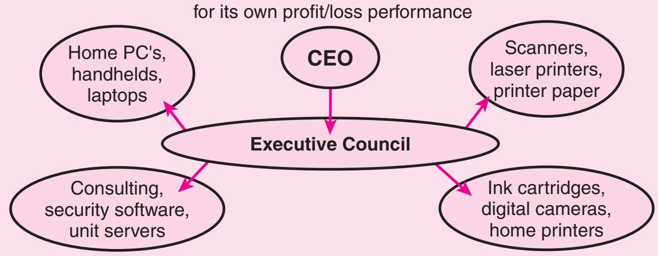
Exhibit 10–1

The Fiorina Way

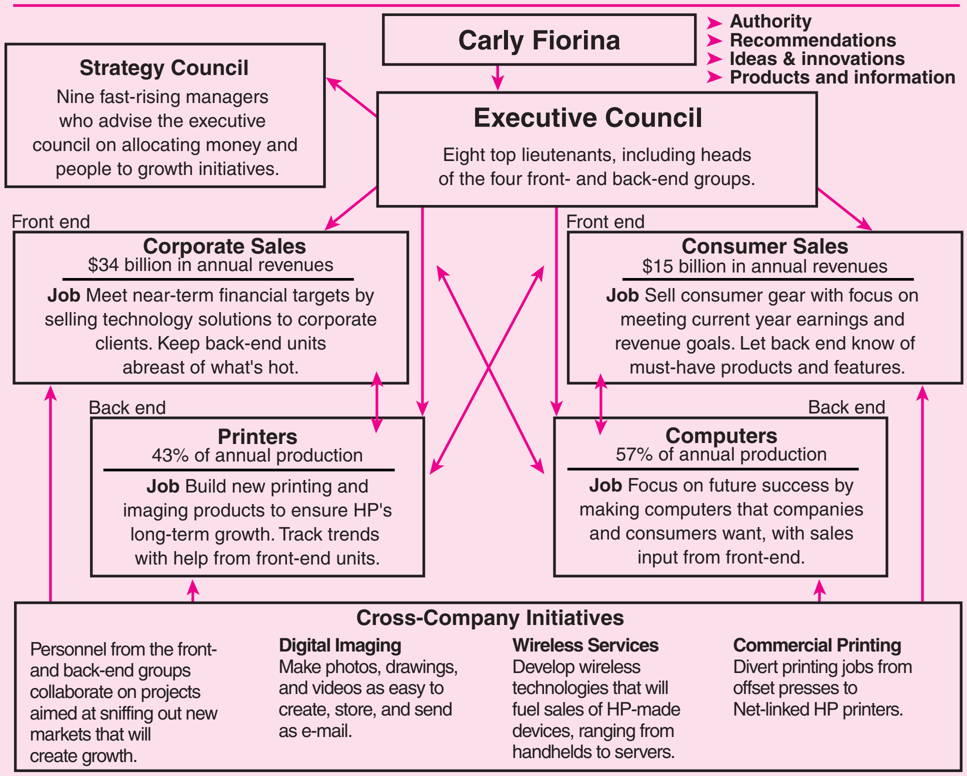
When Fiorina arrived at HP, the company was a confederation of 83 autonomous product units reporting through four groups. She radically revamped the structure into two "back-end" divisions–one developing printers, scanners, and the like, and the other computers. These report to "front-end" groups that market and sell HP's wares. Here's how the overhaul stacks up:

The Old HP

Each product unit was responsible for its own profit/loss performance



The New HP



The Assessment

Benefits

Happier Customers Clients should find HP easier to deal with, since they'll work with just one account team.

Sales Boost HP should maximize its selling opportunities because account reps will sell all HP products, not just those from one division.

Real Solutions HP can sell its products in combination as "solutions"—instead of just PCs or printers—to companies facing e-business problems.

Financial Flexibility With all corporate sales under one roof, HP can measure the total value of a customer, allowing reps to discount some products and still maximize profits on the overall contract.

Risks

Overwhelmed with duties With so many products being made and sold by just four units, HP execs have more on their plates and could miss the details that keep products competitive

Poorer Execution When product managers oversaw everything from manufacturing to sales, they could respond quickly to changes. That will be harder with front- and back-end groups synching their plans only every few weeks.

Less Accountability Profit-and-loss responsibility is shared between the front- and back-end groups so no one person is on the hot seat. Finger-pointing and foot-dragging could replace HP's collegial cooperation.

Fewer Spending Controls With powerful division chiefs keeping a tight rein on the purse strings, spending rarely got out of hand in the old HP. In the fourth quarter, expenses soared as those lines of command broke down.

EXHIBIT 10–2
What a Difference a Century Can Make

Source: "21st Century Corporation," *BusinessWeek,* August 28, 2000.

Contrasting views of the corporation:

Characteristic	20th Century	21st Century
ORGANIZATION	The Pyramid	The Web or Network
FOCUS	Internal	External
STYLE	Structured	Flexible
SOURCE OF STRENGTH	Stability	Change
STRUCTURE	Self-sufficiency	Interdependencies
RESOURCES	Atoms—physical assets	Bits—information
OPERATIONS	Vertical integration	Virtual integration
PRODUCTS	Mass production	Mass customization
REACH	Domestic	Global
FINANCIALS	Quarterly	Real-time
INVENTORIES	Months	Hours
STRATEGY	Top-down	Bottom-up
LEADERSHIP	Dogmatic	Inspirational
WORKERS	Employees	Employees and free agents
JOB EXPECTATIONS	Security	Personal growth
MOTIVATION	To compete	To build
IMPROVEMENTS	Incremental	Revolutionary
QUALITY	Affordable best	No compromise

professor Robert Burgelman at the time, "there isn't a major technology company in the world that has solved the problem she's trying to address, and we're all going to learn from her experience."[1]

What CEO Fiorina faced, and Professor Burgelman recognizes, is the vast difference between business organizations of the twentieth century and those of today. Exhibit 10–2 compares both on 18 different characteristics. The contrasts are striking, perhaps most so for leaders and managers faced with implementing strategies within them.

Fiorina offers a courageous example of a leader who recognized these compelling differences in the HP of the twentieth century and what the HP of the twenty-first century needed to be. And her decision to adopt a laserlike focus on three key "levers" within HP to attempt to make HP's strategy successful are reflected in the focus of this chapter. Her first lever was HP's *organizational structure,* which was so important from her point of view that, without major change, would mean a partial or complete failure of HP. Her second concern was *leadership,* both from herself and key managers throughout HP. Finally, she knew that the HP *culture,* in this case birth of a new one, was the third critical lever with which to make the new HP vision and strategy have a chance for success.

STRUCTURING AN EFFECTIVE ORGANIZATION

Exhibit 10–2 offers a useful starting point in examining effective organizational structure. In contrasting twentieth century and twenty-first century corporations on different characteristics, it offers a historical or evolutionary perspective on organizational attributes associated with successful strategy execution today and just a few years ago. Successful organization once required an internal focus, structured interaction, self-sufficiency, a top-down approach. Today and tomorrow, organizational structure reflects an external focus,

[1] "The Radical," *BusinessWeek,* February 19, 2001.

flexible interaction, interdependency, and a bottom-up approach, just to mention a few characteristics associated with strategy execution and success. Three fundamental trends are driving decisions about effective organizational structures in the twenty-first century: globalization, the Internet, and speed of decision making.

Globalization The earlier example at Hewlett-Packard showed CEO Fiorina facing a desperate truth: HP's cumbersome organization was losing touch with its global customers. So she radically reorganized HP in part so multinational clients could go to just one sales and marketing group to buy everything from ink cartridges to supercomputers, in Buffalo or Bangkok. Over two-thirds of all industry either operates globally (e.g., computers, aerospace) or will soon do so. In the last ten years, the percentage of sales from outside the home market for these five companies grew dramatically:

	1995	2000	2005
General Electric	16.5%	35.1%	41.7%
Wal-Mart	0.0	18.8	32.2
McDonald's	46.9	65.5	71.8
Nokia	85.0	98.6	99.1
Toyota	44.6	53.5	61.2

The need for global coordination and innovation is forcing constant experimentation and adjustment to get the right mix of local initiative, information flow, leadership, and corporate culture. At Swedish-based Ericsson, top managers scrutinize compensation schemes to make managers pay attention to global performance and avoid turf battles, while also attending to their local operations. Companies like Dutch electronics giant Philips regularly move headquarters for different businesses to the hottest regions for new trends—the "high voltage" markets. Its digital set-top box is now in California, its audio business moved from Europe to Hong Kong.[2]

Global once meant selling goods in overseas markets. Next was locating operations in numerous countries. Today it will call on talents and resources wherever they can be found around the globe, just as it now sells worldwide. It may be based in the United States, do its software programming in New Delhi, its engineering in Germany, and its manufacturing in Indonesia. The ramifications for organizational structures are revolutionary.

The Internet The Net gives everyone in the organization, or working with it, from the lowest clerk to the CEO to any supplier or customer, the ability to access a vast array of information—instantaneously, from anywhere. Ideas, requests, instructions zap around the globe in the blink of an eye. It allows the global enterprise with different functions, offices, and activities dispersed around the world to be seamlessly connected so that far-flung customers, employees, and suppliers can work together in real time. The result—coordination, communication and decision-making functions accomplished through and the purpose for traditional organizational structures become slow, inefficient, noncompetitive weights on today's organization.

Speed Technology, or digitization, means removing human minds and hands from an organization's most routine tasks and replacing them with computers and networks. Digitizing everything from employee benefits to accounts receivable to product design cuts cost,

[2] "See the World, Erase Its Borders," *BusinessWeek,* August 28, 2000.

time, and payroll resulting in cost savings and vast improvements in speed. "Combined with the Internet, the speed of actions, deliberations, and information will increase dramatically," says Intel's Andy Grove. "You are going to see unbelievable speed and efficiencies," says Cisco's John Chambers, "with many companies about to increase productivity 20 percent to 40 percent per year." Leading-edge technologies will enable employees throughout the organization to seize opportunity as it arises. These technologies will allow employees, suppliers, and freelancers anywhere in the world to converse in numerous languages online without need for a translator to develop markets, new products, new processes. Again, the ramifications for organizational structures are revolutionary.

Whether technology assisted or not, globalization of business activity creates a potential sheer velocity of decisions that must be made which challenges traditional hierarchial organizational structures. A company like Cisco, for example, may be negotiating 50–60 alliances at one time due to the nature of its diverse operations. The speed at which these negotiations must be conducted and decisions made require a simple and accommodating organizational structure lest the opportunities may be lost.

Faced with these and other major trends, how should managers structure effective organizations? Consider these recent observations by *BusinessWeek* editors at the end of a year-long research effort asking just the same question:

> The management of multinationals used to be a neat discipline with comforting rules and knowable best practices. But globalization and the arrival of the information economy have rapidly demolished all the old precepts. The management of global companies, which must innovate simultaneously and speed information through horizontal, global-spanning networks, has become a daunting challenge. Old, rigid hierarchies are out—and flat, speedy, virtual organizations are in. Teamwork is a must and compensation schemes have to be redesigned to reward team players. But aside from that bit of wisdom, you can throw out the textbooks.
>
> CEOs will have to custom-design their organizations based on their industry, their own corporate legacy, and their key global customers—and they may have to revamp more than once to get it right. Highly admired companies such as General Electric, Hewlett-Packard, ABB Ltd., and Ericsson have already been through several organizational reincarnations in the past decade to boost global competitiveness.[3]

Our research concurs with these findings by *BusinessWeek* editors—there is no one best organizational structure. At the same time, there are several useful guidelines and approaches that help answer this question which we will now cover in the next several sections.

Match Structure to Strategy

The recent changes at Hewlett-Packard in Exhibit 10–1, Strategy in Action, illustrate this fundamental guideline. CEO Fiorina adopted the difficult, career-risking path of creating a major new structure at HP because that new structure reflected the needs of HP's strategy for the twenty-first century. An easier alternative would have been to create a strategy compatible with the existing decentralized structure of 83 semiautonomous business units that had been in place for over half a century. While easier, however, the result would have been damaging to HP in the long run, perhaps even fatal, because strategic priorities and initiatives would have been guided by structural considerations, rather than the other way around.

[3] "The 21st Century Corporation," *BusinessWeek,* August 28, 2000.

The origins of this maxim come from a historical body of strategic management research[4] that examined how the evolution of a business over time and the degree of diversification from a firm's core business affected its choice of organizational structure. The primary organizational structures associated with this important research are still prevalent today—simple functional structures, geographical structures, multidivisional structures, and strategic business units.[5] Four basic conclusions were derived from this research:

1. *A single-product firm or single dominant business firm should employ a functional structure.* This structure allows for strong task focus through an emphasis on specialization and efficiency, while providing opportunity for adequate controls through centralized review and decision making.

2. *A firm in several lines of business that are somehow related should employ a multidivisional structure.* Closely related divisions should be combined into groups within this structure. When synergies (i.e., shared or linked activities) are possible within such a group, the appropriate location for staff influence and decision making is at the group level, with a lesser role for corporate-level staff. The greater the degree of diversity across the firm's businesses, the greater should be the extent to which the power of staff and decision-making authority is lodged within the divisions.

3. *A firm in several unrelated lines of business should be organized into strategic business units.* Although the strategic business unit structure resembles the multidivisional structure, there are significant differences between the two. With a strategic business unit structure, finance, accounting, planning, legal, and related activities should be centralized at the corporate office. Since there are no synergies across the firm's businesses, the corporate office serves largely as a capital allocation and control mechanism. Otherwise, its major decisions involve acquisitions and diverstitures. All operational and business-level strategic plans are delegated to the strategic business units.

4. *Early achievement of a strategy-structure fit can be a competitive advantage.* A competitive advantage is obtained by the first firm among competitors to achieve appropriate strategy-structure fit. That advantage will disappear as the firm's competitors also attain such a fit. Moreover, if the firm alters its strategy, its structure must obviously change as well. Otherwise, a loss of fit will lead to a competitive disadvantage for the firm.

These research-based guidelines were derived from twentieth century companies not yet facing the complex, dynamically changing environments we see today. So an easy conclusion would be to consider them of little use. That is not the case, however. First, the admonition to let strategy guide structure rather than the other way around is very im-

[4] Alfred D. Chandler, *Strategy and Structure* (Cambridge: MIT Press, 1962); Larry Wrigley, *Divisional Autonomy and Diversification,* doctoral dissertation, Harvard Business School, 1970; Richard Rumelt, "Diversification Strategy and Performance," *Strategic Management Journal* 3 (January–February 1982), pp. 359–69; Richard Rumelt, *Strategy, Structure and Economic Performance* (Boston: HBS Press, 1986). Rumelt used a similar, but more detailed classification scheme; D. A. Nathanson and J. S. Cassano, "Organization, Diversity, and Performance," *Wharton's Magazine* 6 (1982), pp. 19–26; and Christopher A. Bartlett and Sumantra Ghoshal, "Matrix Management: Not a Structure, a Frame of Mind," *Harvard Business Review* 68, no. 4 (1990), pp. 138–45; V. R. Galbraith and R. K. Kazanjian, *Strategy Implementation: Structure, Systems & Processes* (St. Paul, MN: West Publishing, 1986).

[5] Each primary structure is diagrammed and described in detail along with the advantages and disadvantages historically associated with each in an appendix to this chapter.

portant today. While seemingly simple and obvious, resistance to changing existing structures—"the way we do things around here"—continues to be a major challenge to new strategies in many organizations even today as HP again illustrates. Second, the notion that firms evolve over time from a single product/service focus to multiple products/services and markets requiring different structures is an important reality to accommodate when implementing growth strategies. Finally, many firms today have found value in multiple structures operating simultaneously in their company. People may be assigned within the company as part of a functional structure, but they work on teams or other groupings that operate outside the primary functional structure. We will explore this practice in a subsequent section, but the important point here is that while new and important hybrid organizational structures have proven essential to strategy implementation in the twenty-first century, these same "innovative" firms incorporate these "older" primary organizational structures in the fabric of their contemporary organizational structure.

Balance the Demands for Control/Differentiation with the Need for Coordination/Integration

Specialization of work and effort allows a unit to develop greater expertise, focus, and efficiency. So it is that some organizations adopt functional, or similar structures. Their strategy depends on dividing different activities within the firm into logical, common groupings—sales, operations, administration, or geography—so that each set of activity can be done most efficiently. Control of sets of activities is at a premium. Dividing activities in this manner, sometimes called "differentiation," is an important structural decision. At the same time, these separate activities, however they are differentiated, need to be coordinated and integrated back together as a whole so the business functions effectively. Demands for control and the coordination needs differ across different types of businesses and strategic situations.

The rise of a consumer culture around the world has led brand marketers to realize they need to take a multidomestic approach to be more responsive to local preferences. Coca-Cola, for example, used to control its products rigidly from its Atlanta headquarters. But managers have found in some markets consumers thirst for more than Coke, Diet Coke, and Sprite. So Coke has altered its structure to reduce the need for control in favor of greater coordination/integration in local markets where local managers independently launch new flavored drinks. At the same time, GE, the paragon of new age organization, had altered its GE Medical Systems organization structure to allow local product managers to handle everything from product design to marketing. This emphasis on local coordination and reduced central control of product design led managers obsessed with local rivalries to design and manufacture similar products for different markets—a costly and wasteful duplication of effort. So GE reintroduced centralized control of product design, with input from a worldwide base of global managers, and their customers, resulting in the design of several single global products produced quite cost competitively to sell worldwide. GE's need for control of product design outweighed the coordination needs of locally focused product managers.[6] At the same time, GE obtained input from virtually every customer or potential customer worldwide before finalizing the product design of several initial products, suggesting that it rebalanced in favor of more control, but organizationally coordinated input from global managers and customers so as to ensure a better potential series of medical scanner for hospitals worldwide.

[6] See the World, Erase Its Borders," *BusinessWeek,* August 28, 2000.

Restructure to Emphasize and Support Strategically Critical Activities

Restructuring has been the buzzword of global enterprise for the last 10 years. Its contemporary meaning is multifaceted. At the heart of the restructuring trend is the notion that some activities within a business's value chain are more critical to the success of the business's strategy than others. Wal-Mart's organizational structure is designed to ensure that its impressive logistics and purchasing competitive advantages operate flawlessly. Coordinating daily logistical and purchasing efficiencies among separate stores lets Wal-Mart lead the industry in profitability yet sell retail for less than many competitors buy the same merchandise at wholesale. Motorola's organizational structure is designed to protect and nurture its legendary R&D and new product development capabilities—spending over twice the industry average in R&D alone each year. Motorola's R&D emphasis continually spawns proprietary technologies that support its technology-based competitive advantage. Coca-Cola emphasizes the importance of distribution activities, advertising, and retail support to its bottlers in its organizational structure. All three of these companies emphasize very different parts of the value chain process, but they are extraordinarily successful in part because they have designed their organizational structures to emphasize and support strategically critical activities. Exhibit 10–3, Strategy in Action, provides some guidelines that should influence how an organization is structured, depending on which among five different sources of competitive advantage are emphasized in its strategy.

Two critical considerations arise when restructuring the organization to emphasize and support strategically critical activities. First, managers need to make the strategically critical activities the central building blocks for designing organization structure. Those activities should be identified and separated as much as possible into self-contained parts of the organization. Then the remaining structure must be designed so as to ensure timely integration with other parts of the organization.

While this is easily proposed, managers need to recognize that strategically relevant activities may still reside in different parts of the organization, particularly in functionally organized structures. Support activities like finance, engineering, or information processing are usually self-contained units, often outside the unit around which core competencies are built. This often results in an emphasis on departments obsessed with performing their own tasks more than emphasizing the key results (customer satisfaction, differentiation, low costs, speed) the business as a whole seeks. So the second consideration is to design the organizational structure so that it helps coordinate and integrate these support activities to (1) maximize their support of strategy-critical primary activities in the firm's value chain and (2) does so in a way to minimize the costs for support activities and the time spent on internal coordination. Managerial efforts to do this in the 1990s have placed reengineering, downsizing, and outsourcing as prominent tools for strategists restructuring their organizations.

Reengineer Strategic Business Processes

Business process reengineering (BPR), popularized by consultants Michael Hammer and James Champy,[7] is one of the more popular methods by which organizations worldwide are undergoing restructuring efforts to remain competitive in the twenty-first century. BPR is intended to place the decision-making authority that is most relevant to the customer closer to the customer, in order to make the firm more responsive to the needs of the customer. This is accomplished through a form of empowerment, facilitated revamping organizational structure.

Business reengineering reduces fragmentation by crossing traditional departmental lines and reducing overhead to compress formerly separate steps and tasks that are strategically intertwined in the process of meeting customer needs. This "process orientation," rather than a traditional functional orientation, becomes the perspective around which various activities

[7] Michael Hammer and James Champy, *Reengineering the Corporation* (New York: HarperBusiness, 1993).

Strategy in Action

Guidelines for Designing a Structure to Accommodate Five Different Strategic Priorities

Exhibit 10–3

One of the key things business managers should keep in mind when restructuring their organizations is to devise the new structure so that it emphasizes strategically critical activities within the business's value chain. This means that the structure should allow those activities to have considerable autonomy over issues that influence their operating excellence and timeliness; they should be in a position to easily coordinate with other parts of the business—to get decisions made fast.

Below are five different types of critical activities that may be at the heart of a business's effort to build and sustain competitive advantage. Beside each one are typical conditions that will affect and shape the nature of the organization's structure:

Potential Strategic Priority and Critical Activities	Concomitant Conditions That May Affect or Place Demands on the Organizational Structure and Operating Activities to Build Competitive Advantage
1. Compete as low-cost provider of goods or services.	Broadens market. Requires longer production runs and fewer product changes. Requires special-purpose equipment and facilities.
2. Compete as high-quality provider.	Often possible to obtain more profit per unit, and perhaps more total profit from a smaller volume of sales. Requires more quality-assurance effort and higher operating cost. Requires more precise equipment, which is more expensive. Requires highly skilled workers, necessitating higher wages and greater training efforts.
3. Stress customer service.	Requires broader development of servicepeople and service parts and equipment. Requires rapid response to customer needs or changes in customer tastes, rapid and accurate information system, careful coordination. Requires a higher inventory investment.
4. Provide rapid and frequent introduction of new products.	Requires versatile equipment and people. Has higher research and development costs. Has high retraining costs and high tooling and changeover costs. Provides lower volumes for each product and fewer opportunities for improvements due to the learning curve.
5. Seek vertical integration.	Enables firm to control more of the process. May not have economies of scale at some stages of process. May require high capital investment as well as technology and skills beyond those currently available within the firm.

and tasks are then grouped to create the building blocks of the organization's structure. This is usually accomplished by assembling a multifunctional, multilevel team that begins by identifying customer needs and how the customer wants to deal with the firm. Customer focus must permeate all phases. Companies that have successfully reengineered their operations around strategically critical business processes have pursued the following steps:[8]

- Develop a flowchart of the total business process, including its interfaces with other value chain activities.

[8] Judy Wade, "How to Make Reengineering Really Work," *Harvard Business Review* 71, no. 6 (November–December 1993), pp. 119–31.

- Try to simplify the process first, eliminating tasks and steps where possible and analyzing how to streamline the performance of what remains.
- Determine which parts of the process can be automated (usually those that are repetitive, time-consuming, and require little thought or decision); consider introducing advanced technologies that can be upgraded to achieve next-generation capability and provide a basis for further productivity gains down the road.
- Evaluate each activity in the process to determine whether it is strategy-critical or not. Strategy-critical activities are candidates for benchmarking to achieve best-in-industry or best-in-world performance status.
- Weigh the pros and cons of outsourcing activities that are noncritical or that contribute little to organizational capabilities and core competencies.
- Design a structure for performing the activities that remain; reorganize the personnel and groups who perform these activities into the new structure.

When asked about his networking-oriented structure that helped revitalize IBM, former IBM CEO Gerstner responded: "It's called *reengineering.* It's called *getting competitive.* It's called *reducing cycle time and cost, flattening organizations, increasing customer responsiveness.* All of these require a collaboration with the customer and with suppliers and with vendors."

Downsize and Self-Manage: Force Decisions to Operating Level

Reengineering and a value orientation have led managers to scrutinize even further the way their organizational structures are crucial to strategy implementation. That scrutiny has led to downsizing, outsourcing, and self-management as three important themes influencing the organizational structures into the twenty-first century. *Downsizing* is eliminating the number of employees, particularly middle management, in a company. The arrival of a global marketplace, information technology, and intense competition caused many companies to reevaluate middle management activities to determine just what value was really being added to the company's products and services. The result of this scrutiny, along with continuous improvements in information processing technology, has been widespread downsizing in the number of management personnel in thousands of companies worldwide. These companies often eliminate whole levels of management. General Electric went from 400,000 to 280,000 employees in the last decade while its sales tripled and its profit rose fivefold. Former CEO Jack Welch's observations about GE's downsizing and the results of *BusinessWeek*'s survey of companies worldwide that have been actively downsizing (which attempts to extract guidelines for downsizing) are shown in Strategy in Action Exhibit 10–4.

One of the outcomes of downsizing was increased *self-management* at operating levels of the company. Cutbacks in the number of management people left those that remained with more work to do. The result was that they had to give up a good measure of control to workers, and they had to rely on those workers to help out. Spans of control, traditionally thought to maximize under 10 people, have become much larger due to information technology, running "lean and mean," and delegation to lower levels. Ameritech, one of the Baby Bells, has seen its spans of control rise to as much as 30 to 1 in some divisions because most of the people that did staff work—financial analysts, assistant managers, and so on—have disappeared. This delegation, also known as empowerment, is accomplished through concepts like self-managed work groups, reengineering, and automation. It is also seen through efforts to create distinct businesses within a business—conceiving a business

Strategy in Action
How Lean Is Your Company?

Exhibit 10–4

BusinessWeek

GE used to have things like department managers, subsection managers, unit managers, supervisors. We're driving those titles out . . . We used to go from the CEO to sectors, to groups, to businesses. We now go from the CEO to businesses. Nothing else.

—Jack Welch

It's hard to find a major corporation that hasn't downsized in recent years. But simple reductions in staffing don't make for lean management. Here's a checklist, developed by *BusinessWeek* from interviews with executives and consultants, that may tell you if your company needs a diet.

Company Characteristic	Analysis
1. Layers of management between CEO and the shop floor.	Some companies, such as Ameritech, now have as few as four or five where as many as 12 had been common. More than six is most likely too many.
2. Number of employees managed by the typical executive.	At lean companies, spans of control range up to one manager to 30 staffers. A ratio of lower than 1:10 is a warning of arterial sclerosis.
3. Amount of work cut out by your downsizing.	Eliminating jobs without cutting out work can bring disaster. A downsizing should be accompanied by at least a 25 percent reduction in the number of tasks performed. Some lean companies have hit 50 percent.
4. Skill levels of the surviving management group.	Managers must learn to accept more responsibility and to eliminate unneeded work. Have you taught them how?
5. Size of your largest profit center by number of employees.	Break down large operating units into smaller profit centers—less than 500 employees is a popular cutoff—to gain the economies of entrepreneurship and offset the burdens of scale.
6. Post-downsizing size of staff at corporate headquarters.	The largest layoffs, on a percentage basis, should be at corporate headquarters. It is often the most overstaffed—and the most removed from customers.

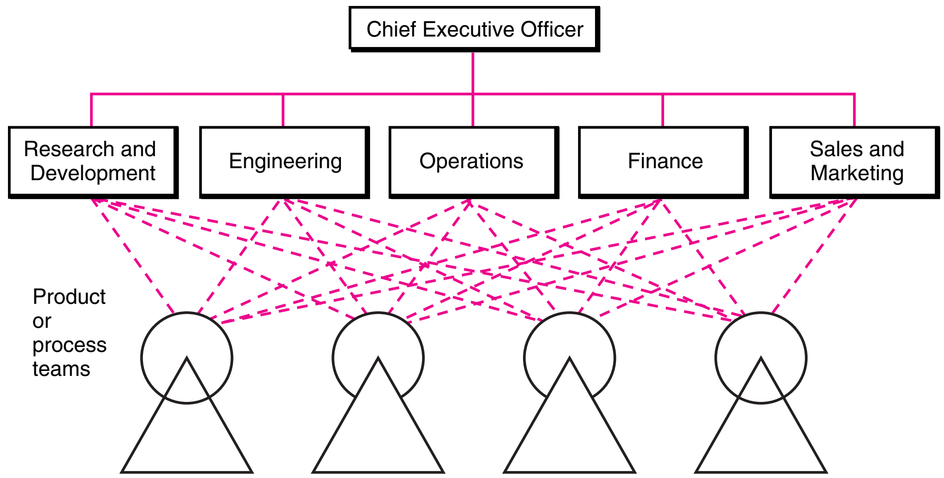
Source: "The 21st Century Corporation," *BusinessWeek,* August 28, 2000.

as a confederation of many "small" businesses, rather than one large, interconnected business. Whatever the terminology, the idea is to push decision making down in the organization by allowing major management decisions to be made at operating levels. The result is often the elimination of up to half the levels of management previously existing in an organizational structure.

Allow Multiple Structures to Operate Simultaneously within the Organization to Accommodate Products, Geography, Innovation and Customers

The *matrix organization* described in this chapter's Appendix was one of the early structural attempts to do this so that skills and resources could be better assigned and used within a large company. People typically had a permanent assignment to a certain organizational unit, usually a functional or staff department, yet they were also frequently assigned to work in another project or activity at the same time. For example, a product development project

EXHIBIT 10–5
The Product-Team Structure



may need a market research specialist for several months and a financial analyst for a week. It was tried by many companies, and is still in use today. The dual chains of command, particularly given a temporary assignment approach, proved problematic for some organizations, particularly in an international context complicated by distance, language, time, and culture.

The *product-team structure* emerged as an alternative to the matrix approach to simplify and amplify the focus of resources on a narrow but strategically important product, project, market, customer or innovation. Exhibit 10–5 illustrates how the product-team structure looks.

The product-team structure assigns functional managers and specialists (e.g., engineering, marketing, financial, R&D, operations) to a new product, project, or process team that is empowered to make major decisions about their product. The team is usually created at the inception of the new product idea, and they stay with it indefinitely if it becomes a viable business. Instead of being assigned on a temporary basis, as in the matrix structure, team members are assigned permanently to that team in most cases. This results in much lower coordination costs and, since every function is represented, usually reduces the number of management levels above the team level needed to approve team decisions.

It appears that product teams formed at the beginning of product-development processes generate cross-functional understanding that irons out early product or process design problems. They also reduce costs associated with design, manufacturing, and marketing, while typically speeding up innovation and customer responsiveness because authority rests with the team allowing decisions to be made more quickly. That ability to make speedier, cost-saving decisions has the added advantage of eliminating the need for one or more management layers above the team level, which would traditionally have been in place to review and control these types of decisions. While seemingly obvious, it has only recently become apparent that those additional management layers were also making these decisions with less firsthand understanding of the issues involved than the cross-functional team members brought to the product or process in the first place. Exhibit 10–6, Strategy in Action, gives examples of a product-team approach at several well-known companies and some of the advantages that appear to have accrued.

Take Advantage of Being a Virtual Organization

True twenty-first century corporations will increasingly see their structure become an elaborate network of external and internal relationships. This organizational phenomenon has been termed the *virtual organization,* which is defined as a temporary network of inde-

Strategy in Action

Increased Use of Cross-Functional Product Teams in Twenty-first Century Winners

Exhibit 10–6

BusinessWeek Building teams is a new organization art form for Corporate America. Getting people to work together successfully has become a critical managerial skill. Those companies that learn the secrets of creating cross-functional teams are winning the battle for global market share and profits. Those that don't are losing out.

One of the most effective uses of the cross-functional teams is in the area of product development—everything from designing cars to developing new prescription drugs. This kind of teamwork not only increases efficiency but boosts innovation—the holy grail of companies hoping to produce the Next Big Thing in their industry. General Motors, for one, chalked up big wins since setting up a collaborative engineering system in 2000 that allows GM employees and external auto parts suppliers to share product design information. Previously, GM had no way of coordinating its complex designs across its 14 engineering sites scattered across the world, plus the dozens of partners who design subsystems. Now, GM's collaboration system serves as a centralized clearinghouse for all the design data. More than 16,000 designers and other workers use the new Web system from Electronic Data Systems Corp. to share 3-D designs and keep track of parts and subassemblies. The system automatically updates the master design when changes are finalized so everyone is on the same page. The result: GM has slashed the time it takes to complete a full mock-up of a car from 12 weeks to two. The time saved by online collaboration frees up workers to think more creatively—mocking up three or four more alternative designs per car.

Consider Modicon Inc., a North Andover (Massachusetts) maker of automation-control equipment with annual revenues of $300 million. Instead of viewing product development as a task of the engineering function, President Paul White defined it more broadly as a process that would involve a team of 15 managers from engineering, manufacturing, marketing, sales, and finance. By working together, Modicon's team avoided costly delays from disagreements and misunderstandings. "In the past," says White, "an engineering team would have worked on this alone with some dialogue from marketing. Manufacturing wouldn't get involved until the design was brought into the factory. Now, all the business issues are right on the table from the beginning." The change allowed Modicon to bring six software products to market in one-third the time it would normally take. The company still has a management structure organized by function. But many of the company's 900 employees are involved in up to 30 teams that span several functions and departments. Predicts White: "In five years, we'll still have some formal functional structure, but people will probably feel free enough to spend the majority of their time outside their functions."

Eastman Chemical Co., the $3.5 billion unit of Eastman Kodak Co. recently spun off as a stand-alone company, replaced several of its senior vice-presidents in charge of the key functions with "self-directed work teams." Instead of having a head of manufacturing, for example, the company uses a team consisting of all its plant managers. "It was the most dramatic change in the company's 70-year history," maintains Ernest W. Deavenport Jr., president of Eastman Chemical. "It makes people take off their organizational hats and put on their team hats. It gives people a much broader perspective and forces decision-making down at least another level." In creating the new organization, the 500 senior managers agreed that the primary role of the functions was to support Eastman's business in chemicals, plastics, fibers, and polymers. "A function does not and should not have a mission of its own," insists Deavenport. Common sense? Of course. But over the years, the functional departments had grown strong and powerful, as they have in many organizations, often at the expense of the overall company as they fought to protect and build turf. Now, virtually all of the company's managers work on at least one cross-functional team, and most work on two or more on a daily basis. For example, Tom O. Nethery, a group vice-president, runs an industrial-business group. But he also serves on three other teams that deal with such diverse issues as human resources, cellulose technology, and product-support services.

Source: "The New Teamwork," *BusinessWeek,* Feb. 18, 2002.

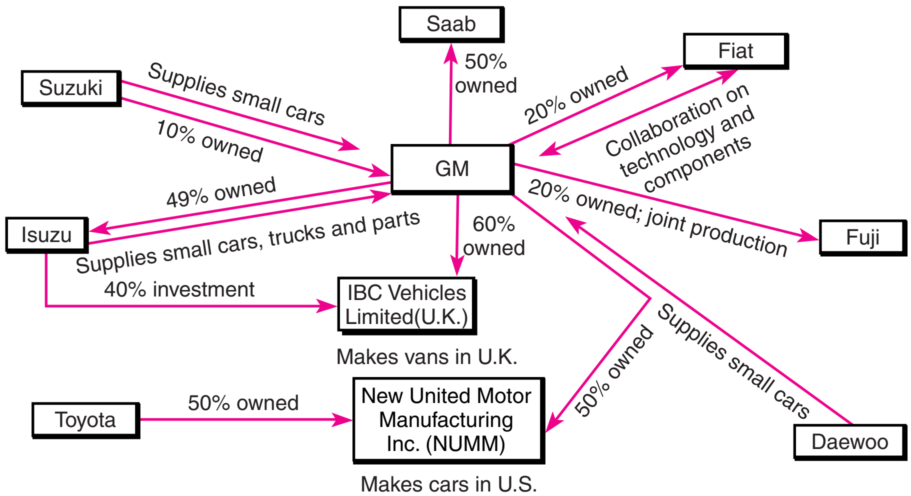
pendent companies—suppliers, customers, subcontractors, even competitors—linked primarily by information technology to share skills, access to markets, and costs.[9] Outsourcing along with strategic alliances are integral in making a virtual organization work. Globalization has accelerated the use of and need for the virtual organization.

Outsourcing was an early driving force for the virtual organization trend. Dell does not make PCs. Cisco doesn't make its world renowned routers. Motorola doesn't make cell phones. Sony makes Apple's low-end PowerBook computers. *Outsourcing* is simply obtaining

[9] W. H. Davidow and M. S. Malone, *The Virtual Corporation* (New York: Harper, 1992).

EXHIBIT 10–7
General Motors: Alliances with Competitors

Source: General Motors Corporation Annual Reports; "Carmakers Take Two Routes to Global Growth," *Financial Times* (July 11, 2000), p. 19.



work previously done by employees inside the companies from sources outside the company. Managers have found that as they attempt to restructure their organizations, particularly if they do so from a business process orientation, numerous activities can often be found in their company that are not "strategically critical activities." This has particularly been the case of numerous staff activities and administrative control processes previously the domain of various middle management levels in an organization. But it can also refer to primary activities that are steps in their business's value chain—purchasing, shipping, making certain parts, and so on. Further scrutiny has led managers to conclude that these activities not only add little or no value to the product or services, but that they can be done much more cost effectively (and competently) by other businesses specializing in these activities. If this is so, then the business can enhance its competitive advantage by outsourcing the activities. Many organizations have outsourced information processing, various personnel activities, and production of parts that can be done better outside the company. Outsourcing, then, can be a source of competitive advantage and result in a leaner, flatter organizational structure.

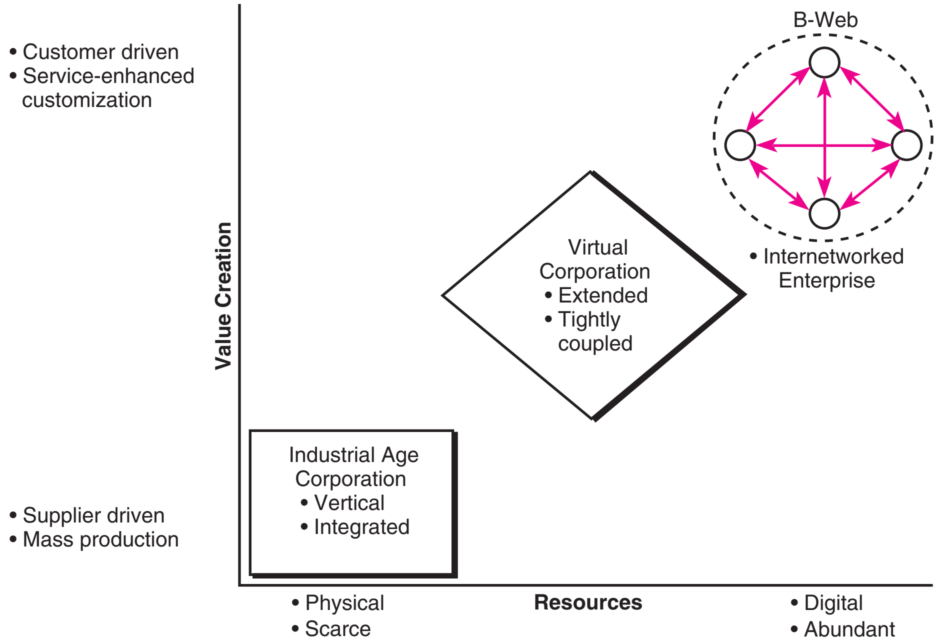
Strategic alliances, some long-term and others for very short periods, with suppliers, partners, contractors, and other providers of world class capabilities allow partners to the alliance to focus on what they do best, farm out everything else, and quickly provide value to the customer. Engaging in alliances, whether long term or one time, lets each participant take advantage of fleeting opportunities quickly, usually without tying up vast amounts of capital. FedEx and the U.S. Postal Service have formed an alliance—FedEx planes carry USPS next-day letters and USPS delivers FedEx ground packages—to allow both to challenge their common rival, UPS. Exhibit 10–7 shows how General Motors, in its effort to become more competitive globally, has entered into numerous alliances with competitors. Cisco owns only two of 34 plants that produce its routers, and over 50 percent of all orders fulfilled by Cisco are done without a Cisco employee being involved.

Web-Based Organizations As we noted at the beginning of this section, globalization has accelerated many changes in the way organizations are structured, and that is certainly the case in driving the need to become part of a virtual organization or make use of one. Technology, particularly driven by the Internet, has and will be a major driver of the virtual organization. Commenting on technology's impact on Cisco, John Chambers observed that with all its outsourcing and strategic alliances, roughly 90 percent of all orders come into Cisco without ever being touched by human hands. "To my customers, it looks like one big virtual plant where my suppliers and inventory systems are directly tied into our virtual or-

EXHIBIT 10–8

From Traditional Structure to B-Web Structure

Source: Adapted and reprinted by permission of Harvard Business School Press. From *Digital Capital: Harnessing the Power of Business Webs* by Don Tapscott, David Ticoll, and Alex Lowy, Boston, MA 1993, p. 18. Copyright © 1993 by Don Tapscott, David Ticoll, and Alex Lowy; all rights reserved.



ganization," he said. "That will be the norm in the future. Everything will be completely connected, both within a company and between companies. The people who get that will have a huge competitive advantage."

The Web's contribution electronically has simultaneously become the best analogy in explaining the future virtual organization. So it is not just the Web as in the Internet, but a web-like shape of successful organizational structures in the future. If there are a pair of images that symbolize the vast changes at work, they are the pyramid and the web. The organizational chart of large-scale enterprise had long been defined as a pyramid of ever-shrinking layers leading to an omnipotent CEO at its apex. The twenty-first century corporation, in contrast, is far more likely to look like a web: a flat, intricately woven form that links partners, employees, external contractors, suppliers, and customers in various collaborations. The players will grow more and more interdependent. Fewer companies will try to master all the disciplines necessary to produce and market their goods but will instead outsource skills—from research and development to manufacturing—to outsiders who can perform those functions with greater efficiency.[10] Exhibit 10–8 illustrates this evolution in organization structure to what it calls the B-Web, a truly Internet-driven form of organization designed to deliver speed, customized service-enhanced products to savvy customers from an integrated virtual B-Web organization pulling together abundant, world-class resources digitally.

Managing this intricate network of partners, spin-off enterprises, contractors, and free-lancers will be as important as managing internal operations. Indeed, it will be hard to tell the difference. All of these constituents will be directly linked in ways that will make it nearly impossible for outsiders to know where an individual firm begins and where it ends. "Companies will be much more molecular and fluid," predicts Don Tapscott, co-author of *Digital Capital.* "They will be autonomous business units connected not necessarily by a big building but across geographies all based on networks. The boundaries of the firm will be not only fluid or blurred but in some cases hard to define."[11]

[10] "The 21st Century Organization," *BusinessWeek,* August 28, 2000.
[11] Ibid.

Remove Structural Barriers and Create a Boundaryless, Ambidextrous Learning Organization

The evolution of the virtual organizational structure as an integral mechanism managers use to implement strategy has brought with it recognition of the central role knowledge plays in this process. *Knowledge* may be in terms of operating know-how, relationships with and knowledge of customer networks, technical knowledge upon which products or processes are based or will be, relationships with key people or a certain person than can get things done quickly, and so forth. Exhibit 10–9, Strategy in Action, shares how McKinsey organizational expert Lowell Bryan sees this shaping future organizational structure with managers becoming knowledge "nodes" through which intricate networks of personal relationships—inside and outside the formal organization—are constantly coordinated to bring together relevant know-how and successful action.

Management icon Jack Welch coined the term *boundaryless* organization, to characterize what he attempted to make GE become in order for it to be able to generate knowledge, share knowledge and get knowledge to the places it could be best used to provide superior value. A key component of this concept was erasing internal divisions so the people in GE could work across functional, business, and geographic boundaries to achieve an integrated diversity—the ability to transfer the best ideas, the most developed knowledge, and the most valuable people quickly, easily, and freely throughout GE. Here is his description:

> Boundaryless behavior is the soul of today's GE . . . Simply put, people seem compelled to build layers and walls between themselves and others, and that human tendency tends to be magnified in large, old institutions like ours. These walls cramp people, inhibit creativity, waste time, restrict vision, smother dreams and above all, slow things down . . . Boundaryless behavior shows up in actions of a woman from our Appliances Business in Hong Kong helping NBC with contacts needed to develop satellite television service in Asia . . . And finally, boundaryless behavior means exploiting one of the unmatchable advantages a multibusiness GE has over almost any other company in the world. Boundaryless behavior combines 12 huge global businesses—each number one or number two in its markets—into a vast laboratory whose principal product is new ideas, coupled with a common commitment to spread them throughout the Company.
>
> —Letter to Shareholders, Jack Welch
> Chairman, General Electric Company, 1981–2001

A shift from what Subramanian Rangan calls *exploitation to exploration* indicates the growing importance of organizational structures that enable a *learning organization* to allow global companies the chance to build competitive advantage.[12] Rather than going to markets to exploit brands or for inexpensive resources, in Rangan's view, the smart ones are going global to learn. This shift in the intent of the structure, then, is to seek information, to create new competences. Demand in another part of the world could be a new product trendsetter at home. So a firm's structure needs to be organized to enable learning, to share knowledge, to create opportunities to create it. Others look to companies like 3M or Procter & Gamble that allow slack time, new product champions, manager mentors—all put in place in the structure to provide resources, support, and advocacy for cross-functional collaboration leading to innovation in new product development, the generation and use of new ideas. This perspective is similar to the boundaryless notion—accommodate the speed of change and therefore opportunity by freeing up historical constraints found in traditional organizational approaches. So having structures that emphasize coordination over control, that allow flexibility (are *ambidextrous*), that emphasize the value and importance of informal relationships

[12] Subramanian Rangan, *A Prism on Globalization* (Fountainebleau, FR.: INSEAD, 1999).

Strategy in Action

Q&A with McKinsey's Lowell Bryan about Organizational Structures

Exhibit 10–9

BusinessWeek Lowell Bryan, a senior partner and director at consultancy McKinsey & Co., leads McKinsey's global industries practice and is the author of *Race for the World: Strategies to Build a Great Global Firm* and *Market Unbound: Unleashing Global Capitalism.*

Q: How will global companies be managed in the twenty-first century?

A: Describing it is hard because the language of management is based on command-and-control structures and "who reports to whom." Now, the manager is more of a network operator. He is part of a country team and part of a business unit. Some companies don't even have country managers anymore.

Q: What is the toughest challenge in managing global companies today?

A: Management structures are now three-dimensional. You have to manage by geography, products, and global customers. The real issue is building networked structures between those three dimensions. That is the state of the art. It's getting away from classic power issues. Managers are becoming nodes, which are part of geographical structures and part of a business unit.

Q: What are the telltale questions that reflect whether a company is truly global?

A: CEOs should ask themselves four questions: First, how do people interact with each other: Do employees around the world know each other and communicate regularly? Second, do management processes reflect a network or an old-style hierarchy? Third, is information provided to everyone simultaneously? And fourth, is the company led from the bottom up, not the top down?

Q: Why do multinationals that have operated for decades in foreign markets need to overhaul their management structures?

A: The sheer velocity of decisions that must be made is impossible in a company depending on an old-style vertical hierarchy. Think of a company [like] Cisco that is negotiating 50 to 60 alliances at one time. The old corporate structures [can't] integrate these decisions fast enough. The CEO used to be involved in every acquisition, every alliance. Now, the role of the corporate center is different. Real business decisions move down to the level of business units.

Q: If there is not clear hierarchy, and managers have conflicting opinions, how does top management know when to take a decision? Doesn't that raise the risk of delay and inaction?

A: In the old centralized model, there was no communication. If you have multiple minds at work on a problem, the feedback is much quicker. If five managers or "nodes" in the network say something is not working right, management better sit up and take notice.

Q: Are there any secrets to designing a new management architecture?

A: Many structures will work. [H]aving the talent and capabilities you need to make a more fluid structure work [is key]. [But] it's much harder to do. The key is to create horizontal flow across silos to meet customers needs. The question is how you network across these silos. [G]etting people to work together [is paramount]. That's the revolution that is going on now.

Q: What is the role of the CEO?

A: The CEO is the architect. He puts in place the conditions to let the organization innovate. No one is smart enough to do it alone anymore. Corporate restructuring should liberate the company from the past. As you break down old formal structures, knowledge workers are the nodes or the glue that hold different parts of the company together. They are the network. Nodes are what it is all about.

Q: How do you evaluate performance in such a squishy system?

A: The role of the corporate center is to worry about talent and how people do relative to each other. Workers build a set of intangibles around who they are. If they are not compensated for their value-added, they will go somewhere else.

Source: *BusinessWeek,* August 28, 2000.

and interaction over formal systems, techniques, and controls are all characteristics associated with what are seen as effective structures for the twenty-first century.

Redefine the Role of Corporate Headquarters from Control to Support and Coordination

The role of corporate management is multibusiness, and multinational companies increasingly face a common dilemma—how can the resource advantages of a large company be exploited, while ensuring the responsiveness and creativity found in the small companies against which each of their businesses compete? This dilemma constantly presents managers with conflicting priorities or adjustments as corporate managers:[13]

- Rigorous financial controls and reporting enable cost efficiency, resource deployment, and autonomy across different units; flexible controls are conductive to responsiveness, innovation and "boundary spanning."
- Multibusiness companies historically gain advantage by exploiting resources and capabilities across different business and markets, yet competitive advantage in the future increasingly depends on the creation of new resources and capabilities.
- Aggressive portfolio management seeking maximum shareholder value is often best achieved through independent businesses; the creation of competitive advantage increasingly requires the management—recognition and coordination—of business interdependencies.

Increasingly, globally engaged multibusiness companies are changing the role of corporate headquarters from one of control, resource allocation, and performance monitoring to one of coordinator of linkages across multiple business, supporter and enabler of innovation and synergy. One way this has been done is to create an executive council comprised of top managers from each business, usually including four to five of their key managers, with the council then serving as the critical forum for corporate decision, discussions, and analysis. Exhibit 10–1, Strategy in Action, at the beginning of this chapter showed this type of forum as central to HP's radical restructuring. GE created this approach over 20 years ago in its rise to top corporate success. These councils replace the traditional corporate staff function of overseeing and evaluating various business units, replacing it instead with a forum to share business unit plans, to discuss problems and issues, to seek assistance and expertise, and to foster cooperation and innovation.

Welch's experience at GE provides a useful example. Upon becoming chairman, he viewed GE headquarters as interfering too much in GE's various businesses, generating too much paperwork, and offering minimal value added. He sought to "turn their role 180 degrees from checker, inquisitor, and authority figure to facilitator, helper, and supporter of GE's 13 businesses." He said, "What we do here at headquarters . . . is to multiply the resources we have, the human resources, the financial resources, and the best practices . . . Our job is to help, it's to assist, it's to make these businesses stronger, to help them grow and be more powerful." GE's Corporate Executive Council was reconstituted from predominantly a corporate level group of sector managers (which was eliminated) into a group comprised of the leaders of GE's 13 businesses and a few corporate executives. They met formally two days each quarter to discuss problems and issues and to enable cooperation and resource sharing. This has expanded to other councils throughout GE intent on greater coordination, synergy, and idea sharing.

[13] Robert M. Grant, *Contemporary Strategy Analysis* (Oxford: Blackwell, 2001), p. 503.

ORGANIZATIONAL LEADERSHIP

The job of leading a company has never been more demanding, and it will only get tougher in the twenty-first century. The CEO will retain ultimate authority, but the corporation will depend increasingly on the skills of the CEO and a host of subordinate leaders. The accelerated pace and complexity of business will continue to force corporations to push authority down through increasingly horizontal management structures. In the future, every line manager will have to exercise leadership's prerogatives—and bear its burdens—to an extent unthinkable 20 years ago.[14]

John Kotter, a widely recognized leadership expert, predicted this evolving role of leadership in an organization when he distinguished between management and leadership:[15]

> Management is about coping with complexity. Its practices and procedures are largely a response to one of the most significant developments of the twentieth century: the emergence of large organizations. Without good management, complex enterprises tend to become chaotic in ways that threaten their very existence. Good management brings a degree of order and consistency to key dimensions like the quality and profitability of products.
>
> Leadership, by contrast, is about coping with change. Part of the reason it has become so important in recent years is that the business world has become more competitive and more volatile. . . . The net result is that doing what was done yesterday, or doing it 5 percent better, is no longer a formula for success. Major changes are more and more necessary to survive and compete effectively in this new environment. More change always demands more leadership.

Organizational leadership, then, involves action on two fronts. The first is in guiding the organization to deal with constant change. This requires CEOs that embrace change, and that do so by clarifying strategic intent, that build their organization and shape their culture to fit with opportunities and challenges change affords. *BusinessWeek* Strategy in Action, Exhibit 10–10, provides an interview with P&G CEO Alan Lafley, who *BusinessWeek* calls "a catalyst and encourager of change," to explore Lafley's thoughts on doing these very things. The second front is in providing the management skill to cope with the ramifications of constant change. This means identifying and supplying the organization with operating managers prepared to provide operational leadership and vision as never before. Let's explore each of these five aspects to organizational leadership.

Strategic Leadership: Embracing Change

The blending of telecommunications, computers, the Internet, and one global marketplace has increased the pace of change exponentially during the last 10 years. All business organizations are affected. Change has become an integral part of what leaders and managers deal with daily.

The leadership challenge is to galvanize commitment among people within an organization as well as stakeholders outside the organization to embrace change and implement strategies intended to position the organization to do so. Leaders galvanize commitment to embrace change through three interrelated activities: clarifying strategic intent, building an organization, and shaping organizational culture.

Clarifying Strategic Intent

Leaders help stakeholders embrace change by setting forth a clear vision of where the business's strategy needs to take the organization. Traditionally, the concept of vision has been

[14] Anthony Bianco, "The New Leadership," *BusinessWeek,* August 28, 2000.
[15] John P. Kotter, "What Leaders Really Do," *Harvard Business Review,* May–June, 1990, p. 104.

Strategy in Action
A Catalyst and Encourager of Change

Exhibit 10–10

BusinessWeek

Chief Exec. A. G. Lafley says he shares his predecessor's zeal to revamp P&G. The difference is the approach. Since becoming Procter & Gamble's chief executive in June 2000, Alan G. "A.G." Lafley has led a turnaround that has defied expectations. In 2003 P&G posted a 13 percent increase in net income on 8 percent higher sales. That would bring P&G's annual compounded earnings growth rate under the three years of Lafley's leadership to 15 percent—a rate well above rivals. During that period, P&G's stock price has climbed by 58 percent, while the Standard & Poor's 500-stock index fell by 32 percent.

Less obvious than his turnaround success, however, is how Lafley is changing P&G. He's undertaking the company's most sweeping remake since it was founded in 1837. Nothing is sacred any longer at the Cincinnati-based maker of Tide, Pampers, and Crest.

Lafley has inverted the invent-it-here mentality by turning outwards for innovation. He's broadening P&G's definition of brands and how it prices goods. He's moving P&G deep into the beauty-care business with its two largest acquisitions ever, Clairol in 2001 and Wella in 2003. And he's redefining P&G's core business by outsourcing operations—like information technology and bar-soap manufacturing.

What's surprising is that at the start, Lafley was perceived as a tame pair of hands—far from a person who would conduct a radical makeover. He followed a forceful change agent, Durk Jager, who had tried to jump-start internal innovation, launching a host of new brands. Jager also criticized P&G's insular culture, which he sought to shake up. In the end, though, he overreached, as P&G missed earnings forecasts and employees bucked under his leadership.

Lafley answered some questions recently about his views on leading **change** at P&G:

Q: When you started, you weren't perceived as a forceful change agent like your predecessor. Yet you're making more dramatic changes. Can you discuss that?

A: Durk and I had believed very strongly that the company had to change and make fundamental changes in a lot of the same directions. There are two simple differences: One is I'm very externally focused. I expressed the change in the context of how we're going to serve consumers better, how we're going to win with the retailer, and how we're going to defeat the competitor in the marketplace.

The most important thing—I didn't attack. I avoided saying P&G people are bad. I thought that was a big mistake [on Jager's part]. The difference is, I preserved the core of the culture and pulled people where I wanted to go. I enrolled them in change. I didn't tell them.

Q: Why did you both see a need for change?

A: We were looking at slow growth. An inability to move quickly, to commercialize on innovation and get full advantage out of it. We were looking at new technologies that were changing competition in our industry, retailers, and the supply base. We were looking at a world that all of a sudden was going to go 24/7, and we weren't ready for that kind of world.

Q: Was the view on the need for change widely held within P&G?

A: It depends on who you ask. Without a doubt, Durk and I and a few others were in the camp of "We need a much bigger change."

a description or picture of what the company could be that accommodates the needs of all its stakeholders. The intensely competitive, rapidly changing global marketplace has refined this to be targeting a very narrowly defined strategic intent—*an articulation of a simple criterion or characterization of what the company must become to establish and sustain global leadership.* Former IBM CEO Lou Gerstner is a good example of a leader in the middle of trying to shape strategic intent. "One of the great things about this industry is that every decade or so, you get a chance to redefine the playing field," said Gerstner. "We're in that phase of redefinition right now, and winners or losers are going to emerge from it. We've got to become *the leader in 'network-centric computing.'*" It's an opportunity brought about by telecommunications-based change that will change IBM more than semiconductors did in the last decade. Said Gerstner, "I sensed there were too many people inside IBM who wanted to fight the war we lost," referring to PCs and PC software, so he aggressively instilled network-centric computing as the strategic intent for IBM in the next decade.

continued

Exhibit 10–10

Q: Jager says he tried to change P&G too fast. What do you think about that?

A: I think he's right.

Q: Are you concerned about the same thing?

A: I'm worried that I will ask the organization to change ahead of its understanding, capability, and commitment, because that's a problem. I have been a catalyst of change and encourager of change and a coach of change management. And I've tried not to drive change for a sake of change.

Q: How do you pace change?

A: I have tremendous trust in my management team. I let them be the brake. I am the accelerator. I help with direction and let them make the business strategic choices.

Q: Did the fact that P&G was in crisis when you came in help you implement change?

A: It was easier. I was lucky. When you have a mess, you have a chance to make more changes.

Q: Jager tried to drive innovation from within. You would like P&G to ultimately get 50 percent of its ideas from outside. Why?

A: Durk and I both wanted more innovation. We both felt we absolutely, positively had to get more innovation. We had to get more innovation commercialized and more innovation globalized. So we were totally together.

He tried to drive it all internally. He tried to rev the R&D organization, supercharge them, and hoped that enough would come out of there that we would achieve the goals of commercializing more of it and globalizing more of it. We got in trouble cause we pulled stuff out that was half-baked or that was never going to be successful. We hadn't developed it far enough.

The difference is that my hypothesis is that innovation and discovery are likely to come from anywhere. What P&G is really good at is developing innovations and commercializing them. So what I said is, "We need an open marketplace."

We're probably as good as the next guy at inventing. But we are not absolutely and positively better than everybody else at inventing. There are a lot of good inventors out there.

Q: How hard will it be to shift P&G's R&D focus outwards, given that it has historically focused inwards?

A: It will be a challenge, but I think we'll get there. It's like a flywheel. That first turn is really difficult. Then the second turn is a little bit easier. This has been like turning a flywheel. We will have failures. We will have to celebrate that failure.

Q: When you couple your outward focus on innovation with your moves toward outsourcing, it seems you're making P&G a less vertically integrated company.

A: I don't believe in vertical integration. I think it's a trap. I believe in horizontal networked organizations.

Our core capability is to develop and commercialize. Branding is a core capability. Customer business development is a core capability. We concluded in a lot of areas that manufacturing isn't. Therefore, I let the businesses go do more outsourcing. We concluded that running a back room wasn't a core capability. You do what you do best and can do world-class.

Source: "P&G: New & Improved," *BusinessWeek*, July 7, 2003.

Clarifying strategic intent can come in many different forms. Coca-Cola's legendary former CEO and Chairman Roberto Goizueta said, "Our company is a global business system for which we raise capital to make concentrate and sell it at an operating profit. Then we pay the cost of that capital. Shareholders pocket the difference." Coke averaged 27 percent annual return on stockholder equity for 18 years under his leadership.

Exhibit 10–10 shows how CEO Alan Lafley articulates a radically different strategic intent for the *new* P&G that involves P&G's legendary R&D focusing outward, instead of inward and outsourcing noncore activities in a historically vertically integrated firm. While Coke and P&G are very different situations, their leaders were both very effective in shaping and clarifying strategic intent in a way that helped stakeholders understand what needed to be done.

Building an Organization

The previous section examined alternative structures to use in designing the organization necessary to implement strategy. Leaders spend considerable time shaping and refining their organizational structure and making it function effectively to accomplish strategic intent. Since leaders are attempting to embrace change, they are often rebuilding or remaking their organization to align it with the ever-changing environment and needs of the strategy. And since embracing change often involves overcoming resistance to change, leaders find themselves addressing problems like the following as they attempt to build or rebuild their organization:

- Ensuring a common understanding about organizational priorities.
- Clarifying responsibilities among managers and organizational units.
- Empowering newer managers and pushing authority lower in the organization.
- Uncovering and remedying problems in coordination and communication across the organization.
- Gaining the personal commitment to a shared vision from managers throughout the organization.
- Keeping closely connected with "what's going on in the organization and with its customers."

Leaders do this in many ways. Larry Bossidy, Chairman of Honeywell and co-author of the best seller, *Execution*, spends 50 percent of his time each year flying to Allied Signal's various operations around the world meeting with managers and discussing decisions, results, and progress. Bill Gates at Microsoft reportedly spent two hours each day reading and sending E-mail to any of Microsoft's 36,000 employees that want to contact him. All managers adapt structures, create teams, implement systems, and otherwise generate ways to coordinate, integrate, and share information about what their organization is doing and might do. Others create customer advisory groups, supplier partnerships, R&D joint ventures, and other adjustments to build an adaptable, learning organization that embraces the leader's vision and strategic intent and the change driving the future opportunities facing the business. These, in addition to the fundamental structural guidelines described in the previous section for restructuring to support strategically critical activities, are the issues leaders constantly address as they attempt to build a supportive organization.

Shaping Organization Culture

Leaders know well that the values and beliefs shared throughout their organization will shape how the work of the organization is done. And when attempting to embrace accelerated change, reshaping their organization's culture is an activity that occupies considerable time for most leaders. Listen to these observations by and about Ryanair CEO Michael O'Leary about competing in the increasingly competitive European airline industry and arch-rival easyJet:

> It was vintage Michael O'Leary. On May 13, the 42-year-old CEO of Dublin-based discount airline Ryanair outfitted his staff in full combat gear, drove an old World War II tank to England's Luton airport, an hour north of London, then demanded access to the base of archrival easyJet Airline Co. With the theme to the old television series The A-Team blaring, O'Leary declared he was "liberating the public from easyJet's high fares." When security—surprise!—refused to let the Ryanair armor roll in, O'Leary led the troops in his own rendition of a platoon march song: "I've been told and it's no lie. EasyJet's fares are way too high!" So it is that there are new rivals for O'Leary to conquer. "When we were a much smaller company, we compared ourselves to British Airways. But they are such a mess, most people just feel sorry for them," O'Leary says. "Now we're turning the guns on easyJet."[16]

It appears that Ryanair CEO O'Leary wanted an organizational culture that was aggressive, competitive and somewhat free-wheeling in order to take advantage of change in the

[16] "Ryanair Rising," *BusinessWeek,* June 2, 2003.

Strategy in Action
A Résumé for the Twenty-first Century

Exhibit 10–11

BusinessWeek

EXPERIENCE

- Multinational Corp.—Worked with top-notch mentors in an established company with global operations. Managed a talented and fickle staff and helped tap new markets.
- Foreign Operation LLC—A stint at a subsidiary of a U.S. company, or at a foreign operation in a local market. Exposure to different cultures, conditions, and ways of doing business.
- Startup Inc.—Helped to build a business from the ground up, assisting with everything from product development to market research. Honed entrepreneurial skills.
- Major Competitor Ltd.—Scooped up by the competition and exposed to more than one corporate culture.

EDUCATION

- Liberal Arts University—Majored in economics, but took courses in psychology (how to motivate customers and employees), foreign language (the world is a lot bigger than the 50 states), and philosophy (to seek vision and meaning in your work).
- Graduate Studies—The subject almost doesn't matter, so long as you developed your thinking and analytical skills.

EXTRACURRICULAR

- Debating (where you learned to market ideas and think on your feet).
- Sports (where you learned discipline and teamwork).
- Volunteer work (where you learned to step outside your own narrow world to help others).
- Travel (where you learned about different cultures).

Source: "A Résumé for the 21st Century," *BusinessWeek,* August 28, 2000.

European airline industry. He did this by example, by expectations felt by his managers, and in the way decision making is approached within Ryanair.

Leaders use reward systems, symbols, and structure among other means to shape the organization's culture. Travelers' Insurance Co.'s notable turnaround was accomplished in part by changing its "hidebound" culture through a change in its agent reward system. Employees previously on salary with occasional bonuses were given rewards that involved substantial cash bonuses and stock options. Observed a customer and risk management director at drugmaker Becton Dickinson, "They're hungrier now. They want to make deals. They're different than the old, hidebound Travelers' culture."

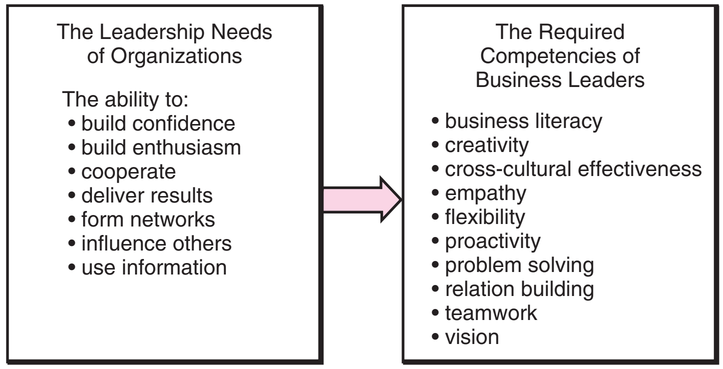
As leaders clarify strategic intent, build an organization, and shape their organization's culture, they look to one key element to help—their management team throughout their organization. As Honeywell's Chairman Larry Bossidy candidly observed when asked about how after 42 years at General Electric, Allied Signal and now Honeywell with seemingly drab businesses he could expect exciting growth: "There's no such thing as a mature market. What we need is mature executives who can find ways to grow." Leaders look to managers they need to execute strategy as another source of leadership to accept risk and cope with the complexity that change brings about. So assignment of key managers becomes a leadership tool.

Recruiting and Developing Talented Operational Leadership

As we noted at the beginning of this section on Organizational Leadership, the accelerated pace and complexity of business will increase pressure on corporations to push authority down in their organizations ultimately meaning that every line manager will have to exercise leadership's prerogatives to an extent unthinkable a generation earlier. They will each be global managers, change agents, strategists, motivators, strategic decision-makers, innovators, and collaborators if the business is to survive and prosper. Exhibit 10–11, Strategy in

EXHIBIT 10–12
What Competencies Should Managers Possess?

Source: From Ruth L. Williams and Joseph P. Cothrel, "Building Tomorrow's Leaders Today," *Strategy and Leadership,* Vol. 26, October 1997, Reprinted with permission of Emerald Group Publishing Limited.



Action, provides an interesting perspective on this reality showing *BusinessWeek*'s version of a résumé for the typical twenty-first century operating manager every company will be looking for in today's fast-paced, global marketplace.

Today's need for fluid, learning organizations capable of rapid response, sharing, and cross-cultural synergy place incredible demands on young managers to bring important competencies to the organization. Exhibit 10–12 describes the needs organizations look to managers to meet, and then identifies the corresponding competencies managers would need to do so. Ruth Williams and Joseph Cothrel drew this conclusion in their research about competencies needed from managers in today's fast-changing business environment:[17]

> Today's competitive environment requires a different set of management competencies than we traditionally associate with the role. The balance has clearly shifted from attributes traditionally thought of as masculine (strong decision making, leading the troops, driving strategy, waging competitive battle) to more feminine qualities (listening, relationship-building, and nurturing). The model today is not so much "take it on your shoulders" as it is to "create the environment that will enable others to carry part of the burden." The focus is on unlocking the organization's human asset potential.

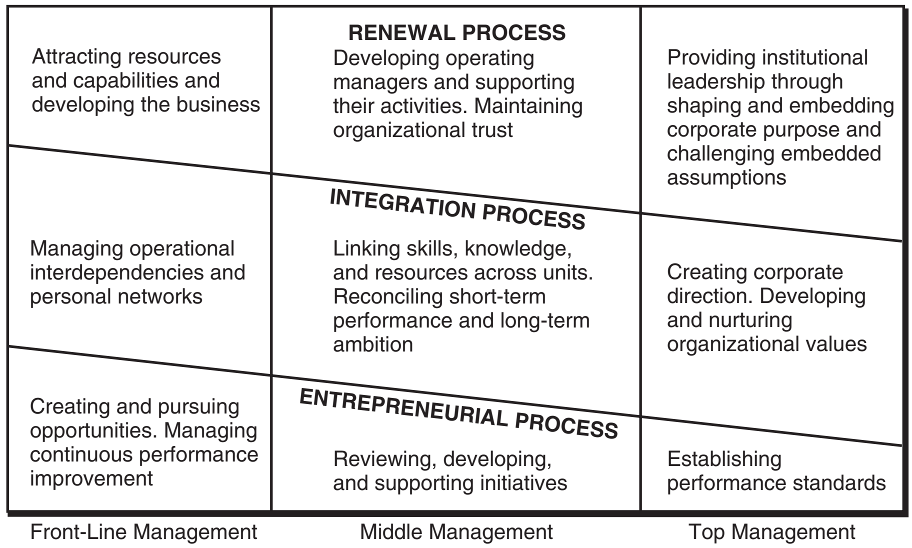
Researcher David Goleman addressed the question of what types of personality attributes generate the type of competencies described in Exhibit 10–12. His research suggested that a set of four characteristics commonly referred to as emotional intelligence play a key role in bringing the competencies needed from today's desirable manager:[18]

- *Self-awareness* in terms of the ability to read and understand one's emotions and assess one's strengths and weaknesses, underlain by the confidence that stems from positive self-worth.
- *Self-management* in terms of control, integrity, conscientiousness, initiative, and achievement orientation.
- *Social awareness* in relation to sensing others' emotions (empathy), reading the organization (organizational awareness), and recognizing customers' needs (service orientation).
- *Social skills* in relation to influencing and inspiring others; communicating, collaborating, and building relationships with others; and managing change and conflict.

[17] Ruth Williams and Joseph Cothrel, "Building Tomorrow's Leaders Today," *Strategy and Leadership* 26 (September–October 1997), p. 21.
[18] D. Goleman, "What Makes a Leader?," *Harvard Business Review* (November–December 1998), pp. 93–102.

EXHIBIT 10–13
Management Processes and Levels of Management

Source: C. A. Bartlett and S. Ghoshal, "The Myth of the General Manager: New Personal Competencies for New Management Roles," *California Management Review* 40 (Fall 1997): R. M. Grant, *Contemporary Strategy Analysis* (Oxford: Blackwell, 2001), p. 529.



One additional perspective on the role of organizational leadership and management selection is found in the work of Bartlett and Ghoshal. Their study of several of the most successful global companies in the last decade suggests that combining flexible responsiveness with integration and innovation requires rethinking the management role and the distribution of management roles within a twenty-first century company. They see three critical management roles: the *entrepreneurial process* (decisions about opportunities to pursue and resource deployment), the *integration process* (building and deploying organizational capabilities), and the *renewal process* (shaping organizational purpose and enabling change). Traditionally viewed as the domain of top management, their research suggests that these functions need to be shared and distributed across three management levels as suggested in Exhibit 10–13.[19]

ORGANIZATIONAL CULTURE

Organizational culture is the set of important assumptions (often unstated) that members of an organization share in common. Every organization has its own culture. An organization's culture is similar to an individual's personality—an intangible yet ever-present theme that provides meaning, direction, and the basis for action. In much the same way as personality influences the behavior of an individual, the shared assumptions (beliefs and values) among a firm's members influence opinions and actions within that firm.

A member of an organization can simply be aware of the organization's beliefs and values without sharing them in a personally significant way. Those beliefs and values have more personal meaning if the member views them as a guide to appropriate behavior in the organization and, therefore, complies with them. The member becomes fundamentally committed to the beliefs and values when he or she internalizes them; that is, comes to

[19] C. A. Barlett and S. Ghoshal, "The Myth of the General Manager: New Personal Competencies for New Management Roles," *California Management Review* 40 (Fall 1997), pp. 92–116; and "Beyond Structure to Process," *Harvard Business Review* (January–February 1995).

hold them as personal beliefs and values. In this case, the corresponding behavior is *intrinsically rewarding* for the member—the member derives personal satisfaction from his or her actions in the organization because those actions are congruent with corresponding personal beliefs and values. *Assumptions become shared assumptions through internalization among an organization's individual members.* And those shared, internalized beliefs and values shape the content and account for the strength of an organization's culture.

Leaders typically attempt to manage and create distinct cultures through a variety of ways. Some of the most common ways are as follows:

Emphasize Key Themes or Dominant Values Businesses build strategies around distinct competitive advantages they possess or seek. Quality, differentiation, cost advantages, and speed are four key sources of competitive advantage. So insightful leaders nurture key themes or dominant values within their organization that reinforce competitive advantages they seek to maintain or build. Key themes or dominant values may center around wording in an advertisement. They are often found in internal company communications. They are most often found as a new vocabulary used by company personnel to explain "who we are." At Xerox, the key themes include respect for the individual and services to the customer. At Procter & Gamble (P&G), the overarching value is product quality; McDonald's uncompromising emphasis on QSCV—quality, service, cleanliness, and value—through meticulous attention to detail is legendary; Delta Airlines is driven by the "family feeling" theme, which builds a team spirit and nurtures each employee's cooperative attitude toward others, cheerful outlook toward life, and pride in a job well done. Du Pont's safety orientation—a report of every accident must be on the chairman's desk within 24 hours—has resulted in a safety record that was 17 times better than the chemical industry average and 68 times better than the all-manufacturing average.

Encourage Dissemination of Stories and Legends about Core Values Companies with strong cultures are enthusiastic collectors and tellers of stories, anecdotes, and legends in support of basic beliefs. Frito-Lay's zealous emphasis on customer service is reflected in frequent stories about potato chip route salespeople who have slogged through sleet, mud, hail, snow, and rain to uphold the 99.5 percent service level to customers in which the entire company takes great pride. Milliken (a textile leader) holds "sharing" rallies once every quarter at which teams from all over the company swap success stories and ideas. Typically, more than 100 teams make five-minute presentations over a two-day period. Every rally is designed around a major theme, such as quality, cost reduction, or customer service. No criticisms are allowed, and awards are given to reinforce this institutionalized approach to storytelling. L. L. Bean tells customer service stories; 3M tells innovation stories; P&G, Johnson & Johnson, IBM, and Maytag tell quality stories. These stories are very important in developing an organizational culture, because organization members identify strongly with them and come to share the beliefs and values they support.

Institutionalize Practices That Systematically Reinforce Desired Beliefs and Values Companies with strong cultures are clear on what their beliefs and values need to be and take the process of shaping those beliefs and values very seriously. Most important, the values these companies espouse undergird the strategies they employ. For example, McDonald's has a yearly contest to determine the best hamburger cooker in its chain. First, there is a competition to determine the best hamburger cooker in each store; next, the store winners compete in regional championships; finally, the regional winners compete in the "All-American" contest. The winners, who are widely publicized throughout the company, get trophies and All-American patches to wear on their McDonald's uniforms.

Adapt Some Very Common Themes in Their Own Unique Ways The most typical beliefs that shape organizational culture include (1) a belief in being the best (or, as at GE, "better than the best"); (2) a belief in superior quality and service; (3) a belief in the importance of people as individuals and a faith in their ability to make a strong contribution; (4) a belief in the importance of the details of execution, the nuts and bolts of doing the job well; (5) a belief that customers should reign supreme; (6) a belief in inspiring people to do their best, whatever their ability; (7) a belief in the importance of informal communication; and (8) a belief that growth and profits are essential to a company's well-being. Every company implements these beliefs differently (to fit its particular situation), and every company's values are the handiwork of one or two legendary figures in leadership positions. Accordingly, every company has a distinct culture that it believes no other company can copy successfully. And in companies with strong cultures, managers and workers either accept the norms of the culture or opt out from the culture and leave the company.

The stronger a company's culture and the more that culture is directed toward customers and markets, the less the company uses policy manuals, organization charts, and detailed rules and procedures to enforce discipline and norms. The reason is that the guiding values inherent in the culture convey in crystal-clear fashion what everybody is supposed to do in most situations. Poorly performing companies often have strong cultures. However, their cultures are dysfunctional, being focused on internal politics or operating by the numbers as opposed to emphasizing customers and the people who make and sell the product.

Managing Organizational Culture in a Global Organization[20]

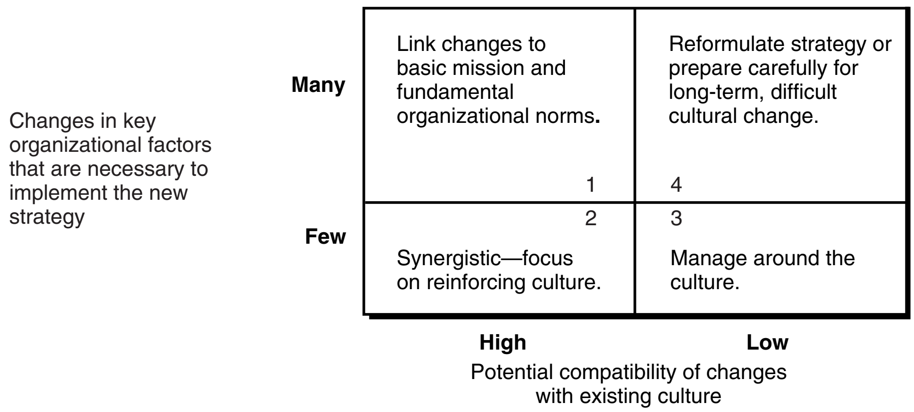
The reality of today's global organizations is that organizational culture must recognize cultural diversity. *Social norms* create differences across national boundaries that influence how people interact, read personal cues, and otherwise interrelate socially. *Values* and *attitudes* about similar circumstances also vary from country to country. Where individualism is central to a North American's value structure, the needs of the group dominate the value structure of their Japanese counterparts. *Religion* is yet another source of cultural differences. Holidays, practices, and belief structures differ in very fundamental ways that must be taken into account as one attempts to shape organizational culture in a global setting. Finally, *education,* or ways people are accustomed to learning, differ across national borders. Formal classroom learning in the United States may teach things that are only learned via apprenticeship in other cultures. Since the process of shaping an organizational culture often involves considerable "education," leaders should be sensitive to global differences in approaches to education to make sure their cultural education efforts are effective. The discussion case on Procter & Gamble at the end of this chapter provides some relevant examples of how CEO Alan Lafley is trying to radically alter P&G's organization's culture.

Managing the Strategy-Culture Relationship

Managers find it difficult to think through the relationship between a firm's culture and the critical factors on which strategy depends. They quickly recognize, however, that key components of the firm—structure, staff, systems, people, style—influence the ways in which key managerial tasks are executed and how critical management relationships are formed. And implementation of a new strategy is largely concerned with adjustments in these components to accommodate the perceived needs of the strategy. Consequently,

[20] Differing backgrounds, often referred to as *cultural diversity,* is something that most managers will certainly see more of, both because of the growing cultural diversity domestically and the obvious diversification of cultural backgrounds that result from global acquisitions and mergers. For example, Harold Epps, manager of DEC's computer keyboard plant in Boston, manages 350 employees representing 44 countries of origin and 19 languages.

EXHIBIT 10–14
Managing the Strategy-Culture Relationship



managing the strategy-culture relationship requires sensitivity to the interaction between the changes necessary to implement the new strategy and the compatibility or "fit" between those changes and the firm's culture. Exhibit 10–14 provides a simple framework for managing the strategy-culture relationship by identifying four basic situations a firm might face.

Link to Mission

A firm in cell 1 is faced with a situation in which implementing a new strategy requires several changes in structure, systems, managerial assignments, operating procedures, or other fundamental aspects of the firm. However, most of the changes are potentially compatible with the existing organizational culture. Firms in this situation usually have a tradition of effective performance and are either seeking to take advantage of a major opportunity or are attempting to redirect major product-market operations consistent with proven core capabilities. Such firms are in a very promising position: They can pursue a strategy requiring major changes but still benefit from the power of cultural reinforcement.

Four basic considerations should be emphasized by firms seeking to manage a strategy-culture relationship in this context. First, *key changes should be visibly linked to the basic company mission.* Since the company mission provides a broad official foundation for the organizational culture, top executives should use all available internal and external forums to reinforce the message that the changes are inextricably linked to it. Second, *emphasis should be placed on the use of existing personnel* where possible to fill positions created to implement the new strategy. Existing personnel embody the shared values and norms that help ensure cultural compatibility as major changes are implemented. Third, *care should be taken if adjustments in the reward system are needed.* These adjustments should be consistent with the current reward system. If, for example, a new product-market thrust requires significant changes in the way sales are made, and, therefore, in incentive compensation, common themes (e.g., incentive oriented) should be emphasized. In this way, current and future reward approaches are related and the changes in the reward system are justified (encourage development of less familiar markets). Fourth, *key attention should be paid to the changes that are least compatible with the current culture,* so current norms are not disrupted. For example, a firm may choose to subcontract an important step in a production process because that step would be incompatible with the current culture.

IBM's strategy in entering the Internet-based market is an illustration. Serving this radically different market required numerous organizational changes. To maintain maximum compatibility with its existing culture while doing so, IBM went to considerable public and internal effort to link its new Internet focus with its long-standing mission. Numerous messages relating the network-centric computing to IBM's tradition of top-quality service appeared on television and in magazines, and every IBM manager was encouraged to go online. Where feasible, IBM personnel were used to fill the new positions created to implement the strategy. But because the software requirements were not compatible with IBM's current operations, virtually all of its initial efforts were linked to newly acquired Lotus Notes Software.

Maximize Synergy

A firm in cell 2 needs only a few organizational changes to implement its new strategy, and those changes are potentially quite compatible with its current culture. A firm in this situation should emphasize two broad themes: (1) *take advantage of the situation to reinforce and solidify the current culture* and (2) *use this time of relative stability to remove organizational roadblocks to the desired culture.* Holiday Inns' move into casino gambling required a few major organizational changes. Holiday Inns saw casinos as resort locations requiring lodging, dining, and gambling/entertainment services. It only had to incorporate gambling/entertainment expertise into its management team, which was already capable of managing the lodging and dining requirements of casino (or any other) resort locations. It successfully inculcated this single major change by selling the change internally as completely compatible with its mission of providing high-quality accommodations for business and leisure travelers. The resignation of Roy Clymer, its CEO, removed an organizational roadblock, legitimizing a culture that placed its highest priority on quality service to the middle-to-upper-income business traveler, rather than a culture that placed its highest priority on family-oriented service. The latter priority was fast disappearing from Holiday Inns' culture, with the encouragement of most of the firm's top management, but its disappearance had not yet been fully sanctioned because of Clymer's personal beliefs. His voluntary departure helped solidify the new values that top management wanted.

Manage around the Culture

A firm in cell 3 must make a few major organizational changes to implement its new strategy, but these changes are potentially inconsistent with the firm's current organizational culture. The critical question for a firm in this situation is whether it can make the changes with a reasonable chance of success.

A firm can manage around the culture in various ways: create a separate firm or division; use task forces, teams, or program coordinators; subcontract; bring in an outsider; or sell out. These are a few of the available options, but the key idea is to create a method of achieving the change desired that avoids confronting the incompatible cultural norms. As cultural resistance diminishes, the change may be absorbed into the firm.

In the Southeast, Rich's was a highly successful, quality-oriented department store chain that served higher income customers in several southeastern locations. With Wal-Mart and Kmart experiencing rapid growth in the sale of mid- to low-priced merchandise, Rich's decided to serve this market as well. Finding such merchandise inconsistent with the successful values and norms of its traditional business, it created a separate business called Richway to tap this growth area in retailing. Through a new store network, it was able to *manage around its culture.* Both Rich's and Richway experienced solid regional success, though their cultures are radically different in some respects.

Reformulate the Strategy or Culture

A firm in cell 4 faces the most difficult challenge in managing the strategy-culture relationship. To implement its new strategy, such a firm must make organizational changes

Strategy in Action

To Fix a Business, Change the Culture

Exhibit 10–15

BusinessWeek *Thomas Charlton, president and CEO of software outfit TIDAL, fits the latter category. As he tells it, the company was going nowhere when he stepped up from his former job as vice-president for sales to helm the entire business, which is based in Mountain View, Calif., and produces job-scheduling software that manages business processes in large corporate data systems.* BusinessWeek Online *invited Charlton to explain the challenges he faced, the steps he took to meet them, and the end result: the fastest-growing independent software vendor in the job-scheduling market.*

The date was May 15, 2000. I was the 33-year-old vice-president of sales for a privately held software company in Silicon Valley. The company had received an initial round of funding and I'd been hired to substantially increase revenues after 17 years of flat growth, and expand the sales organization from a staff of four tele-salespeople. Within 18 months of overhauling sales, our team had grown to almost two-dozen presales and account executives, and five regional offices. Revenues for the company more than doubled.

While my task had been accomplished I saw significant challenges ahead for TIDAL Software. The marketing department erroneously positioned the core product for a niche market, eliminating a huge source of prospects. The vice-president of development was reluctant to make simple changes to the product, even though it would result in winning large competitive deals. The CEO was not providing direction, and TIDAL's board of directors had lost confidence in the management team. And, although revenues had doubled, the infrastructure was growing faster than product sales. TIDAL was losing approximately $800,000 per quarter. We were in desperate need of cash to survive.

STAY OR GO?

Moreover, the dot-com explosion was in full swing and sales-executive positions were plentiful. I was left with a few options: resign, grab one of the dot-com "dangling carrots" and retire in six months—or remain at TIDAL and watch a sinking ship.

The third choice was to make a radical proposal to the board that, if they turned control of the company over to me, we would grow revenues in record time. My recommendation came with one proviso: jettison the executive staff.

By my observation, TIDAL employees had a tremendous commitment to see the company succeed: Our flagship product could easily compete among the larger vendors. Our developers were capable of programming new features in record time and expanding the product line. The intrepid sales reps were unwilling to take "no" for an answer. Senior management, however, wasn't providing the proper mentoring to train and mobilize their teams and sustain the company's growth.

The problem was overwhelmingly a cultural one.

HEADS ROLL

So, on that Monday in May, after receiving board support for taking operational control of the company and initiating a growth plan, the management team was removed . . . all managers in every department, with the exception of sales.

That afternoon, I faced the 40 remaining employees, who had invested a lot of time and energy in the company. I told them that it was up to us as a group of individuals to pull together as a team if we wanted to enjoy some of the Silicon Valley dream. I asked for their commitment over the next 12 months, with the option of evaluating my performance every 30 days. Except for one unplanned turnover no one left the entire year.

Once the foundation was laid, I chose an employee from each department to represent the company and meet with me to create and execute a turn-around plan. Together we engendered a renewed sense of pride for TIDAL. As the new president and CEO, I established the following rules of engagement for fostering a new culture and growing the company:

- Build trust upon reorganizing the company.
- Enlist the support and alignment of remaining employees, and prove my ability to lead.
- Establish a new performance-based culture.
- Instill in each employee that their value to the company is measured by their individual contribution to the organization. Personal relationships are secondary to the needs of the team's objective.
- Get employees very busy with projects that focus on the future and don't give them time to bemoan the past.

that are incompatible with its current, usually entrenched, values and norms. A firm in this situation faces the complex, expensive, and often long-term challenge of changing its culture; it is a challenge that borders on impossible. Exhibit 10–15, Strategy in Action, describes how 33-year-old Thomas Charlton transformed a 17-year-old Silicon Valley software vendor into the fastest-growing job-scheduling software vendor by radically changing its culture.

continued **Exhibit 10–15**

- Pick team leaders from each department and get them engaged with their teams in the success and growth of TIDAL.
- Have each employee set individual goals and objectives for his or her department that contributes to the overall revenue goals.
- Make sure each and every employee knows what the quarterly revenue goals are and knows what his or her specific role is in achieving those goals.
- Instill the belief that the entire company closes the sale—in other words, deals get done because every employee contributes his or her specific, measurable value to the sales process. Even tech-support personnel bring in sales leads.
- Learn more from direct interactions, rather than through hearsay, by inviting people to communicate openly and honestly with their managers and the executive team.
- Get employees to focus on the big picture by creating a safe structure where they have permission to communicate grievances, suggestions, etc. to their managers, with impunity.
- Encourage employees to take risks.
- Be a student and a teacher. Accept the wisdom of others, including frontline staff.
- Treat every employee as a solid contributor and encourage feedback, knowing they can see what the CEO can't always see. They may know what the CEO doesn't.
- Challenge employees and give them the opportunity to show conviction and commitment to the company's success. Test their mettle and turn employees into warriors who fight for the company.
- Understand how management style affects the bottom line.
- Put managers through rigorous training with quarterly training updates and evaluations.
- As employees helped TIDAL grow and become successful, they developed and grew themselves.
- By establishing a culture where people are encouraged to take risks in support of the company's success they experience their own personal growth and development.
- Find out why you're struggling. Don't just look to your own brain for the answer.
- Speak to Board members, employees and managers, and read the words of successful business leaders, don't just rely on your own intuition.

As the new culture supplanted the old, we set and achieved our business goals and were able to generate a second round of funding. Some of the results below include:

- TIDAL went from losing $800,000 per quarter to breaking even in three quarters. Instead of raising capital at a low valuation, the company sold its way out of debt.
- Revenues grew from $9.6 million to $14.7 million in the year following the restructuring, an increase of 67 percent.
- Overall, TIDAL revenues have increased 400 percent over the last three years.
- TIDAL raised $12 million in second-round funding from JP Morgan Partners.
- TIDAL moved from ranking one of 29 vendors to being a "Visionary" in [tech research outfit] Gartner's Magic Quadrant. It was also ranked the fastest-growing independent software vendor, and fourth by Gartner behind industry behemoths IBM, Computer Associates, and BMC.
- TIDAL is one of the only vendors to innovate in this space, with a whole-product strategy built around a new automation paradigm—event-driven scheduling.

These results were made possible by the 100 employees at TIDAL who embraced the new vision, direction, and culture, which they brought forth as a team. As CEO, I set the stage for them to perform.

Source: "To Fix a Business, Change the Culture," *BusinessWeek Online,* June 18, 2002.

When a strategy requires massive organizational change and engenders cultural resistance, a firm should determine whether reformulation of the strategy is appropriate. Are all of the organizational changes really necessary? Is there any real expectation that the changes will be acceptable and successful? If these answers are yes, then massive changes in management personnel are often necessary. AT&T offered early retirement to over 20,000 managers as part of a massive recreation of its culture to go along with major strategic changes in recent years. If the answer to these questions is no, the firm might reformulate its strategic plan so as to make it more consistent with established organizational norms and practices.

Merrill Lynch faced the challenge of strategy-culture incompatibility in the last decade. Seeking to remain number one in the newly deregulated financial services industry, it chose to pursue a product development strategy in its brokerage business. Under this strategy, Merrill Lynch would sell a broader range of investment products to a more diverse customer base and would integrate other financial services, such as real estate sales, into the Merrill Lynch organization. The new strategy could succeed only if Merrill Lynch's traditionally service-oriented brokerage network became sales and marketing oriented. Initial efforts to implement the strategy generated substantial resistance from Merrill Lynch's highly successful brokerage network. The strategy was fundamentally inconsistent with long-standing cultural norms at Merrill Lynch that emphasized personalized service and very close broker-client relationships. Merrill Lynch ultimately divested its real estate operation, reintroduced specialists that supported broker/retailers, and refocused its brokers more narrowly on basic client investment needs.

Summary

This chapter examined the idea that a key aspect of implementing a strategy is the *institutionalization* of the strategy so it permeates daily decisions and actions in a manner consistent with long-term strategic success. The "recipe" that binds strategy and organization involves three key ingredients: *organizational structure, leadership,* and *culture.*

Five fundamental organizational structures were examined, and the advantages and disadvantages of each were identified. Institutionalizing a strategy requires a good strategy-structure fit. This chapter dealt with how this requirement often is overlooked until performance becomes inadequate and then indicated the conditions under which the various structures would be appropriate.

Organizational leadership is essential to effective strategy implementation. The CEO plays a critical role in this regard. Assignment of key managers, particularly within the top-management team, is an important aspect of organizational leadership. Deciding whether to promote insiders or hire outsiders is often a central leadership issue in strategy implementation. This chapter showed how this decision could be made in a manner that would best institutionalize the new strategy.

Organizational culture has been recognized as a pervasive influence on organizational life. Organizational culture, which is the shared beliefs and values of an organization's members, may be a major help or hindrance to strategy implementation. This chapter discussed an approach to managing the strategy-culture fit. It identified four fundamentally different strategy-culture situations and provided recommendations for managing the strategy-culture fit in each of these situations.

The chapter concluded with an examination of structure, leadership, and culture for twenty-first century companies. Networked organizations, with intense customer focus, and alliances are keys to success. Talent-focused acquisitions, success sharing, and leaders as coaches round out the future success scenario.

Questions for Discussion

1. What key structural considerations must be incorporated into strategy implementation? Why does structural change often lag behind a change in strategy?
2. Which organizational structure is most appropriate for successful strategy implementation? Explain how state of development affects your answer.
3. Why is leadership an important element in strategy implementation? Find an example in a major business periodical of the CEO's key role in strategy implementation.
4. Under what conditions would it be more appropriate to fill a key management position with someone from outside the firm when a qualified insider is available?
5. What is organizational culture? Why is it important? Explain two different situations a firm might face in managing the strategy-culture relationship.

Chapter 10 Discussion Case

BusinessWeek

P&G: New and Improved

How A. G. Lafley Is Revolutionizing a Bastion of Corporate Conservatism

1 It's Mother's Day, and Alan G. "A.G." Lafley, chief executive of Procter & Gamble Co., is meeting with the person he shares time with every Sunday evening—Richard L. Antoine, the company's head of human resources. Lafley doesn't invite the chief financial officer of the $43 billion business, nor does he ask the executive in charge of marketing at the world's largest consumer-products company. He doesn't invite friends over to watch *The Sopranos,* either. No, on most Sunday nights it's just Lafley, Antoine, and stacks of reports on the performance of the company's 200 most senior executives. This is the boss's signature gesture. It shows his determination to nurture talent and serves notice that little escapes his attention. If you worked for P&G, you would have to be both impressed and slightly intimidated by that kind of diligence.

2 On this May evening, the two executives sit at the dining-room table in Antoine's Cincinnati home hashing over the work of a manager who distinguished himself on one major assignment but hasn't quite lived up to that since. "We need to get him in a position where we can stretch him," Lafley says. Then he rises from his chair and stands next to Antoine to peer more closely at a spreadsheet detailing P&G's seven management layers. Lafley points to one group while tapping an empty water bottle against his leg. "It's not being felt strongly enough in the middle of the company," he says in his slightly high-pitched voice. "They don't feel the hot breath of the consumer."

3 If they don't feel it yet, they will. Lafley, who took over when Durk I. Jager was pressured to resign in June, 2000, is in the midst of engineering a remarkable turnaround. The first thing Lafley told his managers when he took the job was just what they wanted to hear: Focus on what you do well—selling the company's major brands such as Tide, Pampers, and Crest—instead of trying to develop the next big thing.

4 Now, those old reliable products have gained so much market share that they are again the envy of the industry. So is the company's stock price, which has climbed 58 percent, to $92 a share, since Lafley started, while the Standard & Poor's 500-stock index has declined 32 percent. Banc of America analyst William H. Steele forecasts that P&G's profits for its current fiscal year, which ended June 30, will rise by 13 percent, to $5.57 billion, on an 8 percent increase in sales, to $43.23 billion. That exceeds most rivals. Volume growth has averaged 7 percent over the past six quarters, excluding acquisitions, well above Lafley's goal and the industry average.

5 The conventional thinking is that the soft-spoken Lafley was exactly the antidote P&G needed after Jager. After all, Jager had charged into office determined to rip apart P&G's insular culture and remake it from the bottom up. Instead of pushing P&G to excel, however, the torrent of proclamations and initiatives during Jager's 17-month reign nearly brought the venerable company to a grinding halt.

6 Enter Lafley. A 23-year P&G veteran, he wasn't supposed to bring fundamental change; he was asked simply to restore the company's equilibrium. In fact, he came in warning that Jager had tried to implement too many changes too quickly (which Jager readily admits now). Since then, the mild-mannered 56-year-old chief executive has worked to revive both urgency and hope: urgency because, in the previous 15 years, P&G had developed exactly one successful new brand, the Swiffer dust mop; and hope because, after Jager, employees needed reassurance that the old ways still had value. Clearly, Lafley has undone the damage at P&G.

7 What's less obvious is that, in his quiet way, Lafley has proved to be even more of a revolutionary than the flamboyant Jager. Lafley is leading the most sweeping transformation of the company since it was founded by William Procter and James Gamble in 1837 as a maker of soap and candles. Long before he became CEO, Lafley had been pondering how to make P&G relevant in the twenty-first century, when speed and agility would matter more than heft. As president of North American operations, he even spoke with Jager about the need to remake the company.

8 So how has Lafley succeeded where Jager so spectacularly failed? In a word, style. Where Jager was gruff, Lafley is soothing. Where Jager bullied, Lafley persuades. He listens more than he talks. He is living proof that the messenger is just as important as the message. As he says, "I'm not a screamer, not a yeller. But don't get confused by my style. I am very

decisive." Or as Robert A. McDonald, president of P&G's global fabric and home-care division, says, "people want to follow him. I frankly love him like my brother."

9 Indeed, Lafley's charm offensive has so disarmed most P&Gers that he has been able to change the company profoundly. He is responsible for P&G's largest acquisitions ever, buying Clairol in 2001 for $5 billion and agreeing to purchase Germany's Wella in March for a price that now reaches $7 billion. He has replaced more than half of the company's top 30 officers, more than any P&G boss in memory, and cut 9,600 jobs. And he has moved more women into senior positions. Lafley skipped over 78 general managers with more seniority to name 42-year-old Deborah A. Henretta to head P&G's then-troubled North American baby-care division. "The speed at which A. G. has gotten results is five years ahead of the time I expected," says Scott Cook, founder of software maker Intuit (INTU) Inc., who joined P&G's board shortly after Lafley's appointment.

10 Still, the Lafley revolution is far from over. Precisely because of his achievements, Lafley is now under enormous pressure to return P&G to what it considers its rightful place in Corporate America: a company that is admired, imitated, and uncommonly profitable. Nowhere are those expectations more apparent than on the second floor of headquarters, where three former chief executives still keep offices. John Pepper, a popular former boss who returned briefly as chairman when Jager left but gave up the post to Lafley last year, leans forward in his chair as he says: "It's now clear to me that A. G. is going to be one of the great CEOs in this company's history."

OUTSOURCING If it's not a core function, the new P&G won't do it. Info tech and bar-soap manufacturing have already been contracted out. Other jobs will follow.

ACQUISITIONS Not everything has to be invented in company labs. Lafley wants half of all new-product ideas to come from the outside.

BUILDING STAFF Managers are under much closer scrutiny, as Lafley scans the ranks for the best and the brightest and singles them out for development.

BRAND EXPANSION The Crest line now includes an electric toothbrush and tooth-whitening products along with toothpaste. Lafley is making similar moves elsewhere.

PRICING P&G isn't just the premium-priced brand. It will go to the lower end if that's where opportunity lies.

11 But here's the rub: What Lafley envisions may be far more radical than what Pepper has in mind. Consider a confidential memo that circulated among P&G's top brass in late 2001 and angered Pepper for its audacity. It argued that P&G could be cut to 25,000 employees, a quarter of its current size. Acknowledging the memo, Lafley admits: "It terrified our organization."

12 Lafley didn't write the infamous memo, but he may as well have. It reflects the central tenet of his vision—that P&G should do only what it does best, nothing more. Lafley wants a more outwardly focused, flexible company. That has implications for every facet of the business, from manufacturing to innovation. For example, in April he turned over all bar-soap manufacturing, including Ivory, P&G's oldest surviving brand, to a Canadian contractor. In May, he outsourced P&G's information-technology operation to Hewlett-Packard Co.

13 No bastion has been more challenged than P&G's research and development operations. Lafley has confronted head-on the stubbornly held notion that everything must be invented within P&G, asserting that half of its new products should come from the outside. (P&G now gets about 20 percent of its ideas externally—up from about 10 percent when he took over.) "He's absolutely breaking many well-set molds at P&G," says eBay (EBAY) Inc.'s CEO, Margaret C. "Meg" Whitman, whom Lafley appointed to the board.

14 Lafley's quest to remake P&G could still come to grief. As any scientist will attest, buying innovation is tricky. Picking the winners from other labs is notoriously difficult and often expensive. And P&G will remain uncomfortably reliant on Wal-Mart (WMT) Stores Inc., which accounts for nearly a fifth of its sales. Lafley is looking to pharmaceuticals and beauty care for growth, where the margins are high but where P&G has considerably less experience than rivals.

15 The biggest risk, though, is that Lafley will lose the P&Gers themselves. Theirs is a culture famously resistant to new ideas. To call the company insular may not do it justice. Employees aren't kidding when they say they're a family. They often start out there and grow up together at P&G, which only promotes from within. Cincinnati itself is a small town: Employees live near one another, they go to the same health clubs and restaurants. They are today's company men and women—and proud of it.

16 Lafley is well aware of his predicament. On a June evening, as he sits on the patio behind his home, he

muses about just that. The house, which resembles a Tuscan villa and overlooks the Ohio River and downtown Cincinnati, is infused with P&G history. Lafley bought it from former CEO John G. Smale three years before he was named chief executive. A black-and-gold stray cat the family feeds sits a few feet away and watches Lafley as he sips a Beck's beer. The clouds threaten rain. "I am worried that I will ask the organization to change ahead of its understanding, capability, and commitment," Lafley admits.

17 For most of its 166 years, P&G was one of America's preeminent companies. Its brands are icons: It launched Tide in 1946 and Pampers, the first disposable diaper, in 1961. Its marketing was innovative: In the 1880s, P&G was one of the first companies to advertise nationally. Fifty years later, P&G invented the soap opera by sponsoring the *Ma Perkins* radio show and, later, *Guiding Light.*

P&G Famous Firsts

1931	Promotion department manager and future CEO Neil McElroy creates modern theory of **brand management.**
1960	P&G wins **American Dental Assn.** approval of Crest as an effective cavity fighter.
1961	The company launches Pampers, **the first disposable diaper.**
1986	Pert Plus, **the first shampoo conditioner combination**, is unveiled.

18 Its management techniques, meanwhile, became the gold standard: In the 1930s, P&G developed the idea of brand management—setting up marketing teams for each brand and urging them to compete against each other. P&G has long been the business world's finest training ground. General Electric (GE) Co.'s Jeffrey R. Immelt and 3M (MMM) W. James McNerney Jr. both started out on Ivory. Meg Whitman and Steven M. Case were in toilet goods, while Steven A. Ballmer was an assistant product manager for Duncan Hines cake mix, among other goods. They, of course, went on to lead eBay, AOL Time Warner (AOL), and Microsoft.

19 But by the 1990s, P&G was in danger of becoming another Eastman Kodak (EK) Co. or Xerox (XRX) Corp., a once-great company that had lost its way. Sales on most of its 18 top brands were slowing; the company was being outhustled by more focused rivals such as Kimberly-Clark (KMB) Corp. and Colgate-Palmolive (CL) Co. The only way P&G kept profits growing was by cutting costs, hardly a strategy for the long term. At the same time, the dynamics of the industry were changing as power shifted from manufacturers to massive retailers. Through all of this, much of senior management was in denial. "Nobody wanted to talk about it," Lafley says. "Without a doubt, Durk and I and a few others were in the camp of 'We need a much bigger change.' "

20 When Jager took over in January, 1999, he was hell-bent on providing just that—with disastrous results. He introduced expensive new products that never caught on while letting existing brands drift. He wanted to buy two huge pharmaceutical companies, a plan that threatened P&G's identity but never was carried out. And he put in place a companywide reorganization that left many employees perplexed and preoccupied. Soaring commodity prices, unfavorable currency trends, and a tech-crazed stock market didn't help either. At a company prized for consistent earnings, Jager missed forecasts twice in six months. In his first and last full fiscal year, earnings per share rose by just 3.5 percent instead of an estimated 13 percent. And during that time, the share price slid 52 percent, cutting P&G's total market capitalization by $85 billion. Employees and retirees hold about 20 percent of the stock. The family began to turn against its leader.

21 But Jager's greatest failing was his scorn for the family. Jager, a Dutchman who had joined P&G overseas and worked his way to corporate headquarters, pitted himself against the P&G culture, contending that it was burdensome and insufferable, says Susan E. Arnold, president of P&G's beauty and feminine care division. Some go-ahead employees even wore buttons that read "Old World/New World" to express disdain for P&G's past. "I never wore one," Arnold sneers. " 'The old Procter is bad, and the new world is good.' That didn't work."

22 On June 6, 2000, his thirtieth wedding anniversary, Lafley was in San Francisco when he received a call from Pepper, then a board member: Would he become CEO? Back in Cincinnati, a boardroom coup unprecedented in P&G's history had taken place.

23 As Lafley steps into the small study in his house three years later, a Japanese drawing on the wall

reminds him of what it was like to become CEO. The room, with its painting of a samurai warrior and red elephant-motif wallpaper, alludes to his stint running P&G's Asian operations. Bookshelves hold leather-bound volumes of Joseph Conrad and Mark Twain. A simple wooden desk faces the window. Lafley focuses on the drawing, which depicts a man caught in a spider's web; it was given to him by the elder of his two sons, Patrick. "In the first few days, you are just trying to figure out what kind of web it is," he says.

24 In a sense, Lafley had been preparing for this job his entire adult life. He never hid the fact that he wanted to run P&G one day. Or if not the company, then a company. That itself is unusual since, like almost all P&Gers, Lafley has never worked anywhere else. After graduating from Hamilton College in 1969, Lafley decided to pursue a doctorate in medieval and Renaissance history at the University of Virginia. But he dropped out in his first year to join the Navy (and avoid being drafted into the Army). He served in Japan, where he got his first experience as a merchandiser, supplying Navy retail stores. When his tour of duty ended in 1975, he enrolled in the MBA program at Harvard Business School. And from there, he went directly to Cincinnati.

25 When he was hired as a brand assistant for Joy dish detergent in 1977 at age 29; he was older than most of his colleagues and he worried that his late start might hinder his rise at P&G. Twice within a year in the early 1980s, Lafley quit. "Each time, I talked him back in only after drinking vast amounts of Drambuie," says Thomas A. Moore, his boss at the time, who now runs biotech company Biopure (BPUR) Corp. On the second occasion, then-CEO John Smale met with Lafley, who had accepted a job as a consultant in Connecticut (NIPNY). Without making any promises, Smale says he told Lafley that "we thought there was no limit on where he was going to go."

26 Sure enough, Lafley climbed quickly to head P&G's soap and detergent business, where he introduced Liquid Tide in 1984. A decade later, he was promoted to head the Asian division. Lafley returned from Kobe, Japan, to Cincinnati in 1998 to run the company's entire North American operations. To ease the transition home, he and his younger son, Alex, who was then 12, studied guitar together. Two years later, Lafley was named CEO.

27 Along the way, he developed a reputation as a boss who stepped back to give his staff plenty of responsibility and helped shape decisions by asking a series of keen questions—a process he calls "peeling the onion." And he retained a certain humility. He still collects baseball cards, comic books, and rock 'n' roll 45s. Whereas some executives might have a garage full of antique cars or Harley-Davidsons (HDI); Lafley keeps two Vespa motor scooters. "People wanted him to succeed," says Virginia Lee, a former P&Ger who worked for Lafley at headquarters and overseas.

28 As CEO, Lafley hasn't made grand pronouncements on the future of P&G. Instead, he has spent an inordinate amount of time patiently communicating how he wants P&G to change. In a company famed for requiring employees to describe every new course of action in a one-page memo, Lafley's preferred approach is the slogan. For example, he felt that P&G was letting technology rather than consumer needs dictate new products. Ergo: "The consumer is boss." P&G wasn't working closely enough with retailers, the place where consumers first see the product on the shelf: "The first moment of truth." P&G wasn't concerned enough with the consumer's experience at home: "The second moment of truth."

29 Lafley uses these phrases constantly, and they are echoed throughout the organization. At the end of a three-day leadership seminar, 30 young marketing managers from around the world present what they have learned to Lafley. First on the list: "We are the voice of the consumer within P&G, and they are the heart of all we do." Lafley, dressed in a suit, sits on a stool in front of the group and beams. "I love the first one," he laughs as the room erupts in applause.

30 When he talks about his choice of words later, Lafley is a tad self-conscious. "It's *Sesame Street* language—I admit that," he says. "A lot of what we have done is make things simple because the difficulty is making sure everybody knows what the goal is and how to get there."

31 Lafley has also mastered the art of the symbolic gesture. The eleventh floor at corporate headquarters had been the redoubt of senior executives since the 1950s. Lafley did away with it, moving all five division presidents to the same floors as their staff. Then he turned some of the space into a leadership training center. On the rest of the floor, he knocked down the walls so that the remaining executives, including himself, share open offices. Lafley sits next to the two people he talks to the most, which, in true P&G style, was officially established by a flow study: HR head Antoine and Vice-Chairman Bruce Byrnes. As

if the Sunday night meetings with Antoine weren't proof enough of Lafley's determination to make sure the best people rise to the top. And Byrnes, whom Lafley refers to as "Yoda"—the sage-like *Star Wars* character—gets a lot of face time because of his marketing expertise. As Lafley says, "the assets at P&G are what? Our people and our brands."

32 Just as emblematic of the Lafley era is the floor's new conference room, where he and P&G's 12 other top executives meet every Monday at 8 A.M. to review results, plan strategy, and set the drumbeat for the week. The table used to be rectangular; now it's round. The execs used to sit where they were told; now they sit where they like. At one of those meetings, an outsider might have trouble distinguishing the CEO: He occasionally joins in the discussion, but most of the time the executives talk as much to each other as to Lafley. "I am more like a coach," Lafley says afterward. "I am always looking for different combinations that will get better results." Jeff Immelt, who asked Lafley to join GE's board in 2002, describes him as "an excellent listener. He's a sponge."

33 And now, Lafley is carefully using this information to reshape the company's approach to just about everything it does. When Lafley describes the P&G of the future, he says: "We're in the business of creating and building brands." Notice, as P&Gers certainly have, that he makes no mention of manufacturing. While Lafley shies away from saying just how much of the company's factory and back-office operations he may hand over to someone else, he does admit that facing up to the realities of the marketplace "won't always be fun." Of P&G's 102,000 employees, nearly one-half work in its plants. So far, "Lafley has deftly handled the outsourcing deals, which has lessened fear within P&G," says Roger Martin, a close adviser of Lafley's who is dean of the University of Toronto's Joseph L. Rotman School of Management. All 2,000 of the information-technology workers were moved over to HP. At the bar-soap operations, based entirely in Cincinnati, 200 of the 250 employees went to work for the Canadian contractor.

34 Lafley's approach to selling P&G products is unprecedented at the company, too: He argues that P&G doesn't have to produce just premium-priced goods. So now there's a cheaper formulation for Crest in China. The Clairol deal gave P&G bargain shampoos such as Daily Defense. And with Lafley's encouragement, managers have looked at their most expensive products to make sure they aren't too costly. In many cases, they've actually lowered the prices.

35 And Lafley is pushing P&G to approach its brands more creatively. Crest, for example, isn't just about toothpaste anymore: There's also an electric toothbrush, SpinBrush, which P&G acquired in January, 2001. P&G is also willing to license its own technologies to get them to the marketplace faster. It joined with Clorox Co., maker of Glad Bags, last October to share a food-wrap technology it had developed. It was unprecedented for P&G to work with a competitor, says licensing head Jeffrey Weedman. The overall effect is undeniable. "Lafley has made P&G far more flexible," says Banc of America's Steele.

36 But Lafley still faces daunting challenges. Keeping up the earnings growth, for example, will get tougher as competitors fight back and as P&G winds down a large restructuring program—started under Jager but accelerated under Lafley. Furthermore, some of the gains in profit have resulted from cuts in capital and R&D spending, which Lafley has pared back to the levels of the company's rivals. And already, P&G has missed a big opportunity: It passed up the chance to buy water-soluble strips that contain mouthwash. Now, Listerine is making a bundle on the product.

37 Nor are all investors comfortable with growth through acquisitions. The deals make it harder for investors to decipher earnings growth from existing operations. Then there's the risk of fumbling the integration, notes Arthur B. Cecil, an analyst at T. Rowe Price Group (TROW) Inc., which holds 1.74 million P&G shares. "I would prefer they not make acquisitions," he says. Already, Clairol hair color, the most important product in P&G's recent purchase, has lost five points of market share to L'Oréal in the United States, according to ACNeilsen Corp.

38 Making deals, however, could be the only way to balance P&G's growing reliance on Wal-Mart. Former and current P&G employees say the discounter could account for one-third of P&G's global sales by the end of the decade. Meanwhile, the pressure from consumers and competitors to keep prices low will only increase. "P&G has improved its ability to take on those challenges, but those challenges are still there," says Lehman analyst Ann Gillin.

39 Still, Lafley may be uniquely suited to creating a new and improved P&G. Even Jager agrees that

P&G Turning the Tide

	Sales	Operating Profit Margin	Outlook
Baby and Family Care	23%	17%	GOOD
P&G now vies with Kimberly-Clark to dominate the disposable-diaper market. But competition has pushed prices down, which is why this division has the slowest profit-margin growth.			
Fabric and Home Care	29%	25%	VERY GOOD
Lafley has aggressively cut costs in the company's largest division. But Tide in particular faces intense competition from lower-priced rivals. To compensate, Lafley is introducing high-margin products, such as the Swiffer Duster.			
Beauty Care	28%	23%	GOOD
Lafley has quickly expanded this business by acquiring Clairol and Wella. But the company has less expertise here and still has to prove it can grow internally.			
Health Care	13%	18%	MIXED
With its SpinBrush and tooth-whitening products, P&G has regained the lead in oral care from Colgate. The division will get a lift from distributing heart-burn drug Prilosec over the counter. But the pharmaceutical business depends on one big seller, Actonel for osteoporosis.			
Snacks and Beverages	7%	15%	WEAK
Because the division generates the company's lowest profit margins, many expect Lafley to continue to extricate P&G from these businesses. He has already sold Crisco and Jiff to J. M. Smuckers.			

*Share of total sales. Estimates for fiscal year ending June 30, 2003

Data: Banc America Securities

Lafley was just what the company needed. "He has calmed down the confusion that happened while I was there," says the former CEO. Jager left a letter on Lafley's desk the day he resigned telling his successor not to feel responsible for his fall. "You earned it," he recalls writing. "Don't start out with guilt."

40 Lafley says he learned from Jager's biggest mistake. "I avoided saying P&G people were bad," he says. "I enrolled them in change." Lafley, a company man through and through, just can't resist trying out a new slogan.

Source: "P&G: New and Improved," *BusinessWeek,* July 7, 2003.

Appendix 10

Primary Organizational Structures and Their Strategy-Related Pros and Cons

Matching the structure to the strategy is a fundamental task of company strategists. To understand how that task is handled, we first must review the five basic primary structures. We will then turn to guidelines for matching structure to strategy.

The five basic primary structures are: (1) functional, (2) geographic, (3) divisional, or strategic business unit, (4) matrix, and (5) product team. Each structure has advantages and disadvantages that strategists must consider when choosing an organization form.

FUNCTIONAL ORGANIZATIONAL STRUCTURE

Functional structures predominate in firms with a single or narrow product focus. Such firms require well-defined skills and areas of specialization to build competitive advantages in providing their products or services. Dividing tasks into functional specialties enables the personnel of these firms to concentrate on only one aspect of the necessary work. This allows use of the latest technical skills and develops a high level of efficiency.

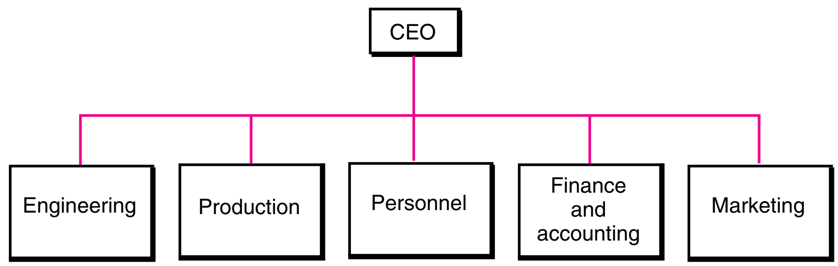
Product, customer, or technology considerations determine the identity of the parts in a functional structure. A hotel business might be organized around housekeeping (maids), the front desk, maintenance, restaurant operations, reservations and sales, accounting, and personnel. An equipment manufacturer might be organized around production, engineering/quality control, purchasing, marketing, personnel, and finance/accounting. Two examples of functional organizations are illustrated in Exhibit 10–A.

The strategic challenge presented by the functional structure is effective coordination of the functional units. The narrow technical expertise achieved through specialization can lead to limited perspectives and to differences in the priorities of the functional units. Specialists may see the firm's strategic issues primarily as "marketing" problems or "production" problems. The potential conflict among functional units makes the coordinating role of the chief executive critical. Integrating devices (such as project teams or planning committees) are frequently used in functionally organized firms to enhance coordination and to facilitate understanding across functional areas.

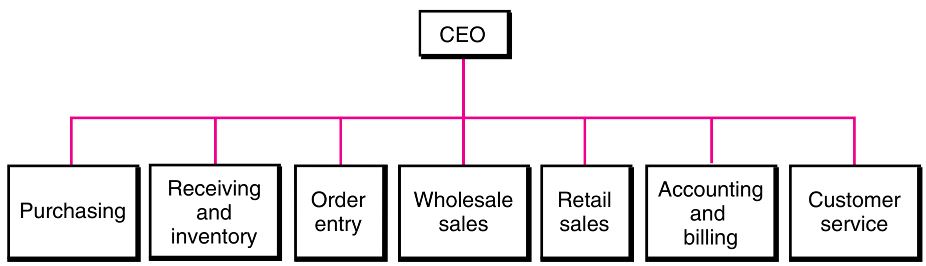
GEOGRAPHIC ORGANIZATIONAL STRUCTURE

Firms often grow by expanding the sale of their products or services to new geographic areas. In these areas, they frequently encounter differences that necessitate different approaches in producing, providing, or selling their products or services. Structuring by geographic areas is usually required to accommodate these differences. Thus, Holiday Inns is organized by regions of the world because of differences among nations in the laws, customs, and economies affecting the lodging industry. And even within its U.S. organization, Holiday Inns is organized geographically because of regional differences in traveling requirements, lodging regulations, and customer mix.

EXHIBIT 10–A
Functional Organization Structures



A process-oriented functional structure (an electronics distributor):



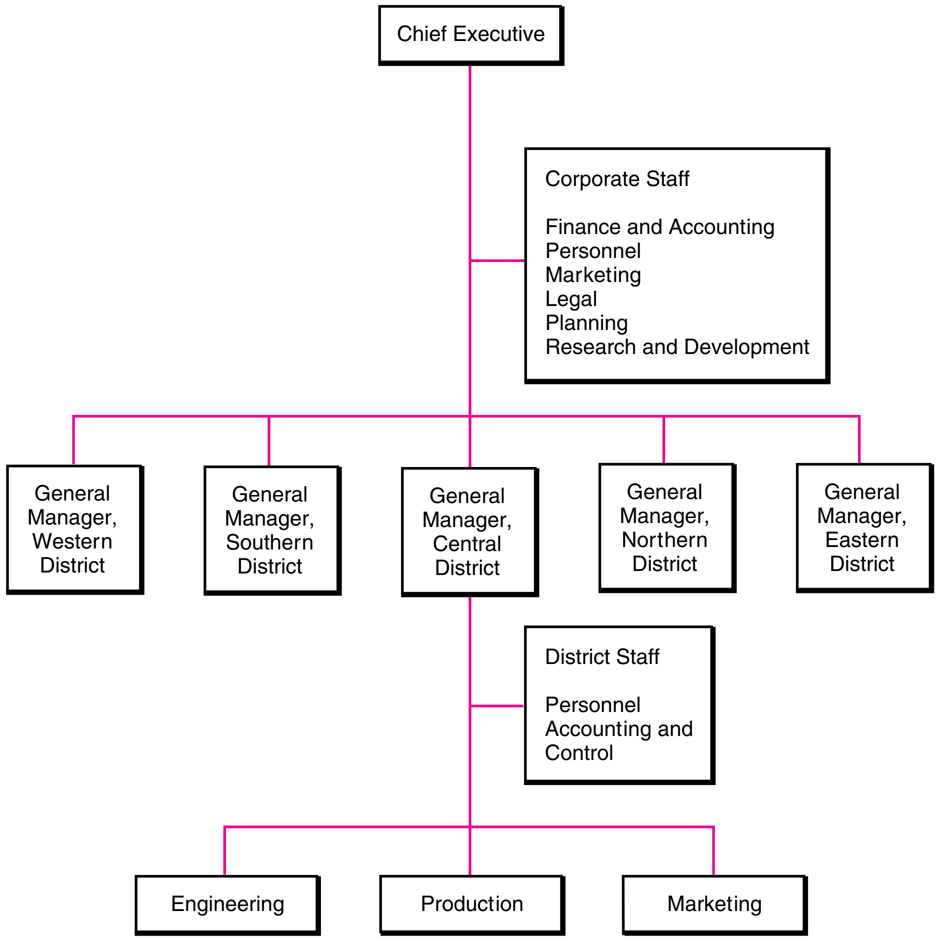
Strategic Advantages	Strategic Disadvantages
1. Achieves efficiency through specialization.	1. Promotes narrow specialization and functional rivalry or conflict.
2. Develops functional expertise.	2. Creates difficulties in functional coordination and interfunctional decision making.
3. Differentiates and delegates day-to-day operating decisions.	3. Limits development of general managers.
4. Retains centralized control of strategic decisions.	4. Has a strong potential for interfunctional conflict—priority placed on functional areas, not the entire business.
5. Tightly links structure to strategy by designating key activities as separate units.	

The key strategic advantage of geographic organizational structures is responsiveness to local market conditions. Exhibit 10–B illustrates a typical geographic organizational structure and itemizes the strategic advantages and disadvantages of such structures.

DIVISIONAL OR STRATEGIC BUSINESS UNIT STRUCTURE

When a firm diversifies its product/service lines, utilizes unrelated market channels, or begins to serve heterogeneous customer groups, a functional structure rapidly becomes inadequate. If a functional structure is retained under these circumstances, production managers may have to oversee the production of numerous and varied products or services, marketing managers may have to create sales programs for vastly different products or sell through vastly different distribution channels, and top management may be confronted with excessive coordination

EXHIBIT 10–B
A Geographic Organizational Structure



Strategic Advantages	Strategic Disadvantages
1. Allows tailoring of strategy to needs of each geographic market.	1. Poses problem of deciding whether headquarters should impose geographic uniformity or geographic diversity should be allowed.
2. Delegates profit/loss responsibility to lowest strategic level.	2. Makes it more difficult to maintain consistent company image/reputation from area to area.
3. Improves functional coordination within the target market.	3. Adds layer of management to run the geographic units.
4. Takes advantage of economies of local operations.	4. Can result in duplication of staff services at headquarters and district levels.
5. Provides excellent training grounds for higher level general managers.	

demands. A new organizational structure is often necessary to meet the increased coordination and decision-making requirements that result from increased diversity and size, and the divisional or strategic business unit (SBU) organizational structure is the form often chosen.

For many years, Ford and General Motors have used divisional/SBU structures organized by product groups. Manufacturers often organize sales into divisions based on differences in distribution channels.

A divisional/SBU structure allows corporate management to delegate authority for the strategic management of distinct business entities—the division/SBU. This expedites decision making in response to varied competitive environments and enables corporate management to concentrate on corporate-level strategic decisions. The division/SBU usually is given profit responsibility, which facilitates accurate assessment of profit and loss.

Exhibit 10–C illustrates a divisional/SBU organizational structure and specifies the strategic advantages and disadvantages of such structures.

MATRIX ORGANIZATIONAL STRUCTURE

In large companies, increased diversity leads to numerous product and project efforts of major strategic significance. The result is a need for an organizational form that provides skills and resources where and when they are most vital. For example, a product development project needs a market research specialist for two months and a financial analyst one day per week. A customer site application needs a software engineer for one month and a customer service trainer one day per month for six weeks. Each of these situations is an example of a matrix organization that has been used to temporarily put people and resources where they are most needed. Among the firms that now use some form of matrix organization are Citicorp, Matsushita, DaimlerChrysler, Microsoft, Dow Chemical, and Texas Instruments.

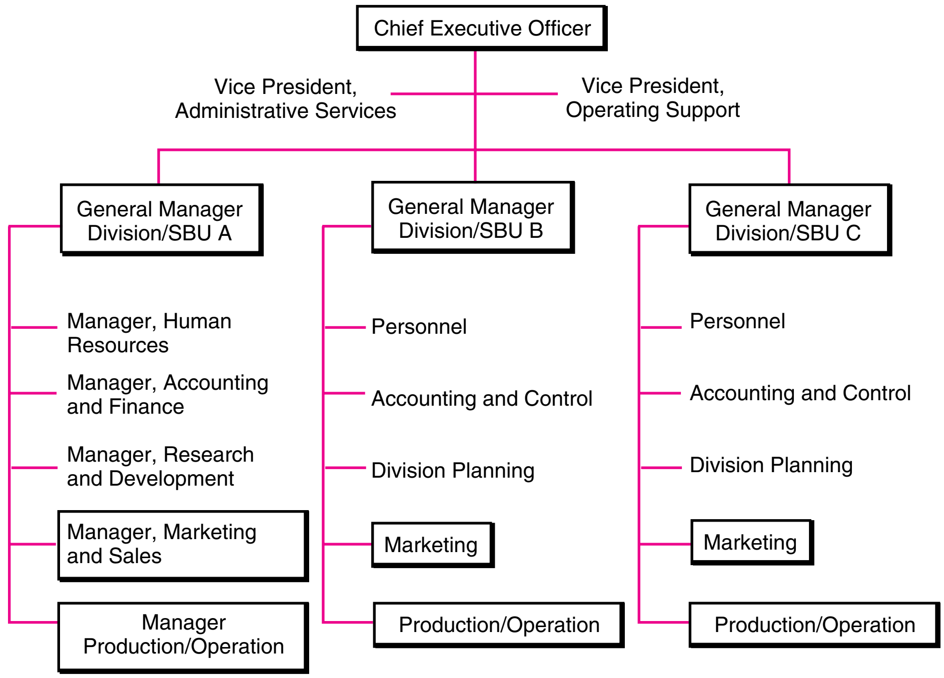
The matrix organization provides dual channels of authority, performance responsibility, evaluation, and control, as shown in Exhibit 10–D. Essentially, subordinates are assigned both to a basic functional area and to a project or product manager. The matrix form is intended to make the best use of talented people within a firm by combining the advantages of functional specialization and product-project specialization.

The matrix structure also increases the number of middle managers who exercise general management responsibilities (through the project manager role) and, thus, broaden their exposure to organizationwide strategic concerns. In this way, the matrix structure overcomes a key deficiency of functional organizations while retaining the advantages of functional specialization.

Although the matrix structure is easy to design, it is difficult to implement. Dual chains of command challenge fundamental organizational orientations. Negotiating shared responsibilities, the use of resources, and priorities can create misunderstanding or confusion among subordinates. These problems are heightened in an international context with the complications introduced by distance, language, time, and culture.

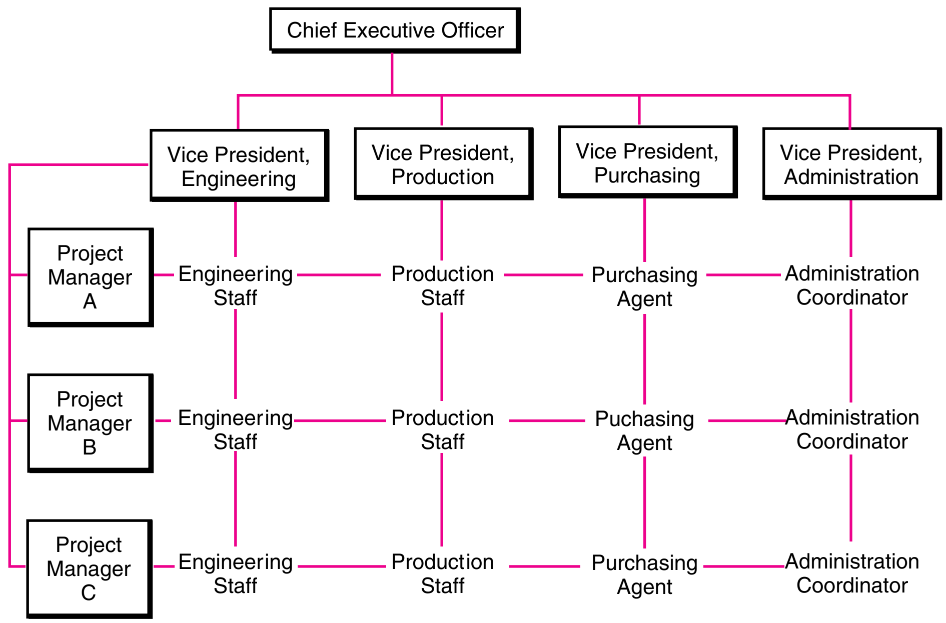
To avoid the deficiencies that might arise from a permanent matrix structure, some firms are accomplishing particular strategic tasks, by means of a "temporary" or "flexible" *overlay structure.* This approach, used recently by such firms as NEC, Matsushita, Philips, and Unilever, is meant to take *temporary* advantage of a matrix-type team while preserving an underlying divisional structure. Thus, the basic idea of the matrix structure—*to simplify and amplify the focus of resources on a narrow but strategically important product, project, or market*—appears to be an important structural alternative for large, diverse organizations.

EXHIBIT 10–C
Divisional or Strategic Business Unit Structure



Strategic Advantages	Strategic Disadvantages
1. Forces coordination and necessary authority down to the appropriate level for rapid response.	1. Fosters potentially dysfunctional competition for corporate-level resources.
2. Places strategy development and implementation in closer proximity to the unique environments of the divisions/SBUs.	2. Presents the problem of determining how much authority should be given to division/SBU managers.
3. Frees chief executive officer for broader strategic decision making.	3. Creates a potential for policy inconsistencies among divisions/SBUs.
4. Sharply focuses accountability for performance.	4. Presents the problem of distributing corporate overhead costs in a way that's acceptable to division managers with profit responsibility.
5. Retains functional specialization within each division/SBU.	5. Increases costs incurred through duplication of functions.
6. Provides good training grounds for strategic managers.	6. Creates difficulty maintaining overall corporate image.
7. Increases focus on products, markets, and quick response to change.	

EXHIBIT 10–D
Matrix Organizational Structure



Strategic Advantages	Strategic Disadvantages
1. Accommodates a wide variety of project-oriented business activity.	1. May result in confusion and contradictory policies.
2. Provides good training grounds for strategic managers.	2. Necessitates tremendous horizontal and vertical coordination.
3. Maximizes efficient use of functional managers.	3. Can proliferate information logjams and excess reporting.
4. Fosters creativity and multiple sources of diversity.	4. Can trigger turf battles and loss of accountability.
5. Gives middle management broader exposure to strategic issues.	