CHAPTER TEN

Configuring the Organization

The companies that look after their people are the companies that do really well.

Sir Richard Branson
Entrepreneur, founder and chairman of the Virgin Group

The idea that we have to choose between a mediocre, well executed strategy and a brilliant, poorly executed one is deeply flawed.

Roger L. Martin
Author, professor and former Dean of Rotman School of Management

Learning Objectives

When you have read this chapter you should be able to:

LO 10.1 Identify what issues to consider in establishing a strategy-supportive organizational structure and organizing the work effort.

LO 10.2 Explain why hiring, training and retaining the right people constitute key components of the strategy execution process.

LO 10.3 Discuss the different systems that underpin good strategy execution.

LO 10.4 Evaluate the role of processes, policies and procedures in enabling superior strategy execution.

LO 10.5 Discuss how aligning/configuring the levers managers use to execute strategy can be balanced with responding to changing contexts.

Opening Case

TURNING AROUND THE CO-OPERATIVE BANK

Apart from some of the high-profile casualties of the 2007/8 recession, a number of smaller financial institutions in Europe and the United States were severely affected. However, The Co-operative Bank was a rare example of an organization that had done well from the crisis. The Bank was an offshoot of The Co-operative Group, a retail conglomerate whose mutual status (it was owned by its members rather than shareholders) had been praised as an alternative governance model to public limited companies. While The Co-operative Bank appeared to have weathered the initial storm, which had taken down the likes of Lehman Brothers and Northern Rock, its decision to merge with another UK mutual organization, the Britannia Building Society, would prove to be its undoing.

Like many other financial institutions, The Co-operative Bank saw the recession as an opportunity as well as a threat. Because the bank obtained most of its funds from its savers' deposits, it was not as vulnerable to the capital markets as other lenders. This placed it in a strong position to benefit from the problems of other firms which had fared much worse. One of these was the Britannia Building Society and senior executives from The Co-operative Bank began talks with that organization in 2008. The attraction of the UK's second largest building society as a partner came from the fact that it would enable The Co-operative Bank to expand its branch network at little cost and give it greater scale in a consolidating market. Senior managers at the bank also estimated that the merger would produce integration savings of £88 million. The merger of the two organizations was agreed in January 2009 and completed in August that year.

The post-merger integration process was managed by a member of the senior team from Britannia, and the building society's CEO, Neville Richardson, became the head of the merged organization. The bank was also trying to replace its ageing IT systems as part of a modernization push. The Britannia merger complicated this significantly. The restructuring of the combined organizations resulted in the loss of more than 600 jobs, while in addition many of Britannia's former senior team left – including Richardson, who quit in July 2011. Less than a month later, the new CEO, former finance director Barry Tootell, announced the bank would be buying more than 600 branches from Lloyds, another UK bank, which had been bailed out by the British government after the financial crisis.

The banking regulator in the UK, the Financial Services Authority (FSA), had shown concern, both about Britannia's assets, most of which were connected to commercial property loans, and The Co-operative Bank's management of risk. Commercial property had been one of the areas that had suffered in the recession, with portfolios being revalued to take account of lower property prices. However, it was the merged organization's management of risk that would prove a deciding factor in the delivery of its strategy. The regulator had expressed concerns to the bank in 2011, but it was only in March 2012 with the appointment of an interim Chief Risk Officer, Peter Shaw, that the organization began to tackle some of the issues.

Despite these problems, the new CEO forged ahead with the plan to buy the branches from Lloyds and appeared to have government backing for this bold move, described by some as creating a new 'challenger' to the large high-street banks such as HSBC and Barclays. However, within a few months the fragility of The Co-operative Bank's position became clear. The development of the new IT system was paused after encountering significant problems and the whole project was abandoned early in 2013 and written off at a cost of more than £300 million – on top of sunk costs of several 100 million more over the previous five years. The bank also had to set aside £269 million to cover potential compensation claims for the mis-selling of payment protection insurance to bank customers. Finally, the value of the commercial property portfolio the bank had acquired through the merger with Britannia was revalued at more than £800 million less. All this led to the bank's parent, The Co-operative Group, making a loss of in excess of £600 million. The regulator also raised serious questions about the viability of the Bank as it had substantially raised the amount of capital banks needed to hold as a buffer to events like the 2007/8 credit crunch. For The Co-operative Bank, this meant it needed £3.4 billion instead of the £1.9 billion required of it a year earlier. In practical terms, the bank needed £1.5 billion in 2013 to remain as a going concern. Any bid to grow through the acquisition of branches from Lloyds had now been abandoned.

By mid-2013, Barry Tootell had resigned as CEO, to be replaced by Niall Booker, a former HSBC executive, with the experience of the banking sector the organization now badly needed. The Chairman, Paul Flowers, also resigned, but was embroiled in further problems later in 2013 when he appeared to have limited knowledge of the sector at a hearing of the UK Parliament's Treasury Select Committee and was then alleged, by the *Mail on Sunday,* a popular UK newspaper, to have been involved in trying to buy drugs.

The Co-operative Group as a whole was forced to sell a number of its businesses to cover the bank's shortfall and also to offer shares in the bank on the open market, which first diluted and then removed its mutual status. By 2014 the bank was owned by various hedge funds and had recorded some of the largest losses in its history: £709 million in 2013 and £1.3 billion in 2014. New CEO Booker was forced to close branches and dispose of the risky commercial property-based assets it had acquired from Britannia. In mid-2014, a report commissioned to look into the bank's problems, written by Sir Christopher Kelly, was published and claimed that the organization could have been managed more effectively and avoided the disaster that followed the Britannia merger.

QUESTIONS

1. What were the principal causes of the failure of The Co-operative Bank's growth strategy?
2. What could the bank's senior management have done differently to ensure the strategy was delivered more effectively?

Sources: Kelly, C. (2014) 'Failings in management and governance: report of the independent review into the events leading to the Cooperative Bank's capital shortfall', 30 April. Available online at www.co-operative.coop/corporate/the-kelly-review/ (accessed 10 April 2016); Kolloe, J. and Treanor, J. (2015) 'The Co-operative Bank's timeline of troubles', *The Guardian* online, 11 August. Available online at www.theguardian.com/business/2015/jun/23/cooperative-bank-timeline-troubles (accessed 10 April 2016); Wallace, T. and Spence, P. (2015) 'Co-op Bank losses almost triple as turnaround drags on', *The Telegraph* online, 20 August. Available online at www.telegraph.co.uk/finance/newsbysector/banksandfinance/11813576/Co-op-Bank-losses-almost-triple-as-turnaround-drags-on.html (accessed 10 April 2016).

As we have seen from the opening case, there are a number of factors that are critical in ensuring a strategy is delivered effectively: (1) recruiting and/or retaining the right people with the skills needed to put the strategy into action; (2) ensuring that the organization's structure and systems support the organization's chosen strategic direction, as well as developing robust processes and procedures to allocate and develop resources and capabilities. Putting the strategy into place and getting the organization to execute it well call for different sets of managerial skills. Whereas crafting strategy is largely a market-driven and resource-driven activity, executing strategy is an operations-driven activity revolving around the management of people and business processes. Whereas successful strategy-making depends on strategic vision, solid industry and competitive analysis, and shrewd market positioning, successful strategy execution depends on doing a good job of working with and through others; allocating resources; building and strengthening competitive capabilities; creating an appropriate organizational structure; instituting strategy-supportive policies, processes and systems; motivating and rewarding people; and instilling a discipline of getting things done. Executing strategy is an action-oriented, make-things-happen task that tests a manager's ability to direct organizational change, achieve continuous improvement in operations and business processes, create and nurture a strategy-supportive culture, and consistently meet or beat performance targets.

Most experienced managers are clear that it is much easier to develop a sound strategic plan than it is to execute the plan and achieve the desired outcomes. According to one executive, 'It's been rather easy for us to decide where we wanted to go. The hard part is to get the organization to act on the new priorities'.[1] In a recent study of 1,000 companies, government agencies and not-for-profit organizations in more than 50 countries, 60 per cent of employees rated their organizations poor in terms of strategy implementation.[2] *Just because senior managers announce a new strategy does not mean that organization members will embrace it and move forward enthusiastically to implement it.* Senior executives cannot simply direct immediate subordinates to abandon old ways and take up new ways, and they certainly cannot expect the needed actions and changes to occur in rapid-fire fashion and still lead to the desired outcomes. Some managers and employees may be sceptical about the merits of the strategy, seeing it as contrary to the organization's best interests, unlikely to succeed, or threatening to their departments or careers. Moreover, employees may have misconceptions about the new strategy or different ideas about what internal changes are needed to execute it. Long-standing attitudes, vested interests, inertia and ingrained organizational practices do not melt away when managers decide on a new strategy and begin efforts to implement it, especially if only a few people have been involved in crafting the strategy or if the rationale for strategic change requires quite a bit of salesmanship.

It takes adept managerial leadership to convincingly communicate a new strategy and the reasons for it, overcome pockets of doubt and disagreement, secure the commitment and enthusiasm of key personnel, gain agreement on how to implement the strategy and move forward to get all the pieces into place. Company personnel must understand – in their heads and hearts – why a new strategic direction is necessary and where the new strategy is taking them.[3] Instituting change is, of course, easier when the problems with the old strategy have become obvious and/or the company has spiralled into a financial crisis.

Core Concept

Good **strategy execution** requires a *team effort.* All managers have strategy-executing responsibility in their areas of authority, and all employees are active participants in the strategy execution process.

But the challenge of successfully implementing new strategic initiatives goes well beyond managerial adeptness in overcoming resistance to change. What really makes **strategy execution** a tougher, more time-consuming management challenge than crafting strategy are the wide array of managerial activities that need to be addressed and the number of complex issues that must be worked out. Managers need to have a clear idea of what has to be done to put new strategic initiatives in place and, further, how best to get these things done in a timely manner that yields good results. Demanding people-management skills and perseverance are required to get a variety of initiatives launched and moving, and to integrate the efforts of many different work groups into a smoothly functioning whole. Depending on how much consensus-building and organizational change is involved, the process of implementing strategy changes can take several months to several years. To achieve *real proficiency* in executing the strategy can take even longer.

Even traditional firms with pyramidal hierarchies find that, like crafting strategy, *executing strategy is a job for the whole organization, not just a few senior managers.* In such firms, while the chief executive officer and the heads of major units (business divisions, functional departments and key operating units) are ultimately responsible for seeing that strategy is executed successfully, the process typically affects every part of the firm – all value chain activities and all work-groups. Top-level managers must rely on the active support and co-operation of middle and lower managers to institute whatever new operating practices are needed in the various functional areas and operating units to achieve proficient strategy execution. It is middle and lower-level managers who ultimately must ensure that work-groups and front-line employees do a good job of performing strategy-critical value chain activities and produce operating results that allow company-wide performance targets to be met. In consequence, strategy execution requires every manager to think through the answer to the question: *'What does my area have to do to implement its part of the strategic plan, and what should I do to get these things accomplished efficiently and effectively?'* In organizations with flatter structures or with more emergent strategy processes, managers tend to have more of a co-ordinating role, and have to strike a balance between empowering staff to unleash their creativity and ensuring consistency with the overall goals and vision of the organization's top-level strategy. A study of 7,600 managers in more than 250 companies between 2010 and 2015 found that many employees did not understand their organization's strategic objectives properly and that one of the principal reasons strategy execution unravelled was because of a lack of co-ordination between different business units.[4]

A Framework for Executing Strategy

Executing strategy entails figuring out the specific techniques, actions and behaviours that are needed for a smooth strategy-supportive operation, and then following through to get things done and deliver results. With a new strategic direction, often the first step in implementing strategic change is for management to communicate the case for organizational change clearly and persuasively to internal stakeholders such as employees so that they find ways to put the strategy into place, make it work and meet performance targets. Management's handling of the strategy implementation process can be considered successful if and when the company achieves the targeted strategic and financial performance, and shows good progress in making its strategic vision a reality.

The specifics of how to execute a strategy – the exact items that need to be placed on management's action agenda – always need to be customized to fit the particulars of a company's situation. The challenges for successfully executing a low-cost provider strategy are different from those for executing a high-end differentiation strategy. Implementing a new strategy for a struggling company in the midst of a financial crisis is a different job from that of making minor improvements to strategy execution in a company that is doing relatively well. Moreover, some managers are more adept than others at using particular approaches to achieve the desired kinds of organizational changes. Hence, there is no definitive managerial recipe for successful strategy execution that cuts across all company situations and all types of strategies, or that works for all types of managers. Rather, the specific actions required to implement a strategy – the 'to do list' that constitutes management's action agenda – always represents management's judgement about how best to proceed in light of prevailing circumstances.

The Principal Components of the Strategy Execution Process

To ensure delivery of the organization's chosen strategy, managers have a number of levers they can use to change the organization (Figure 10.1). These include the organization's structure and the people through which it puts the strategy into action, plus the systems and processes that help managers organize and control operations. The way all these levers are configured or aligned and the organization's culture add a more conceptual layer, which often takes more effort and time to change. This means that managers try to change the culture of an organization and/or how it is configured only when the other levers, such as structure and systems, have not delivered the desired results.[5]

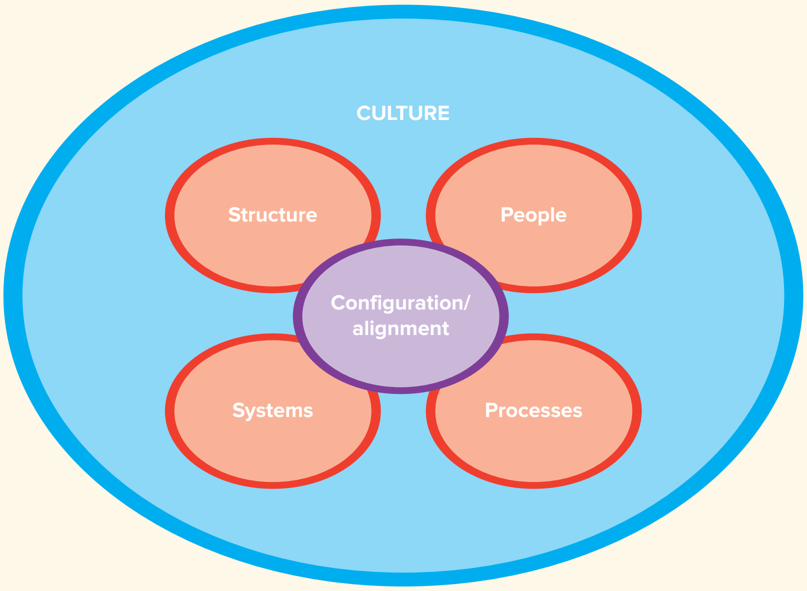

FIGURE 10.1 The principal levers of the strategy execution process

Changes to each of these levers is a continuous process in most organizations (as noted in Chapters 1 and 4) as managers respond to changes in the environment. So the execution of strategy is likewise a continuous process, during which the strategy's performance is monitored and incremental adjustment made to the structure, the people in the organization, and their knowledge and skills, as well as the systems and processes used (Figure 10.2). Successful

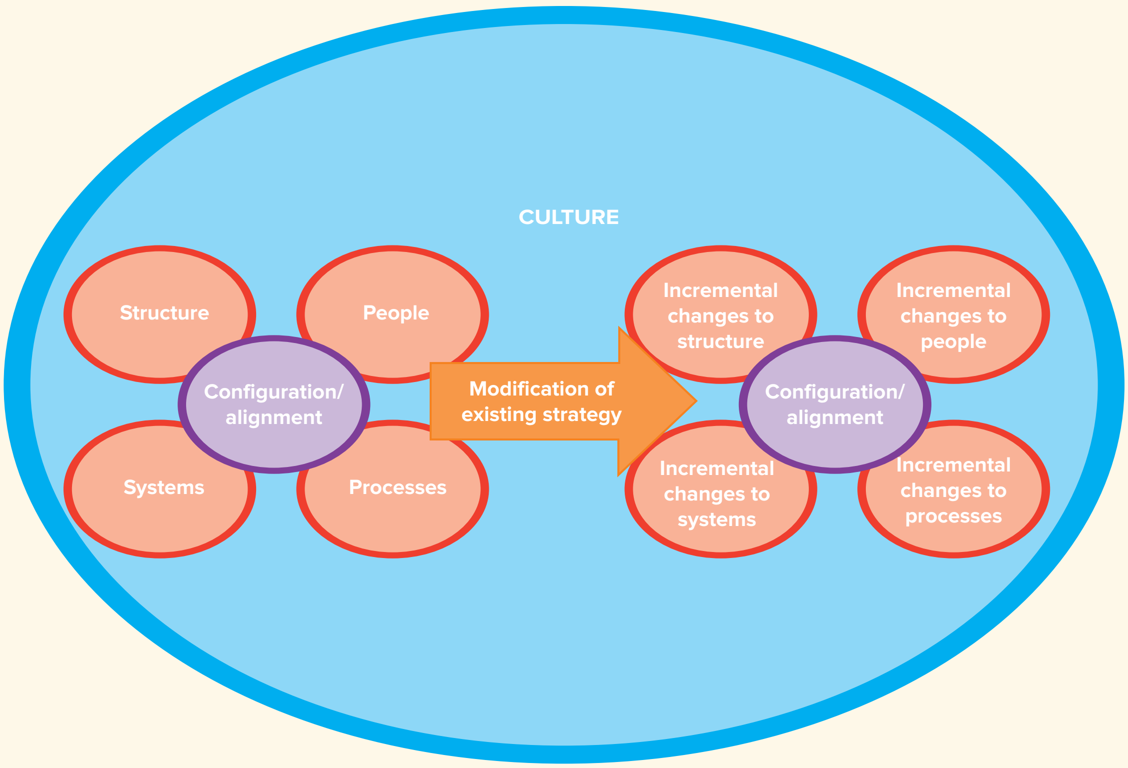

FIGURE 10.2 Incremental changes as part of the strategy execution process

organizations learn from putting a strategy into action and make small-scale changes as a matter of course, by changing product features, packaging, production processes, recruitment procedures, rewards or a whole host of other elements at an operational level. However, the configuration and culture of the organization remain largely unchanged in this context.

When a new strategy is formulated, managers need to cope with more significant changes as the organization enters what Mintzberg et al. (2008) termed a more 'transformation' phase. This might be as a result of more significant changes to the organization's external environment, such as new legislation, or a new competitor entering the market – as we looked at in Chapter 3, or changes to the internal environment, such as a new CEO or the development of new products and services. In these cases the structure, people, systems and processes may need to change in a more radical manner. When this is within existing parameters,[6] such as through the use of a particular technology, or where resources may need to be renewed but where capabilities remain relevant, the change will be less wide-ranging but still significant (Figure 10.3).

In more dynamic and disordered environments, or when the organization has reached a crisis point and needs to develop a turnaround strategy or make a dramatic change of direction, then a radically different strategy will be required (Figure 10.4). The changes to structure, people, systems and processes will then be coupled with significant changes to the way the organization is aligned and may even involve a change to its cultural paradigm.[7]

In devising an action agenda for executing strategy, managers often start with *an assessment of what the organization must do differently to carry out the strategy successfully*. They then consider *how to make the necessary internal changes* as rapidly as possible. Successful strategy implementers have a knack for diagnosing what their organizations need to do to execute the chosen strategy well, and figuring out how to get things done cost-efficiently and with all deliberate speed. They are skilled at promoting results-oriented behaviours

When strategies fail, it is often because of poor execution. Strategy execution is therefore a critical managerial endeavour.

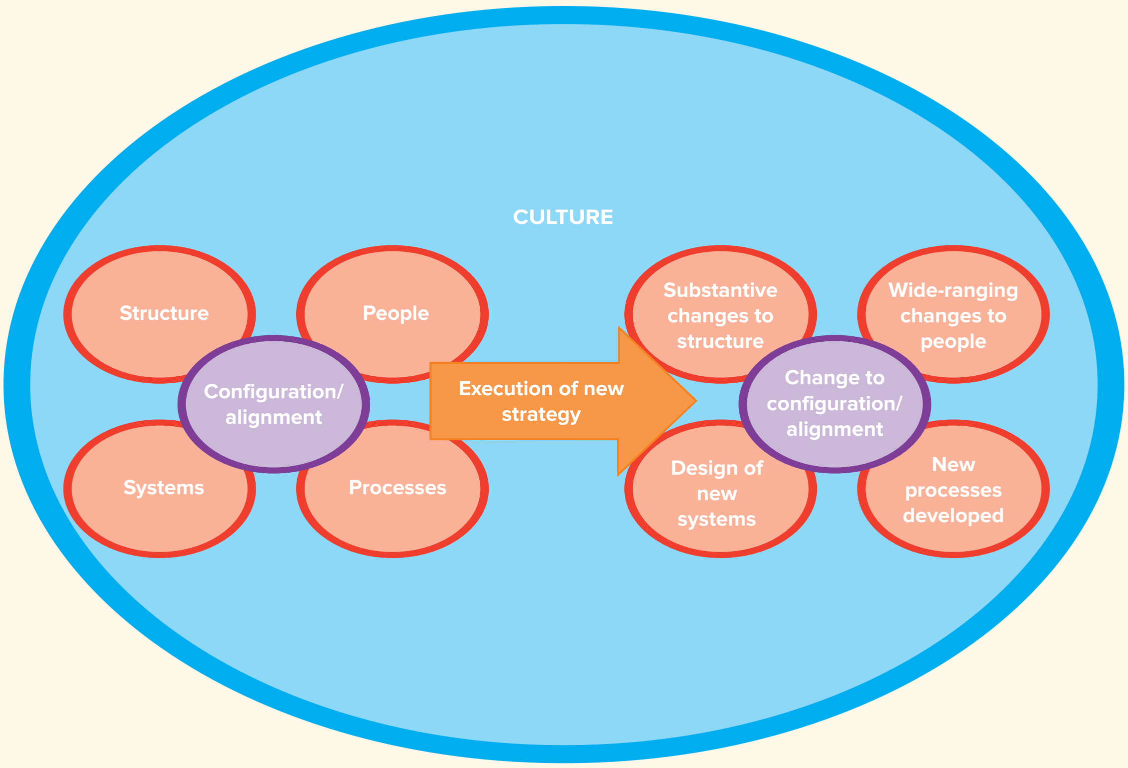

FIGURE 10.3 Executing a new strategy

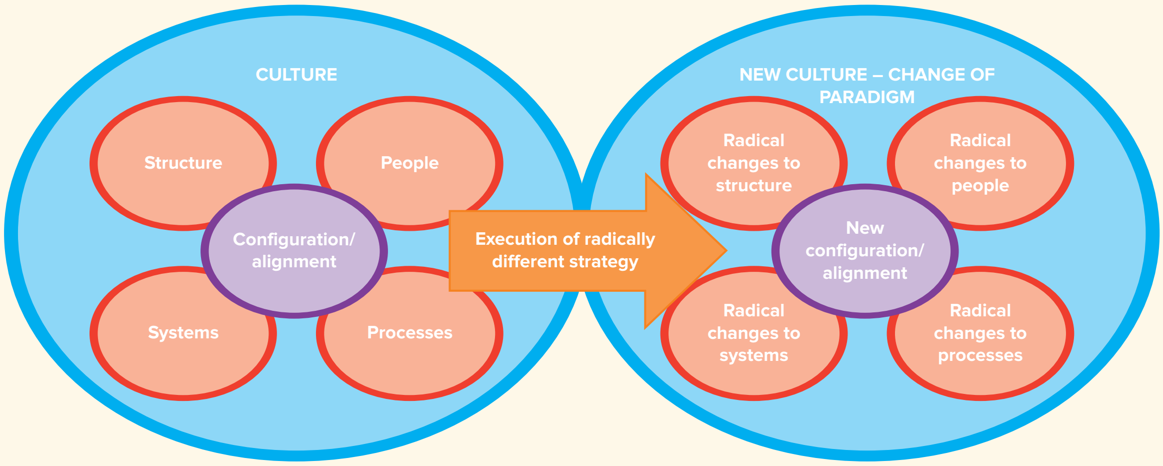

FIGURE 10.4 Execution of radically different strategies – such as a turnaround strategy

> The two best signs of good strategy execution are whether a company is meeting or beating its performance targets and performing value chain activities in a manner that is conducive to company-wide operating excellence.

on the part of company personnel and following through on making the right things happen in a timely fashion.[8]

In big organizations with geographically scattered operating units, the action agenda of senior executives mostly involves communicating the case for change, building consensus for how to proceed, employing strong managers to move the process forward in key organizational units, directing resources to the right places, establishing deadlines and measures of progress, rewarding those who achieve implementation milestones and personally leading the strategic change process. Thus, the bigger the organization, the more that successful strategy execution depends on the co-operation and implementing skills of operating managers who can promote needed changes at the lowest organizational levels and deliver results. In small organizations, top managers can deal directly with front-line managers and employees, personally orchestrating the action steps and implementation sequence, observing at first hand how implementation is progressing and deciding how hard and how fast to push the process along. Regardless of the organization's size and whether implementation involves sweeping or minor changes, the most important leadership trait is a strong, confident sense of what to do and how to do it. Having a strong grip on these two things comes from understanding the circumstances of the organization and the requirements for effective strategy execution. Then it remains for company personnel in strategy-critical areas to step up to the plate and produce the desired results.

What's Covered in Chapters 10 and 11?

The rest of this chapter covers the more concrete elements of strategy execution – choosing the most appropriate options regarding organizational structure and systems, as well as recruiting and retaining the right people, and developing suitable processes to fit the organization's particular strategy. Chapter 11 focuses on the more conceptual aspects of strategy execution, leading change and organizational culture.

Building an Organization Capable of Good Strategy Execution: Where to Begin

Building an organization capable of good strategy execution depends foremost on ensuring that the resources and capabilities that are the basis for the strategy are in place, ready to be deployed. Recall from Chapter 4 that these include the skills, talents, experience and knowledge

of the company's human resources (managerial and otherwise). Proficient strategy execution depends heavily on competent personnel at all levels and in all functions, but because of the many managerial tasks involved and the role of leadership in strategy execution, assembling a strong management team is especially important. Other key resources include processes and organizational systems and structures.

If the strategy being implemented is a new one, the company may need to add to its resource and capability mix in other respects as well. But renewing, upgrading and revising the organization's resources and capabilities is a part of the strategy execution process even if the strategy is fundamentally the same or changing on an incremental basis over time, since resources depreciate and conditions are always changing. Thus, augmenting and strengthening the firm's core competences and seeing that they are suited to the current strategy are also top priorities.

Structuring the organization and work effort is another critical aspect of building an organization capable of good strategy execution. An organizational structure that is well matched to the strategy can help facilitate its implementation; one that is not well suited can lead to higher bureaucratic costs and communication or co-ordination breakdowns.

Strategy Execution and Structure

LO 10.1
Identify what issues to consider in establishing a strategy-supportive organizational structure and organizing the work effort.

There are few hard-and-fast rules for organizing the work effort to support good strategy execution. Every firm's organization chart is partly a product of its particular situation, reflecting prior organizational patterns, varying internal circumstances, executive judgements about reporting relationships and the politics of who gets which assignments. Moreover, every strategy is grounded in its own set of organizational capabilities and value chain activities. But some considerations in organizing the work effort are common to all companies. These are summarized in Figure 10.5 and discussed in the sections that follow.

Deciding Which Value Chain Activities to Perform Internally and Which to Outsource

Choosing wisely which activities to perform internally and which to outsource can lead to several strategy-executing advantages – lower costs, heightened strategic focus, less internal bureaucracy, speedier decision-making and a better arsenal of organizational capabilities.

The advantages of a company having an outsourcing component in its strategy were discussed in Chapter 6, but there is also a need to consider the role of outsourcing in executing the strategy. Aside from the fact that another company (because of its experience, scale of operations and specialized know-how) may be able to perform certain value chain activities better or cheaper than a company can perform them internally, outsourcing can also sometimes make a positive contribution to better strategy execution. Managers too often spend inordinate amounts of time, mental energy and resources haggling with functional support groups or other internal bureaucracies over needed services, leaving less time for them to devote to performing strategy-critical activities in the most proficient manner.

One way to reduce such distractions is to outsource the performance of assorted administrative support functions and perhaps even selected primary value chain activities to outside vendors, thereby enabling the company to concentrate its full energies on performing the value chain activities that are at the core of its strategy, where it can create unique value. For example, E&J Gallo Winery outsources 95 per cent of its grape production, letting farmers take on weather-related and other grape-growing risks while it concentrates its efforts on wine production and sales.[9] Broadcom, a global leader in chips for broadband communication systems, outsources the manufacturing of its chips to Taiwan Semiconductor, thus freeing company personnel to focus their full energies on R&D, new chip design and marketing. Nike concentrates on design, marketing and distribution while outsourcing virtually all production of its shoes and sporting apparel.

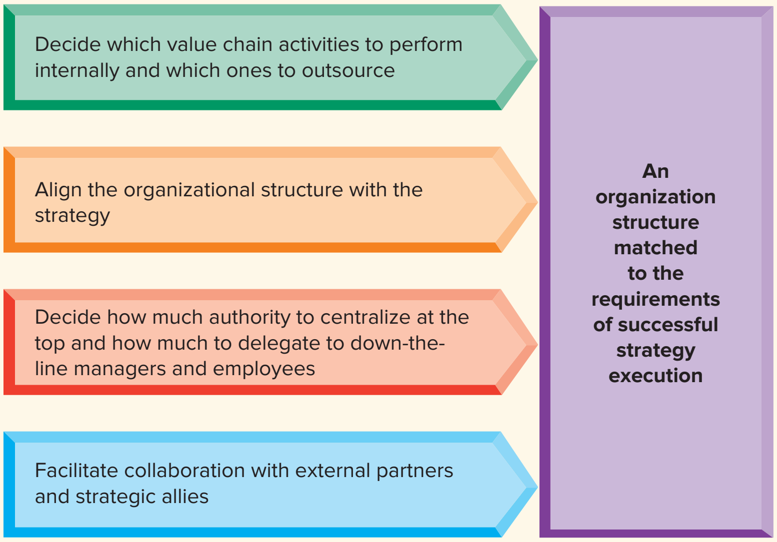

FIGURE 10.5 Structuring the work effort to promote successful strategy execution

Such heightened focus on performing strategy-critical activities can yield three important execution-related benefits:

1. *The company improves its chances of outclassing rivals in the performance of strategy-critical activities and turning a core competence into a distinctive competence.* At the very least, the heightened focus on performing a select few value chain activities should promote more effective performance of those activities. This could materially enhance competitive capabilities by either lowering costs or improving quality. ING Insurance, Hugo Boss, Japan Airlines and Chevron have outsourced their data-processing activities to computer service firms, believing that outside specialists can perform the needed services at lower cost and equal or better quality. A relatively large number of companies outsource the operation of their websites to web design and hosting enterprises. Many businesses that get a lot of enquiries from customers or that have to provide 24/7 technical support to users of their products across the world have found that it is considerably less expensive to outsource these functions to specialists (often located in foreign countries where skilled personnel are readily available and worker compensation costs are much lower) than to operate their own call centres.
2. *The streamlining of internal operations that flows from outsourcing often serves to decrease internal bureaucracies, flatten the organizational structure, speed internal decision-making and shorten the time it takes to respond to changing market conditions.*[10] In consumer electronics, where advancing technology drives new product innovation, organizing the work effort in a manner that expedites getting next-generation products to market ahead of rivals is a critical competitive capability. The world's motor vehicle manufacturers have found that they can shorten the cycle time for new models by outsourcing the large majority of their parts and components to independent suppliers and then working closely with their vendors to swiftly incorporate new technology and better integrate individual parts and components to form engine cooling systems, transmission systems and electrical systems.
3. *Partnerships can add to a company's arsenal of capabilities and contribute to better strategy execution.* By building, continually improving and then leveraging partnerships, a company enhances its overall organizational capabilities and strengthens its competitive assets – assets that deliver more value to customers and consequently pave the way for competitive success. Soft drink and beer manufacturers cultivate their relationships with their bottlers and distributors to strengthen access to local markets, and build loyalty, support and commitment

for corporate marketing programmes, without which their own sales and growth are weakened. In the global hotel industry, many of the major players such as Accor and Intercontinental Hotel Group (IHG) have moved to a more 'asset light' business model, so instead of owning hotel properties, they either manage them on behalf of real-estate partners or they provide support to franchisees, which benefit from their global brands and successful formula. Taking this approach has proved beneficial as it has released large amounts of capital previously tied up in physical assets and allowed the firms to use the cash to invest in emerging markets such as China and India. Companies like Boeing, Aerospatiale, Verizon Communications and Dell have learned that their central R&D groups cannot begin to match the innovative capabilities of a well-managed network of supply chain partners.[11]

However, as was emphasized in Chapter 6, a company must guard against going overboard on outsourcing and becoming overly dependent on outside suppliers. A company cannot be the master of its own destiny unless it maintains expertise and resource depth in performing those value chain activities that underpin its long-term competitive success.[12] As a general rule, therefore, it is the strategically less important activities – like handling customer enquiries and providing technical support, doing the payroll, administering employee benefit programmes, providing corporate security, managing stockholder relations, maintaining fleet vehicles, operating the company's website, conducting employee training, and managing an assortment of information and data-processing functions – for which outsourcing makes the most strategic sense.

Aligning the Firm's Organizational Structure with Its Strategy

The design of the firm's **organizational structure** is a critical aspect of the strategy execution process. The organizational structure comprises the formal and informal arrangement of tasks, responsibilities and lines of authority and communication by which the firm is administered.[13] It specifies the linkages among parts of the organization, the reporting relationships, the direction of information flows and the decision-making processes. It is a key factor in strategy implementation since it exerts a strong influence on how well managers can co-ordinate and control the complex set of activities involved.[14]

Core Concept

A firm's **organizational structure** comprises the formal and informal arrangement of tasks, responsibilities, lines of authority and reporting relationships by which the firm is administered.

A well-designed organizational structure is one in which the various parts (e.g. decision-making rights, communication patterns) are aligned with one another and also matched to the requirements of the strategy. With the right structure in place, managers can orchestrate the various aspects of the implementation process with an even hand and a light touch. Without a supportive structure, strategy execution is more likely to become bogged down in administrative confusion, political manoeuvring and bureaucratic waste.

Video

Michael Jarrett, INSEAD Professor of Organizational Behaviour: '*Getting Strategy Execution Right*'

Good organizational design may even contribute to the firm's ability to create value for customers and realize a profit. By enabling lower bureaucratic costs and facilitating operational efficiency, it can lower a firm's operating costs. By facilitating the co-ordination of activities within the firm, it can improve the capability-building process, leading to greater differentiation and/or lower costs. Moreover, by improving the speed with which information is communicated and activities co-ordinated, it can enable the firm to beat rivals to the market and profit from a period of unrivalled advantage.

Making Strategy-critical Activities the Main Building Blocks of the Organizational Structure

In any business, some activities in the value chain are always more critical to successful strategy execution than others. For instance, a ski apparel manufacturer must be good at styling and design, low-cost manufacturing, distribution (convincing an attractively large number of retailers to stock and promote the company's brand), and marketing and advertising (building a brand image that generates buzz and appeal among ski enthusiasts). In discount stock

brokerage, the strategy-critical activities are fast access to information, accurate order execution, efficient record-keeping and transactions processing, and good customer service. In speciality chemicals, the critical activities are R&D, product innovation, getting new products to market quickly, effective marketing and expertise in assisting customers. Where such is the case, it is important for management to build its organizational structure around proficient performance of these activities, making them the centrepieces or main building blocks in the enterprise's organizational structure.

The rationale for making strategy-critical activities the main building blocks in structuring a business is compelling: if activities crucial to strategic success are to have the resources, decision-making influence and organizational impact they need, they have to be centrepieces in the organizational scheme. Making them the focus of structuring efforts will also facilitate their co-ordination and promote good internal fit – an essential attribute of a winning strategy, as summarized in Chapter 1. To the extent that implementing a new strategy entails new or altered key activities or capabilities, different organizational arrangements may be required.[15]

Matching Type of Organizational Structure to Strategy Execution Requirements

Organizational structures can be classified into a limited number of standard types. The type that is most suitable for a given firm will depend on the firm's size and complexity as well as its strategy. As firms grow and their needs for structure evolve, their structural form is likely to evolve from one type to another. The four basic types are the *simple structure*, the *functional structure*, the *multidivisional structure* and the *matrix structure*, as described below.

Core Concept

A **simple structure** consists of a central executive who handles all major decisions and oversees all operations with the help of a small staff.

1. Simple structure – A **simple structure** is one in which a central executive (often the owner-manager) handles all major decisions and oversees the operations of the organization with the help of a small staff.[16] Simple structures are also known as *line-and-staff structures*, since a central administrative staff supervises line employees who conduct the operations of the firm, or *flat structures*, since there are few levels of hierarchy.[17] It is characterized by limited task specialization; few rules; informal relationships; minimal use of training, planning and liaison devices; and a lack of sophisticated support systems. It has all the advantages of simplicity, including low administrative costs, ease of co-ordination, flexibility, quick decision-making, adaptability and responsiveness to change.[18] Its informality and lack of rules may foster creativity and heightened individual responsibility.

   Simple organizational structures are typically employed by small firms and entrepreneurial start-ups. The simple structure is the most common type of organizational structure since small firms are the most prevalent type of business. As an organization grows, however, this structural form becomes inadequate to the demands that come with size and complexity. In response, growing firms tend to alter their organizational structure from a simple structure to a functional structure.

Simple structures are also called *line-and-staff* structures or *flat* structures.

Core Concept

A **functional structure** is organized into functional departments, with departmental managers who report to the CEO and small corporate staff.

2. Functional structure – A **functional structure** is one that is organized along functional lines, where a function represents a major step in the firm's value chain, such as R&D, engineering and design, manufacturing, sales and marketing, logistics and customer service. Each functional unit is supervised by functional line managers who report to the CEO and a corporate staff. This arrangement allows functional managers to focus on their area of responsibility, leaving it to the CEO and headquarters to provide direction and ensure that their activities are co-ordinated and integrated. Functional structures are also known as *departmental structures*, since the functional units are commonly called departments, and *unitary structures* or *U-forms*, since a single unit is responsible for each function. This can be seen in Figure 10.6, showing South African gold mining and exploration company, Harmony's structure.

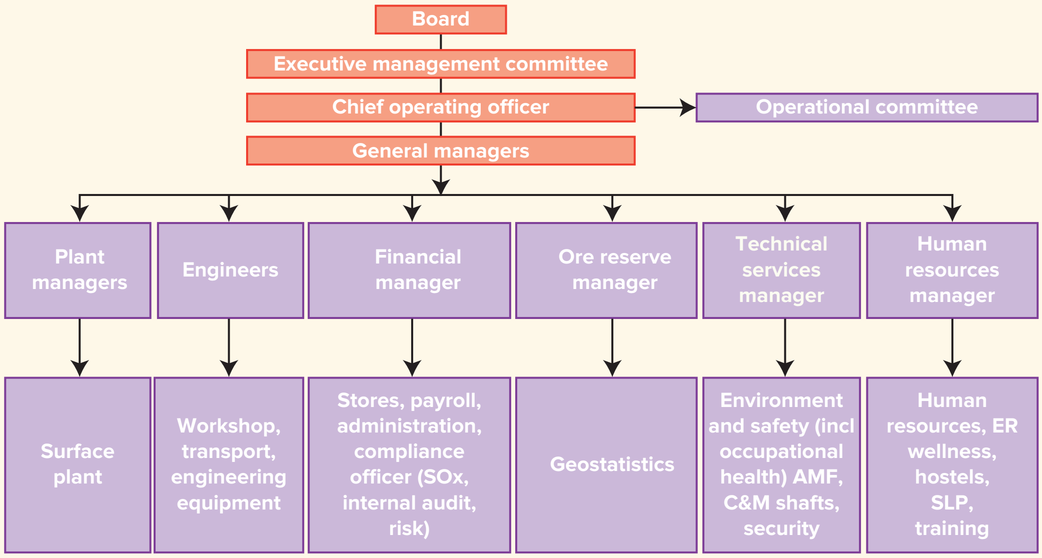

FIGURE 10.6 Harmony's functional structure

Source: Harmony (2009) 'Corporate governance', Annual Report. Available online at www.harmony.co.za/assets/investors/reporting/annual-reports/2009/governance.htm (accessed 29 June 2016).

In large organizations, functional structures lighten the load on top management, relative to simple structures, and make for a more efficient use of managerial resources. Their primary advantage, however, is due to greater task specialization, which promotes learning, enables the realization of scale economies and offers productivity advantages not otherwise available. Their disadvantage is that the departmental boundaries can inhibit the flow of information and limit the opportunities for cross-functional co-operation and co-ordination.

It is generally agreed that some type of functional structure is the best organizational arrangement when a company is in just one particular business (regardless of which of the five generic competitive strategies it opts to pursue). For instance, a technical instruments manufacturer may be organized around R&D, engineering, supply chain management, assembly, quality control, marketing and technical services. A discount retailer, such as Lidl or Aldi, may organize around such functional units as purchasing, warehousing and distribution, store operations, advertising and sales, merchandising and customer service. Functional structures can also be appropriate for firms with high-volume production, products that are closely related and a limited degree of vertical integration.

Functional structures are also called *departmental* structures, *unitary* structures or *U-forms.*

As firms continue to grow, they often become more diversified and complex, placing a greater burden on top management. At some point, the centralized control that characterizes the functional structure becomes a liability, and the advantages of functional specialization begin to break down. To resolve these problems and address a growing need for co-ordination across functions, firms generally turn to the multidivisional structure.

3. Multidivisional structure – A **multidivisional structure** is a decentralized structure consisting of a set of operating divisions organized along market, customer, product or geographic lines, and a central corporate headquarters, which monitors divisional activities, allocates resources, performs assorted support functions and exercises overall control. Since each division is essentially a business, the divisions typically operate as independent profit centres (i.e. with profit/loss responsibility) and are organized internally along functional lines.[19] Division managers oversee day-to-day operations and the development of business-level strategy, while corporate executives

Core Concept

A **multidivisional structure** is a decentralized structure consisting of a set of operating divisions organized along business, product, customer group or geographic lines, and a central corporate headquarters that allocates resources, provides support functions and monitors divisional activities.

attend to overall performance and corporate strategy, the elements of which were described in Chapter 8. Multidivisional structures are also called *divisional structures* or *M-forms*, in contrast to the U-form (functional) structure.

Multidivisional structures are also called *divisional* structures or *M-forms*.

Multidivisional structures are common among companies pursuing some form of diversification strategy or global strategy, with operations in a number of businesses or countries. When the strategy is one of unrelated diversification, as in a conglomerate or holding company, the divisions generally represent separate industries. When the strategy is based on related diversification, the divisions may be organized according to markets, customer groups, product lines, geographic regions or technologies. In this arrangement, the decision about where to draw the divisional lines depends foremost on the nature of the relatedness and the strategy-critical building blocks, in terms of which businesses have key value chain activities in common. For example, a company selling closely related products to business customers as well as two types of end-consumers – online buyers and in-store buyers – may organize its divisions according to customer groups since the value chains involved in serving the three groups differ. Another company may organize by product line due to commonalities in product development and production within each product line. Multidivisional structures are also common among vertically integrated firms. There the major building blocks are often divisional units performing one or more of the major processing steps along the value chain (e.g. raw-material production, components manufacture, assembly, wholesale distribution, retail store operations).

Multidivisional structures offer significant advantages over functional structures in terms of facilitating the management of a complex and diverse set of operations.[20] Putting business-level strategy in the hands of division managers while leaving corporate strategy to top executives

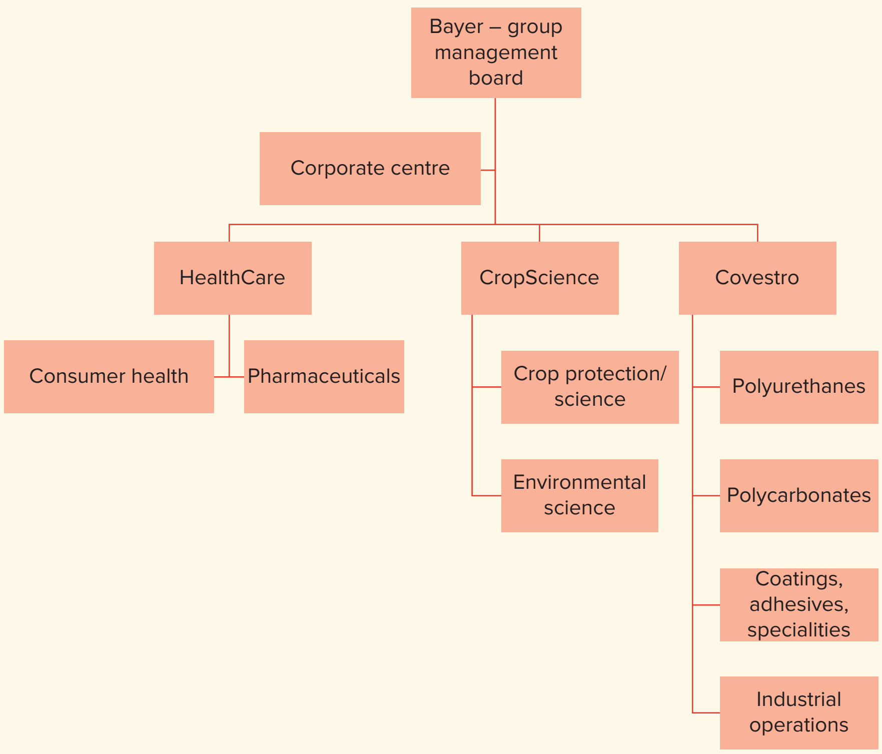

FIGURE 10.7 Bayer AG – example of a multidivisional structure

Source: Based on Bayer AG (2015) Bayer Group Structure 2015, Annual Report, augmented version. Available online at www.annualreport2015.bayer.com/management-report-annexes/fundamental-information-about-the-group/bayer-at-a-glance/corporate-structure.html (accessed 29 June 2016).

reduces the potential for information overload and improves the quality of decision-making in each domain. This also minimizes the costs of co-ordinating division-wide activities while enhancing top management's ability to control a diverse and complex operation. Moreover, multidivisional structures can help align individual incentives with the goals of the corporation and spur productivity by encouraging competition for resources among the different divisions.

But a divisional business-unit structure can also present some problems to a company pursuing related diversification, because having independent business units – each running its own business in its own way – inhibits cross-business collaboration and the capture of cross-business synergies. To solve this type of problem, firms turn to more complex structures, such as the matrix structure.

4. Matrix structure – A **matrix structure** is a combination structure in which the firm is organized along two or more dimensions at once (e.g. business, geographic area, value chain function) for the purpose of enhancing cross-unit communication, collaboration and co-ordination. In essence, it overlays one type of structure onto another type. Matrix structures are managed through multiple reporting relationships, so a middle manager may report to several bosses. For instance, in a matrix structure based on product line, region and function, sales managers for plastic containers in Dubai and Frankfurt might report to the manager of the plastics division, the head of the EMEA sales region and the head of marketing.

Core Concept

A **matrix structure** is a structure that combines two or more organizational forms, with multiple reporting relationships. It is used to foster cross-unit collaboration.

Matrix organizational structures have evolved from the complex, over-formalized structures that were popular in the 1960s, 1970s and 1980s but often produced inefficient, unwieldy bureaucracies. The modern incarnation of the matrix structure is generally a more flexible arrangement, with a single primary reporting relationship that can be overlaid with a temporary secondary reporting relationship as need arises. For example, a software company that is organized into functional departments (software design, quality control, customer relations) may assign employees from those departments to different projects on a temporary basis, so an employee reports to a project manager as well as to his or her primary boss (the functional department head) for the duration of a project.

Matrix structures are also called *composite structures* or *combination structures*. They are often used for project-based, process-based or team-based management. Such approaches are common in businesses involving projects of limited duration, such as consulting, architecture and engineering services. The type of close cross-unit collaboration that a flexible matrix structure supports is also needed to build competitive capabilities in strategically important activities, such as speeding new products to market, which involve employees scattered across several organizational units.[21] Capabilities-based matrix structures that combine process departments (like new product development) with more traditional functional departments provide a solution.

Matrix structures are also called *composite* structures or *combination* structures.

An advantage of matrix structures is that they facilitate the sharing of plant and equipment, specialized knowledge and other key resources – they lower costs by enabling the realization of economies of scope. They also have the advantage of flexibility in form and may allow for better oversight since supervision is provided from more than one perspective. The example in Figure 10.8 shows Nike's matrix structure following its 2009 reorganization. The main changes were to the geographic structure of the organization which moved from four regions to six, and also to the product-based element of the matrix. Nike's managers decided they needed a more granular approach to product decisions so introduced a more detailed sports category layer to give a more holistic approach to activities such as new product development.

However, matrix structures are not without their drawbacks. One disadvantage is that they add an additional layer of management, thereby increasing bureaucratic costs and decreasing response time to new situations.[22] In addition, there is a potential for confusion among employees due to dual reporting relationships and divided loyalties. While there is some controversy over the utility of matrix structures, the modern approach to matrix structures does much to minimize their disadvantages.[23]

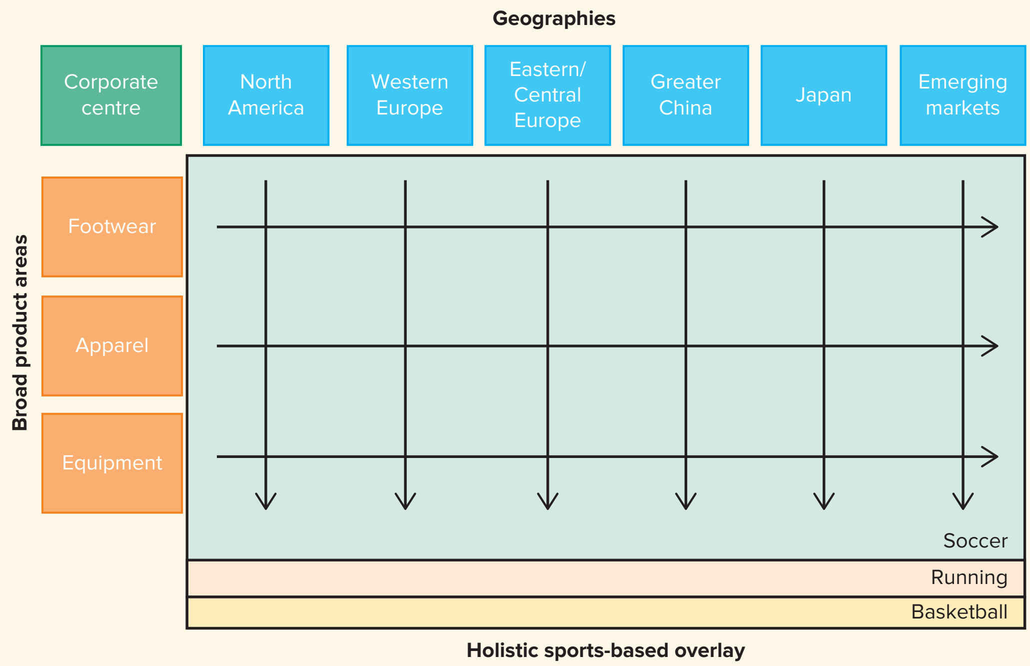

FIGURE 10.8 Nike's matrix structure

Sources: Blenko, M., Mankins, M., Rogers, P. and Morrison, A, (2011) 'Decision insights – Nike's critical workout plan', Bain and Co, *Insights*. Used with permission from Bain & Company. Available online at www.bain.com/publications/articles/decision-insights-nikes-critical-workout-plan-business-spectator.aspx (accessed 29 June 2016); Nike (2009) 'Nike performs geographical restructuring to enhance customer focus', *Nike News.* Available online at http://news.nike.com/news/nike-performs-geographical-restructuring-to-enhance-consumer-focus (accessed 29 June 2016).

Determining How Much Authority to Delegate

On average, larger companies with more complex organizational structures are more decentralized in their decision-making than smaller firms with simple structures – by necessity and by design. Under any organizational structure, however, there is still room for considerable variation in how much authority top managers retain and how much is delegated to down-the-line managers and employees. In executing strategy, then, companies must decide how much authority to delegate to the managers of each organizational unit – especially the heads of divisions, functional departments and other operating units – and how much decision-making latitude to give individual employees in performing their jobs. The two extremes are to centralize decision-making at the top (the CEO and a few close lieutenants) or to decentralize decision-making by giving managers and employees considerable decision-making latitude in their areas of responsibility. As shown in Table 10.1, the two approaches are based on sharply different underlying principles and beliefs, with each having its pros and cons.

Centralized Decision-making: Pros and Cons

In a highly centralized organizational structure, top executives retain authority for most strategic and operating decisions, and keep a tight rein on business-unit heads, department heads and the managers of key operating units; comparatively little discretionary authority is granted to front-line supervisors and rank-and-file employees. The command-and-control paradigm of centralized structures is based on the underlying assumptions that front-line personnel have neither the time nor the inclination to direct and properly control the work they are performing, and that they lack the knowledge and judgement to make wise decisions about how best to do it – hence the need for managerially prescribed policies and procedures, close

TABLE 10.1 Advantages and disadvantages of centralized versus decentralized decision-making

Centralized organizational structures	Decentralized organizational structures
Basic tenets	**Basic tenets**
• Decisions on most matters of importance should be in the hands of top-level managers who have the experience, expertise and judgement to decide what is the best course of action • Lower-level personnel have neither the knowledge, the time, nor the inclination to properly manage the tasks they are performing • Strong control from the top is a more effective means for co-ordinating company actions	• Decision-making authority should be put in the hands of the people closest to, and most familiar with, the situation • Those with decision-making authority should be trained to exercise good judgement • A company that draws on the combined intellectual capital of all its employees can outperform a command-and-control company
Chief advantages	**Chief advantages**
• Fixes accountability through tight control from the top • Eliminates goal conflict among those with differing perspectives or interests • Allows for quick decision-making and strong leadership under crisis situations	• Encourages company employees to exercise initiative and act responsibly • Promotes greater motivation and involvement in the business on the part of more company personnel • Spurs new ideas and creative thinking • Allows fast response to market change • May entail fewer layers of management
Primary disadvantages	**Primary disadvantages**
• Lengthens response times by those closest to the market conditions because they must seek approval for their actions • Does not encourage responsibility among lower-level managers and rank-and-file employees • Discourages lower-level managers and rank-and-file employees from exercising any initiative	• Top management lacks 'full control' – higher-level managers may be unaware of actions taken by empowered personnel under their supervision • Puts the organization at risk if empowered employees happen to make 'bad' decisions • Can impair cross-unit collaboration

supervision and tight control. The thesis underlying authoritarian structures is that strict enforcement of detailed procedures backed by rigorous managerial oversight is the most reliable way to keep the daily execution of strategy on track.

One advantage of an authoritarian structure is tight control by the manager in charge – it is easy to know who is accountable when things do not go well. This structure can also reduce goal conflict among managers from different parts of the organization who may have different perspectives, incentives and objectives. For example, a manager in charge of an engineering department may be more interested in pursuing a new technology than is a marketing manager who doubts that customers will value the technology as highly. Another advantage of a command-and-control structure is that it can enable a more uniform and swift response to a crisis situation that affects the organization as a whole.

However, there are some serious disadvantages too. Hierarchical command-and-control structures make a large organization with a complex structure sluggish in responding to changing market conditions because of the time it takes for the review/approval process to run up all the layers of the management bureaucracy. Furthermore, to work well, centralized decision-making requires top-level managers to gather and process whatever information is relevant to the decision. When the relevant knowledge resides at lower organizational levels (or is technical, detailed or hard to express in words), it is difficult and time-consuming to get all the facts and nuances in front of a high-level executive located far from the scene of the action – full understanding of the situation cannot readily be copied from one mind to another. Hence, centralized decision-making is often impractical – the larger the company and the more scattered its operations, the more that decision-making authority must be delegated to managers closer to the scene of the action.

The ultimate goal of decentralized decision-making is to put authority in the hands of those persons or teams closest to and most knowledgeable about the situation.

Decentralized Decision-making: Pros and Cons

In a highly decentralized organization, decision-making authority is pushed down to the lowest organizational level capable of making timely, informed, competent decisions. The objective is to put adequate decision-making authority in the hands of the people closest to and most familiar with the situation, and train them to weigh all the factors and exercise good judgement. Decentralized decision-making means, for example, that employees with customer contact are empowered to do what it takes to please customers. At Starbucks, for example, employees are encouraged to exercise initiative in promoting customer satisfaction – there is the oft-repeated story of a store employee who, when the computerized cash register system went offline, enthusiastically offered free coffee to waiting customers.[24]

The case for empowering front-line managers and employees to make decisions regarding daily operations and strategy execution is based on the belief that a company that draws on the combined intellectual capital of all its employees can outperform a command-and-control company.[25] The challenge in a decentralized system is in maintaining adequate control. With decentralized decision-making, top management maintains control by determining the limits to authority for each type of position, installing company-wide strategic control systems, holding people accountable for their decisions, instituting compensation incentives that reward people for doing their jobs in a manner that contributes to good company performance and creating a corporate culture where there is strong peer pressure on individuals to act responsibly.[26]

Decentralized organization structures have much to recommend them. Pushing decision-making authority down to subordinate managers, work teams and individual employees shortens organizational response times and spurs new ideas, creative thinking, innovation and greater involvement on the part of all company personnel. Moreover, in worker-empowered structures, jobs can be defined more broadly, several tasks can be integrated into a single job and people can direct their own work. Fewer layers of managers are needed because deciding how to do things becomes part of each person's or team's job. Today's online communication systems and smartphones make it easy and relatively inexpensive for people at all organizational levels to have direct access to data, other employees, managers, suppliers and customers. They can access information quickly (via the Internet or company network), readily check with superiors or whoever else as needed, and take responsible action. Typically, there are genuine gains in morale and productivity when people are provided with the tools and information they need to operate in a self-directed way.

But decentralization also has some disadvantages. Top managers lose an element of control over what goes on (since empowered subordinates have authority to act on their own) and may thus be unaware of actions being taken by personnel under their supervision. Such a lack of control can put a company at risk in the event that empowered employees make unwise decisions. Moreover, because decentralization gives organizational units the authority to act independently, there is a risk of too little collaboration and co-ordination between different organizational units.

Many companies have concluded that the advantages of decentralization outweigh the disadvantages. Over the past 15–20 years, there has been a decided shift from authoritarian multilayered hierarchical structures to flatter, more decentralized structures that stress employee empowerment. This shift reflects a strong and growing consensus that authoritarian, hierarchical organizational structures are not well suited to implementing and executing strategies in an era when extensive information and instant communication are the norm, and when a big fraction of the organization's most valuable assets consists of intellectual capital and resides in the knowledge and capabilities of its employees.

Efforts to decentralize decision-making and give company personnel some leeway in conducting operations must be tempered with the need to maintain adequate control and cross-unit co-ordination.

Capturing Cross-business Strategic Fit in a Decentralized Structure

Diversified companies striving to capture the benefits of synergy between separate businesses have to beware of giving business-unit heads full rein to operate independently. Cross-business strategic fit typically has to be captured either by

enforcing close cross-business collaboration or by centralizing performance of functions requiring close co-ordination at the corporate level.[27] For example, if businesses with overlapping process and product technologies have their own independent R&D departments – each pursuing its own priorities, projects and strategic agendas – it is hard for the corporate parent to prevent duplication of effort, capture either economies of scale or economies of scope, or encourage more collaborative R&D efforts. Where the potential for cross-business R&D synergies exist, the best solution is usually to centralize the R&D function and have a co-ordinated corporate R&D effort that serves the interests of both the individual businesses and the company as a whole. Likewise, centralizing the related activities of separate businesses makes sense when there are opportunities to share a common salesforce, use common distribution channels, rely on a common field service organization, use common e-commerce systems, and so on.

Emerging Theme 10.1

NEW STRUCTURES: EMPTY BIRD'S NESTS, G-FORMS AND RESEARCH COMMONS

Some of the most commonly found organizational structures stem from the early part of the 20th century, when entrepreneurs such as Henry Ford found that to manufacture complex products on an economic scale, hierarchies and planners were needed to control the work done. More diversified organizations adapted divisional structures to cope with the complexities of broad portfolios of increasingly unrelated products and services with control sitting with a corporate centre and based on performance measures. Organizations with these structures will have top-down processes but while what Mintzberg (1989) referred to as the machine organization is generally centralized, the diversified organization will often be looser, with each division having a certain amount of latitude in terms of how it meets its performance targets. Neither would be classed as extreme examples of decentralization.

According to leading management thinker Charles Leadbeater, author of *We-think* (2009), the Internet has given rise to organizations that are changing a lot of the assumptions managers make about what structures and control systems are needed to implement strategy successfully. Some of these organizations, such as Wikipedia, are described as anarchic or, as Leadbeater states (2009, p. 19), are 'like a vast bird's nest of knowledge, each piece of information carefully resting on another. Yet this is a bird's nest with no bird in charge of where to put each piece. It has almost constructed itself.' In the same way that the early pioneers of mass production and multinational corporations experimented with organizational structures to develop a suitable model, Leadbeater contends that Internet-based innovators, such as Jimmy Wales, the founder of Wikipedia, are exploring new forms of organization based around self-organizing networks.

Although there can be no doubt that Wikipedia has achieved much in the few years since its inception in 1999, it is not without its critics. The site has not produced a substantial economic return for its founder and some commentators claim that it has far more errors than a print encyclopaedia produced through more traditional means, such as *Britannica*. However, Wikipedia can correct mistakes within minutes of their discovery and, in a study carried out by *Nature* magazine in 2005, the researchers found an average of 2.92 errors per article in *Britannica* compared to 3.86 for Wikipedia. In January 2011, the online encyclopaedia also had more than 17 million entries in 250 languages compared to *Britannica*'s 120,000 in English (Bennett, 2011). Wikipedia is also not the only organization to have used self-organizing networks to disrupt (intentionally or unintentionally) the status quo in an industry. The Mozilla and Linux networks have successfully competed with IT giants such as Microsoft, and firms such as TripAdvisor and Yelp have created distinctive websites based on user-generated content that a regular review publication relying on paid journalists would find it impossible to imitate (Bennett, 2011).

So, can managers learn anything from entities that are organized without formal organizational features such as job titles, hierarchies and functional departments? Leadbeater argues that the success of such enterprises is the result of three key elements: 'participation, recognition and collaboration' (2009, p. 21). Therefore organizations that make it easy for people with the right skills to participate in crafting and executing strategy find ways to recognize their contribution to the process in ways they will value, and put in place mechanisms that allow effective collaboration where the ideas generated collectively can be screened and evaluated, and have the potential to maximize the potential of their people.

Companies from emerging economies such as China, Brazil and India are also challenging conventional ideas about the way in which organizations are structured. Ricardo Semler's SEMCO, based in Brazil, has shown that traditional hierarchy is not a prerequisite for success – reducing the number of management layers from 12 to 3 and creating what is termed a circular organization where employees are mostly self-organizing. SEMCO also pioneered the concept of the boundaryless organization as many of its employees were encouraged to found satellite companies, which took on some of the tasks previously carried out by the parent.

In India some of the most successful companies are a new form of federated conglomerate, the G-Form (Ramachandran et al., 2013), which is a new take on the H-Form or Holding Company approach seen in such examples as Virgin. Where the G-Form adds value is through the promotion of synergy between different businesses, often brokered by a small but influential corporate centre. An example of the impact this approach can have came when an executive from Tata's group centre brokered a deal between TCS, Titan and Tata Chemicals to create a revolutionary new water filter product, the Swach, which has the potential to produce clean water for even the poorest people in India.

Another newly identified structure has been termed the i-form, or innovation form, organization (Miles et al., 2009), which could be seen as a sort of ecosystem (see Emerging Theme 6.1) based around the sharing of intellectual property. So-called research commons (which operate on a similar basis to common land shared by farmers in some parts of the world) are now managed by groups of organizations around specific technologies or groups of patents. Taiwanese electronics firm Acer was one of the first to pioneer this approach by creating independent business units that continued to share knowledge created by each separate company. Advertising giant WPP has adopted an approach known as 'horizontality' to try to co-ordinate the activities and knowledge of the many advertising agencies it now owns globally.

Sources: Bennett, D. (2011) 'Assessing Wikipedia, Wiki-style, on its 10th anniversary', *Business Week,* 6 January. Available online at www.businessweek.com/magazine/content/11_03/b4211057979684.htm (accessed 25 March 2012); Leadbeater, C. (2009) *We-think,* London, Profile Books; Miles, R., Miles, G., Snow, C., Blomqvist, K. and Rocha, H. (2009) 'The i-form organization', *California Management Review,* 51(4): 61–76; Mintzberg, H. (1989) *Mintzberg on Management: Inside our Strange World of Organizations,* New York, Free Press; Ramachandran, J., Manikandan, K.S. and Pant, A. (2013) 'Why conglomerates thrive (outside the US)', *Harvard Business Review,* December, pp. 110–119.

Facilitating Collaboration with External Partners and Strategic Allies

Organizational mechanisms – whether formal or informal – are also required to ensure effective working relationships with each major outside constituency involved in strategy execution. Strategic alliances, outsourcing arrangements, joint ventures and co-operative partnerships present immediate opportunities and open the door to future possibilities, but little of value can be realized without active management of the relationship. Unless top management sees that constructive organizational bridge-building with strategic partners occurs and that productive working relationships emerge, the value of co-operative relationships is lost and the company's power to execute its strategy is weakened. If close working relationships with suppliers are crucial, then supply chain management must enter into considerations regarding how to create an effective organizational structure. If distributor/dealer/franchisee relationships are important, someone must be assigned the task of nurturing the relationships with forward channel allies. If working in parallel with providers of complementary products and services contributes to enhanced organizational capability, then co-operative organizational arrangements have to be put in place and managed to good effect.

Building organizational bridges with external allies can be accomplished by appointing 'relationship managers' with responsibility for making particular strategic partnerships or alliances generate the intended benefits. Relationship managers have many roles and functions: getting the right people together, promoting good rapport, seeing that plans for specific activities are developed and carried out, helping adjust internal organizational procedures and communication systems, ironing out operating dissimilarities and nurturing interpersonal co-operation. Multiple cross-organization ties have to be established and kept open to ensure proper communication and co-ordination.[28] There has to be enough information-sharing to make the relationship work, as well as periodic frank discussions of conflicts, trouble spots and changing situations.

Organizing and managing a network structure provides another mechanism for encouraging more effective collaboration and co-operation among external partners. A **network structure** is the arrangement linking a number of independent organizations involved in some common undertaking. A well-managed network structure typically includes one firm in a more central role, with the responsibility of ensuring that the right partners are included and the activities across the network co-ordinated. The high-end Italian motorcycle company Ducati operates in this manner, assembling its motorcycles from parts obtained from a hand-picked integrated network of parts suppliers.

Core Concept

A **network structure** is the arrangement linking a number of independent organizations involved in some common undertaking.

Further Perspectives on Structuring the Work Effort

All organization designs have their strategy-related strengths and weaknesses. To do a good job of matching structure to strategy, strategy implementers first have to pick a basic design and modify it as needed to fit the company's particular business line-up. They must then (1) supplement the design with appropriate co-ordinating mechanisms (cross-functional task forces, special project teams, self-contained work teams, and so on) and (2) institute whatever networking and communications arrangements it takes to support effective execution of the firm's strategy. Some companies may avoid setting up 'ideal' organizational arrangements because they do not want to disturb existing reporting relationships or because they need to accommodate other situational idiosyncrasies, yet they must still work towards the goal of building a competitively capable organization.

The ways and means of developing stronger core competences and organizational capabilities (or creating altogether new ones) have to fit a company's own circumstances. Not only do different companies and executives tackle the capabilities-building challenge in different ways, but the task of building different capabilities requires different organizing techniques. Thus, generalizing about how to build capabilities has to be done cautiously. What can be said unequivocally is that building a capable organization entails a process of consciously knitting together the efforts of individuals and groups. Organizational capabilities emerge from establishing and nurturing co-operative working relationships among people and groups to perform activities in a more efficient, value-creating fashion. While an appropriate organizational structure can facilitate this, organization-building is a task in which senior management must be deeply involved. Indeed, effectively managing both internal organization processes and external collaboration to create and develop competitively valuable organizational capabilities remains a top challenge for senior executives in today's companies.

People: Staffing the Organization

LO 10.2

Explain why hiring, training and retaining the right people constitute key components of the strategy execution process.

Organizations will find it hard to perform the activities required for successful strategy execution without attracting and retaining talented managers and employees with suitable skills and intellectual capital.

Putting Together a Strong Management Team

Putting together a talented management team with the right mix of experiences, skills and abilities to get things done is one of the first strategy-implementing steps.

Assembling a capable management team is a cornerstone of the organization-building task.[29] While different strategies and company circumstances sometimes call for different mixes of backgrounds, experiences, management styles and know-how, some commentators state that *the most important consideration is to fill key managerial slots with smart people who are clear thinkers, capable of figuring out what needs to be done, good at managing people and skilled in delivering good results.*[30] Other studies are clear that the task of implementing challenging strategic initiatives must be assigned to executives who have the skills and talents to turn their decisions into results that meet or beat the established performance targets. They state that without a smart, capable, results-oriented management team, the implementation process is likely to be hampered by missed deadlines, misdirected or wasteful efforts and managerial

ineptness.[31] By the same token, there is a view that weak executives are serious impediments to getting optimal results because they are unable to differentiate between ideas that have merit and those that are misguided – the calibre of work done under their supervision usually suffers accordingly.[32] In contrast, managers with strong strategy-implementing capabilities have a talent for asking tough, incisive questions; they know enough about the details of the business to be able to ensure the soundness of the decisions of the people around them, and they can discern whether the resources people are asking for to put the strategy in place make sense. They are good at getting things done through others, partly by making sure they have the right people under them and that these people are put in the right jobs.[33] They consistently follow through on issues, monitor progress carefully, make adjustments when needed and keep important details from slipping through the cracks. In short, they understand how to drive organizational change, and they have the managerial skills and discipline requisite for first-rate strategy execution.

Sometimes a company's existing management team is up to the task; at other times it may need to be strengthened or expanded by promoting qualified people from within or by bringing in outsiders whose experiences, talents and leadership styles better suit the situation. In turnaround and rapid-growth situations, and in instances when a company does not have insiders with the requisite know-how, filling key management slots from the outside is a fairly standard organization-building approach. In addition, it is important to ferret out and replace managers who, for whatever reasons, either do not buy in to the case for making organizational changes or do not see ways to make things better.[34] Industry experts state that, for a management team to be truly effective at strategy execution, it must be composed of managers who recognize that organizational changes are needed and who are ready to get on with the process. Weak executives and die-hard resisters have to be replaced or side-lined, perhaps by shifting them to areas where they cannot hamper new strategy execution initiatives.

The overriding aim in building a management team should be to assemble a *critical mass* of talented managers who can function as agents of change and further the cause of first-rate strategy execution. Every manager's success is enhanced (or limited) by the quality of his or her managerial colleagues, and the degree to which they freely exchange ideas, debate ways to make operating improvements and join forces to tackle issues and solve problems.[35] When a first-rate manager enjoys the help and support of other first-rate managers, it is possible to create a managerial whole that is greater than the sum of individual efforts – talented managers who work well together as a team can produce organizational results that are dramatically better than those that one or two star managers acting individually can achieve.[36]

Illustration Capsule 10.1 describes General Electric's (GE's) widely acclaimed approach to developing a top-calibre management team.

Illustration Capsule 10.1

HOW GE DEVELOPS A TALENTED AND DEEP MANAGEMENT TEAM

GE is widely considered to be one of the best-managed companies in the world, partly because of its concerted effort to develop outstanding managers. It ranked number one among the best companies for leadership in the most recent global survey conducted by the Hay Group. For a start, GE strives to hire talented people with a high potential for executive leadership; it then goes to great lengths to expand the leadership, business and decision-making capabilities of all its managers. The company spends about $1 billion annually on training and education programmes. In 2009, all of its 191 most senior executives had spent at least 12 months in training and professional development during their first 15 years at GE.

Four key elements undergird GE's efforts to build a talent-rich stable of managers:

1. GE makes a practice of transferring managers across divisional, business or functional lines for sustained periods of time. Such transfers allow managers to develop relationships with colleagues in other parts of the company, help break down insular thinking in business 'silos', promote the sharing of cross-business ideas and best practices, and build a mind-set open and adaptive to international

markets. There is an enormous emphasis at GE on transferring ideas and best practices from business to business, and making GE a 'boundaryless' company.

2. In selecting executives for key positions, GE is strongly disposed to candidates who exhibit what are called the 'four Es': enormous personal *energy,* the ability to *energize* others, *edge* (a GE code word for instinctive competitiveness and the ability to make tough decisions in a timely fashion – saying yes or no, and not maybe) and *execution* (the ability to carry things through to fruition). Considerable attention is also paid to problem-solving ability, experience in multiple functions or businesses, and experience in driving business growth (as indicated by good market instincts, in-depth knowledge of particular markets, customer touch and technical understanding).
3. All managers are expected to be proficient at what GE calls *workout* – a process in which managers and employees come together to confront issues as soon as they come up, pinpoint the root cause of the issues and bring about quick resolutions so that the business can move forwards. Workout is GE's way of training its managers to diagnose what to do and how to do it.
4. Each year GE sends about 10,000 newly hired and long-time managers to its John F. Welch Leadership Development Centre (generally regarded as one of the best corporate training centres in the world) for a three-week course on the company's Six Sigma quality initiative. GE's Leadership Development Centre also offers advanced courses for senior managers, which may focus on a single management topic for a month. All classes involve managers from different GE businesses and different parts of the world. Some of the most valuable learning comes between formal class sessions when GE managers from different businesses trade ideas about how to improve processes and better serve the customer. This knowledge sharing not only spreads best practices throughout the organization but also improves each GE manager's knowledge.

One of the keys to the success of the management development process at GE is its ability to be adapted to a changing environment: 'It's a constant evolution', according to Chief Learning Officer Susan Peters.* Under the leadership of Jack Welch, GE's CEO from 1980 to 2001, training activities were focused around cost-cutting, efficiency and deal-making. His successor, Jeffrey Immelt, adapted the focus of development programmes to drive towards new goals of risk-taking, innovation and customer focus. Recently, GE has tackled the ascendancy of emerging markets by an increased focus on global capability development, including the development of the China Learning Centre in Shanghai. This has had a visible impact on the organization: in the past seven years the proportion of non-US executives has doubled, from 15 per cent to more than 30 per cent.

As a key part of talent development, talent assessment and feedback are approached with characteristic GE energy. Each of GE's 85,000 managers and professionals is graded in an annual process that divides them into five tiers: the top 10 per cent, the next 15 per cent, the middle 50 per cent, the next 15 per cent and the bottom 10 per cent. Everyone in the top tier gets stock awards, nobody in the fourth tier gets shares of stock and most of those in the fifth tier become candidates for being weeded out. Business heads are pressured to weed out 'C' players. CEO Jeffrey Immelt personally checks the performance reviews of the top 600 employees each year, as part of GE's intensive, months-long performance review process.

*Brady, D. (2010) 'Can GE still manage?' *Bloomberg Businessweek,* 25 April, pp. 26–32. Available online at www.bloomberg.com/news/articles/2010-04-15/can-ge-still-manage.

Note: Illustration Capsule developed with Jeffrey L. Boyink.

Sources: GE website (accessed June 2010); Hewitt Associates, 'Managing leadership in turbulent times – why and how the global top companies for leaders optimize leadership talent in emerging markets' (White Paper). Available online at www.aon.com/attachments/thought-leadership/Managing_Leadership_Turbulent_Times_033009.pdf; DOUG KANTER / Stringer; 'Hay Group study identifies best companies for leadership', *Bloomberg Businessweek.com,* 17 February 2010. Available online at www.haygroup.com/hu/press/details.aspx?id=27804.

In many industries, adding to a company's talent base and building intellectual capital are more important to good strategy execution than additional investments in capital projects.

Recruiting, Training and Retaining Capable Employees

Assembling a capable management team is not enough. Staffing the organization with the right kinds of people must go much deeper than managerial jobs in order for strategy-critical value chain activities to be performed competently. *The quality of an organization's people is always an essential ingredient of successful strategy execution – knowledgeable, engaged employees are a company's best source of creative ideas for the nuts-and-bolts operating improvements that lead to operating excellence.* Companies like Google, Microsoft, McKinsey & Company, KPMG, Cisco Systems, Amazon.com, Unilever, Britvic, Adidas, SAP, Goldman Sachs and Intel make a concerted effort to recruit the best and brightest people they can find and then retain them with excellent compensation packages, opportunities for rapid advancement and professional growth, and interesting assignments. Even though many employers have scaled down their talent management programmes during the recession, those that have learned the lessons of previous downturns keep investing in their workforce and seek to retain their best people.

The best companies make a point of recruiting and retaining talented employees – the objective is to make the company's entire workforce (managers and rank-and-file employees) a genuine competitive asset.

The NHS operates a scheme called Gateway that seeks outsiders with the skills and experience to undertake director-level roles. It also provides support and development to help them find suitable roles in the organization.[37] McKinsey & Company, one of the world's premier management consulting firms, recruits only cream-of-the-crop MBAs from Europe's top business schools; such talent is essential to McKinsey's strategy of performing high-level consulting for the world's top corporations. The leading global accounting firms screen candidates not only on the basis of their accounting expertise but also on whether they possess the people skills needed to relate well with clients and colleagues. In high-tech companies, the challenge is to staff workgroups with gifted, imaginative and energetic people who can bring life to new ideas quickly and inject into the organization what one Dell executive calls 'hum'.[38] The saying 'People are our most important asset' may seem trite, but it fits high-tech companies precisely. Besides checking closely for functional and technical skills, Dell tests applicants for their tolerance of ambiguity and change, their capacity to work in teams and their ability to learn on the fly. Companies like Amazon.com, Google and Cisco Systems have broken new ground in recruiting, hiring, cultivating, developing and retaining talented employees – almost all of whom are in their 20s and 30s. Cisco goes after the top 10 per cent, raiding other companies and endeavouring to retain key people at the companies it acquires. Cisco executives believe that a cadre of star engineers, programmers, managers, salespeople and support personnel is the backbone of the company's efforts to execute its strategy and remain the world's leading provider of Internet infrastructure products and technology.

The practices listed below are common among companies dedicated to recruiting, training and retaining the most capable people they can find:

1. Spending considerable effort on screening and evaluating job applicants – selecting only those with suitable skill sets, energy, initiative, judgement, aptitude for learning, and personality traits that mesh well with the company's work environment and culture
2. Putting employees through training programmes that continue throughout their careers
3. Providing promising employees with challenging, interesting and skill-stretching assignments
4. Rotating people through jobs that span functional and geographic boundaries – providing people with opportunities to gain experience in a variety of international settings is increasingly considered an essential part of career development in multinational or global companies
5. Making the work environment stimulating and engaging so that employees will consider the company a great place to work – progressive companies work hard at creating an environment in which employees are made to feel that their views and suggestions count

Video

Marshall Goldsmith, Coach and Author: '*Six Questions to Increase Employee Engagement*'

6. Striving to retain talented, high-performing employees via promotions, salary increases, performance bonuses, stock options and equity ownership, fringe-benefit packages and other perks
7. Coaching average performers to improve their skills and capabilities, while weeding out underperformers and benchwarmers.

Systems for Strategy Execution

LO 10.3
Discuss the different systems that underpin good strategy execution.

Organization strategies cannot be executed well without a number of internal systems. These can be broadly divided into those that **Support** various key operational processes of strategy execution, those that **Control** execution by providing information critical to strategy implementation, and those that **Reward** desired behaviour. Each of these systems needs to be aligned to the strategy the organization is following in order to underpin effective execution and so will be tailored to fit.[39] For example, a firm following a differentiation strategy based on innovation and technological advances might have support systems that facilitate processes such as knowledge sharing and control systems that measure innovation performance – perhaps in the form of number of patents secured or the percentage of ideas that become successfully commercialized. Reward systems may focus on bonus payments to teams for successful new product launches or recognize the contribution of technical staff – such as 3M's Carlton Society, which has now been acting as a Hall of Fame for employees for more than 50 years.

Support Systems

Southwest Airlines, Singapore Airlines, Lufthansa, British Airways and other successful airlines cannot hope to provide a passenger-pleasing service without a user-friendly online reservation system, an accurate and speedy baggage-handling system and a strict aircraft maintenance programme that minimizes problems requiring at-the-gate service that delay departures. FedEx has internal communication systems that allow it to co-ordinate its 80,000-plus vehicles in handling an average of 8 million packages a day. Its leading-edge flight operations systems allow a single controller to direct as many as 200 of FedEx's 664 aircraft simultaneously, overriding their flight plans should weather problems or other special circumstances arise. In addition, FedEx has created a series of e-business tools for customers that allow them to ship and track packages online, create address books, review shipping history, generate customized reports, simplify customer billing, reduce internal warehousing and inventory management costs, purchase goods and services from suppliers, and respond to quickly changing customer demands. All of FedEx's systems support the organization's strategy of providing businesses and individuals with a broad array of package delivery services (from premium next-day to economical five-day deliveries) and enhancing its competitiveness against United Parcel Service and DHL.

In mining and quarrying, one of the most important pieces of equipment is the fleet of vehicles that transport materials such as ore and coal around the site. These large trucks rely on specialist off-road tyres that have to withstand an often hostile environment. Tyre organizations such as OTR and Michelin have developed tyre monitoring systems that detect pressure, temperature and depth of tread without the need to stop the trucks from working. Michelin's system is within the tyre itself and transmits data to the control centre at the mine or quarry via a tyre management system. Hand-held units are used to monitor tread depth and the external condition of the tyres. Using these sorts of systems has allowed mining organizations, such as Norwegian iron ore producer Sydvaranger, to increase productivity by reducing the amount of downtime required for inspecting their vehicles.[40]

Amazon.com ships customer orders of books, CDs, toys and a myriad other items from fully computerized warehouses with a capacity of more than 17.5 million square feet (2010). The warehouses are so technologically sophisticated that they require about as many lines of code to run as Amazon's website. Using complex picking algorithms, computers initiate the order-picking process by sending signals to workers' wireless receivers, telling them which items to pick off the shelves in which order. Computers also generate data on misboxed items, chute backup times,

line speed, worker productivity and shipping weights on orders. Systems are upgraded regularly, and productivity improvements are aggressively pursued. In 2003 Amazon turned its inventory over 20 times annually in an industry whose average was 15 turns; by 2009 its industry turnover had decreased to an unprecedented 12. Amazon's warehouse efficiency and cost per order filled was so low that one of the fastest-growing and most profitable parts of its business was using its warehouses to run the e-commerce operations of other large retail chains.

Most telephone organizations, electric utilities and TV broadcasting systems have online monitoring systems to spot transmission problems within seconds and increase the reliability of their services. At eBay, there are systems for real-time monitoring of new listings, bidding activity, website traffic and page views. Chelsea and Westminster Healthcare Trust, which operates hospital sites in West London, installed an e-pharmacy system with a robotic dispenser and linked e-procurement system in 2004. The system improved the accuracy of the operations by reducing prescribing errors as well as reducing waiting times for patients and overtime for staff.[41] IBM makes extensive use of social software applications such as Lotus Connections to support its 1,796 online communities, having discovered that many of its employees depend on these tools to do their work.[42] In businesses such as public accounting and management consulting, where large numbers of professional staff need cutting-edge technical know-how, organizations have developed systems that identify when it is time for certain employees to attend training programmes to update their skills and know-how. Many organizations have catalogued best-practice information on their intranets to promote faster transfer and implementation organization-wide.[43]

Well-conceived state-of-the-art operating systems not only enable better strategy execution but also strengthen organizational capabilities – sometimes enough to provide a competitive edge over rivals. For example, an organization with a differentiation strategy based on superior quality (covered in Chapter 5) has added capability if it has systems for training personnel in quality techniques, tracking product quality at each production step and ensuring that all goods shipped meet quality standards. If the systems it employs are advanced systems that have not yet been adopted by rivals, the systems may provide the organization with a competitive advantage as long as the costs of deploying the systems do not outweigh their benefits. Luxury chocolate maker Godiva makes use of an electronic resource planning system (ERP) and a tailored customer relationship management system (CRM) to manage operations in its diverse markets (North America, Europe, Hong Kong and Japan). The various systems have been integrated with an e-commerce platform.[44] Similarly, an organization striving to be a low-cost provider is competitively stronger if it has an unrivalled benchmarking system that identifies opportunities to implement best practices and drive costs out of the business. Fast-growing organizations get an important lift from having capabilities in place to recruit and train new employees in large numbers and from investing in infrastructure that gives them the capability to handle rapid growth as it occurs. It is nearly always better to put infrastructure and support systems in place before they are actually needed than to have to scramble to catch up to customer demand.

Control Systems

Accurate and timely information about daily operations is essential if managers are to gauge how well the strategy execution process is proceeding. Information systems need to cover five broad areas: (1) customer data; (2) operations data; (3) employee data; (4) supplier/partner/collaborative ally data; and (5) financial performance data. All key strategic performance indicators must be tracked and reported in real time where possible. Long the norm, monthly profit-and-loss statements and monthly statistical summaries are fast being replaced with daily statistical updates and even up-to-the-minute performance monitoring, made possible by online technology. Most retail organizations have automated online systems that generate daily sales reports for each store and maintain up-to-the-minute inventory and sales records on each item. Manufacturing plants typically generate daily production reports and track labour productivity on every shift. Many retailers and manufacturers have online data systems connecting them with their suppliers that monitor the status of inventories, track shipments and deliveries, and measure defect rates.

Having state-of-the-art operating systems, information systems and real-time data is another way organizations can facilitate superior strategy execution and operating excellence.

Real-time information systems permit organization managers to stay on top of implementation initiatives and daily operations and to intervene if things seem to be drifting off course. Tracking key performance indicators, gathering information from operating personnel, quickly identifying and diagnosing problems, and taking corrective actions are all integral pieces of the process of managing strategy implementation and exercising adequate control over operations. A number of organizations have recently begun creating 'electronic scorecards' for senior managers that gather daily or weekly statistics from different databases about inventory, sales, costs and sales trends; such information enables these managers to easily stay abreast of what is happening and make better on-the-spot decisions.[45] Telephone organizations have elaborate information systems to measure signal quality, connection times, interrupts, wrong connections, billing errors and other measures of reliability that affect customer service and satisfaction. British Petroleum (BP) has fitted out rail wagons carrying hazardous materials with sensors and global-positioning systems (GPS) so that it can track the status, location and other information about these shipments via satellite and relay the data to its corporate intranet. Organizations that rely on empowered customer-contact personnel to act promptly and creatively in pleasing customers have installed online information systems that make essential customer data accessible to such personnel through a few keystrokes; this enables them to respond more effectively to customer enquiries and deliver personalized customer service.

Statistical information gives managers a feel for the numbers; briefings and meetings provide a feel for the latest developments and emerging issues; and personal contacts add a feel for the people dimension. All are good barometers. Managers must identify problem areas and deviations from plans before they can take action to get the organization back on course, by either improving the approaches to strategy execution or fine-tuning the strategy. Jeff Bezos, Amazon's CEO, is an ardent proponent of managing by the numbers. As he puts it, 'Math based decisions always trump opinion and judgment. The trouble with most corporations is that they make judgment-based decisions when data-based decisions could be made.'[46]

Monitoring Employee Performance

Information systems also provide managers with a means for monitoring the performance of empowered workers to see that they are acting within the specified limits.[47] Leaving empowered employees to their own devices in meeting performance standards without appropriate checks and balances can expose an organization to excessive risk.[48]

Scrutinizing daily and weekly operating statistics is one of the important ways in which managers can monitor the results that flow from the actions of empowered subordinates without resorting to constant over-the-shoulder supervision; if the operating results flowing from the actions of empowered employees look good, then it is reasonable to assume that empowerment is working. But close monitoring of operating performance is only one of the control tools at management's disposal. Another valuable lever of control in organizations that rely on empowered employees, especially in those that use self-managed workgroups or other such teams, is peer-based control. Because peer evaluation is such a powerful control device, organizations structured into teams can remove some layers of the management hierarchy and rely on strong peer pressure to keep team members operating between the white lines. This is especially true when an organization has the information systems capability to monitor team performance daily or in real time.

Balanced Scorecards and Dashboards

As we saw in Chapter 1, performance measures need to go beyond the financial data the organization generates. Kaplan and Norton likened using only financial measures to trying to fly a plane using only the airspeed indicator.[49] In order to ensure that employees implement the organization's strategy effectively it is important to have measures that relate to the work they do and that they understand. Many organizations now use real-time data and have developed dashboards showing a range of strategic measures – often in the form of key performance indicators

(KPIs) – focusing on those aspects of the business that are critical to success. Kaplan and Norton suggested that an effective scorecard should consider four perspectives:[50]

1. Financial measures, such as those covered in Chapter 4, from ROCE to untilization of assets, depending on what the business views as critical to its success
2. Internal measures – often focused around productivity and quality
3. Customer measures – from market share to customer satisfaction – again dependent on what the business needs to focus on to succeed
4. Learning and growth measures – such as the rate at which new products or services are developed, and the numbers that are brought to market effectively.

In recent years, others have brought further perspectives to the fore. Parmenter added Employee Satisfaction and Environment & Community measures to a six-perspective scorecard.[51] Individual companies have also adapted this basic framework to include supplier perspectives and other measures they have considered critical to implementing their strategy effectively.

A Different View - Dynamic Control Systems

Harvard Professor Robert Simons identified four types of control system he described as 'levers'.[52] Use of these four levers in combination, he argued, helps to retain flexibility as well as giving managers control, especially in organizations operating in dynamic or high-velocity environments. The levers are all linked to the organization's business strategy and cover the following:

1. *Diagnostic control systems:* these are the systems that measure key outputs and allow managers to track progress against strategically significant goals. The systems allow managers to make adjustments based on periodic feedback, and realign processes and inputs to ensure that future outputs meet the desired goals.
2. *Belief systems:* these are the business's core values. They need to be broad enough to appeal to the different groups in the organization, from sales and marketing to production and clerical personnel. Senior managers use belief systems to orient employees and promote commitment to the organization's vision. They can encapsulate the ways of working employees are expected to embrace – 'respect for the individual', 'pursuit of excellence', and so on.
3. *Boundary systems:* these show employees what the limits of acceptable activity are. Using standard operating procedures and rules to state what staff are allowed to do can stifle creativity, defining what employees should not do promotes innovation, although there are still limits managers set by stating the acceptable scope of activities. Boundary systems are often stated as minimum standards or in codes of ethical conduct. They act as the 'organization's brakes'.
4. *Interactive control systems:* these are important to help organizations deal with strategic uncertainties. In large organizations these are often formal systems that help managers to pick up on emerging information. They support the development of new strategies by allowing managers to sense and respond to threats and opportunities in the organization's environment. These systems are distinct from diagnostic control in that they relate to changing factors such as trends in consumer behaviour, changes to government regulation, new technologies and the moves of existing and potential competitors.

Using all the levers in combination allows managers to unleash the creative talents of their workforce without losing ultimate control of the operational activities that are critical to the execution of the organization's strategy.

Reward Systems

In order to focus staff on performance targets that are critical to the successful execution of a strategy, organization managers typically use an assortment of motivational techniques and rewards to enlist organization-wide commitment to the strategic plan. A properly designed reward system can be a powerful tool for mobilizing organizational commitment to successful strategy execution. But incentives and rewards do more than just strengthen the resolve of an organization's personnel to succeed – they also focus their attention on the accomplishment of specific strategy execution objectives. Not only do they spur the efforts of individuals to achieve

those aims, but they can also help to co-ordinate the activities of individuals throughout the organization by aligning their personal motives with the goals of the organization. In this manner, reward systems serve as an indirect type of control mechanism that conserves on the more costly control mechanism of supervisory oversight.

To win employees' sustained, energetic commitment to the strategy execution process, management must be resourceful in designing and using motivational incentives – both monetary and non-monetary. The more a manager understands what motivates his or her team, and the more he or she relies on motivational incentives as a tool for achieving the targeted strategic and financial results, the greater will be employees' commitment to good day-in, day-out strategy execution and achievement of performance targets.[53]

Incentives and Motivational Practices that Facilitate Good Strategy Execution

Financial incentives are still an important motivating tool for gaining employee commitment to good strategy execution and focusing attention on strategic priorities. They can provide **high-powered incentives** for some individuals to increase their efforts when rewards are tied to specific outcome objectives. An organization's package of monetary rewards typically includes some combination of base-pay increases, performance bonuses, profit-sharing plans, stock awards, organization contributions to employee pensions and piecework incentives (in the case of production workers). But most successful organizations and managers also make extensive use of non-monetary incentives. Some of the most important non-monetary approaches organizations can use to enhance motivation are listed below:[54]

Core Concept

Financial rewards can provide **high-powered incentives** when rewards are tied to specific outcome objectives.

- *Provide attractive perks and fringe benefits.* The various options include full coverage of health insurance premiums, college tuition reimbursement, generous paid leave allowances, on-site childcare, on-site fitness centres, holiday opportunities at organization-owned recreational facilities, personal concierge services, subsidized cafeterias and free lunches, casual dress every day, personal travel services, paid sabbaticals, maternity and paternity leaves, paid leave to care for family members who are ill, telecommuting, compressed work weeks (four 10-hour days instead of five 8-hour days), flexitime (variable work schedules that accommodate individual needs), college scholarships for children, and relocation services.
- *Give awards and other forms of public recognition to high performers, and celebrate the achievement of organizational goals.* Many organizations hold award ceremonies to honour top-performing individuals, teams and organizational units, and to showcase organization successes. This can help create healthy competition among units and teams within the organization, but it can also create a positive *esprit de corps* within the organization as a whole. Other examples include special recognition at informal organization gatherings or in the organization newsletter, tangible tokens of appreciation for jobs well done, and frequent words of praise.
- *Rely on promotion from within whenever possible.* The practice of promoting from within helps bind workers to their employer, and employers to their workers, providing strong incentives for good performance. Moreover, promoting from within helps ensure that people in positions of responsibility have knowledge specific to the business, technology and operations they are managing.
- *Invite and act on ideas and suggestions from employees.* Many organizations find that their best ideas for nuts-and-bolts operating improvements come from the suggestions of employees. Moreover, research indicates that the moves of many organizations to push decision-making down the line and empower employees increases employees' motivation and satisfaction as well as their productivity. The use of self-managed teams has much the same effect.
- *Create a work atmosphere in which there is genuine caring and mutual respect among workers, and between management and employees.* A 'family' work environment, where people are on a first-name basis and there is strong camaraderie, promotes teamwork and cross-unit collaboration.

- *State the strategic vision in inspirational terms so that employees feel they are a part of something very worthwhile in a larger social sense.* There is a strong motivating power associated with giving people a chance to be part of something exciting and personally satisfying. Jobs with noble purpose tend to inspire employees to give their all. As described in Chapter 9, this not only increases productivity but reduces turnover and lowers costs for staff recruitment and training as well.

Video
Mark Zuckerberg, CEO and co-founder of Facebook: *'The Future of Social'*

- *Share information with employees about financial performance, strategy, operational measures, market conditions and competitors' actions.* Broad disclosure and prompt communication send the message that managers trust their workers and regard them as valued partners in the enterprise. Keeping employees in the dark denies them information useful to performing their jobs, prevents them from being intellectually engaged, saps their motivation and detracts from performance.
- *Maintain attractive office space and facilities.* A workplace environment that is attractive and comfortable usually has decidedly positive effects on employee morale and productivity. An appealing work environment is particularly important when workers are expected to spend long hours at work.

For specific examples of the motivational tactics employed by several prominent organizations (many of which appear on the list of the 100 best organizations to work for in Europe), see Illustration Capsule 10.2.

Illustration Capsule 10.2

WHAT ORGANIZATIONS DO TO MOTIVATE AND REWARD EMPLOYEES

Organizations have come up with an impressive variety of motivational and reward practices to help create a work environment that energizes employees and promotes better strategy execution. Here is a sample of what organizations are doing:

- London and Quadrant Housing Trust is one of the largest providers of social housing in London. The housing association employs 1,100 people and manages more than 67,000 homes. In 2008 the organization developed a Leadership Academy for its managers, which runs a three-day residential programme to develop their leadership skills to foster collaborative working. All staff participate in a bonus scheme that is linked to resident satisfaction and can be up to 5 per cent of salary.
- Baringa Partners, a management consultancy specializing in energy and utilities markets, starts its motivational tactics while it is still recruiting staff. New members of staff are sent a bottle of champagne and, at their first organization meeting, presented with a branded T-shirt as a sign they have joined the team. New members of staff are assigned a 'buddy' who acts as a mentor. The organization has a quarterly award of £500 for exceptional contributions by any individual employee, as well as Star Player and Team of the Year, Cheerleader and One to Watch awards. Other rewards include dinners and weekend breaks for teams that hit significant milestones.
- Centor Insurance is a financial services organization, based in London, which employs just 38 people but has an employee retention rate of 94 per cent and several staff in line for their 20-year long-service award, which is remarkable in an industry where staff tend to change jobs every three or four years. The organization operates a 'War Stories' scheme so that staff who have performed well or overcome particular problems are encouraged to pass on their learning and gain the respect of their colleagues. The organization also has very flexible working practices and is committed to helping its staff achieve a good work–life balance. Jobs have been redesigned to suit part-time hours, and home working is facilitated through dedicated technical support.
- At W.L. Gore (the maker of GORE-TEX), which employs more than 1,000 people in its European operations, employees get to choose what project/team they work on, and each team member's compensation is based on other team members' rankings of his or her contribution to the enterprise.
- Jewellery retailer Beaverbrook's motivates its employees by building a high level of trust through listening and acting on their suggestions. Although the organization runs 66 retail outlets in the UK, the managing

director and other senior managers try to do most of their communication with staff face to face by visiting the stores and holding focus groups. This access to the top team extends to Beaverbrook's suggestion scheme. A member of the executive team responds personally to every request made.

- Lansons Communications is one of the top independent PR agencies in the UK. The organization offers a mix of hard and soft benefits to its employees including a share ownership scheme, pensions, a savings scheme and a bonus scheme that is funded with a third share of the annual profits. Lansons also provides subsidized massages, manicures and pedicures as well as buying gifts for children's birthdays and giving staff time off for school plays.

Sources: www.greatplacetowork.co.uk and organization websites (accessed March 2012).

Striking the Right Balance Between Rewards and Punishment

Decisions on salary increases, incentive compensation, promotions, key assignments, and the ways and means of awarding praise and recognition are potent attention-getting, commitment-generating devices. Such decisions seldom escape the closest employee scrutiny, thus saying more about what is expected and who is considered to be doing a good job than virtually any other factor. While most approaches to motivation, compensation and people management accentuate the positive, organizations also combine positive rewards with the risk of punishment. A number of organizations deliberately give employees heavy workloads and tight deadlines – personnel are pushed hard to achieve 'stretch' objectives and are expected to put in long hours (nights and weekends if need be). At most organizations, senior executives and key personnel in underperforming units are pressured to raise performance to acceptable levels and keep it there or risk being replaced.

Some organizations feel it is unwise to take off the pressure for good individual and group performance or play down the adverse consequences of shortfalls in performance. High-performing organizations often have a cadre of ambitious people who relish the opportunity to climb the ladder of success, love a challenge, thrive in a performance-oriented environment, and find some competition and pressure useful to satisfy their own drives for personal recognition, accomplishment and self-satisfaction. However, there is also research which shows that other employees may be more motivated by intrinsic factors.

Also, if an organization's motivational approaches and reward structure induce too much stress, internal competitiveness, job insecurity and fear of unpleasant consequences, the impact on workforce morale and strategy execution can be counterproductive. Evidence shows that managerial initiatives to improve strategy execution should incorporate more positive than negative motivational elements because when co-operation is positively enlisted and rewarded, rather than coerced by orders and threats (implicit or explicit), people tend to respond with more enthusiasm, dedication, creativity and initiative.[55]

Linking Rewards to Strategically Relevant Performance Outcomes

To create a strategy-supportive system of rewards and incentives, organizations usually reward people for accomplishing results, not for just dutifully performing assigned tasks. To make the work environment results-oriented, managers will focus job holders' attention and energy on what to *achieve* as opposed to what to *do*. It is flawed management to tie incentives and rewards to satisfactory performance of duties and activities instead of desired business outcomes and organization achievements.[56] In any job, performing assigned tasks is not equivalent to achieving intended outcomes. Diligently showing up for work and attending to one's job assignment does not, by itself, guarantee results.

> The key to creating a reward system that promotes good strategy execution is to make measures of good business performance and good strategy execution the *dominating basis* for designing incentives, evaluating individual and group efforts and handing out rewards.

Ideally, performance targets should be set for every organizational unit, every manager, every team or workgroup and perhaps every employee – targets that measure whether strategy execution is progressing satisfactorily. If the organization's strategy is to be a low-cost provider, the incentive system must reward actions and achievements that result in lower costs. If the

organization has a differentiation strategy based on superior quality and service, the incentive system must reward such outcomes as Six Sigma defect rates, infrequent need for product repair, low numbers of customer complaints, speedy order processing and delivery, and high levels of customer satisfaction. If an organization's growth is predicated on a strategy of new product innovation, incentives should be tied to factors such as the percentages of revenues and profits coming from newly introduced products.

Incentive compensation for top executives is typically tied to such financial measures as revenue and earnings growth, stock price performance, return on investment and creditworthiness, or to strategic measures such as market share growth. However, incentives for department heads, teams and individual workers may be tied to performance outcomes more closely related to their strategic area of responsibility. In manufacturing, incentive compensation may be tied to unit manufacturing costs, on-time production and shipping, defect rates, the number and extent of work stoppages due to equipment breakdowns, and so on. In sales and marketing, there may be incentives for achieving sales or unit volume targets, market share, sales penetration of each target customer group, the fate of newly introduced products, the frequency of customer complaints, the number of new accounts acquired, and customer satisfaction. Which performance measures to base incentive compensation on depends on the situation – the priority placed on various financial and strategic objectives, the requirements for strategic and competitive success and what specific results are needed in different facets of the business to keep strategy execution on track.

Once an organization's incentive plan is designed, it is then communicated and explained. Everybody needs to understand how his or her incentive compensation is calculated and how individual/group performance targets contribute to organizational performance targets. The pressure to continuously improve strategy execution and achieve performance objectives should be unrelenting, with no loopholes for rewarding shortfalls in performance. Organizations relying on this approach need to ensure that people at all levels are held accountable for carrying out their assigned parts of the strategic plan, and they must understand that their rewards are based on the calibre of results achieved. But with the pressure to perform should come meaningful rewards that will effectively motivate the workforce.

LO 10.4
Evaluate the role of processes, policies and procedures in enabling superior strategy execution.

Organizational Processes, Policies and Procedures that Facilitate Strategy Execution

While systems are all about interactions and the creation of outcomes, processes are the basic building blocks of a system and are about activities and outputs. A system is normally the product of the interactions between several processes, so managers need to master a range of processes in order to execute strategy effectively.[57] Some of the key processes in building and sustaining competitive advantage concern the allocation of existing resources, and developing new resources and capabilities in response to changes in the environment.

Allocating Resources to the Strategy Execution Effort

Early in the process of implementing a new strategy, managers need to determine what resources (in terms of funding, people, etc.) will be required for good strategy execution and how they should be distributed across the various organizational units involved. An organization's ability to marshal the resources needed to support new strategic initiatives has a major impact on the strategy execution process. Too little funding slows progress and impedes the efforts of organizational units to execute their pieces of the strategic plan proficiently. Too much funding wastes organizational resources and reduces financial performance. Both outcomes argue for managers to be deeply involved in reviewing budget proposals and directing the proper amounts of resources to strategy-critical organizational units. This includes carefully screening requests for more people and new facilities and equipment, approving those that hold promise for making a

contribution to strategy execution and turning down those that do not. Should internal cash flows prove insufficient to fund the planned strategic initiatives, then management must raise additional funds through borrowing or selling additional shares of stock to willing investors.

A change in strategy nearly always calls for budget reallocations and resource shifting. Previously important units having a lesser role in the new strategy may need downsizing. Units that now have a bigger strategic role may need more people, new equipment, additional facilities and above-average increases in their operating budgets. Implementing a new strategy requires managers to take an active and sometimes forceful role in shifting resources, downsizing some functions and upsizing others, not only to amply fund activities with a critical role in the new strategy but also to avoid inefficiency and achieve profit projections. When the National Trust launched its Go Local strategy in 2009/10, regional and central services were cut in order to shift emphasis and resources to the local groups and managers. Implementing a new strategy also requires putting enough resources behind new strategic initiatives to fuel their success and making the tough decisions to kill projects and activities that are no longer justified. Honda's strong support of research and development (R&D) activities allowed it to develop the first motorcycle airbag, the first low-polluting four-stroke outboard marine engine, a wide range of ultra-low-emission cars, the first hybrid car (Honda Insight) in the US market and the first hydrogen fuel cell car (Honda Clarity). However, Honda managers had no trouble stopping production of the Honda Insight in 2006 when its sales failed to take off, and then shifting resources to the development and manufacture of other promising hybrid models, including a totally redesigned Insight that was launched in Europe in 2009.

The funding requirements of good strategy execution must drive how capital allocations are made and the size of each unit's operating budget. Underfunding organizational units and activities pivotal to the strategy impedes successful strategy implementation.

Visible actions to reallocate operating funds and move people into new organizational units signal a determined commitment to strategic change and frequently are needed to catalyse the implementation process and give it credibility. Microsoft has made a practice of regularly shifting hundreds of programmers to new high-priority programming initiatives within a matter of weeks or even days. Fast-moving developments in many markets are prompting organizations to abandon traditional annual or semi-annual budgeting and resource allocation cycles in favour of resource allocation processes supportive of more rapid adjustments in strategy.

An organization's operating budget should be both *strategy-driven* (in order to amply fund the performance of key value chain activities) and *lean* (in order to operate as cost-efficiently as possible).

The bigger the change in strategy (or the more obstacles that lie in the path of good strategy execution), the bigger the resource shifts that are likely to be required. Merely fine-tuning the execution of an organization's existing strategy seldom requires big movements of people and money from one area to another. The desired improvements can usually be accomplished through above-average budget increases to organizational units launching new initiatives and below-average increases (or even small budget cuts) for the remaining organizational units. However, there are times when strategy changes or new execution initiatives need to be made without adding to total organization expenses. In such circumstances, managers have to work their way through the existing budget line by line and activity by activity, looking for ways to trim costs and shift resources to higher-priority activities where new execution initiatives are needed. In the event that an organization needs to make significant cost cuts during the course of launching new strategic initiatives, managers have to be especially creative in finding ways to do more with less and execute the strategy more efficiently. Indeed, it is not unusual for strategy changes and the drive for good strategy execution to be conducted in a manner that entails achieving considerably higher levels of operating efficiency and, at the same time, making sure key activities are performed as effectively as possible.

Building and Strengthening Core Competences and Competitive Capabilities

High among the organization-building priorities in the strategy execution process is the need to build and strengthen competitively valuable core competences and capabilities. As explained in

Chapter 4, a company's ability to perform the value-creating activities that express its strategy derives from its resources and capabilities. In the course of crafting strategy, managers identify the resources and capabilities that will enable the firm's strategy. In executing the strategy, managers deploy those resources and capabilities in the form of value-creating activities. But the first step is to ensure that the necessary resources and capabilities are in place and that they are renewed, upgraded or augmented, as needed.

If the strategy being implemented is new, company managers may have to acquire new resources, significantly broaden or deepen certain capabilities or even add entirely new competences in order to put the strategic initiatives in place and execute them proficiently. But even if the strategy has not changed materially, good strategy execution involves refreshing and strengthening the firm's resources and capabilities to keep them on top form. Moreover, it involves augmenting and modifying them to keep pace with evolving market needs and competitive conditions.

Building new competences and capabilities is a multi-stage process that occurs over a period of months and years. It is not something that is accomplished overnight.

Three Approaches to Building and Strengthening Capabilities

Building core competences and competitive capabilities is a time-consuming, managerially challenging exercise. While some assistance can be had from discovering how best-in-industry or best-in-world companies perform a particular activity, trying to replicate and then improve on the competences and capabilities of others is, however, much easier said than done.

With deliberate effort, well-orchestrated organizational actions and continued practice, however, it is possible for a firm to become proficient at capability-building despite the difficulty. Indeed, by making capability-building activities a routine part of their strategy execution endeavours, some firms are able to develop *dynamic capabilities* that assist them in managing resource and capability change, as discussed in Chapter 4. We saw that certain environmental conditions required different types of dynamic capabilities – Figure 10.9 illustrates why managers need to take into account the level of Disorder and Dynamism in their organization's environment when developing new and existing capabilities.

The most common approaches to capability-building include (1) internal development, (2) acquiring capabilities through mergers and acquisitions, and (3) accessing capabilities via collaborative partnerships.[58]

Capabilities develop incrementally along an evolutionary development path as organizations search for solutions to their problems. The process is a complex one, since capabilities are the product of bundles of skills and know-how that are integrated into organizational routines and deployed within activity systems through the combined efforts of teams and workgroups that are often cross-functional in nature, spanning a variety of departments and locations. For instance, the capability of speeding new products to market involves the collaborative efforts of personnel in R&D, engineering and design, purchasing, production, marketing and distribution. Similarly, the capability to provide superior customer service is a team effort among people in customer call centres (where orders are taken and enquiries are answered), shipping and delivery, billing and accounts receivable, and after-sales support. The process of building a capability begins when managers set an objective of developing a particular capability and organize activity around that objective.[59] Managers can ignite the process by having high aspirations and setting 'stretch goals' for the organization.[60]

A company's capabilities must be continually refreshed and renewed to remain aligned with changing customer expectations, altered competitive conditions and new strategic initiatives.

Because the process is incremental, the first step is to develop the *ability* to do something, however imperfectly or inefficiently. This entails selecting people with the requisite skills and experience, upgrading or expanding individual abilities as needed, and then moulding the efforts of individuals into a collaborative effort to create an organizational ability. At this stage, progress can be fitful since it depends on experimentation, active search for alternative solutions, and learning through trial and error.[61]

As experience grows and company personnel learn how to perform the activities consistently well and at an acceptable cost, the ability evolves into a

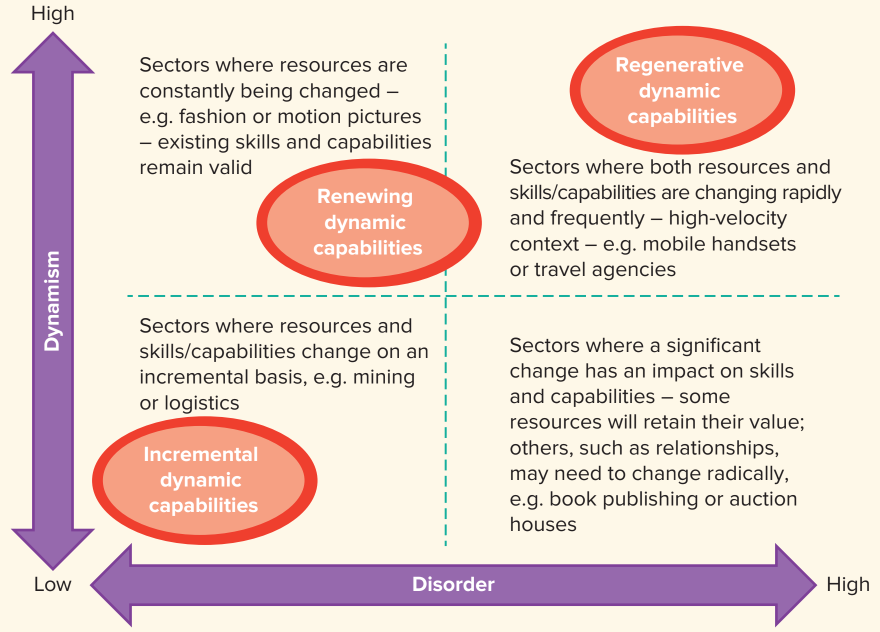

FIGURE 10.9 Dynamic capabilities in context

Adapted from Ambrosini, V., Bowman, C. and Collier, N. (2009) 'Dynamic capabilities: an exploration of how firms renew their resource base', *British Journal of Management,* 20: S9–S24; McGahan, A. (2004) 'How industries change', *Harvard Business Review,* October, pp. 86–94.

tried-and-true competence or capability. Getting to this point requires a continual investment of resources and systematic efforts to improve processes and solve problems creatively as they arise. Improvements in the functioning of a capability come from task repetition and the resulting learning by doing of individuals and teams.[62] But the process can be accelerated by making learning a more deliberate endeavour and providing the incentives that will motivate company personnel to achieve the desired ends.[63] This can be critical to successful strategy execution when market conditions are changing rapidly. Here the dynamic capabilities can be classed as *incremental* or *renewing*, but also *regenerative*.[64] This last type of capability is one that changes the nature of other dynamic capabilities in the organization and can be particularly important in the types of hyper-competitive environments discussed in Chapters 1 and 3. By helping an organization to refresh its resources and competences, regenerative dynamic capabilities are able to help it break away from a strategic path that is no longer helping it to perform well in a changed environment. For example, if an organization has developed strong capabilities in R&D, with substantial investments in facilities, scientists and engineers, these may aid the creation of new products and also other useful resources and competences. The experimentation and creative skills might also be leveraged into other parts of the business and help to renew the resource base. However, in a changing environment, where customers want an increased role in product creation, there might be a significant advantage for this organization to develop dynamic capabilities in managing open innovation (see Key Debate 6.1 in Chapter 6 for more on this topic). This would change the resource base of the organization, but also the nature of the dynamic capabilities, because incorporating customers into the new product development process would fundamentally change the way the organization operated. Instead of just being good at leveraging ideas between strategic business units (SBUs), the organization would need to excel at co-ordinating external relationships.

It is generally much easier and less time-consuming to update and remodel a company's existing capabilities as external conditions and company strategy change than it is to create them from scratch. Maintaining capabilities in top form may simply require exercising them continually and fine-tuning them as necessary. Refreshing and updating capabilities requires

only a limited set of modifications to a set of routines that is otherwise in place. Phasing out an existing capability takes significantly less effort than adding a brand-new one. Replicating a company capability, while not an easy process, still begins with an established template.[65] Even the process of augmenting a capability may require less effort if it involves the recombination of well-established company capabilities and draws on existing company resources.[66] Companies like Cray in large computers and Honda in gasoline engines, for example, have leveraged the expertise of their talent pool by frequently re-forming high-intensity teams and reusing key people on special projects designed to augment their capabilities. Canon combined miniaturization capabilities that it developed in producing calculators with its existing capabilities in precision optics to revolutionize the 35 mm camera market.[67] Toyota, en route to overtaking General Motors as the global leader in motor vehicles, has aggressively upgraded its capabilities in fuel-efficient hybrid engine technology and constantly fine-tuned its famed Toyota Production System to enhance its already proficient capabilities in manufacturing top-quality vehicles at relatively low costs – see Illustration Capsule 10.3.

Illustration Capsule 10.3

TOYOTA'S LEGENDARY PRODUCTION SYSTEM: A CAPABILITY THAT TRANSLATES INTO COMPETITIVE ADVANTAGE

The heart of Toyota's strategy in motor vehicles is to outcompete rivals by manufacturing world-class, quality vehicles at lower costs and selling them at competitive price levels. Executing this strategy requires top-notch manufacturing capability and super-efficient management of people, equipment and materials. Toyota began conscious efforts to improve its manufacturing competence more than 50 years ago. Through tireless trial and error, the company gradually took what started as a loose collection of techniques and practices and integrated them into a fully fledged process that has come to be known as the Toyota Production System (TPS). The TPS drives all plant operations and the company's supply chain management practices. TPS is grounded in the following principles, practices and techniques:

- *Use just-in-time delivery of parts and components to the point of vehicle assembly.* The idea here is to cut out all the bits and pieces of transferring materials from place to place and to discontinue all activities on the part of workers that don't add value (particularly activities where nothing ends up being made or assembled).
- *Develop people who can come up with unique ideas for production improvements.* Toyota encourages employees at all levels to question existing ways of doing things – even if this means challenging a boss on the soundness of a directive. Former Toyota president Katsuaki Watanabe encouraged the company's employees to 'pick a friendly fight'. Also, Toyota doesn't fire its employees who, at first, have little judgement for improving work flows; instead, the company gives them extensive training to become better problem-solvers.
- *Emphasize continuous improvement.* Workers are expected to use their heads and develop better ways of doing things, rather than mechanically follow instructions. Toyota managers tout messages such as 'Never be satisfied' and 'There's got to be a better way.' Another mantra at Toyota is that the *T* in TPS also stands for 'Thinking'. The thesis is that a work environment where people have to think generates the wisdom to spot opportunities for making tasks simpler and easier to perform, increasing the speed and efficiency with which activities are performed, and constantly improving product quality.
- *Empower workers to stop the assembly line when there's a problem or a defect is spotted.* Toyota views worker efforts to purge defects and sort out the problem immediately as critical to the whole concept of building quality into the production process. According to TPS, 'If the line doesn't stop, useless defective items will move on to the next stage. If you don't know where the problem occurred, you can't do anything to fix it.'
- *Deal with defects only when they occur.* TPS philosophy holds that when things are running smoothly they should not be subject to control; if attention is directed to fixing problems that are found, quality control along the assembly line can be handled with fewer personnel.
- *Ask yourself 'Why?' five times.* While errors need to be fixed whenever they occur, the value of asking 'Why?' five times enables identification of the root cause of the error and correcting it so that the error won't recur.

- *Organize all jobs around human motion to create a production/assembly system with no wasted effort.* Work organized in this fashion is called 'standardized work' and people are trained to observe standardized work procedures (which include supplying parts to each process on the assembly line at the proper time, sequencing the work in an optimal manner, and allowing workers to do their jobs continuously in a set sequence of sub-processes).
- *Find where a part is made cheaply, and use that price as a benchmark.*

The TPS utilizes a unique vocabulary of terms (such as *kanban, takt-time, jikoda, kaizen, heijunka, monozukuri, poka yoke* and *muda*) that facilitates precise discussion of specific TPS elements. In 2003, Toyota established its Global Production Centre to efficiently train large numbers of shop-floor experts in the latest TPS methods and better operate an increasing number of production sites worldwide. Since then, additional upgrades and refinements have been introduced, some in response to the large number of defects in Toyota vehicles that surfaced in 2009–10.

There is widespread agreement that Toyota's ongoing effort to refine and improve on its renowned TPS gives it important manufacturing capabilities that are the envy of other motor vehicle manufacturers. Not only have such auto manufacturers as Ford, Daimler, Volkswagen and General Motors attempted to emulate key elements of the TPS, but elements of Toyota's production philosophy have been adopted by hospitals and postal services.

However, Toyota's systems are not without their critics and one former employee, Darius Mehri, has claimed that many of the productivity improvements have been made at the expense of the health and safety of employees, and are actually underpinned by social control and a bullying culture.

Sources: Information posted at www.toyotageorgetown.com; Hirotaka, T., Osono, E. and Shimizu, N. (2008) 'The contradictions that drive Toyota's success', *Harvard Business Review,* 86(6): 96–104; Ohno, T. (1988) *Toyota Production System: Beyond Large-scale Production,* New York, Sheridan; Mehri, D. (2006) 'The darker side of lean: an insider's perspective on the realities of the Toyota Production System', *Academy of Management Perspective,* May, pp. 21–42.

Managerial actions to develop core competences and competitive capabilities generally take one of two forms: either strengthening the company's base of skills, knowledge and intellect, or co-ordinating and integrating the efforts of the various workgroups and departments. Actions of the first sort can be undertaken at all managerial levels, but actions of the second sort are best orchestrated by senior managers who not only appreciate the strategy-executing significance of strong capabilities but also have the clout to enforce the necessary co-operation and co-ordination among individuals, groups, departments and external allies.[68]

Acquiring Capabilities through Mergers and Acquisitions

Sometimes a company can refresh and strengthen its competences by acquiring another company with attractive resources and capabilities.[69] An acquisition aimed at building a stronger portfolio of competences and capabilities can be every bit as valuable as an acquisition aimed at adding new products or services to the company's line-up of offerings. The advantage of this mode of acquiring new capabilities is primarily one of speed, since developing new capabilities internally can take many years of effort. Capabilities-motivated acquisitions are essential

(1) when a market opportunity can slip by faster than a needed capability can be created internally, and (2) when industry conditions, technology or competitors are moving at such a rapid speed that time is of the essence.

At the same time, acquiring capabilities in this way is not without difficulty. Capabilities involve tacit knowledge and complex routines that cannot be transferred readily from one organizational unit to another. This may limit the extent to which the new capability can be utilized. French advertising firm, the Publicis Groupe, has had to become highly skilled in ensuring that its horizontal acquisitions bring their full value to the parent organization. Talent in global advertising is highly mobile, and account directors and creatives can often take major clients with them if they decide to leave post-merger. Publicis CEO Maurice Lévy went to great lengths in 2000 to ensure the group's acquisition of Saatchi & Saatchi kept the talent and knowledge the British firm had built up over many years. The Publicis Groupe was restructured to give the UK firm equal billing with Publicis Worldwide, the French firm's original advertising agency arm and Saatchi executives were invited to lead post-acquisition integration talks.[70] Integrating the capabilities of two firms involved in a merger or acquisition may pose an additional challenge, particularly if there are underlying incompatibilities in their supporting systems or processes. Moreover, since internal fit is important, there is always the risk that under new management the acquired capabilities may not be as productive as they had been. In a worst case scenario, the acquisition process may end up damaging or destroying the very capabilities that were the object of the acquisition in the first place.

Accessing Capabilities through Collaborative Partnerships

Another method of acquiring capabilities from an external source is to access them via collaborative partnerships with suppliers, competitors or other companies having the cutting-edge expertise. There are three basic ways to pursue this course of action:

1. *Outsource the function requiring the capabilities to a key supplier or another provider.* Whether this is a wise move depends on what can be safely delegated to outside suppliers or allies versus what internal capabilities are key to the company's long-term success. As discussed in Chapter 6, outsourcing has the advantage of conserving resources so that the firm can focus its energies on those activities most central to its strategy. It may be a good choice for firms that are too small and resource-constrained to execute all the parts of their strategy internally.
2. *Collaborate with a firm that has complementary resources and capabilities in a joint venture, strategic alliance or other type of partnership established for the purpose of achieving a shared strategic objective.* This requires launching initiatives to identify the most attractive potential partners and to establish collaborative working relationships. Since the success of the venture will depend on how well the partners work together, potential partners should be selected as much for their management style, culture and goals as for their resources and capabilities. As we saw in the closing case of Chapter 6, UK telecoms company Vodafone collaborated with Kenyan mobile network Safaricom to pilot its mobile money service, M-Pesa. Vodafone had the technological expertise, but Safaricom had the network of agents and the knowledge of the local Kenyan market.
3. *Engage in a collaborative partnership for the purpose of learning how the partner does things, internalizing its methods and thereby acquiring its capabilities.* Since this method involves an abuse of trust, it not only puts the co-operative venture at risk but also encourages the firm's partner to treat the firm similarly or refuse further dealings with the firm.

Upgrading Employee Skills and Knowledge Resources

Good strategy execution also requires that employees have the skills and knowledge resources they will need to perform their tasks well. Employee training thus plays an important role in the strategy execution process. Training and retraining are important when a company shifts to a strategy requiring different skills, competitive capabilities and operating methods. Training is also strategically important in organizational efforts to build skills-based competences. And it is a key activity in businesses where technical know-how is changing so rapidly that a company loses its ability to compete unless its employees have cutting-edge knowledge and expertise.

Successful strategy implementers see to it that the training function is both adequately funded and effective. If the chosen strategy calls for new skills, deeper technological capability, or the building and using of new capabilities, training should be placed near the top of the action agenda.

The strategic importance of training has not gone unnoticed. More than 600 companies have established internal 'universities' to lead the training effort, facilitate continuous organizational learning and help upgrade company capabilities. One of the world's leading hotel companies, Paris-based Accor, has had a corporate 'university' since 1985: the Academie Accor. This underpins much of the firm's career development for its employees and the Academie now has 17 locations worldwide to underpin Accor's diverse global workforce. Many companies conduct orientation sessions for new employees, fund an assortment of competence-building training programmes, and reimburse employees for tuition and other expenses associated with obtaining additional college education, attending professional development courses and earning professional certifications of one kind or another. A number of companies offer online, just-in-time training courses to employees around the clock. Increasingly, employees at all levels are expected to take an active role in their own professional development and assume responsibility for keeping their skills up to date and in line with the company's needs.

Strategy Execution Capabilities and Competitive Advantage

Superior strategy execution capabilities are the only source of sustainable competitive advantage when strategies are easy for rivals to copy.

As firms get better at executing their strategies, they develop capabilities in the domain of strategy execution much as they build other organizational capabilities. Superior strategy execution capabilities allow companies to get the most from their organizational resources and competitive capabilities. In this way they contribute to the success of a firm's business model. But excellence in strategy execution can also be a more direct source of competitive advantage, since more efficient and effective strategy execution can lower costs and permit firms to deliver more value to customers. Superior strategy execution capabilities may also enable a company to react more quickly to market changes, and beat other firms to the market with new products and services. This can allow a company to profit from a period of uncontested market dominance.

Because strategy execution capabilities are socially complex capabilities that develop with experience over long periods of time, they are hard to imitate. And there is no substitute for good strategy execution. (Recall the tests of resource advantage from Chapter 4.) As such, they may be as important a source of sustained competitive advantage as the capabilities that drive a firm's strategies. Indeed, they may be a far more important avenue for securing a competitive edge over rivals in situations where it is relatively easy for rivals to copy promising strategies. In such cases, the only way for firms to achieve lasting competitive advantage is to out-execute their competitors.

Instituting Policies and Procedures that Facilitate Strategy Execution

An organization's policies and procedures can either support or obstruct good strategy execution. Any time an organization moves to put new strategy elements in place or improve its strategy execution capabilities, some changes in work practices and the behaviour of organization personnel are usually required. Managers are thus well advised to examine whether existing policies and procedures support such changes, and to proactively revise or discard those that are out of line.

As shown in Figure 10.10, well-conceived policies and operating procedures facilitate strategy execution in three ways:

1. *They provide top-down guidance regarding how things need to be done.* Policies and procedures provide organization personnel with a set of guidelines for how to perform organizational activities, conduct various aspects of operations, solve problems as they arise and accomplish particular tasks. In essence, they represent a store of organizational or managerial knowledge about efficient and effective ways of doing things. They clarify uncertainty about how to proceed in executing strategy and align the actions and behaviour of organization personnel with

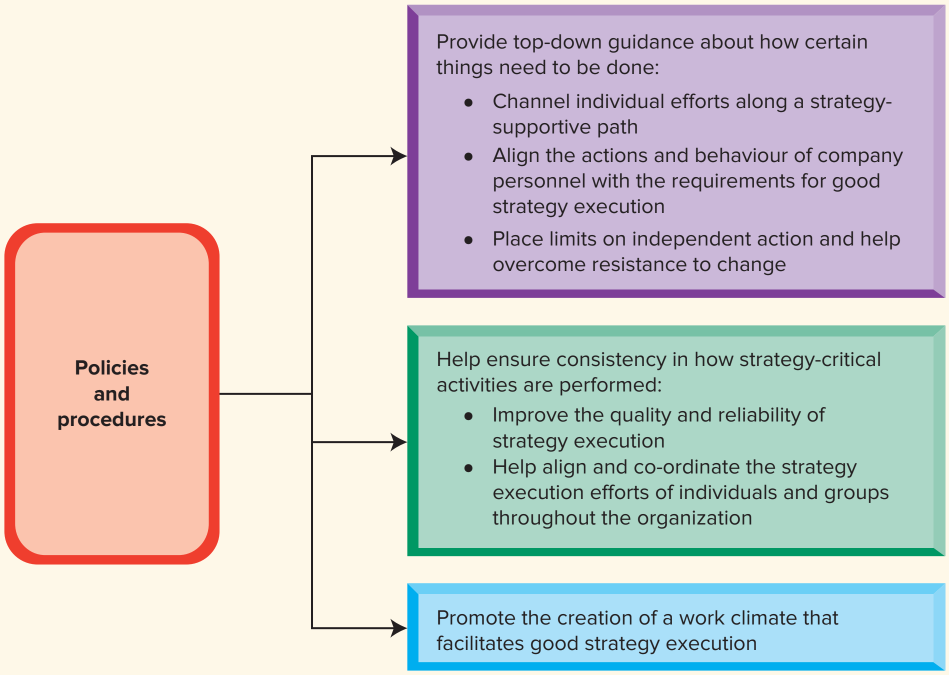

FIGURE 10.10 How policies and procedures can facilitate good strategy execution

the requirements for good strategy execution. Moreover, they place limits on ineffective independent action. When they are well matched with the requirements of the strategy implementation plan, they channel the efforts of individuals along a path that supports the plan and facilitates good strategy execution. When existing ways of doing things are misaligned with strategy execution initiatives, actions and behaviours have to be changed. Under these conditions, the managerial role is to establish and enforce new policies and operating practices that are more conducive to executing the strategy appropriately. Policies are a particularly useful way to counteract tendencies for some people to resist change. People generally refrain from violating organization policy or going against recommended practices and procedures without gaining clearance and having strong justification. As we saw in the Siemens illustration in Chapter 9, changing and enforcing the organization's ethical policies was a vital step in Peter Löscher's strategy to turn the German engineering giant around.

2. *They help ensure consistency in how execution-critical activities are performed.* For some organizations, policies and procedures serve to standardize the way that activities are performed, and encourage strict conformity to the standardized approach. This is important for ensuring the quality and reliability of the strategy execution process. It helps align and co-ordinate the strategy execution efforts of individuals and groups throughout the organization – a feature that is particularly beneficial when there are geographically scattered operating units. For example, eliminating significant differences in the operating practices of different plants, sales regions, customer service centres or the individual outlets in a chain operation helps an organization deliver consistent product quality and service to customers. Good strategy execution often entails an ability to replicate product quality and the calibre of customer service at every location where the organization does business.
3. *They promote the creation of a work climate that facilitates good strategy execution.* An organization's policies and procedures help to set the tone of an organization's work climate and contribute to a common understanding of 'how we do things around here'. Because discarding old policies and procedures in favour of new ones invariably alters the internal work climate, managers can use the policy-changing process as a powerful lever for changing the corporate culture in ways that produce a stronger fit with the new strategy.

To ensure consistency in product quality and service behaviour patterns, McDonald's policy manual spells out detailed procedures that personnel in each McDonald's unit are expected to observe. For example, 'Cooks must turn, never flip, hamburgers. If they haven't been purchased, Big Macs must be discarded in 10 minutes after being cooked and French fries in 7 minutes. Cashiers must make eye contact with and smile at every customer.' To ensure that its R&D activities are responsive to customer needs and expectations, Hewlett-Packard requires its R&D people to make regular visits to customers to learn about their problems and learn their reactions to HP's latest products.

One of the big policy-making issues concerns which activities need to be rigidly prescribed and which ought to allow room for independent action on the part of empowered personnel. Few organizations need thick policy manuals to direct the strategy execution process or prescribe exactly how daily operations are to be conducted. Too much policy can be as much of a hindrance as wrong policy and as confusing as no policy. There is wisdom in a middle approach: *prescribe enough policies to give organization members a clear direction and to place reasonable boundaries on their actions; then empower them to act within these boundaries in whatever way they think makes sense.* Allowing organization personnel to act with some degree of freedom is especially appropriate when individual creativity and initiative are more essential to good strategy execution than standardization and strict conformity. Instituting policies that facilitate strategy execution can therefore mean more policies, fewer policies or different policies. It can mean policies that require things to be done according to a strictly defined standard or policies that give employees substantial leeway to do activities in the way they think best.

Configuration/Alignment

LO 10.5
Discuss how aligning/configuring the levers managers use to execute strategy can be balanced with responding to changing contexts.

Having covered some of the key individual elements of strategy implementation in the preceding sections, we now need to look at how they fit together to create a coherent approach to executing the organization's strategy. Chandler's 1962 work on structure and strategy demonstrated that an organization's structure often developed as a result of the strategy its senior managers had chosen. However, as we have seen in previous sections, a command-and-control, top-down approach to strategy is only one of many approaches. At the end of the 1970s and into the early 1980s, research carried out by both academics and practitioners looked beyond structure to a wider range of design elements that could be aligned to support a particular strategy.

Configuration

Waterman, Peters and Phillips, three McKinsey consultants, developed a framework to help their clients configure different levers used to execute strategy.[71]

The McKinsey 7S framework covers systems, strategy and structure as the 'hard' elements of implementation, but adds skills, staff and leadership style to the mix, along with superordinate goals or the shared values of the organization. We have covered the first five elements in the previous sections of this chapter and go on to look at the last two in Chapter 11. However, the key messages for managers are that they need to look at a range of levers to execute strategy successfully, but more importantly they need to ensure those levers are connected and provide coherent support for the chosen strategy.

Academic research also covered configuration but sought to provide a way of classifying different types of configuration. Henry Mintzberg, Danny Miller and others at McGill University in Canada developed a series of archetypes for different configurations.[72] So these were essentially idealized forms and unlikely to exist in a pure form in the real world. The theory took account of both structure and power as well as considering context:

- *The Entrepreneurial organization:* similar in form to the simple structure outlined earlier in the chapter, this type of organization is most effective in dynamic environments where it can use its fast decision-making to gain advantage over slower-moving, more bureaucratic organizations.

- *The Machine organization:* these are organizations geared to producing mass-market, standardized products. Work is highly planned and scheduled with many specialized tasks. This type of organization tends to dominate stable and mature industries.
- *The Professional organization:* the work in this organization is standardized but much less centralized than in the machine organization as it is carried out by professionals such as doctors or lawyers.
- *The Diversified organization:* this is the classic M-form organization as covered earlier in this chapter; it tends to be decentralized with each division developing its own structures, systems and ways of working.
- *The Adhocracy organization:* this has more in common with the matrix-style organization mentioned earlier, but it also has characteristics of the innovation or i-form organizations covered in Emerging Theme 10.1, in that much of the work is carried out by experts working in temporary project teams.
- *The Missionary organization:* typical of not-for-profit and religious organizations, this form has its culture at the core. More recently a range of commercial organizations have become more like this archetype, attracted by the power a strong culture can create in terms of aligning the workforce, and allowing a substantial degree of delegation and decentralization.
- *The Political organization:* this archetype acknowledges that, in some cases, organizations could have a number of competing power bases pulling in different directions. This could produce a more destructive configuration and would tend to be found in commercial environments where market forces are weak, such as in the case of semi-monopolies, state-owned enterprises, or in other sectors such as government agencies and NGOs.

Alignment

Aligning the organization's activities to strategic direction of the organization is not a new concept – common techniques, such as Drucker's Management By Objectives (MBO), have long formed part of many organization's execution processes. The McKinsey 7S framework described above extended the idea of alignment to a wider range of design elements, and later Miller and Whitney argued that alignment of all elements of organizational design with an 'orchestrating theme' could provide a strong competitive advantage. According to Verweire (2014), the organization's orchestrating theme relates back to the combination of value proposition and operating model, which defines the organization's business model (see Chapter 1 for details). However, alignment is distinct from configuration in that it should take account of factors external to the organization,[73] so not only are the internal design elements of the organization aligned with one another but they are also aligned with external contextual factors. Examples might include the level of uncertainty in the external environment or technological change.

As organizations have faced more complex and volatile environments, resulting from increasing globalization, technological development and reduced levels of regulation, they have also needed to be more flexible in their execution of strategy. This can result in a tension between a very tight approach to alignment and the need for the organization to respond rapidly to changes in its environment. We cover this in more detail in Key Debate 10.1.

Key Debate 10.1

ALIGNMENT VS AGILITY

The idea of success in strategy execution stemming from managers' ability to align different design elements of the organization can be very persuasive. Being able to align the organization in a manner that fits the external situation can be seen as a competitively important competence as, according to Powell (1992), it is a socially complex skill, often tacit and causally ambiguous in nature and therefore hard to copy. Miller and

Whitney (1999) argue that, unless all the different organizational design elements are configured with the strategic direction of the organization, it cannot achieve good performance. Beer (2009) sees alignment as one of three critical prerequisites for developing a sustained competitive advantage.

Verweire (2014) emphasizes that the orchestrating theme should be at the heart of successful alignment because this provides the common thread that helps employees at all levels of the organization understand the strategic direction and act in a consistent manner. He suggests that Treacy and Wiersema's (1995) three generic strategic positions, Operational Excellence, Product Leadership and Customer Intimacy, provide such themes. Aligning the organization's value proposition and operating model to these positions has the potential to provide it with a winning strategy, capable of being implemented by all levels of employees. Martin (2010) offers a slightly different angle on this point. He suggests that a 'choice-cascade' within the context of a firm's strategic direction is needed in order to empower employees. In other words, the rationale behind the orchestrating theme has to be clear to employees, and guidance given for how this relates to the choices and decisions they make. Martin gives the example of the Four Seasons hotel company and its 'Golden Rule', a goal that applies to all employees, 'to deal with others – partners, customers, co-workers, everyone – as we would want them to deal with us'. Employees are empowered to make decisions, solve problems and tackle complaints there and then using the 'Golden Rule' for guidance.

However, Sull et al. (2015) argue that alignment can be overplayed. Their five-year research project surveyed more than 8,000 managers in 250 companies and found that alignment was not the key issue when execution failed. Co-ordination between departments, and in some cases external partners, was a more critical problem. In other words, vertical alignment – or cascading objectives and details of the orchestrating theme to different levels in the organization – worked well, but horizontal alignment – or ensuring that the various functions in the organization worked together effectively – did not.

Sull et al.'s (2015) research also found that one-third of managers considered that their strategy failed because their organization was not sufficiently agile. In other words they were too slow to seize opportunities in rapidly changing environments. Often, managers suggested that it was the resource allocation process that prevented the organization from responding quickly. Guillen and Garcia-Canal (2012) provide some concrete examples of emerging-economy firms that support this view. According to the cases they studied, success often stemmed from the ability to take risks, cope with chaotic and uncertain environments, and adapt to local conditions in a process they term 'execution as strategy'. For example, Grupo Bimbo, a Mexican bakery firm, expanded into China successfully by investing in tricycles to deliver its bread-based products in towns where the streets were too narrow for its trucks. It developed a new product – beef rolled in bread – to introduce Chinese consumers, who did not eat much bread, to its range of bakery products. In many cases, the resource allocation process was an ongoing one rather than a once-a-year part of the planning cycle. By encouraging and resourcing bottom-up initiatives executives can legitimize what Schon (1963) referred to as 'bootlegging' – secret innovation projects carried out by employees. Sull et al. (2015) also suggest that this ability to allocate or reallocate resources at any time in the execution process is an important consideration. However, they caution against pursuing all opportunities, especially those that fall outside the organization's strategic objectives, because even in the largest organizations there is still a limit on the resources available for executing strategic initiatives.

QUESTIONS

1. In which contexts will alignment be a critical factor in successful execution?
2. How can organizations successfully combine alignment and agility?

Sources: Beer, M. (2009) *High Commitment High Performance: How to Build a Resilient Organisation for Sustained Advantage,* San Francisco, CA, Jossey-Bass; Guillen, M. and Garcia-Canal, E. (2012) 'Execution as strategy', *Harvard Business Review,* October, pp. 103–107; Martin, R. (2010) 'The execution trap', *Harvard Business Review,* July–August, pp. 64–71; Miller, D. and Whitney, J. (1999) 'Beyond strategy: configuration as a pillar of competitive advantage', *Business Horizons,* May–June, pp. 5–17; Powell, T. (1992) 'Organisational alignment as competitive advantage', *Strategic Management Journal,* 13(2): 119–134; Schon, D. (1963) 'Champions for radical new inventions', *Harvard Business Review,* March–April, pp. 77–86; Sull, D., Homkes, R. and Sull, C. (2015) 'Why strategy execution unravels and what to do about it', *Harvard Business Review,* March, pp. 58–66; Treacy, M. and Wiersema, F. (1995) *The Discipline of Market Leaders,* Reading, MA, Addison-Wesley; Verweire, K. (2014) *Strategy Implementation,* Abingdon, Routledge.

Chapter Summary and Key Points

1. Executing strategy is an action-oriented, operations-driven activity revolving around the management of people and business processes. The way for managers to start implementing a new strategy is with *a probing assessment of what the organization must do differently to carry out the strategy successfully.* They should then consider *precisely how to make the necessary internal changes* as rapidly as possible.
2. Good strategy execution requires a *team effort.* All managers have strategy-executing responsibility in their areas of authority, and all employees are active participants in the strategy execution process.
3. To ensure a strategy is executed effectively managers have a number of levers they can use. These include the structure of the organization, its people, a variety of systems, as well as organizational processes, policies and procedures. Finally, the culture of the organization can be used when managers consider that a major change of direction is needed.
4. Strategy execution is rarely a one-off event and tends to be a continuous process of change in response to external factors. Managers will make incremental adjustments to the various levers in response to performance data.
5. The two best signs of good strategy execution are whether a company is meeting or beating its performance targets and performing value chain activities in a manner that is conducive to company-wide operating excellence. *Shortfalls in performance signal weak strategy, weak execution or both.*
6. Building an organization capable of good strategy execution entails three types of organization-building actions: (1) *staffing the organization* – assembling a talented management team, and recruiting and retaining employees with the needed experience, technical skills and intellectual capital; (2) *building and strengthening core competences and competitive capabilities* – developing proficiencies in performing strategy-critical value chain activities, and updating them to match changing market conditions and customer expectations; and (3) *structuring the organization and work effort* – instituting organizational arrangements that facilitate good strategy execution, deciding how much decision-making authority to delegate and managing external relationships.
7. Structuring the organization and organizing the work effort in a strategy-supportive fashion has four aspects: (1) deciding which value chain activities to perform internally and which to outsource; (2) aligning the firm's organizational structure with its strategy; (3) deciding how much authority to centralize at the top and how much to delegate to down-the-line managers and employees; and (4) facilitating the necessary collaboration and co-ordination with external partners and strategic allies.
8. To align the firm's organizational structure with its strategy, it is important to make strategy-critical activities the main building blocks. There are four basic types of organizational structure: the simple structure, the functional structure, the multidivisional structure and the matrix structure. Which is most appropriate depends on the firm's size, complexity and strategy.
9. Organization strategies can not be implemented or executed well without a number of support systems to carry on business operations. Real-time information systems and control systems further aid the cause of good strategy execution.
10. Strategy-supportive motivational practices and reward systems are powerful management tools for gaining employee commitment and focusing their attention on the strategy execution goals.
11. Building core competences and competitive capabilities is a time-consuming, managerially challenging exercise that can be approached in three ways: (1) developing capabilities internally; (2) acquiring capabilities through mergers and acquisitions; and (3) accessing capabilities via collaborative partnerships.
12. In building capabilities internally, the first step is to develop the *ability* to do something, through experimentation, active search for alternative solutions, and learning by trial and error. As experience grows and company personnel learn how to perform the activities consistently well and at an acceptable cost, the ability evolves into a tried-and-true capability. The process can be accelerated by making learning a more deliberate endeavour and providing the incentives that will motivate company personnel to achieve the desired ends.

13. As firms get better at executing their strategies, they develop capabilities in the domain of strategy execution. Superior strategy execution capabilities allow companies to get the most from their organizational resources and competitive capabilities. But excellence in strategy execution can also be a more direct source of competitive advantage, since more efficient and effective strategy execution can lower costs and permit firms to deliver more value to customers. Superior strategy execution capabilities are hard to imitate and have no good substitutes. As such, they can be an important source of *sustainable* competitive advantage. Any time rivals can readily duplicate successful strategies, making it impossible to *out-strategize* rivals, the chief way to achieve lasting competitive advantage is to *out-execute* them.
14. Implementing and executing a new or different strategy calls for managers to identify the resource requirements of each new strategic initiative, and then consider whether the current pattern of resource allocation and the budgets of the various sub-units are suitable.
15. Organization policies and procedures facilitate strategy execution when they are designed to fit the strategy and its objectives. When an organization alters its strategy, managers should review existing policies and operating procedures and replace those that are out of line with the new direction of the organization. Well-conceived policies and procedures aid the task of strategy execution by: (1) providing top-down guidance to organization personnel regarding how certain things need to be done and what the boundaries are on independent actions and decisions; (2) enforcing consistency in the performance of strategy-critical activities, thereby improving the quality of the strategy execution effort and aligning the actions of organization personnel, however widely dispersed; and (3) promoting the creation of a work climate conducive to good strategy execution.
16. Aligning or configuring the different execution levers has the potential to improve strategy execution by ensuring actions are co-ordinated with an orchestrating theme. However, this should be tempered with the need for the organization to remain agile and able to respond to changes in its environment.

Closing Case

LEGO: BRICK BY BRICK TO THE TOP OF THE PILE

A COMPANY IN CRISIS

When Jórgen Vig Knudstorp became LEGO's CEO in 2004 (see Exhibit 10.1 for a brief biography), the Danish toy company was in deep trouble. Despite having secured an exclusive licensing deal with Lucasfilm to develop *Star Wars*-themed toys in the late 1990s, the firm had also made a series of ill-fated strategic moves, which had seen sales plummet by up to 30 per cent in a single year. The company had diversified into theme parks back in 1968, when it launched the first LEGOLAND in its home town of Billund. However, new parks launched in 1996 near Windsor in Britain and in 1999 in California, USA, had both been unprofitable. A range of new products, such as an action figure called Galidor, and Clikits, a building system aimed at girls, had failed and, by 2004, the firm was near bankruptcy. Its own estimates were that it was losing close to €750,000 a day.

LEGO was famous as the producer of the LEGO brick, the main component of its interlocking building

EXHIBIT 10.1 Jórgen Vig Knudstorp: brief biography

1968	Born Fredericia, Denmark
1988–97	BA, master's degree and PhD in Economics, Aarhus University
1998	Joined McKinsey & Company as a consultant and later became head of recruitment for its European operations
2001	Joined LEGO
2002	Appointed head of LEGO's Strategy Department
2003	Acting Chief Financial Officer for LEGO, then Chief Vice-President for Corporate Affairs
2004	Appointed CEO of LEGO

system. The firm was founded in 1932 in Denmark by carpenter Ole Kirk Christiansen and the name is a contraction of the Danish words for 'play good'. The toy became very popular because it could be used to build a huge range of models from houses to cars, boats, aeroplanes and trains. However, in the early 2000s it began to look as if such a traditional toy would inevitably lose ground to the Internet and technology-based products.

By the end of 2015 the story was very different, LEGO had posted its best year ever, with revenues rising to $5.2 billion for the year ended December 2015 (see Exhibit 10.2 for selected figures), up 25 per cent on the previous year, which had been 13 per cent up on 2013 thanks to a huge boost from the first LEGO movie. The company was now the second largest toy firm in the world and was fast catching industry leader Mattel, whose 2015 revenues had fallen to $5.7 billion.

LEGO's share of the traditional toys and games sector had risen to more than 7 per cent of the market worldwide and construction toys were being hailed as the most dynamic part of a buoyant global market. In contrast, the video game element of the industry was seeing slower growth in terms of revenue, partly as a result of free-to-play games. Some of the resurgence in the traditional element of the industry had been attributed to LEGO's amazing turnaround.

MANAGING CREATIVITY

Innovation had always played a major role in the toys and games industry. LEGO was typical in having superior capabilities in developing new products. In the 1980s, a partnership with MIT researching links between learning and technology had enabled the company to create toys like LEGO Technic and LEGO Mindstorms, a robotic construction toolset. The firm had also branched out into toys for younger children with Duplo and, in 2004, LEGO Quatro. The turnaround in the firm's fortunes came from more than just good new product development processes. LEGO created a new structure (see Exhibit 10.3) to ensure that its innovation activities were co-ordinated at a strategic level by an Executive Innovation Governance Group. This body made sure developments were mutually reinforcing and consistent with the organization's overall strategy. The Group also acted as investor by allocating resources to specific projects. Rather than focusing on a single type of innovation, LEGO's strategy aimed to embrace eight key areas at three different levels, from incremental changes to fundamentally new products. Alongside new product development, a team was charged with innovating core and enabling processes. Other areas of the firm worked on innovating business models and platforms as well as making effective use of LEGO's many fans through seeking user-generated ideas.

One of the major issues that Knudstorp and his senior team identified was the mismatch between what LEGO's designers were producing and what its customers valued. In the years prior to 2004, the firm's designers had been given free rein as a way of fostering their creativity. Design was seen as one of LEGO's core competences and a major source of competitive advantage over some of its lower-priced, low-cost competitors such as Mega Brands and Tyco Toys. However, by delegating many of the design and product decisions to the designers, LEGO ended up producing toys that no longer appealed to its customers, and increasing costs as the number of components required for LEGO kits rose from 7,000 to 12,400. The restructuring of innovation was one way that Knudstorp planned to change this situation. By getting the designers to work more closely with other teams, such as marketing, supply chain and manufacturing, rather than as an isolated and untouchable group, the CEO hoped to create a more commercial focus. In a counter-intuitive move, the designers were given less flexibility and control over design decisions. New components were manufactured only if they won a vote from a majority of designers. Working with manufacturing teams also helped to keep costs under control and, within a couple of years, the number of components being manufactured had fallen to its 1997 level of 7,000. Opening the innovation process to many of LEGO's user communities also had an impact on the process of design. The design teams had more customer feedback and the links to observational market research data gave them much more insight about how children played with the toys they created. The firm had always struggled to connect with girls and had seen a number of failed product lines aimed at this market segment. The knowledge generated by anthropologists employed by the firm led to the launch of the LEGO Friends line in 2012. By the end of that year, sales of LEGO kits to girls had tripled in the US market.

The company's values played an increasingly important role in ensuring that employees acted in ways that would support LEGO's strategic direction. Recruitment processes were designed to ensure that new staff were comfortable with values such as collaboration and the 'work hard, play hard' culture that typified the organization. One of the recruitment exercises involved using LEGO bricks and was to assess prospective employees' willingness to have fun.

LEGO also developed partnerships with a wide range of other organizations. Some of its most successful collaborations now came from working with firms in the film

EXHIBIT 10.2 LEGO selected financial data 2002–2011

mDKK	2015	2014	2013	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002
Income statement														
Revenue	35,780	28,578	25,294	23,095	18,731	16,014	11,661	9,526	8,027	7,823	7,050	6,315	6,792	9,601
Expenses	(23,536)	(18,881)	(16,958)	(15,489)	(13,065)	(10,899)	(8,659)	(7,522)	(6,556)	(6,475)	(6,582)	(6,252)	(7,902)	(8,795)
Operating profit	12,244	9,697	8,336	7,606	5,666	4,973	2,902	2,100	1,449	1,528	459	(1,162)	(1,565)	806
Financial income and expenses	(96)	(206)	(97)	(84)	(124)	(84)	(15)	(248)	(35)	34	(3)	(75)	67	(189)
Profit/(loss) before tax	12,148	9,491	8,239	7,522	5,542	4,889	2,887	1,852	1,414	1,562	456	(1,237)	(1,498)	617
Net profit/(loss) for the year	9,174	7,025	6,119	5,613	4,160	3,718	2,204	1,352	1,028	1,430	505	(1,931)	(935)	326
Balance sheet														
Total assets	27,877	21,419	17,952	16,352	12,904	10,972	7,788	6,496	6,009	9,022	7,689	8,089	10,049	12,560
Equity	17,751	12,832	11,075	9,864	6,975	5,473	3,291	2,066	1,679	4,727	3,589	2,948	4,892	6,478
Liabilities	10,126	8,587	6,877	6,488	5,929	5,499	4,497	4,430	4,330	4,295	4,100	4,731	5,157	6,082

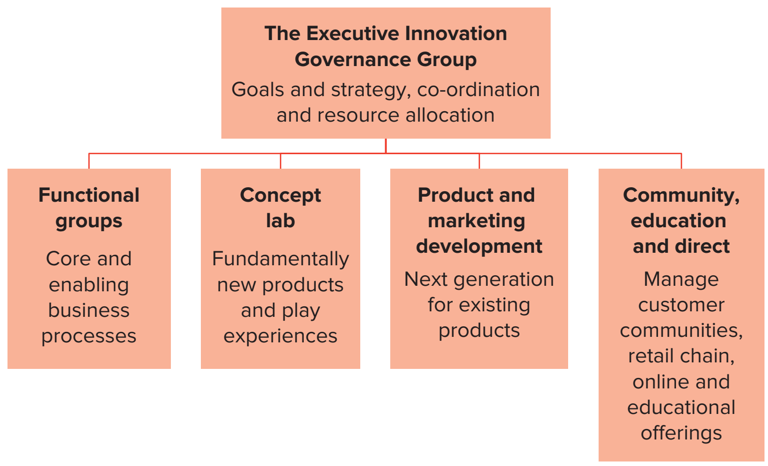

EXHIBIT 10.3 Innovation structure

industry. Building on its experience of the *Star Wars* franchise, LEGO also formed alliances with Disney and Warner Bros to create toys based on other popular films such as *Indiana Jones, Harry Potter* and *Pirates of the Caribbean.* This led to cross-over products such as websites and video games, allowing LEGO to extend its brand from the traditional part of the market into the electronic world, which had appeared to be such a threat in the past. But as well as benefiting from the strength of other brands, LEGO's own reputation proved a source of significant advantage. Named the toy of the century in 2000 by *Fortune* magazine, LEGO licensed its brand to other firms manufacturing everything from clothing and watches to bags and sunglasses. This enabled the company to benefit from its brand reputation without having to build capabilities in manufacturing a wide range of products.

Despite its unique heritage and strong brand, LEGO's turnaround was also underpinned by an aggressive cost-reduction programme. Knudstorp's first priority on becoming CEO in 2004 was to reduce production costs by 20 per cent. This was followed by a series of plant closures as manufacturing capacity was concentrated in Kladno in the Czech Republic. Between 2004 and 2006 restructuring had cost the firm €96 million in additional expenses. By 2008 only premium brands were still being manufactured in the Billund factory in Denmark. The new CEO also had to make some tough decisions about what the firm did and what it should outsource. LEGO's theme parks, developed with Blackstone, a key partner, had been flagships for the company since 1968, but were a drain on resources and did not fit with the organization's core capabilities. In 2005, all the LEGOLAND parks were sold to Merlin Entertainments for $800 million.

Knudstorp's assessment of the firm in 2004 was that 'LEGO had lost its identity. The company strayed too far from having the building system at its core.' Eight years on, LEGO had become a major player in video games, developed online communities to support innovation and tied itself to film companies – and, brick by brick, it had come back from the brink.

QUESTIONS

1. How did the execution of LEGO's strategy strengthen its core competences and competitive capabilities?
2. Explain the structural changes that resulted from the new strategy.
3. Comment on the part staffing decisions played in LEGO's turnaround.

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ASSURANCE OF LEARNING EXERCISES

LO 10.1

1. Examine the overall corporate organizational structure chart for Exelon Corporation. The chart can be found by going to www.exeloncorp.com and using the website search feature to locate 'organizational charts'. Does it appear that strategy-critical activities are the building blocks of Exelon's organizational arrangement? Is its organizational structure best characterized as a departmental structure tied to functional, process or geographic departments? Is the company's organizational structure better categorized as a divisional structure? Would you categorize Exelon's organizational structure as a matrix arrangement? Explain your answer.

LO 10.1

2. Using Google Scholar or your university library's access to EBSCO, InfoTrac or other online databases, do a search for recent writings on decentralized decision-making and employee empowerment. According to the articles you find in the various management journals, what are the conditions under which decision-making should be pushed down to lower levels of management?

LO 10.2

3. Review the Careers link on L'Oréal's worldwide corporate website (go to www.loreal.com and click on the company's worldwide corporate website option). The section provides extensive information about personal development, international learning opportunities, integration of new hires into existing teams and other areas of management development. How do the programmes discussed help L'Oréal to hire good people and build core competences and competitive capabilities? Please use the chapter's discussions of recruiting, training and retaining capable employees and building core competences and competitive capabilities as a guide for preparing your answer.

LO 10.3

4. Using your favourite search engine, do a search on the term *balanced scorecard.* Browse through the search results to identify at least four examples of organizations that are using balanced scorecards as part of their strategic control system. Make notes on each organization's approach. What are the differences and similarities between the approaches and the measures used?

EXERCISES FOR SIMULATION PARTICIPANTS

LO 10.1

1. How would you describe the organization of your company's top management team? Is some decision making decentralized and delegated to individual managers? If so, explain how the decentralization works. Or are decisions made more by consensus, with all co-managers having input? What do you see as the advantages and disadvantages of the decision-making approach your company is employing?

LO 10.4

2. What specific actions have you and your co-managers taken to develop core competences or competitive capabilities that can contribute to good strategy execution and potential competitive advantage? If no actions have been taken, explain your rationale for doing nothing.

LO 10.1

3. What value chain activities are most crucial to good execution of your company's strategy? Does your company have the ability to outsource any value chain activities? If so, have you and your co-managers opted to engage in outsourcing? Why, or why not?

LO 10.4

4. Have you and your co-managers allocated ample resources to strategy-critical areas? If so, explain how these investments have contributed to good strategy execution and improved organization performance.

LO 10.3

5. Does your organization have opportunities to use incentive compensation techniques? If so, explain your organization's approach to incentive compensation. Is there any hard evidence you can cite that indicates your organization's use of incentive compensation techniques has worked? For example, have your organization's compensation incentives actually increased productivity? Can you cite evidence indicating that the productivity gains have resulted in lower labour costs? If the productivity gains have *not* translated into lower labour costs, is it fair to say that your organization's use of incentive compensation is a failure?

Recommended Reading

Classic texts:

- Bartlett, C.A. and Ghoshal, S. (2002) 'Building competitive advantage through people', *MIT Sloan Management Review,* 43(2): 34–41. This paper provides a good summary of the arguments for putting human resources and talent management at the heart of strategy execution.
- Powell, T. (1992) 'Organisational alignment as competitive advantage', *Strategic Management Journal,* 13(2): 119–134. Combines the market-based view of competitive advantage – covering industry factors and positions – and integrates this with the extent to which the structure of the organization is aligned to the external context.
- Simons, R. (1995) 'Control in an age of empowerment', *Harvard Business Review,* 73: 80–88. This paper gives good coverage of one of the key dilemmas managers face when executing strategy – that of retaining control without losing employees' entrepreneurship and ability to innovate; as relevant today as it was 20 years ago.
- Waterman, R., Peters, T. and Phillips, J. (1980) 'Structure is not organisation', *Business Horizons,* June, pp. 14–26. A paper that was ahead of its time in 1980 and has stood the test of time in some aspects. The 7S framework provides a very useful framework for thinking about how to align the different strategy execution levers.

More advanced reading:

- Martin, R. (2010) 'The execution trap', *Harvard Business Review,* July–August, pp. 64–71. Roger Martin's paper is a very thoughtful discussion that recommends empowering employees but also ensuring that strategy is communicated effectively. In common with Simons' view, he argues that effective guidance and a clear direction are preferable to too much control
- Sull, D., Homke, R. and Sull, C. (2015) 'Why strategy unravels and what to do about it', *Harvard Business Review,* March, pp. 58–66. This paper is based on a large survey of managers and contains some very relevant and credible data. The paper presents a strong challenge to some of the more popular approaches to execution, such as that of Bossidy and Charan.

Endnotes

1. As quoted in Floyd, S.W. and Wooldridge, B. (1992) 'Managing strategic consensus: the foundation of effective implementation', *Academy of Management Executive,* 6(4): 27.
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3. Welch, J. with Welch, S. (2005) *Winning,* New York, HarperBusiness, p. 135.
4. Sull, D., Homke, R. and Sull, C. (2015) 'Why strategy unravels and what to do about it', *Harvard Business Review,* March, pp. 58–66.
5. A good discussion of managed change and a classification of the different organizational changes, their links to changes in different elements of a firm's strategy and their relative position on a concrete–conceptual continuum, can be found in Mintzberg, H. and Westley, F. (1992) 'Cycles of organizational change', *Strategic Management Journal,* 13: 39–59.
6. Wilson, D. (1992) *A Strategy of Change,* London, Thomson Learning.
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8. For an excellent and very pragmatic discussion of this point, see Bossidy, L. and Charan, R. (2002) *Execution: The Discipline of Getting Things Done,* New York, Crown Business, Ch. 1.
9. Quinn, J.B. (1992) *Intelligent Enterprise,* New York, Free Press, p. 43.
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11. Quinn, 'Strategic outsourcing: leveraging knowledge capabilities', p. 17.
12. Quinn, *Intelligent Enterprise,* pp. 39–40; also see Pisano, G.P. and Shih, W.C. (2009) 'Restoring American competitiveness', *Harvard Business Review,* 87(7–8): 114–125; Barthélemy, 'The seven deadly sins of outsourcing'.
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