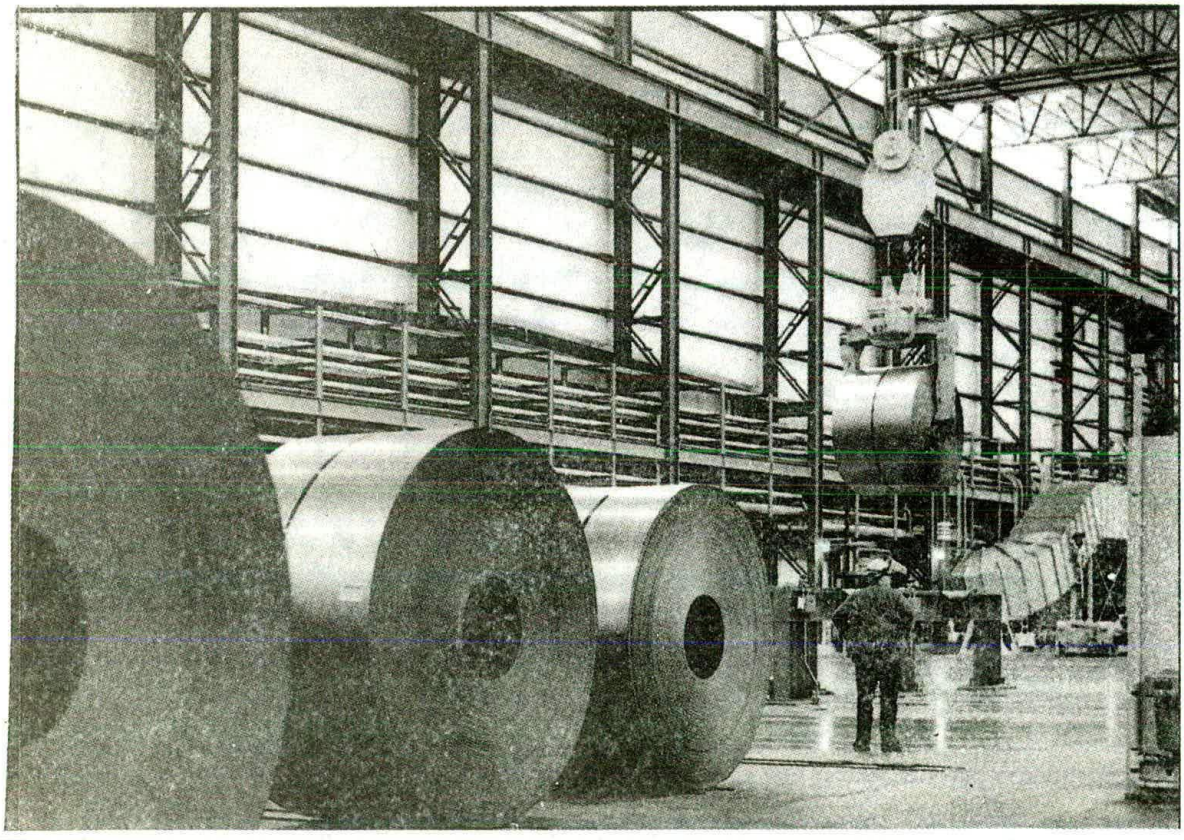
Management

PART ONE

An Introduction to Management

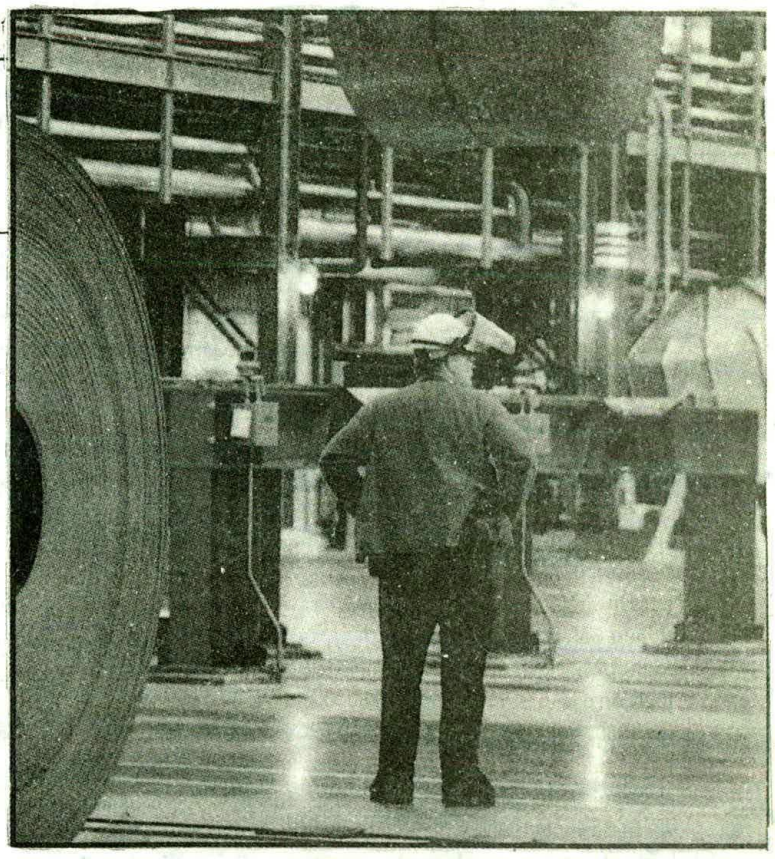


CHAPTER 1

Managing and the Manager's Job

CHAPTER 2

Traditional and Contemporary Issues and Challenges



CHAPTER 1

Managing and the Manager's Job

OPENING INCIDENT

Motorola can trace its roots back to 1928, when Paul Galvin started a small business making electronic products and parts. The firm grew rapidly in the 1940s when it first began making automobile radios and then televisions. In 1947 Galvin renamed the company Motorola after the brand name it was using on its car radios. As time passed, and under the leadership of Robert Galvin, the founder's son, Motorola branched out into increasingly diverse product areas and by the 1980s had become one of the world's largest and most successful electronic enterprises.

In the early 1990s, with a new leadership team at the helm, Motorola was a leader in semiconductors, data communications, and cellular telephone technology. It was also renowned for its quality, winning the first Malcolm Baldrige U.S. National Quality Award in 1988. By the mid-1990s, however, Motorola was on a downward spiral that seemed irreversible. A series of managerial blunders, poorly conceived plans, and plain old bad luck had cost the firm dearly—it had lost its preeminence in the marketplace, had lost touch with its customers, and was taking heat for shoddy product and service quality.

For one thing, Motorola fell behind in digital telephone technology and lost crucial market leadership to Finland's Nokia Group. The semiconductor market also shifted, leaving the firm's semiconductor business poorly positioned for new technologies and areas of new growth potential. Moreover, because the firm did about 24 percent of its business in Asia, the currency crisis that wracked that continent also hit Motorola hard. And a $6 billion iridium communications satellite system that the company invented, financed, and helped build missed its launch date, failed to attract customers, and eventually had to file for bankruptcy protection.

Finally, in 1997 Motorola's board had seen enough. It fired the company's CEO and installed Christopher Galvin, the founder's grandson, in the top spot. Galvin, meanwhile, knew the firm was in dire straits but was a bit unsure where even to begin to start to rebuild the firm. In late 1997 and 1998, the company really hit rock bottom and analysts were writing it off as an also-ran, and a few were quietly already questioning whether or not Galvin had the same managerial skills as his father and grandfather. By that time, though, Galvin had figured out what to do and reconciled both himself and other top managers to the hard realities they faced.

"This is a journey, not a destination."

—Christopher Galvin, CEO of Motorola and chief architect of the firm's amazing turnaround.

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- Describe the nature of management, define management and managers, and characterize their importance to organizations.
- Identify and briefly explain the four basic management functions in organizations.
- Describe the kinds of managers found at different levels and in different areas of the organization.
- Identify the basic managerial roles that managers may play and the skills they need to be successful.
- Discuss the science and the art of management and describe how people become managers.
- Summarize the scope of management in organizations.

Over a period of the next several months Galvin refocused the business on its core strengths, selling off numerous underperforming and peripheral operations. He also renewed Motorola's commitment to innovation and new product development and made marketing a much higher priority than at any time in the firm's history. As part of these changes, Galvin also revamped how the firm was organized, eliminating managerial in-fighting and fiefdoms that had built up over decades. He also played a key inspirational role as well, rallying employees behind the firm's revitalization efforts and encouraging them to develop bold new ideas and to think in different ways. But he also made tough decisions when he had to, cutting 15,000 jobs at one point.

And the result? Motorola has indeed turned itself around and is once again at the forefront of its industry. For example, quality has again become a watchword at Motorola, analysts are promoting Motorola stock, and the company's products are again market leaders.

But Galvin isn't finished yet. In his own words, "This is a journey, not a destination." He plans to continue refining and developing the company to make it even more effective. He has grand visions for the future, visions filled with amazing new products, technologies, and services. And Galvin sees the name "Motorola" emblazoned across this future technology landscape.[1]



CHAPTER OUTLINE

- An Introduction to Management
  - The Management Process
  - Planning and Decision Making: Determining Courses of Action
  - Organizing: Coordinating Activities and Resources
  - Leading: Motivating and Managing People
  - Controlling: Monitoring and Evaluating Activities
- Kinds of Managers
  - Managing at Different Levels of the Organization
  - Managing in Different Areas of the Organization
- Basic Managerial Roles and Skills
  - Managerial Roles
  - Managerial Skills
- The Nature of Managerial Work
  - The Science and the Art of Management
  - Becoming a Manager
- The Scope of Management
  - Managing in Profit-Seeking Organizations
  - Managing in Not-for-Profit Organizations

Christopher Galvin is clearly a manager. So, too, are Philip Knight (CEO of Nike), Carly Fiorina (CEO of Hewlett-Packard), Mikio Sasaki (president of Mitsubishi Corp.), Sir David Wilson (director of the British Museum), Debbie Fields (president of Mrs. Fields Inc. cookie stores), Joe Torre (coach of the New York Yankees), George W. Bush (President of the United States), Jeff Bezos (CEO of Amazon.com), John Paul II (pope of the Roman Catholic Church), and Marilyn Ferguson (owner of the Garden District Gift Shop in Bryan, Texas). As diverse as they and as their organizations are, all of these managers are confronted by many of the same challenges, they strive to achieve many of the same goals, and they apply many of the same concepts of effective management in their work.

For better or worse, our society is strongly influenced by managers and their organizations. Most people in the United States are born in a hospital (an organization), educated by public or private schools (all organizations), and buy almost all their consumable products and services from businesses (organizations). And much of our behavior is influenced by various government agencies (also organizations). We define an **organization** as a group of people working together in a structured and coordinated fashion to achieve a set of goals. The goals may include such things as profit (Starbucks Corporation), the discovery of knowledge (Iowa State University), national defense (the U.S. Army), coordination of various local charities (United Way of America), or social satisfaction (a sorority). Because they play such a major role in our lives, understanding how organizations operate and how they are managed is important.

organization A group of people working together in a structured and coordinated fashion to achieve a set of goals

This book is about managers and the work they do. In Chapter 1, we examine the general nature of management, its dimensions, and its challenges. We explain the concepts of management and managers, discuss the management process and present an overview of the book, and identify various kinds of managers. We describe the different roles and skills of managers, discuss the nature of managerial work, and examine the scope of management in contemporary organizations. In Chapter 2 we describe how both the practice and theory of management have evolved. As a unit, then, these first two chapters provide an introduction to the field with both contemporary and historical perspectives on management.

■ An Introduction to Management

While defining "organization" is relatively simple, the concept of "management" is a bit more elusive. It is perhaps best understood from a resource-based perspective. As we discuss more completely in Chapter 2, all organizations use four basic kinds of resources from their environment: human, financial, physical, and information. Human resources include managerial talent and labor. Financial resources are the capital used by the organization to finance both ongoing and long-term operations. Physical resources include raw materials, office and production facilities, and equipment. Information resources are usable data needed to make effective decisions. Examples of resources used in four very different kinds of organizations are shown in Table 1.1.

Table 1.1

Examples of Resources Used by Organizations

All organizations, regardless of whether they are large or small, profit-seeking or not-for-profit, domestic or multinational, use some combination of human, financial, physical, and information resources to achieve their goals. These resources are generally obtained from the organization's environment.

Organization	Human Resources	Financial Resources	Physical Resources	Information Resources
Shell Oil	Drilling platform workers Corporate executives	Profits Stockholder investments	Refineries Office buildings	Sales forecasts OPEC proclamations
Iowa State University	Faculty Administrative staff	Alumni contributions Government grants	Computers Campus facilities	Research reports Government publications
New York City	Police officers Municipal employees	Tax revenue Government grants	Sanitation equipment Municipal buildings	Economic forecasts Crime statistics
Susan's Corner Grocery Store	Grocery clerks Bookkeeper	Profits Owner investment	Building Display shelving	Price lists from suppliers Newspaper ads for competitors

Managers are responsible for combining and coordinating these various resources to achieve the organization's goals. A manager at Royal Dutch/Shell Group, for example, uses the talents of executives and drilling platform workers, profits earmarked for reinvestment, existing refineries and office facilities, and sales forecasts to make decisions regarding the amount of petroleum to be refined and distributed during the next quarter. Similarly, the mayor (manager) of New York City might use police officers, a government grant (perhaps supplemented with surplus tax revenues), existing police stations, and detailed crime statistics to launch a major crime prevention program in the city.

How do these and other managers combine and coordinate the various kinds of resources? They do so by carrying out four basic managerial functions or activities: planning and decision making, organizing, leading, and controlling. **Management**, then, as illustrated in Figure 1.1, can be defined as a set of activities (including planning and decision making, organizing, leading, and controlling) directed at an organization's resources (human, financial, physical, and information) with the aim of achieving organizational goals in an efficient and effective manner.

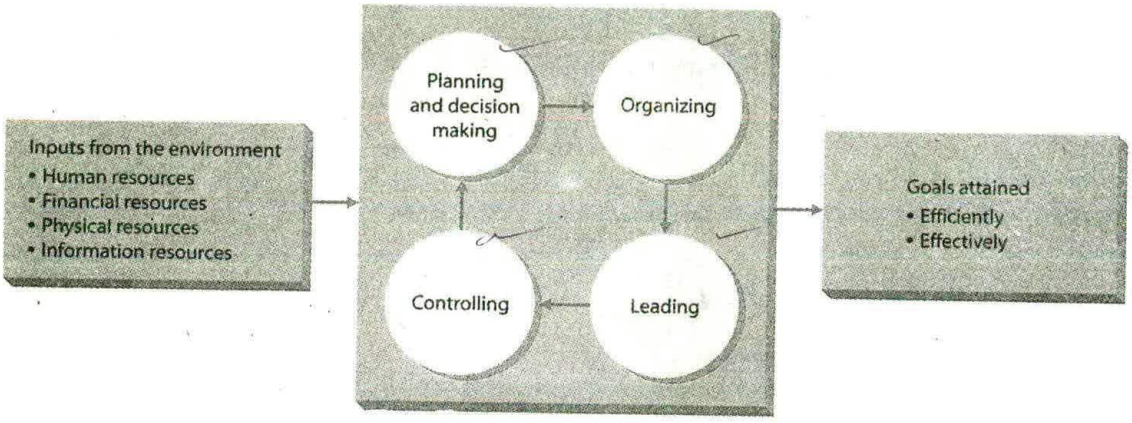
Management is a complex, challenging, and exciting process. Rapid changes in today's business environment make it imperative that managers stay abreast of business opportunities and trends. Catherine Rodriguez, for example, is the training manager at Cisco System's plant in San Jose. Key components of her job include knowing the latest technology, designing instructional content, and assisting others in using advanced training methods to improve their own job performance. She is shown here helping an assembler master electronic learning. About 90 percent of all of Cisco's training is handled through electronic media.



Figure 1.1

Management in Organizations

Basic managerial activities include planning and decision making, organizing, leading, and controlling. Managers engage in these activities to combine human, financial, physical, and information resources efficiently and effectively and to work toward achieving the goals of the organization.



management A set of activities (including planning and decision making, organizing, leading, and controlling) directed at an organization's resources (human, financial, physical, and information) with the aim of achieving organizational goals in an efficient and effective manner

efficient Using resources wisely and in a cost-effective way

effective Making the right decisions and successfully implementing them

manager Someone whose primary responsibility is to carry out the management process

The last phrase in our definition is especially important because it highlights the basic purpose of management—to ensure that an organization's goals are achieved in an efficient and effective manner. By **efficient**, we mean using resources wisely and in a cost-effective way. For example, a firm like Toyota Motor Corp. that produces high-quality products at relatively low costs is efficient. By **effective**, we mean making the right decisions and successfully implementing them. Toyota also makes cars with the styling and quality to inspire consumer interest and confidence. A firm could produce black-and-white console televisions very efficiently but still not succeed because black-and-white televisions are no longer popular. A firm that produces products that no one wants is therefore not effective. In general, successful organizations are both efficient and effective.[2]

With this basic understanding of management, defining the term *manager* becomes relatively simple—a **manager** is someone whose primary responsibility is to carry out the management process. In particular, a manager is someone who plans and makes decisions, organizes, leads, and controls human, financial, physical, and information resources. Today's managers face a variety of interesting and challenging situations. The average executive works sixty hours a week, has enormous demands placed on his or her time, and faces increased complexities posed by globalization, domestic competition, government regulation, shareholder pressure, and Internet-related uncertainties. The job is complicated even more by rapid changes, unexpected disruptions, and both minor and major crises. The manager's job is unpredictable and fraught with challenges, but it is also filled with opportunities to make a meaningful difference.

Many of the characteristics that contribute to the complexity and uncertainty of management stem from the environment in which their organizations function. For example, as shown in Figure 1.1, the resources used by organizations to create products and services all come from the environment. Thus, it is critical that managers understand this environment. Part II of the text discusses the environmental context of management in detail. Chapter 3 provides a general overview and discussion of the organization's environment, and Chapters 4 through 6 address specific aspects of the environment more fully. In particular, Chapter 4 discusses the ethical and social context of management. Chapter 5 explores the global context of management. Chapter 6 describes the cultural and multicultural environment of management. After reading these chapters, you will be better prepared to study the essential activities that comprise the management process.

■ The Management Process

We noted earlier that management involves the four basic functions of planning and decision making, organizing, leading, and controlling. Because these functions represent the framework around which this book is organized, we introduce them here and note where they are discussed more fully. Their basic definitions and interrelationships are shown in Figure 1.2. (Note that Figure 1.2 is an expanded version of the central part of Figure 1.1.)

Recall the details of Motorola's turnaround discussed earlier. Christopher Galvin first created a clear set of goals and plans that articulated what he wanted the company to become. He also created a more effective organization to help make those goals and plans a reality. Galvin also pays close attention to the people who work for Motorola. And he keeps a close eye on how well the company is performing. Each of these activities represents one of the four basic managerial functions illustrated in the figure—setting goals is part of planning, setting up the organization is part of organizing, managing people is part of leading, and monitoring performance is part of control. *Managing in an E-business World* summarizes how managers at one company, United Parcel Service, are also using these same functions as they move the company more and more into the world of electronic commerce.

It is important to note, however, that the functions of management do not usually occur in a tidy, step-by-step fashion. Managers do not plan on Monday, make

Figure 1.2

The Management Process

Management involves four basic activities—planning and decision making, organizing, leading, and controlling. Although there is a basic logic for describing these activities in this sequence (as indicated by the solid arrows), most managers engage in more than one activity at a time and often move back and forth between the activities in unpredictable ways (as shown by the dotted arrows).



MANAGING IN AN *e*-BUSINESS WORLD

MANAGING E-COMMERCE DELIVERIES

When a consumer clicks to make a purchase on-line, United Parcel Service (UPS) wants to deliver the package. Because other shippers are also jockeying for position in e-commerce delivery, UPS's managers will need skillful planning, organizing, leading, and controlling to stay ahead of the pack.

UPS ships more than half of all consumer e-commerce purchases, while the U.S. Postal Service ships about one-third and FedEx ships just one-tenth. But all three companies want more of this fast-growing market, which could top 4.2 million packages daily within a few years.

Knowing that the stakes are high, UPS CEO James Kelly starts the planning process by setting strategic goals. A top priority is building UPS into the leading shipper of on-line purchases to any destination. From there, other management decisions—such as investing in sophisticated technology to track packages—are designed to bring UPS closer to its goals.

Organizing to implement these decisions, UPS has combined its air express and ground shipping businesses so customers can arrange for any delivery with one phone call. Kelly, like nearly every top manager, started his career driving a UPS truck, so he has firsthand knowledge of what employees can and should be doing to stay ahead of competitors.

As Kelly and his top managers rose through the ranks, they forged connections with other managers and employees and learned what works (and doesn't work) when leading and motivating the UPS workforce. Profit-sharing is a powerful incentive, for example, as is the opportunity to own company stock now that UPS has gone public.

Controlling is vital in the shipping business, where customers demand on-time delivery. UPS managers use technology to track every shipment and to analyze the productivity of personnel and other resources. The system runs so smoothly that UPS now offers a money-back guarantee for ground shipments. By monitoring progress and making corrections as needed, Kelly and his managers are keeping UPS on course to remain the leader in e-commerce delivery.

We are going to involve ourselves in global commerce more deeply and more extensively than ever.

—James Kelly, CEO, United Parcel Service*

References: Brian O'Reilly, "They've Got Mail!" *Fortune,* February 7, 2000, pp. 100–112 (*quote on p. 103); David Rocks, "Going Nowhere Fast in Cyberspace," *Business Week,* January 31, 2000, pp. 58–59.

decisions on Tuesday, organize on Wednesday, lead on Thursday, and control on Friday. At any given time, as illustrated in the cartoon, for example, a manager is likely to be engaged in several different activities simultaneously. Indeed, from one setting to another, managerial work is as different as it is similar. The similarities that pervade most settings are the phases in the management process. Important differences include the emphasis, sequencing, and implications of each phase.[3] Thus, the solid lines in Figure 1.2 indicate how, in theory, the functions of management are performed. The dotted lines, however, represent the true reality of management. In the sections that follow, we explore each of these activities.

Planning and Decision Making: Determining Courses of Action

In its simplest form, **planning** means setting an organization's goals and deciding how best to achieve them. **Decision making**, a part of the planning process, involves selecting a course of action from a set of alternatives. Planning and decision making help maintain managerial effectiveness by serving as guides for future activities. That is, the organization's goals and plans clearly help managers know how to allocate their time and resources. Carly Fiorina was appointed as CEO of Hewlett-Packard in 1999 and given a mandate to get the struggling firm back on track. Her first actions, in turn, included developing a new set of corporate goals refocusing the company on its core competencies and outlining a new business strategy to energize the company and integrate Internet technology throughout all its operations.[4]



"Do you mind? I happen to be on the phone!"

Drawing by S. Gross

Managers are constantly engaged in many different activities. The types and sequences of activities are often difficult to predict from one day to the next, however, and managers often do their work in impromptu settings or on airplanes, in taxis, over meals, or even when walking down the street. The manager shown here, for example, may be helping a colleague develop goals for the next quarter (planning), discussing a proposed company restructuring (organizing), praising a subordinate for outstanding performance (leading), or checking on last month's sales information (controlling). The pace of this work may be stressful for some people, and exhilarating for others.

Four chapters making up Part III of this text are devoted to planning and decision making. Chapter 7 examines the basic elements of planning and decision making, including the role and importance of organizational goals. Chapter 8 looks at strategy and strategic planning, which provide overall direction and focus for the organization. Chapter 9 explores managerial decision making and problem solving in detail. Finally, Chapter 10 addresses planning and decision making as they relate to the management of new ventures and entrepreneurial activities, increasingly important parts of managerial work.

Organizing: Coordinating Activities and Resources

Once a manager has set goals and developed a workable plan, the next management function is to organize people and the other resources necessary to carry out the plan. Specifically, **organizing** involves determining how activities and resources are to be grouped. One of the immediate obstacles facing Carly Fiorina at Hewlett-Packard was a rigid and bureaucratic hierarchy that promoted insular thinking and limited innovation. She swept this structure aside, creating a much more organic and flexible organization that, in turn, quickly became much more responsive and forward looking.

Organizing is the subject of Part IV. Chapter 11 introduces the basic elements of organizing, such as job design, departmentalization, authority relationships, span of control, and line and staff roles. Chapter 12 explains how managers fit these elements and concepts together to form an overall organization design. Organization change and innovation are the focus of Chapter 13. Finally, processes associated with hiring and assigning people to carry out organizational roles are described in Chapter 14.

planning Setting an organization's goals and deciding how best to achieve them

decision making Part of the planning process that involves selecting a course of action from a set of alternatives

organizing Determining how activities and resources are to be grouped

Leading: Motivating and Managing People

leading The set of processes used to get members of the organization to work together to advance the interests of the organization

The third basic managerial function is leading. Some people consider leading to be both the most important and the most challenging of all managerial activities. **Leading** is the set of processes used to get members of the organization to work together to advance the interests of the organization. Carly Fiorina came to Hewlett-Packard with a reputation for being a trustworthy and honest manager, but also one who would make tough decisions and hard choices. Her personality blended perfectly with other top managers at the company and they were soon working together as a cohesive and effective team.

Leading involves several different processes and activities, which are discussed in Part V. The starting point is understanding basic individual and interpersonal processes, which we focus on in Chapter 15. Motivating employees is discussed in Chapter 16, and leadership itself and the leader's efforts to influence others are covered in Chapter 17. Managing interpersonal relations and communication is the subject of Chapter 18. Finally, managing work groups and teams, another important part of leading, is addressed in Chapter 19.

Controlling: Monitoring and Evaluating Activities

controlling Monitoring the organization's progress toward its goals

The final phase of the management process is **controlling**, or monitoring the organization's progress toward its goals. As the organization moves toward its goals, managers must monitor progress to ensure that it is performing so that it arrives at its "destination" at the appointed time. A good analogy is that of a space mission to Mars. NASA does not simply shoot a rocket in the general direction of the planet and then look again in four months to see whether the rocket hit its mark. NASA monitors the spacecraft almost continuously and makes whatever course corrections are needed to keep it on track. Controlling helps ensure the effectiveness and efficiency needed for successful management. While Carly Fiorina is off to a great start at Hewlett-Packard, the firm still has a long way to go to regain its technological leadership. Thus, she has set in place numerous benchmarks that will be used to assess the firm's progress over the next few years as it evolves toward her model of strategic competitiveness.

The control function is explored in Part VI. First, Chapter 20 explores the basic elements of the control process, including the increasing importance of strategic control. Managing operations, quality, and productivity is explored in Chapter 21, along with productivity and operations management. Finally, Chapter 22 addresses the management of information and information technology, still other critical areas of organizational control.

MANAGEMENT IMPLICATIONS Managers should thoroughly understand each of the basic functions—planning and decision making, organizing, leading, and controlling—that comprise their jobs. They should also recognize that while each is important in its own right, effective managers are skilled in performing each function, must be capable of moving back and forth among the functions as circumstances warrant, and must often juggle multiple functions and activities

simultaneously. Managers cannot afford to be effective in or to enjoy performing only some of the functions because all are important.

■ Kinds of Managers

Earlier in this chapter we identified as managers people from a variety of organizations. Clearly, there are many kinds of managers. One point of differentiation is among organizations, as those earlier examples imply. Another point occurs within an organization. Figure 1.3 shows how managers within an organization can be differentiated by level and area.

Managing at Different Levels of the Organization

Managers can be differentiated according to their level in the organization. Although large organizations typically have several **levels of management**, the most common view considers three basic levels: top, middle, and first-line managers.

levels of management The differentiation of managers into three basic levels—top, middle, and first-line

Top Managers Top managers make up the relatively small group of executives who manage the overall organization. Titles found in this group include president,

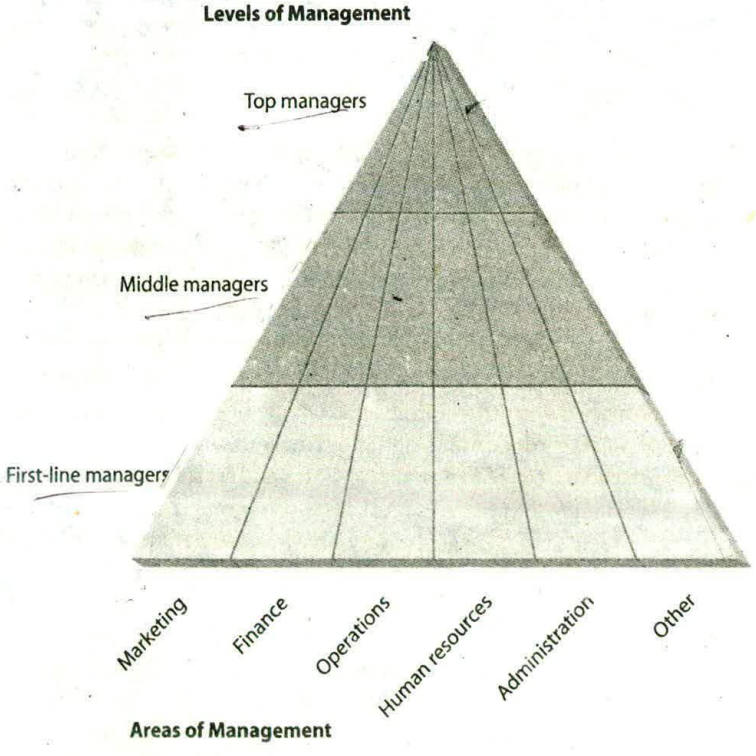


Figure 1.3

Kinds of Managers by Level and Area

Organizations generally have three levels of management, represented by top managers, middle managers, and first-line managers. Regardless of level, managers are also usually associated with a specific area within the organization, such as marketing, finance, operations, human resources, administration, or some other area.



Businesses have many different kinds of managers. Top managers are the small group of executives who manage the overall organization. Matt Massengill (left) is president and CEO of Western Digital; Carly Fiorina (center) is the president and CEO of Hewlett-Packard; and Michael Capellas (right) is president and CEO of Compaq Computer. Each is a top manager. The three are shown here at a news conference where Ms. Fiorina is explaining a new venture between twelve high-tech companies, including Western, HP, and Compaq, that will create an Internet exchange to serve the needs of its member companies. Top managers are instrumental in developing concepts for such new enterprises, are responsible for committing resources for them, and are ultimately accountable for their success or failure.

vice president, and chief executive officer (CEO). Top managers create the organization's goals, overall strategy, and operating policies. They also officially represent the organization to the external environment by meeting with government officials, executives of other organizations, and so forth. *Today's Management Issues* explores the question of how involved a CEO should be in day-to-day operations versus "bigger picture" kinds of issues. Howard Schultz, CEO of Starbucks, is a top manager, as is Deidra Wager, the firm's Senior Vice President for Retail Operations. The job of a top manager is likely to be complex and varied. Top managers make decisions about such activities as acquiring other companies, investing in research and development, entering or abandoning various markets, and building new plants and office facilities. They often work long hours and spend much of their time in meetings or on the telephone. In most cases, top managers are also very well paid. In fact, the elite top managers of very large firms sometimes make several million dollars a year in salary, bonuses, and stock.[5]

Middle Managers Middle management is probably the largest group of managers in most organizations. Common middle-management titles include plant manager, operations manager, and division head. Middle managers are primarily responsible for implementing the policies and plans developed by top managers and for supervising and coordinating the activities of lower-level managers.[6] Plant

TODAY'S MANAGEMENT ISSUES

No Detail Too Small for Top Management Attention?

How should top executives spend their time? Walt Disney CEO Michael Eisner believes his time is best spent delving into minute details of his company's operations. Bill Gates of Microsoft and Steve Case of AOL Time Warner, on the other hand, believe their time is better spent on strategic issues. Which way is most effective?

Eisner enjoys getting deeply involved in everyday decisions. After naming Robert A. Iger as Disney's president and chief operating officer, Eisner could have turned his attention to the big picture. After all, Disney is a multifaceted organization, with movie studios, television stations, theme parks, retail stores, Internet sites, and other businesses. Instead, Eisner began reading movie scripts and discussing new park rides, while delegating long-range planning to the head of strategic planning and the chief financial officer. He's especially interested in cost-cutting measures. Paging through one script, for example, he made a note about a change that could save the company several million dollars during filming.

In contrast, after Microsoft's Bill Gates promoted Steve Ballmer into the CEO position, he named himself chief software architect. Given the regulatory and competitive challenges that Microsoft is facing, this role enables Gates to think through major issues about the company's future. Similarly, AOL's founder, Steve Case, decided to become chairman of the board after his company acquired Time Warner. He named Gerald Levin as CEO and then stepped back from day-to-day operations to make long-term plans for new technology and global expansion.

Should top managers follow Eisner's example and make nitty-gritty decisions about operational details? Or should they follow the example of Gates and Case and concentrate on strategy, letting other executives make daily decisions? There is no correct answer, of course, especially since all three of these managers are acknowledged as being very effective. But each manager needs to assess carefully both her or his personal preferences and the needs of the organization and work to ensure that they align effectively.

In the entertainment business, it's about the details.

*—Michael Eisner, CEO, Walt Disney**

References: Bruce Orwall, "Michael Eisner's New Agenda: Details, Details," *Wall Street Journal*, January 26, 2000, pp. B1, B4 (*quote on p. B1); Joseph Nocera, "The Men Who Would Be King," *Fortune*, February 7, 2000, pp. 66–69.

managers, for example, handle inventory management, quality control, equipment failures, and minor union problems. They also coordinate the work of supervisors within the plant. Jason Hernandez, a regional manager at Starbucks responsible for the firm's operations in three eastern states, is a middle manager.

In recent years, many organizations have thinned the ranks of middle managers to lower costs and eliminate excess bureaucracy. Still, middle managers are necessary to bridge the upper and lower levels of the organization and to implement the strategies developed at the top. Although many organizations have found that they can indeed survive with fewer middle managers, those who remain play an even more important role in determining how successful the organization will be.[7]

First-Line Managers First-line managers supervise and coordinate the activities of operating employees. Common titles for first-line managers are supervisor, coordinator, and office manager. Positions such as these are often the first held by

employees who enter management from the ranks of operating personnel. Wayne Maxwell and Jenny Wagner, managers of Starbucks coffee shops in Texas, are first-line managers. They oversee the day-to-day operations of their respective stores, hire operating employees to staff them, and handle other routine administrative duties required of them by the parent corporation. In contrast to top and middle managers, first-line managers typically spend a large proportion of their time supervising the work of subordinates.

Managing in Different Areas of the Organization

areas of management Managers can be differentiated into marketing, financial, operating, human resource, administration, and other areas

Regardless of their level, managers may work in various areas within an organization. In any given firm, for example, **areas of management** may include marketing, financial, operations, human resource, administrative, and other areas.

Marketing Managers Marketing managers work in areas related to the marketing function—getting consumers and clients to buy the organization's products or services (be they Motorola digital cell phones, Ford automobiles, *Newsweek* magazines, Associated Press news reports, flights on Southwest Airlines, or cups of latte at Starbucks). These areas include new product development, promotion, and distribution. Given the importance of marketing for virtually all organizations, developing good managers in this area can be critical.

Financial Managers Financial managers deal primarily with an organization's financial resources. They are responsible for activities such as accounting, cash management, and investments. In some businesses, such as banking and insurance, financial managers are found in especially large numbers. Jacques Nasser, CEO of Ford Motor Co., started his career with the company more than thirty years ago as a financial analyst.

Operations Managers Operations managers are concerned with creating and managing the systems that create an organization's products and services. Typical responsibilities of operations managers include production control, inventory control, quality control, plant layout, and site selection.

Human Resource Managers Human resource managers are responsible for hiring and developing employees. They are typically involved in human resource planning, recruiting and selecting employees, training and development, designing compensation and benefit systems, formulating performance appraisal systems, and discharging low-performing and problem employees.

Administrative Managers Administrative, or general, managers are not associated with any particular management specialty. Probably the best example of an administrative management position is that of a hospital or clinic administrator. Administrative managers tend to be generalists; they have some basic familiarity with all functional areas of management rather than specialized training in any one area.[8]

Other Kinds of Managers Many organizations have specialized management positions in addition to those already described. Public relations managers, for example, deal with the public and media for firms like Philip Morris Companies, Inc., and The Dow Chemical Co. to protect and enhance the image of the organization. Research and development (R&D) managers coordinate the activities of scientists and engineers working on scientific projects in organizations such as Monsanto Company, NASA, and Merck & Co. Internal consultants are used in organizations such as The Prudential Insurance Co. of America to provide specialized expert advice to operating managers. International operations are often coordinated by specialized managers in organizations like Eli Lilly and Rockwell International Corp. The number, nature, and importance of these specialized managers vary tremendously from one organization to another. As contemporary organizations continue to grow in complexity and size, the number and importance of such managers are also likely to increase.

MANAGEMENT IMPLICATIONS Managers can be found at all levels and in all areas of an organization. A career path up the organizational ladder might be primarily within a single area, or might span several areas. Thus, managers should try to understand where their current position fits into the organization, and what path they may want to pursue to advance their career goals. Cutbacks in the ranks of middle managers also mean that lower-level managers in major corporations may have to wait longer for a promotion, since there are fewer jobs at the higher levels for them to enter.[9]

■ Basic Managerial Roles and Skills

Regardless of their level or area within an organization, all managers must play certain roles and exhibit certain skills if they are to be successful. The concept of a role, in this sense, is similar to the role an actor plays in a theatrical production. A person does certain things, meets certain needs in the organization, and has certain responsibilities. In the sections that follow, we first highlight the basic roles managers play and then discuss the skills they need to be effective.

Managerial Roles

Henry Mintzberg offers a number of interesting insights into the nature of managerial roles.[10] He closely observed the day-to-day activities of a group of CEOs by literally following them around and taking notes on what they did. From his observations, Mintzberg concluded that managers play ten different roles, as summarized in Table 1.2, and that these roles fall into three basic categories: interpersonal, informational, and decisional.

Interpersonal Roles There are three **interpersonal roles** inherent in the manager's job. First, the manager is often asked to serve as a *figurehead*—taking visitors to dinner, attending ribbon-cutting ceremonies, and the like. These activities are

interpersonal roles The roles of figurehead, leader, and liaison, all of which involve dealing with other people

Table 1.2

Ten Basic Managerial Roles

Research by Henry Mintzberg suggests that managers play ten basic managerial roles.

Category	Role	Sample Activities
Interpersonal	Figurehead	Attending ribbon-cutting ceremony for new plant
	Leader	Encouraging employees to improve productivity
	Liaison	Coordinating activities of two project groups
Informational	Monitor	Scanning industry reports to stay abreast of developments
	Disseminator	Sending memos outlining new organizational initiatives
	Spokesperson	Making a speech to discuss growth plans
Decisional	Entrepreneur	Developing new ideas for innovation
	Disturbance handler	Resolving conflict between two subordinates
	Resource allocator	Reviewing and revising budget requests
	Negotiator	Reaching agreement with a key supplier or labor union

typically more ceremonial and symbolic than substantive. The manager is also asked to serve as a *leader*—hiring, training, and motivating employees. A manager who formally or informally shows subordinates how to complete tasks and how to perform under pressure is leading. Finally, managers can have a *liaison* role. This role often involves serving as a coordinator or link between people, groups, or organizations. For example, companies in the computer industry may use liaisons to keep other companies informed about their plans. This enables Microsoft, for example, to create software for interfacing with new Hewlett-Packard printers while those printers are being developed. And, at the same time, managers at Hewlett-Packard can also incorporate new Microsoft features into the printers they introduce.

Managers play several basic roles in organizations. Consider, for example, the case of Charlie Woo. Mr. Woo, an immigrant from Hong Kong, started a new toy company in downtown Los Angeles called ABC Toys. He imports cheap but sturdy toys from Asia and then sells them in the United States and Mexico. ABC Toys are generally cheaper than those offered by big multinationals like Mattel but of higher quality than most cheap knock-offs offered by other small toy importers. By effectively playing the various interpersonal, information, and decisional roles, Woo has made his firm one of the most profitable in the industry.



Informational Roles The three **informational roles** flow naturally from the interpersonal roles just discussed. The process of carrying out these roles places the manager at a strategic point to gather and disseminate information. The first informational role is that of *monitor*, one who actively seeks information that may be of value. The manager questions subordinates, is receptive to unsolicited information, and attempts to be as well informed as possible. The manager is also a *disseminator* of information, transmitting relevant information back to others in the workplace. When the roles of monitor and disseminator are viewed together, the manager emerges as a vital link in the organization's chain of

communication. The third informational role focuses on external communication. The *spokesperson* formally relays information to people outside the unit or outside the organization. For example, a plant manager at Union Carbide Corp. may transmit information to top-level managers so that they will be better informed about the plant's activities. The manager may also represent the organization before a chamber of commerce or consumer group. Although the roles of spokesperson and figurehead are similar, there is one basic difference between them. When a manager acts as a figurehead, the manager's presence as a symbol of the organization is what is of interest. In the spokesperson role, however, the manager carries information and communicates it to others in a formal sense.

informational roles The roles of monitor, disseminator, and spokesperson, all of which involve the processing of information

Decisional Roles The manager's informational roles typically lead to the **decisional roles**. The information acquired by the manager as a result of performing the informational roles has a major bearing on important decisions that he or she makes. Mintzberg identified four decisional roles. First, the manager has the role of *entrepreneur*, the voluntary initiator of change. A manager at 3M Company developed the idea for the Post-it Note Pad but had to "sell" it to other skeptical managers inside the company. A second decisional role is initiated not by the manager but by some other individual or group. The manager responds to her role as *disturbance handler* by handling such problems as strikes, copyright infringements, or problems in public relations or corporate image.

decisional roles The roles of entrepreneur, disturbance handler, resource allocator, and negotiator, all of which relate primarily to making decisions

The third decisional role is that of *resource allocator*. As resource allocator, the manager decides how resources are distributed, and with whom he or she will work most closely. For example, a manager typically allocates the funds in the unit's operating budget among the unit's members and projects. A fourth decisional role is that of *negotiator*. In this role the manager enters into negotiations with other groups or organizations as a representative of the company. For example, managers may negotiate a union contract, an agreement with a consultant, or a long-term relationship with a supplier. Negotiations may also be internal to the organization. The manager may, for instance, mediate a dispute between two subordinates or negotiate with another department for additional support.

Managerial Skills

In addition to fulfilling numerous roles, managers also need a number of specific skills if they are to succeed. The most fundamental management skills are technical, interpersonal, conceptual, diagnostic, communication, decision-making, and time-management skills.[11]

Technical Skills **Technical skills** are the skills necessary to accomplish or understand the specific kind of work being done in an organization. Technical skills are especially important for first-line managers. These managers spend much of their time training subordinates and answering questions about work-related problems. They must know how to perform the tasks assigned to those they supervise if they are to be effective managers. Horst Schulze, CEO of Ritz-Carlton, got his start washing dishes and waiting tables at hotels in Germany. Over the next several

technical skills The skills necessary to accomplish or understand the specific kind of work being done in an organization

years he also worked as a bellhop, a front-desk clerk, and a concierge. These experiences gave him keen insight into the inner workings of a quality hotel operation, insights he has used to take Ritz-Carlton to the top of its industry.[12]

Interpersonal Skills Managers spend considerable time interacting with people both inside and outside the organization. For obvious reasons, then, the manager also needs **interpersonal skills**—the ability to communicate with, understand, and motivate both individuals and groups. As a manager climbs the organizational ladder, she must be able to get along with subordinates, peers, and those at higher levels of the organization. Because of the multitude of roles managers must fulfill, a manager must also be able to work with suppliers, customers, investors, and others outside the organization. Although some managers have succeeded with poor interpersonal skills, a manager who has good interpersonal skills is likely to be more successful. When A. G. Lafley was recently appointed CEO of Procter & Gamble, observers were quick to praise him for his strong interpersonal skills. As one colleague put it, "A. G. has a reputation for both people skills and strategic thinking."[13]

interpersonal skills The ability to communicate with, understand, and motivate both individuals and groups

Conceptual Skills **Conceptual skills** depend on the manager's ability to think in the abstract. Managers need the mental capacity to understand the overall workings of the organization and its environment, to grasp how all the parts of the organization fit together, and to view the organization in a holistic manner. These conceptual skills allow them to think strategically, to see the "big picture," and to make broad-based decisions that serve the overall organization.

conceptual skills The manager's ability to think in the abstract

Diagnostic Skills Successful managers also possess **diagnostic skills**, or skills that enable a manager to visualize the most appropriate response to a situation. A physician diagnoses a patient's illness by analyzing symptoms and determining their probable cause. Similarly, a manager can diagnose and analyze a problem in the organization by studying its symptoms and then developing a solution. According to one source, Eckhard Pfeiffer ultimately failed as CEO of Compaq Computer because he did not have strong diagnostic skills.[14]

diagnostic skills The manager's ability to visualize the most appropriate response to a situation

Communication Skills **Communication skills** refer to the manager's abilities both to convey ideas and information effectively to others and to receive ideas and information effectively from others. These skills enable a manager to transmit ideas to subordinates so that they know what is expected, to coordinate work with peers and colleagues so that they work well together properly, and to keep higher-level managers informed about what is going on. In addition, they help the manager listen to what others say and to understand the real meaning behind letters, reports, and other written communication.

communication skills The manager's abilities both to convey ideas and information effectively to others and to receive ideas and information effectively from others

Decision-Making Skills Effective managers also have good decision-making skills. **Decision-making skills** refer to the manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action to solve problems and capitalize on opportunities. No manager makes the

decision-making skills The manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action to solve problems and capitalize on opportunities

right decision all the time. However, effective managers make good decisions most of the time. And when they do make a bad decision, they usually recognize their mistake quickly and then make good decisions to recover with as little cost or damage to their organization as possible.

Time-Management Skills Finally, effective managers usually have good time-management skills. **Time-management skills** refer to the manager's ability to prioritize work, to work efficiently, and to delegate appropriately. As already noted, managers face many different pressures and challenges. It is too easy for a manager to get bogged down doing work that can easily be postponed or delegated to others. When this happens, unfortunately, more pressing and higher-priority work may get neglected.[15] Jeff Bezos, CEO of Amazon.com, schedules all his meetings on three days a week, but insists on keeping the other two days clear so that he can pursue his own ideas and maintain the flexibility to interact with his employees informally.[16]

time-management skills The manager's ability to prioritize work, to work efficiently, and to delegate appropriately

MANAGEMENT IMPLICATIONS Effective managers recognize both the multiplicity of roles inherent in their jobs and the array of skills they need to perform those jobs. Few managers have equally strong skills in all areas. However, it is very useful for managers to understand their own strengths and weaknesses and to use this understanding to capitalize on their strengths while also working to overcome their weaknesses. For example, a manager with weak time-management skills might be sure to hire an especially effective assistant to help maintain an efficient schedule, while a manager with weak decision-making skills can use group decision making whenever possible to help utilize the skills of others.

■ *The Nature of Managerial Work*

We have already noted that managerial work does not follow an orderly, systematic progression through the workweek. Indeed, the manager's job is fraught with uncertainty, change, interruption, and fragmented activities. Mintzberg's study, mentioned earlier, found that in a typical day, CEOs were likely to spend 59 percent of their time in scheduled meetings, 22 percent doing "desk work," 10 percent in unscheduled meetings, 6 percent on the telephone, and the remaining 3 percent on tours of company facilities. (These proportions, of course, are different for managers at lower levels.) Moreover, the nature of managerial work continues to change in complex and often unpredictable ways.[17]

In addition, managers also perform a wide variety of tasks. In the course of a single day, for example, a manager might have to make a decision about the design of a new product, settle a complaint between two subordinates, hire a new assistant, write a report for the boss, coordinate a joint venture with an overseas colleague, form a task force to investigate a problem, search for information on the Internet, and deal with a labor grievance. Moreover, the pace of the manager's job can be relentless. She may feel bombarded by mail, telephone calls, and people waiting to see her. Decisions may have to be made quickly and plans formulated with little

time for reflection.[18] But in many ways, these same characteristics of managerial work also contribute to its richness and meaningfulness. Making critical decisions under intense pressure, and making them well, can be a major source of intrinsic satisfaction. And managers are usually well paid for the pressures they bear.

The Science and the Art of Management

Given the complexity inherent in the manager's job, a reasonable question relates to whether management is a science or an art. In fact, effective management is a blend of both science and art. And successful executives recognize the importance of combining both the science and the art of management as they practice their craft.[19] *Management InfoTech* details how electronic commerce is making it even more important for top managers to recognize the roles of science and art in the way they perform their jobs.

The Science of Management Many management problems and issues can be approached in ways that are rational, logical, objective, and systematic. Managers

MANAGEMENT INFOTECH

Making Decisions at the Speed of Technology

As technology picks up the pace of change in the business world, managers have to move faster than ever before and make decisions on the fly. In addition to Internet technology, managers are also dealing with challenges and opportunities brought on by advances in computing power and software. The result is full-speed-ahead management, where every second counts in the race to attract customers and beat the competition.

In the past, managers had more time to analyze and debate key decisions such as acquisitions. Today, the luxury of time is almost a memory. For example, Halsey Minor, chairman of CNET, an on-line publisher of technology news and reviews, acquired three companies in three weeks after learning that a rival was about to sell stock to the public. Minor knew that if he didn't act quickly, the competitor would soon have the financing to buy those companies and pose a stronger threat to CNET.

Technology helps managers stay connected with employees as well as with outside sources of information so they can get up to speed quickly. Even when they're out of the office, managers are never more than a click, chime, or buzz away, using wireless Internet access devices, mobile phones, laptop computers, and pagers.

Despite these tools, managers still have to make quick decisions that are all too often based on insufficient or incomplete data, as Bill Harris well knows. Harris is CEO of Intuit, the software company that produces Quicken and other finance programs. Competing against Microsoft and others, Harris uses his long-range vision of where the industry and the technology are headed to fuel lightning-fast decisions—even when the immediate future is unclear. For Harris, Minor, and other managers making decisions in today's technology-rich environment, management is clearly as much an art as it is a science.

You have to be deadly, brutally honest with yourself and others because if you let a problem fester a day or two, you'll see someone in your rear-view mirror coming after you.

*—Roger Siboni, CEO, Epiphany**

Reference: Geoffrey Colvin, "How to Be a Great E-CEO," *Fortune*, May 24, 1999, pp. 104–110 (*quote on p. 105).

can gather data, facts, and objective information. They can use quantitative models and decision-making techniques to arrive at "correct" decisions. And they need to take such a scientific approach to solving problems whenever possible, especially when they are dealing with relatively routine and straightforward issues. When Starbucks considers entering a new market, its managers look closely at a wide variety of objective details as they formulate their plans. Technical, diagnostic, and decision-making skills are especially important when practicing the science of management.

The Art of Management Even though managers may try to be scientific as much as possible, they must often make decisions and solve problems on the basis of intuition, experience, instinct, and personal insights. Relying heavily on conceptual, communication, interpersonal, and time-management skills, for example, a manager may have to decide between multiple courses of action that look equally attractive. And even "objective facts" may prove to be wrong. When Starbucks was planning its first store in New York, market research clearly showed that New Yorkers preferred drip coffee to more exotic espresso-style coffees. After first installing more drip coffee makers and fewer espresso makers than in their other stores, managers had to backtrack when New Yorkers lined up clamoring for espresso. Starbucks now introduces a standard menu and layout in all its stores, regardless of presumed market differences, and then makes necessary adjustments later. Thus, managers must blend an element of intuition and personal insight with hard data and objective facts.[20]

Becoming a Manager

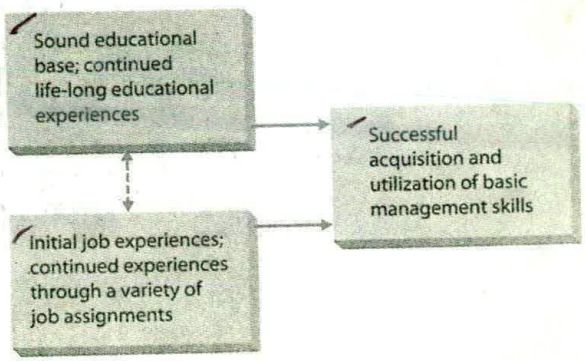
How does one acquire the skills necessary to blend the science and the art of management and thus become a successful manager? Although there are as many variations as there are managers, the most common path involves a combination of education and experience.[21] Figure 1.4 illustrates how this generally happens.

The Role of Education Many of you reading this book right now are doing so because you are enrolled in a management course at a college or university. Thus, you are acquiring management skills in an educational setting. When you complete the course (and this book), you will have a foundation for developing your management skills in more advanced courses. A college degree has become almost a requirement for career advancement in business, and virtually all CEOs in the United States have a college degree. MBA degrees are also common among successful executives today. More and more foreign universities, especially in Europe, are also beginning to offer academic programs in management.

Figure 1.4

Sources of Management Skills

Most managers acquire their skills as a result of education and experience. Though a few CEOs today do not hold college degrees, most students preparing for management careers earn college degrees and go on to enroll in MBA programs.



Even after obtaining a degree, most prospective managers have not seen the end of their management education. Many middle and top managers periodically return to campus to participate in executive or management development programs ranging in duration from a few days to several weeks. First-line managers also take advantage of extension and continuing education programs offered by institutions of higher education. A recent innovation in extended management education is the Executive MBA program offered by many top business schools, in which middle and top managers with several years of experience complete an accelerated program of study on weekends.[22] Finally, many large companies have in-house training programs for furthering managers' education. Regardless of the type of training, there is also a distinct trend toward educational development for managers conducted online.[23]

The primary advantage of education as a source of management skills is that, as a student, a person can follow a well-developed program of study, becoming familiar with current research and thinking on management. And many college students can devote full-time energy and attention to learning. On the negative side, management education is often very general to meet the needs of a wide variety of students, and specific know-how may be hard to obtain. Further, many aspects of the manager's job can be discussed in a book but cannot really be appreciated and understood until they are experienced.

The Role of Experience This book will help provide you with a solid foundation for enhancing your management skills. Even if you were to memorize every word in every management book ever written, however, you could not then step into a top-management position and be effective. The reason? Management skills must also be learned through experience. Most managers advanced to their present position from other jobs. Only by experiencing the day-to-day pressures a manager faces and by meeting a variety of managerial challenges can an individual develop insights into the real nature and character of managerial work.

For this reason most large companies, and many smaller ones as well, have developed management training programs for their prospective managers. People are hired from college campuses, from other organizations, or from the ranks of the organization's first-line managers and operating employees. These people are systematically assigned to a variety of jobs. Over time, the individual is exposed to most, if not all, of the major aspects of the organization. In this way the manager learns by experience. The training programs at some companies, such as Procter & Gamble, General Mills, and Shell Oil, are so good that other companies try to hire people who have gone through their training.[24] Even without formal training programs, managers can achieve success as they profit from varied experiences. For example, Herb Kelleher was a practicing attorney before he took over at Southwest Airlines. Of course, natural ability, drive, and self-motivation also play roles in acquiring experience and developing management skills.

Most effective managers learn their skills through a combination of education and experience. Some type of college degree, even if it is not in business administration, usually provides a foundation for a management career. The individual then gets his or her first job and subsequently progresses through a variety of man-

agement situations. During the manager's rise in the organization, occasional education "updates," such as management development programs, may supplement on-the-job experience. And increasingly, managers need to acquire international expertise as part of their personal development. As with general managerial skills, international expertise can also be acquired through a combination of education and experience.

MANAGEMENT IMPLICATIONS Students should recognize that even if certain material in a course does not seem relevant, they are still building an intellectual foundation for future growth. They should also recognize, however, that knowledge alone is usually not sufficient for success in the business world. Finally, students should also understand that just because they walk across the stage and get a diploma, their education is far from complete. People already in the business world, meanwhile, should not forget the importance of continuing to learn, regardless of how or where this learning occurs.

■ The Scope of Management

When most people think of managers and management, they think of profit-seeking organizations. Throughout this chapter we have used people like Christopher Galvin of Motorola, Howard Schultz of Starbucks, and Carly Fiorina of Hewlett-Packard as examples. But we also mentioned examples from sports, religion, and other fields in which management is essential. Indeed, any group of two or more persons working together to achieve a goal and having human, material, financial, or informational resources at its disposal requires the practice of management.

Managing in Profit-Seeking Organizations

Large Businesses Most of what we know about management comes from large profit-seeking organizations because their survival has long depended on efficiency and effectiveness. Examples of large businesses include industrial firms like Tenneco, BP Amoco, Toyota, Xerox, Unilever, and Levi Strauss; commercial banks like Citicorp, The Fuji Bank, and Wells Fargo; insurance companies like Prudential, State Farm, and Metropolitan Life; retailers like Sears, Safeway, and Kmart; transportation companies like Delta Air Lines and Consolidated Freightways; utilities like Pacific Gas & Electric and Consolidated Edison of New York; communication companies like CBS and The New York Times Company; and service organizations like Kelly Services, Kinder-Care Learning Centers, and Century 21 Real Estate.

Small and Start-Up Businesses Although many people associate management primarily with large businesses, effective management is also essential for small businesses, which play an important role in the country's economy. In fact, most of this nation's businesses are small. In some respects, effective management is more important in a small business than in a large one. A large firm such as Texaco or



Management is an important part of any organization, regardless of its size or mission. Luke Davis combines his business acumen with technical skills as he reaches out to a wide array of different kinds of organizations and offers his services as a web site designer. Here, for instance, he is demonstrating the new web site he designed for the Tyburn Convent in London. Davis has become quite successful by focusing on diverse kinds of religious, civic, and social organizations.

Monsanto can easily recover from losing several thousand dollars on an incorrect decision; even losses of millions of dollars would not threaten their long-term survival. But a small business may ill afford even a much smaller loss. Of course, some small businesses become big ones. Compaq Computer Corporation, for example, was started by three men in 1982. By 1999 it had become one of the largest businesses in the United States, with annual sales of over $31 billion.

International Management In recent years, the importance of international management has increased dramatically. The list of U.S. firms doing business in other countries is staggering. Exxon Mobil, for example, derives almost 75 percent of its revenues from foreign markets, and Coca-Cola derives more than 80 percent of its sales from foreign markets. Other major U.S. exporters include General Motors, General Electric, Boeing, and Caterpillar. And even numbers like Ford's are deceptive. For example, the automaker has large subsidiaries based in many European countries whose sales are not included as foreign revenue. Moreover, a number of major firms that do business in the United States have their headquarters in other countries. Firms in this category include the Royal Dutch/Shell Group (the Netherlands), Fiat S.P.A. (Italy), Nestlé SA (Switzerland), and Massey-Ferguson Inc. (Canada). International management is not confined, however, to profit-seeking organizations. Several international sports federations (such as Little League Baseball), branches (embassies) of the federal government, and the Roman Catholic Church are established in most countries as well. In some respects, the military was one of the first multinational organizations. International management is covered in depth in Chapter 5.

Managing in Not-for-Profit Organizations

Intangible goals such as education, social services, public protection, and recreation are often the primary aim of not-for-profit organizations. Examples include United Way of America, the U.S. Postal Service, Girl Scouts of the United States of America, the International Olympic Committee, art galleries, museums, and the Public Broadcasting System. Although these and similar organizations may not

have to be profitable to attract investors, they must still employ sound management practices if they are to survive and work toward their goals.[25] And they must handle money in an efficient and effective way. If the United Way were to begin to spend large portions of its contributions on administration, contributors would lose confidence in the organization and make their charitable donations elsewhere.

Government Organizations The management of government organizations and agencies is often regarded as a separate specialty: public administration. Government organizations include the Federal Trade Commission, the Environmental Protection Agency, the National Science Foundation, all branches of the military, state highway departments, and federal and state prison systems. Tax dollars support government organizations, and politicians and citizens' groups are acutely sensitive to the need for efficiency and effectiveness.

Educational Organizations Public and private schools, colleges, and universities all stand to benefit from the efficient use of resources. Taxpayer "revolts" in states such as California and Massachusetts have drastically cut back the tax money available for education, forcing administrators to make tough decisions about allocating remaining resources.

Healthcare Facilities Managing healthcare facilities such as clinics, hospitals, and HMOs (health maintenance organizations) is now considered a separate field of management. Here, as in other organizations, scarce resources dictate an efficient and effective approach. In recent years many universities have established healthcare administration programs to train managers as specialists in this field.

Management in Nontraditional Settings Good management is also required in nontraditional settings to meet established goals. To one extent or another, management is practiced in religious organizations, terrorist groups, fraternities and sororities, organized crime, street gangs, neighborhood associations, and households. In short, as we noted at the beginning of this chapter, management and managers have a profound influence on all of us.

MANAGEMENT IMPLICATIONS Management is applicable to all organizations. Thus, when a manager leaves work and goes to a weekly meeting of a civic or church group, to an organizing meeting for a child's youth soccer league, or to do volunteer work in a political campaign, he or she should keep in mind that many of the same functions used in a business can also be used in these other organizations as well. And while each organization has its own unique goals and mission, effective management can help every organization better accomplish those goals and more successfully realize its mission.

Summary of Key Points

Management is a set of activities (including planning and decision making, organizing, leading, and controlling) directed at an organization's resources (human, financial, physical, and information) with the aim of achieving organizational goals in an efficient and effective manner. A manager is someone whose primary responsibility is to carry out the management process within an organization.

The basic activities that comprise the management process are planning and decision making (determining courses of action), organizing (coordinating activities and resources), leading (motivating and managing people), and controlling (monitoring and evaluating activities). These activities are not performed on a systematic and predictable schedule.

Managers can be differentiated by level and by area. By level, we can identify top, middle, and first-line managers. Managers differentiated by area include marketing, financial, operations, human resource, administrative, and specialized managers.

Managers have ten basic roles to play: three interpersonal roles (figurehead, leader, and liaison), three informational roles (monitor, disseminator, and spokesperson), and four decisional roles (entrepreneur, disturbance handler, resource allocator, and negotiator). Effective managers also tend to have technical, interpersonal, conceptual, diagnostic, communication, decision-making, and time-management skills. The manager's job is characterized by varied, unpredictable, nonroutine, and fragmented work, often performed at a relentless pace. Managers also receive a variety of intrinsic and extrinsic rewards.

The effective practice of management requires a synthesis of science and art, that is, a blend of rational objectivity and intuitive insight. Most managers attain their skills and positions through a combination of education and experience.

Management processes are applicable in a wide variety of settings, including profit-seeking organizations (large, small, and start-up businesses and international businesses) and not-for-profit organizations (government organizations, educational organizations, healthcare facilities, and nontraditional organizations).

Discussion Questions

Questions for Review

1. What are the four basic activities that comprise the management process? How are they related to one another?
2. Identify different kinds of managers by both level and area in the organization.
3. Briefly describe the ten managerial roles identified by Mintzberg. Give an example of each.
4. Identify the different important skills that help managers succeed. Give an example of each.

Questions for Analysis

5. The text notes that management is both a science and an art. Is one of these more important than the other? Under what circumstances might one characteristic be more important than the other?
6. Recall a recent group project or task in which you have participated. Explain how each of the four basic management functions was performed.
7. Some people argue that CEOs in the United States are paid too much. Find out the pay

for a CEO and discuss whether you think he or she is overpaid.

Questions for Application

8. Interview a manager from a local organization. Learn about how he or she performs each of the functions of management, the roles he or she plays, and the skills necessary to do the job.
9. Locate a recent business management publication like *Fortune, Business Week,* or *Forbes.* Read an article in the magazine that profiles a specific manager or executive. Identify as many examples in the article as you can that illustrate management functions, roles, and/or skills.
10. Watch a television program that involves an organization of some type. Good choices include *N.Y.P.D. Blue, The West Wing, Spin City,* or *E.R.* Identify as many management functions, skills, and roles as you can.

BUILDING EFFECTIVE *technical* SKILLS

Exercise Overview

Technical skills refer to the manager's abilities to accomplish or understand work done in an organization. More and more managers today are realizing that having the technical ability to use the Internet is an important part of communication, decision making, and other facets of their work. This exercise helps you see the link between the Internet and management.

Exercise Background

The so-called information highway, or the Internet, is an interconnected network of information and information-based resources accessed by computers, computer systems, and other devices. While electronic mail was perhaps the first widespread application of the Internet, increasingly popular applications are based on home pages and search engines.

A home page is a file (or set of files) created by an individual, business, or other entity. It contains whatever information its creator chooses to include. For example, a company might create a home page for itself that includes its logo, its address and telephone number, information about its products and services, and so forth. An individual seeking employment might create a home page that includes a résumé and a statement of career interests. Home pages are indexed by key words chosen by their creators.

A search engine is a system through which an Internet user can search for home pages according to their indexed key words. Suppose an individual is interested in knowing more about art collecting. Key words that might logically be linked to home pages related to this interest include *art, artists, galleries,* and *framing.* A search engine will take these key words and provide a listing of all home pages that are indexed to them. The user can then browse each page to see what information it contains. Popular search engines include Yahoo, Google, and Webcrawler.

Exercise Task

1. Review the content of this chapter and identify three or four general management-related terms (i.e., *management, organization, business*).
2. Using whichever search engine you prefer, conduct a search for these terms.
3. Now select a more specific management topic and search for two or three specific terms (if you cannot think of any terms, scan the margin notes in this book).
4. Finally, select three or four companies and search for their home pages.
5. Comment on the relative ease and value of each of these searches from the standpoint of a practicing manager.

BUILDING EFFECTIVE *diagnostic* SKILLS

Exercise Overview

Diagnostic skills are those that enable a manager to visualize the most appropriate response to a situation. This exercise will encourage you to apply your diagnostic skills to a real business problem and to assess the possible consequences of different courses of action.

Exercise Background

For some time now college textbook publishers have been struggling with a significant problem. The subject matter that comprises a particular field, such as management, chemistry, or history, continues to increase in size, scope, and complexity. Thus, authors feel compelled to add more and more information to new editions of their textbooks. Publishers have also sought to increase the visual sophistication of their texts by adding more color and photographs. At the same time, some instructors find it increasingly difficult to cover the material in longer textbooks. Moreover, longer and more attractive textbooks cost more money to produce, resulting in higher selling prices to students.

Publishers have considered a variety of options to confront this situation. One option is to work with authors to produce shorter and more economical books (such as this one). Another option is to cut back on the complimentary supplements that publishers provide to instructors (such as videos and color transparencies) as a way of lowering the overall cost of producing a book. Another option is to eliminate traditional publishing altogether and provide educational resources via CD-ROM, the Internet, or other new media.

Confounding this situation, of course, is cost. Profit margins in the industry are such that managers feel the need to be cautious and conservative. That is, they cannot do everything and must not risk alienating their users by taking too radical a step. Remember, too, that publishers must consider the concerns of three different sets of customers: the instructors who make adoption decisions, the bookstores that buy educational materials for resale (at a retail markup), and students who buy the books for classroom use and then often resell them back to the bookstore.

Exercise Task

With this background in mind, respond to the following:

1. Discuss the pros and cons of each option currently being considered by textbook publishers.
2. Identify the likely consequences of each option.
3. Can you think of other alternatives that publishers in the industry should consider?
4. What specific recommendations would you make to an executive in a publishing company regarding this set of issues?

BUILDING EFFECTIVE *conceptual* SKILLS

Exercise Overview

Conceptual skills form the manager's ability to think in the abstract. This exercise will help you extend your conceptual skills by identifying potential generalizations of management functions, roles, and skills for different kinds of organizations.

Exercise Background

This introductory chapter discusses four basic management functions, ten common managerial roles, and seven vital management skills. The chapter also stresses that management is applicable across many of different kinds of organizations.

Identify one large business, one small business, one educational organization, one health-care organization, and one government organization. These might be organizations about which you have some personal knowledge or simply organizations that you recognize. Now imagine yourself in the position of a top manager in each organization.

Write the names of the five organizations across the top of a sheet of paper. List the four functions, ten roles, and seven skills down the left side of the paper. Now think of a situation, problem, or opportunity relevant to the intersection of each row and column on the paper. For example, how might a manager in a government organization engage in planning and need diagnostic skills? Similarly, how might a manager in a small business carry out the organizing function and play the role of negotiator?

Exercise Task

1. What meaningful similarities can you identify across the five columns?
2. What meaningful differences can you identify across the five columns?
3. Based on your assessment of the similarities and differences as identified in Exercise Tasks 1 and 2, how easy or difficult do you think it might be for a manager to move from one type of organization to another?

CHAPTER CLOSING CASE

MANAGING IN A WIRED WORLD

Although Amazon.com is not yet a decade old, it's already a case study in Internet success. Founded by Jeff Bezos in 1995 as an on-line bookstore, Seattle-based Amazon rings up more than $1.6 billion in e-commerce sales every year. First books, then music and videos, and now software, screwdrivers, and sofas—Amazon has grown into a virtual department store for its 17 million on-line customers worldwide. Even as successful chains such as Barnes and Noble and Wal-Mart try to grab a larger piece of the on-line retailing pie, CEO Bezos has maintained Amazon's market leadership and customer base through constant innovation.

Nothing like Amazon existed when Bezos was researching software and the Internet for a New York City firm in 1994. He became intrigued by the business possibilities of selling books on the World Wide Web in much the same way that mail-order firms sell books by mail. This idea proved so compelling that Bezos quickly quit his job, raised money from family and friends, wrote a business plan, and moved to Seattle to be located near a major book wholesaler. One year later, Amazon.com was open for business. In its first month, without advertising or public relations, the site attracted customers from every U.S. state and more than forty other countries.

In those early days, the giant bookstore chains paid little attention to Amazon. Within two years, however, Amazon's discount prices, free e-mail book reviews, and easy search capabilities had attracted so many shoppers and so much media coverage that competitors started scrambling to open their own Internet book stores. But Amazon's established reputation and loyal customer following were major hurdles for rivals to overcome. In fact, despite aggressive promotions and pricing, Barnesandnoble.com is still trying to catch up to Amazon's on-line sales and sizable customer base.

Meanwhile, Bezos has expanded into all kinds of products by buying stakes in e-commerce companies such as drugstore.com and pets.com. He's also set up an auction section on Amazon to tap the excitement generated by the success of eBay, the first Internet auction site. In addition, he made room on the Amazon site for zShops, an area where smaller businesses can, for a fee, sell products.

One reason for Amazon's success is founder Bezos's action-oriented management style. Although he carefully plans his company's future moves, he also wants to avoid the paralysis that can come from endless analysis and deliberation. As an e-commerce pioneer,

Bezos is accustomed to making speedy decisions to take advantage of unexpected or fleeting opportunities. He encourages everyone at Amazon to do the same, even if that means an occasional misstep. Working on Internet time, Bezos would rather lead his troops into the unknown, and fix problems later, than slow down now.

To continue growing and innovating, Amazon must keep recruiting, training, and motivating good managers and employees. Bezos gets personally involved in hiring decisions about top managers, who he trusts to hire the people who will work under them. Because he knows that a skilled workforce is critical to Amazon's success, Bezos asks probing questions about hiring techniques when he interviews top management candidates.

Still, Bezos carves out precious time from his hectic management schedule to surf the Web, click around the Amazon site, and, on occasion, wander through shopping malls in search of new ideas. To stay in touch, he goes out of his way to thank specific employees for their efforts, and he reads e-mail messages from customers to find out what they like and don't like. About one-third of the CEO's time is devoted to visiting Amazon's national network of distribution centers, where he answers employee questions and reinforces the company's six "core values": customer obsession, ownership, bias for action, frugality, high hiring bar, and innovation.

Every December, Bezos and his entire management team pitch in to meet the holiday rush. By wrapping packages for customer shipments or answering customer service phone calls, they all get a better sense of what Amazon's first-line managers and employees face—and what their customers want. This yearly tradition of hands-on experience also rekindles the managers' sense of purpose, no small consideration in an industry where change is the only constant.

Case Questions

1. Which managerial skills does Jeff Bezos appear to be emphasizing at Amazon?
2. How does Bezos carry out his interpersonal, informational, and decisional roles at Amazon?
3. Why are communication skills particularly vital for managers at a fast-growing firm such as Amazon?

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CHAPTER 2

Traditional and Contemporary Issues and Challenges

OPENING INCIDENT

When Leslie Wexner opened the first Limited clothing store in an Ohio shopping mall in 1963, he had no idea that his fledgling business would grow to include thousands of specialty stores comprised of such well-known brands as Express, Abercrombie & Fitch, and Victoria's Secret. But by 1993 his firm was running out of steam and rivals like Gap and J. Crew were attracting more and more attention. Now, though, Limited seems to have righted itself and is again moving toward the forefront of the specialty retailing industry. The reasons for the decline and rebirth of Limited underscore the importance of maintaining compatibility between a manager's style and the organization's situation.

When Wexner started Limited, he was clearly an entrepreneur and his focus was primarily on business growth and expansion. He pursued this growth in two ways. First, he continually looked for ways to branch out and systematically launched several different chains. Second, he grew each chain rapidly by opening new stores at a breakneck pace. Part of Wexner's strategy was to place his stores adjacent to one another in large shopping malls. Thus, customers might walk from The Limited to Express to Lerner, buying clothes at each without realizing that they were actually buying from the same company.

Wexner created or bought several major chains, including The Limited, Express, Lerner New York, Lane Bryant, Henri Bendel, Victoria's Secret, Bath & Body Works, Structure, and Abercrombie & Fitch. Wexner himself also jumped from business to business, leaving the day-to-day operations in the hands of others. His focus, meanwhile, continued to be on growth and expansion as he continued to buy other chains, retool his existing chains, and build more and more stores. In some malls, for instance, Limited stores might comprise as much as 25 percent of total square footage.

But in the early 1990s troubles began to surface. Sales declined in some markets, for example, and costs and operating expenses began to creep up. Moreover, competitors such as Gap and Old Navy started attracting more customers and were increasingly the store of choice for hip young consumers. Investors also began to get nervous and the company's stock price plummeted. And some experts openly questioned whether or not Limited could be turned around.

Wexner recognized that he had a problem, but he also didn't know quite how to define it. So, starting in the mid-1990s, he began to visit several of the very best managers in the United States, including such lumi-

"I was an entrepreneur. . . . I think what went wrong was the . . . entrepreneurial style wasn't working."

—Leslie Wexner, founder and CEO of Limited

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- **Justify the importance of history and theory to management and discuss precursors to modern management theory.**
- **Summarize and evaluate the classical perspective on management, including scientific and administrative management, and note its relevance to contemporary managers.**
- **Summarize and evaluate the behavioral perspective on management, including the Hawthorne studies, human relations movement, and organizational behavior, and note its relevance to contemporary managers.**
- **Summarize and evaluate the quantitative perspective on management, including management science and operations management, and note its relevance to contemporary managers.**
- **Discuss the systems and contingency approaches to management and explain their potential for integrating the other areas of management.**
- **Identify and describe contemporary management issues and challenges.**

naries as Sam Walton (founder of Wal-Mart), Jack Welch (CEO of General Electric), and Wayne Calloway (former CEO of PepsiCo). And he gradually began to recognize the problem: Limited had stopped being an entrepreneurial start-up operation and had evolved into a mature major business operation, yet he was still trying to run it using the same managerial style he had used when he had only a few dozen stores. Clearly, he realized, running a global company with more than five thousand stores, generating annual revenues of $9.3 billion, and employing 127,000 people required a different approach than he had been using.

So Wexner immersed himself in a crash-course on how to manage a mature business. He learned about operations and financial control, revamped the firm's organization design, and implemented a more professional approach to human resource management. He also began to focus more on profit margins and acknowledged that sometimes you have to close or sell underperforming stores and businesses. And he learned the difference between competitive strategy and growth strategy.

By the end of the decade, signs were clearly pointing to a resurgence at Limited. For example, same-store sales are again increasing and the firm's stock price reached a record high in mid-2000. But Wexner is quick to point out that, even though he has helped reinvent his company, that he doesn't want to make the same mistake again. Hence, he has committed himself to staying abreast of modern management techniques and contemporary management thought.[1]



CHAPTER OUTLINE

- **The Role of Theory and History in Management**
  - The Importance of Theory and History
  - Precursors to Management Theory
- **The Classical Management Perspective**
  - Scientific Management
  - Administrative Management
  - The Classical Management Perspective Today
- **The Behavioral Management Perspective**
  - The Hawthorne Studies
  - The Human Relations Movement
  - The Emergence of Organizational Behavior
  - The Behavioral Management Perspective Today
- **The Quantitative Management Perspective**
  - Management Science
  - Operations Management
  - The Quantitative Management Perspective Today
- **Integrating Perspectives for Managers**
  - The Systems Perspective
  - The Contingency Perspective
  - An Integrating Framework
- **Contemporary Management Issues and Challenges**
  - Contemporary Applied Perspectives
  - Contemporary Management Challenges

One lesson managers can learn from Leslie Wexner is that as circumstances change, so too must they be prepared to change their approach to running their business. It is critically important that all managers focus on today's competitive environment and how that environment will change tomorrow. But it is also important that they use the past as context. Managers in a wide array of organizations can learn both effective and less effective practices and strategies by understanding what managers have done in the past. Indeed, history plays an important role in many businesses today, and more and more managers are recognizing that the lessons of the past are important ingredients of future success.

This chapter provides an overview of traditional management thought so that you, too, can better appreciate the importance of history in today's business world. We set the stage by establishing the historical context of management. We then discuss the three traditional management perspectives—classical, behavioral, and quantitative. Next we describe the systems and contingency perspectives as approaches that help integrate the three traditional perspectives. Finally, we introduce and discuss a variety of contemporary management issues and challenges.

The Role of Theory and History in Management

Practicing managers are increasingly seeing the value of theory and history in their work. In this section we first explain why theory and history are important and then identify important precursors to management theory.

The Importance of Theory and History

Some people question the value of history and theory. Their arguments are usually based on the assumptions that history has no relevance to contemporary society



No one knows the origins of Stonehenge, a mysterious circle of huge stones rising from Salisbury Plain in England. But one fact that is known is that whoever built the ancient monument must have relied heavily on a variety of management tools and techniques. For example, the stones were probably cut over 300 miles away, in Wales, and transported to Salisbury Plain. This enormous feat alone would have required careful planning and coordination and the united efforts of hundreds of laborers.

and that theory is abstract and of no practical use. In reality, however, both theory and history are important to all managers today.

Why Theory? A theory is simply a conceptual framework for organizing knowledge and providing a blueprint for action. Although some theories seem abstract and irrelevant, others appear very simple and practical. Management theories, used to build organizations and guide them toward their goals, are grounded in reality. Practically any organization that uses assembly lines (such as Emerson Electric, Black & Decker, and Fiat) is drawing on what we describe later in this chapter as scientific management. Many organizations, including Monsanto, Texas Instruments, and Seiko, use the behavioral perspective (also introduced later) to improve employee satisfaction and motivation. And naming a large company that does not use one or more techniques from the quantitative management perspective would be difficult. For example, retailers like Kroger and Target Stores routinely use operations management to determine how many check-out stands they need. In addition, most managers develop and refine their own theories of how they should run their organizations and manage the behavior of their employees.

For example, Andrew Grove, CEO of Intel Corp., has developed his own operating theory of organizations. The basis of his theory is that organizations need to focus on continually becoming more agile and responsive to their environment. By implementing his theory, Grove has transformed Intel into just such a company. As a direct result of Grove's keen understanding of his business and his ability to implement his operating theory, Intel has become the world's largest manufacturer of semiconductors.[3]

Why History? An awareness and understanding of important historical developments are also important to contemporary managers.[4] Understanding the historical context of management provides a sense of heritage and can help managers avoid the mistakes of others. Most courses in U.S. history devote time to business and economic developments in this country, including the Industrial Revolution, the early labor movement, and the Great Depression, and to captains of U.S. industry such as Cornelius Vanderbilt (railroads), John D. Rockefeller (oil), and Andrew Carnegie (steel). The contributions of those and other industrialists left a profound imprint on contemporary culture.[5]

Many managers are also realizing that they can benefit from a greater understanding of history in general. For example, Ian M. Ross of AT&T Bell Laboratories cites *The Second World War* by Winston Churchill as a major influence on his approach to leadership. Other books often mentioned by managers for their relevance to today's business problems include such classics as Plato's *Republic*, Homer's *Iliad*, and Machiavelli's *The Prince*.[6] And in recent years, new business history books have appeared that are directed more at women managers and the lessons they can learn from the past.[7]

Managers at Wells Fargo & Company clearly recognize the value of history. For example, the company maintains an extensive archival library of its old banking documents and records and even employs a full-time corporate historian. As part of their orientation and training, new managers at Wells Fargo take courses to

become acquainted with the bank's history.[8] Similarly, Polaroid, Shell Oil, Levi Strauss, Ford, Lloyd's of London, Disney, Honda, and Unilever all maintain significant archives about their past and frequently evoke images from that past in their orientation and training programs, advertising campaigns, and other public relations activities.

Precursors to Management Theory

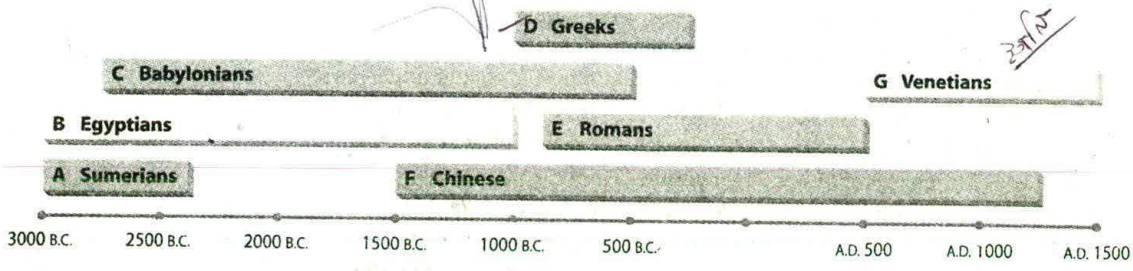
Even though large businesses have been around for only a few hundred years, management has been practiced for thousands of years. By examining management in antiquity and identifying some of the first management pioneers, we set the stage for a more detailed look at the emergence of management theory and practice over the last one hundred years.

Management in Antiquity The practice of management can be traced back thousands of years. The Egyptians used the management functions of planning, organizing, and controlling when they constructed the great pyramids. Alexander the Great employed a staff organization to coordinate activities during his military campaigns. The Roman Empire developed a well-defined organizational structure that greatly facilitated communication and control. Management practices and concepts were discussed by Socrates in 400 B.C.; Plato described job specialization in 350 B.C., and Alfarabi listed several leadership traits in A.D. 900.[9] Figure 2.1 is a simple time line showing a few of the most important management breakthroughs and practices over the last four thousand years.

Figure 2.1

Management in Antiquity

Management has been practiced for thousands of years. For example, the ancient Babylonians used management in governing their empire, and the ancient Romans used management to facilitate communication and control throughout their far-flung territories. The Egyptians used planning and controlling techniques in the construction of their pyramids.



A Used written rules and regulations for governance

B Used management practices to construct pyramids

C Used extensive set of laws and policies for governance

D Used different governing systems for cities and state

E Used organized structure for communication and control

F Used extensive organization structure for government agencies and the arts

G Used organization design and planning concepts to control the seas

Early Management Pioneers In spite of this history, however, management per se was not given serious attention for several centuries. Indeed, the study of management did not begin until the nineteenth century. Robert Owen (1771–1858), a British industrialist and reformer, was one of the first managers to recognize the importance of an organization's human resources. Until his era, factory workers were generally viewed in much the same way that machinery and equipment were. A factory owner himself, Owen believed that workers deserved respect and dignity. He implemented better working conditions, a higher minimum working age for children, meals for employees, and reduced work hours. He assumed that giving more attention to workers would pay off in increased output.

Whereas Owen was primarily interested in employee welfare, Charles Babbage (1792–1871), an English mathematician, focused his attention on efficiencies of production. His primary contribution was his book, *On the Economy of Machinery and Manufactures*.[10] Babbage placed great faith in division of labor and advocated the application of mathematics to problems such as the efficient use of facilities and materials. In a sense, his work was a forerunner to both the classical and quantitative management perspectives. Nor did he overlook the human element. He understood that a harmonious relationship between management and labor could serve to benefit both, and he favored such devices as profit-sharing plans. In many ways, Babbage was an originator of modern management theory and practice.

MANAGEMENT IMPLICATIONS While all managers should obviously focus their attention on present-day and future issues, they should also remember the lessons from the past. An understanding of business history in general and the history of their own company in particular can help them better understand why contemporary circumstances have developed as they have, and also provide useful ideas for enhancing the effectiveness of their organization.[11] In addition, managers should recognize the value of theory as a way of organizing and thinking about information and ideas.[12]

■ The Classical management Perspective

At the dawn of the twentieth century, the preliminary ideas and writings of these and other managers and theorists converged with the emergence and evolution of large-scale businesses and management practices to create interest and focus attention on how businesses should be operated. The first important ideas to emerge are now called the **classical management perspective**. This perspective actually includes two different viewpoints: scientific management and administrative management.

classical management perspective Consists of two distinct branches—scientific management and administrative management

Scientific Management

Productivity emerged as a serious business problem during the first few years of the twentieth century. Business was expanding and capital was readily available,



Frederick W. Taylor was a pioneer in the field of labor efficiency. He introduced numerous innovations in how jobs were designed and how workers were trained to perform them. These innovations resulted in higher-quality products and improved employee morale. Taylor also formulated the basic ideas of scientific management.

but labor was in short supply. Hence, managers began to search for ways to use existing labor more efficiently. In response to this need, experts began to focus on ways to improve the performance of individual workers. Their work led to the development of **scientific management**. Some of the earliest advocates of scientific management included Frederick W. Taylor (1856–1915), Frank Gilbreth (1868–1924), Lillian Gilbreth (1878–1972), Henry Gantt (1861–1919), and Harrington Emerson (1853–1931).[13] Taylor played the dominant role.

scientific management Concerned with improving the performance of individual workers

soldiering Employees deliberately working at a pace slower than their capabilities

One of Taylor's first jobs was as a foreman at the Midvale Steel Company in Philadelphia. There he observed what he called **soldiering**—employees deliberately working at a pace slower than their capabilities. Taylor studied and timed each element of the steelworkers' jobs. He determined what each worker should be producing, and then he designed the most efficient way of doing each part of the overall task. Next he implemented a piecework pay system. Rather than paying all employees the same wage, he began increasing the pay of each worker who met and exceeded the target level of output set for his or her job.

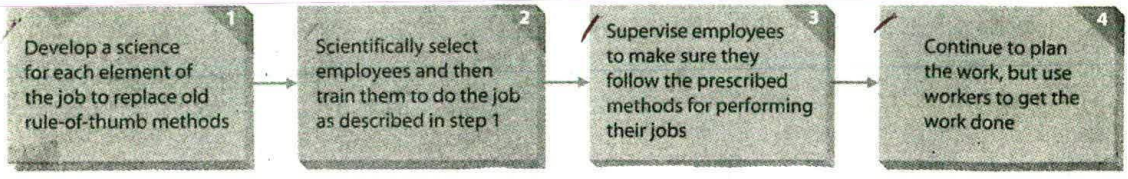
After Taylor left Midvale, he worked as a consultant for several companies, including Simonds Rolling Machine Company and Bethlehem Steel. At Simonds he studied and redesigned jobs, introduced rest periods to reduce fatigue, and implemented a piecework pay system. The results were higher quality and quantity of output and improved morale. At Bethlehem Steel, Taylor studied efficient ways of loading and unloading rail cars and applied his conclusions with equally impressive results. During these experiences, he formulated the basic ideas that he called scientific management. Figure 2.2 illustrates the basic steps Taylor suggested. He believed that managers who followed his guidelines would improve the efficiency of their workers.[14]

Taylor's work had a major impact on U.S. industry. By applying his principles, many organizations achieved major gains in efficiency. Taylor was not without his detractors, however. Labor argued that scientific management was just a device to

Figure 2.2

Steps in Scientific Management

Frederick Taylor developed this system of scientific management, which he believed would lead to a more efficient and productive workforce. Bethlehem Steel was among the first organizations to profit from scientific management and still practices some parts of it today.



get more work from each employee and to reduce the total number of workers needed by a firm. There was a congressional investigation into Taylor's ideas, and evidence suggests that he falsified some of his findings.[15] Nevertheless, Taylor's work left a lasting imprint on business.[16]

Frank and Lillian Gilbreth, contemporaries of Taylor, were a husband-and-wife team of industrial engineers. One of Frank Gilbreth's most interesting contributions was to the craft of bricklaying. After studying bricklayers at work, he developed several procedures for doing the job more efficiently. For example, he specified standard materials and techniques, including the positioning of the bricklayer, the bricks, and the mortar at different levels. The results of these changes were a reduction from eighteen separate physical movements to five and an increase in output of about 200 percent. Lillian Gilbreth made equally important contributions to several different areas of work, helped shape the field of industrial psychology, and made substantive contributions to the field of personnel management. Working individually and together, the Gilbreths developed numerous techniques and strategies for eliminating inefficiency. They applied many of their ideas to their family and documented their experiences raising twelve children in the book and movie *Cheaper by the Dozen*. Of course, as illustrated in the cartoon, concerns for efficiency can be carried too far!



Harley Schwadron

All organizations, of course, should be concerned about efficiency and productivity. But as this cartoon illustrates, they might sometimes go a bit too far! While there are no organizations that are likely to go as far as this one, there are work sites today that forbid talking among employees at work, prohibit any personal telephone calls, and require employees to have permission to take a restroom break. Managers responsible for such practices would most likely argue that employees should be doing nothing but work when they are being paid and that they can't be trusted to exercise self-control about work, and so they must be tightly supervised and strictly controlled.

Henry Gantt, another contributor to scientific management, was an associate of Taylor at Midvale, Simonds, and Bethlehem Steel. Later, working alone, he developed other techniques for improving worker output. One, called the Gantt chart, is still used today. A Gantt chart is essentially a means of scheduling work and can be generated for each worker or for a complex project as a whole. Gantt also refined Taylor's ideas about piecework pay systems.

Like Taylor, the Gilbreths, and Gantt, Harrington Emerson was also a management consultant. He made quite a stir in 1910 when he appeared before the Interstate Commerce Commission to testify about a rate increase requested by the railroads. As an expert witness, Emerson asserted that the railroads could save $1 million a day by using scientific management. He was also a strong advocate of specialized management roles in organizations, believing that job specialization was as relevant to managerial work as it was to operating jobs.

Administrative Management

Whereas scientific management deals with the jobs of individual employees, **administrative management** focuses on managing the total organization. The primary contributors to administrative management were Henri Fayol (1841–1925), Lyndall Urwick (1891–1983), Max Weber (1864–1920), and Chester Barnard (1886–1961).

administrative management Focuses on managing the total organization

Henri Fayol was administrative management's most articulate spokesperson. A French industrialist, Fayol was unknown to U.S. managers and scholars until his most important work, *General and Industrial Management*, was translated into English in 1930.[17] Drawing on his own managerial experience, he attempted to systematize the practice of management to provide guidance and direction to other managers. Fayol also was the first to identify the specific managerial functions of planning, organizing, leading, and controlling. He believed that these functions accurately reflect the core of the management process. Most contemporary management books (including this one) still use this framework, and practicing managers agree that these functions are critical parts of their jobs.

After a career as a British army officer, Lyndall Urwick became a noted management theorist and consultant. He integrated scientific management with the work of Fayol and other administrative management theorists. He also advanced modern thinking about the functions of planning, organizing, and controlling. Like Fayol, he developed a list of guidelines for improving managerial effective-

MANAGING IN AN *e*-BUSINESS WORLD

B2B Sites Bring Organizational Changes

Max Weber developed his ideas about bureaucracy many decades before computers became commonplace business tools. Yet he would have been pleased at the way business-to-business (B2B) Web sites are improving organizational efficiency through more productive purchasing.

Traditionally, the purchasing department was considered a backwater compared with line positions in production or other departments. Today, however, purchasing agents are at the forefront of an Internet-driven revolution. E-purchasing—buying goods and services via B2B Web sites—is helping companies slash costs and streamline their organizations.

Here's one example. When Norfolk Southern Railway needed contractors to handle repair work, employees would spend days calling construction companies to solicit bids. These days, the railroad posts simple requests for bids on RailNet-USA.com, a B2B site for rail contractors. With e-purchasing, the railroad receives more bids and more competitive pricing in far less time, which frees employees to work on other tasks.

The potential savings are enormous. John Deere, a leading farm-equipment manufacturer, will shave 5 percent off the cost of supplies and components through e-purchasing—a savings of $1 billion within five years. United Technologies has already sliced its supplier bills by more than $700 million. In some industries, e-purchasing could reduce supply costs as much as 20 percent.

Just as important, e-purchasing through B2B sites is shaking up the organizational pyramid. Processing a single transaction, from the initial requisition to the final payment, used to require a stream of paperwork handled as many as nine times. Now e-purchasing is trimming the paperwork and reducing the handling to as few as three steps. General Electric says that getting rid of so much paperwork will reduce transaction costs by at least $49 per purchase. And, with a simpler, speedier process, companies will need fewer employees in purchasing. Once John Deere completes its move to e-purchasing, its purchasing department will drop from 1,200 to 900 or fewer employees. Max Weber would have applauded such bottom-line savings.

> ***Collectively, [e-purchasing agents] will drive efficiency across industries and geographies.***
>
> *—Leah Knight, e-business analyst**

References: Laura Cohn, "B2B: The Hottest Net Bet Yet?" *Business Week*, January 17, 2000, pp. 36–37; Del Jones, "E-purchasing Saves Businesses Billions," *USA Today*, February 7, 2000, pp. 1B–2B (*quote on p. 2B).

Table 2.1

The Classical Management Perspective

General Summary	The classical management perspective had two primary thrusts. Scientific management focused on employees within organizations and on ways to improve their productivity. Noted pioneers of scientific management were Frederick Taylor, Frank and Lillian Gilbreth, Henry Gantt, and Harrington Emerson. Administrative management focused on the total organization and on ways to make it more efficient and effective. Prominent administrative management theorists were Henri Fayol, Lyndall Urwick, Max Weber, and Chester Barnard.
Contributions	Laid the foundation for later developments in management theory. Identified important management processes, functions, and skills that are still recognized today. Focused attention on management as a valid subject of scientific inquiry.
Limitations	More appropriate for stable and simple organizations than for today's dynamic and complex organizations. Often prescribed universal procedures that are not appropriate in some settings. Even though some writers (such as Lillian Gilbreth and Chester Barnard) were concerned with the human element, many viewed employees as tools rather than resources.

ness. Urwick is noted not so much for his own contributions as for his synthesis and integration of the work of others.

Although Max Weber lived and worked at the same time as Fayol and Taylor, his contributions were not recognized until some years had passed. Weber was a German sociologist, and his most important work was not translated into English until 1947.[18] Weber's work on bureaucracy laid the foundation for contemporary organization theory, discussed in detail in Chapter 12. The concept of bureaucracy, as we discuss later, is based on a rational set of guidelines for structuring organizations in the most efficient manner.

Chester Barnard, former president of New Jersey Bell Telephone Company, made notable contributions to management in his book *The Functions of the Executive*.[19] The book proposes a major theory about the acceptance of authority. The theory suggests that subordinates weigh the legitimacy of a supervisor's directives and then decide whether to accept them. An order is accepted if the subordinate understands it, is able to comply with it, and views it as appropriate. The importance of Barnard's work is enhanced by his experience as a top manager.

The Classical Management Perspective Today

The contributions and limitations of the classical management perspective are summarized in Table 2.1. The classical perspective is the framework from which later theories evolved, and many of its insights still hold true today. For example, many of the job specialization techniques and scientific methods espoused by Taylor and his contemporaries are still reflected in the way that many industrial jobs are designed today.[20] Moreover, many contemporary organizations still use some of the bureaucratic procedures suggested by Weber. Also, these early theorists were the first to focus attention on management as a meaningful field of study. Several aspects of the classical perspective are also relevant to our later discussions of planning, organizing, and controlling. And, as described more fully in *Managing in an E-business World*, recent advances in areas such as business-to-business (B2B) commerce also have efficiency as their primary goal.

The limitations of the classical perspective, however, should not be overlooked. These early writers dealt with stable, simple organizations; many organizations today, in contrast, are changing and complex. They also proposed universal guidelines that we now recognize do not fit every organization. A third limitation of the classical management perspective is that it slighted the role of the individual in organizations. This role was much more fully developed by advocates of the behavioral management perspective.

MANAGEMENT IMPLICATIONS The classical management perspective provides many techniques and approaches to management that are still relevant today. For example, thoroughly understanding the nature of the work being performed, selecting the right people for that work, and approaching decisions rationally are all useful ideas—and each was developed during this period. Similarly, some of the core concepts from the bureaucratic model can still be used in the design of modern organizations as long as their limitations are recognized.[21] Managers should also recognize that efficiency and productivity can indeed be measured and controlled in many situations. On the other hand, managers must also recognize the limitations of the classical perspective and avoid its narrow focus on efficiency to the exclusion of other important perspectives.

The Behavioral Management Perspective

behavioral management perspective Emphasizes individual attitudes and behaviors and group processes and recognizes the importance of behavioral processes in the workplace.

Early advocates of the classical management perspective essentially viewed organizations and jobs from a mechanistic point of view; that is, they essentially sought to conceptualize organizations as machines and workers as cogs within those machines. Even though many early writers recognized the role of individuals, their focus tended to be on how managers could control and standardize the behavior of their employees. In contrast, the **behavioral management perspective** emphasizes individual attitudes and behaviors and group processes and recognized the importance of behavioral processes in the workplace.

The behavioral management perspective was stimulated by a number of writers and theoretical movements. One of those movements was industrial psychology, the practice of applying psychological concepts to industrial settings. Hugo Munsterberg (1863–1916), a noted German psychologist, is recognized as the father of industrial psychology. He established a psychological laboratory at Harvard in 1892, and his pioneering book, *Psychology and Industrial Efficiency*, was translated into English in 1913.[22] Munsterberg suggested that psychologists could make valuable contributions to managers in the areas of employee selection and motivation. Industrial psychology is still a major course of study at many colleges and universities. Another early advocate of the behavioral approach to management was Mary Parker Follett.[23] Follett worked during the scientific management era but quickly came to recognize the human element in the workplace. Indeed, her work clearly anticipated the behavioral management perspective and she appreciated the need to understand the role of behavior in organizations.

The Hawthorne Studies

Although Munsterberg and Follett made major contributions to the development of the behavioral approach to management, its primary catalyst was a series of studies conducted near Chicago at Western Electric's Hawthorne plant between 1927 and 1932. The research, originally sponsored by General Electric, was conducted by Elton Mayo and his associates.[24] Mayo was a faculty member and consultant at Harvard. The first study involved manipulating illumination for one group of workers and comparing their subsequent productivity with the productivity of another group whose illumination was not changed. Surprisingly, when illumination was increased for the experimental group, productivity went up in both groups. Productivity continued to increase in both groups, even when the lighting for the experimental group was decreased. Not until the lighting was reduced to the level of moonlight did productivity begin to decline (and General Electric withdrew its sponsorship).



The Hawthorne studies were a series of early experiments that focused on behavior in the workplace. In one experiment involving this group of workers, for example, researchers monitored how productivity changed as a result of changes in working conditions. The Hawthorne studies and subsequent experiments led scientists to the conclusion that the human element is very important in the workplace.

Another experiment established a piecework incentive pay plan for a group of nine men assembling terminal banks for telephone exchanges. Scientific management would have predicted that each man would try to maximize his pay by producing as many units as possible. Mayo and his associates, however, found that the group itself informally established an acceptable level of output for its members. Workers who overproduced were branded "rate busters," and underproducers were labeled "chiselers." To be accepted by the group, workers produced at the accepted level. As they approached this acceptable level of output, workers slacked off to avoid overproducing.

Other studies, including an interview program involving several thousand workers, led Mayo and his associates to conclude that human behavior was much more important in the workplace than had been previously believed. In the lighting experiment, for example, the results were attributed to the fact that both groups received special attention and sympathetic supervision for perhaps the first time. The incentive pay plans did not work because wage incentives were less important to the individual workers than was social acceptance in determining output. In short, individual and social processes played a major role in shaping worker attitudes and behavior.

The Human Relations Movement

The **human relations movement**, which grew from the Hawthorne studies and was a popular approach to management for many years, proposed that workers respond primarily to the social context of the workplace, including social conditioning,

human relations movement Proposed that workers respond primarily to the social context of the workplace, including social conditioning, group norms, and interpersonal dynamics

group norms, and interpersonal dynamics. A basic assumption of the human relations movement was that the manager's concern for workers would lead to increased satisfaction, which would in turn result in improved performance. Two writers who helped advance the human relations movement were Abraham Maslow and Douglas McGregor.

In 1943, Maslow advanced a theory suggesting that people are motivated by a hierarchy of needs, including monetary incentives and social acceptance.[25] Maslow's hierarchy, perhaps the best known human relations theory, is described in detail in Chapter 16. Meanwhile, Douglas McGregor's, Theory X and Theory Y model best represents the essence of the human relations movement (see Table 2.2).[26] According to McGregor, Theory X and Theory Y reflect two extreme belief sets that different managers have about their workers. **Theory X** is a relatively negative view of workers and is consistent with the views of scientific management. **Theory Y** is more positive and represents the assumptions that human relations advocates make. In McGregor's view, Theory Y was a more appropriate philosophy for managers to adhere to. Both Maslow and McGregor notably influenced the thinking of many practicing managers.

Theory X A relatively negative view of workers consistent with the views of scientific management

Theory Y A positive view of workers; it represents the assumptions that human relations advocates make

The Emergence of Organizational Behavior

Munsterberg, Mayo, Maslow, McGregor, and others have made valuable contributions to management. Contemporary theorists, however, have noted that many assertions of the human relationists were simplistic and inadequate descriptions of work behavior. For example, the assumption that worker satisfaction leads to improved performance has been shown to have little, if any, validity. If anything, satisfaction follows good performance rather than precedes it. (These issues are addressed in Chapters 15 and 16.)

Table 2.2

Theory X and Theory Y

Douglas McGregor developed Theory X and Theory Y. He argued that Theory X best represented the views of scientific management and Theory Y represented the human relations approach. McGregor believed that Theory Y was the best philosophy for all managers.

Theory X Assumptions	1. People do not like work and try to avoid it. 2. People do not like work, so managers have to control, direct, coerce, and threaten employees to get them to work toward organizational goals. 3. People prefer to be directed, to avoid responsibility, and to want security; they have little ambition.
Theory Y Assumptions	1. People do not naturally dislike work; work is a natural part of their lives. 2. People are internally motivated to reach objectives to which they are committed. 3. People are committed to goals to the degree that they receive personal rewards when they reach their objectives. 4. People will both seek and accept responsibility under favorable conditions. 5. People have the capacity to be innovative in solving organizational problems. 6. People are bright, but under most organizational conditions their potentials are underutilized.

Source: Douglas McGregor, "Theory X and Theory Y" from *The Human Side of Enterprise*, Copyright © 1960 by McGraw-Hill. Reprinted by permission of The McGraw-Hill Companies, Inc.

Current behavioral perspectives on management, known as **organizational behavior**, acknowledge that human behavior in organizations is much more complex than the human relationists realized. The field of organizational behavior draws from a broad, interdisciplinary base of psychology, sociology, anthropology, economics, and medicine. Organizational behavior takes a holistic view of behavior and addresses individual, group, and organization processes. These processes are major elements in contemporary management theory.[27] Important topics in this field include job satisfaction, stress, motivation, leadership, group dynamics, organizational politics, interpersonal conflict, and the structure and design of organizations.[28] A contingency orientation also characterizes the field (discussed more fully later in this chapter). Our discussions of organizing (Chapters 11–14) and leading (Chapters 15–19) are heavily influenced by organizational behavior. And finally, as noted in *Working with Diversity*, managers need a solid understanding of human behavior as they address such diversity-related issues as religion in the workplace.

organizational behavior Contemporary field focusing on behavioral perspectives on management

WORKING WITH DIVERSITY

RELIGION AND THE WORKPLACE

Globalization and an increasingly diverse workforce has brought more employees of varying religious beliefs together in the workplace. What can companies do about managing on-the-job conflicts that can arise from different religious customs?

Some companies, such as Jeepers, a theme-park operator, have eased restrictions on facial hair to accommodate men who wear beards for religious or medical reasons. Others, including Royal Caribbean Cruises, have rehired Muslim women who were fired for wearing head scarves while working. But other workplace issues raised by religious practices can be more difficult to resolve, as Whirlpool has learned.

At Whirlpool's appliance factory in LaVergne, Tennessee, Muslims comprise about 10 percent of the workforce during the peak production months of January to June. Initially, the assembly line for air conditioners and refrigerators was disrupted when Muslim employees stopped working to pray during work hours. Another problem was arranging the work schedule so Muslim employees could attend a midday congregational prayer session every Friday. Ultimately, plant managers found a way to handle scheduling better. Now some Muslim employees start working earlier on Fridays so they can take an extended break for the noontime prayer session.

Clothing is another area where religious customs can conflict with workplace requirements. For safety reasons, Whirlpool's plant managers decided that women employees could not wear head scarves near assembly lines and similar equipment. After discussing the issue with the Muslim women on staff, however, the managers agreed to allow scarves tied close to the head.

We've had conflicts and confrontations over any number of things. I'm just happy things didn't erupt into a religious war.

*—William J. Chickering, director of employee relations, Whirlpool**

A more complex issue is differing attitudes toward women in positions of authority. Some Muslim men have left Whirlpool rather than remain in positions where they were supervised by women managers. Yet other Muslim men have learned to adapt to such workplace situations. In the end, managing diversity means finding creative ways to resolve these kinds of conflicts so both employees and the organization are satisfied.

Reference: Timothy Q. Schellhardt, "In a Factory Schedule, Where Does Religion Fit In?" *Wall Street Journal*, March 4, 1999, pp. B1, B12 (*quote on p. B1).

Table 2.3

The Behavioral Management Perspective

General Summary	The behavioral management perspective focuses on employee behavior in an organizational context. Stimulated by the birth of industrial psychology, the human relations movement supplanted scientific management as the dominant approach to management in the 1930s and 1940s. Prominent contributors to this movement were Elton Mayo, Abraham Maslow, and Douglas McGregor. Organizational behavior, the contemporary outgrowth of the behavioral management perspective, draws from an interdisciplinary base and recognizes the complexities of human behavior in organizational settings.
Contributions	Provided important insights into motivation, group dynamics, and other interpersonal processes in organizations. Focused managerial attention on these same processes. Challenged the view that employees are tools and furthered the belief that employees are valuable resources.
Limitations	The complexity of individual behavior makes prediction of that behavior difficult. Many behavioral concepts have not yet been put to use because some managers are reluctant to adopt them. Contemporary research findings by behavioral scientists are often not communicated to practicing managers in an understandable form.

The Behavioral Management Perspective Today

Table 2.3 summarizes the behavioral management perspective and lists its contributions and limitations. The primary contributions relate to ways in which this approach has changed managerial thinking. Managers are now more likely to recognize the importance of behavioral processes and to view employees as valuable resources instead of mere tools. On the other hand, organizational behavior is still imprecise in its ability to predict behavior. It is not always accepted or understood by practicing managers. Hence, the contributions of the behavioral school have yet to be fully realized.

MANAGEMENT IMPLICATIONS Managers should remember that people are not machines and should not focus so much on the technical side of things that they ignore behavioral forces and processes in their organizations. People and their behaviors represent a powerful force that can enhance—or diminish—the effectiveness of any organization.[29] At the same time, managers should also not fall prey to the commonsense fallacy that improving employee satisfaction will result in increased performance. Further, while employee morale and satisfaction are indeed important, managers should not stress these and other behavioral forces to the detriment of productivity and operating systems.

■ *The Quantitative Management Perspective*

The third major school of management thought began to emerge during World War II. During the war, government officials and scientists in England and the United States worked to help the military deploy its resources more efficiently and effectively. These groups took some of the mathematical approaches to management developed decades earlier by Taylor and Gantt and applied them to logistical

problems during the war.[30] They learned that problems regarding troop, equipment, and submarine deployment, for example, could all be solved through mathematical analysis. After the war, companies such as Du Pont and General Electric began to use the same techniques for deploying employees, choosing plant locations, and planning warehouses. Basically, then, this perspective is concerned with applying quantitative techniques to management. More specifically, the **quantitative management perspective** focuses on decision making, economic effectiveness, mathematical models, and the use of computers. There are two branches of the quantitative approach: management science and operations management.

quantitative management perspective Applies quantitative techniques to management

Management Science

Unfortunately, the term *management science* appears to be related to scientific management, the approach developed by Taylor and others early in this century. But the two have little in common and should not be confused. **Management science** focuses specifically on the development of mathematical models. A mathematical model is a simplified representation of a system, process, or relationship.

management science Focuses specifically on the development of mathematical models

At its most basic level, management science focuses on models, equations, and similar representations of reality. For example, managers at Detroit Edison use mathematical models to determine how best to route repair crews during blackouts. The Bank of New England uses models to figure out how many tellers need to be on duty at each location at various times throughout the day. In recent years, paralleling the advent of the personal computer, management science techniques have become increasingly sophisticated. For example, automobile manufacturers Daimler Chrysler and Ford use realistic computer simulations to study collision damage to cars. These simulations give them precise information and avoid the costs of "crashing" so many test cars.

Operations Management

Operations management is somewhat less mathematical and statistically sophisticated than management science and can be applied more directly to managerial situations. Indeed, we can think of **operations management** as a form of applied management science. Operations management techniques are generally concerned with helping the organization produce its products or services more efficiently and can be applied to a wide range of problems.

operations management Concerned with helping the organization produce its products or services more efficiently

For example, Rubbermaid and The Home Depot each use operations management techniques to manage their inventories. (Inventory management is concerned with specific inventory problems such as balancing carrying costs and ordering costs and determining the optimal order quantity.) Linear programming (which involves computing simultaneous solutions to a set of linear equations) helps United Air Lines plan its flight schedules, Consolidated Freightways develop its shipping routes, and General Instrument Corporation plan what instruments to produce at various times. Other operations management techniques include queuing theory, breakeven analysis, and simulation. All of these techniques and procedures apply directly to operations, but they are also helpful in such areas as finance, marketing, and human resource management.

Table 2.4

The Quantitative Management Perspective

General Summary	The quantitative management perspective focuses on applying mathematical models and processes to management situations. Management science specifically deals with the development of mathematical models to aid in decision making and problem solving. Operations management focuses more directly on the application of management science to organizations. Management information systems are developed to provide information to managers.
Contributions	Developed sophisticated quantitative techniques to assist in decision making. Application of models has increased our awareness and understanding of complex organizational processes and situations. Has been very useful in the planning and controlling processes.
Limitations	Cannot fully explain or predict the behavior of people in organizations. Mathematical sophistication may come at the expense of other important skills. Models may require unrealistic or unfounded assumptions.

The Quantitative Management Perspective Today

Like the other management perspectives, the quantitative management perspective has made important contributions and has certain limitations. Both are summarized in Table 2.4. It has provided managers with an abundance of decision-making tools and techniques and has increased understanding of overall organizational processes. It has been particularly useful in the areas of planning and controlling. On the other hand, mathematical models cannot fully account for individual behaviors and attitudes. Some believe that the time needed to develop competence in quantitative techniques retards the development of other managerial skills. Finally, mathematical models typically require a set of assumptions that may not be realistic.

MANAGEMENT IMPLICATIONS It is important for managers to learn and understand the basic mathematical techniques and procedures that have been developed within management science. They should also know when to use these techniques and when to recognize their limitations. Further, managers should also avoid placing so much reliance on quantitative results that they ignore their own experience and intuition.

Integrating Perspectives for Managers

Recognizing that the classical, behavioral, and quantitative approaches to management are not necessarily contradictory or mutually exclusive is important. Even though very different assumptions and predictions are made by each of the three perspectives, each can also complement the others. Indeed, a complete understanding of management requires an appreciation of all three perspectives. The

systems and contingency perspectives can help us integrate the earlier approaches and enlarge our understanding of all three.

The Systems Perspective

We briefly introduced the systems perspective in Chapter 1 in our definition of management. A **system** is an interrelated set of elements functioning as a whole.[31] As shown in Figure 2.3, by viewing an organization as a system, we can identify four basic elements: inputs, transformation processes, outputs, and feedback. First, inputs are the material, human, financial, and information resources the organization gets from its environment. Next, through technological and managerial processes, inputs are transformed into outputs. Outputs include products, services, or both (tangible and intangible); profits, losses, or both (even not-for-profit organizations must operate within their budgets); employee behaviors; and information. Finally, the environment reacts to these outputs and provides feedback to the system.

system An interrelated set of elements functioning as a whole

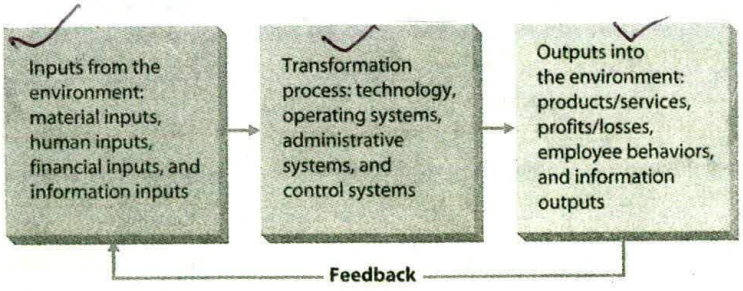
Thinking of organizations as systems provides us with a variety of important viewpoints on organizations, such as the concepts of open systems, subsystems, synergy, and entropy. **Open systems** are systems that interact with their environment, whereas **closed systems** do not interact with their environment. Although organizations are open systems, some make the mistake of ignoring their environment and behaving as though their environment is not important.

open system An organizational system that interacts with its environment

closed system An organizational system that does not interact with its environment

The systems perspective also stresses the importance of **subsystems**—systems within a broader system. For example, the marketing, production, and finance functions within Mattel are systems in their own right but are also subsystems within the overall organization. Because they are interdependent, a change in one subsystem can affect other subsystems as well. If the production department at Mattel lowers the quality of the toys being made (by buying lower-quality materials, for example), the effects are felt in finance (improved cash flow in the short run owing to lower costs) and marketing (decreased sales in the long run because of customer dissatisfaction). Managers must therefore remember that, although organizational subsystems can be managed with some degree of autonomy, their interdependence should not be overlooked.

subsystem A system within a broader system



2.3

Figure 2.3

The Systems Perspective of Organizations

By viewing organizations as systems, managers can better understand the importance of their environment and the level of interdependence among subsystems within the organization. Managers must also understand how their decisions affect and are affected by other subsystems within the organization.



Open systems are those that interact with their environment. In an age of increasing globalization and diversity, an open systems perspective is becoming increasingly important to all businesses. For example, this food service center in Singapore was created to serve Chinese, Indian, and Malay dishes. Not only does the station provide a variety of foods, but it must also offer different varieties of cutlery and other dining accoutrements as well as use signage in different languages.

synergy Two or more subsystems working together may often be more successful than when working alone

Synergy suggests that organizational units (or subsystems) may often be more successful working together than working alone. The Walt Disney Company, for example, benefits greatly from synergy. The company's movies, theme parks, television programs, and merchandise licensing programs all benefit one another. Children who enjoy a Disney movie like Tarzan want to go to Disney World and see the Tarzan show there and buy stuffed animals of the film's characters. Music from the film generates additional revenues for the firm, as do computer games and other licensing arrangements for lunch boxes, clothing, and so forth. Synergy was also the major objective in the first megamerger of 2000 between America Online and Time Warner.[32] Synergy is an important concept for managers because it emphasizes the importance of working together in a cooperative and coordinated fashion.[33]

entropy A normal process leading to system decline

Finally, **entropy** is a normal process that leads to system decline. When an organization does not monitor feedback from its environment and make appropriate adjustments, it may fail. For example, witness the problems of Studebaker (an automobile manufacturer) and Montgomery Ward (a major retailer). Each of these organizations went bankrupt because it failed to revitalize itself and keep pace with changes in its environment. A primary objective of management, from a systems perspective, is to re-energize the organization continually to avoid entropy.

The Contingency Perspective

universal perspective An attempt to identify the one best way to do something

contingency perspective Suggests that appropriate managerial behavior in a given situation depends on, or is contingent on, unique elements in that situation

Another recent noteworthy addition to management thinking is the contingency perspective. The classical, behavioral, and quantitative approaches are considered **universal perspectives** because they tried to identify the "one best way" to manage organizations. The **contingency perspective**, in contrast, suggests that universal theories cannot be applied to organizations because each organization is unique. Instead, the contingency perspective suggests that appropriate managerial behavior in a given situation depends on, or is contingent on, unique elements in that situation.[34]

Stated differently, effective managerial behavior in one situation cannot always be generalized to other situations. Recall, for example, that Frederick Taylor assumed that all workers would generate the highest possible level of output to maximize their own personal economic gain. We can imagine some people being motivated primarily by money—but we can just as easily imagine other people being motivated by the desire for leisure time, status, social acceptance, or any combination of these (as Mayo found at the Hawthorne plant). This perspective relates perfectly to Leslie Wexner and Limited, featured in the chapter opening incident. His managerial style worked perfectly when his firm was small and rapidly growing, but it did not match as well when Limited became a huge, mature enterprise. Thus, he had to alter his style at that point to match the changing needs of his business.

An Integrating Framework

We noted earlier that the classical, behavioral, and quantitative management perspectives can be complementary and that the systems and contingency perspectives can help integrate them. Our framework for integrating the various approaches to management is shown in Figure 2.4. The initial premise of the framework is that before attempting to apply any specific concepts or ideas from the three major perspectives, managers must recognize the interdependence of units within the organization, the effect of environmental influences, and the need to respond to the unique characteristics of each situation. The ideas of subsystem interdependencies and environmental influences are given to us by systems theory, and the situational view of management is derived from a contingency perspective.

With these ideas as basic assumptions, the manager can use valid tools, techniques, concepts, and theories of the classical, behavioral, and quantitative

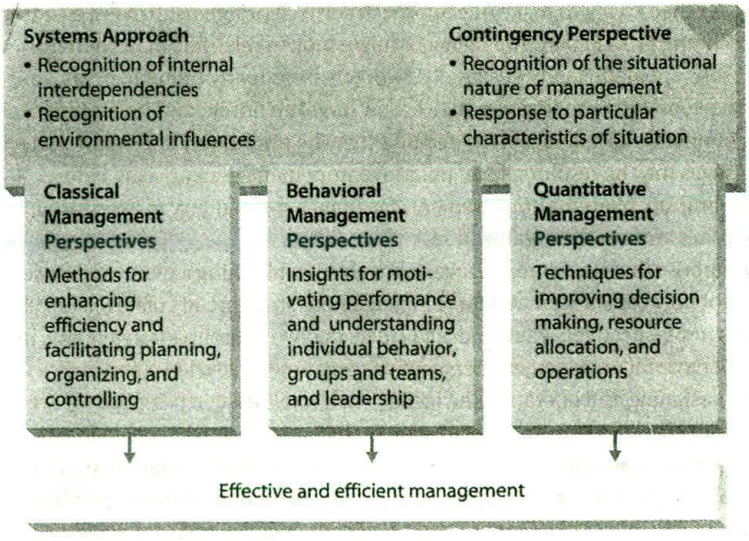


Figure 2.4

An Integrative Framework of Management Perspectives

Each of the major perspectives on management can be useful to modern managers. Before using any of them, however, the manager should recognize the situational context within which they operate. The systems and contingency perspectives serve to integrate the classical, behavioral, and quantitative management perspectives.

management perspectives. For example, managers can still use many of the basic techniques from scientific management. In many contemporary settings, the scientific study of jobs and production techniques can enhance productivity. But managers should not rely solely on these techniques, nor should they ignore the human element. The behavioral perspective is also of use to managers today. By drawing on contemporary ideas of organizational behavior, the manager can better appreciate the role of employee needs and behaviors in the workplace. Motivation, leadership, communication, and group processes are especially important. The quantitative perspective provides the manager with a set of useful tools and techniques. The development and use of management science models and the application of operations management methods can help managers increase their efficiency and effectiveness.

Consider the new distribution manager of a large wholesale firm whose job is to manage one hundred truck drivers and to coordinate standard truck routes in the most efficient fashion. This new manager, with little relevant experience, might attempt to increase productivity by employing strict work specialization and close supervision (as suggested by scientific management). But doing so may decrease employee satisfaction and morale and increase turnover (as predicted by organizational behavior). The manager might also develop a statistical formula to use route driver time more efficiently (from management science), but this new system could disrupt existing work groups and social patterns (from organizational behavior). The manager might create even more problems by trying to impose programs and practices derived from her previous job. An incentive program welcomed by retail clerks, for example, might not work for truck drivers.

The manager should soon realize that a broader perspective is needed. Systems and contingency perspectives help provide broader solutions. Also, as the integrative framework in Figure 2.4 illustrates, applying techniques from several schools works better than trying to make one approach solve all problems. To solve a problem of declining productivity, the manager might look to scientific management (perhaps jobs are inefficiently designed or workers improperly trained), organizational behavior (worker motivation may be low or group norms may be limiting output), or operations management (facilities may be improperly laid out or materials shortages may be resulting from poor inventory management). And before implementing any plans for improvement, the manager should try to assess their effect on other areas of the organization.

Now suppose that the same manager is involved in planning a new warehouse. She will probably consider what type of management structure to create (classical management perspective), what kinds of leaders and work-group arrangements to develop (behavioral management perspective), and how to develop a network model for designing and operating the facility itself (quantitative perspective). As a final example, if employee turnover is too high, the manager might consider an incentive system (classical perspective), plan a motivational enhancement program (behavioral perspective), or use a mathematical model (quantitative perspective) to discover that turnover costs may actually be lower than the cost of making any changes at all.

MANAGEMENT IMPLICATIONS Managers should always remember that there are no universal solutions to problems or standard responses to situations. Just as a carpenter selects certain tools for certain jobs, so too should a manager carefully evaluate each situation and then select from the broad array of management techniques, models, and theories that best suit each situation. Managers should also keep in mind that any given situation may require multiple perspectives and viewpoints.

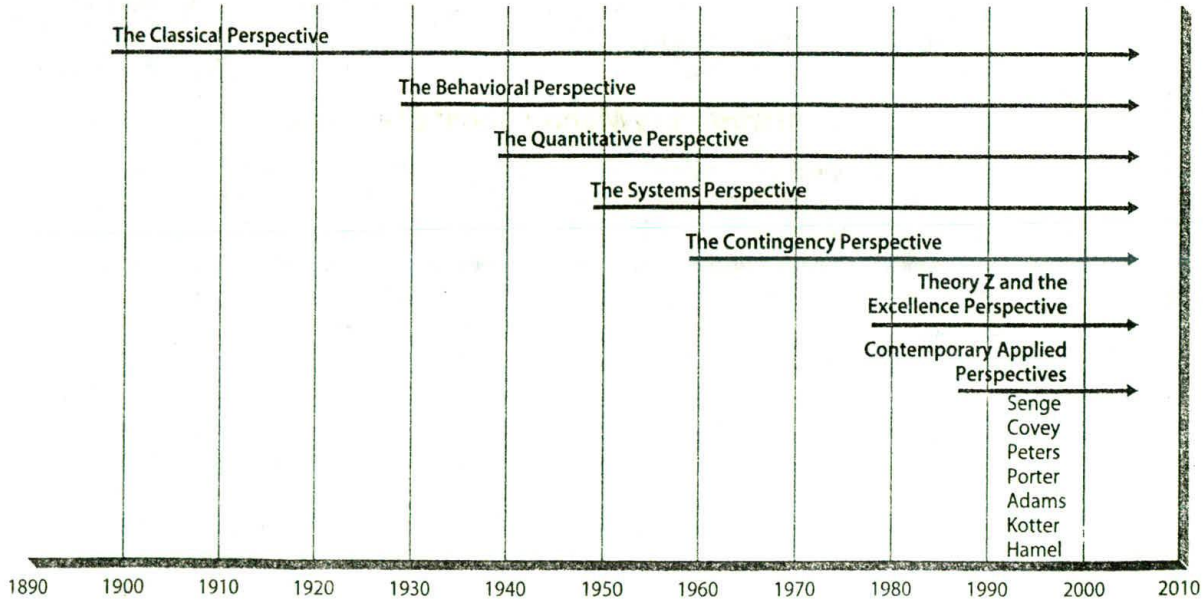
■ Contemporary Management Issues and Challenges

Interest in management theory and practice has heightened in recent years as new issues and challenges have emerged. No new paradigm has been formulated that replaces the traditional views, but managers continue to strive toward a better understanding of how they can better compete and lead their organizations toward improved effectiveness. Figure 2.5 summarizes the historical development of the major models of management, described in the preceding sections, and

Figure 2.5

The Emergence of Modern Management Perspectives

Most contemporary management perspectives have emerged and evolved over the last one hundred years or so. Beginning with the classical management perspective, first developed toward the end of the nineteenth century, and on through contemporary applied perspectives, managers have an array of useful techniques, methods, and approaches for solving problems and enhancing the effectiveness of their organizations. Of course, managers also need to recognize that not every idea set forth is valid, and that even those that are useful are not applicable in all settings. And new methods and approaches will continue to be developed in the future.



puts into historical context the contemporary applied perspectives discussed in the next section.



One of the biggest issues facing businesses today is how to integrate most effectively traditional operations with e-business opportunities. Consider, for example, the approach taken by Sephora Dimensions, the leading chain of perfume and cosmetics stores in France and the second-largest in Europe. Sephora builds traditional "brick-and-mortar" stores in key fashion centers. But each store also has computer terminals, such as the one shown here, that allow customers to browse for other products and place on-line orders. Sephora has recently transferred this business model to U.S. and Asian markets and now has over 200 stores around the world.

Contemporary Applied Perspectives

In recent years, books written for the so-called popular press have also had a major impact on both the field of organizational behavior and the practice of management. This trend first became noticeable in the early 1980s with the success of books such as William Ouchi's *Theory Z* and Thomas Peters and Robert Waterman's *In Search of Excellence.* Each of these books spent time on the *New York Times* best-seller list and was virtually required reading for any manager wanting at least to appear informed. Biographies of executives like Lee Iacocca and Donald Trump also received widespread attention. And bidding for the publishing rights to Jack Welch's memoirs, to be published when he retires as CEO from General Electric in 2001, exceeded $7 million.[35]

In recent years other applied authors have had a major impact on management theory and practice. Among the most popular applied authors today are Peter Senge, Stephen Covey, Tom Peters, Michael Porter, John Kotter, and Gary Hamel. These books highlight the management practices of successful firms like Shell, Ford, IBM, and others or outline conceptual or theoretical models or frameworks to guide managers as they formulate strategy or motivate their employees. The impact of their work is discussed in more depth in *Today's Management Issues.* Scott Adams, creator of the popular comic strip *Dilbert,* is also immensely popular today. Adams himself is a former communications industry worker who developed his strip to illustrate some of the absurdities that occasionally afflict contemporary organizational life. The daily strip is routinely posted outside office doors, above copy machines, and beside water coolers in hundreds of offices.

Contemporary Management Challenges

Managers today also face an imposing set of challenges as they guide and direct the fortunes of their companies. Coverage of each of these challenges is thoroughly integrated throughout this book. In addition, many of them are also highlighted and/or given focused coverage in one or more special ways.

One of the most critical challenges facing managers today is an acute labor shortage. The booming economy has combined with rapid advances in technology to provide more jobs in some employment sectors than there are qualified employees. This pattern manifests itself in several ways. First, companies in high-technology markets are finding that they must offer lavish benefits and high salaries to attract talented and motivated employees. And even though they continue to provide an ever-growing array of benefits, many of these same employees still move on to other—and more lucrative—jobs more quickly than at any time in recent memory. This trend has also trickled down to lower-skill jobs as well. Many hotels and restaurants, for example, are having difficulties in maintaining

TODAY'S MANAGEMENT ISSUES

CAN GURUS HELP COMPANIES COPE?

Contemporary management perspectives have been shaped and advanced by the ideas of a number of high-powered gurus. Michael Porter's groundbreaking analyses of competitive forces affecting businesses and nations have attracted AT&T and other companies as clients for his consulting firm, Monitor. Gary Hamel's work on corporate strategy has brought to *Strategos*, his consulting firm, clients such as General Motors. Like nearly every other well-known guru, both Porter and Hamel have written best-selling books that spread their ideas throughout the corporate world. But can gurus really help companies cope with thorny business issues and challenges?

Sam Hill, a marketing consultant based in Connecticut, observes that some gurus may be good at counseling—offering broad, general advice—but not at consulting—which requires in-depth research and analysis of a specific problem to find a specific solution. In Hill's view, few consultants are equipped to solve complicated business problems off the cuff. He also says that digging down to the nitty-gritty of a problem and weighing possible solutions requires any number of "constructive arguments." Yet clients rarely debate with gurus; most of the time, they simply listen and make notes as gurus speak.

For their part, clients who hire a guru may have unrealistic expectations. Because they are paying thousands of dollars per day for the guru's time, clients may want the expert to offer solutions too quickly. Gurus realize that complex management problems cannot be solved with simplistic, one-solution-fits-all answers. Nonetheless, some clients believe that gurus should have the expertise and background to go to the heart of the matter and suggest answers without a great deal of analysis.

Companies that bring in gurus as consultants tend to think that if they're paying $20 a minute, the guru should bypass the analysis and get straight to the answer.

*—Sam Hill, co-founder of Helios Consulting Group**

Some gurus have built large consulting firms to help clients apply their ideas and tackle major business challenges. Others disseminate their insights through books, articles, and speeches. In general, gurus can be a rich source of new ideas and a spark for creative problem-solving—if managers are careful to analyze critically how concepts apply to their particular organizations and situations.

Reference: Stuart Crainer and Des Dearlove, "Gurus Inc.," *Across the Board*, October 1999, pp. 17–22 (*quote on p. 18).

an adequate staff of house cleaners and dishwashers because of the abundance of more attractive jobs available today.[36]

A second important challenge today is the management of diversity. Diversity refers to differences among people. While diversity may be reflected along numerous dimensions, most managers tend to focus on age, gender, ethnicity, and physical abilities/disabilities. The internationalization of businesses has also increased diversity in many organizations, carrying with it additional challenges as well as new opportunities. We cover diversity in detail in Chapter 6 and in several boxed features called *Working with Diversity*, which appaer throughout the text.

Aside from demographic composition, the workforce today is also changing in other ways. It seems like the values, goals, and ideals of each succeeding generation differ from those of their parents. Today's young workers, for example, are sometimes stereotyped as being less devoted to long-term career prospects and are less willing to conform to a corporate mind-set that stresses conformity and

uniformity. Thus, managers are increasingly faced with the challenge of first creating an environment that will be attractive to today's worker. And they must address the challenge of providing new and different incentives to keep people motivated and interested in their work. And finally, they must incorporate sufficient flexibility in the organization to accommodate an ever-changing set of lifestyles and preferences.

Another management challenge that managers must be prepared to address is change. While organizations have always had to be concerned with managing change, the rapid and constant environmental change faced by businesses today has made change management even more critical. Simply put, an organization that fails to monitor its environment and to keep pace with that environment is doomed to failure. But more and more managers are seeing change as an opportunity, not a cause for alarm. Indeed, some managers think that if things get too calm in an organization and people start to become complacent, managers should shake things up to get everyone energized. We discuss the management of organizational change in more detail in Chapter 13.

New technology, especially as it relates to information, also poses an increasingly important management challenge. The Internet and the increased use of e-mail and voice-mail systems are among the most recent technological changes in this area. Among the key issues associated with information technology are employee privacy, decision-making quality, and optimizing a firm's investments in new forms of technology as they continue to emerge. A related issue confronting managers has to do with the increased capabilities this technology provides for people to work at places other than their offices. Finally, the appropriate role of the Internet in business strategy is also a complex arena for managers. We cover information technology in Chapter 22, as well as in several boxed features called *Management InfoTech.* We also provide numerous illustrations of Internet-related business issues in other boxes called *Managing in an E-business World.*

Another important management challenge today is the complex array of new ways of organizing that managers can consider. Recall from our earlier discussion that early organization theorists like Max Weber advocated "one best way" of organizing. These organizational prototypes generally resembled pyramids—tall structures with power controlled at the top and rigid policies and procedures governing most activities. Now, however, many organizations are seeking greater flexibility and the ability to respond more quickly to their environment by adopting flat structures. These flat structures are characterized by few levels of management, wide spans of management, and fewer rules and regulations. The increased use of work teams also goes hand in hand with this new approach to organizing. These issues are given considerable attention in Chapters 12 and 19.

Globalization is yet another significant contemporary challenge for managers. Managing in a global economy poses many different challenges and opportunities. For example, at a macro level, property ownership arrangements vary widely. So does the availability of natural resources and components of the infrastructure, as well as the role of government in business. But for our purposes, a very important consideration is how behavioral processes vary widely across cultural and national boundaries. For example, values, symbols, and beliefs differ sharply among cul-

tures. Different work norms and the role work plays in a person's life, for example, influence patterns of both work-related behavior and attitudes toward work. They also affect the nature of supervisory relationships, decision-making styles and processes, and organizational configurations. Group and intergroup processes, responses to stress, and the nature of political behaviors also differ from culture to culture. Chapter 5 is devoted to global issues, as are numerous boxed features called *The World of Management.*

Another management challenge that has taken on renewed importance is ethics and social responsibility. Unfortunately, business scandals have become almost commonplace today. From the view of social responsibility, increasing attention has been focused on pollution and business's obligation to help clean our environment, business contributions to social causes, and so forth. Chapter 4 covers ethics and social responsibility in more detail, as do several boxed features called *Today's Management Issues.*

Quality also continues to pose an important management challenge today. Quality is an important issue for several reasons. First, more and more organizations are using quality as a basis for competition. Continental Airlines, for example, stresses its high rankings in the J.D. Powers survey of customer satisfaction in its print advertising. Second, improving quality tends to increase productivity because making higher-quality products generally results in less waste and rework. Third, enhancing quality lowers costs. Whistler Corporation once found that it was using one hundred of its 250 employees to repair defective radar detectors that were built incorrectly the first time. Quality is also important because of its relationship to productivity. Quality is highlighted in Chapter 21.

Finally, the shift toward a service economy also continues to be important. Traditionally, most businesses were manufacturers—they used tangible resources like raw materials and machinery to create tangible products like automobiles and steel. In the last few decades, however, the service sector of the economy has become much more important. Indeed, services now account for well over half of the gross domestic product in the United States and play a similarly important role in many other industrialized nations as well. Service technology involves the use of both tangible resources (such as machinery) and intangible resources (such as intellectual property) to create intangible services (such as a haircut, insurance protection, or transportation between two cities). While there are obviously many similarities between managing in a manufacturing and a service organization, there are also many fundamental differences.

MANAGEMENT IMPLICATIONS Staying abreast of contemporary management issues and challenges is a bit of a juggling act for managers. On the one hand, they need to keep up with current developments in their field by reading current literature. On the other hand, some of the popular press material about business and management is simply fad or, worse, an incomplete or inaccurate "recipe" for success.[37] Similarly, new challenges and issues often arise with little or no advance warning. Some of these remain significant and enduring, while others fall by the wayside very quickly. Thus, the astute manager will learn to take an open-minded but critical view toward new ideas and issues.

Summary of Key Points

Theories are important as organizers of knowledge and as road maps for action. Understanding the historical context and precursors of management and organizations provides a sense of heritage and can also help managers to avoid repeating the mistakes of others. Evidence suggests that interest in management dates back thousands of years, but a scientific approach to management has emerged only in the last one hundred years. During the first few decades of the twentieth century, three primary perspectives on management emerged: the classical perspective, the behavioral perspective, and the quantitative perspective.

The classical management perspective had two major branches: scientific management and administrative management. Scientific management was concerned with improving efficiency and work methods for individual workers. Administrative management was more concerned with how organizations themselves should be structured and arranged for efficient operations. Both branches paid little attention to the role of the worker.

The behavioral management perspective, characterized by a concern for individual and group behavior, emerged primarily as a result of the Hawthorne studies. The human relations movement recognized the importance and potential of behavioral processes in organizations but made many overly simplistic assumptions about those processes. Organizational behavior, a more realistic outgrowth of the behavioral perspective, is of interest to many contemporary managers.

The quantitative management perspective and its two components, management science and operations management, attempt to apply quantitative techniques to decision making and problem solving. These areas are also of considerable importance to contemporary managers. Their contributions have been facilitated by the tremendous increase in the use of personal computers and integrated information networks.

The three major perspectives should be viewed in a complementary, not a contradictory, light. Each has something of value to offer. The key is understanding how to use them effectively. Two relatively recent additions to management theory, the systems and contingency perspectives, appear to have great potential both as approaches to management and as frameworks for integrating the other perspectives.

A variety of popular applied perspectives influence management practice today. Important issues and challenges facing managers include employee retention, diversity, the new workforce, organization change, ethics and social responsibility, the importance of quality, and the continued shift toward a service economy.

Discussion Questions

Questions for Review

1. Briefly summarize the classical management perspective and identify the most important contributors to each of its two branches.
2. Briefly summarize the Hawthorne studies. What are the primary conclusions reached following their completion?
3. Describe the contingency perspective and outline its usefulness to the study and practice of management.
4. What are some contemporary issues and challenges that managers must confront?

Questions for Analysis

5. In what ways do you think management in other countries evolved in the same ways as in the United States, and in what ways do you think it may have evolved differently?
6. Explain how a manager can use tools and techniques from each of the major management perspectives in a complementary fashion.
7. What recently published popular business books have been especially successful? Who are the prominent business leaders today whose ideas are widely accepted?

Questions for Application

8. Go to the library and locate material on Confucius. Outline his major ideas. Which seem to be applicable to management in the United States today?
9. Identify a local firm that has been in existence for a long time. Interview the current owner about the history of the firm and see if you can gain a better understanding of its current practices by learning about its past.
10. Read about or study the history of a company in which you are interested. Prepare for the class a brief report that stresses the impact of the firm's history on its current practices.

BUILDING EFFECTIVE *decision-making* SKILLS

Exercise Overview

As defined in Chapter 1, decision-making skills refer to a manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action to solve those problems and capitalize on the opportunities. This exercise will help you develop your own decision-making skills while also helping you to understand better the importance of subsystem interdependencies in organizations.

Exercise Background

Assume you are the vice president of operations for a large manufacturing company. Your firm makes home office furniture and cabinets for home theater systems. Because of the growth in each product line, the firm has also grown substantially in recent years. At the same time, this growth has not gone unnoticed, and several competitors have entered the market in the last two years. Your CEO has just instructed you to determine how to cut costs by 10 percent so prices can be cut by that same amount. She feels that this tactic is necessary to retain your market share in the face of new competition.

You have looked closely at the situation and have decided that there are three different ways you can accomplish this cost reduction. One option is to begin buying slightly lower-grade materials, such as wood, glue, and stain. Another option is to lay off a portion of your workforce and then pressure the remaining workers to work harder. As part of this same option, employees hired in the future will be selected from a lower-skilled labor pool and thus be paid a lower wage. The third option is to replace your existing equipment with newer, more efficient equipment. While this will require a substantial up-front investment, you are certain that lower production costs can be achieved.

Exercise Task

With this background in mind, respond to the following:

1. Carefully examine each of the three alternatives under consideration. In what ways might each alternative affect other parts of the organization?
2. Which is the most costly option (in terms of impact on other parts of the organization, not absolute dollars)? Which is the least costly?
3. What are the primary obstacles that you might face regarding each of the three alternatives?
4. Can you think of other alternatives that might accomplish the cost-reduction goal?

BUILDING EFFECTIVE *communication and interpersonal* SKILLS

Exercise Overview

As defined in Chapter 1, communication skills refer to the manager's abilities both to convey ideas and information to others effectively and to receive ideas and information effectively from others, and interpersonal skills refer to the ability to communicate with, understand, and motivate individuals and groups. This exercise applies these skills from a contingency perspective in selecting modes of communication to convey various kinds of news.

Exercise Background

You are the regional branch manager for a large insurance company. For the last week you have been so tied up in meetings that you have had little opportunity to communicate with any of your subordinates. You are now caught up, however, and have a lot of information to convey. Specifically, here is what people need to know and/or what you need to do:

1. Three people need to be told that they are getting a pay raise of 10 percent.
2. One person needs to be told that she has been placed on probation and will lose her job if her excessive absenteeism isn't corrected.
3. One person needs to be congratulated for receiving his master's degree.
4. Everyone needs to be informed about the schedule for the next cycle of performance reviews.
5. Two people need to be informed that their requests for transfers have been approved, while a third was denied. In addition, one other person is being transferred, even though she did not submit a transfer request. You know that she will be unhappy.

You can convey this information via telephone calls during regular office hours, a cell phone call as you're driving home this evening, a formal written letter, a handwritten memo, a face-to-face meeting, or e-mail.

Exercise Task

With this background in mind, respond to the following:

1. Choose a communication mode for each message you need to convey.
2. What factors went into your decision about each situation?
3. What would be the least appropriate communication mode for each message?
4. What would be the likely consequences for each inappropriate choice?

BUILDING EFFECTIVE *diagnostic and conceptual* SKILLS

Exercise Overview

Diagnostic skills are the skills that enable a manager to visualize the most appropriate response to a situation. Conceptual skills refer to the manager's ability to think in the abstract. This exercise will enable you to apply your diagnostic and conceptual skills to extrapolate from the past to the present to the future.

Exercise Background

While some basic consumer products have been around for decades, others have only recently come into being. Likewise, a variety of products were once commonplace but are now no longer available. Examples of such products include the automobile crank (once used to start car engines manually before electric starters were invented) and the wooden slide rule (once used to

perform calculations before electronic calculators were invented).

Working alone, identify ten products or services currently available that might not exist in the next few years. Next, form small groups of four or five. Compare your individual lists and create a single group list that contains the ten best examples of products or services that may not exist in the future.

Exercise Task

Using the group list, respond to the questions that follow (your instructor will tell whether to do this individually or as a group):

1. Why might each product or service disappear?
2. Can you think of ways to prolong the existence of each product or service?
3. What advice might you give to the owner or top manager of a firm in these industries?
4. How easy or difficult was it to identify the ten requested examples? What factors made it easy or difficult?

CHAPTER CLOSING CASE

ConAgra Searches for Synergy

What do Hunt's ketchup, Orville Redenbacher's popcorn Healthy Choice frozen meals, and Slim Jim jerky have in common? All are part of ConAgra's empire of food brands. With $25 billion in annual sales, ConAgra is the number-two U.S. food products company behind Kraft Foods. Aggressive acquisitions during the 1980s brought ninety different operating companies into the ConAgra family. Now CEO Bruce Rohde is working to lower systemwide costs and boost overall profits by improving coordination and cooperation among these diverse operations.

The corporate buying spree took place under Charles M. Harper, ConAgra's CEO before Rohde. Harper snapped up well-known food brands such as Butterball (turkeys), Swift Premium (cold cuts), and Hunt-Wesson (salad oils and tomato-based foods). Once under the ConAgra banner, these different companies were encouraged to continue operating as independent divisions. ConAgra had no corporate computer system; instead, the divisions used their own systems for accounting. In addition, each division continued to sell through its own sales force, forcing supermarket chains to arrange separate purchases with each division. Harper also started the Healthy Choice line of low-fat foods after suffering a heart attack and changing his diet to emphasize healthier fare.

ConAgra's highly decentralized structure worked well as long as sales and profits were growing at a strong pace. By the time Rohde was named to the top slot in 1996, however, consumers were spending more on restaurant meals, which meant they weren't spending as much on groceries for home-cooked meals. At the same time, the supermarket chains were consolidating through mergers and acquisitions, which gave the stores even more bargaining power when dealing with ConAgra and other suppliers. Meanwhile, competitors Kraft and Quaker Oats stepped up their trade promotions, offering special displays and other inducements to solidify relationships with major food chains. The road ahead looked extremely challenging for ConAgra.

As CEO, Rohde has cooked up a new recipe for synergy, reorganizing ConAgra's diverse collection of companies into three divisions. The food-service division sells ConAgra products such as chicken to restaurant chains such as Wendy's and Arby's. This division already accounts for half of the corporation's sales revenues and could potentially contribute even more to the bottom line. The retail division sells ConAgra products such as

Parkay margarine and Peter Pan peanut butter to grocery stores and supermarkets. The agricultural products division sells fertilizer and other products to farm producers. As part of this reorganization, ConAgra is closing more than a dozen inefficient factories and laying off 7,000 workers. So far, this reorganization has helped the company cut its costs by $100 million, a figure that could soon rise to $600 million in annual cost savings as reorganization continues.

ConAgra is also preparing a coordinated program to cross-sell brands inside supermarkets. For example, the company is considering offering a supermarket chain like Kroger's a special display featuring various foods for backyard barbecues. The display might hold bottles of Hunt's ketchup, cans of Van Camp's baked beans, and packages of Healthy choice bread—plus a sign reminding shoppers to pick up a package of Armour hot dogs in the refrigerated meats section. This enterprising cross-sell approach is designed to help ConAgra's powerful brands sell each other while giving supermarkets an attractive tool for sales building.

Today, ConAgra is continuing to acquire food-related businesses such as Seaboard poultry. It is also readying a counterattack on rivals with a fatter advertising budget for consumer campaigns to support its brands. But the environment remains challenging, and competitors are not letting up. Can Rohde's recipe successfully combine such disparate units as Marie Callender frozen foods, Egg Beaters egg substitutes, and Monfort beef products into one highly profitable corporate entity?

Case Questions

1. What management actions seem to have contributed to inefficient operation of ConAgra's subsystems?
2. What signs of entropy should ConAgra's management be alert for—and why?
3. What other kinds of programs might ConAgra develop to improve synergy among its brand-name food products?

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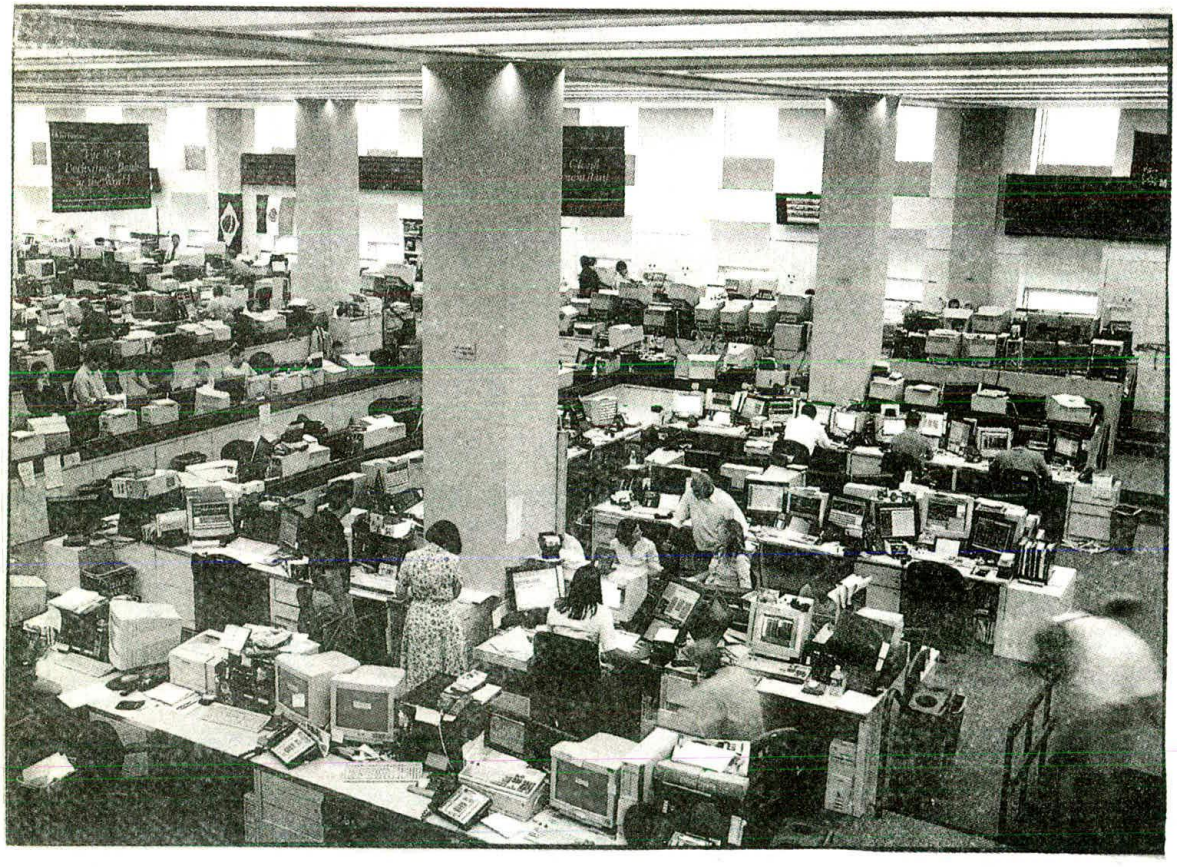
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33. Kathleen M. Eisenhardt and D. Charles Galunic, "Coevolving—At last, a Way to Make Synergies Work," *Harvard Business Review*, January–February 2000, pp. 91–103.
34. Fremont E. Kast and James E. Rosenzweig, *Contingency Views of Organization and Management* (Chicago: Science Research Associates, 1973).
35. "Welch Memoirs Fetch $7.1M," *USA Today*, July 14, 2000, p. 1B.
36. See Angelo S. DeNisi and Ricky W. Griffin, *Human Resource Management* (Boston: Houghton Mifflin, 2001), Chapter 17.
37. "A Way Too Short History of Fads," Forbes ASAP, April 7, 1997, p. 72; "Management Theory—Or Fad of the Month?" *Business Week*, June 23, 1997, p. 47.

PART TOW

The Environmental Context of Management



CHAPTER 3

The Environment of Organizations and Managers

CHAPTER 4

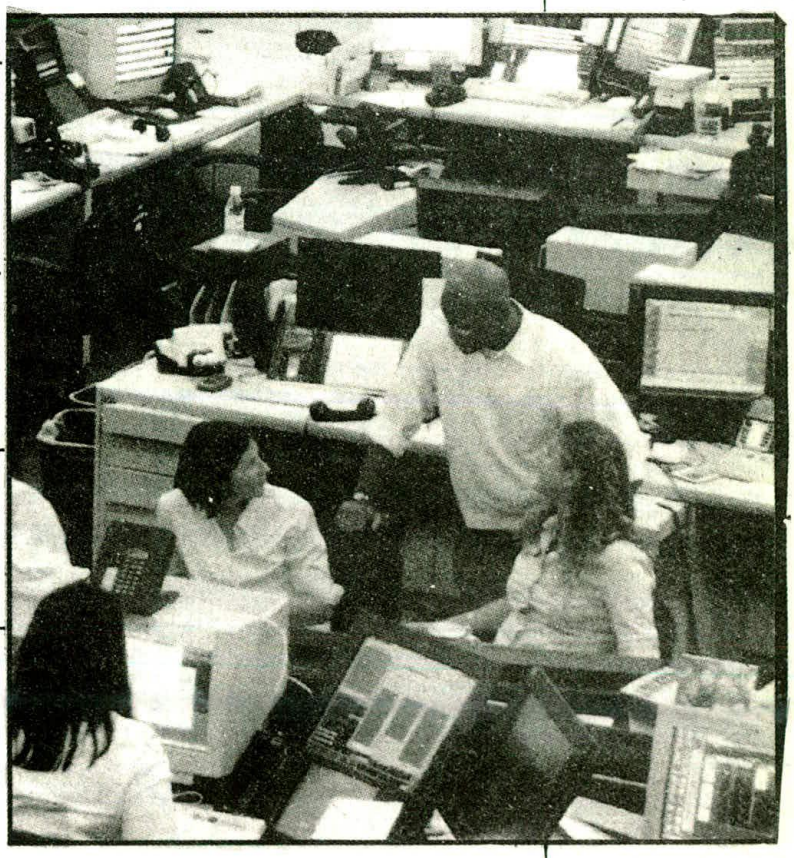
The Ethical and Social Environment

CHAPTER 5

The Global Environment

CHAPTER 6

The Cultural and Multicultural Environment



CHAPTER 3

The Environment of Organizations and Managers

OPENING INCIDENT

Most organizations operate within a complex network of environmental markets. A market is simply a mechanism for exchange between the buyers and sellers of a particular good or service. In earlier times, markets were actual physical settings where buyers and sellers would gather. While such market settings are still used for things like fish, fruits and vegetables, and antiques and collectibles, many commercial markets today are fundamentally different because buyers and sellers are not at the same place—they arrange their exchange via mail orders, telephones, fax machines, and so forth. And the growth of the Internet is serving to transform some markets and thus make it even easier for buyers and sellers to transact their business at a distance.

A good example of this trend is the recently announced partnership among some of the world's largest automobile manufacturers. It all started when various individual automobile makers began to create their own global purchasing web sites. Ford, for instance, was creating a site called Auto-Xchange. The company intended to post all of its global procurement needs on the site, while also requesting that its suppliers post availability and prices for the parts and equipment they had to offer.

Concerns began to arise, however, when it quickly became apparent that other automobile companies were planning to do the same thing. Major suppliers to the auto industry, meanwhile, began to realize that they might soon be facing an unwieldy array of separate web sites for each car company, potentially driving their own costs up. So a coalition of the largest suppliers approached Ford and General Motors with a novel proposal—why not team up and create a single site both firms could use?

Ford and GM executives quickly saw the wisdom of this idea and then convinced DaimlerChrysler to join them. Their plan is to create a single web site that will serve as a marketplace for all interested automobile manufacturers, suppliers, and dealers—essentially creating a global virtual market for all firms in the industry. Almost immediately, France's Renault and Japan's Nissan, which is controlled by Renault, indicated they would join. Toyota also

"We brought in DaimlerChrysler to prevent Europe from creating a separate standard. We think we'll have the industry standard, and we see value in having that."

—Harold Kutner, General Motors vice president responsible for purchasing

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- Discuss the nature of the organizational environment and identify the environments of interest to most organizations.
- Describe the components of the general and task environments and discuss their impact on organizations.
- Identify the components of the internal environment and discuss their impact on organizations.
- Identify and describe how the environment affects organizations and how organizations adapt to their environment.
- Discuss the meaning of and approaches to assessing organizational effectiveness.

showed strong interest. In addition, both Ford and GM said that they would encourage their foreign affiliates and strategic partners to join as well. The three partners creating the web site also intend to establish it as a self-contained organization that will eventually offer shares to the public.

Experts also believe that the impact of this global electronic market will be tremendous. For example, it currently costs GM about $100 per transaction in ordering costs to buy parts or supplies the traditional way—with paper, over the telephone, etc. But the firm estimates that its ordering costs will drop to less than $10 per transaction under the new system. Clearly, then, the automobile makers will realize substantial cost savings. The suppliers, too, will benefit in various ways. Besides having more information about what different companies need, they will be able to buy and sell among themselves.[1]



CHAPTER OUTLINE

- **The Organization's Environments**
  - The External Environment
  - The General Environment
  - The Task Environment
- **The Internal Environment**
  - Owners
  - Board of Directors
  - Employees
  - Physical Work Environment
- **Organization-Environment Relationships**
  - How Environments Affect Organizations
  - How Organizations Adapt to Their Environments
- **The Environment and Organizational Effectiveness**
  - Models of Organizational Effectiveness
  - Examples of Organizational Effectiveness

The Internet has become a major business tool for managers. On-line auctions are just one of the myriad applications that managers can leverage for competitive advantage. And sometimes, as illustrated in the chapter opening incident, it pays for competitors to work together. Indeed, the catalyst for cooperation among Ford, General Motors, and other competitors was their own suppliers, many of whom also compete with one another. Clearly, then, the environmental context of business today is changing in unprecedented ways.

As we noted in Chapter 1, managers must have a deep understanding and appreciation of the environment in which they and their organizations function. Without this understanding they are like a rudderless ship—moving along but with no way of maneuvering or changing direction. This chapter is the first of four devoted to the environmental context of management. After introducing the nature of the organization's environment, we describe first the general and then the task environments in detail. We then discuss key parts of the internal environment of an organization. We then address organization-environment relationships and, finally, how these relationships determine the effectiveness of the organization.

■ The Oraganization's Environments

To illustrate the importance of the environment to an organization, consider the analogy of a swimmer crossing a wide stream. The swimmer must assess the current, obstacles, and distance before setting out. If these elements are properly evaluated, the swimmer will arrive at the expected point on the far bank of the stream. But if they are not properly understood, the swimmer might end up too far upstream or downstream. The organization is like a swimmer, and the environment is like the stream. Thus, just as the swimmer needs to understand conditions in the water, the organization must understand the basic elements of its environment to maneuver among them properly.[2] More specifically, a key element in the effective management of an organization is determining the ideal alignment between the environment and the organization and then working to achieve and maintain that alignment. To do these things, however, the manager must first thoroughly understand the nature of the organization's environments.[3]

external environment Everything outside an organization's boundaries that might affect it

internal environment The conditions and forces within an organization

The **external environment** is everything outside an organization's boundaries that might affect it. As shown in Figure 3.1, there are actually two separate external environments: the general environment and the task environment. An organization's **internal environment** consists of conditions and forces within the organization. Of course, not all parts of these environments are equally important for all organizations. A small two-person partnership does not have a board of directors, for example, whereas a large public corporation is required by law to have one. A private university with a large endowment (like Harvard) may be less concerned about general economic conditions than might a state university (like the University of Missouri) that is dependent on state funding from tax revenues. Still, organizations need to understand fully which environmental forces are important and how the importance of others might increase.

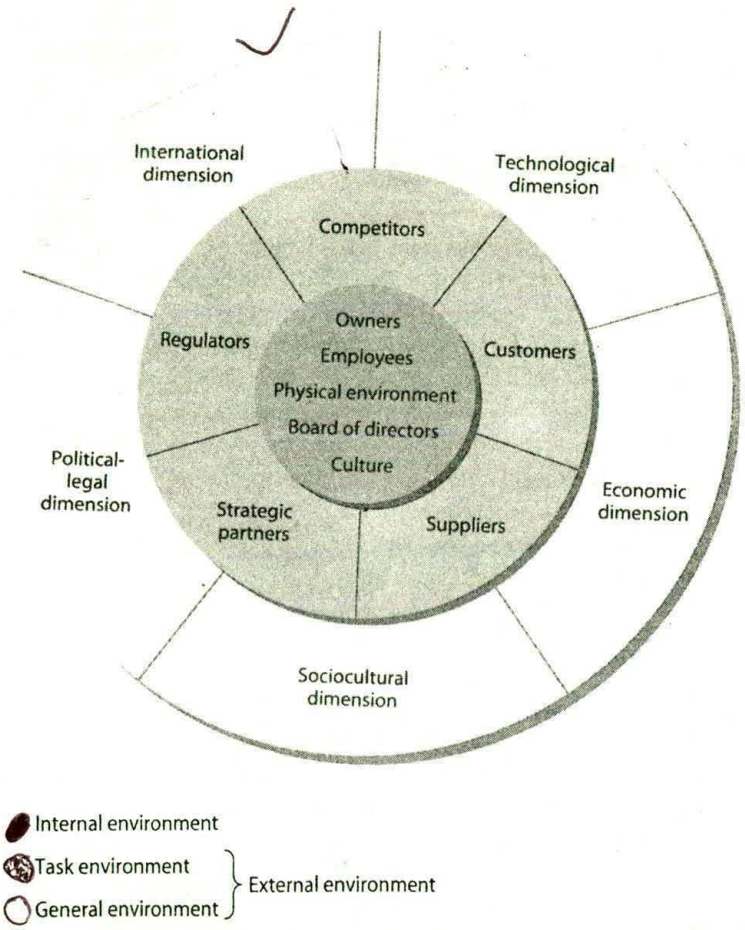


Figure 3.1

The Organization and Its Environments

Organizations have both an external and an internal environment. The external environment consists of two layers: the general environment and the task environment.

MANAGEMENT IMPLICATIONS Managers should always be aware of the environments in which they and their organizations function. Indeed, maintaining an effective alignment between the organization and the environment is a key part of the manager's job. And managers themselves must also be cognizant of the environment in which they as individuals and as members of groups carry out their responsibilities.

■ *The External Environment*

As just noted, an organization's external environment consists of two parts. The **general environment** of an organization is the set of broad dimensions and forces in its surroundings that create its overall context. These dimensions and forces are not necessarily associated with other specific organizations. The general environment

general environment The set of broad dimensions and forces in an organization's surroundings that create its overall context

task environment Specific external organizations or groups that influence an organization

of most organizations has economic, technological, sociocultural, political-legal, and international dimensions. The other significant external environment for an organization is its task environment. The **task environment** consists of specific external organizations or groups that influence an organization.

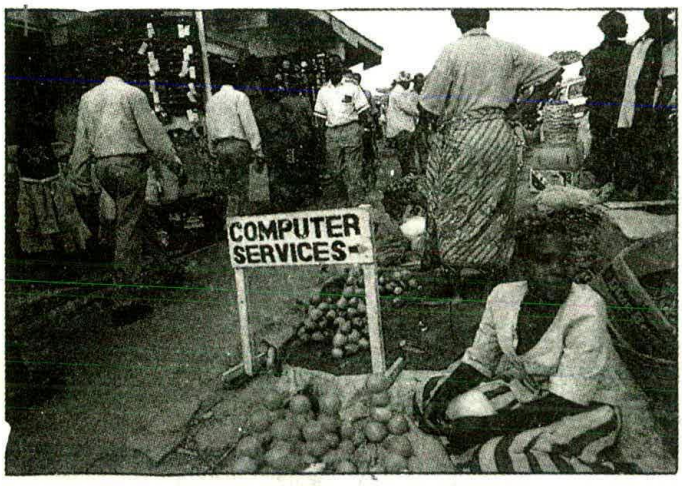
The General Environment

Each of these dimensions embodies conditions and events that have the potential to influence the organization in important ways. Some examples to illustrate these dimensions as they relate to McDonald's Corporation are shown in Figure 3.2.

economic dimension The overall health and vitality of the economic system in which the organization operates

The Economic Dimension The **economic dimension** of an organization's general environment is the overall health and vitality of the economic system in which the organization operates.[4] Particularly important economic factors for business are general economic growth, inflation, interest rates, and unemployment. As noted in Figure 3.2, McDonald's U.S. operation is functioning in an economy currently characterized by strong growth, low unemployment, and low inflation.[5] But economic strength sometimes has two sides. For example, low unemployment means that more people can eat out, but McDonald's also has to pay higher wages to attract new employees. Similarly, low inflation means that the prices McDonald's must pay for its supplies remain relatively constant, but it also is somewhat constrained from increasing the prices it charges consumers for a hamburger or a milk shake. The economic dimension is also important to nonbusiness organizations as well. For example, during weak economic conditions, funding for state universities may drop and charitable organizations like the Salvation Army are asked to provide greater assistance at the same time their own incoming contributions dwindle. Similarly, hospitals are affected by the availability of government grants and the number of low-income patients they must treat for free.

The technological dimension of the general environment continues to evolve at breakneck speed. The pace of change and complexity involving computers and information technology is especially pronounced. Take this marketplace in Kampala, Uganda, for example. Buyers and sellers of fruits and vegetables have gathered here for centuries. But the presence of an Internet Service Provider is a new feature at the market, and one that has the potential to revolutionize how the citizens of Africa live, work and interact with the rest of the world.



The Technological Dimension The **technological dimension** of the general environment refers to the methods available for converting resources into products or services. Although technology is applied within the organization, the forms and availability of that technology come from the general environment. Computer-assisted manufacturing and design techniques, for example, allow Boeing to simulate the more than three miles of hydraulic tubing that run through a 777 aircraft. The results include decreased warehouse needs, higher-quality tube fittings, fewer employees, and major time savings. While some people associate technology with manufacturing firms, it is also relevant in the

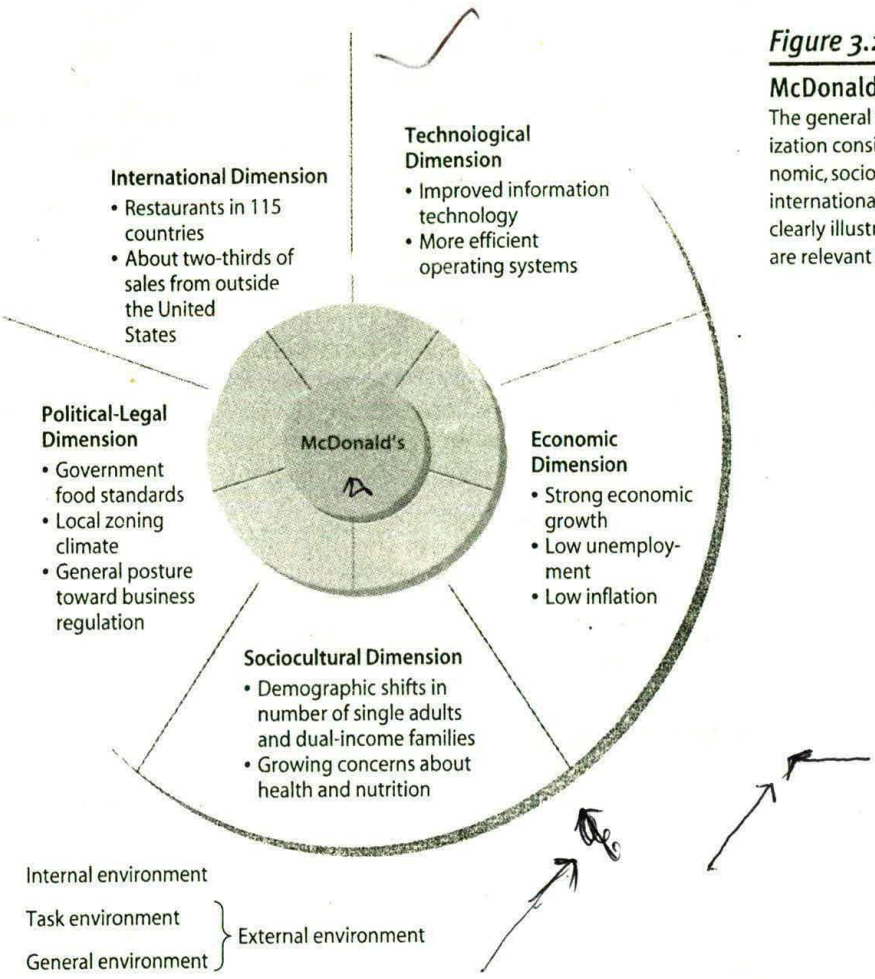


Figure 3.2

McDonald's General Environment

The general environment of an organization consists of technological, economic, sociocultural, political-legal, and international dimensions. This figure clearly illustrates how these dimensions are relevant to managers at McDonald's.

service sector. For example, just as an automobile follows a predetermined pathway along an assembly line as it is built, a hamburger at McDonald's similarly follows a predefined path as the meat is cooked, the burger is assembled, and then it is wrapped and bagged for a customer. The rapid advancement of the Internet into all areas of business is also a reflection of the technological dimension.

technological dimension The methods available for converting resources into products or services

The Sociocultural Dimension The **sociocultural dimension** of the general environment includes the customs, mores, values, and demographic characteristics of the society in which the organization functions. Sociocultural processes are important because they determine the products, services, and standards of conduct that the society is likely to value. In some countries, for example, consumers are willing to pay premium prices for designer clothes. But the same clothes have virtually no market in other countries. Consumer tastes also change over time. Preferences for

sociocultural dimension The customs, mores, values, and demographic characteristics of the society in which the organization functions

color, style, taste, and so forth, change from season to season, for example. Drinking hard liquor and smoking cigarettes are less common activities in the United States today than they were just a few years ago. And sociocultural factors influence how workers in a society feel about their jobs and organizations. *Working with Diversity* explores another change in the sociocultural dimension of the environment.

Appropriate standards of business conduct also vary across cultures. In the United States, accepting bribes and bestowing political favors in return are considered unethical. In other countries, however, payments to local politicians may be expected in return for a favorable response to common business transactions such as applications for zoning and operating permits. The shape of the market, the ethics of political influence, and attitudes in the workforce are only a few of the many ways in which culture can affect an organization. Figure 3.2 shows that McDonald's is clearly affected by sociocultural factors. For example, in response to concerns about nutrition and health, McDonald's has added salads to its menus and experimented with

WORKING WITH DIVERSITY

Femininity in the Workplace

How the workplace has changed. A few decades ago, working women felt like outsiders in a man's world, so they donned suits and floppy ties and tried to blend in. Today, women are in nearly every career and work position, even cracking the glass ceiling to assume top-management posts at Hewlett-Packard and other companies. The working women of this generation are more comfortable with their roles in the workplace—and more willing to show their softer sides.

Just as tailored suits have given way to casual dress in many job settings, a growing number of women are becoming less formal in the way they look and act at work. Instead of wearing buttoned-down shirts, some women are wearing t-shirts—and a few even wear tank tops. Behavior is also changing as more women choose to emphasize their feminine qualities. One woman says that she smoothes the way in her mostly male office by offering a smile and being enthusiastic. Another, an Internet entrepreneur, talks about capturing the attention of male business contacts because she is attractive.

Is this flirting behavior—and is it appropriate? Jill Ireland, the president of the National Organization for Women, argues that flirting is a short-term strategy that can confuse male coworkers and invite unwanted attention. But Brian Bogosian, CEO of Valens Information Systems, says that good-natured banter makes the workplace fun and more interesting. Leonard Brown, an engineer, has yet another perspective: he says that men get angry because they believe attractive women have an edge that they shouldn't be allowed to use in business.

Men are more comfortable with you if you're able to banter with them and engage in that way as opposed to being very stiff.

*—Michelle Kramer, consultant, McKinsey & Co.**

Times have definitely changed. Now that fewer working women are dressing and acting much like their male colleagues, men and women are negotiating new adjustments to clarify the fine line between appropriate and inappropriate behavior.

Reference: Ellen Joan Pollock, "In Today's Workplace, Women Feel Freer to Be, Well, Women," *Wall Street Journal*, February 7, 2000, pp. A1, A20 (*quote on p. A1).

other low-fat foods. And the firm was the first fast-food chain to provide customers with information about the ingredients used in its products.

The Political-Legal Dimension The **political-legal dimension** of the general environment refers to the government regulation of business and the general relationship between business and government. It is important for three basic reasons. First, the legal system partially defines what an organization can and cannot do. Although the United States is basically a free market economy, there is still major regulation of business activity. McDonald's, for example, is subject to a variety of political and legal forces, including food preparation standards and local zoning requirements.

Second, pro- or antibusiness sentiment in government influences business activity. For example, during periods of probusiness sentiment, firms find it easier to compete and have fewer concerns about antitrust issues. On the other hand, during a period of antibusiness sentiment, firms may find their competitive strategies more restricted and have fewer opportunities for mergers and acquisitions because of antitrust concerns. Among the most recent examples of the effects of the political-legal dimension were the court-order breakup of Microsoft in 2000 and the Justice Department's efforts to block a proposed merger between WorldCom and Sprint that same year.[6]

Finally, political stability has ramifications for planning. No business wants to set up shop in another country unless trade relationships with that country are relatively well defined and stable. Hence, U.S. firms are more likely to do business with England, Mexico, and Canada than with Haiti and El Salvador. Similar issues are also relevant to assessments of local and state governments. A new mayor or governor can affect many organizations, especially small firms that do business in only one location and are susceptible to deed and zoning restrictions, property and school taxes, and the like.

political-legal dimension The government regulation of business and the general relationship between business and government

The International Dimension Yet another component of the general environment for many organizations is the **international dimension**, or the extent to which an organization is involved in or affected by business in other countries.[7] As we discuss more fully in Chapter 5, multinational firms such as General Electric, Boeing, Nestlé, Sony, Siemens, and Hyundai clearly affect and are affected by international conditions and markets. For example, as noted in Figure 3.2, McDonald's operates restaurants in 115 countries and derives about two-thirds of its total sales outside the United States. More information about McDonald's international experiences are documented in *The World of Management*. Even firms that do business in only one country may face foreign competition at home, and they may use materials or production equipment imported from abroad. The international dimension also has implications for not-for-profit organizations. For example, the Peace Corps sends representatives to underdeveloped countries. As a result of advances in transportation and information technology in the past century, almost no part of the world is cut off from the rest. As a result, virtually every organization is affected by the international dimension of its general environment.

international dimension The extent to which an organization is involved in or affected by business in other countries

WORLD OF MANAGEMENT

Mexican Firms Go Global

For Mexico's Grupo Industrial Bimbo SA, the drive to sell internationally began the day a buyer for McDonald's tried and rejected the company's hamburger buns. Sensing future opportunity despite this setback, the company chairman, Roberto Servitje, invested $30 million to make improvements that ultimately allowed Bimbo to win over the McDonald's buyer. Now Bimbo is McDonald's only bun supplier in Mexico, Peru, Colombia, and Venezuela. The company also exports snacks, candy, cakes, and other foods to more than a dozen countries. This aggressive international expansion has helped Bimbo increase sales fivefold during the past ten years.

Bimbo, like other leading Mexican firms, started thinking about global markets when the North American Free Trade Agreement (NAFTA) paved the way for nontariff trade throughout the continent. U.S. companies quickly stormed into Mexico in search of suppliers, partners, and customers. Managers of local companies were exposed to new management and production techniques—which they adapted to compete more effectively within Mexico as well as in other countries.

Grupo Mabe SA has taken a slightly different route to international success. As the top Mexican appliance manufacturer, Mabe was chosen by U.S.-based General Electric to make kitchen appliances for the North American market under the GE brand. This arrangement worked so well that GE contracted with Mabe to produce appliances for Latin American countries. Meanwhile, Mabe decided that NAFTA was making the U.S. market too crowded. Instead of exporting to the north, the company took advantage of other regional trade agreements to expand south into Brazil, Venezuela, Colombia, and Argentina.

We put our ranges and washing machines in Manizales, Colombia, and our refrigerators in Maracaibo, Venezuela.

*—Luis Berrondo, director, Grupo Mabe**

Thanks to NAFTA and nimble management, Mexican companies have catapulted the country onto the list of the world's top ten exporting nations. Its export levels are still one-quarter of Japan's levels. However, with more Mexican firms going global, the country will soon move ahead of South Korea and Hong Kong on the list.

Reference: Joel Millman, "Trade Wins: The World's New Tiger on the Export Scene Isn't Asia; It's Mexico," *Wall Street Journal*, May 9, 2000, pp. A1, A10 (*quote on p. A10).

The Task Environment

Because the impact of the general environment is often vague, imprecise, and long-term, most organizations tend to focus their attention on their task environment. This environment includes competitors, customers, suppliers, regulators, and strategic allies. Although the task environment is also quite complex, it provides useful information more readily than does the general environment because the manager can identify environmental factors of specific interest to the organization rather than having to deal with the more abstract dimensions of the general environment.[8] Figure 3.3 depicts the task environment of McDonald's.

competitor An organization that competes with other organizations for resources

Competitors An organization's **competitors** are other organizations that compete with it for resources. The most obvious resources that competitors vie for are customer dollars. Reebok, Adidas, and Nike are competitors, as are Albertson's,

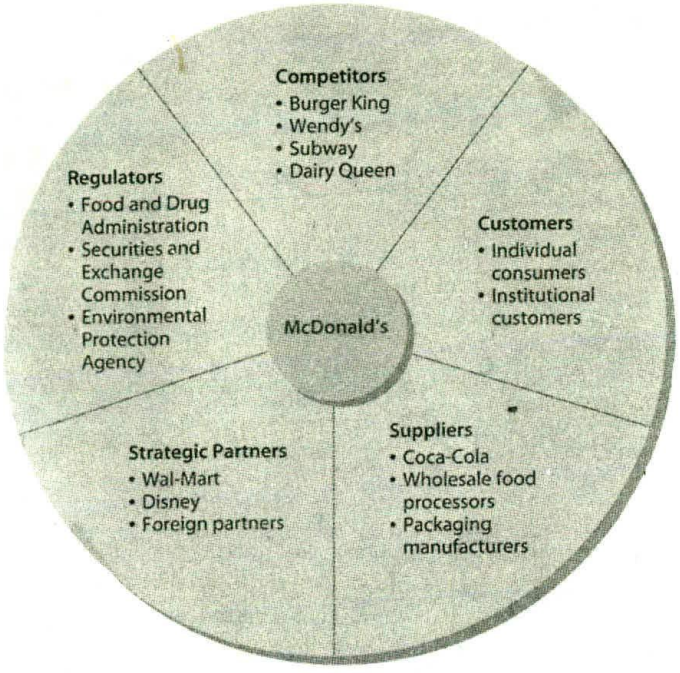


Figure 3.3

McDonald's Task Environment

An organization's task environment includes its competitors, customers, suppliers, strategic partners, and regulators. This figure clearly highlights how managers at McDonald's can use this framework to identify and understand their key constituents.

Safeway, and Kroger. McDonald's competes with other fast-food operations like Burger King, Wendy's, Subway, and Dairy Queen. But competition also occurs between substitute products. Thus, Ford competes with Yamaha (motorcycles) and Schwinn (bicycles) for your transportation dollars, and Walt Disney World, Club Med, and Carnival Cruise Lines compete for your vacation dollars. Nor is competition limited to business firms. Universities compete with trade schools, the military, other universities, and the external labor market to attract good students, and art galleries compete with each other to attract the best exhibits.

Organizations may also compete for different kinds of resources besides consumer dollars. For example, two totally unrelated organizations may compete to acquire a loan from a bank that has only limited funds to lend. Two retailers might compete for the right to purchase a prime piece of real estate in a growing community. In a large city, the police and fire departments may compete for the same tax dollars. And businesses also compete for quality labor, technological breakthroughs and patents, and scarce raw materials.

Customers A second dimension of the task environment is **customers**, or whoever pays money to acquire an organization's products or services. Most of

customer Whoever pays money to acquire an organization's products or services

McDonald's customers are individuals who walk into a restaurant to buy food. But customers need not be individuals. Schools, hospitals, government agencies, wholesalers, retailers, and manufacturers are just a few of the many kinds of organizations that may be major customers of other organizations. Some institutional customers like schools, prisons, and hospitals also buy food in bulk from restaurants like McDonald's.

Dealing with customers has become increasingly complex in recent years. New products and services, new methods of marketing, and more discriminating customers have all added uncertainty to how businesses relate to their customers, as has lower brand loyalty. A few years ago McDonald's introduced a new sandwich called the Arch Deluxe, intended to appeal to adult customers. Unfortunately, the product failed because most adult customers preferred existing menu choices like the Quarter Pounder. Similarly, Tommy Hilfiger, a popular clothing designer, has fallen from favor in recent years in large part because his organization has lost touch with its customers.[9]

Companies face especially critical differences among customers as they expand internationally. McDonald's sells beer in its German restaurants, for example, and wine in its French restaurants. Customers in those countries see those particular beverages as normal parts of a meal, much as customers in the United States routinely drink water, tea, or soft drinks with their meals. And the firm has even opened restaurants with no beef on the menu! Those restaurants are in India, where beef is not a popular menu option. Instead, the local McDonald's restaurants in that country use lamb in their sandwiches.

supplier An organization that provides resources for other organizations

Suppliers **Suppliers** are organizations that provide resources for other organizations. McDonald's buys soft-drink products from Coca-Cola; individually packaged servings of ketchup from Heinz; ingredients from wholesale food processors; and napkins, sacks, and wrappers from packaging manufacturers. Common wisdom in the United States used to be that a business should try to avoid depending exclusively on particular suppliers. A firm that buys all of a certain resource from one supplier may be crippled if the supplier goes out of business or is faced with a strike. This practice can also help maintain a competitive relationship among suppliers, keeping costs down. But firms eager to emulate successful Japanese firms have recently tried to change their approach. Japanese firms have a history of building major ties with only one or two major suppliers. This enables them to work together more smoothly for their mutual benefit and makes the supplier more responsive to the customer's needs.

Honda picked Donnelly Corp. to make all the mirrors for its U.S.-manufactured cars. Honda chose Donnelly because it learned enough about the firm to know it did high-quality work and that its corporate culture and values were consistent with those endorsed by Honda. Recognizing the value of Honda as a customer, Donnelly built an entirely new plant to make the mirrors. And all this was accomplished with only a handshake. Motorola goes even further, providing its principal suppliers with access to its own renowned quality training program and evaluating the performance of each supplier as a way of helping that firm boost its own quality.

Regulators **Regulators** are elements of the task environment that have the potential to control, legislate, or influence an organization's policies and practices. There are two important kinds of regulators. The first, **regulatory agencies**, are created by the government to protect the public from certain business practices or to protect organizations from one another. Powerful federal regulatory agencies include the Environmental Protection Agency (EPA), the Securities and Exchange Commission (SEC), the Food and Drug Administration (FDA), and the Equal Employment Opportunity Commission (EEOC).

regulator A unit that has the potential to control, legislate, or influence an organization's policies and practices

regulatory agency An agency created by the government to protect the public from certain business practices or to protect organizations from one another

Many of these agencies play important roles in protecting the rights of individuals. The FDA, for example, helps ensure that the food we eat is free from contaminants and thus is an important regulator for McDonald's. At the same time, many managers complain that there is too much government regulation. Most large companies must devote thousands of labor hours and hundreds of thousands of dollars a year to comply with government regulations. To complicate the lives of managers even more, different regulatory agencies sometimes provide inconsistent—or even contradictory—mandates.

For example, several years ago the *Exxon Valdez* tanker ran aground, spilling 11 million gallons of crude oil off the coast of Alaska. The Environmental Protection Agency (EPA) forced Exxon to cover the costs of the ensuing cleanup. Since many observers thought that the ship's captain was drunk at the time, the EPA also mandated that Exxon impose stricter hiring standards for employees in high-risk jobs. To comply with this mandate, Exxon adopted a policy of not assigning anyone with a history of alcohol or substance abuse to certain jobs like tanker captain. However, another regulatory agency, the Equal Employment Opportunity Commission (EEOC), then sued Exxon on the grounds that restricting people who have been

Danny Shanahan



The regulatory environment of business imposes numerous constraints on organizations. Laws regarding employment practices have become particularly complicated in recent years. For example, a firm that uses discriminatory practices can be sued for not hiring someone or for firing a current employee. But the firm can also be penalized if it should reject or fire someone but fails to do so! Not surprisingly, then, many employment decisions today are routinely reviewed by attorneys. And the opinions of these attorneys often determine whether or not someone will be hired or fired.

rehabilitated from alcohol abuse from any job violates their rights under the Americans with Disabilities Act. Exxon was thus forced to change its policy, but was then again criticized by the EPA. The cartoon provides another take on this type of issue.

The regulatory environment in other countries, however, is even more stringent. When U.S. retailer Wal-Mart wants to open a new store, its regulatory requirements are actually quite low and the procedures it must follow are clearly spelled out. In a sense, within reason and general basic ground rules, the firm can open a store just about anywhere it wants and operate it in just about any manner it wants. But conditions in Germany are quite different. That country's largest retailer, Allkauf, tried to open a store in one town—on land that it already owned—for over fifteen years. But the city government did not allow it because it feared that local competitors would suffer. And by German law Allkauf's existing stores can be open only 68.5 hours a week; they must close no later than 6:30 P.M. on weekdays and 2:00 P.M. on Saturday, and must remain closed on Sunday. And they can only hold large sales twice a year and can never discount food items.

interest group A group organized by its members to attempt to influence organizations

The other basic form of regulator is the interest group. An **interest group** is organized by its members to attempt to influence organizations. Prominent interest groups include the National Organization for Women (NOW), Mothers Against Drunk Driving (MADD), the National Rifle Association (NRA), the League of Women Voters, the Sierra Club, Ralph Nader's Center for the Study of Responsive Law, the Consumers Union, and industry self-regulation groups like the Council of Better Business Bureaus. Although interest groups lack the official power of government agencies, they can exert considerable influence by using the media to call attention to their positions. MADD, for example, puts considerable pressure on alcoholic-beverage producers (to put warning labels on their products), automobile companies (to make it more difficult for intoxicated people to start their cars), local governments (to stiffen drinking ordinances), and bars and restaurants (to refuse to sell alcohol to people who are drinking too much).

strategic partner or **ally** An organization working together with one or more other organizations in a joint venture or other partnership

Strategic Partners A final dimension of the task environment is **strategic partners** (also called **strategic allies**)—two or more organizations that work together in joint ventures or other partnerships.[10] As shown in Figure 3.3, McDonald's has several strategic partners. For example, it has one arrangement with Wal-Mart whereby small McDonald's restaurants are built in many Wal-Mart stores. The firm also has a long-term deal with Disney; McDonald's will promote Disney movies in its stores, and Disney will build McDonald's restaurants or kiosks in its theme parks. And many of the firm's foreign stores are built in collaboration with local investors. Strategic partnerships help companies get from other companies the expertise they lack. They also help spread risk and open new market opportunities. Indeed, most strategic partnerships are actually among international firms. For example, Ford has strategic partnerships with Volkswagen (sharing a distribution and service center in South America) and Nissan (building minivans in the United States).

MANAGEMENT IMPLICATIONS The external environment of an organization can appear complex and ambiguous. Managers can help bring order to this complexity and ambiguity by realizing that some parts of the external environ-

ment are of a more general character (the general environment), while others are more concrete and definable (the task environment). This understanding allows managers to monitor all parts of the environment while focusing more attention on and being more responsive to those dimensions most relevant to the organization itself.

■ The Internal Environment

As shown earlier in Figure 3.1, organizations also have an internal environment that consists of their owners, board of directors, employees, and the physical work environment. (Another especially important part of the internal environment is the organization's culture, discussed separately in Chapter 6.)

Owners

The **owners** of a business are, of course, the people who have legal property rights to that business. Owners can be a single individual who establishes and runs a small business, partners who jointly own the business, individual investors who buy stock in a corporation, or other organizations. McDonald's has 700 million shares of stock, each of which represents one unit of ownership of the firm. The family of McDonald's founder Ray Kroc stills owns a large block of this stock, as do several large institutional investors. In addition, there are thousands of individuals who own just a few shares each. McDonald's, in turn, also owns other businesses. For example, it owns several large regional bakeries that supply its restaurants with buns. These are each incorporated as separate legal entities and managed as wholly-owned subsidiaries by the parent company. McDonald's has also recently bought partial ownership of Chipotle Mexican Grill and Donatos Pizza chain.

owner Someone who has legal property rights to a business

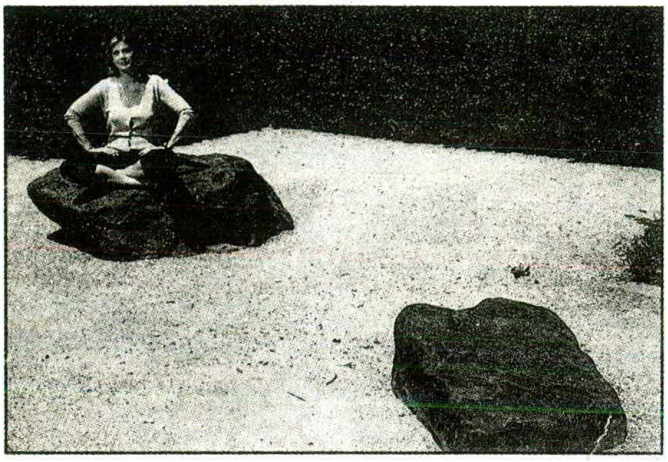
Board of Directors

A corporate **board of directors** is elected by the stockholders and is charged with overseeing the general management of the firm to ensure that it is being run in a way that best serves the stockholders' interests. Some boards are relatively passive. They perform a general oversight function but seldom get actively involved in how the company is really being run. But this trend is changing, however, as more and more boards are more carefully scrutinizing the firms they oversee and exerting more influence over how they are being managed.

board of directors Governing body elected by a corporation's stockholders and charged with overseeing the general management of the firm to ensure that it is being run in a way that best serves the stockholders' interests

Employees

An organization's employees are also a major element of its internal environment. *Managing in an E-business World* discusses what can happen when a firm's own employees disagree over business strategy. Of particular interest to managers



Employees are a critical part of an organization's internal environment. Ann Bamesberger is director of workplace effectiveness for Sun Microsystems. Her primary responsibilities are to insure that employees and workplaces are appropriately aligned so that the goals of individual employees and the goals of the company are all met. Ms. Bamesberger is very creative when it comes to workplace design. She gives employees a big say in how their workplace is designed and is very open to letting them work at home and/or design their offices in whatever way they think works best for them.

today is the changing nature of the workforce as it becomes increasingly more diverse in terms of gender, ethnicity, age, and other dimensions. Workers are also calling for more job ownership—either partial ownership in the company or at least more say in how they perform their jobs.[11] Another trend in many firms is the increased reliance on temporary workers—individuals hired for short periods of time with no expectation of permanent employment. Employers often prefer to use "temps" because they provide greater flexibility, earn lower wages, and often do not participate in benefits programs. But these managers also have to deal with what often amounts to a two-class workforce and with a growing number of employees who have no loyalty to the organization where they work because they may be working for a different one tomorrow.[12]

The permanent employees of many organizations are organized into labor unions, representing yet another layer of complexity for managers. The National Labor Relations Act of 1935 requires organizations to recognize and bargain with a union if that union has been legally established by the organization's employees. Presently, around 23 percent of the U.S. labor force is represented by unions. Some large firms such as Ford, Exxon, and General Motors have several different unions. Even when an organization's labor force is not unionized, its managers do not ignore unions. For example, Kmart, J. P. Stevens, Honda of America, and Delta Air Lines all actively work to avoid unionization. And even though people think primarily of blue-collar workers as union members, many white-collar workers such as government employees and teachers are also represented by unions.

Physical Work Environment

A final part of the internal environment is the actual physical environment of the organization and the work that people do. Some firms have their facilities in downtown skyscrapers, usually spread across several floors. Others locate in suburban or rural settings and may have facilities more closely resembling a college campus. Some facilities have long halls lined with traditional offices. Others have modular cubicles with partial walls and no doors. The top one hundred managers at Mars, makers of Snickers and Milky Way, all work in a single large room. Two co-presidents are located in the very center of the room, while others are arrayed in concentric circles around them. Increasingly, newer facilities have an even more open arrangement where people work in large rooms, moving between different tables to interact with different people on different projects. Free-standing computer workstations are available for those who need them, and a few small rooms might be off to the side for private business.[13]

MANAGING IN AN *e*-BUSINESS WORLD

SEEKING A HARMONIOUS E-BUSINESS STRATEGY

The e-business revolution has brought innovation—and dissension—to the music industry. Sony, a leader in consumer electronics, pioneered the Walkman and other devices for recording and listening to music. Sony has also been a major force in the recording side of the music business, distributing songs by Celine Dion, Savage Garden, and other artists. Even as Web-based technology was reshaping the way people obtain songs, managers at the two Sony music divisions were unable to agree on one consistent strategy.

Both divisions were eyeing the rising popularity of MP3 and similar software used to digitize songs for downloading from the Internet. Managers at Sony's record labels worried that this type of technology would lead to illegal copying of songs and thus hurt CD sales. They wanted to go slow and wait for an industry test of on-line music sales. Sony's electronics division already had some intriguing music technology in the works. Its managers saw how the Internet was changing consumer behavior, and they believed the public would soon be ready to buy portable players for listening to downloaded music.

The two divisions argued about an overall direction for more than a year. The stakes are high: nearly one billion CDs were being sold every year, and Sony's music revenues topped $6 billion. Meanwhile, Sony's top management began investing in Internet music companies and negotiating agreements for digital-music and copyright-protection technologies. Customer habits were changing so rapidly that the company could not afford to ignore the digital music movement—especially with over thirteen million consumers using the Napster web site to download and trade digital music files for free.

Sony's president finally intervened, establishing a committee to resolve the issues so the company could move forward with a suitable strategy. Within months, the company was showing prototypes of new devices to store and play digital music downloaded from web sites. Although the U.S. music industry was not yet prepared for full-scale digital downloading, Sony was selling copyright-protected downloadable songs in Japan by the end of 1999. Now Sony was fully committed to an e-business music strategy.

People didn't want to go too fast. It could have had a lot of repercussions.

—Masao Morita, head of Sony Music Entertainment Japan's international business*

References: Robert A. Guth, "Inside Sony, A Clash Over Web Music," *Wall Street Journal*, January 26, 2000, pp. B1, B4 (*quote on p. B1); Alex Berenson and Matt Richtel, "Heartbreakers, Dream Makers," *New York Times*, June 25, 2000, sec. 3, pp. 1, 6.

MANAGEMENT IMPLICATIONS While managers strive to align their organizations with the external environment, they must also remember that their own work is carried out within the internal environment of their organizations. Owners, a corporate board of directors, employees, the physical environment, and the organization's culture interact to define the environment of managers.

■ *Organization-Environment Relationships*

Our discussion to this point has identified and described the various dimensions of organizational environments. Because organizations are open systems, they interact with these various dimensions in many different ways. Hence, we will now

examine those interactions. First we discuss how environments affect organizations and then note several ways in which organizations adapt to their environments.

How Environments Affect Organizations

Three basic perspectives can be used to describe how environments affect organizations: environmental change and complexity, competitive forces, and environmental turbulence.[14]

Environmental Change and Complexity James D. Thompson was one of the first people to recognize the importance of the organization's environment.[15] Thompson suggests that the environment can be described along two dimensions: its degree of change and its degree of homogeneity. The degree of change is the extent to which the environment is relatively stable or relatively dynamic. The degree of homogeneity is the extent to which the environment is relatively simple (few elements, little segmentation) or relatively complex (many elements, much segmentation). These two dimensions interact to determine the level of uncertainty faced by the organization. **Uncertainty**, in turn, is a driving force that influences many organizational decisions. Figure 3.4 illustrates a simple view of the four levels of uncertainty defined by different levels of homogeneity and change.

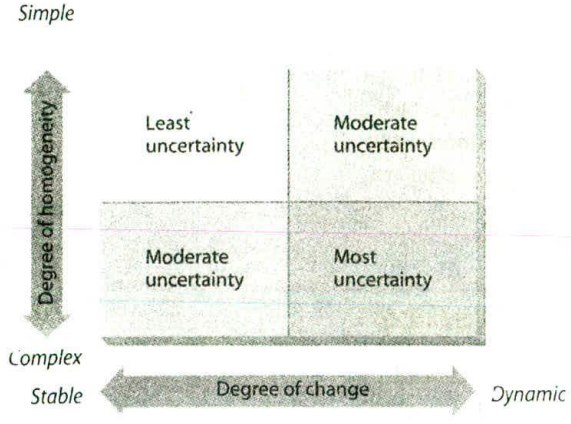
uncertainty A driving force caused by change and complexity that influences many organizational decisions

The least environmental uncertainty is faced by organizations with stable and simple environments. Although no environment is totally without uncertainty, some entrenched franchised food operations (such as Subway and Taco Bell) and many container manufacturers (like Ball Corporation and Federal Paper Board) have relatively low levels of uncertainty to contend with. Subway, for example, focuses on a certain segment of the consumer market, produces a limited product line, has a constant source of suppliers, and faces relatively consistent competition.

Figure 3.4

Environmental Change, Complexity, and Uncertainty

The degree of homogeneity and the degree of change combine to create uncertainty for organizations. For example, a simple and stable environment creates the least uncertainty, and a complex and dynamic environment creates the most uncertainty.



Source: Adapted from J. D. Thompson, *Organizations in Action*. Copyright © 1967 by McGraw-Hill. Reprinted by permission of The McGraw-Hill Companies.

Organizations with dynamic but simple environments generally face a moderate degree of uncertainty. Examples of organizations functioning in such environments include clothing manufacturers (targeting a certain kind of clothing buyer but sensitive to fashion-induced changes) and compact disc (CD) producers (catering to certain kinds of music buyers but alert to changing tastes in music). Levi Strauss faces relatively few competitors (Wrangler and Lee), has few suppliers and few regulators, and uses limited distribution channels. This relatively simple task environment, however, also changes quite rapidly as competitors adjust prices and styles, consumer tastes change, and new fabrics become available.

Another combination of factors is one of stability and complexity. Again, a moderate amount of uncer-

tainty results. Ford, DaimlerChrysler, and General Motors face these basic conditions. Overall, they must interact with a myriad of suppliers, regulators, consumer groups, and competitors. Change, however, occurs quite slowly in the automobile industry. Despite many stylistic changes, cars of today still have four wheels, a steering wheel, an internal combustion engine, a glass windshield, and many of the other basic features that have characterized cars for decades.

Finally, very dynamic and complex environmental conditions yield a high degree of uncertainty. The environment has a large number of elements, and the nature of those elements is constantly changing. Intel, Compaq, IBM, Sony, and other firms in the electronics field face these conditions because of the rapid rate of technological innovation and change in consumer markets that characterize their industry, their suppliers, and their competitors. Likewise, Internet-based firms like eBay and Amazon.com face similar high levels of uncertainty.



Organizations and their environments affect each other in a variety of ways. For example, gasoline prices in Europe are considerably higher than they are in the United States—recent prices for a gallon of gasoline were $4.29 in London, $3.64 in Italy, and $3.58 in Belgium. In each case well over half the price is tax. To protest high prices, these truckers in Belgium worked together to blockade a major highway for several hours. In this one instance, oil companies, government agencies, and transportation firms all affect one another in a variety of ways.

Competitive Forces Although Thompson's general classifications are useful and provide some basic insights into organization-environment interactions, in many ways they lack the precision and specificity needed by managers who must deal with their environments on a day-to-day basis. Michael E. Porter, a Harvard professor and expert in strategic management, has proposed a more refined way to assess environments. In particular, he suggests that managers view the environment of their organizations in terms of **five competitive forces**.[16]

five competitive forces The threat of new entrants, competitive rivalry, the threat of substitute products, the power of buyers, and the power of suppliers

The *threat of new entrants* is the extent to which new competitors can easily enter a market or market segment. It takes a relatively small amount of capital to open a dry-cleaning service or a pizza parlor, but it takes a tremendous investment in plant, equipment, and distribution systems to enter the automobile business. Thus, the threat of new entrants is fairly high for a local hamburger restaurant but fairly low for Ford and Toyota. The arrival of the Internet has reduced the costs and other barriers of entry in many market segments, however, so the threat of new entrants has increased for many firms in recent years.

Competitive rivalry is the nature of the competitive relationship between dominant firms in the industry. In the soft-drink industry, Coca-Cola and Pepsi often engage in intense price wars, comparative advertising, and new-product introductions. Other firms that have intense rivalries include American Express and Visa, and Fuji and Kodak. And U.S. auto companies continually try to outmaneuver each other with warranty improvements and rebates. Xerox also faces extreme

competition from a variety of firms.[17] Local car-washing establishments, in contrast, seldom engage in such practices.

The *threat of substitute products* is the extent to which alternative products or services may supplant or diminish the need for existing products or services. The electronic calculator eliminated the need for slide rules. The advent of personal computers, in turn, has reduced the demand for calculators as well as for typewriters and large mainframe computers. Nutra-Sweet is a viable substitute product threatening the sugar industry. And DVD players may render VCRs obsolete in the next few years.

The *power of buyers* is the extent to which buyers of the products or services in an industry have the ability to influence the suppliers. For example, a Boeing 747 has relatively few potential buyers. Only companies such as Delta, Northwest, and KLM Royal Dutch Airlines can purchase them. Hence, these buyers have considerable influence over the price they are willing to pay, the delivery date for the order, and so forth. On the other hand, some DaimlerChrysler dealerships charged premium prices for the company's PT Cruiser, introduced to high demand in mid-2000. They could charge these prices because if the first buyer wouldn't pay the price, two more customers were waiting in line who would. In this case, buyers had virtually no power.

The *power of suppliers* is the extent to which suppliers have the ability to influence potential buyers. The local electric company is the only source of electricity in your community. Subject to local or state regulation (or both), it can therefore charge what it wants for its product, provide service at its convenience, and so forth. Likewise, even though Boeing has few potential customers, those same customers have only two suppliers that can sell them a 300-passenger jet (Boeing and Airbus, a European firm). So Boeing, too, has power. Indeed, the firm recently exercised its power by entering into long-term, sole supplier agreements with three major U.S. airlines.[18] On the other hand, a small vegetable wholesaler has little power in selling to restaurants because if they don't like the produce, they can easily find an alternative supplier.

Environmental Turbulence Although always subject to unexpected changes and upheavals, the five competitive forces can nevertheless be studied and assessed systematically and plans developed for dealing with them. At the same time, though, organizations also face the possibility of environmental change or turbulence, occasionally with no warning at all. The most common form of organizational turbulence is a crisis of some sort.

For example, in mid-1999 reports surfaced in Belgium that several dozen local schoolchildren had become nauseous after drinking Coca-Cola. Similar reports subsequently started coming from France, Luxembourg, and the Netherlands. France quickly ordered Coke to cease production in its Dunkirk bottling plant; other countries in the region started banning all Coca-Cola products. The firm eventually traced its problems to defective carbon dioxide in one plant and to wood preservative leaking onto cans in another. While no truly serious health problems resulted, Coke nevertheless lost considerable income and suffered a blow to its public image as a result of all the bad publicity it received.[19]

Other notable examples of crises include the crash of the space shuttle *Challenger* in 1986, which essentially paralyzed the U.S. space program for almost three years; product tampering aimed at Tylenol in 1982, which cost Johnson & Johnson $750 million in product recalls and changes in packaging and product design; and the 2000 crash of an Alaska Airlines plane that killed everyone on board. Another type of crisis that has captured the attention of managers in recent years is workplace violence—situations in which disgruntled workers or former workers assault other employees, often resulting in injury and sometimes in death. Finally, yet another kind of crisis that can affect business today, as detailed more fully in *Management InfoTech*, is the rapid spread of computer viruses such as the so-called love bug, which shut down businesses around the world in early 2000.

Such crises affect organizations in different ways, and many organizations are developing crisis plans and teams.[20] When a Delta Air Lines plane crashed at the

MANAGEMENT INFOTECH

Viruses Add to Environmental Uncertainty

Who could resist opening an e-mail love letter?

When computer users opened an e-mail with the subject line, "I love you," they unleashed a computer virus that clogged electronic systems around the world in a matter of hours. Dubbed the "love bug," this virus infected computer networks at Ford, the U.S. Congress, the British Parliament, Nomura Securities in Japan, and nearly everywhere in between.

The virus lay hidden in an e-mail disguised as a love letter. Once a computer user opened the e-mail attachment, the virus launched itself and looked for the user's Microsoft Outlook mail program. Then it sent copies of its nasty attachment to every name in the user's on-line address book. These copies looked as though they actually came from the user, which is why recipients were tempted to open them. Some recipients maintained extensive on-line address books, so the virus spread quickly from user to user and organization to organization. The huge volume of messages crippled some corporate e-mail systems. Adding insult to injury, once the love bug was launched, it also damaged sound and graphics files on the recipient's hard drive.

The love bug virus demonstrated how computer problems are adding to the uncertainty of the organizational environment. First, no two viruses are exactly the same, so new viruses mean more change—and more scrambling to cope with the change. Second, managers never know what form a virus will take or when it will strike, yet they must plan in advance to prevent disasters.

The less destructive Melissa virus, which circulated a year before the love bug, was regarded as a wake-up call for organizations to strengthen their antivirus safeguards. However, months without any major virus attacks may have lulled computer users into a false sense of complacency. By the time the love bug emerged, people opened it without worrying about potential viruses. Now, while computer security firms develop new ways of detecting and disabling viruses, hackers are working on new types of viruses. The best antidote to this uncertainty remains prevention—training employees to leave suspicious e-mails (even love letters) unopened.

All the technology in the world and they can't stop it from happening because people won't act responsibly.

*—Richard Power, Computer Security Institute.**

Reference: Kevin Maney, "Tainted Love," *Wall Street Journal*, May 5, 2000, pp. 1B–2B (*quote on p. 2B).

Dallas–Fort Worth airport a few years ago, for example, fire-fighting equipment was at the scene in minutes. Only a few flights were delayed, and none had to be canceled. Similarly, a grocery store in Boston once received a threat that someone had poisoned cans of its Campbell's tomato juice. Within six hours, a crisis team from Campbell Soup Co. removed two truckloads of juice from all eighty-four stores in the grocery chain. Still, far too few companies in the United States have a plan for dealing with major crises.

How Organizations Adapt to Their Environments

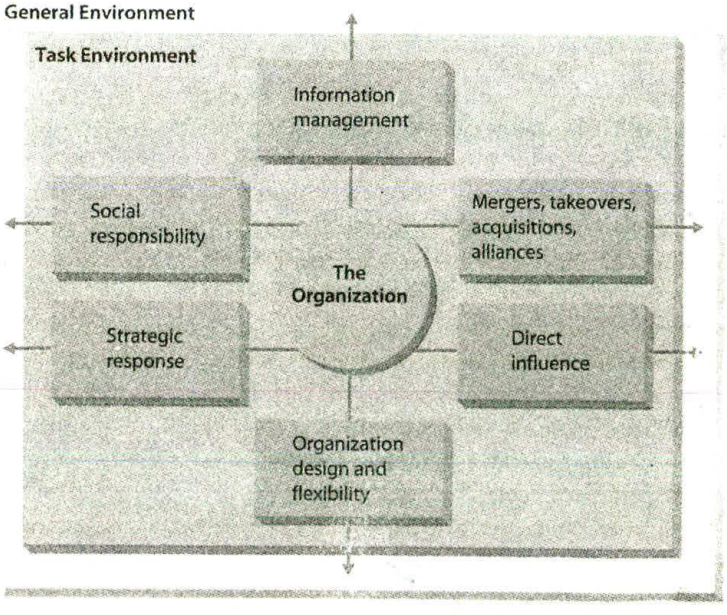
Given the myriad issues, problems, and opportunities in an organization's environments, how should the organization adapt? Obviously, each organization must assess its own unique situation and then adapt according to the wisdom of its senior management. Figure 3.5 illustrates the six basic mechanisms through which organizations adapt to their environment. One of these, social responsibility, is given special consideration in Chapter 4.

Information Management One way organizations adapt to their environment is through information management. Information management is especially important when forming an initial understanding of the environment and when monitoring the environment for signs of change. One technique for managing information is relying on boundary spanners. A *boundary spanner* is an employee, such as a sales representative or a purchasing agent, who spends much of his or

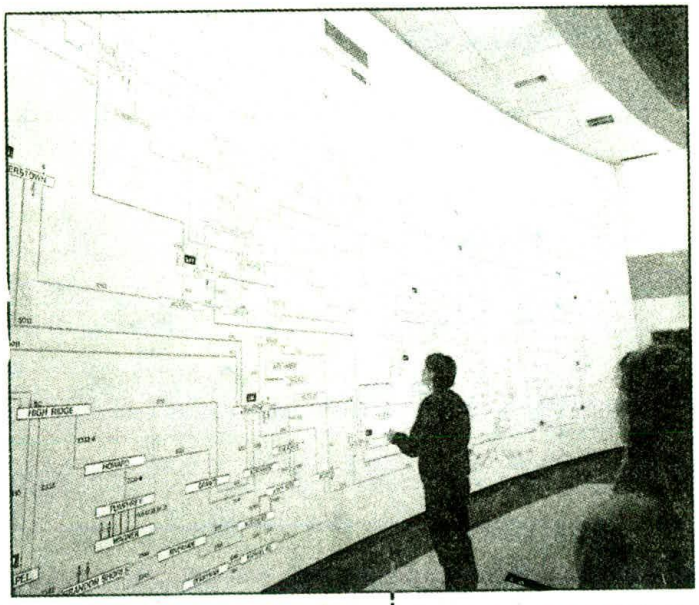
Figure 3.5

How Organizations Respond to Their Environments

Organizations attempt to influence their environments. The most common methods are through information management, strategic response, mergers, takeovers, acquisitions, alliances, organization design and flexibility, and direct influence.



her time in contact with others outside the organization. Such people are in a good position to learn what other organizations are doing. All effective managers engage in *environmental scanning*, the process of actively monitoring the environment through activities such as observation and reading. Within the organization, most firms have also established computer-based *information systems* to gather and organize relevant information for managers and to assist in summarizing that information in the form most pertinent to each manager's needs. (Information systems are covered more fully in Chapter 22.)



Organizations attempt to adapt to their environments in a variety of different ways. PJM Interconnection manages the entire electrical grid for the Middle Atlantic region of the United States. This means that PJM managers must remain continually on top of power supplies and power usage to maintain the optimum balance of electric power across the entire grid. Information management, then, is a key element in how PJM operates. Charts such as this one are updated constantly so as to provide decision makers with the information they need to keep the power flowing properly.

Strategic Response Another way that an organization adapts to its environment is through a strategic response. Options include maintaining the status quo (for example, if an organization's management believes that it is doing very well with its current approach), altering strategy a bit, or adopting an entirely new strategy. If the market that a company currently serves is growing rapidly, the firm might decide to invest even more heavily in products and services for that market. Likewise, if a market is shrinking or does not provide reasonable possibilities for growth, the company may decide to cut back. For example, during the late 1990s managers at Starbucks realized that the firm's growth opportunities in the United States were slowing simply because there already were so many Starbucks coffee shops. Accordingly, they devised a new plan to expand aggressively into international markets, thus providing an avenue for continued rapid growth.

Mergers, Acquisitions, and Alliances A related strategic approach that some organizations use to adapt to their environment involves mergers, acquisitions, and partnerships. A *merger* occurs when two or more firms combine to form a new firm. For example, DaimlerChrysler was created as a result of a merger between Daimler-Benz (a German firm) and Chrysler (a U.S. company). An *acquisition* occurs when one firm buys another, sometimes against its will (usually called a hostile takeover). The firm taken over may cease to exist and becomes part of the other company. For example, as part of its international expansion Starbucks bought a British coffee shop chain called the Seattle Coffee Company. Starbucks then systematically changed each Seattle Coffee outlet into a Starbucks coffee shop.

In other cases, the acquired firm often continues to operate as a subsidiary of the acquiring company. Royal Caribbean Cruise Lines bought controlling interest in Celebrity Cruise Lines but maintains it as a separate cruise line. And as already

discussed, in a *partnership* or *alliance* the firm undertakes a new venture with another firm. A company engages in these kinds of strategies for a variety of reasons, such as easing entry into new markets or expanding its presence in a current market.

Organization Design and Flexibility An organization may also adapt to environmental conditions by incorporating flexibility in its structural design. For example, a firm that operates in an environment with relatively low levels of uncertainty might choose to use a design with many basic rules, regulations, and standard operating procedures. Alternatively, a firm that faces a great deal of uncertainty might choose a design with relatively few standard operating procedures, instead allowing managers considerable discretion and flexibility over decisions. The former type, sometimes called a mechanistic organization design, is characterized by formal and rigid rules and relationships. The latter, sometimes called an organic design, is considerably more flexible and permits the organization to respond quickly to environmental change. We learn much more about these and related issues in Chapter 12.

Direct Influence of the Environment Organizations are not necessarily helpless in the face of their environments. Indeed, many organizations are able to influence their environment directly in many different ways. For example, firms can influence their suppliers by signing long-term contracts with fixed prices as a hedge against inflation. Or a firm might become its own supplier. Sears, for example, owns some of the firms that produce the goods it sells, and Campbell Soup Company makes its own soup cans. Similarly, almost any major activity a firm engages in affects its competitors. When Mitsubishi lowers the prices of its DVD players, Sony may be forced to follow suit. Organizations also influence their customers by creating new uses for a product, finding entirely new customers, and taking customers away from competitors. Organizations also influence their customers by convincing them that they need something new. Automobile manufacturers use this strategy in their advertising to convince people that they need a new car every two or three years.

Organizations influence their regulators through lobbying and bargaining. Lobbying involves sending a company or industry representative to Washington in an effort to influence relevant agencies, groups, and committees. For example, the U.S. Chamber of Commerce lobby, the nation's largest business lobby, has an annual budget of more than $100 million. The automobile companies have been successful on several occasions in bargaining with the EPA to extend deadlines for compliance with pollution control and mileage standards. Continental Airlines routinely criticizes what it considers an antiquated air traffic control system in an effort to get the U.S. government to upgrade its technology and systems.

MANAGEMENT IMPLICATIONS Managers should remember that their organization is influenced by a wide array of forces and elements in the external environment. Some of these forces and elements are relatively easy to recognize

and anticipate, while others are more unpredictable or even impossible to anticipate. Fortunately, managers can adopt one or more strategies to adapt to their environment. While some events are, of course, uncontrollable, managers can at least buffer their organizations to some extent through the astute use of these strategies.

■ The Environment and Organizational Effectieness

Earlier in this chapter we noted the vital importance of maintaining proper alignment between the organization and its environments. The various mechanisms through which environments and organizations influence one another can cause this alignment to shift, however, and even well-managed organizations sometimes slip from their preferred environmental position. But well-managed companies recognize when this happens and take corrective action to get back on track. In Chapter 1 we said that effectiveness involved doing the right things. Given the interactions between organizations and their environments, it follows that effectiveness is ultimately related to how well an organization understands, reacts to, and influences its environment.[21]

Models of Organizational Effectiveness

Unfortunately, there is no consensus about how to measure effectiveness. For example, an organization can make itself look extremely effective in the short term by ignoring research and development (R&D), buying cheap materials, ignoring quality control, and skimping on wages. Over time, though, the firm will no doubt falter. On the other hand, taking action consistent with a long-term view, such as making appropriate investments in R&D, may displease investors who have a short-term outlook. Little wonder, then, that there are many different models of organizational effectiveness.

The *systems resource* approach to organizational effectiveness focuses on the extent to which the organization can acquire the resources it needs.[22] A firm that can get raw materials during a shortage is effective from this perspective. The *internal processes approach* deals with the internal mechanisms of the organization and focuses on minimizing strain, integrating individuals and the organization, and conducting smooth and efficient operations.[23] An organization that focuses primarily on maintaining employee satisfaction and morale and being efficient subscribes to this view. The *goal approach* focuses on the degree to which an organization obtains its goals.[24] When a firm establishes a goal of increasing sales by 10 percent and then achieves that increase, the goal approach maintains that the organization is effective. Finally, the *strategic constituencies approach* focuses on the groups that have a stake in the organization.[25] In this view, effectiveness is the extent to which the organization satisfies the demands and expectations of all these groups.

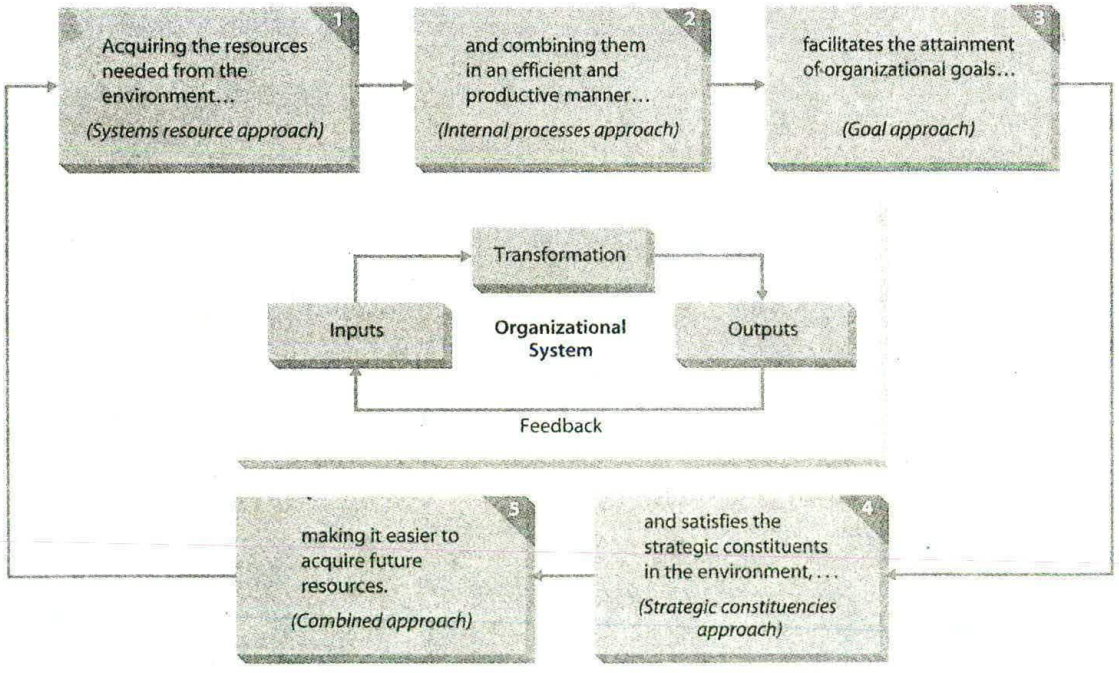
Although these four basic models of effectiveness are not necessarily contradictory, they do focus on different things. The systems resource approach focuses on inputs, the internal processes approach focuses on transformation processes, the goal approach focuses on outputs, and the strategic constituencies approach focuses on feedback. Thus, rather than adopting a single approach, organizational effectiveness can best be understood by an integrated perspective, such as the one illustrated in Figure 3.6. At the core of this unifying model is the organizational system, with its inputs, transformations, outputs, and feedback. Surrounding this core are the four basic approaches to effectiveness as well as a combined approach, which incorporates each of the other four. The basic argument is that an organization must essentially satisfy the requirements imposed on it by each of the effectiveness perspectives.

Achieving organizational effectiveness is not an easy task. The key to doing so is understanding the environment in which the organization functions. With this understanding as a foundation, managers can then chart the "correct" path for the

Figure 3.6

A Model of Organizational Effectiveness

The systems resource, internal processes, goal, and strategic constituencies each focuses on a different aspect of organizational effectiveness. Thus, they can be combined to create an overall integrative perspective on effectiveness.



organization as it positions itself in that environment. If managers can identify where they want the organization to be relative to other parts of their environment, and how best to get there, they stand a good chance of achieving effectiveness. On the other hand, if they pick the wrong target to aim for, or if they go about achieving their goals in the wrong way, they are likely to be less effective.

Examples of Organizational Effectiveness

Given the various models and perspectives on organizational effectiveness, it's not surprising that even the experts do not always agree on which companies are most effective. For example, for years *Fortune* has compiled an annual list of the "most admired" companies in the United States. Based on a large survey of leading executives, the rankings presumably reflect the organizations' innovativeness; quality of management; value as a long-term investment; community and environmental responsibility; quality of products and services; financial soundness; use of corporate assets; and ability to attract, develop, and keep talented people. The 2000 list of *Fortune's* ten most admired firms is shown in Table 3.1.

Also illustrated in the table is a list published in *Business Week*, also in 2000. This list represents the ten best performing companies in the United States as determined by revenue and profit growth, return on investment, net profit margins, and return on equity over periods of one and three years. Interestingly, there are more differences than similarities between the lists. Given that "admiration" and "performance" would each seem to be highly related to effectiveness, a stronger correspondence between the two lists might have been expected. It is important to note, of course, that different variables and methods are used to develop the two lists, and every firm included on one list but not the other is still a very well-managed company. But the disparities in the lists also underscores the difficulties and judgment calls that are involved when trying to evaluate the effectiveness of any given company or organization.

MANAGEMENT IMPLICATIONS Managers need to remember that the performance of their organization is best evaluated from a multifaceted and dynamic point of view. No one single measure or calculation can be used to judge effectiveness. Instead, effectiveness must be approached from several perspectives. Moreover, managers should also keep in mind that even experts may disagree about what constitutes effectiveness and how different organizations compare to one another.

Table 3.1

Examples of Admired and High-Performing Firms

***Fortune's* Most Admired Companies (2000)**	***Business Week's* Best Performing Companies (2000)**
1. General Electric	1. Microsoft
2. Microsoft	2. Time Warner
3. Dell Computer	3. Cisco Systems
4. Cisco Systems	4. Oracle
5. Wal-Mart	5. EMC
6. Southwest Airlines	6. Citrix Systems
7. Berkshire Hathaway	7. Morgan Stanley Dean Witter
8. Intel	8. Gap
9. Home Depot	9. Warner-Lambert
10. Lucent Technologies	10. Lucent Technologies

Source: "America's Most Admired Companies," *Fortune*, February 21, 2000, pp. 108–110; "The Business Week 50," *Business Week*, March 27, 2000, pp. 123–125.

Summary of Key Points

Environmental factors play a major role in determining an organization's success or failure. Managers should strive to maintain the proper alignment between their organization and its environment. All organizations have both external and internal environments.

The external environment is composed of general and task environment layers. The general environment is composed of the nonspecific elements of the organization's surroundings that might affect its activities. It consists of five dimensions: economic, technological, sociocultural, political-legal, and international. The effects of these dimensions on the organization are broad and gradual. The task environment consists of specific dimensions of the organization's surroundings that are very likely to influence the organization. It also consists of five elements: competitors, customers, suppliers, regulators, and strategic partners. Because these dimensions are associated with specific organizations in the environment, their effects are likely to be more direct and immediate.

The internal environment consists of the organization's owners, board of directors, employees, physical work environment, and culture (discussed separately in Chapter 6). Owners are those who have property rights claims on the organization. The board of directors, elected by stockholders, is responsible for overseeing a firm's top managers. Individual employees and the labor unions they sometimes join are other important parts of the internal environment. The physical environment, yet another part of the internal environment, varies greatly across organizations.

Organizations and their environments affect each other in several ways. Environmental influences on the organization can occur through uncertainty, competitive forces, and turbulence. Organizations, in turn, use information management; strategic response; mergers, acquisitions, and alliances; organization design and flexibility; direct influence; and social responsibility to adapt to their task environments.

One important indicator of how well an organization deals with its environment is its level of effectiveness. Organizational effectiveness requires that the organization do a good job of procuring resources, managing them properly, achieving its goals, and satisfying its constituencies. Because of the complexities associated with meeting these requirements, however, experts may disagree about the effectiveness of any given organization at any given point in time.

Discussion Questions

Questions for Review

1. Why is an organization's environment so important? Identify and discuss each of the major dimensions of the general environment.
2. What is an organization's task environment? What are the major dimensions of that environment?
3. What are the major forces that affect organization-environment relationships? Describe those forces.
4. What is organizational effectiveness? How is it studied and assessed?

Questions for Analysis

5. Can you think of dimensions of the task environment that are not discussed in the text? Indicate their linkage to those that are discussed.
6. Some organizations become part-owners of other firms through mergers and acquisitions. How does the nature of partial ownership complicate the organization-environment relationship?
7. How would each dimension of an organization's task environment and internal envi-

ronment assess the organization's effectiveness? Can an organization be equally effective to each of these different groups? Why or why not?

Questions for Application

8. Go to the library and research a company. Characterize its level of effectiveness according to each of the four basic models. Share your results with the class.
9. Interview a manager from a local organization about his or her organization's environments—general, task, and internal. In the course of the interview, are all of the major dimensions identified? Why or why not?
10. Outline the several environments of your college or university. Be detailed about the dimensions, and provide specific examples to illustrate how each dimension affects your institution.

BUILDING EFFECTIVE *time management* SKILLS

Exercise Overview

Time-management skills refer to the manager's ability to prioritize work, to work efficiently, and to delegate appropriately. This exercise will provide you with an opportunity to relate time-management issues to environment pressures and opportunities.

Exercise Background

As discussed in this chapter, managers and organizations must be sensitive to a variety of environment dimensions and forces reflected in the general, task, and internal environments. The general environment consists of the economic, technological, political-legal, sociocultural, and international dimensions. The task environment includes competitors, customers, suppliers, regulators, and strategic partners. The internal environment consists of owners, board of directors, employees, and the physical work environment.

The problem faced by managers is that time is a finite resource. There are only so many hours in a day and only so many tasks that can be accomplished in a given period of time. Thus, managers must constantly make choices about how they spend their time. Clearly, of course, they should try to use their time wisely and direct it at the more important challenges and opportunities they face. Spending time on a trivial issue while neglecting an important issue is a mistake.

Time-management experts often suggest that managers begin each day by listing what they need to accomplish that day. After the list is compiled, the manager is then advised to sort these daily tasks into three groups: those that must be addressed that day, those that should be addressed that day but could be postponed if necessary, and those that can easily be postponed. The manager is then advised to perform the tasks in order of priority.

Exercise Task

With the background information above as context, do the following:

1. Write across the top of a sheet of paper the three priority levels noted above.
2. Write down the left side of the same sheet of paper the various elements and dimensions of the task and internal environment of business.
3. At the intersection of each row and column, think of an appropriate example that a manager might face; That is, think of a higher priority, a moderate priority, and a low-priority situation involving a customer.
4. Form a small group with two or three classmates and share the examples you each developed. Focus on whether or not there is agreement about the prioritization of each example.

BUILDING EFFECTIVE *diagnostic* SKILLS

Exercise Overview

Diagnostic skills are the skills that enable a manager to visualize the most appropriate response to a situation. These skills are especially important as managers try to achieve effective environmental alignment. In some ways the various elements of the environment are like a chess board—taking action with respect to one part of the environment may also affect other parts of the environment. Diagnostic skills can help a manager anticipate these second-level influences.

Exercise Background

Assume that you are the top manager at a relatively young retailing company specializing in children's clothes and accessories. The firm (today) is healthy, has almost 1,000 stores, and is growing rapidly. To fuel new growth, however, you want to implement some new plans. One option you are considering is launching a new chain of stores targeted at older consumers. Another option is to expand your existing stores to include nonclothing products like compact disks, videos, DVDs, books, and magazines also geared to younger consumers. The logic behind this strategy is to provide one-stop shopping for your existing customers.

Exercise Task

With the background information above as context, do the following:

1. On a sheet of paper list the elements that comprise an organization's task environment.
2. Beside each element write down how the first strategy above might affect your relationship with that part of the task environment. For example, how might strategy one affect your relationship with your existing suppliers?
3. Repeat this activity for the second strategy.

BUILDING EFFECTIVE *communication* SKILLS

Exercise Overview

Communication skills refer to the manager's abilities both to convey ideas and information to others effectively and to receive ideas and information effectively from others. Communication skills are very important when a manager is attempting to respond to or influence some element from the organization's external environment. This exercise will help you develop your communication skills as they relate to this situation.

Exercise Background

Assume that you work for a large manufacturing firm. Nine years ago a factory owned by your company was involved in a major environmental disaster involving toxic waste disposal. The managers involved in the disaster, clearly your company's fault, were all fired. New procedures for dealing with waste disposal were also developed, and since that earlier situation, no further problems have occurred.

The state where the factory is located is currently under fire from the Environmental Protection Agency to impose tighter environmental protection regulations on a variety of industries. The state, however, has a very tight budget and cannot afford to impose these regulations out of its existing budget. A plan recently introduced in the state legislature calls for the imposition of a new tax on all businesses found guilty of improper waste disposal, as well as other forms of pollution, any time during the last ten years. This tax will be used to enforce the new regulations.

At the present time it is unclear whether the tax would apply to your firm for a single year, or if it will be imposed indefinitely on any firm that initially qualifies. Your boss has told you—off the record—that the firm can live with a one-time tax. But if the tax will remain in place for your company indefinitely, the company will close the plant. A plant closure would also have a serious negative impact on the state's economy. Your boss has also placed you in charge of media relations regarding this situation.

Exercise Task

With the background information above as context, do the following:

1. Draft a press release stating your company's position on the potential tax.
2. Imagine that you are going to be interviewed by a reporter known to be "friendly" to your company. The reporter has agreed that you can submit potential interview questions in advance. Draft three such questions and your answers to them.
3. Imagine that a reporter known to be "hostile" to your company has requested an interview. List three questions that might be asked and draft your answers to them.

CHAPTER CLOSING CASE

ENRON POWERS UP THE ENERGY WORLD

Enron is putting new power into the energy industry Until fairly recently, U.S. power companies enjoyed highly regulated, stable environments. Houston-based Enron, like other companies operating interstate pipelines, was forced to follow complex government rules for buying and selling natural gas. Although the regulations simplified the company's planning process in many ways, it also prevented Enron from adjusting its pricing, regardless of actual supply and demand.

That inflexibility became a liability when, in the mid-1980s, oil prices dropped lower than gas prices. Many utilities saw a chance to lower their costs by switching from gas to oil for their generating plants, creating a two-pronged problem for the pipelines. First, Enron was locked into multiyear contracts that forced it to buy from gas producers at specified prices. And second, the company could not deviate from federal pricing rules, so it was unable to lower prices to retain its utility customers.

CEO Kenneth Lay quickly realized that the industry was headed for trouble. He tried, without success, to persuade government regulators to change the rules. Eventually, to avoid financial ruin, Enron and many other pipeline companies abandoned their purchasing contracts, which led to years of legal battles. Meanwhile, the regulators finally changed the rules. Now the pipeline companies are free to buy and sell gas supplies in the marketplace.

In deregulation, Enron's managers saw enormous opportunity where competitors saw dangerous, uncharted waters. Up to that point, nobody had thought of buying and selling gas and electricity as if they were commodities such as pork bellies. However, Lay and his team knew that utility companies were unsettled by the unaccustomed up-and-down movement of deregulated gas prices. So they customized their offerings to balance each utility's specific requirements for gas supply and pricing. Whether a utility was interested in steady prices over a certain period or needed uninterrupted gas supplies for peak times, Enron was ready to help—at a profit.

Gas deregulation was just the beginning. Within a few years, the U.S. electric power industry was also deregulated. Once again, Enron's management recognized the potential for new, profitable activities. Building

on its experience in buying and selling natural gas, Enron was able to outmaneuver competitors by forging highly sophisticated deals to buy and sell electric power across a sprawling network of suppliers and customers. This head start allowed the company to start and keep trading power supplies at volumes that are 25 percent higher than its rivals.

As deregulation spread to other countries, Enron began to widen its reach as well. Country by country, it became the largest energy trading company in Europe, which allowed management to monitor issues affecting future energy prices closely, such as regional weather patterns. The company also entered the Indian market by building a giant generating plant in Dabhol, south of Bombay. Enron managers became so skilled at navigating India's legal structure that the contracts they negotiated led the country to change its laws on business arbitration, currency controls, and insurance.

One of Enron's latest ventures is buying and selling excess bandwidth on the fiber-optic networks that carry Internet connections. Telecommunications firms traditionally offered only long-term, fixed-rate contracts for connections to such networks—the kinds of deals that were once all too common in the energy industry. Sensing opportunity, Enron acquired a specialized software company to help develop a system for switching surplus bandwidth with only fifteen minutes of lead time. The company then partnered with Sun Microsystems to create a gigantic distribution network for fiber-optic bandwidth. Now Enron is buying and selling bandwidth, energy, pulp and paper products, coal, and plastics. What industry will Enron energize next?

Case Questions

1. Identify how dimensions of the task environment created new opportunities for Enron.
2. Describe how elements of Enron's general environment affected its ability to exploit new opportunities.
3. Discuss the various ways in which Enron adapted to its environment. What other adaptations would allow Enron to maintain its market leadership in the power industry?

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CHAPTER 4

The Ethical and Social Environment

OPENING INCIDENT

Businesses exist for one fundamental purpose—to earn profits for their owners. But the manner in which they work to fulfill this purpose and the uses to which they put those profits can vary dramatically. Consider, for example, the case of Patagonia, Inc., a small, privately held, outdoor apparel business. Patagonia was founded in 1973 by a group of surfers in Ventura, California, and was led by Yvon Chouinard. Chouinard still runs the business today.

The founders enjoyed spending part of their time hiking and mountain climbing but felt that the equipment available for such activities was often of poor quality and/or was overpriced. Their objective, then, was to become a provider of high-quality, reasonably priced outdoor equipment. But they expressed this in the form of an unusual goal—to do the right thing. Indeed, in Chouinard's words, "Business[people] who focus on profits wind up in the hole. For me, profit is what happens when you do everything else right."

At first, this meant making the most useful, durable, and environmentally friendly products possible. For instance, for years mountain climbers had embedded steel "chocks" into rocks for attaching their ropes and creating hand- and foot-holds. But Patagonia began selling aluminum chocks because they were less damaging to the rocks. Once the firm started making outdoor adult clothing, it quickly added a line of children's clothing as well, not because there was a known market for such products but because they wanted to find a use for the scraps that were cut from sheets of fabric in making the larger pieces. Patagonia also markets a line of shirts made of fibers from recycled plastic bottles and shirts made from hemp, which is easy to grow organically.

As the firm grew, its environmental concerns also became more and more tangible. For example, in 1996 it decided to use only organic cotton (grown without fertilizers or chemical insecticides) in its clothing. This created a problem, however, because most cotton grown and sold in the United States doesn't meet one or the other of the requirements for being organic. Thus, the firm had to start dealing directly with farmers, instructing them about what they wanted to buy and guaranteeing them competitive

"Business[people] who focus on profits wind up in the hole. For me, profit is what happens when you do everything else right."

—Yvon Chouinard, founder and CEO of Patagonia

LEARNING OBJECTIVES

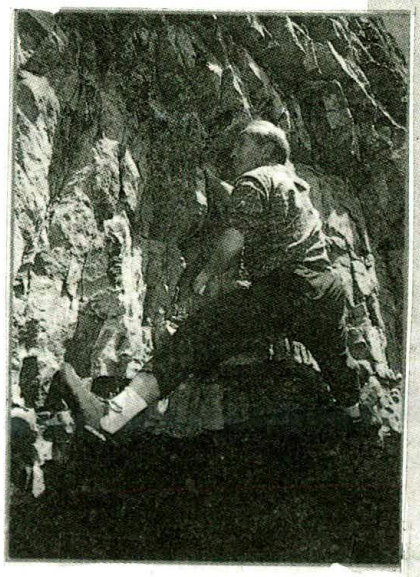
After studying this chapter, you should be able to:

- **Discuss managerial ethics, three areas of special ethical concern for managers, and how organizations manage ethical behavior.**
- **Discuss the concept of social responsibility, specify to whom or what an organization might be considered responsible, and describe four types of organizational approaches to social responsibility.**
- **Explain the relationship between the government and organizations regarding social responsibility.**
- **Describe some of the activities organizations may engage in to manage social responsibility.**

prices to reduce their risk. In a few cases, Patagonia even had to co-sign loans for farmers so that they could buy new equipment and technology to meet the company's stringent requirements.

More recently Chouinard has mandated that henceforth 1 percent of Patagonia's revenues would be given to environmental groups each year. (Because the firm is private, its financial records are not disclosed. However, estimates suggest that the firm generates about $180 million in revenues each year.) And Chouinard himself has been actively involved in efforts aimed at removing dams from rivers to return the rivers to their natural states.

Patagonia always seems to put its social agenda at the forefront of everything it does. For example, in early 2000 the firm set up a major new operation on the Internet to sell its products more efficiently to consumers. One of the more interesting twists, though, is a section called "Rants & Raves." Customers can use this section to post on-line reviews and comments about Patagonia products—both positive and negative. But even a firm as socially active as Patagonia is not always above criticism. For instance, some people criticize the fact that part of its social giving goes to such radical groups as Earth First.[1]



CHAPTER OUTLINE

- **Individual Ethics in Organizations**
  - Managerial Ethics
  - Ethics in an Organizational Context
  - Managing Ethical Behavior
- **Social Responsibility and Organizations**
  - Areas of Social Responsibility
  - Arguments For and Against Social Responsibility
  - Organizational Approaches to Social Responsibility
- **The Government and Social Responsibility**
  - How Government Influences Organizations
  - How Organizations Influence Government
- **Managing Social Responsibility**
  - Formal Organizational Dimensions
  - Informal Organizational Dimensions
  - Evaluating Social Responsibility

Businesses everywhere need to earn profits to remain in existence. But there are disparate views about how a firm can legitimately pursue and then use those profits. Some companies aggressively seek to maximize their profits, to grow at any cost, and focus on nothing but what's best for the company. Others, like Patagonia, take a much different approach to business and actively work for the betterment of society, even when it means less profit for the owners. Most businesses, however, adopt a position somewhere between these extremes. Decisions about which of these approaches to take, in turn, are affected by managerial ethics and social responsibility.

This chapter explores the basic issues of ethics and social responsibility in detail. We look first at individual ethics and their organizational context. Next, we expand our discussion to the more general subject of social responsibility. After we explore the relationships among businesses and the government regarding socially responsible behavior, we examine the activities organizations sometimes undertake to be more socially responsible.

■ Individual Ethics in Organizations

ethics An individual's personal beliefs about whether a behavior, action, or decision is right or wrong

ethical behavior Behavior that conforms to generally accepted social norms

unethical behavior Behavior that does not conform to generally accepted social norms

We define **ethics** as an individual's personal beliefs about whether a behavior, action, or decision is right or wrong.[2] Note that we define ethics in the context of the individual—people have ethics, organizations do not. Likewise, what constitutes ethical behavior varies from one person to another. For example, one person who finds a twenty-dollar bill on the floor believes that it is okay to stick it in his pocket, whereas another feels compelled to turn it in to the lost-and-found department. Further, although **ethical behavior** is in the eye of the beholder, it usually refers to behavior that conforms to generally accepted social norms. **Unethical behavior**, then, is behavior that does not conform to generally accepted social norms.

A society generally adopts formal laws that reflect the prevailing ethical standards—the social norms—of its citizens. For example, because most people consider theft to be unethical, laws have been passed to make such behaviors illegal and to prescribe ways of punishing those who do steal. But while laws attempt to be clear and unambiguous, their application and interpretation still lead to ethical ambiguities. For example, virtually everyone would agree that forcing employees to work excessive hours, especially for no extra compensation, is unethical. Accordingly, laws have been passed to define work and pay standards. But applying that law to organizational settings can still result in ambiguous situations that can be interpreted in different ways.

An individual's ethics are determined by a combination of factors. People start to form ethical standards as children in response to their perceptions of the behavior of their parents and/or other adults and the behaviors they are allowed to choose. As children grow and enter school, they are also influenced by peers with whom they interact every day. Dozens of important individual events also shape people's lives and contribute to their ethical beliefs and behavior as they grow into adulthood. Values and morals also contribute to ethical standards. Peo-

ple who place financial gain and personal advancement at the top of their list of priorities, for example, will adopt personal codes of ethics that promote the pursuit of wealth. Thus, they may be ruthless in efforts to gain these rewards, regardless of the costs to others. In contrast, people who clearly establish their family and/or friends as their top priority will adopt different ethical standards.

Managerial Ethics

Managerial ethics are the standards of behavior that guide individual managers in their work.[3] Although ethics can affect managerial work in any number of ways, three areas of special concern for managers are shown in Figure 4.1.

managerial ethics Standards of behavior that guide individual managers in their work

How an Organization Treats Its Employees One important area of managerial ethics is the treatment of employees by the organization. This area includes things such as hiring and firing, wages and working conditions, and employee privacy and respect. For example, both ethical and legal guidelines suggest that hiring

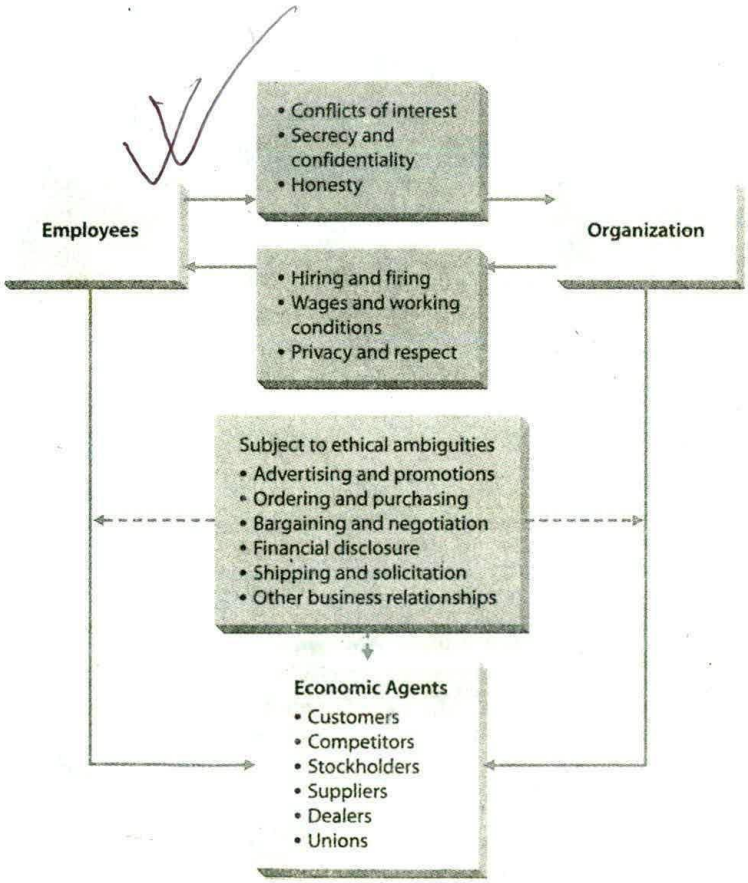
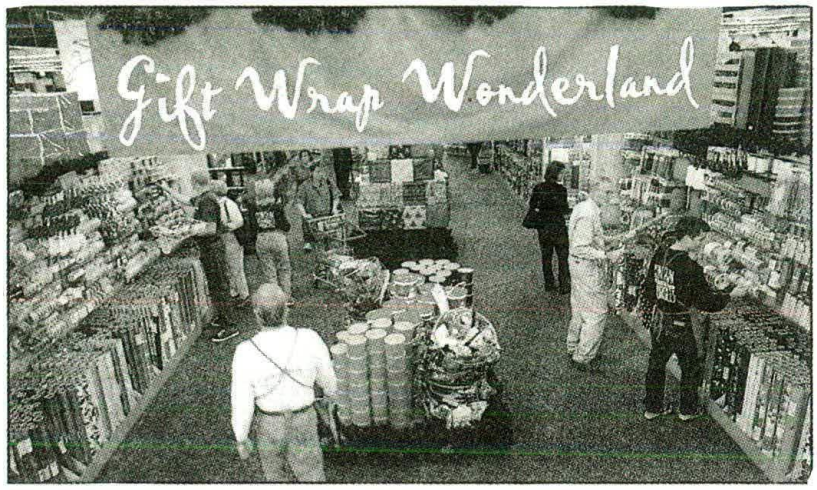


Figure 4.1

Managerial Ethics

The three basic areas of concern for managerial ethics are the relationships of the firm to the employee, the employee to the firm, and the firm to other economic agents. Managers need to approach each set of relationships from an ethical and moral perspective.



The Container Store is consistently ranked as one of the best companies to work for in the United States. One key factor in this recognition is the manner in which management treats the firm's employees. For example, the company allows all employees to have access to all its financial information. The company also provides extensive training for its employees and works to insure that its compensation and benefits packages are the best in the industry. And all employees from top management on down are treated as equals.

and firing decisions should be based solely on an individual's ability to perform the job. A manager who discriminates against African Americans in hiring is exhibiting both unethical and illegal behavior. But consider the case of a manager who does not discriminate in general, but occasionally hires a close friend or relative when other applicants might be just as qualified. While these hiring decisions may not be illegal, they may be objectionable on ethical grounds.

Wages and working conditions, while also tightly regulated, are also areas for potential controversy. For example, the fact that a manager is paying an employee less than he deserves, simply because the manager knows the employee cannot afford to quit or risk losing his job by complaining, might be considered unethical. Finally, most observers also would agree that an organization is obligated to protect the privacy of its employees. A manager's spreading a rumor that an employee has AIDS or is having an affair with a coworker is generally seen as an unethical breach of privacy. Likewise, the manner in which an organization responds to and addresses issues associated with sexual harassment also involves employee privacy and related rights.

How Employees Treat the Organization Numerous ethical issues also stem from how employees treat the organization, especially in regard to conflicts of interest, secrecy and confidentiality, and honesty. A conflict of interest occurs when a decision potentially benefits the individual to the possible detriment of the organization. To guard against such practices, most companies have policies that forbid their buyers from accepting gifts from suppliers. Divulging company secrets is also clearly unethical. Employees who work for businesses in highly competitive industries—electronics, software, and fashion apparel, for example—might be tempted to sell information about company plans to competitors. A third area of concern is honesty in general. Relatively common problems in this area include

using a business telephone to make personal long-distance calls, stealing supplies, and padding expense accounts. While most employees are inherently honest, organizations must nevertheless be vigilant to avoid problems from behaviors such as these.

How Employees and the Organization Treat Other Economic Agents Managerial ethics also come into play in the relationship between the firm and its employees and other economic agents. As listed previously in Figure 4.1, the primary agents of interest include customers, competitors, stockholders, suppliers, dealers, and unions. The behaviors between the organization and these agents that may be subject to ethical ambiguity include advertising and promotions, financial disclosures, ordering and purchasing, shipping and solicitations, bargaining and negotiation, and other business relationships.

For example, businesses in the pharmaceuticals industry have been under growing fire because of the rapid escalation of the prices they are charging for many of their drugs. These firms counter that they need to invest more heavily in research and development programs to develop new drugs, and that higher prices are needed to cover these costs. The key in situations like this, then, is to find the right balance between reasonable pricing and price gouging. And like so many questions involving ethics, there are significant differences of opinion.[4] Another area of concern in recent years involves financial reporting by various e-commerce firms. Because of the complexities inherent in these firms, some of them have been very aggressive in presenting their financial positions in a very positive light. And in at least a few cases, some firms have substantially overstated their earnings projections to entice more investment.[5]

Additional complexities faced by many firms today are the variations in ethical business practices in different countries. In many countries bribes and side payments are a normal and customary part of doing business. However, U.S. laws forbid these practices, even if a firm's rivals from other countries are paying them. For example, a U.S. power-generating company lost a $320 million contract in the Middle East because government officials demanded a $3 million bribe. A Japanese firm paid the bribe and won the contract. Enron Company had a big project in India cancelled because newly elected officials demanded bribes. While these kinds of cases are illegal under U.S. law, other situations are more ambiguous. In China, for example, local journalists expect their cabfare to be paid if they are to cover a business-sponsored news conference. In Indonesia the normal time to get a driver's license for a foreigner is over a year, but it can be "expedited" for an extra $100. And in Romania, building inspectors routinely expect a "tip" for a favorable review.[6] *The World of Management* summarizes a recent incident of international price fixing.

Ethics in an Organizational Context

It is also important to note that while ethics are an individual phenomenon, ethical or unethical actions by particular managers do not occur in a vacuum. Indeed, they most often occur in an organizational context that is conducive to them.

WORLD OF MANAGEMENT

Dealing with International Price Fixing

When managerial ethics collide with profits, customers pay the price. That's what happened in a recent case of global pricing collusion. Switzerland's F. Hoffmann-LaRoche, France's Rhone-Poulenc, and Germany's BASF all cooperated in a sophisticated conspiracy to control international pricing of vitamins and vitamin ingredients for cereals and other foods.

During the course of their inquiry, U.S. Department of Justice investigators learned that the firms got together every year to set prices and track progress. In effect, the three acted more like a single company than a set of rivals, setting specific agendas and budgets for their meetings and activities. Investigators found that top managers initiated and directed the price-fixing arrangement, middle managers implemented the prices, and first-line managers confirmed that the prices were set as agreed.

Hoffmann-LaRoche paid $500 million to settle this price-fixing case, one of the highest fines levied by the Justice Department for antitrust violations. In addition, Hoffmann-LaRoche's former director of worldwide marketing was ordered to pay a $100,000 fine and serve four months in prison. This was not the pharmaceutical company's first brush with antitrust proceedings. Only two years earlier, it had been fined for its part in a price-fixing case involving citric acid.

BASF paid a $225 million fine to settle the vitamin price-fixing case. Rhone-Poulenc was able to avoid prosecution because it cooperated with the Department of Justice's investigation. Even after the antitrust case was settled, the legal maneuvering continued as distributors and food processors who purchased vitamins from the three firms filed suit for restitution. Despite the settlement, experts doubted that consumers would see any drop in vitamin prices. So although the negative publicity and heavy fines hurt the conspirators, customers ultimately paid the price for this global price-fixing scandal.

The criminal conduct of these companies hurt the pocketbook of virtually every American consumer—anyone who took a vitamin, drank a glass of milk, or had a bowl of cereal.
*—Joel Klein, Assistant Attorney General**

Reference: Jayne O'Donnell, "U.S. Fines Drug Companies $725M for Price Fixing," *USA Today*, May 21, 1999, p. 1B (*quote on p. 1B).

Actions of peer managers and top managers, as well as the organization's culture, all contribute to the ethical context of the organization.[7]

The starting point in understanding the ethical context of management is, of course, the individual's own ethical standards. Some people, for example, will risk personal embarrassment or lose their job before they would do something unethical. Other people are much more easily swayed by the unethical behavior they see around them and other situational factors, and they may be willing to commit major crimes to further their own careers or for financial gain. Organizational practices may strongly influence the ethical standards of employees. Some organizations openly permit unethical business practices as long as they are in the best interests of the firm.

If managers become aware of unethical practices and allow them to continue, they have contributed to an organization culture that says such activity is permitted. For example, a few years ago Lars Bildman was fired from his post as CEO of Astra USA, a subsidiary of a large Swedish drug manufacturer, Astra AB. During his



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tenure with the firm, he allegedly sexually harassed dozens of Astra employees, used company funds to remodel his home, and took frequent company-paid private cruises with other company executives and prostitutes. While only Bildman was formally charged with criminal wrongdoing, dozens of senior managers apparently knew of the problems at Astra and either ignored them or began to participate in similar activities themselves. Thus, their collective behaviors served first to create and then to reinforce an environment that appeared to sanction those behaviors.[8]

The organization's environment also contributes to the context for ethical behavior. In a highly competitive or regulated industry, for example, a manager may feel more pressure to achieve high performance. When managers feel pressure to meet goals or lower costs, they may explore a variety of alternatives to help achieve these ends. And in some cases, the alternative they adopt may be unethical or even illegal. The cartoon illustrates one way this can happen—if a manager feels pressure to get more work done, she or he may apply similar pressure on others to work extra hours, stay later in the evenings, and so forth.

Managers should strive to be ethical in all their dealings with their employees. Sometimes the pressures and stresses they experience cause them to apply those same pressures and stresses to employees, often in inappropriate ways. For example, as illustrated here, managers sometimes go too far in their efforts to entice employees to work harder or to spend more time on the job. The result can be disgruntled employees and low morale.

Managing Ethical Behavior

Spurred partially by increased awareness of ethical scandals in business and partially from a sense of enhanced corporate consciousness about the importance of ethical and unethical behaviors, many organizations have reemphasized ethical behavior on the part of employees. This emphasis takes many forms, but any effort to enhance ethical behavior must begin with top management. Top managers, for example, establish the organization's culture and define what will and will not be acceptable behavior. Some companies have also started offering employees training in how to cope with ethical dilemmas. At Boeing, for example, line managers lead training sessions for other employees, and the company also has an ethics committee that reports directly to the board of directors. The training sessions involve discussions of different ethical dilemmas that employees might face and how managers might handle those dilemmas. Chemical Bank and Xerox also have ethics training programs for their managers.

Organizations are also going to greater lengths to formalize their ethical standards. Some, such as General Mills and Johnson & Johnson, have prepared

code of ethics A formal, written statement of the values and ethical standards that guide a firm's actions

guidelines that detail how employees are to treat suppliers, customers, competitors, and other constituents. Others, such as Whirlpool and Hewlett-Packard, have developed formal **codes of ethics**—formal, written statements of the values and ethical standards that guide a firm's actions.

Of course, no code, guideline, or training program can truly make up for the quality of an individual's personal judgment about what is right behavior and what is wrong behavior in a particular situation. Such devices may prescribe what people should do, but they often fail to help people understand and live with the consequences of their choices. Making ethical choices may lead to very unpleasant outcomes—firing, rejection by colleagues, and the forfeiture of monetary gain, to name a few. Thus managers must be prepared to confront their own consciences and weigh the options available when making difficult ethical decisions. *Today's Management Issues* highlights an increasingly important issue that relates to this point, privacy and the Internet.

Unfortunately, what distinguishes ethical from unethical behavior is often subject to differences of opinion. So how does one go about deciding whether or not a

TODAY'S MANAGEMENT ISSUES

PRIVACY ON THE INTERNET

Who's watching when people surf the Internet?

On-line privacy has become a hot issue as companies sort out the ethical and management issues. DoubleClick, an on-line advertising network, is one of the firms at the eye of the privacy storm. The company has collected data on the habits of millions of web surfers, recording which sites they visit and which ads they click on. DoubleClick insists the profiles are anonymous and are used to match surfers better with appropriate ads. After the company announced a plan to add names and addresses to its database, however, it was forced to back down because of public concerns over invasion of on-line privacy.

DoubleClick isn't the only firm gathering personal data about people's Internet activities. People who register at Yahoo! are asked to list date of birth, among other details. Amazon.com, eBay, and other sites also ask for personal information. As Internet use increases, however, surveys show that people are troubled by the amount of information being collected and who sees it.

One way management can address these concerns is to post a privacy policy on the web site. The policy should explain exactly what data the company collects and who sees the data. It should also allow people a choice about having their information shared with others and indicate how people can opt out of data collection. Walt Disney, IBM, and other companies support this position by refusing to advertise on web sites that have no posted privacy policies.

In addition, companies can offer web surfers the opportunity to review and correct information that has been collected, especially medical and financial data. In the off-line world, consumers are legally allowed to inspect credit and medical records. In the on-line world, this kind of access can be costly and cumbersome because data are often spread across several computer systems. Despite the technical difficulties, government agencies are already working on Internet privacy guidelines, which means companies will need internal guidelines, training, and leadership to ensure compliance.

I am troubled, very troubled, by leaders who have failed to recognize our responsibility in the transformation of the new economy.

—Louis Gerstner, chairman, IBM*

Reference: Heather Green, Mike France, Marcia Stepanek, and Amy Borrus, "Online Privacy: It's Time for Rules in Wonderland," *Business Week*, March 20, 2000, pp. 83–96 (*quote on p. 85).

particular action or decision is ethical? Traditionally, experts have suggested a three-step model for applying ethical judgments to situations that may arise during the course of business activities. These steps are (1) gather the relevant factual information, (2) determine the most appropriate moral values, and (3) make an ethical judgment based on the rightness or wrongness of the proposed activity or policy.

But this analysis is seldom as simple as these few steps might imply. For instance, what if the facts are not clear-cut? What if there are no agreed-upon moral values? Nevertheless, a judgment and a decision must be made. Experts point out that, otherwise, trust is impossible; and trust, they add, is indispensable to any business transaction. Thus, to assess more completely the ethics of a particular behavior, a more complex perspective is necessary. To illustrate this perspective, consider a common dilemma faced by managers involving their expense accounts.[9]

Companies routinely provide their managers with an account to cover their work-related expenses when they are traveling on company business and/or entertaining clients for business purposes. Common examples of such expenses include hotel bills, meals, rental cars or taxis, and so forth. But employees, of course, are expected to claim only expenses that are accurate and work-related. For example, if a manager takes a client out to dinner while in another city on business and spends $100 for dinner, submitting a receipt for that dinner to be reimbursed for $100 is clearly accurate and appropriate. Suppose, however, that the manager then has a $100 dinner the next night in that same city with a good friend for purely social purposes. Submitting that receipt for full reimbursement would be unethical. A few managers, however, might rationalize that it would be okay to submit a receipt for dinner with a friend. They might argue, for example, that they are underpaid and this is just a way for them to increase their income.

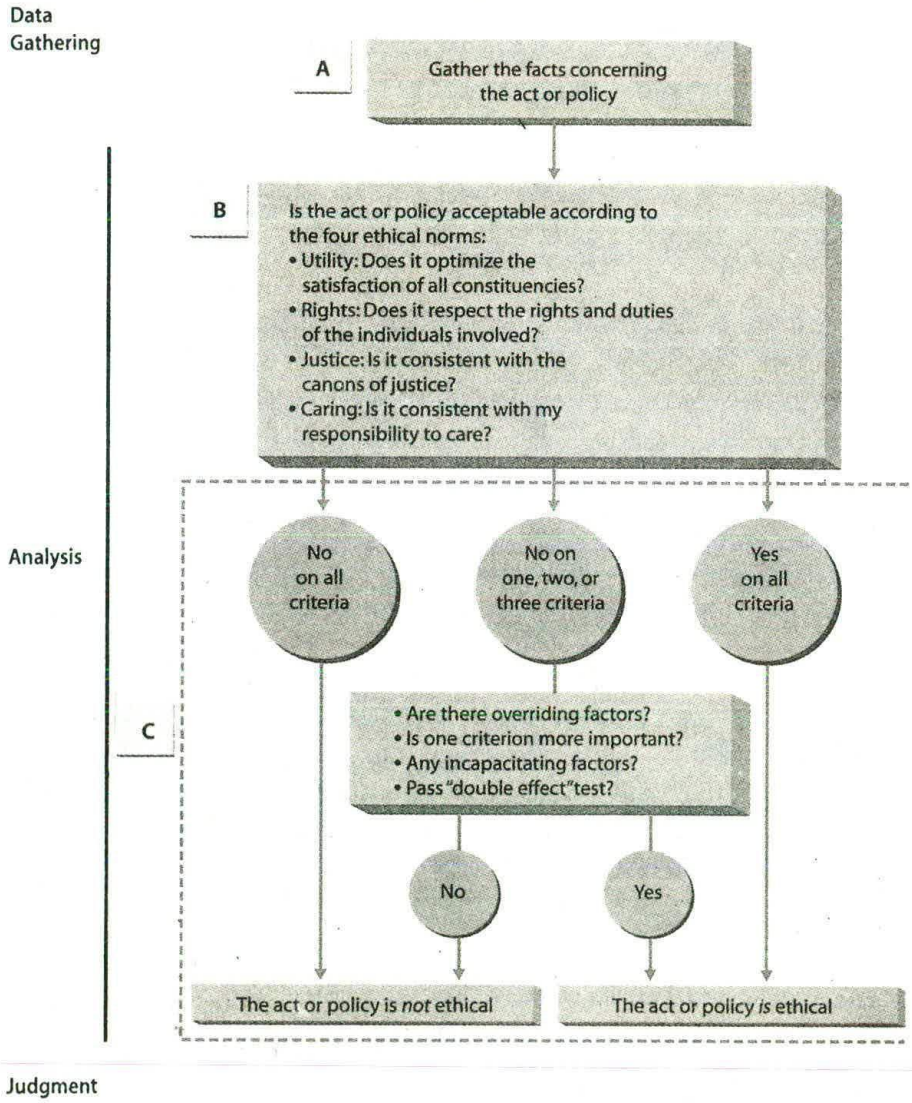
Other principles that come into play in a case like this include various ethical norms. Four such norms involve utility, rights, justice, and caring. By utility, we mean deciding whether a particular act optimizes what is best for its constituencies. By rights, we mean deciding whether a particular act respects the rights of the individuals involved. By justice, we mean deciding whether it is consistent with what we would see as being fair. And by caring, we mean deciding whether it is consistent with people's responsibilities to each other. Figure 4.2 illustrates a model that incorporates these ethical norms.

Now, reconsider the case of the inflated expense account. While the utility norm would acknowledge that the manager benefits from padding an expense account, others, such as coworkers and owners, do not. Similarly, most experts would agree that it does not respect the rights of others. Moreover, it is clearly unfair and compromises responsibilities to others. Thus, this particular act appears to be clearly unethical. However, the figure also provides mechanisms for considering unique circumstances that might fit certain limited situations. For example, suppose the manager loses the receipt for the legitimate dinner but has the receipt for the same amount for the social dinner. Some people would now argue that it is okay to submit the social dinner receipt because the manager is doing so only to get what he or she is entitled to. Others, however, would still argue that submitting the social dinner receipt is wrong under any circumstances. The point, simply, is that changes in the situation can make the issue more or less clear-cut.

Figure 4.2

A Guide for Ethical Decision Making

Managers should attempt to apply ethical judgment to the decisions they make. For example, this useful framework for guiding ethical decision making suggests that managers apply a set of four criteria based on utility, rights, justice, and caring when assessing decision options options. The resulting analysis allows a manager to make a clear assessment of whether or not a decision or policy is ethical.



Source: Adapted from Gerald F. Cavanagh, Dennis J. Moberg, and Manuel Velasquez, "Making Business Ethics Practical," *Business Ethics Quarterly* (July 1995); and Manuel Velasquez, Gerald F. Cavanagh, and Dennis Moberg, "Organizational Statesmenship and Dirty Politics," *Organizational Dynamics* (Autumn, 1983). p. 84. Copyright 1983, with permission from Elesevier Science. Reprinted from Gerald F. Cavanagh, *American Business Values*, 4th Edition (Upper Saddle River, N.J.: Prentice-Hall, 1998). Reprinted by permission of Prentice-Hall, Inc.

MANAGEMENT IMPLICATIONS Managers need to understand the basic meanings of ethical and unethical behaviors. They also need to understand fully the various ethical links among the organization, its employees, and other economic agents and to ensure, to the extent possible, that these links are maintained according to the proper ethical standards. Managers should also acknowledge the organizational context of individual ethics and be prepared to interpret ethical problems from an organizational perspective. And finally, managers should take various measures to maintain ethical behavior by those in their organizations, while also recognizing that any individual's personal actions may offset the best organizational strategies for promoting ethical conduct. The key, then, is to make a thorough attempt to apply reasonable judgment to ethical situations.

■ Social Responsibility and Organizations

As we have seen, ethics relate to individuals and their decisions and behaviors. Organizations themselves do not have ethics, but they do relate to their environment in ways that often involve ethical dilemmas and decisions. These situations are generally referred to within the context of the organization's social responsibility. Specifically, **social responsibility** is the set of obligations an organization has to protect and enhance the society in which it functions.

social responsibility The set of obligations an organization has to protect and enhance the society in which it functions

Areas of Social Responsibility

Organizations may exercise social responsibility toward their stakeholders, toward the natural environment, and toward general social welfare. Some organizations acknowledge their responsibilities in all three areas and strive diligently to meet each of them, while others emphasize only one or two areas of social responsibility. And a few acknowledge no social responsibility at all.

Organizational Stakeholders In Chapter 3 we described the task environment as comprising those elements in an organization's external environment that directly affect the organization in one or more ways. Another way to describe these same elements is from the perspective of **organizational stakeholders**, or those people and organizations who are directly affected by the behaviors of an organization and that have a stake in its performance.[10] Major stakeholders are depicted in Figure 4.3.

Most companies that strive to be responsible to their stakeholders concentrate first and foremost on

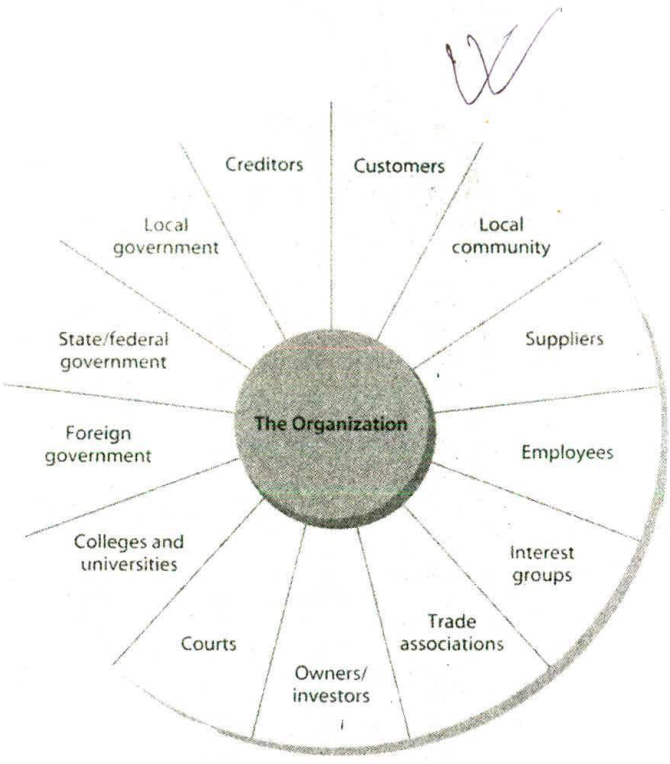


Businesses face an array of stakeholders when addressing issues of social responsibility. For example, consider the problems faced by McDonald's. The firm contracted with a Chinese manufacturer to make toys for its Happy Meals and various promotional ventures. The Chinese firm, in turn, allegedly used child labor in its factory. As a result, these protestors are calling on consumers in Hong Kong to boycott McDonald's. They also demanded that the firm provide additional compensation to the families of the underage children.

Figure 4.3

Organizational Stakeholders

All organizations have a variety of stakeholders that are directly affected by the organization and that have a stake in its performance. These are people and organizations to whom an organization should be responsible.



organizational stakeholders
People and organizations who are directly affected by the behaviors of an organization and that have a stake in its performance

three main groups: customers, employees, and investors. They then select other stakeholders that are particularly relevant or important to the organization and then attempt to address their needs and expectations as well.

Organizations that are responsible to their customers strive to treat them fairly and honestly. They also seek to charge fair prices, to honor warranties, to meet delivery commitments, and to stand behind the quality of the products they sell. Companies that have established excellent reputations in this area include L.L.Bean, Land's End, Dell Computer, and Johnson & Johnson.

Organizations that are socially responsible in their dealings with employees treat their workers fairly, make them part of the team, and respect their dignity and basic human needs. Organizations such as 3M Company, Hoescht Celanese, SAS Institute, and Southwest Airlines have all established strong reputations in this area. In addition, they also go to great lengths to find, hire, train, and promote qualified minorities. *Working with Diversity* also explains how some organizations today are helping their employees prepare for and compete in the Olympic Games.

To maintain a socially responsible stance toward investors, managers should follow proper accounting procedures, provide appropriate information to shareholders about the financial performance of the firm, and manage the organization to protect shareholder rights and investments. Moreover, they should be accurate and candid in their assessment of future growth and profitability and avoid even

WORKING WITH DIVERSITY

SUPPORTING OLYMPIC ATHLETES

Summer and winter Olympic games take place every four years, which leaves plenty of time between for athletes to climb the career ladder while funding their dreams. Although training for the Olympics takes time and costs money, some U.S. athletes have a new source of support: their employers. Companies such as U.S. West, UPS, and Home Depot, which have paid millions of dollars for Olympic sponsorship, are also demonstrating their social responsibility by supporting employees who are training for slots on U.S. Olympic teams.

Telecommunications giant U.S. West pays training costs—as much as $100,000—for eight employees who are Olympic-level athletes, including Anthony Washington, a market analyst who competes in the discus throw. U.S. West, like other sponsors, proudly lets the world know about its employees' achievements. After Washington won the World Track and Field Championships, U.S. West offered public congratulations in a special advertisement.

UPS, the global delivery firm, is another strong supporter of Olympic athletes on staff. Tongula Givens, who competes in the triple jump event, is one of several UPS employees whose training and travel expenses are paid by the company. UPS also adjusts work schedules to accommodate its employees' training needs, allowing time off with full pay for intensive training just before Olympic events. The UPS athletes have become in-house celebrities, giving motivational talks to employees and appearing in UPS ads and on shipping materials.

Home Depot has become a magnet for Olympic hopefuls. Over the past five years, nearly 100 top athletes have worked for the home improvement retailer. Each works a flexible part-time schedule at full-time pay while in training. Like UPS, Home Depot touts its sponsorship of Olympic athletes through advertising and other promotions. After the Olympics, employees who have won medals appear at corporate meetings and new store openings. Then it's back to work and back to training until the next Olympic games.

It's good for marketing purposes. But it's also a good thing to do for athletes who might otherwise give up competing.

*—Anthony Washington, market analyst and discus thrower, U.S. West**

Reference: Bruce Horovitz, "Employers Back Olympic Hopefuls," *USA Today*, February 7, 2000, p. 1B (*quote on p. 1B).

the appearance of improprieties involving such sensitive areas as insider trading, stock price manipulation, and the withholding of financial data.[11]

The Natural Environment A second critical area of social responsibility relates to the natural environment.[12] Not long ago, many organizations indiscriminately dumped sewage, waste products from production, and trash into streams and rivers, into the air and on vacant land. When Shell Oil first explored the Amazon River Basin for potential drilling sites in the late 1980s, its crews ripped down trees and left a trail of garbage in their wake. Now, however, many laws regulate the disposal of waste materials. In many instances, companies themselves have also become more socially responsible in their release of pollutants and general treatment of the environment. For example, when Shell launched its most recent exploration expedition into another area of the Amazon Basin, the group included a biologist to oversee environmental protection and an anthropologist to help the team interact more effectively with native tribes.[13]

Still, much remains to be done. Companies need to develop economically feasible ways to avoid contributing to acid rain and global warming; to avoid depleting the ozone layer; and to develop alternative methods of handling sewage, hazardous wastes, and ordinary garbage. Procter & Gamble, for example, is an industry leader in using recycled materials for containers. Hyatt Corporation established a new company to help recycle waste products from its hotels. Monsanto is launching an entirely new product line aimed at improving the environment with genetically engineered crops.[14] Ford has also announced its intention to create a new brand to cover the development and marketing of low-pollution and electric powered vehicles.[15] The Internet is also seen as potentially playing an important role in resource conservation because many e-commerce businesses and transactions reduce both energy costs and pollution.[16]

Companies also need to develop safety policies that cut down on accidents with potentially disastrous environmental results. When one of Ashland Oil's storage tanks ruptured several years ago, spilling more than five hundred thousand gallons of diesel fuel into Pennsylvania's Monongahela River, the company moved quickly to clean up the spill but was still indicted for violating U.S. environmental laws.[17] After the Exxon oil tanker *Valdez* spilled millions of gallons of oil off the coast of Alaska, it adopted new and more stringent procedures to keep another disaster from happening.

General Social Welfare Some people believe that in addition to treating constituents and the environment responsibly, business organizations should also promote the general welfare of society. Examples include making contributions to charities, philanthropic organizations, and not-for-profit foundations and associations; supporting museums, symphonies, and public radio and television; and taking a role in improving public health and education. Some people also believe that organizations should act even more broadly to correct the political inequities that exist in the world. For example, these observers would argue that businesses should not conduct operations in countries with a record of human rights violations. Thus, they stand in opposition to companies doing business in China and Vietnam.

Arguments For and Against Social Responsibility

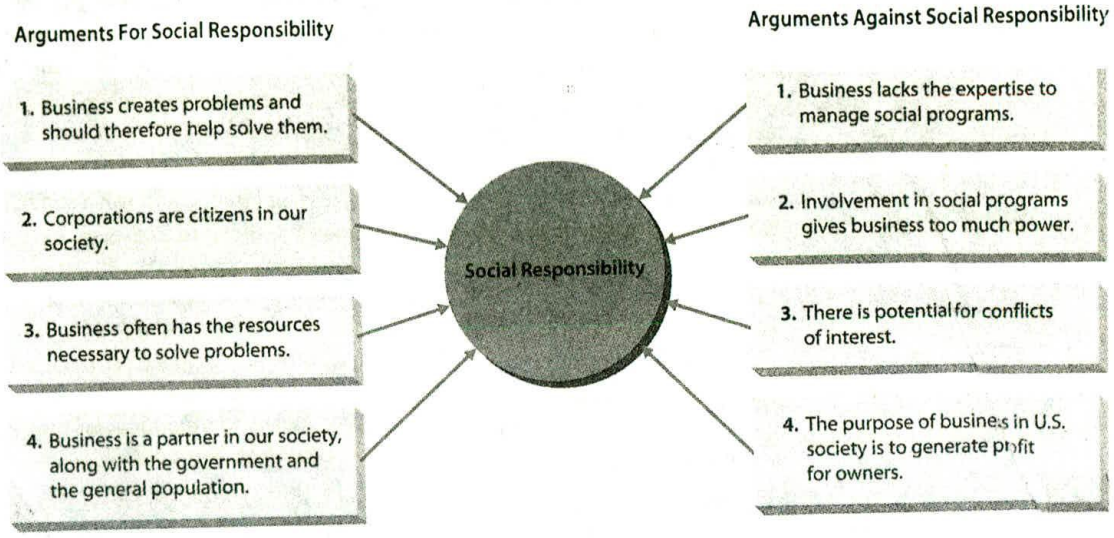
On the surface, there seems to be little disagreement about the need for organizations to be socially responsible. In truth, though, those who oppose wide interpretations of social responsibility use several convincing arguments.[18] Some of the more salient arguments on both sides of this contemporary debate are summarized in Figure 4.4 and are further explained in the following sections.

Arguments for Social Responsibility People who argue in favor of social responsibility claim that because organizations create many of the problems that need to be addressed, such as air and water pollution and resource depletion, they should play a major role in solving them. They also argue that because corporations are legally defined entities with most of the same privileges as private citizens, businesses should not try to avoid their obligations as citizens. Advocates of social responsibility point out that while governmental organizations have

Figure 4.4

Arguments For and Against Social Responsibility

While many people want everyone to see social responsibility as a desirable aim, there are in fact several strong arguments that can be used both for and against social responsibility. Hence, organizations and their managers should carefully assess their own values, beliefs, and priorities when deciding which stance and approach to take regarding social responsibility.



stretched their budgets to the limit, many large businesses often have surplus revenues that could potentially be used to help solve social problems. For example, IBM routinely donates surplus computers to schools and many restaurants give leftover food to homeless shelters.

Although each of the arguments just summarized is a distinct justification for socially responsible behaviors on the part of organizations, another more general reason for social responsibility is profit itself. For example, organizations that make clear and visible contributions to society can achieve enhanced reputations and garner greater market share for their products. Although claims of socially responsible activities can haunt a company if they are exaggerated or untrue, they can also work to the benefit of both the organization and society if the advertised benefits are true and accurate.

Arguments Against Social Responsibility Some people, however, including the famous economist Milton Friedman, argue that widening the interpretation of social responsibility will undermine the U.S. economy by detracting from the basic mission of business: to earn profits for owners. For example, money that Chevron or General Electric contributes to social causes or charities is money that could otherwise be distributed to owners as a dividend. Ben & Jerry's Homemade Inc. has a very ambitious and widely touted social agenda. But some shareholders recently criticized the firm when it refused to accept a lucrative exporting deal to Japan simply because the Japanese distributor did not have a similar social agenda.[19]

Another objection to deepening the social responsibility of businesses points out that corporations already wield enormous power and that their activity in social programs gives them even more power. Another argument focuses on the potential for conflict of interest. Suppose, for example, that one manager is in charge of deciding which local social program or charity will receive a large grant from her business. The local civic opera company (a not-for-profit organization that relies on contributions for its existence) might offer her front-row tickets for the upcoming season in exchange for her support. If opera is her favorite form of music, she might be tempted to direct the money toward the local company, when it might actually be needed more in other areas.[20]

Finally, critics argue that organizations lack the expertise to understand how to assess and make decisions about worthy social programs. How can a company truly know, they ask, which cause or program is most deserving of its support, or how money might best be spent? For example, Exxon recently announced a commitment to spend $5 million to help save the tiger, an endangered species that serves as the firm's corporate symbol. Exxon committed most of the money to support breeding programs in zoos and to help educate people about the tiger. But conservationists criticized the firm and its plan, arguing instead that the money might have been better spent on eliminating poaching, the illegal trade of tiger fur, and the destruction of the tiger's natural habitat.[21]

Organizational Approaches to Social Responsibility

As we have seen, some people advocate a larger social role for organizations, and others argue that the role is already too large. Not surprisingly, organizations themselves adopt a wide range of positions on social responsibility. As Figure 4.5 illustrates, the four stances that an organization can take concerning its obligations to society fall along a continuum ranging from the lowest to the highest degree of socially responsible practices.

obstructionist stance An approach to social responsibility in which firms do as little as possible to solve social or environmental problems

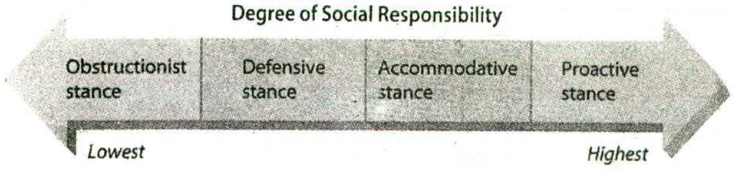
Obstructionist Stance The few organizations that take what might be called an **obstructionist stance** to social responsibility usually do as little as possible to solve social or environmental problems. When they cross the ethical or legal line that separates acceptable from unacceptable practices, their typical response is to deny or avoid accepting responsibility for their actions. For example, when the various problems at Astra USA, noted earlier in the chapter, first began to surface, top officials at both that firm and its Swedish parent company all denied any wrongdoing.

Another more recent case of a firm taking this approach involves IBP, a major Iowa-based meat-processing firm with a truly checkered history. In the

Figure 4.5

Approaches to Social Responsibility

Organizations can adopt a variety of approaches to social responsibility. For example, a firm that never considers the consequences of its decisions and tries to hide its transgressions is taking an obstructionist stance. At the other extreme, a firm that actively seeks to identify areas where it can help society is pursuing a proactive stance toward social responsibility.



early 1970s one of the firm's founders was found guilty of paying a mob-related meat broker $1 million to ensure that unions wouldn't interfere with the firm's New York City distribution plans. In the late 1970s the company was investigated for anticompetitive practices, although this inquiry was subsequently dropped. In the 1980s, IBP was fined $2.6 million and penalized by OSHA for not reporting workers' hand injuries caused by its meat-cutting equipment. The firm also has a long history of abysmal labor relations with its employees.

In January 2000 the U.S. Justice Department, acting on behalf of the Environmental Protection Agency, filed a lawsuit accusing IBP of violating numerous federal air, water, and hazardous waste laws at the company's flagship plant and former headquarters in Dakota City, Nebraska. Among the charges in this case are that the firm emitted up to 1,800 pounds of hydrogen sulfide per day from the Dakota City plant without informing federal regulators (disclosure is required if total emissions exceed 100 pounds per day) and that IBP violated the federal Clean Water Act by dumping excessive ammonia into the Missouri River. Moreover, the suit charges IBP with either failing to file or else filing incorrectly federal toxic-air reports at several of its plants in Iowa, Nebraska, and Kansas. In addition, various state agencies where IBP has operations are investigating numerous allegations against the company regarding pollution. Idaho's State Division of Environmental Quality has charged the firm with exceeding its state wastewater guidelines by as much as 1,200 percent. Illinois's state attorney general is seeking fines against IBP for violating the state's odor law. And officials in Nebraska are closely watching the federal investigation to see if there have been violations that fall under state regulation.[22]



Organizations can take a number of different approaches to questions of social responsibility. Consider, for example, the situation when charges emerged that Firestone tires mounted on Ford vehicles experienced systematic tread separation such that passengers were endangered. Both firms indicated that they wanted to do the right thing, but each was also cautious about accepting too much of the blame. As a result of what they saw as an overly conservative response, Venezuelan officials have filed lawsuits against both firms. In the United States, in contrast, Ford in particular has generally been praised for its quick and thorough response.

Defensive Stance One step removed from the obstructionist stance is the **defensive stance**, whereby the organization does everything that is required of it legally but nothing more. This approach is most consistent with the arguments used against social responsibility just described. Managers in organizations that take a defensive stance insist that their job is to generate profits. For example, such a firm would install pollution-control equipment dictated by law but would not install higher-quality equipment even though it might limit pollution further. Tobacco companies such as Philip Morris take this position in their marketing efforts. In the United States, they are legally required to include warnings to smokers on their products and to limit their advertising to prescribed media. Domestically they follow these rules to the letter of the law but use broader marketing methods in countries that have no such rules. In many African countries, for

defensive stance A social responsibility stance in which an organization does everything that is required of it legally but nothing more

example, cigarettes are heavily promoted, contain higher levels of tar and nicotine than those sold in the United States, and carry few or no health warning labels.[23] Firms that take this position are also unlikely to cover up wrongdoing and will generally admit their mistakes and take appropriate corrective actions.

accommodative stance A social responsibility stance in which an organization meets its legal and ethical obligations and also goes beyond these requirements in selected cases

Accommodative Stance A firm that adopts an **accommodative stance** meets its legal and ethical obligations and also goes beyond these requirements in selected cases. Such firms voluntarily agree to participate in social programs, but solicitors have to convince the organization that the programs are worthy of their support. Both Exxon and IBM, for example, will match contributions made by their employees to selected charitable causes. And many organizations will respond to requests for donations to Little League, Girl Scouts, youth soccer programs, and so forth. The point, though, is that someone has to knock on the door and ask—the organizations do not proactively seek such avenues for contributing.

proactive stance A social responsibility stance in which an organization views itself as a citizen in a society and proactively seeks opportunities to contribute to that society

Proactive Stance The highest degree of social responsibility that a firm can exhibit is the **proactive stance**. Firms that adopt this approach take to heart the arguments in favor of social responsibility. They view themselves as citizens in a society and proactively seek opportunities to contribute to that society. An excellent example of a proactive stance is the Ronald McDonald House program undertaken by McDonald's Corp. These houses, located close to major medical centers, can be used by families for minimal cost while their sick children are receiving medical treatment nearby. Sears offers fellowships that support promising young performers while they develop their talents. Target has stopped selling guns in its stores, while some national toy retailers such as KayBee and Toys "R" Us have voluntarily stopped selling realistic toy guns. These and related activities and programs exceed the accommodative stance—they indicate a sincere and potent commitment to improving the general social welfare in this country and thus represent a proactive stance to social responsibility.

Remember that these categories are not discrete but merely define stages along a continuum of approach. Organizations do not always fit neatly into one category. The Ronald McDonald House program has been widely applauded, for example, but McDonald's also came under fire a few years ago for allegedly misleading consumers about the nutritional value of its food products. And even though Astra and IBF took an obstructionist stance in the cases we cited, many individual employees and managers at both firms have no doubt made substantial contributions to society in several different ways.

MANAGEMENT IMPLICATIONS Managers need to be aware of their key and relevant stakeholders and to ensure that their organization's interactions with those stakeholders, as well as their interactions with the natural environment and society in general, are handled with the appropriate level of social responsibility. Managers should also carefully weigh the various arguments for and against social responsibility and use these arguments in developing a coherent and consistent stance that their organization can take to social responsibility.

■ The Government and Social Responsibility

An especially important element of social responsibility is the relationship between business and government. For example, in planned economies the government heavily regulates business activities, ostensibly to ensure that business supports some overarching set of social ideals. And even in market economies there is still considerable government control of business, much of it again directed at making sure that social interests are not damaged by business interests. On the other side of the coin, however, business also attempts to influence the government. Such influence attempts are usually undertaken in an effort to offset or reverse government restrictions. As Figure 4.6 shows, organizations and the government use several methods in their attempts to influence each other.

How Government Influences Organizations

The government attempts to shape social responsibility practices through both direct and indirect channels. Direct influence is most frequently manifested through regulation, whereas indirect influence can take a number of forms, most notably taxation policies.

Direct Regulation The government most often directly influences organizations through **regulation**, or the establishment of laws and rules that dictate what organizations can and cannot do. As noted earlier in the chapter, this regulation usually evolves from societal beliefs about what businesses should or should not be allowed to do. To implement legislation, the government generally creates special agencies to monitor and control certain aspects of business activity. For example, the Environmental Protection Agency handles environmental issues; the

regulation Government's attempts to influence business by establishing laws and rules that dictate what businesses can and cannot do in prescribed areas

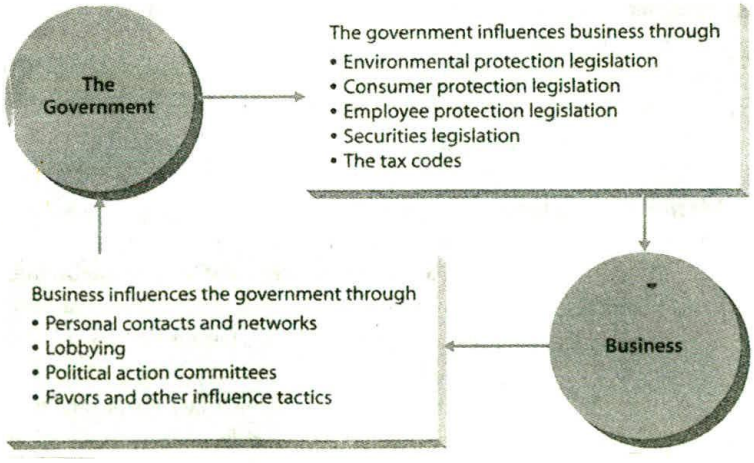


Figure 4.6

How Business and the Government Influence Each Other

Business and the government influence each other in a variety of ways. Government influence can be direct or indirect. Business influence relies on personal contacts, lobbying, political action committees (PACs), and favors. Federal Express, for example, has a very active PAC.

Federal Trade Commission and the Food and Drug Administration focus on consumer-related concerns; the Equal Employee Opportunity Commission, the National Labor Relations Board, and the Department of Labor help protect employees; and the Securities and Exchange Commission handles investor-related issues. These agencies have the power to levy fines or bring charges against organizations that violate regulations.

Indirect Regulation Other forms of regulation are indirect. For example, the government can indirectly influence the social responsibility of organizations through its tax codes. In effect, the government can influence how organizations spend their social responsibility dollars by providing greater or lesser tax incentives. For instance, suppose that the government wanted organizations to spend more on training the hard-core unemployed. Congress could then pass laws that provide tax incentives to companies that opened new training facilities. As a result, more businesses would probably do so. Of course, some critics argue that regulation is already excessive. They maintain that a free market system would eventually accomplish the same goals as regulation with lower costs to both organizations and the government.

How Organizations Influence Government

As we mentioned in Chapter 3, organizations can influence their environment in many different ways. In particular, businesses have four main methods of addressing governmental pressures for more social responsibility.

Personal Contacts Because many corporate executives and political leaders travel in the same social circles, personal contacts and networks offer one method of influence. A business executive, for example, may be able to contact a politician directly and present his or her case regarding a piece of legislation being considered.

lobbying The use of persons or groups to represent an organization or group of organizations formally before political bodies to influence legislation

Lobbying **Lobbying**, or the use of persons or groups to represent an organization or group of organizations formally before political bodies, is also an effective way to influence the government. The National Rifle Association (NRA), for example, has a staff of lobbyists in Washington with a large annual budget. These lobbyists work to represent the NRA's position on gun control and potentially to influence members of Congress when they vote on legislation that affects the firearms industry and the rights of gun owners.

political action committee (PAC) An organization created to solicit and distribute money to political candidates

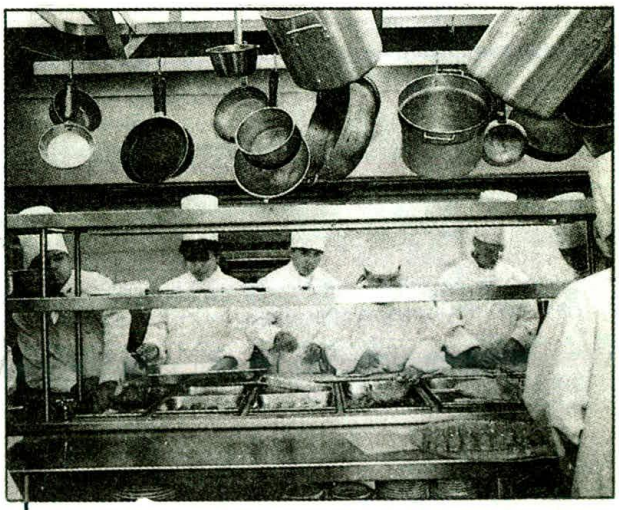
Political Action Committees Companies themselves cannot legally make direct donations to political campaigns, so they influence the government through political action committees. **Political action committees (PACs)** are organizations created to solicit and distribute money to political candidates. Employees of a firm may be encouraged to make donations to particular PACs because managers know that it will support candidates with political views similar to their own. PACs, in turn, make the contributions themselves, usually to a broad slate of state and national candidates. For example, Federal Express's PAC is called Fepac. Fepac makes regular contributions to the campaign funds of political candidates who are most likely to work in the firm's best interests.

Favors Finally, organizations sometimes rely on favors and other influence tactics to gain support. Although these favors may be legal, they are still subject to criticism. A few years back, for example, two influential members of a House committee attending a fund-raising function in Miami were needed in Washington to finish work on a piece of legislation that Federal Express wanted passed. The law being drafted would allow the company and its competitors to give their employees standby seats on airlines as a tax-free benefit. As a favor, Federal Express provided one of its corporate jets to fly the committee members back to Washington. The company was eventually reimbursed for its expenses, so its assistance was not illegal, but some people argue that such actions are dangerous because of how they might be perceived. Similarly, in 1997 there were congressional hearings into allegations that certain foreign interests had attempted to influence political elections in the United States through illegal campaign contributions.[24]

MANAGEMENT IMPLICATIONS Managers should understand fully the various ways in which business and the government influence one another. Further, while recognizing that under certain conditions it may be both legal and appropriate to endeavor to influence the government, managers should also be careful to avoid crossing legal or ethical boundaries.

■ *managing Social Responsibility*

The demands for social responsibility placed on contemporary organizations by an increasingly sophisticated and educated public are probably stronger than ever. As we have seen, there are pitfalls for managers who fail to adhere to high ethical standards and for companies that try to circumvent their legal obligations. Organizations therefore need to fashion an approach to social responsibility the same way that they develop any other business strategy; that is, they should view social responsibility as a major challenge that requires careful planning, decision making, consideration, and evaluation. They may accomplish their approach through both formal and informal dimensions of managing social responsibility.



The effective management of social responsibility requires care and thought. For example, Hyatt Corporation is recognized as an excellent employer for minorities. The firm donated a state-of-the-art kitchen to predominantly Hispanic Robert Clemente High School in Chicago. These students are exploring their passion for cooking and may one day be head chefs at a leading hotel or restaurant.

Formal Organizational Dimensions

Some dimensions of managing social responsibility are formal and planned activities on the part of the organization. Formal organizational dimensions that can help manage social responsibility are legal compliance, ethical compliance, and philanthropic giving.

legal compliance The extent to which an organization complies with local, state, federal, and international laws

Legal Compliance **Legal compliance** is the extent to which the organization complies with local, state, federal, and international laws. The task of managing legal compliance is generally assigned to the appropriate functional managers. For example, the organization's top human resource executive is responsible for ensuring compliance with regulations concerning hiring, pay, and workplace safety and health. Likewise, the top finance executive generally oversees compliance with securities and banking regulations. The organization's legal department is also likely to contribute to this effort by providing general oversight and answering queries from managers about the appropriate interpretation of laws and regulations.

ethical compliance The extent to which an organization and its members follow basic ethical (and legal) standards of behavior

Ethical Compliance **Ethical compliance** is the extent to which an organization and its members follow basic ethical (and legal) standards of behavior. We noted earlier that organizations have increased their efforts in this area—providing training in ethics and developing guidelines and codes of conduct, for example. These activities serve as vehicles for enhancing ethical compliance. Many organizations also establish formal ethics committees, which may be asked to review proposals for new projects, help evaluate new hiring strategies, or assess a new environmental protection plan. They might also serve as a peer review panel to evaluate alleged ethical misconduct by an employee.[25]

philanthropic giving The awarding of funds or gifts to charities or other social programs

Philanthropic Giving Finally, **philanthropic giving** is the awarding of funds or gifts to charities or other social programs. Dayton-Hudson Corp. routinely gives 5 percent of its taxable income to charity and social programs. Giving across national boundaries is also becoming more common. For example, Alcoa gave $112,000 to a small town in Brazil to build a sewage treatment plant. And Japanese firms like Sony and Mitsubishi make contributions to a number of social programs in the United States. Unfortunately, in this age of cutbacks, many corporations have also had to limit their charitable gifts over the past several years as they continue to trim their own budgets. And many firms that continue to make contributions are increasingly targeting them to programs or areas where the firm will get something in return. For example, firms today are more likely to give money to job training programs than to the arts, which wasn't the case just a few years ago. The logic is that they get more direct payoff from the former type of contribution—in this instance, a better trained workforce from which to hire new employees.[26]

Informal Organizational Dimensions

In addition to these formal dimensions for managing social responsibility, there are also informal ones. Leadership, organization culture, and how the organization responds to whistle blowers each helps shape and define people's perceptions of the organization's stance on social responsibility.

Organization Leadership and Culture Leadership practices and organization culture can go a long way toward defining the social responsibility stance an organization and its members will adopt.[27] For example, Johnson & Johnson executives for years provided a consistent message to employees that customers, employees, com-

munities where the company did business, and shareholders were all important—and primarily in that order. Thus, when packages of poisoned Tylenol showed up on store shelves in the 1980s, Johnson & Johnson employees didn't need to wait for orders from headquarters to know what to do: they immediately pulled all the packages from shelves before any other customers could buy them.[28] By contrast, the message sent to Astra USA employees by the actions of their top managers communicates much less regard for social responsibility.

Whistle-Blowing **Whistle-blowing** is the disclosure by an employee of illegal or unethical conduct on the part of others within the organization.[29] How an organization responds to this practice often indicates its stance toward social responsibility. Whistle blowers may have to proceed through a number of channels to be heard, and they may even get fired for their efforts. Many organizations, however, welcome their contributions. A person who observes questionable behavior typically first reports the incident to his or her boss. If nothing is done, the whistle blower may then inform higher level managers or an ethics committee if one exists. Eventually, the person may have to go to a regulatory agency or even the media to be heard. For example, Charles W. Robinson Jr. once worked as a director of a SmithKline lab in San Antonio. One day he noticed a suspicious billing pattern the firm was using to collect lab fees from Medicare that were considerably higher than the firm's normal charges for those same tests. He pointed out the problem to higher level managers, but his concerns were ignored. He subsequently took his findings to the U.S. government, which sued SmithKline and eventually reached a settlement of $325 million.[30]

whistle-blowing The disclosure by an employee of illegal or unethical conduct on the part of others within the organization

Evaluating Social Responsibility

Any organization that is serious about social responsibility must ensure that its efforts are producing the desired benefits. Essentially this assurance requires applying the concept of control to social responsibility. Many organizations now require current and new employees to read their guidelines or code of ethics and then sign a statement agreeing to abide by it. An organization should also evaluate how it responds to instances of questionable legal or ethical conduct. Does it follow up immediately? Does it punish those involved? Or does it use delay and cover-up tactics? Answers to these questions can help an organization form a picture of its approach to social responsibility.

More formally, an organization may evaluate the effectiveness of its social responsibility efforts. For example, when Amoco recently established a job training program in Chicago, it allocated additional funds to evaluate how well the program was meeting its goals. Some organizations occasionally conduct corporate social audits. A **corporate social audit** is a formal and thorough analysis of the effectiveness of the firm's social performance. The audit is usually conducted by a task force of high-level managers from within the firm. It requires that the organization clearly define all its social goals, analyze the resources it devotes to each goal, determine how well it is achieving the various goals, and make recommendations about which areas need additional attention.

corporate social audit A formal and thorough analysis of the effectiveness of a firm's social performance

Ben & Jerry's conducts a formal audit of its social responsibility programs each year and publishes the results—favorable or otherwise—in its annual report. For example, one recent audit found that the firm was using a misleading label on one of its ice cream products. This criticism was published in the firm's next annual report, along with a promise both to correct the error and to strive to avoid similar problems in the future.[31] Unfortunately, such audits are not conducted often because they are expensive and time consuming. Indeed, most organizations probably could do much more to evaluate the extent of their social responsibility than they do.[32]

MANAGEMENT IMPLICATIONS Managers should understand that social responsibility is not something that just "happens." Instead, like other organizational activities, it must be actively managed. Recognizing and using both formal and informal dimensions can help manage the social responsibility process, as can actually evaluating the firm's social responsibility efforts and strategies.

Summary of Key Points

Ethics are an individual's personal beliefs about what constitutes right and wrong behavior. Important areas of ethical concern for managers are how the organization treats its employees, how employees treat the organization, and how the organization and its employees treat other economic agents. The ethical context of organizations consists of each manager's individual ethics and messages sent by organizational practices. Organizations use leadership, culture, training, codes, and guidelines to help them manage ethical behavior.

Social responsibility is the set of obligations an organization has to protect and enhance the society in which it functions. Organizations may be considered responsible to their stakeholders, to the natural environment, and to the general social welfare. Even so, organizations present strong arguments both for and against social responsibility. The approach an organization adopts toward social responsibility falls along a continuum of lesser to greater commitment: the obstructionist stance, the defensive stance, the accommodative stance, and the proactive stance.

Government influences organizations through regulation, which is the establishment of laws and rules that dictate what businesses can and cannot do in prescribed areas. Organizations, in turn, rely on personal contacts, lobbying, political action committees, and favors to influence the government.

Organizations use three types of activities to manage social responsibility formally: legal compliance, ethical compliance, and philanthropic giving. Leadership, culture, and whistleblowing are informal means for managing social responsibility. Organizations should evaluate the effectiveness of their socially responsible practices as they would any other strategy.

Discussion Questions

Questions for Review

1. Do organizations have ethics? Why or why not?
2. Summarize the basic stances that an organization can take regarding social responsibility.
3. What are the arguments for and against social responsibility?
4. How does the government influence organizations? How do organizations influence the government?

Questions for Analysis

5. What is the relationship between the law and ethical behavior? Can illegal behavior possibly be ethical?
6. How are the ethics of an organization's CEO related to social responsibility?
7. How do you feel about whistle-blowing? If you were aware of a criminal activity taking place in your organization, and if reporting it might cost you your job, would you report it?

Questions for Application

8. Refresh your memory about the Exxon *Valdez* oil spill. Evaluate the social responsibility dilemmas facing the company. For example, if Exxon had pledged unlimited resources to the cleanup, would this action have been fair to the company's stockholders?
9. Assume that you own a large and highly profitable business. What stance would you take toward social responsibility? List five specific programs or causes that you might be inclined to support.
10. Review the arguments for and against social responsibility. On a scale of one to ten, rate the validity and importance of each point. Use these ratings to develop a position regarding how socially responsible an organization should be. Now compare your ratings and position with those of two of your classmates. Discuss your respective positions, focusing primarily on disagreements.

BUILDING EFFECTIVE *decision-making* SKILLS

Exercise Overview

Decision-making skills refer to the manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action to solve problems and capitalize on opportunities. Many decisions made by managers have an ethical component. This exercise will help you better appreciate the potential role of ethics in making decisions.

Exercise Background

Read and reflect on each of the following scenarios:

1. You are the top manager of a major international oil company. Because of a recent oil spill by another firm, all the companies in the industry have been subjected to close scrutiny regarding the safety of various work practices. Your safety manager has completed a review and informed you that your firm has one potential problem area. The manager estimates the probability of a problem within the next five years as being about 3 percent. The costs of fixing things now would be about $1.5 million. Should you do nothing and a problem develop, however, the costs will be $10 million, plus your firm will receive a lot of bad publicity.
2. You manage a small fast-food restaurant. The owner has just informed you that you need to cut your payroll by twenty hours per week. There are two obvious choices. One is a retired woman who works part-time for

you. She lives on a fixed income, is raising three grandchildren, and really needs the money she earns from this job. The other is a college student who also works part-time. He is one year away from getting his degree and must work to pay his tuition and fees.

3. You have decided to donate $1,000 to a worthy cause in your neighborhood on behalf of the small business you own. Based on your own research, you have learned that the groups and charities most in need of funds are a local homeless shelter, a youth soccer league, an abortion clinic, and a tutoring program for illiterate adults.

Exercise Task

With the background information above as context, do the following:

1. Make a decision between the two courses of action for scenario one.
2. Decide which of the two employees to terminate in scenario two.
3. Decide where to donate your money in scenario three.
4. What role did your own personal ethics play in making each of these decisions?
5. Compare your decisions with those of a classmate and discuss why any differences arose.

BUILDING EFFECTIVE *interpersonal* SKILLS

Exercise Overview

Interpersonal skills refer to the ability to communicate with, understand, and motivate individuals and groups. Interpersonal skills may be especially important in a situation in which ethics and social responsibility issues are involved. This exercise will help you better relate interpersonal skills to ethical situations.

Exercise Background

Assume that you are a department manager in a large retail store. Your work group recently had a problem with sexual harassment. Specifically, one of your female employees reported to you that a male employee was telling off-color jokes and making mildly suggestive comments. When you asked him about the charges, he did not deny them but instead attributed them to a misunderstanding.

He was subsequently suspended with pay while the situation was investigated. The human resource manager who interviewed both parties, as well as other employees, concluded that the male employee should not be fired but should instead be placed on six months' probation. During this period, any further substantiated charges against him will result in immediate dismissal.

The basis for this decision included the following: (1) the male has worked in the store for over ten years, has a good performance record, and has had no earlier problems; (2) the female indicated that she did not believe that he was directly targeting her for harassment but instead was guilty of general insensitivity; and (3) the female did not think that his actions were sufficiently blatant as to warrant dismissal but simply wanted him to stop those behaviors.

Tomorrow will be his first day back at work. You are a bit worried about tensions in the group when he returns. You intend to meet with the female today and with the male tomorrow morning and attempt to minimize this tension.

Exercise Task

With the background information above as context, do the following:

1. Write general notes about what you will say to the female.
2. Write general notes about what you will say to the male.
3. What are the ethical issues in this situation?
4. If you have the option of having them work closely together or keeping them separated, which would you do? Why?

BUILDING EFFECTIVE *communication* SKILLS

Exercise Overview

Communication skills refer to the manager's abilities both to convey ideas and information effectively to others and to receive ideas and information effectively from others. Communication, ethics, and social responsibility are closely intertwined in certain situations. This exercise will help you relate these concepts to one another.

Exercise Background

You are the public relations manager for a large chemical company. One of your foreign plants has just suffered an explosion. While no one was killed, several dozen employees were injured. In addition, toxic chemical compounds were discharged into a nearby river and will undoubtedly cause major environmental damage. It is also clear that your company's managers at the plant are responsible for the explosion. You have learned, for example, that they took shortcuts when safety equipment was installed, used inferior materials, and failed to train key employees adequately in basic safety procedures.

Your experts' best estimates now are that it will take at least six months to clean up the river. There are also reports that the injured employees are already preparing lawsuits against the company. The local press at the plant site is also calling for an immediate and public apology and a commitment by the firm to make full restitution for all damages caused by the explosion.

A press conference has been called for one hour from now. You will be making a prepared statement about the situation and then answering questions from the reporters. Your boss, however, has given you some directions. For one thing, he says that acknowledging that six months will be needed to clean up the river will be disastrous. Instead, he wants you to indicate that cleanup will be completed in two months. He also wants you to recognize the pain caused to your injured employees and to wish them a speedy recovery, but not to acknowledge any guilt or liability on the part of your company.

Exercise Task

With the background information above as context, do the following:

1. Write a press statement that meets your boss's mandate.
2. Write a press statement that is completely accurate.
3. What are the likely short- and long-term ethical implications of each statement?
4. Could you personally deliver the first statement?

CHAPTER CLOSING CASE

ETHICAL CHARGES ROCK PRUDENTIAL

In recent years, Prudential Insurance Company of America has been rocked by charges of unethical behavior. Soon after the company settled one class-action lawsuit over questionable sales tactics, it became embroiled in a second round of legal battles over charges related to the first lawsuit.

The trouble started in the mid-1990s, when thousands of customers complained about the way Prudential salespeople were selling insurance policies. Some customers were told they were buying retirement programs when, in actuality, they were buying insurance. Others were told, incorrectly, that the dividends on their insurance policies would build up enough to cover the premium payments within as little as seven years. Still others said they were tricked into turning in older insurance policies and buying new, more costly policies.

More than six hundred thousand Prudential customers banded together in a class-action lawsuit over these sales abuses. The suit was settled in 1997 for $2.7 billion, but the terms of the settlement were controversial: Prudential was given the task of reviewing customers' claims to determine the level of restitution for each. Because of the pervasiveness of the sales abuses, observers believed that many customers would receive large restitution awards. After Prudential reviewed the cases, however, it awarded the top level of restitution to only one in four customers.

The second round of lawsuits stemmed from the way Prudential handled its review of customer claims in the wake of the class-action suit. The company had to hire thousands of new workers to investigate these claims and recommend appropriate compensation on a case-by-case basis. Although the new employees received fast but intensive training, they had difficulty getting clear direction from their managers as they worked to unravel the complexities of individual claims.

When insurance regulators who were hoping to get quicker restitution for customers protested the slow pace of the reviews, Prudential management decided to put more emphasis on productivity. The company promised employees money, gift certificates, candy, and gifts to reward speedier processing of claims reviews. As the process speeded up, reviewers began to complain that managers were ordering them to overlook documents that might support the customer's side. They also said some managers balked when reviewers tried to recommend the top level of restitution for some customers.

Prudential admitted seeking higher productivity but said it was still keeping a close eye on quality. The company also stressed that customers could appeal to independent arbitrators (at Prudential's expense) if they believed they were due higher levels of restitution. Only about one in ten customers who were eligible wound up appealing, perhaps because few knew how the appeals process operated.

Meanwhile, some of the employees reviewing claims became upset at the situation and filed suit. One said the insurer retaliated against him by demoting him for attempting to obtain top-level restitution for customers. Another said he was pressured to hurry through the review process by setting aside some types of documentation, rather than examining all the information for each case. In all, dozens of employees went to court against Prudential.

This second round of lawsuits drew the attention of the federal judge who handled the original class-action suit. He ordered Prudential and the class-action attorneys for its customers to investigate the employees' charges. As the probe progressed, Prudential said that it had safeguards in place to protect customers and to correct errors that might have been made during the review process. The insurer was eager to close this troubled chapter in its history.

Case Questions

1. Do you think the court was right to leave Prudential in charge of reviewing its customers' claims after the class-action lawsuit? Should someone outside the company have been given this responsibility instead? Why?
2. Within which of the three areas of concern for managerial ethics did Prudential appear to be experiencing problems?
3. If you headed Prudential, what standards would you include in a code of ethics to guide managers in making ethical decisions when dealing with customers and employees?

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CHAPTER 5 The Global Environment

OPENING INCIDENT

Mickey Mouse's famed silhouette is no doubt just as recognizable in Brazil, India, Italy, or Nigeria as is the shape of a Coca-Cola bottle or the golden arches of McDonald's. But the Walt Disney Company has done a surprisingly poor job of capitalizing on the global potential for its various products. In 1999, for instance, 80 percent of Disney's $23.4 billion in revenues came from the United States, a country with only 5 percent of the world's population. This statistic contrasts markedly with Coca-Cola and McDonald's, who each derive about two-thirds of their revenue from other countries.

Disney's most visible global efforts have involved theme parks. Its first foreign venture, Tokyo Disneyland, opened in 1984. To limit its risk, the firm did not directly invest in the park. Instead, a Japanese investment group financed and owns Tokyo Disneyland. Disney oversaw construction and manages the park but receives only royalty income. Tokyo Disneyland has been an enormous success. For example, it greeted its one hundred millionth visitor after only eight years, a milestone that Disneyland in California took twice as long to reach. Indeed, in retrospect, Disney managers acknowledge that they were overly cautious when they chose not to risk equity ownership in the park.

Disney subsequently decided to build a theme park in Europe just outside Paris. This time, though, Disney decided to participate more fully in the park and retained 49 percent ownership for itself. The French government also provided numerous economic incentives by selling the land for the park to Disney at bargain-basement prices and extending the Parisian rail system to the park's front gate. But as Euro Disney opened its doors to the public on April 12, 1992, amid widespread hoopla, problems started to arise.

For example, the French cultural elite lambasted Euro Disnev as an affront to the country's cultural heritage, and farmers picketed aside the main gates protesting the manner in which their land had been taken. Disney also severely misjudged the spending and lodging habits of its visitors. Disney planners had presumed hotel guests would stay an average of three days, as they do in Orlando. But Euro Disney visitors typically stayed two days or less. A recession also led to weak attendance and even lower spending. At this point, Euro Disney seemed to be burning money, and it even came close to being shut down. Eventually, a complex and costly financial restructuring plan implemented in 1994 barely saved the park, and it has only been within the last few years

"Disney is in the ironic position of being one of the best-known brands on the planet, but with too little of its income being generated outside of the United States."

—Michael Eisner, CEO of The Walt Disney Company

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- **Describe the nature of international business, including its meaning, recent trends, the management of globalization, and competition in a global environment.**
- **Discuss the structure of the global economy and how it affects international management.**
- **Identify and discuss the environmental challenges inherent in international management.**
- **Describe the basic issues involved in competing in a global economy, including organization size and the management challenges in a global economy.**

CHAPTER OUTLINE

- **The Nature of International Business**
  - The Meaning of International Business
  - Trends in International Business
  - Managing the Process of Globalization
  - Competing in a Global Environment
- **The Structure of the Global Economy**
  - Mature Market Economies and Systems
  - High Potential/High Growth Economies
  - Other Economies
- **Environmental Challenges of International Management**
  - The Economic Environment
  - The Political/Legal Environment
  - The Cultural Environment
- **Competing in a Global Economy**
  - Globalization and Organization Size
  - Management Challenges in a Global Economy

that Disneyland Paris, as the park was renamed, has begun earning profits.

Fortunately, Disney seems to be getting its act together regarding international theme park operations. For example, in 2001 it opened Tokyo DisneySea adjacent to Tokyo Disneyland. Both attendance and spending have improved at Disneyland Paris, and a new park will also open there in 2002. Disney's biggest news, though, was its recent announcement that it would build a new park in Hong Kong. The company gets a 43 percent equity stake in the $3.6 billion project in exchange for an investment of only $314 million. The local government, in turn, will invest over $2.9 billion in low-interest loans, land, and infrastructure improvements for the remaining 57 percent share.

But Disney continues to struggle in other areas of its international operations. For example, there are only 11 million subscribers to the Disney Channel cable television network outside the United States; this contrasts with 54 million foreign subscribers to Time Warner's Cartoon Network. And the company has experienced a $159 million decline in worldwide licensing revenues in recent years. Indeed, things have gotten so bad that Disney is overhauling its business and has created a separate unit called Walt Disney International. Its goal? Obviously, to increase international revenues. For example, managers have calculated that if they can increase per capita consumer spending on Disney-related products in just five countries—England, Italy, Germany, France, and Japan—to 80 percent of the level in the United States, the firm would generate an additional $2 billion in annual revenues.[1]



While every business is unique, the challenges and opportunities facing The Walt Disney Company are increasingly common among today's multinational corporations. Specifically, such businesses must make critical decisions regarding how they will allocate their resources in different markets and how they will strive to gain a competitive advantage in those markets. Indeed, to be successful today, managers have to understand the global context within which they function. And this fact holds true regardless of whether the manager runs a *Fortune* 500 firm or a small independent company.

This chapter explores the global context of management. We start by describing the nature of international business. We then discuss the structure of the global market in terms of different economies and economic systems. The basic environmental challenges of management are introduced and discussed next. We then focus on issues of competition in a global economy. We conclude by characterizing the managerial functions of planning, organizing, leading, and controlling as management challenges in a global economy.

■ The Nature of International Business

As you prepared breakfast this morning, you may have plugged in a coffee pot manufactured in Asia and perhaps ironed a shirt or blouse made in Taiwan with an iron made in Mexico. The coffee you drank was probably made from beans grown in South America. To get to school, you may have driven a Japanese car. Even if you drive a Ford or Chevrolet, some of its parts were engineered or manufactured abroad. Perhaps you didn't drive a car to school but rather rode a bus (manufactured by DaimlerChrysler, a German company, or by Volvo, a Swedish company) or a motorcycle (manufactured by Honda, Kawasaki, Suzuki, or Yamaha—all Japanese firms).

Our daily lives are strongly influenced by businesses from around the world. But no country is unique in this respect. For instance, people drive Fords in Germany, use Dell computers in China, eat McDonald's hamburgers in France, and snack on Mars candy bars in England. They drink Pepsi and wear Levi Strauss jeans in China. The Japanese buy Kodak film and use American Express credit cards. People around the world fly on American Airlines in planes made by Boeing. Their buildings are constructed with Caterpillar machinery, their factories are powered by General Electric engines, and they buy Chevron oil.

In truth, we have become part of a global village and have a global economy where no organization is insulated from the effects of foreign markets and competition.[2] Indeed, more and more firms are reshaping themselves for international competition and are discovering new ways to exploit markets in every corner of the world. Failure to take a global perspective is one of the biggest mistakes managers can make.[3] Thus, we start laying the foundation of our discussion by introducing and describing the basics of international business.



Figure 5.1
Levels of International Business Activity

The Meaning of International Business

There are many different forms and levels of international business. While the lines that distinguish one from another are perhaps arbitrary, we can identify four general levels of international activity that differentiate organizations.[4] These levels are illustrated in Figure 5.1. A **domestic business** acquires essentially all its resources and sells all its products or services within a single country. Most small businesses are essentially domestic in nature, as are many banks, retailers, agricultural enterprises, and service firms. However, there are very few large domestic businesses left in the world today.

domestic business A business that acquires all its resources and sells all its products or services within a single country

Indeed, most large firms today are either international or multinational companies. An **international business** is one that is primarily based in a single country but acquires some meaningful share of its resources or revenues (or both) from other countries. Sears fits this description. Most of its stores are in the United States, for example, and the retailer earns around 90 percent of its revenues from its U.S. operations, with the remaining 10 percent coming from Sears stores in Canada. At the same time, however, many of the products it sells, such as tools and clothing, are made abroad.[5]

international business A business that is primarily based in a single country but acquires some meaningful share of its resources or revenues (or both) from other countries

A **multinational business** has a worldwide marketplace from which it buys raw materials, borrows money, and manufactures its products and to which it subsequently sells its products. Ford Motor Company is an excellent example of a multinational company. It has design and production facilities around the world. The Ford Focus, for instance, was jointly designed by European and U.S. teams and is sold with only minor variations in dozens of foreign markets. Ford makes and sells other cars in Europe that are never seen in the United States. Ford cars are designed, produced, and sold for individual markets, wherever they are and without regard for national boundaries. Multinational businesses are often called *multinational corporations* or *MNCs*.[6]

multinational business One that has a worldwide marketplace from which it buys raw materials, borrows money, and manufactures its products and to which it subsequently sells its products

The final form of international business is the global business. A **global business** is one that transcends national boundaries and is not committed to a single home country. Although no business has truly achieved this level of international involvement, a few are edging closer and closer. For example, Hoechst AG, a large German chemical company, portrays itself as a "non-national company." Similarly, Unocal Corporation is legally headquartered in California. But in its company literature, Unocal says it "no longer considers itself as a U.S. company," but is, instead, a "global energy company."[7]

global business A business that transcends national boundaries and is not committed to a single home country

Trends in International Business

To understand why and how these different levels of international business have emerged, we must briefly look to the past. Most of the industrialized countries in Europe had been devastated during the last world war. Many Asian countries, especially Japan, had fared no better. There were few passable roads, few standing bridges, and even fewer factories dedicated to the manufacture of peacetime products. And those regions less affected by wartime destruction—Canada, Latin America, and Africa—had not yet developed the economic muscle to threaten the economic pre-eminence of the United States.

Businesses in war-torn countries like Germany and Japan had no choice but to rebuild from scratch. Because of this position, they essentially had to rethink every facet of their operations, including technology, production, finance, and marketing. Although it took many years for these countries to recover, they eventually did so, and their economic systems were subsequently poised for growth. During the same era, U.S. companies grew complacent. Their customer base was growing rapidly. Increased population spurred by the baby boom and increased affluence resulting from the postwar economic boom greatly raised the average person's standard of living and expectations. The U.S. public continually wanted new and better products and services. Many U.S. companies profited greatly from this pattern, but most were also perhaps guilty of taking it for granted.

But U.S. firms are no longer isolated from global competition or the global market. A few simple numbers help tell the full story of international trade and industry. First of all, the volume of international trade increased more than 3,000 percent from 1960 to 2000. Further, while 162 of the world's largest corporations are headquartered in the United States, there are also 126 in Japan, 42 in France, 41 in Germany, and 34 in Britain.[8] Within certain industries, the pre-eminence of non-U.S. firms is even more striking. For example, only one each of the world's ten largest banks and ten largest electronics companies is based in the United States. Only two of the ten largest chemical companies are U.S. firms. On the other hand, U.S. firms comprise six of the eight largest aerospace companies, four of the seven largest airlines, six of the nine largest computer companies, four of the five largest diversified financial companies, and six of the ten largest retailers.[9]

U.S. firms are also finding that international operations are an increasingly important element of their sales and profits. For example, in 1999 Exxon Corporation realized 82 percent of its revenues and 68 percent of its profits abroad. For Avon, these percentages were 66 percent and 70 percent, respectively.[10] From any perspective, then, it is clear that we live in a truly global economy. Virtually all businesses today must be concerned with the competitive situations they face in lands far from home and with how companies from distant lands are competing in their homeland.

Managing the Process of Globalization

Managers should also recognize that their global context dictates two related but distinct sets of challenges. One set of challenges must be confronted when an organization chooses to change its level of international involvement. For example, a

firm that wants to move from being an international to a multinational business has to manage that transition.[11] The other set of challenges occurs when the organization has achieved its desired level of international involvement and must then function effectively within that environment. This section highlights the first set of challenges, and the next section introduces the second set of challenges. When an organization makes the decision to increase its level of international activity, there are several alternative strategies that can be adopted.

Importing and Exporting Importing or exporting (or both) is usually the first type of international business in which a firm gets involved. **Exporting**, or making the product in the firm's domestic marketplace and selling it in another country, can involve both merchandise and services. **Importing** is bringing a good, service, or capital into the home country from abroad. For example, automobiles (Mazda, Ford, Volkswagen, Mercedes-Benz, Ferrari) and stereo equipment (Sony, Bang and Olufsen, Sanyo) are routinely exported by their manufacturers to other countries. Likewise, many wine distributors buy products from vineyards in France, Italy, and/or California and import them into their own countries for resale.

exporting Making a product in the firm's domestic marketplace and selling it in another country

importing Bringing a good, service, or capital into the home country from abroad

An import/export operation has several advantages. For example, it is the easiest way of entering a market with a small outlay of capital. Because the products are sold as is, there is no need to adapt the product to the local conditions, and little risk is involved. Nevertheless, there are also disadvantages. For example, imports and exports are subject to taxes, tariffs, and higher transportation expenses. Furthermore, because the products are not adapted to local conditions, they may miss the needs of a large segment of the market. Finally, some products may be restricted and thus can be neither imported nor exported.

Licensing is an increasingly popular method for entering foreign markets. Franchising, a form of licensing, is especially popular these days. Pizza Hut, for example, is rapidly expanding into new markets around the world via franchising agreements with local investors and managers. The popular restaurants can now be found in over 100 different countries. St. Petersburg, Russia, is one of the more recent markets where Pizza Hut has set up shop.



Licensing A company may prefer to arrange for a foreign company to manufacture or market its products under a licensing agreement. Factors that may lead to this decision include excessive transportation costs, government regulations, and home production costs. **Licensing** is an arrangement whereby a firm allows another company to use its brand name, trademark, technology, patent, copyright, or other assets. In return, the licensee pays a royalty, usually based on sales. For example, Kirin Brewery, Japan's largest producer of beer, wanted to expand its international operations but feared that the time involved in shipping beer from Japan would cause it to lose its freshness. Thus, it has entered into a number of licensing arrangements with breweries in other markets. These brewers make beer according to strict guidelines provided by

licensing An arrangement whereby a firm allows another company to use its brand name, trademark, technology, patent, copyright, or other assets in exchange for a royalty based on sales

the Japanese firm, and then package and market it as Kirin Beer. They then pay a royalty to Kirin for each case sold. Molson produces Kirin in Canada under such an agreement, while the Charles Wells brewery does the same in England.[12]

Two advantages of licensing are increased profitability and extended profitability. This strategy is frequently used for entry into less developed countries where older technology is still acceptable and, in fact, may be state of the art. A primary disadvantage of licensing is inflexibility. A firm can tie up control of its product or expertise for a long period of time. And if the licensee does not develop the market effectively, the licensing firm can lose profits. A second disadvantage is that licensees can take the knowledge and skill that they have been given access to for a foreign market and exploit them in the licensing firm's home market. When this happens, what used to be a business partner becomes a business competitor.

strategic alliance A cooperative arrangement between two or more firms for mutual gain

Strategic Alliances In a **strategic alliance**, two or more firms jointly cooperate for mutual gain.[13] For example, Kodak and Fuji, along with three major Japanese camera manufacturers, collaborated on the development of a new film cartridge. This collaboration allowed Kodak and Fuji to share development costs, prevented an advertising war if the two firms had developed different cartridges, and made it easier for new cameras to be introduced at the same time as the new film cartridges. A **joint venture** is a special type of strategic alliance in which the partners share ownership of a new enterprise. General Mills and Nestlé formed a new company called Cereal Partners Worldwide (CPW). The purpose of CPW is to produce and market cereals. General Mills supplies the technology and proven formulas, while Nestlé provides its international distribution network. The two partners share equally in the new enterprise. Strategic alliances have enjoyed a tremendous upsurge in the past few years. In most cases, each party provides a portion of the equity or the equivalent in physical plant, raw materials, cash, or other assets. The proportion of the investment then determines the percentage of ownership in the venture.[14]

joint venture A special type of strategic alliance in which the partners share ownership of a new enterprise

Strategic alliances have both advantages and disadvantages. For example, they can allow quick entry into a market by taking advantage of the existing strengths of participants. Japanese automobile manufacturers employed this strategy to their advantage to enter the U.S. market by using the already established distribution systems of U.S. automobile manufacturers. Strategic alliances are also an effective way of gaining access to technology or raw materials. And they allow the firms to share the risk and cost of the new venture. One major disadvantage of this approach lies with the shared ownership of joint ventures. Although it reduces the risk for each participant, it also limits the control and the return that each firm can enjoy.[15]

Direct Investment Another level of commitment to internationalization is direct investment. **Direct investment** occurs when a firm headquartered in one country builds or purchases operating facilities or subsidiaries in a foreign country. The foreign operations then become wholly owned subsidiaries of the firm. Ford's acquisitions of Jaguar, Volvo, and Kia and British Petroleum's acquisition of Amoco were each major forms of direct investment. Similarly, Dell Computer's new factory in China is also a direct investment.

direct investment When a firm headquartered in one country builds or purchases operating facilities or subsidiaries in a foreign country

A major reason many firms make direct investments is to capitalize on lower labor costs; that is, the goal is often to transfer production to locations where labor is cheap. Japanese businesses have moved much of their production to Thailand because labor costs are much lower there than in Japan. Many U.S. firms are using maquiladoras for the same purpose. **Maquiladoras** are light assembly plants built in northern Mexico close to the U.S. border. The plants are given special tax breaks by the Mexican government, and the area is populated with workers willing to work for very low wages. More than one thousand plants in the region employ three hundred thousand workers, and more are planned. The plants are owned by major corporations, primarily from the United States, Japan, South Korea, and major European industrial countries. This concentrated form of direct investment benefits the country of Mexico, the companies themselves, and workers who might otherwise be without jobs. Some critics argue, however, that the low wages paid by the maquiladoras amount to little more than slave labor.[16]

maquiladoras Light assembly plants built in northern Mexico close to the U.S. border that are given special tax breaks by the Mexican government

Like the other approaches for increasing a firm's level of internationalization, direct investment carries with it a number of benefits and liabilities. Managerial control is more complete, and profits do not have to be shared as they do in joint ventures. Purchasing an existing organization provides additional benefits because the human resources, plant, and organizational infrastructure are already in place. Acquisition is also a way to purchase the brand-name identification of a product. This could be particularly important if the cost of introducing a new brand is high. When Nestlé bought the U.S. firm Carnation Company several years ago, it retained the firm's brand names for all its products sold in the United States. Notwithstanding these advantages, the company is now operating part of its business entirely within the borders of a foreign country. The additional complexity in the decision making, the economic and political risks, and so forth, may outweigh the advantages that can be obtained by international expansion.

Of course, we should also note that these approaches to internationalization are not mutually exclusive. Indeed, most large firms use all of them simultaneously. MNCs have a global orientation and worldwide approach to foreign markets and production. They search for opportunities all over the world and select the best strategy to serve each market. In some settings, they may use direct investment; in others, licensing; in others, strategic alliances; in still others they might limit their involvement to exporting and importing. The advantages and disadvantages of each approach are summarized in Table 5.1.

Competing in a Global Environment

Even when a firm is not actively seeking to increase its desired level of internationalization, its managers are still responsible for seeing that it functions effectively within whatever level of international involvement the organization has achieved. In one sense, the job of a manager in an international business may not be that much different from the job of a manager in a domestic business. Each may be responsible for acquiring resources and materials, making products, providing services, developing human resources, advertising, or monitoring cash flow.

In another sense, however, the complexity associated with each of these activities may be much greater for managers in international firms. Rather than buying

Table 5.1

Advantages and Disadvantages of Different Approaches to Internationalization

When organizations decide to increase their level of internationalization, they can adopt several strategies. Each strategy is a matter of degree, as opposed to being a discrete and mutually exclusive category. And each has unique advantages and disadvantages that must be considered.

Approaches to Internationalization	Advantages	Disadvantages
Importing or Exporting	1. Small cash outlay 2. Little risk 3. No adaptation necessary	1. Tariffs and taxes 2. High transportation costs 3. Government restrictions
Licensing	1. Increased profitability 2. Extended profitability	1. Inflexibility 2. Helps competitors
Strategic Alliance/ Joint Ventures	1. Quick market entry 2. Access to materials and technology	1. Shared ownership (limits control and profits)
Direct investment	1. Enhances control 2. Existing infrastructure	1. Complexity 2. Greater economic and political risk 3. Greater uncertainty

raw materials from sources in California, Texas, and Missouri, an international purchasing manager may buy materials from sources in Peru, India, and Spain. Rather than train managers for new plants in Michigan, Florida, and Oregon, the international human resources executive may be training new plant managers for facilities in China, Mexico, and Scotland. And instead of developing a single marketing campaign for the United States, an advertising director may be working on promotional efforts in France, Brazil, and Japan. *Managing in an E-world* illustrates some of the complexity associated with e-commerce in Latin America.

The key question that must be addressed by any manager trying to be effective in an international market is whether to focus on globalization or regionalism. A global thrust requires that activities be managed from an overall global perspective as part of an integrated system. Regionalism, on the other hand, involves managing within each region with less regard for the overall organization. In reality, most larger MNCs manage some activities globally (for example, finance and manufacturing) and others locally (such as human resources management and advertising). We explore these approaches more fully later in this chapter.

MANAGEMENT IMPLICATIONS All managers need to understand the global environment in which they function. For managers in large multinational corporations, the global context is obvious. But even smaller domestic companies are affected by international forces. It is also important to understand the different methods for entering a foreign market and the strengths and weaknesses of each. Managers should also recognize the distinctions between the processes of internationalization and the management issues inherent in running a company with an existing international context.

MANAGING IN AN *e*-BUSINESS WORLD

E-Commerce Growth in Latin America

Problems with old computer systems, unwieldy distribution channels, and credit card fraud are keeping many Latin American businesses from jumping on the e-commerce bandwagon. Other barriers to growth in Latin American e-commerce include government policies that lag behind the Internet revolution and a scarcity of venture capital to fund entrepreneurial web start-ups.

Despite this slow start, e-commerce in the region is on the brink of a major growth spurt. Experts say that nearly seven million people will be logging onto the Internet from Latin America by 2004. Not surprisingly, this fast-growing market is drawing the interest of visionary local companies as well as MNCs based in other countries.

For example, America Online is offering Internet access in Brazil and Mexico, and Telefonos de Mexico SA has partnered with Microsoft to create a Spanish language portal. Grupo Televisa, Mexico's leading television network, is expanding into on-line media with its own web portal. Eyeing cross-border sales potential, U.S.-based e-commerce veterans such as Dell and Compaq are mounting campaigns to sell computers on-line in Latin America.

While some Latin American companies are reluctant to be on-line pioneers, others are moving full speed ahead. Consider the experience of Infosel in Mexico. Owned by Madrid-based Terra Networks SA, Infosel serves as an Internet service provider (ISP), sells on-line subscriptions to financial data, and hosts a well-trafficked consumer portal. The company is also launching a web retail site to sell a variety of high- and low-tech items within Mexico. Still, the head of Infosel has had difficulty convincing Mexican retail chains, mutual fund companies, and other businesses to give e-commerce a try.

If the Mexican businesses lose, I'm going to lose. Mexicans will end up buying products on Yahoo!

—Arturo Galvan, head of the Mexican unit of Terra Networks SA*

As the external environment for Mexican e-commerce becomes friendlier, however, more companies—local and global—will take advantage of the opportunities. Infosel is helping things along by developing the technology for secure digital signatures, a legal innovation that will accelerate the growth of business-to-business e-commerce in Mexico. Day by day, business by business, innovation by innovation, Latin America is becoming a major on-line market.

References: Andrea Petersen, "Opening a Portal: E-Commerce Apostles Target Latin America, But It's a Tough Sell," *Wall Street Journal*, January 25, 2000, pp. A1, A8 (*quote on p. A8); Jim Hu, "Lycos Bought In First Foreign Portal Deal," *CNET News.com*, May 16, 2000, http://news.cnet.com/news/0-1005-200-1877185.html?tag=st (July 10, 2000).

■ The Structure of the Global Economy

One thing that can be helpful to managers seeking to operate in a global environment is to understand the structure of the global economy better. Although each country, and indeed each region within any given country, is unique, we can still note some basic similarities and differences. We describe three different elements of the global economy: mature market economies and systems, high potential/high growth economies, and other economies.[17]

Mature Market Economies and Systems

market economy An economy based on the private ownership of business and allows market factors such as supply and demand to determine business strategy

A **market economy** is based on the private ownership of business and allows market factors such as supply and demand to determine business strategy. Mature market economies include the United States, Japan, the United Kingdom, France, Germany, and Sweden. These countries have several traits in common. For example, they tend to employ market forces in the allocation of resources. They also tend to be characterized by private ownership of property, although there is some variance along this dimension. France, for example, has a relatively high level of government ownership among the market economies.

U.S. managers have relatively few problems operating in market economies. Many of the business "rules of the game" that apply in the United States, for example, also apply in Germany or England. And consumers there often tend to buy the same kinds of products. For these reasons it is not unusual for U.S. firms seeking to expand geographically to begin operations in another market economy. Although the task of managing an international business in an industrial market country is somewhat less complicated than operating in some other type of economy, it still poses some challenges. Perhaps foremost among them is that the markets in these economies are typically quite mature. Many industries, for example, are already dominated by large and successful companies. Thus, competing in these economies poses a major challenge.

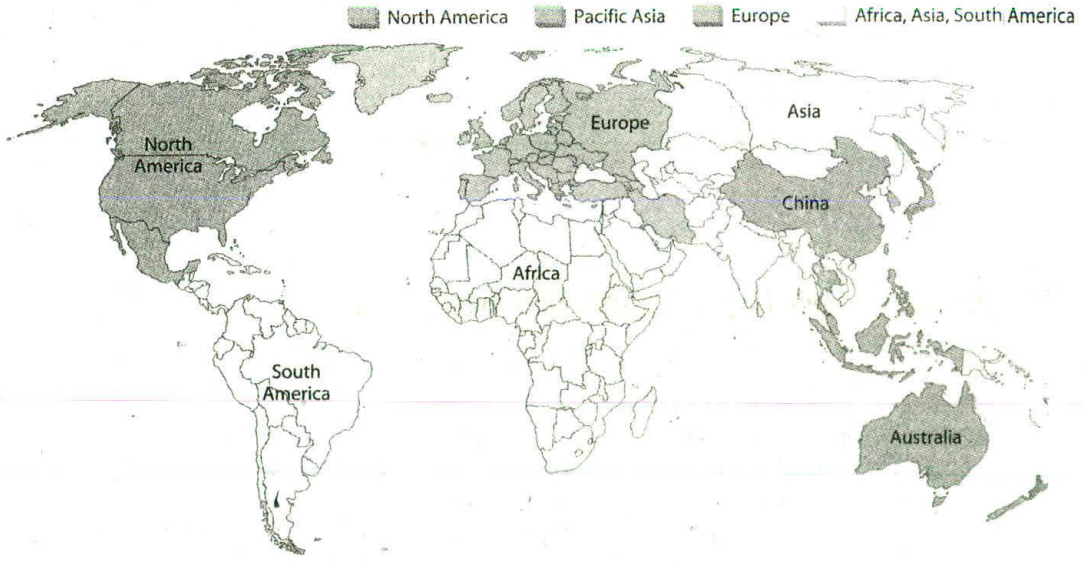
market systems Clusters of countries that engage in high levels of trade with each other

The map in Figure 5.2 highlights three relatively mature market systems. **Market systems** are clusters of countries that engage in high levels of trade with

Figure 5.2

The Global Economy

The global economy is dominated by three relatively mature market systems. As illustrated here, these market systems consist of North America, Europe (especially those nations in the European Union), and Pacific Asia (parts of which are high potential/high growth economies). Other areas of Asia, as well as Africa and South America, have the potential for future growth but currently play only a relatively small role in the global economy.



each other. One mature market system is North America. The United States, Canada, and Mexico are major trading partners with one another; more than 70 percent of Mexico's exports go to the United States, and more than 65 percent of what Mexico imports comes from the United States. During the last several years these countries have negotiated a variety of agreements to make trade even easier. The most important of these, the **North American Free Trade Agreement**, or **NAFTA**, eliminates many of the trade barriers—quotas and tariffs, for example—that existed previously.[18]

North American Free Trade Agreement (NAFTA) An agreement among the United States, Canada, and Mexico to promote trade with one another

Another mature market system is Europe. Until recently, Europe was two distinct economic areas. The eastern region consisted of communist countries such as Poland, Czechoslovakia, and Romania. These countries relied on government ownership of business and greatly restricted trade. In contrast, western European countries with traditional market economies have been working together to promote international trade for decades. In particular, the **European Union** (or **EU** as it is often called) has long been a formidable market system. The formal members of the EU are Denmark, the United Kingdom, Portugal, the Netherlands, Belgium, Spain, Ireland, Luxembourg, France, Germany, Italy, and Greece. For years these countries followed a basic plan that led to the elimination of most trade barriers in 1992.

European Union (EU) The first and most important international market system

The European situation has recently grown more complex, however. Communism has collapsed in most eastern countries, and they are trying to develop market economies. They also want greater participation in trade with the western European countries. In some ways the emergence of the east has slowed and complicated business activities in the west. In the long-term, however, the new markets in the east are likely to make Europe an even more important part of the world economy. For example, Poland is increasingly becoming a significant market for many MNCs.

Yet another mature market system is **Pacific Asia**. As shown in Figure 5.2, this market system includes Japan, China, Thailand, Malaysia, Singapore, Indonesia,

Pacific Asia A market system located in Southeast Asia



Most international business managers see the People's Republic of China as the most important emerging marketplace in the world. Its vast population and growing interest in consumerism combine to offer tremendous potential for a wide array of products and services. For example, even farmers in China's most remote regions hunger for new technology like the satellite dish shown here. Products like televisions, cellular telephones, computers, and automobiles are also experiencing strong demand as the citizens of China take their place alongside consumers from Japan, Europe, the United States, and the rest of the world.

South Korea, Taiwan, the Philippines, and Australia. Indeed, Japan, Taiwan, Singapore, Thailand, and South Korea were major economic powerhouses until a regional currency crisis slowed their growth in the 1990s. That crisis appears to be coming to an end, however; trade among these nations is on the rise, and talk has started about an Asian economic community much like the EU.[19]

High Potential/High Growth Economies

In contrast to the highly developed and mature market economies just described, other countries have what is termed *high potential/high growth economies*. These economies have been relatively underdeveloped and immature and, until recently, were characterized by weak industry, weak currency, and relatively poor consumers.[20] The governments in these countries, however, have been actively working to strengthen their economies by opening their doors to foreign investment and by promoting international trade. Some of these countries have only recently adopted market economies, while others still use a command economy.

Even though it is technically part of Pacific Asia, the People's Republic of China is largely underdeveloped. The transfer of control of Hong Kong from Great Britain to China in 1997 focused even more attention on the market potential in the world's most populous country.[21] India is also showing signs of becoming a major market in the future.[22] Vietnam has become a potentially important market, and Brazil is becoming more important as well.[23] Likewise, Russia and the other states and republics that previously made up the Commonwealth of Independent States are being closely watched by many companies for emerging market opportunities.[24]

The primary challenges presented by the developing economies to those interested in conducting international business there are the lack of wealth on the part of potential consumers and the underdeveloped infrastructure. Developing economies have enormous economic potential, but much of it remains untapped. Thus, international firms entering these markets often have to invest heavily in distribution systems, in training consumers how to use their products, and even in providing living facilities for their workers. They also run the risk of major policy changes that can greatly distort the value of their investments.[25]

Other Economies

There are some economic systems around the world that defy classification as either mature markets or high potential/high growth economies. One major area that falls outside these categories is the oil-exporting region generally called the Middle East. The oil-exporting countries present mixed models of resource allocation, property ownership, and the development of infrastructure. These countries all have access to major amounts of crude oil, however, and thus are important players in the global economy.

The oil-exporting countries include Iran, Iraq, Kuwait, Saudi Arabia, Libya, Syria, and the United Arab Emirates. High oil prices in the 1970s and 1980s created

enormous wealth in these countries. Many of them invested heavily in their infrastructures. Whole new cities were built, airports were constructed, and the population was educated. As oil prices have fallen, many of the oil-producing countries have been forced to cut back on these activities. Nevertheless, they are still quite wealthy. The per capita incomes of the United Arab Emirates and Qatar, for example, are among the highest in the world. Although there is great wealth in the oil-producing nations, they provide great challenges to managers. Political instability (as evidenced by the Persian Gulf War in 1991) and tremendous cultural differences, for example, combine to make doing business in many parts of the Middle East both very risky and very difficult.

Other countries pose risks to business of a different sort. Politically and ethnically motivated violence, for example, still characterizes some countries. Foremost among these are Peru, El Salvador, Turkey, Colombia, and Northern Ireland. Cuba presents special challenges because it is so insulated from the outside world. With the fall of communism, some experts believe that Cuba will eventually join the ranks of the market economies. If so, its strategic location will quickly make it an important business center.

MANAGEMENT IMPLICATIONS International managers need to have a fundamental understanding of the structure of the global economy. They should also recognize the advantages and disadvantages of competing in mature market economies and systems, high potential/high growth economies, and other economies.

■ *Environmental Challenges of International management*

We noted earlier that managing in a global context both poses and creates additional challenges for the manager. As illustrated in Figure 5.3, three environmental challenges in particular warrant additional exploration at this point—the economic environment, the political/legal environment, and the cultural environment of international management.[26]

The Economic Environment

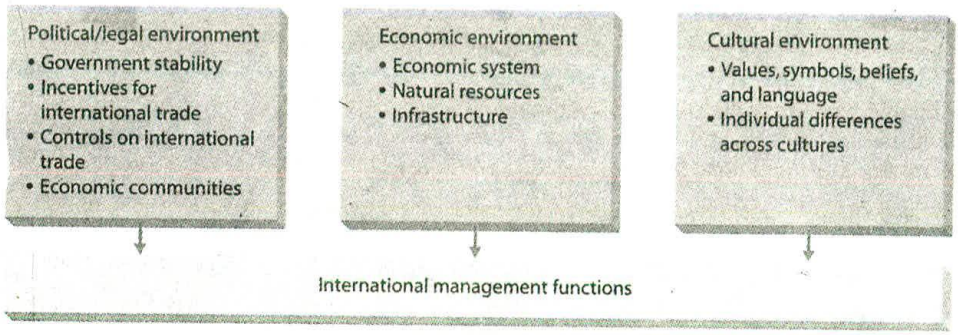
Every country is unique and creates a unique set of challenges for managers trying to do business there. However, there are three aspects of the economic environment that in particular can help managers anticipate the kinds of economic challenges they are likely to face when working abroad.

Economic System The first of these is the economic system used in the country. As we described earlier, most countries today are moving toward market economies. In a mature market economy, the key element for managers is freedom of choice. Consumers are free to make decisions about which products they prefer to purchase, and firms are free to decide what products and services to provide. As long as both

Figure 5.3

Environmental Challenges of International Management

Managers functioning in a global context must be aware of several environmental challenges. Three of the most important include economic, political/legal, and cultural challenges.



the consumer and the firm are free to decide to be members in the market, then supply and demand determine which firms and which products will be available.

A related characteristic of market economies that is relevant to managers concerns the nature of property ownership. There are two pure types—complete private ownership and complete public ownership. In systems with private ownership, individuals and organizations—not the government—own and operate the companies that conduct business. In systems with public ownership, the government directly owns the companies that manufacture and sell products. Few countries have pure systems of private ownership or pure systems of public ownership. Most countries tend toward one extreme or the other, but usually a mix of public and private ownership exists.

Natural Resources Another important aspect of the economic environment in different countries is the availability of natural resources. A very broad range of resources are available in different countries. Some countries, like Japan, have few resources of their own. Japan is thus forced to import all of the oil, iron ore, and other natural resources it needs to manufacture products for its domestic and overseas markets. The United States, in contrast, has enormous natural resources and is a major producer of oil, natural gas, coal, iron ore, copper, uranium, and other metals and materials that are vital to the development of a modern economy.

One natural resource that is particularly important in the modern global economy is oil. As we noted earlier, a small set of countries in the Middle East, including Saudi Arabia, Iraq, Iran, and Kuwait, controls a very large percentage of the world's total known reserves of crude oil. Access to this single natural resource has given these oil-producing countries enormous clout in the international economy. One of the more controversial global issues involving natural resources today is the South American rain forest. Developers and farmers in Brazil, Peru, and other countries are clearing vast areas of rain forest, arguing that it is their land and they

can do what they want with it. Many environmentalists, however, fear that deforestation is wiping out entire species of animals and may so alter the environment that it will affect weather patterns around the world.[27]

Infrastructure Yet another important aspect of the economic environment of relevance to international management is infrastructure. A country's **infrastructure** is composed of its schools, hospitals, power plants, railroads, highways, ports, communication systems, air fields, commercial distribution systems, and so forth. The United States has a highly developed infrastructure. For example, its educational system is modern, roads and bridges are well developed, and most people have access to medical care. Overall, the United States has a relatively complete infrastructure sufficient to support most forms of economic development and activity.

infrastructure The schools, hospitals, power plants, railroads, highways, ports, communication systems, air fields, and commercial distribution systems of a country

Some countries, on the other hand, lack a well-developed infrastructure. Some countries do not have enough electrical generating capacity to meet demand. Such countries—Kenya, for example—often schedule periods of time during which power is turned off. These planned power failures reduce power demands but can be an enormous inconvenience to business. In the extreme, when a country's infrastructure is greatly underdeveloped, firms interested in beginning business may have to build an entire township, including housing, schools, hospitals, and perhaps even recreation facilities, to attract a sufficient overseas workforce.

The Political/Legal Environment

A second environmental challenge facing the international manager is the political/legal environment in which he or she will do business. *Today's Management Issues* describes how the political/legal environment affects immigration policies. Four other especially important aspects of the political/legal environment of international management are government stability, incentives for multinational trade, controls on international trade, and the influence of economic communities on international trade.

Government Stability Stability can be viewed in two ways—as the ability of a given government to stay in power against other opposing factions in the country and as the permanence of government policies toward business. A country that is stable in both respects is preferable because managers have a higher probability of successfully predicting how government will affect their business. Civil war in countries such as Lebanon has made it virtually impossible for international managers to predict what government policies are likely to be and whether the government will be able to guarantee the safety of international workers. Consequently, international firms have been very reluctant to invest in Lebanon.



Government stability is of keen interest to managers looking for international opportunities. No business wants to set up shop in a foreign market only to see its investment disappear in the face of government nationalization or civil unrest. Continued clashes in the Middle East, for example, have made many managers wary of making new investments or seeking to expand their operations in that troubled part of the world.

TODAY'S MANAGEMENT ISSUES

CHANGING POLICIES ON IMMIGRATION

During the heyday of the Industrial Revolution, immigration helped the United States build its infrastructure, laying a solid foundation for future economic growth. Over the years, however, government policy on immigration changed, allowing fewer immigrants to enter the United States. Now U.S. companies eager to tap the global labor pool are clamoring for government changes that will ease immigration restrictions.

In a low-unemployment economy, both low-skilled and high-skilled workers are in great demand. All kinds of companies are turning to immigrants to keep their operations humming. Service businesses such as hotels and restaurants need a constant stream of job applicants to keep up with the high turnover in employees. High-tech companies are also suffering a labor shortage. The Information Technology Association of America estimates that more than eight hundred thousand high-tech job openings will remain unfilled if immigration laws are not changed. This shortfall is hurting businesses that need to hire more employees if they want to expand.

The seven hundred thousand immigrants legally admitted to the United States every year are helping to ease the labor shortage and keep the economy moving ahead. Coming from Mexico, India, China, the Philippines, Vietnam, Canada, and many other countries, these immigrants have a range of educational and work backgrounds. In addition, illegal immigration brings as many as six hundred thousand people into the United States every year.

An increase in the number of immigrants is fundamental to us keeping a competitive position in the New Economy.

*—Jack Mollen, senior vice president of human resources, EMC Corporation**

Although some legislators and labor leaders are concerned about how many immigrants the country can absorb, many managers and company owners believe that the U.S. government must significantly increase the number of immigrants who are granted permanent residency status. Otherwise, U.S. businesses may not have the personnel power to keep growing and competing effectively in the global economy.

Reference: Wendy Zellner, "Keeping the Hive Humming," *Business Week*, April 24, 2000, pp. 50–52 (*quote on p. 51).

nationalized Taken over by the government

In many countries—the United States, Great Britain, and Japan, for example—changes in government occur with very little disruption. In other countries—India, Argentina, and Greece, for example—changes are likely to be somewhat chaotic. Even if a country's government remains stable, the risk remains that the policies adopted by that government might change. In some countries foreign businesses may be **nationalized** (taken over by the government) with little or no warning. The government of Peru once nationalized Perulac, a domestic milk producer owned by Nestlé, because of a local milk shortage.

Incentives for International Trade Another facet of the political environment is incentives to attract foreign business. For example, the state of Alabama offered Mercedes-Benz huge tax breaks and other incentives to entice the German firm to select a location in that state for a new factory. In like fashion, as noted earlier, the French government sold land to The Walt Disney Company far below its market

value and agreed to build a connecting freeway in exchange for the company's agreement to build its European theme park outside Paris.

Such incentives can take a variety of forms. Some of the most common include reduced interest rates on loans, construction subsidies, and tax incentives. Less developed countries tend to offer different packages of incentives. In addition to lucrative tax breaks, for example, they can also attract investors with duty-fee entry of raw materials and equipment, market protection through limitations on other importers, and the right to take profits out of the country. They may also have to correct deficiencies in their infrastructures, as noted above, to satisfy the requirements of foreign firms.

Controls on International Trade A third element of the political environment that managers need to consider is the extent to which there are controls on international trade. In some instances, the government of a country may decide that foreign competition is hurting domestic trade. To protect domestic business, such governments may enact barriers to international trade. These barriers include tariffs, quotas, export restraint agreements, and "buy national" laws.

A **tariff** is a tax collected on goods shipped across national boundaries. Tariffs can be collected by the exporting country, countries through which goods pass, and the importing country. Import tariffs, which are the most common, can be levied to protect domestic companies by increasing the cost of foreign goods. Japan charges U.S. tobacco producers a tariff on cigarettes imported into Japan as a way to keep their prices higher than the prices charged by domestic firms. Tariffs can also be levied, usually by less developed countries, to raise money for the government.

tariff A tax collected on goods shipped across national boundaries

Quotas are the most common form of trade restriction. A **quota** is a limit on the number or value of goods that can be traded. The quota amount is typically designed to ensure that domestic competitors will be able to maintain a certain market share. Honda is allowed to import 425,000 autos each year into the United States. This quota is one reason Honda opened manufacturing facilities here. The quota applies to cars imported into the United States, but the company can produce as many other cars within our borders as it wants because they are not considered imports. **Export restraint agreements** are designed to convince other governments to limit voluntarily the volume or value of goods exported to a particular country. They are, in effect, export quotas. Japanese steel producers voluntarily limit the amount of steel they send to the United States each year.

quota A limit on the number or value of goods that can be traded

export restraint agreements Accords reached by governments in which countries voluntarily limit the volume or value of goods they export and import from one another

"Buy national" legislation gives preference to domestic producers through content or price restrictions. Several countries have this type of legislation. Brazil requires that Brazilian companies purchase only Brazilian-made computers. The United States requires that the Department of Defense purchase only military uniforms manufactured in the United States, even though the price of foreign uniforms would be half as much. Mexico requires that 50 percent of the parts of cars sold in Mexico be manufactured in Mexico.

Economic Communities Just as government policies can either increase or decrease the political risk facing international managers, trade relations between

countries can either help or hinder international business. Relations dictated by quotas, tariffs, and so forth, can hurt international trade. There is currently a strong movement around the world to reduce many of these barriers. This movement takes its most obvious form in international economic communities.

economic community A set of countries that agree to reduce or eliminate trade barriers markedly among its member nations (a formalized market system)

An international **economic community** is a set of countries that agree to reduce or eliminate trade barriers markedly among its member nations. The first, and in many ways still the most important, of these economic communities is the European Union (EU), discussed earlier. The passage of NAFTA, as also noted earlier, represents perhaps the first step toward the formation of a North American economic community. Other important economic communities include the Latin American Integration Association (Bolivia, Brazil, Colombia, Chile, Argentina, and other South American countries) and the Caribbean Common Market (the Bahamas, Belize, Jamaica, Antigua, Barbados, and twelve other countries).

The Cultural Environment

Another environmental challenge for the international manager is the cultural environment and how it affects business. A country's culture includes all the values, symbols, beliefs, and language that guide behavior. *The World of Management* provides an interesting illustration of cultural dynamics at work!

Values, Symbols, Beliefs, and Language Cultural values and beliefs are often unspoken; they may even be taken for granted by those who live in a particular country. Cultural factors do not necessarily cause problems for managers when the cultures of two countries are similar. Difficulties can arise, however, when there is little overlap between the home culture of a manager and the culture of the country in which business is to be conducted. For example, most U.S. managers find the culture and traditions of England familiar. The people of both countries speak the same language and share strong historical roots, and there is a history of strong commerce between the two countries. When U.S. managers begin operations in Japan or the People's Republic of China, however, most of those commonalities disappear.

In Japanese the word *hai* (pronounced "hi") means "yes." In conversation, however, this word is used much like people in the United States use "uh-huh"; it moves a conversation along or shows the person you are talking to that you are paying attention. So when does "hai" mean "yes" and when does it mean "uh-huh"? This question turns out to be relatively difficult to answer. If a U.S. manager asks a Japanese manager if he agrees to some trade arrangement, the Japanese manager is likely to say "hai"—which may mean "yes, I agree," or "yes, I understand," or "yes, I am listening." Many U.S. managers become frustrated in negotiations with the Japanese because they believe that the Japanese continue to raise issues that have already been settled (the Japanese managers said "yes"). What many of these managers fail to recognize is that "yes" does not always mean "yes" in Japan.

Cultural differences between countries can have a direct impact on business practice. For example, the religion of Islam teaches that people should not make a living by exploiting the misfortune of others and that making interest payments is immoral. This means that in Saudi Arabia there are few businesses that provide auto-wrecking services to tow stalled cars to the garage (because that would be

WORLD OF MANAGEMENT

FRENCH LANGUAGE SPECIALISTS COIN NEW WEB WORDS

As the Internet revolution sweeps the world, the Academie Française in France is fighting to maintain the language by coining uniquely French words and phrases for well-known Internet buzzwords. The World Wide Web, which hip Parisian netizens call "le Web," is officially known as *la toile*, which translates into "the spider web." Similarly, the academy's official phrase for e-mail is *message électronique*.

Subtle differences, perhaps, but the writers who serve on the academy are determined to keep foreign words out of the language by providing French substitutes for use in government documents and schools. Ordinary citizens are not required to use the terms offered by the academy, although officials hope they will adopt suggested French phrases such as *causette* instead of chattering on about on-line chat sessions.

Sometimes the drive to use French words makes for unusual designations. The academy calls hackers—programmers who break into computer systems and web sites—*les fouineurs*, meaning "the nosy people." Other substitutes are fairly close, such as *localisateur universal*, which translates into "universal locator," the official French term for URL (universal resource locator), a web address.

Since the Academie Française was founded by Cardinal Richelieu in 1635, it has made considerable headway in persuading the French to adopt its substitutes for non-French words. Nobody talks about a computer in France; instead, they talk about an *ordinateur*, a word the academy proposed. On the other hand, many Internet entrepreneurs resist the official French phrases. They prefer to say "le start-up" instead of *la jeune pousse*, which means "young sapling." Although the popular press continues to mix French and web terms with headlines such as "Surfez le Web," the academy is pressing on with its mission to keep non-French buzzwords out of the language.

***In a few years, no one in France will use* le Web.**

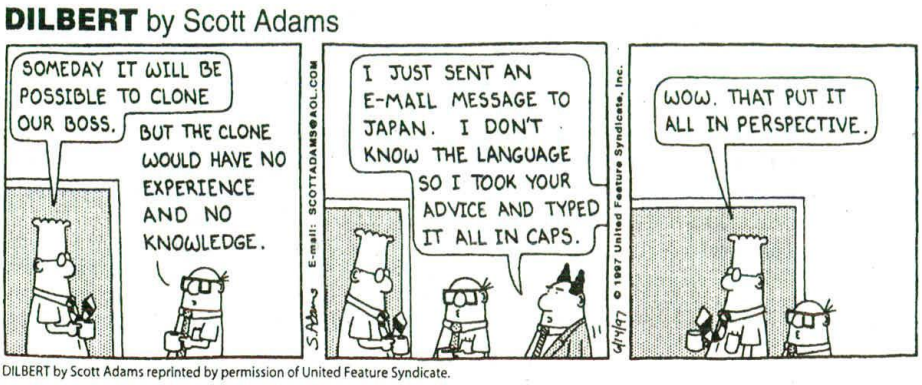
—Serge Petillot-Niemetz, director of external affairs, Academie Française*

Reference: Vivienne Walt, "E-Words Are Tough for France to Swallow," *USA Today*, May 1, 2000, pp. 1A, 2A (*quote on p. 2A).

capitalizing on misfortune), and in the Sudan banks cannot pay or charge interest. Given these cultural and religious constraints, those two businesses—automobile towing and banking—don't seem to hold great promise for international managers in those particular countries!

Some cultural differences between countries can be even more subtle and yet have a major impact on business activities. For example, in the United States most managers clearly agree about the value of time. Most U.S. managers schedule their activities very tightly and then adhere to their schedules. Other cultures don't put such a premium on time. In the Middle East, managers do not like to set appointments, and they rarely keep appointments set too far into the future. U.S. managers interacting with managers from the Middle East might misinterpret the late arrival of a potential business partner as a negotiation ploy or an insult, when it is rather a simple reflection of different views of time and its value.[28]

Language itself can be an important factor. Beyond the obvious and clear barriers posed by people who speak different languages, subtle differences in meaning



DILBERT by Scott Adams reprinted by permission of United Feature Syndicate.

Dealing with people from other cultures can be a rewarding experience, and it can also be a challenge. Language barriers, for example, pose major obstacles. Interestingly, some people believe that if they talk slower or louder, people who do not speak their language will somehow have a better understanding of what is being said. As illustrated in this cartoon, this flawed logic can even extend to electronic communication!

can also play a major role. For example, Imperial Oil of Canada markets gasoline under the brand name Esso. When the firm tried to sell its gasoline in Japan, it learned that Esso means "stalled car" in Japanese. The Chevrolet Nova was not selling well in Latin America, and General Motors executives couldn't understand why until it was brought to their attention that, in Spanish, *no va* means "it doesn't go." The color green is used extensively in Moslem countries, but it signifies death in some other countries. The color associated with femininity in the United States is pink, but in many other countries yellow is the most feminine color.

Individual Behaviors Across Cultures From another perspective, there also appear to be clear differences in individual behaviors and attitudes across different cultures. For example, Geert Hofstede, a Dutch researcher, studied 116,000 people working in dozens of different countries and found several interesting differences.[29] Hofstede's initial work identified four important dimensions along which people seem to differ across cultures. More recently, he has added a fifth dimension. These dimensions are illustrated in Figure 5.4.

social orientation A person's beliefs about the relative importance of the individual versus groups to which that person belongs

The first dimension identified by Hofstede is social orientation.[30] **Social orientation** is a person's beliefs about the relative importance of the individual versus groups to which that person belongs. The two extremes of social orientation are individualism and collectivism. *Individualism* is the cultural belief that the person comes first. Hofstede's research suggested that people in the United States, the United Kingdom, Australia, Canada, New Zealand, and the Netherlands tend to be relatively individualistic. *Collectivism*, the opposite of individualism, is the belief that the group comes first. Hofstede found that people from Mexico, Greece, Hong Kong, Taiwan, Peru, Singapore, Colombia, and Pakistan tend to be relatively collectivistic in their values. In countries with higher levels of individualism, many workers may prefer reward systems that link pay with the performance of individual employees. In a more collectivistic culture, such a reward system may, in fact, be counterproductive.

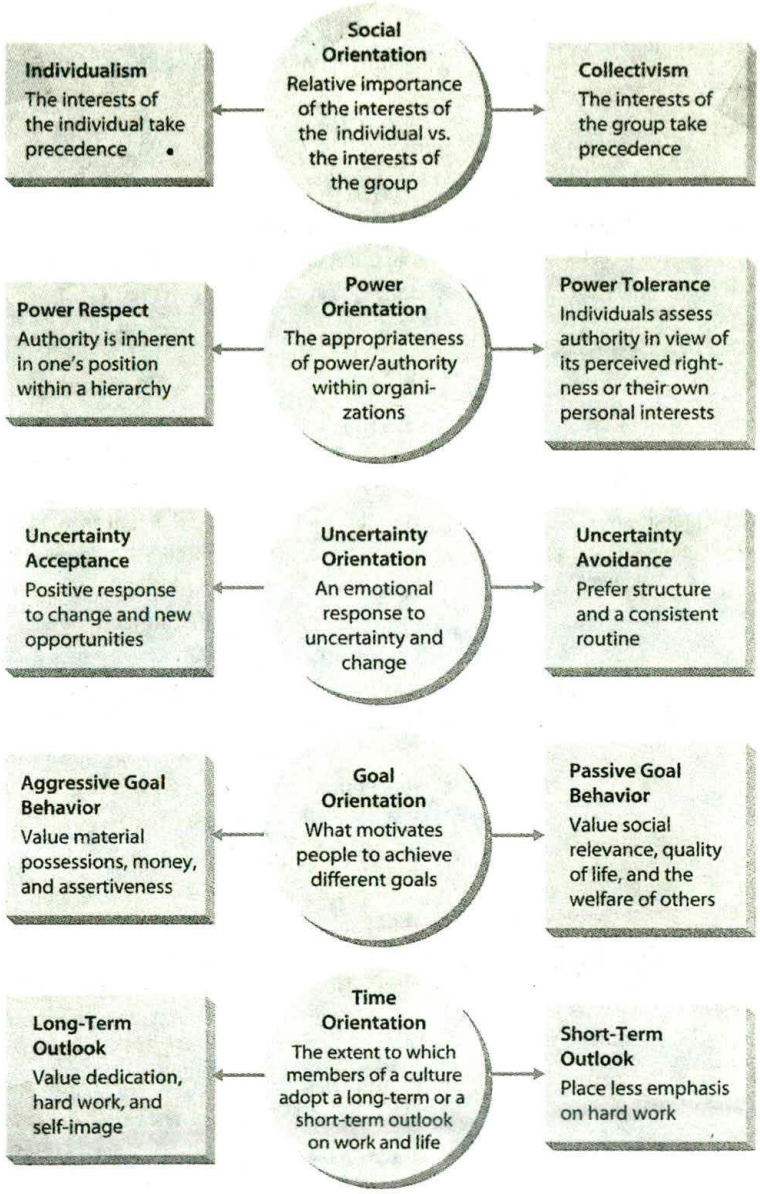
power orientation The beliefs that people in a culture hold about the appropriateness of power and authority differences in hierarchies such as business organizations

A second important dimension is **power orientation**, the beliefs that people in a culture hold about the appropriateness of power and authority differences in hierarchies such as business organizations. Some cultures are characterized by *power respect*. This means that people tend to accept the power and authority of

Figure 5.4

Individual Differences Across Cultures

Hofstede identified five fundamental differences that can be used to characterize people in different cultures. These dimensions are social orientation, power orientation, uncertainty orientation, goal orientation, and time orientation. Different levels of each dimension affect the perceptions, attitudes, values, motivation, and behaviors of people in different cultures.



Source: R. W. Griffin/M. Pustay, *International Business* © 1996. Reprinted by permission of Pearson Education, Inc. Upper Saddle River, NJ 07458.

their superiors simply on the basis of their position in the hierarchy and to respect their right to control that power. Hofstede found that people in France, Spain, Mexico, Japan, Brazil, Indonesia, and Singapore were relatively power accepting. In contrast, people in cultures with a *power tolerance* orientation attach much less significance to a person's position in the hierarchy. These individuals are more willing to question a decision or mandate from someone at a higher level or perhaps even refuse to accept it. Hofstede's work suggested that people in the United States, Israel, Austria, Denmark, Ireland, Norway, Germany, and New Zealand tended to be more power tolerant.

uncertainty orientation The feeling individuals have regarding uncertain and ambiguous situations

The third basic dimension of individual differences studied by Hofstede was uncertainty orientation. **Uncertainty orientation** is the feeling individuals have regarding uncertain and ambiguous situations. People in cultures with *uncertainty acceptance* are stimulated by change and thrive on new opportunities. Hofstede suggested that many people from the United States, Denmark, Sweden, Canada, Singapore, Hong Kong, and Australia are among those in this category. In contrast, people with *uncertainty avoidance* tendencies dislike and will avoid ambiguity whenever possible. Hofstede found that many people in Israel, Austria, Japan, Italy, Colombia, France, Peru, and Germany tended to avoid uncertainty whenever possible.

goal orientation The manner in which people are motivated to work toward different kinds of goals

The fourth dimension of cultural values measured by Hofstede is goal orientation. In this context, **goal orientation** is the manner in which people are motivated to work toward different kinds of goals. One extreme on the goal orientation continuum is *aggressive goal behavior*. People who exhibit aggressive goal behaviors tend to place a high premium on material possessions, money, and assertiveness. On the other hand, people who adopt *passive goal behavior* place a higher value on social relationships, quality of life, and concern for others. According to Hofstede's research, many people in Japan tend to exhibit relatively aggressive goal behaviors, whereas many people in Germany, Mexico, Italy, and the United States reflect moderately aggressive goal behaviors. People from the Netherlands and the Scandinavian countries of Norway, Sweden, Denmark, and Finland all tend to exhibit relatively passive goal behaviors.

time orientation The extent to which members of a culture adopt a long-term versus a short-term outlook on work, life, and other elements of society

A recently identified fifth dimension is called Time orientation.[31] **Time orientation** is the extent to which members of a culture adopt a long-term versus a short-term outlook on work, life, and other elements of society. Some cultures, such as Japan, Hong Kong, Taiwan, and South Korea, have a long-term orientation that values dedication, hard work, perseverance, and the importance of self-image. Other cultures, like Pakistan and West Africa, are more likely to have a short-term orientation. These cultures, in contrast, put considerably less emphasis on work, perseverance, and similar values. Hofstede's work suggests that people in the United States and Germany tend to have an intermediate time orientation.

MANAGEMENT IMPLICATIONS Managers need to understand the basic environmental challenges that confront them as they do business in international settings. These basic challenges involve political/legal differences in different countries, differences in the economic environments of different countries, and variations in the cultural environment. Each difference adds to the complexities that international managers must address.

■ Competing in a Global Economy

Competing in a global economy is both a major challenge and an opportunity for businesses today. The nature of these challenges depends on a variety of factors, including the size of the organization. In addition, international management also has implications for the basic functions of planning, organizing, leading, and controlling.

Globalization and Organization Size

Although organizations of any size may compete in international markets, there are some basic differences in the challenges and opportunities faced by MNCs, medium-size organizations, and small organizations.

Multinational Corporations The large MNCs have long since made the choice to compete in a global marketplace. In general, these firms take a global perspective. They transfer capital, technology, human resources, inventory, and information from one market to another. They actively seek new expansion opportunities wherever feasible. MNCs tend to allow local managers a great deal of discretion in addressing local and regional issues. At the same time, each operation is ultimately accountable to a central authority. Managers at this central authority (headquarters, a central office, etc.) are responsible for setting the overall strategic direction for the firm, making major policy decisions, and so forth. MNCs need senior managers who understand the global economy and who are comfortable dealing with executives and government officials from a variety of cultures. Table 5.2 lists the world's largest multinational enterprises.

Medium-Size Organizations Many medium-size businesses remain primarily domestic organizations. But they still may buy and sell products made abroad and compete with businesses from other countries in their own domestic market. Increasingly, however, medium-size organizations are expanding into foreign markets as well. For example, Gold's Gym, a U.S. fitness chain, has opened a very successful facility in Moscow.[32] In contrast to MNCs, medium-size organizations doing business abroad are much more selective about the markets they enter. They also depend more on a few international specialists to help them manage their foreign operations.

Small Organizations More and more small organizations are also finding that they can benefit from the global economy. Some, for example, serve as local suppliers for MNCs. A dairy farmer who sells milk to Carnation Company, for example, is actually transacting business with Nestlé. Local parts suppliers have also been successfully selling products to the Toyota and Honda plants in the United States. Beyond serving as local suppliers, some small businesses also buy and sell products and services abroad. For example, the Collin Street Bakery, based in Corsicana, Texas, ships fruitcakes around the world. In 1999, the firm shipped over 150,000 pounds of fruitcake to Japan. Most small businesses rely on simple

Table 5.2

The World's Largest MNCs: Industrial Corporations

Rank 1999	Company	Country	Revenues $ million	Profits $ million	Assets $ million	Employees Number
1	General Motors	U.S.	176,558.0	6,002.0	273,921.0	388,000
2	Wal-Mart Stores	U.S.	166,809.0	5,377.0	70,245.0	1,140,000
3	Exxon Mobil	U.S.	163,881.0	7,910.0	144,521.0	106,000
4	Ford Motor	U.S.	162,558.0	7,237.0	276,229.0	364,550
5	DaimlerChrysler	Germany	159,985.7	6,129.1	175,068.8	466,938
6	Mitsui	Japan	118,555.2	320.5	62,360.0	38,454
7	Mitsubishi	Japan	117,765.6	233.7	78,949.2	42,050
8	Toyota Motor	Japan	115,670.9	3,653.4	160,571.6	214,631
9	General Electric	U.S.	111,630.0	10,717.0	405,200.0	340,000
10	Itochu	Japan	109,068.9	(792.8)	59,153.9	5,306
11	Royal Dutch/Shell Group	Brit./Neth.	105,366.0	8,584.0	113,883.0	96,000
12	Sumitomo	Japan	95,701.6	314.9	47,819.8	33,057
13	Nippon Telegraph & Telephone	Japan	93,591.7	(609.0)	179,512.2	223,954
14	Marubeni	Japan	91,807.4	18.5	54,446.9	32,000
15	Axa	France	87,645.7	2,155.8	508,647.3	92,008
16	International Business Machines	U.S.	87,548.0	7,712.0	87,495.0	307,401
17	BP Amoco	Britain	83,566.0	5,008.0	89,561.0	80,400
18	Citigroup	U.S.	82,005.0	9,867.0	716,900.0	176,900
19	Volkswagen	Germany	80,072.7	874.7	67,275.9	306,275
20	Nippon Life Insurance	Japan	78,515.1	3,405.4	423,281.5	71,434
21	Siemens	Germany	75,337.0	1,773.7	65,488.8	443,000
22	Allianz	Germany	74,178.2	2,382.1	383,686.9	113,584
23	Hitachi	Japan	71,858.5	152.0	95,911.7	398,348
24	Matsushita Electric Industrial	Japan	65,555.6	895.5	74,946.3	290,448
25	Nissho Iwai	Japan	65,393.2	91.8	39,762.9	18,446

Source: Adapted from *Fortune*, July 24, 2000; p. F-1. Used with permission from Fortune, Inc.

importing or exporting operations (or both) for their international sales. Thus, only a few specialized management positions are needed. Collin Street Bakery, for example, has one local manager who handles international activities. Mail-order activities within each country are subcontracted to local firms in each market.

Management Challenges in a Global Economy

The management functions that constitute the framework for this book—planning, organizing, leading, and controlling—are just as relevant to international managers as to domestic managers. International managers need to have a clear view of where they want their firm to be in the future, they have to organize to implement their plans, they have to motivate those who work for them, and they have to develop appropriate control mechanisms.[33]



Most large businesses have already faced the challenges of entering major foreign markets and now focus their energies on competing with other companies in those markets. Take Vodafone, for example, the world's largest cell phone operator. Vodafone has over 65 million subscribers in 25 countries, including the Netherlands. But as successful as the firm has become, it must still compete with such other global telecommunications giants as Sprint PCS, NTT, and AT&T.

Planning in a Global Economy To plan effectively in a global economy, managers must have a broad-based understanding of both environmental issues and competitive issues. They need to understand local market conditions and technological factors that will affect their operations. At the corporate level, executives need a great deal of information to function effectively. What markets are growing? What markets are shrinking? What are our domestic and foreign competitors doing in each market? They must also make a variety of strategic decisions about their organization. For example, if a firm wishes to enter the market in France, should it buy a local firm there, build a plant, or seek a strategic alliance? Critical issues include understanding environmental circumstances, the role of goals and planning in a global organization, and how decision making affects the global organization. We note special implications for global managers as we discuss planning in Chapters 7 through 10.

Organizing in a Global Economy Managers in international businesses must also attend to various organizing issues. For example, General Electric has operations scattered around the globe. The firm has made the decision to give local managers a great deal of responsibility for how they run their business. In contrast, many Japanese firms give managers of their foreign operations relatively little responsibility. As a result, those managers must frequently travel back to Japan to present problems or get decisions approved. Managers in an international business must address the basic issues of organization structure and design, managing change, and dealing with human resources. We address the special issues of organizing the international organization in Chapters 11 through 14.

Leading in a Global Economy We noted earlier some of the cultural factors that affect international organizations. Individual managers must be prepared to deal with these and other factors as they interact with people from different cultural backgrounds. Supervising a group of five managers, each of whom is from a different state in the United States, is likely to be much simpler than supervising a

group of five managers, each of whom is from a different culture. Managers must understand how cultural factors affect individuals, how motivational processes vary across cultures, the role of leadership in different cultures, how communication varies across cultures, and the nature of interpersonal and group processes in different cultures. In Chapters 15 through 19 we note special implications for international managers that relate to leading and interacting with others.

Controlling in a Global Economy Finally, managers in international organizations must also be concerned with control. Distances, time zone differences, and cultural factors all play a role in control. For example, in some cultures close supervision is seen as being appropriate, and in other cultures it is not. Likewise, executives in the United States and Japan may find it difficult to communicate vital information to one another because of the time zone differences. Basic control issues for the international manager revolve around operations management, productivity, quality, technology, and information systems. These issues are integrated throughout our discussion of control in Chapters 20 through 22.

MANAGEMENT IMPLICATIONS The international challenges and opportunities facing managers in large multinational corporations, medium-size businesses, and small companies are subtly different. Similarly, the basic management functions of planning, organizing, leading, and controlling are also affected by the degree of internationalization of the organization. Thus, managers need to appreciate both the size of their organization and the relevant functional activities as they carry out their work in a global environment.

Summary of Key Points

International business has become one of the most important features of the world's economy. Learning to operate in a global economy is an important challenge facing many managers today. Businesses can be primarily domestic, international, multinational, or global in scope. Managers need to understand both the process of internationalization as well as how to manage within a given level of international activity.

To compete in the global economy, managers must understand its structure. Mature market economies and systems dominate the global economy today. North America, the European Union, and Pacific Asia are especially important. High potential/high growth economies in eastern Europe, Latin America, the People's Republic of China, India, and Vietnam are increasingly important to managers. The oil-exporting economies in the Middle East are also important.

Many of the challenges of management in a global context are unique issues associated with the international environmental context. These challenges reflect the economic, political/legal, and cultural environments of international management.

Basic issues of competing in a global economy vary according to whether the organization is an MNC, a medium-size organization, or a small organization. In addition, the basic managerial functions of planning, organizing, leading, and controlling must all be addressed in international organizations.

Discussion Questions

Questions for Review

1. Describe the four basic levels of international business activity. Do you think any organization will achieve the fourth level? Why or why not?
2. Summarize the basic structure of the global economy. What are the major changes today occurring within that structure?
3. Briefly note some of the basic environmental challenges of international management.
4. What are the basic cultural differences identified by Hofstede?

Questions for Analysis

5. An organization seeking to expand its international operations must monitor several different environments. Which aspect of each environment is likely to have the greatest impact on decisions involved in such a strategic move? Why?
6. What industries do you think will have the greatest impact on international business? Are there any industries that might not be affected by the trend toward international business? If so, what are they? If there are none, why are there none?
7. You are the CEO of an up-and-coming toy company and have plans to go international soon. What steps would you take to carry out that strategy? What areas would you stress in your decision-making process? How would you organize your company?

Questions for Application

8. Identify a local company that does business abroad. Interview an executive in that company. Why did the company go international? What major obstacles did it face? How successful has that decision been? Share your findings with the class.
9. Go to the library and find some information about the European Union's continued move toward a relaxation of trade barriers. What will be the effect of that relaxation? What will be some of the difficulties? Do you think that it is a good idea? Why or why not?
10. Many organizations fail to allow for cultural and language differences when they do business with other countries. For example, Pepsi was introduced into Asia with the slogan "Come alive with Pepsi." The slogan, however, was translated as "Bring your ancestors back from the dead with Pepsi." Go to the library and locate mistakes made by other companies entering foreign markets. What did they do wrong? How could they have prevented their mistakes?

BUILDING EFFECTIVE *interpersonal* SKILLS

Exercise Overview

Interpersonal skills refer to the manager's ability to communicate with, understand, and motivate individuals and groups. Managers in international organizations must understand how culture and other factors affect how they communicate with other people in different parts of the organization. This exercise will enable you to learn more about your current levels of cultural understanding and to develop insights into areas where you may need additional cultural awareness.

Exercise Task

The task that follows consists of ten statements. Indicate your level of agreement with each statement as described in the instructions below.

Instructions: You will agree with some of the following statements and disagree with others. In some cases, you may find it difficult to make

a decision, but you should force a choice. Record your answers next to each statement according to the following scale:

4 Strongly agree **2** Somewhat disagree
3 Somewhat agree **1** Strongly disagree

____ 1. Some areas of Switzerland are very much like Italy.
____ 2. Although aspects of behavior such as motivation and attitudes within organizational settings remain quite diverse across cultures, organizations themselves appear to be increasingly similar in terms of design and technology.
____ 3. Spain, France, Japan, Singapore, Mexico, Brazil, and Indonesia have cultures with a strong orientation toward authority.
____ 4. Japan and Austria define male-female roles more rigidly and value qualities like forcefulness and achievement more than Norway, Sweden, Denmark, and Finland.
____ 5. Some areas of Switzerland are very much like France.
____ 6. Australia, Great Britain, the Netherlands, Canada, and New Zealand have cultures that view people first as individuals and place a priority on their own interests and values, whereas Colombia, Pakistan, Taiwan, Peru, Singapore, Mexico, Greece, and Hong Kong have cultures in which the good of the group or society is considered the priority.
____ 7. The United States, Israel, Austria, Denmark, Ireland, Norway, and New Zealand have cultures with a low orientation toward authority.
____ 8. The same manager may behave differently in different cultural settings.
____ 9. Denmark, Canada, Norway, Singapore, Hong Kong, and Australia have cultures in which employees tolerate a high degree of uncertainty, but such levels of uncertainty are not well tolerated in Israel, Austria, Japan, Italy, Argentina, Peru, France, and Belgium.
____ 10. Some areas of Switzerland are very much like Germany.

BUILDING EFFECTIVE *technical* SKILLS

Exercise Overview

Technical skills are the skills necessary to accomplish or understand the specific kind of work being done in an organization. Some managers in international businesses must pay attention to fluctuations in currency exchange rates in the countries where the firm does business. These fluctuations affect the financial impact of many different kinds of decisions. This exercise will help you better understand the impact of exchange rates.

Exercise Background

The exchange rates of most major currencies relative to the others are published regularly in newspapers such as the *Wall Street Journal, USA Today,* and the *New York Times.* Locate a recent edition of such a newspaper and determine the exchange rate on that day for U.S. dollars relative to British pounds. (Note that the pound is one of the few currencies that has a value greater than the dollar.)

Next, assume that six months has passed from the date of the exchange rate you have located. Major economic shifts have caused the exchange rate to fluctuate to a level such that one pound is worth one dollar; that is, the exchange rate six months hence will be 1 to 1.

Exercise Task

Using the information gathered above, do the following:

1. Determine the impact of this exchange rate shift on a U.S. tourist visiting England.

2. Determine the impact of the shift on an English tourist visiting the United States.
3. Determine the impact of this shift on a U.S. business that exports its products to England, where they compete with locally made products.
4. Determine the impact of this shift on an English business that exports its products to the United States, where they compete with locally made products.
5. Determine the impact of this shift on a U.S. business that buys raw materials in England, imports them into the United States, and makes products for shipment to Japan.

BUILDING EFFECTIVE *communication* SKILLS

Exercise Overview

Communication skills refer to the manager's ability both to convey ideas and information effectively to others and to receive ideas and information effectively from others. International managers have additional communication complexities due to differences in language, time zones, and so forth. This exercise will enable you to enhance your communication skills by better understanding the impact of different time zones.

Exercise Background

Assume that you are a manager in a large multinational firm. Your office is located in San Francisco. You need to arrange a conference call with several other managers to discuss an upcoming strategic change by your firm. The other managers are located in New York, London, Rome, Moscow, Tokyo, Singapore, and Sydney.

Exercise Task

Using the information above, do the following:

1. Determine the time-zone differences in each of these cities.
2. Assuming that people in each city have a "normal" workday of 8 A.M. to 5 P.M., determine the "optimal" time for your conference call; that is, what time can you place the call and thus minimize the number of people who are inconvenienced?
3. Now assume that you need to visit each office in person. You need to spend one full day in each city. Using the Internet, review airline schedules, account for differences in time zones, and develop an itinerary.

CHAPTER CLOSING CASE

WAL-MART COURTS EUROPEAN SHOPPERS

With a beachhead of stores spread across England and Germany, Wal-Mart is bringing American-style retailing to European shoppers. Already the world's largest retail chain, with $165 billion in global sales, Wal-Mart entered the United Kingdom by buying the Asda chain, which operates more than 230 stores across the country. Wal-Mart wants its non–U.S. sales to bring in a larger chunk of its overall sales revenue, and Europe is an attractive region for a retailer that knows its business.

The Arkansas-based Wal-Mart began shaking up British retailing by cutting prices, highlighting selection, and promoting friendly service. Because British retailers are accustomed to higher profit margins, the Wal-Mart

formula of low markup pricing has put pressure on rival chains such as Tesco and given smaller stores even bigger headaches. Wal-Mart has touched off price wars in food products and other categories, sending competitors scrambling to meet or beat its price tags. Through Asda@Home, the chain's first European Internet shopping site, Wal-Mart is expanding its brand of low-price retailing to reach shoppers in other countries.

In Germany, however, giant discounters are commonplace, so Wal-Mart is basing its competitive strategy there on service and selection. Many German stores have a much narrower merchandise selection than Wal-Mart. Small wonder that shoppers gawk at the huge quantities of food items, from fresh fruits and vegetables to specialty meats and cheeses in Wal-Mart outlets in Dortmund and other cities. As in the United States, the Wal-Mart stores in Germany also carry all sorts of toys, clothing, appliances, and assorted products for household and personal use. Customer service is as much a draw as selection, because service in German stores is much less friendly and personalized. The twin weaknesses of poor selection and poor service leave German retailing open to aggressive competitive attacks from Internet retailers as well as from Wal-Mart.

To enter the German market, Wal-Mart bought ninety-five stores from two struggling local chains and hung an American flag outside each to herald the change in management. Then it began a massive renovation project to enlarge and modernize each outlet. Renovations have proceeded slowly, however. Within three years of the acquisition, fewer than one-third of the stores had been renovated. The renovated stores are definitely more spacious and inviting, with wider aisles, brighter lights, and more accessible shelving loaded with merchandise—all of which is helping to boost sales. Few German stores allow credit payments, so Wal-Mart is successfully attracting shoppers by accepting major credit cards. German shoppers are also pleased at not having to bag their own purchases or pay for the plastic bags at Wal-Mart, amenities that U.S. shoppers take for granted.

Just as visible as the physical changes are the managerial changes. The managers in each Wal-Mart store hold a daily staff meeting to extol new products and motivate store personnel. For example, the comanager of the store in Dortmund, Germany, dressed in a sailor suit when announcing the introduction of a new line of nautical gifts. Knowing that customer service is spotlighted in the chain's television commercials, managers in the German stores encourage good service by praising good performance and keeping communication lines open. Still, even the best service will not make up for cramped stores, so Wal-Mart will have to speed up its renovations if it wants German shoppers to come back and buy—again and again.

Case Questions

1. On which of Hofstede's five dimensions are Wal-Mart's American roots and German operations fairly similar? How do these similarities affect the company's ability to manage its German stores?
2. Why would Wal-Mart choose to operate in Germany and Great Britain on the basis of direct investment rather than through a joint venture or strategic alliance?
3. If you were a retailer in Great Britain or Germany, what would you do to blunt Wal-Mart's competitive advantages?

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CHAPTER 6

The Cultural and Multicultural Environment

OPENING INCIDENT

Old Navy is clearly one of the funkiest retailers around. Where else, for example, can young consumers buy today's hottest fashions stacked in old freezers, surrounded by old advertising signs, and in the shadows of a vintage Chevrolet at bargain-basement prices? Indeed, Old Navy is growing at the rate of over 100 stores per year and is the current favorite among the budget-minded younger set. And observers give much of the credit for the firm's success to its president, Jenny Ming. For her part, Ming brings to the table a keen understanding of the importance of corporate culture and a sense of fashion tastes that are in tune with a diverse population of younger consumers.

For Ming, the starting point in building a successful business is having a strong foundation built on people. Thus, she populates Old Navy stores with high-energy, fashion-conscious people just like the firm's target consumers. She also encourages everyone to lead a well-balanced life; she herself, for example, doesn't work on weekends and she doesn't expect her staff to, either. Ming also puts a lot of emphasis on teamwork in Old Navy stores and is always on the alert for new ways to get people to work together as a team rather than individually. In short, she wants Old Navy to become *the* place to work among those interested in a retailing job.

Ming also works hard to stay ahead of the game in terms of fashion trends and fads. For example, she was one of the first in the industry to spot the emergence of both baggy cotton cargo pants and fleece pullovers as fashion staples. By relying on her own intuition, she was able to order these and other products in massive quantities before other retailers caught on and then get a head start by establishing a reputation as the first and best place to buy them. Indeed, it seems like Old Navy is the first retailer to pick up on one fashion trend after another.

So, how does Ming do it? She relies on several tactics to learn about and spot emerging fashion trends. For one thing, she watches and talks to her own teen-age daughters and their friends. One daughter, she says, latches on to things just as they are on the verge of becoming a trend, while another picks up on things just as they've peaked. So, Ming might be willing to bet on trends she sees in the first daughter's clothing. But she knows that if it's the other daughter who tries something new that it may be too late.

"One thing I know best is when to maximize something. If I believe in something, I'll push it bigger and harder."

—Jenny Ming, president of Old Navy

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LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- **Describe the nature of organization and social culture.**
- **Discuss the importance and determinants of an organization's culture and how the culture can be managed.**
- **Identify and describe the major trends and dimensions of diversity and multiculturalism in organizations.**
- **Discuss the primary effects of diversity and multiculturalism in organizations.**
- **Describe individual and organizational strategies and approaches to managing diversity and multiculturalism.**
- **Discuss the six characteristics of the fully multicultural organization.**

Ming also travels extensively to keep abreast of trends in other parts of the world. For example, she makes regular trips to London, Paris, and New York to observe firsthand what people are wearing in the street cafés and other student hangouts. In addition, she reads fashion magazines voraciously and contracts with various market-research firms to ensure that she has the very latest information about what's going on. And as a result, while Old Navy stores pull in the hip young consumers Ming sees as the firm's bread-and-butter, they also attract older consumers who want to look fashionable, as well as others who are simply looking for good value.

With an eye on the future, Old Navy and Jenny Ming are currently riding a crest of popularity. Old Navy itself is one division of The Gap, a long-time darling of the retailing trade; and Ming, hand-picked by the CEO of The Gap to lead the charge at Old Navy, is widely recognized as one of the industry's rising stars. For her, of course, the trick will be to stay ahead of the pack. And for Old Navy, the trick will be to maintain its popularity and growth rate while avoiding major mistakes. The culture that Ming has created at the firm and her understanding of diverse fashion tastes may not guarantee continued success, but they certainly give the company a great chance to ride the crest of popularity for a while longer yet.[1]



CHAPTER OUTLINE

- **The Nature of Organization and Social Culture**
- **The Organization's Culture**
  - The Importance of Organization Culture
  - Determinants of Organization Culture
  - Managing Organization Culture
- **Diversity and Multiculturalism in Organizations**
  - Trends in Diversity and Multiculturalism
  - Dimensions of Diversity and Multiculturalism
- **Effects of Diversity and Multiculturalism in Organizations**
  - Multiculturalism and Competitive Advantage
  - Multiculturalism and Conflict
- **Managing Diversity and Multiculturalism in Organizations**
  - Individual Strategies
  - Organizational Approaches
- **Toward the Multicultural Organization**

Like many other organizations in the world today, Old Navy faces a variety of challenges, opportunities, and issues in its quest to grow and become an increasingly vital part of the retailing landscape. One key ingredient to the firm's success is the strong and focused culture that president Jenny Ming has created. Another is her keen understanding of diverse consumer tastes and how those cultural tastes translate into fashion trends and fads.

This chapter is about these two broad forms of culture—organization and social. After establishing the similarities and differences between the two, we discuss organization culture first. We then turn to diversity and multiculturalism, in organizations. We begin by describing trends in diversity and multiculturalism, and identify and discuss several common dimensions of diversity. The effects of diversity and multiculturalism on organizations are then explored. We next address individual strategies and organizational approaches for managing diversity and multiculturalism. Finally, we characterize and describe the fully multicultural organization.

■ The Nature of Organization and Social Culture

At its most general level, *culture* refers to the collection of values, beliefs, behaviors, customs, and attitudes that characterize a community of people. Such a community can range from a small group of individuals to an entire nation. Our interests here start with culture at the organizational level. Thus, since the members of an organization can be viewed as a community, the organization they comprise will have its own unique community. **Organization culture**, therefore, is the set of values, beliefs, behaviors, customs, and attitudes that help the members of the organization understand what it stands for, how it does things, and what it considers important.[2]

organization culture The set of values, beliefs, behaviors, customs, and attitudes that help the members of the organization understand what it stands for, how it does things, and what it considers important.

At a much broader level, culture can also be used to characterize the community of people who comprise an entire society. Some of the basic managerial issues associated with doing business across cultures were introduced and explored in Chapter. 5. But a different set of issues involving social culture also arises within the boundaries of an organization. That is, when the people comprising an organization represent different cultures, their differences in values, beliefs, behaviors, customs, and attitudes pose unique opportunities and challenges for managers. These broad issues are generally referred to as **multiculturalism**.

multiculturalism The broad issues associated with differences in values, beliefs, behaviors, customs, and attitudes held by people in different cultures.

A related area of interest is diversity. **Diversity** exists in a community of people when its members differ from one another along one or more important dimensions. These differences can obviously reflect the multicultural composition of a community. In the business world, however, the term *diversity* per se is more generally used to refer to demographic differences among people within a culture—differences in gender, age, and so forth. Diversity is not an absolute phenomenon, of course, wherein a group or organization is or is not diverse. Instead, diversity can be conceptualized as a continuum. If everyone in the community is exactly

diversity Exists in a group or organization when its members differ from one another along one or more important dimensions such as age, gender, or ethnicity



An organization's culture plays a vital and fundamental role in its successes and failures. Khai Minh Phan is the founder and CEO of Easy PlaNet, an Internet start-up firm that is constructing a new kind of web portal intended to compete with Yahoo! and other existing portals. Mr. Phan is shown here leading a discussion about strategic issues with his managers at his home in California. Even if PlaNet succeeds and grows to become a major corporation with dozens of foreign subsidiaries, each employing thousands of people, its culture will have been largely formed from these early intense and exciting brainstorming sessions.

like everyone else, there is no diversity whatsoever. If everyone is different along every imaginable dimension, total diversity exists. In reality, of course, these extremes are more hypothetical than real. Most settings are characterized by a level of diversity somewhere between these extremes. Therefore, diversity should be thought of in terms of degree or level along relevant dimensions.

Organization culture, multiculturalism, and diversity are all closely related to one another. For example, the culture of an organization will affect the levels of diversity and multiculturalism that exist within its boundaries. Old Navy, for example, has an open culture that promotes diversity throughout its business. And similarities and differences arising from diversity and multicultural forces will also influence the culture of an organization. Social culture and diversity are also interrelated. For example, the norms reflected in a social culture will partially determine how that culture values demographic differences among people of that culture.

Each of these levels of culture represents important opportunities and challenges for managers. As we will see, if managers effectively understand, appreciate, and manage their organization's culture, diversity, and multiculturalism, their organization is more likely to be effective. But if managers ignore cultural forces or, even worse, attempt to circumvent or control them, then their organization is almost certain to experience serious problems.

MANAGEMENT Managers need to have a clear understanding of organizational culture, multiculturalism, and the relationship between the two.

■ The Organization's Culture

Culture is an amorphous concept that defies objective measurement or observation. Nevertheless, because it is the foundation of the organization's internal environment, it plays a major role in shaping managerial behavior.

The Importance of Organization Culture

Executives at Ford Motor Company recently decided to move the firm's Lincoln Mercury division from Detroit to southern California. Interestingly, though, this move had little to do with costs or any of the other reasons most business relocations occur. Instead, they wanted to move Lincoln Mercury out from the corporate shadow of its dominating bigger corporate cousin, Ford itself. For years, Lincoln Mercury managers had complained that their business was always given short shrift and that most of Detroit's attention was focused on Ford. At least partially as a result, Mercury products all tended to look like clones of Ford products, and the division consistently failed to meet its goals or live up to its expectations. Finally, the company decided that the only way to turn the division around was to give it its own identity. And where better to start than by moving the whole operation—lock, stock, and barrel—to car-centric southern California, where its managers could be freer to hire new creative talent and start carving out a new and unique business niche for themselves.[3] In short, they wanted to create a new culture.



While all organizations have a culture, each one is also unique. Take the Peter Morgan Band, for instance. Morgan and some of his amateur musician co-workers at Intel composed a little number called "The Cubicle Blues," poking fun at their Intel workspaces. After they started playing it at corporate parties, it quickly embedded itself into Intel's culture. And today, Intel flies the band all over the world to perform at company meetings and charity events.

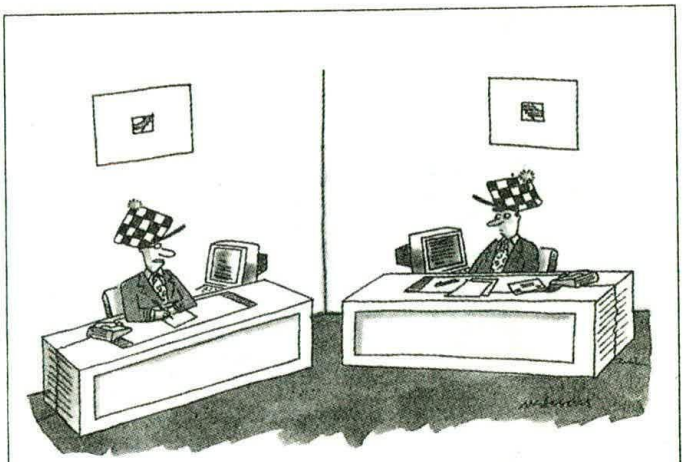
Culture determines the "feel" of the organization. The stereotypic image of Microsoft, for example, is a workplace where people dress very casually and work very long hours. In contrast, the image of Bank of America, for some observers, is a formal setting with rigid work rules and people dressed in conservative business attire. And Texas Instruments likes to talk about its "shirt-sleeve" culture, in which ties are avoided and few managers ever wear jackets. Southwest Airlines maintains a culture that stresses fun and excitement. The firm's CEO, Herb Kelleher, explains the company's emphasis on fun in an orientation video set to rap music.

Of course, the same culture is not necessarily found throughout an entire organization. For example, the sales and marketing department may have a culture quite different from that of the operations and manufacturing department. Regardless of its nature, however, culture is a powerful force in organizations, one

that can shape the firm's overall effectiveness and long-term success. Companies that can develop and maintain a strong culture, such as Hewlett-Packard and Procter & Gamble, tend to be more effective than companies that have trouble developing and maintaining a strong culture, such as Kmart.[4]

Determinants of Organization Culture

Where does an organization's culture come from? Typically it develops and blossoms over a long period of time. Its starting point is often the organization's founder. For example, James Cash Penney believed in treating employees and customers with respect and dignity. Employees at J.C. Penney are still called associates rather than employees (to reflect partnership), and customer satisfaction is of paramount importance. The impact of Sam Walton, Ross Perot, and Walt Disney is still felt in the organizations they founded.[5] As an organization grows, its culture is modified, shaped, and refined by symbols, stories, heroes, slogans, and ceremonies. For example, an important value at Hewlett-Packard (HP) is the avoidance of bank debt. A popular story still told at the company involves a new project being considered for several years. All objective criteria indicated that HP should borrow money from a bank to finance it, yet Bill Hewlett and David Packard rejected it out of hand simply because "HP avoids bank debt." This story, involving two corporate heroes and based on a slogan, dictates corporate culture today. And many decisions at Walt Disney Company today are still framed by asking, "What would Walt have done?"



"I don't know how it started, either. All I know is that it's part of our corporate culture."

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An organization's culture can be determined in a variety of ways. Symbols, stories, heroes, slogans, and ceremonies, for example, all play a role in defining and continuing culture. Sometimes, however, the meaning of some element of culture can become blurred or even forgotten over time. As illustrated here, some organizations do things simply because they "always have," even to the point where these things become institutionalized standard practices. And occasionally, some of these things may even border on the absurd!

Corporate success and shared experiences also shape culture. For example, Hallmark Cards has a strong culture derived from its years of success in the greeting cards industry. Employees speak of the Hallmark family and care deeply about the company; many of them have worked at the company for years. At Kmart, in contrast, the culture is quite weak, the management team changes rapidly, and few people sense any direction or purpose in the company. The differences in culture at Hallmark and Kmart are in part attributable to past successes and shared experiences.

Managing Organization Culture

How can managers deal with culture, given its clear importance but intangible nature? Essentially, the manager must understand the current culture and then decide if it should be maintained or changed. By understanding the organization's current culture, managers can take appropriate actions. At Hewlett-Packard, the values represented by "the HP way" still exist and guide most important activities

undertaken by the firm. Indeed, the firm's CEO, Carly Fiorina, launched her tenure at the firm with a series of television commercials focusing on the firm's Silicon Valley roots and the garage where it started. Culture can also be maintained by rewarding and promoting people whose behaviors are consistent with the existing culture and by articulating the culture through slogans, ceremonies, and so forth. *The World of Management* describes how Merrill Lynch has extended its famed organizational culture into its foreign offices.

But managers must walk a fine line between maintaining a culture that still works effectively versus changing a culture that has become dysfunctional. For example, many of the firms already noted, as well as numerous others, take pride in perpetuating their cultures. Shell Oil Company, for example, has an elaborate display in the lobby of its Houston headquarters building that tells the story of the firm's past. But other companies may face situations in which their culture is no longer a strength. For example, some critics feel that the organization culture at General Motors places too much emphasis on product development and internal competition among divisions and not enough on marketing and competition with other firms.

WORLD OF MANAGEMENT

Spreading the Merrill Lynch Culture

Merrill Lynch & Co. is the largest brokerage operation in the United States. Ever since Charles Merrill and Edmund Lynch formed the company in 1914, the firm has focused its attention on individual investors and has based its operations on customer service. A manager who has been totally immersed in the company's culture heads each local Merrill Lynch office. These managers start as assistants in existing offices to learn the ropes and then go through an extended series of training programs at the firm's training center in Princeton, New Jersey. One ongoing component of this training focuses on the firm's culture—where it started and how it is to be perpetuated.

In the last several years Merrill Lynch has been undergoing a major expansion into international markets. Fueled in part by opening new offices and in part by buying existing brokerage firms, Merrill Lynch has become one of the largest retail brokerage companies in the world. When this expansion started, many of the firm's competitors doubted that it would be able to transfer its culture abroad. But, so far at least, these skeptics are wrong.

Merrill Lynch knew from the beginning of its internationalization efforts that sustaining its culture would be both important and difficult. Therefore, the company made the same commitment to global training as it makes to training its local managers—each and every Merrill Lynch office manager from foreign offices receives the same level of training as the firm's domestic managers receive. And like domestic managers, international managers receive continued exposure to the firm's heritage and culture. As a result, company executives say, the organization culture of any Merrill Lynch office, regardless of where it is, remains true to the spirit of the company's founders.

Visit our offices, whether it be Thailand, Malaysia, South Africa, or Germany, and you will see the same plaques on the wall with those same Merrill Principles in the local language.

—David H. Komansky, Merrill Lynch CEO*

References: "In a Matter of Months, Merrill Sets Itself Up as a Force in Japan," *The Wall Street Journal*, April 8, 1998, pp. A1, A10; "Merrillizing the World," *Forbes*, February 10, 1997, pp. 146–151 (*quote on p. 147); Shawn Tully, "Merrill Lynch Takes Over," *Fortune*, April 27, 1999, pp. 138–144.

Culture problems sometimes arise from mergers or the growth of rival factions within an organization. For example, Wells Fargo and Company, which relies heavily on snazzy technology and automated banking services, acquired another large bank, First Interstate, which had focused more attention on personal services and customer satisfaction. Blending the two disparate organization cultures was difficult for the firm as managers have argued over how best to serve customers and operate the new enterprise.[6]

To change culture, managers must have a clear idea of what they want to create. Schwinn has tried to redefine itself to be more competitive and to break free of its old approaches to doing business. The firm's new motto—"Established 1895. Re-established 1994."—represents an effort to create a new culture that better reflects today's competitive environment in the bicycle market. Likewise, when Continental Airlines "re-invented" itself a few years ago, employees were taken outside the corporate headquarters building in Houston to watch the firm's old policies and procedures manuals set afire. The firm's new strategic direction is known throughout Continental as the "Go Forward" plan, intentionally named to avoid reminding people about the firm's troubled past and to focus instead on the future.

One major way to shape culture is by bringing outsiders into important managerial positions. The choice of a new CEO from outside the organization is often a clear signal that things will be changing. Indeed, new CEOs were the catalyst for the changes at Schwinn and Continental noted above. Adopting new slogans, telling new stories, staging new ceremonies, and breaking with tradition can also alter culture. Culture can also be changed by methods discussed in Chapter 13.[7] We now turn our attention to other related parts of the cultural environment of management: diversity and multiculturalism.

MANAGEMENT IMPLICATIONS Managers need to have a clear understanding and appreciation of the importance of organization culture. In addition, they need to know how culture is determined. They should also understand how to manage organization culture.

■ Diversity and Multiculturalism in Organizations

As introduced and defined earlier in this chapter, diversity and multiculturalism essentially relate to differences among people. Because organizations today are becoming more diverse and multicultural, it is important that all managers understand the major trends and dimensions of diversity and multiculturalism.

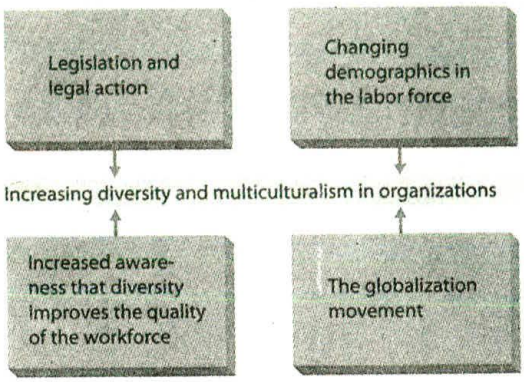
Trends in Diversity and Multiculturalism

The most fundamental trend in diversity and multiculturalism is that virtually all organizations, simply put, are becoming more diverse and multicultural. The

Figure 6.1

Reasons for Increasing Diversity and Multiculturalism

Diversity and multiculturalism are increasing in most organizations today for four basic reasons. These reasons promise to make diversity even greater in the future.



composition of their workforces is changing in many different ways. The basic reasons for this trend are illustrated in Figure 6.1.

One factor contributing specifically to increased diversity is changing demographics in the labor force. As more women and minorities enter the labor force, for example, the available pool of talent from which organizations hire employees has changed in both size and composition. If talent within each segment of the labor pool is evenly distributed (for example, if the number of very talented men in the workforce as a percentage of all men in the workforce is the same as the number of very talented women in the labor force as a percentage of all women in the workforce), it follows logically that, over time, proportionately more women and proportionately fewer men will be hired by an organization.

A related factor contributing to diversity is the increased awareness by organizations that they can improve the overall quality of their workforce by hiring and promoting the most talented people available. By casting a broader net in recruiting and looking beyond traditional sources for new employees, organizations are finding more broadly qualified and better qualified employees from many different segments of society. Thus, these organizations are finding that diversity can be a source of competitive advantage.[8]

Another reason for the increase in diversity is that legislation and legal actions have forced organizations to hire more broadly. In earlier times, organizations in the United States were essentially free to discriminate against women, blacks, and other minorities. While not all organizations consciously and/or openly engaged in these practices, many firms nevertheless came to be dominated by white males. But starting with the passage of the Civil Rights Act in 1964, numerous laws have outlawed discrimination against African Americans and most other groups. As we detail in Chapter 14, organizations must hire and promote people today solely on the basis of their qualifications.

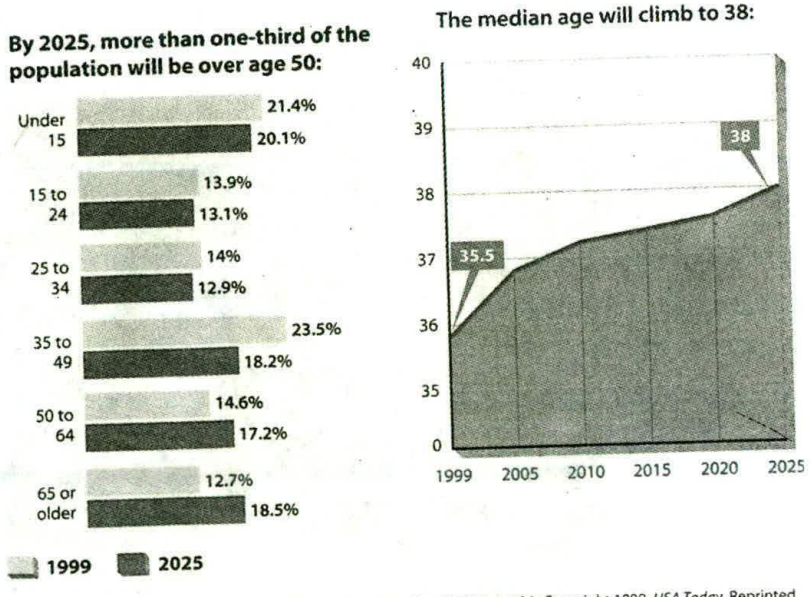
A final factor contributing to increased multiculturalism in particular is the globalization movement. Organizations that have opened offices and related facilities in other countries have had to learn to deal with different customs, social norms, and mores. Strategic alliances and foreign ownership also contribute because managers today are more likely to have job assignments in other countries and/or to work with foreign managers within their own countries. As employees and managers move from assignment to assignment across national boundaries, organizations and their subsidiaries within each country thus become more diverse and multicultural.

Dimensions of Diversity and Multiculturalism

As we indicated earlier, many different dimensions of diversity and multiculturalism can characterize an organization. In this section we discuss age, gender, ethnicity, and other dimensions of diversity.

Age Distributions One important dimension of diversity in any organization is the age distribution of its workers. The average age of the U.S. workforce is gradually increasing and will continue to do so for the next several years. Figure 6.2 presents age distributions for U.S. workers in 1999 and projected age distributions through the year 2025; over that span the median age is expected to rise from 35.5 years to 38 years.

Several factors are contributing to this pattern. For one, the baby-boom generation (a term used to describe the unusually large number of people who were born in the twenty-year period after World War II) continues to age. Declining birth rates among the post-baby-boom generations simultaneously account for smaller percentages of new entrants into the labor force. Another factor that contributes to the aging workforce is improved health and medical care. As a result of these improvements, people are able to remain productive and active for longer periods of time. Combined with higher legal limits for mandatory retirement, more and more people are working beyond the age at which they might have retired just a few years ago.



Source: U.S. Census Bureau as reported in *USA Today*, September 7, 1999, p. 13A. Copyright 1999, *USA Today*. Reprinted with permission.

Figure 6.2

Age Distribution Trends in the United States

The U.S. population is gradually growing older. For example, in 1999 the median age in the United States was 35.5 years; by 2025, however, this figure will rise to 38 years. By that same year, more than one-third of the entire U.S. population will be over age 50.

How does this trend affect organizations? Older workers tend to have more experience, to be more stable, and to make greater contributions to productivity than younger workers. On the other hand, despite the improvements in health and medical care, older workers are nevertheless likely to require higher levels of insurance coverage and medical benefits. And the declining labor pool of younger workers will continue to pose problems for organizations as they find fewer potential new entrants into the labor force.[9]

Gender As more and more women have entered the workforce, organizations have subsequently experienced changes in the relative proportions of male and female employees. In the United States, for example, the workforce in 1964 was 66 percent male and 34 percent female. In 1994 the relative proportions had changed to 54 percent male and 46 percent female. By the year 2000 the proportions were around 52 percent male and 48 percent female.

glass ceiling A barrier that keeps women from advancing to top management positions in many organizations

These trends aside, a major gender-related problem that many organizations face today is the so-called glass ceiling. The **glass ceiling** describes a barrier that keeps women from advancing to top management positions in many organizations.[10] This ceiling is a real barrier that is difficult to break, but it is also so subtle that it is hard to discern. Indeed, whereas women comprise almost 45 percent of all managers, there are very few female CEOs among the one thousand largest businesses in the United States. Similarly, the average pay of women in organizations is lower than that of men. Although the pay gap is gradually shrinking, inequalities are present nonetheless. *Management InfoTech* explains how the gender gap is an especially big problem in some high-tech firms.



Many different dimensions of diversity are relevant in organizations today. Gender is among the most significant. Gender barriers are being broken almost every day at all levels in virtually all organizations as women and men increasingly move into positions that have traditionally been dominated by one gender or the other. One area where it has been particularly difficult for women to advance has been the wine industry, traditionally a tightly controlled male bastion. However, Michaela Rodeno has made it to the top spot in France's St. Supery U.S. subsidiary. Indeed, she and several other women have recently assumed executive positions in leading wine producing and distributing firms, both in the United States and in Europe.

MANAGEMENT INFOTECH

THE MALE NERD CULTURE OF SILICON VALLEY

In the work-hard, play-hard environment of California's Silicon Valley, eligible single women are almost as scarce as snow. As a result, too many engineering or programming nerds in dot-coms or software start-ups have hot cars and stock options but few dates. Why? In most areas of the United States, unmarried women outnumber unmarried men. However, the situation is reversed in Santa Clara County. Attracted by the infotech opportunities, this area contains sixty-eight thousand more single men than women.

Given the long hours and dedication that infotech careers demand, many men and women have very little free time for romance. When two people do manage to connect, the intense competition among area firms complicates matters even further. To protect themselves and their employers, the two may ask each other to sign nondisclosure agreements—forbidding any outside discussion of company secrets—before they start to date.

Not surprisingly, dating services, singles mixers, and matchmakers in the area are doing a booming business as men go on the hunt for potential partners. Silicon Valley is so lopsidedly male that some recruiters are concerned about being able to attract a steady influx of talented single men for local high-tech jobs. In fact, some men have already switched jobs, moving to Boston and other infotech zones in search of a better ratio of unattached women to unattached men. For their part, women in Silicon Valley are enjoying their after-hours popularity—working in the male nerd culture is not a problem for them.

This is the best time in history to be a woman in Northern California.

*-Nicole Lorenzo, Stanford Graduate School of Business student**

References: Michelle Conlin, "Valley of No Dolls," *Business Week*, March 6, 2000, pp. 126, 129 (*quote on p. 126); Joel Dreyfuss, "Valley of Denial," *Fortune*, July 19, 1999, pp. 60–61.

Why does the glass ceiling still seem to exist? One reason may be that real obstacles to advancement for women, such as subtle discrimination, may still exist in some organizations.[11] Another is that many talented women choose to leave their jobs in large organizations and start their own businesses. Still another factor is that some women choose to suspend or slow their career progression to have children. But there are also many talented women continuing to work their way up the corporate ladder and getting closer and closer to a corporate "top spot."[12]

Ethnicity A third major dimension of cultural diversity in organizations is enthnicity. **Ethnicity** refers to the ethnic composition of a group or organization. Within the United States, most organizations reflect varying degrees of ethnicity comprising whites, African Americans, Hispanics, and Asians. Figure 6.3 shows the ethnic composition of the U.S. workforce in 1999 and projections for the year 2025 in terms of these ethnic groups.[13]

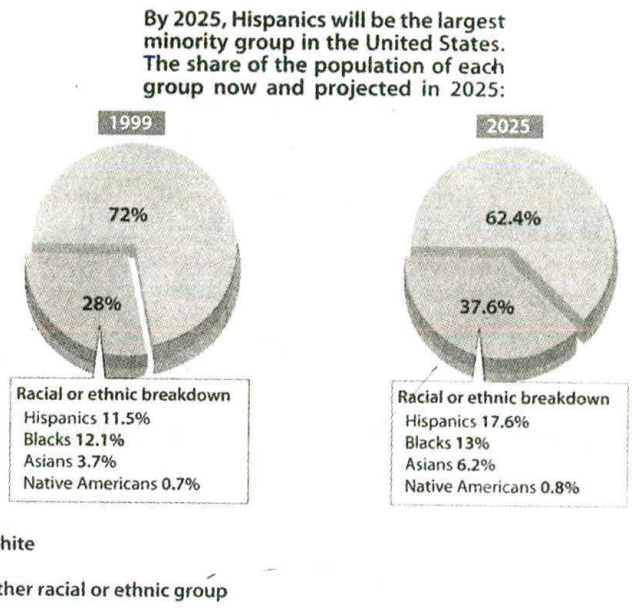
ethnicity The ethnic composition of a group or organization

The biggest projected changes involve whites and Hispanics. In particular, the percentage of whites in the workforce is expected to drop from 72 percent to 62.4 percent. At the same time, the percentage of Hispanics is expected to climb from 11.5 percent to 17.6 percent. The percentages of African Americans, Asians, and

Figure 6.3

Ethnicity Distribution Trends in the United States

Ethnic diversity in the United States is also increasing. For example, while 72 percent of the U.S. population was white in 1999, this will drop to 62.4 percent by 2025. Hispanics will reflect the largest percentage increase, moving from 11.5 percent in 1999 to 17.6 percent of the U.S. population by 2025.



Source: U.S. Census Bureau as reported in *USA Today*, September 7, 1999, p. 13A. Copyright 1999, *USA Today*. Reprinted with permission.

others are also expected to climb, but at lower rates. As with women, members of the African American, Hispanic, and Asian groups are generally underrepresented in the executive ranks of most organizations today. And their pay is similarly lower than might be expected. But as is the case for women, the differences are gradually disappearing as organizations fully embrace equal employment opportunity and recognize the higher overall level of talent available to them.[14]

Other Dimensions of Diversity In addition to age, gender, and ethnicity, organizations are also confronting other dimensions of diversity. Handicapped and physically challenged employees are increasingly important in many organizations, especially since the recent passage of the Americans with Disabilities Act. Different religious beliefs also constitute an important dimension of diversity.[15] And single parents, dual-career couples, gays and lesbians, people with special dietary preferences (e.g., vegetarians), and people with different political ideologies and viewpoints also represent major dimensions of diversity in today's organizations.[16]

Multicultural Differences In addition to these various diversity-related dimensions, organizations are increasingly being characterized by multicultural differences as well. Some organizations, especially international businesses, are actively seeking to enhance the multiculturalism of their workforce. But even organiza-

tions that are more passive in this regard may still become more multicultural because of changes in the external labor market. Immigration into the United States is at its highest rate since 1910, for example. Over five million people from Asia, Mexico, Europe, and other parts of the world entered the United States between 1991 and 1995.[17]

MANAGEMENT IMPLICATIONS Managers should be thoroughly familiar with recent trends in diversity and multiculturalism. In addition, they should understand the basic dimensions of diversity and multiculturalism in organizations.

■ Effects of Diversity and Multiculturalism in Organizations

There is no question that organizations are becoming ever more diverse and multicultural. But how does this affect organizations? As we see, diversity and management provide both opportunities and challenges for organizations. They also play a number of important roles in organizations today.

Multiculturalism and Competitive Advantage

Many organizations are finding that diversity and multiculturalism can be sources of competitive advantage in the marketplace. In general, six arguments have been proposed for how they contribute to competitiveness.[18] These arguments are illustrated in Figure 6.4.

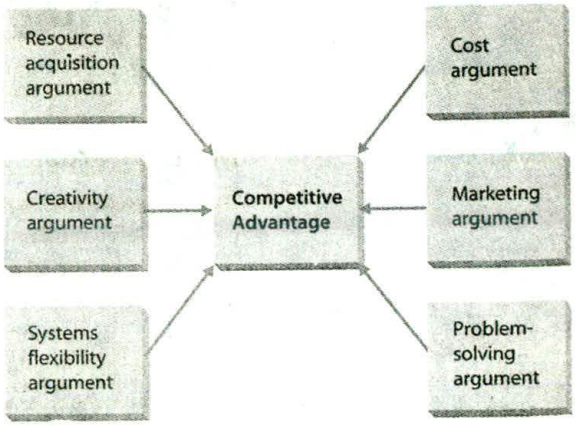
The *cost argument* suggests that organizations that learn to manage diversity and multiculturalism generally have higher levels of productivity and lower levels of turnover and absenteeism. Those organizations that do a poor job of managing diversity and multiculturalism, on the other hand, suffer from problems of lower productivity and higher levels of turnover and absenteeism. Because each of these factors has a direct impact on costs, the former organization remains more competitive than does the latter. Ortho Pharmaceutical Corporation estimates that it has saved $500,000 by lowering turnover among women and ethnic minorities.[19]

The *resource acquisition argument* suggests that organizations who manage diversity and multiculturalism effectively become known among women and minorities as good places to work. These organizations are thus better able to attract qualified employees from among these groups. Given the increased importance of these groups in the overall labor force, organizations that can attract talented employees from all segments of society

Figure 6.4

How Diversity and Multiculturalism Promote Competitive Advantage

Many organizations today are finding that diversity and multiculturalism can be sources of competitive advantage. Various arguments have been developed to support this viewpoint. For example, an African-American sales representative for Revlon helped that firm improve its packaging and promotion for its line of darker skin-tone cosmetics.



are likely to be more competitive. Table 6.1 lists companies that have an especially good reputation for minorities to work.

The *marketing argument* suggests that organizations with diverse and multicultural workforces are better able to understand different market segments than are less diverse organizations. For example, a cosmetics firm like Avon that wants to sell its products to women and African Americans can better understand how to create such products and effectively market them if women and African-American managers are available to provide input into product development, design, packaging, advertising, and so forth.[20] Both Sears and Target have profited by focusing part of their marketing efforts on building consumer awareness among Hispanics.[21]

The *creativity argument* suggests that organizations with diverse and multicultural workforces are generally more creative and innovative than other organizations. If an organization is dominated by one population segment, it follows that its members will generally adhere to norms and ways of thinking that reflect that segment. Moreover, they have little insight or stimulus for new ideas that might be derived from different perspectives. The diverse and multicultural organization, in contrast, is characterized by multiple perspectives and ways of thinking and is therefore more likely to generate new ideas and ways of doing things.[22]

Related to the creativity argument is the *problem-solving argument.* Diversity and multiculturalism are accompanied by an increased pool of information. In virtually any organization, there is some information that everyone has and other information that is unique to each individual. In an organization with little diversity, the larger pool of information is common and the smaller pool is unique. But in a more diverse organization, the pool of unique information is larger. Thus, because more information can be brought to bear on a problem, there is a higher probability that better solutions can be identified.[23]

Finally, the *systems flexibility argument* suggests that organizations must become more flexible as a way of managing a diverse and multicultural workforce. As a direct consequence, the overall organizational system also becomes more flexible. As we discuss in Chapters 3 and 13, organizational flexibility enables the organization to respond better to changes in its environment. Thus, by effectively managing diversity and multiculturalism within its workforce, an organization simultaneously becomes better equipped to address its environment.

Multiculturalism and Conflict

Unfortunately, diversity and multiculturalism in an organization can also create conflict. This conflict can arise for a variety of reasons.[24] One potential avenue for conflict is when an individual thinks that someone has been hired, promoted, or fired because of her or his diversity status. For example, suppose that a male executive loses a promotion to a female executive. If he believes that she was promoted because the organization simply wanted to have more female managers rather than because she was the better candidate for the job, he will likely feel resentful toward both her and the organization itself.

Table 6.1

America's Best Companies for Minorities

Rank 2000 (1999) Company 1999 revenues (millions)	No. of Minorities		Percentages that Are Minorities			
	Board of Directors	Top Fifty Paid	Officials and Managers	Total Workforce	Asian, Black, Hispanic, Native American	Minorities as a Percentage of New Hires
1 (6) **Advantica** Spartanburg, S.C. $1,735	4 of 11	8	33.4%	49.9%	4.3% 10.6% 34.7% 0.3%	69%
2 (*) **Levi Strauss & Co.** San Francisco $6,000	2 of 12	7	35.3%	58%	6.9% 9.2% 41.6% 0.3%	51%
3 (2) **Fannie Mae** Washington D.C. $36,969	N.A.	8	27.6%	40.2%	9.6% 26.3% 4.0% 0.2%	46%
4 (4) **Sempra Energy** San Diego $5,435	5 of 16	6	27.9%	47.1%	7.7% 11.0% 27.7% 0.7%	45%
5 (*) **Dole Food** Westlake Village, CA $5,061	1 of 7	17	36.6%	55.6%	38.9% 1.6% 14.7% 0.4%	71%
6 (1) **Union Bank of California** San Francisco $2,749	4 of 14	6	35.7%	54%	25.9% 8.4% 19.3% 0.4%	61%
7 (3) **Public Service Co. of N.M.** Albuquerque $1,158	3 of 9	9	32.1%	47.1%	0.6% 1.7% 40.7% 4.2%	51%
8 (*) **Avis Rent A Car** Garden City, N.Y. $3,333	2 of 11	5	25%	48%	6.0% 25.9% 15.5% 0.6%	63%
9 (*) **U.S. Postal Service** Washington, D.C. $62,726	2 of 11	11	30%	35.7%	6.4% 21.5% 7.2% 0.5%	50%
10 (7) **SBC Communications** San Antonio $49,489	4 of 24	4	26.1%	34.4%	3.7% 18.4% 11.7% 0.7%	52%
11 (20) **Xerox** Stamford, Conn. $19,228	2 of 16	10	23.4%	28.7%	5.2% 15.4% 7.4% 0.7%	40%

N.A. Not Available

*Not on last year's list.

Source: *Fortune*, July 10, 2000, pp. 190–193. © Time Inc. All rights reserved.

Another source of conflict stemming from diversity or multiculturalism is through misunderstood, misinterpreted, or inappropriate interactions between people of different groups.[25] For example, suppose that a male executive tells a sexually explicit joke to a new female executive. He may intentionally be trying to embarrass her, he may be clumsily trying to show her that he treats everyone the same, or he may think he is making her feel like part of the team. Regardless of his intent, however, if she finds the joke offensive, she will justifiably feel anger and hostility. These feelings may be directed at only the offending individual or more generally toward the entire organization if she believes that its culture facilitates such behaviors. And, of course, sexual harassment itself is both unethical and illegal.

Conflict can also arise as a result of other elements of multiculturalism. For example, when a U.S. manager publicly praises the work of a Japanese employee for his outstanding work, the action stems from the dominant cultural belief in the United States that such recognition is important and rewarding. But because the Japanese culture places a much higher premium on group loyalty and identity than on individual accomplishment, the employee will likely feel ashamed and embarrassed. Thus, a well-intentioned action may backfire and result in unhappiness. A joint venture among IBM (a U.S. company), Siemens (a German company), and Toshiba (a Japanese company) had difficulties attributed to cultural differences in work hours, working styles, interpersonal relations, and conflict.[26]

Conflict may also arise as a result of fear, distrust, or individual prejudice. Members of the dominant group in an organization may worry that newcomers from other groups pose a personal threat to their own position in the organization. For example, when U.S. firms have been taken over by Japanese firms, U.S. managers have sometimes been resentful or hostile to Japanese managers assigned to work with them. People may also be unwilling to accept people who are different from themselves. And personal bias and prejudices are still very real among some people today and can lead to potentially harmful conflict.

Several high-profile problems involving diversity and multiculturalism focused attention on the potential for conflict and how important it is that managers respond appropriately when problems occur. Shoney's Inc., a southern restaurant chain, was charged with racism throughout its managerial ranks. Denny's, another restaurant business, was charged with similar practices. At Texaco, senior executives used racial slurs on a tape subsequently released to the public. And a class-action lawsuit against the financial brokerage giant Smith Barney alleged widespread hostilities and discrimination toward women throughout the firm.[27] In each of these cases, fortunately, the organizations involved have undertaken major programs designed to eliminate such problems in the future.

MANAGEMENT IMPLICATIONS All managers need to know the effects of diversity and multiculturalism in organizations. In particular, they need to appreciate how multiculturalism can provide a basis for competitive advantage. They must also understand how multiculturalism can result in conflict.

■ Managing Diversity and Multiculturalism in Organizations

Because of the tremendous potential that diversity and multiculturalism hold for competitive advantage, as well as the possible consequences of associated conflict, much attention has been focused in recent years on how individuals and organizations can manage diversity and multiculturalism better. In the sections that follow, we first discuss individual strategies for dealing with diversity and multiculturalism and then summarize organizational approaches to managing both.

Individual Strategies

One important element of managing diversity and multiculturalism in an organization consists of what individuals themselves can do. The four basic attitudes that individuals can strive for are understanding, empathy, tolerance, and willingness to communicate.

Understanding The first of these is understanding the nature and meaning of diversity and multiculturalism. Some managers, for example, have taken the basic concepts of equal employment opportunity to an unnecessary extreme. They know that, by law, they cannot discriminate against people on the basis of sex, race, and so forth. Thus, in following this mandate they come to believe that they must treat everyone the same.

But this belief can cause problems when translated into workplace behaviors among people after they have been hired because people are not the same. Although people need to be treated fairly and equitably, managers must understand that differences among people do, in fact, exist. Thus, any effort to treat everyone the same, without regard to their fundamental human differences, will only lead to problems. Managers must understand that cultural factors cause people to behave in different ways and that these differences should be accepted.

Empathy Related to understanding is empathy. People in an organization should try to understand the perspective of others. For example, suppose a woman joins a group that has traditionally been comprised of white men. Each man may be a little self-conscious about how to act toward the new member and may be interested in making her feel comfortable and welcome. But they may be able to do this even more effectively by empathizing with how she may feel. For example, she may feel disappointed or elated about her new assignment, she may be confident or nervous about her position in the group, and she may be experienced or inexperienced in working with male colleagues. By learning more about her feelings, the group members can further facilitate their ability to work together effectively.

Tolerance A third related individual approach to dealing with diversity and multiculturalism is tolerance. Even though people learn to understand others,

and even though they may try to empathize with others, the fact remains that they may still not accept or enjoy some aspect of their behavior. For example, one organization reported that it had experienced considerable conflict among its U.S. and Israeli employees. The Israeli employees always seemed to want to argue about every issue that arose. The U.S. managers preferred to conduct business more harmoniously and became uncomfortable with the conflict. Finally, after considerable discussion it was learned that many of the Israeli employees simply enjoyed arguing and saw it as part of getting work done. The firm's U.S. employees do not enjoy the arguing, but they are more willing to tolerate it as a fundamental cultural difference between themselves and their colleagues from Israel.[28]

Willingness to Communicate A final individual approach to dealing with diversity and multiculturalism is communication. Problems often get magnified over these issues because people are afraid or otherwise unwilling to discuss openly issues that relate to diversity or multiculturalism. For example, suppose that a young employee has a habit of making jokes about the age of an elderly colleague. Perhaps the young colleague means no harm and is just engaging in what she sees as good-natured kidding. But the older employee may find the jokes offensive. If the two do not communicate, the jokes will continue and the resentment will grow. Eventually, what started as a minor problem may erupt into a much bigger one.

For communication to work, it must be two-way. If a person wonders if a certain behavior on her or his part is offensive to someone else, the curious individual should just ask. Similarly, if someone is offended by the behavior of another person, he or she should explain to the offending individual how the behavior is perceived and request that it stop. As long as such exchanges are friendly, low key, and nonthreatening, they will generally have a positive outcome. Of course, if the same message is presented in an overly combative manner or if a person continues to engage in offensive behavior after having been asked to stop, problems will only escalate. At this point, third parties within the organization may have to intervene. And in fact, most organizations today have one or more systems in place to address questions and problems that arise as a result of diversity. We now turn our attention to various ways that organizations can indeed better manage diversity.

Organizational Approaches

Whereas individuals are important in managing diversity and multiculturalism, the organization itself must play a fundamental role.[29] Through its various policies and practices, people in the organization come to understand what behaviors are and are not appropriate. Diversity and multicultural training is an even more direct method for managing diversity. And the organization's culture is the ultimate context from which diversity and multiculturalism must be addressed.

Organizational Policies The starting point in managing diversity and multiculturalism is the policies that an organization adopts to affect, directly or indirectly,

how people are treated. Obviously, for instance, the extent to which an organization embraces the premise of equal employment opportunity will determine to a large extent the potential diversity within an organization. But the organization that follows the law to the letter and practices only passive discrimination differs from the organization that actively seeks a diverse and varied workforce.

Another aspect of organizational policies that affects diversity and multiculturalism is how the organization addresses and responds to problems that arise from differences among people. Consider the example of a manager charged with sexual harassment. If the organization's policies put an excessive burden of proof on the individual being harassed and invoke only minor sanctions against the guilty party, it is sending a clear signal about the importance of such matters. But the organization that has a balanced set of policies for addressing questions like sexual harassment sends its employees a message that diversity and individual rights and privileges are important.

Indeed, perhaps the major policy through which an organization can reflect its stance on diversity and multiculturalism is its mission statement. If the organization's mission statement articulates a clear and direct commitment to differences among people, it follows that everyone who comes into contact with that mission statement will grow to understand and accept the importance of diversity and multiculturalism, at least to that particular organization.

Organizational Practices Organizations can also help manage diversity and multiculturalism through a variety of ongoing practices and procedures. Avon's creation of networks for various groups represents one example of an organizational practice that fosters diversity. In general, the idea is that, because diversity and multiculturalism are characterized by differences among people, organizations can manage that diversity more effectively by following practices and procedures that are based on flexibility rather than rigidity.

Benefits packages, for example, can be structured to accommodate individual situations better. An employee who is part of a dual-career couple and who has no children may require relatively little insurance (perhaps because his spouse's employer provides more complete coverage) and would like to be able to schedule vacations to coincide with those of his spouse. An employee who is a single parent may need a broad spectrum of insurance coverage and may prefer to schedule his vacation time to coincide with school holidays.

Flexible working hours are also a useful organizational practice for accommodating diversity. Differences in family arrangements, religious holidays, cultural events, and so forth, may each dictate that employees have some degree of flexibility in the times when they work. For example, a single parent may need to leave the office every day at 4:30 to pick up the children from their day-care center. An organization that truly values diversity will make every reasonable attempt to accommodate such a need.

Organizations can also facilitate diversity and multiculturalism by making sure that its important committees and executive teams are diverse. Even if diversity exists within the broader organizational context, an organization that does not reflect diversity in groups like committees and teams implies that diversity is not a fully

ingrained element of its culture. In contrast, if all major groups and related work assignments reflect diversity, the message is quite a different one. *Today's Management Issues* discusses organizational practices related to gays in the workforce.

Diversity and Multicultural Training Many organizations are finding that diversity and multicultural training is an effective means for managing diversity and minimizing its associated conflict. More specifically, **diversity and multicultural training** is training that is specifically designed to enable members of an organization to function better in a diverse and multicultural workplace.[30] This training can take a variety of forms. For example, many organizations find it useful to help people learn more about their similarities to and differences from others. Men and women can be taught to work together more effectively and can gain insights into how their own behaviors affect and are interpreted by others. In one organization, a diversity training program helped male managers gain

diversity and multicultural training Training that is specifically designed to enable members of an organization to function better in a diverse and multicultural workplace

TODAY'S MANAGEMENT ISSUES

DIVERSITY STRATEGIES FOR GAY-FRIENDLY COMPANIES

Managing diversity is a critical strategy in today's tight labor market, where employers are fighting to keep their employees satisfied while continuing to recruit talented applicants from every possible source. Increasingly, top companies are developing specific strategies for attracting and retaining gay job applicants and employees. Pressure for gay-friendly policies is also coming from within many companies, where gay and lesbian managers and employees have formed formal and informal groups to network, provide support, and push for a more welcoming internal environment.

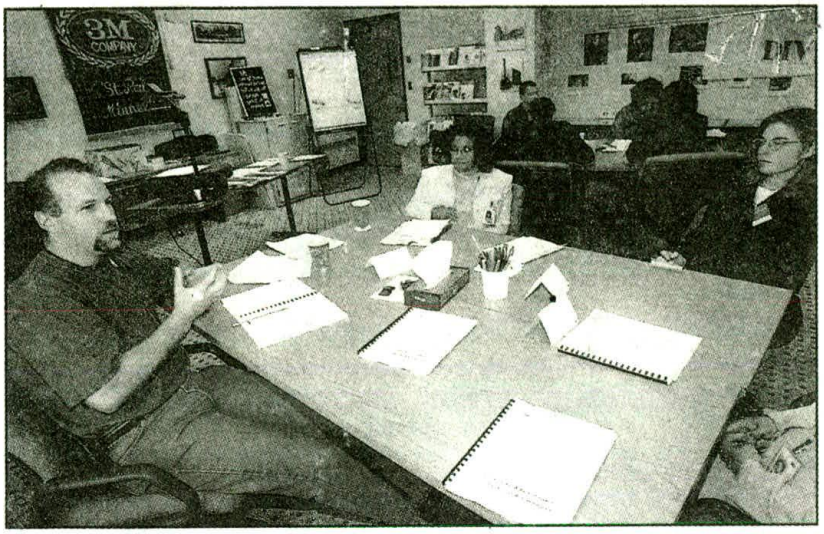
As a foundation, companies such as J.P. Morgan and IBM, among others, are ensuring that sexual orientation is covered within their corporatewide nondiscrimination policies. Like a growing number of companies, both J.P. Morgan and IBM also offer the same benefits to their employees' domestic partners, regardless of gender. Nearly three thousand U.S. companies follow this practice.

Establishing these kinds of policies and practices is only a start, however. Gay-friendly companies are going beyond the basics to communicate their emphasis on workforce diversity. Xerox, for example, advertises in gay and lesbian publications, putting the spotlight on the company's diversity and benefits. In addition, more companies are arranging recruiting programs targeted for gay and lesbian job applicants. For example, among the financial services firms that have underwritten recruiting dinners for gay business school students are J.P. Morgan, American Express, and Goldman Sachs. Kodak is one of the sponsors for the Gay Games, a sports event; McKinsey sponsors conferences for gay business students. These kinds of initiatives show the gay community—and everyone else—that the companies value diversity based on sexual orientation as well as gender, age, ethnicity, and other dimensions of diversity.

It's getting the message out that Xerox is a gay-friendly company.

*—Christa Carone, spokesperson, Xerox**

Reference: Stephanie Armour, "Companies Work to Be More Gay-Friendly," *USA Today*, February 28, 2000, p. 1B (*quote on p. 1B).



Diversity training is one strategy for helping to manage diversity in organizations. While some experts question its effectiveness, many businesses nevertheless encourage or require their employees to participate in such training. It is especially common in settings that have recently experienced diversity problems or issues, in part perhaps because it is a tangible action that the organization can point to as part of a campaign to overcome bad press and a damaged corporate reputation that can follow a diversity-related controversy. While 3M already has an exemplary record in the area of diversity, these engineers are participating in what the company calls the "Diversity Training Advantage" to help them gain new insights into how they can more effectively work with others.

insights into how various remarks they made to one another could be interpreted by others as being sexist. In the same organization, female managers learned how to point out their discomfort with those remarks without appearing overly hostile.[31]

Similarly, white and African-American managers may need training to understand each other better. Managers at Mobil Corporation noticed that four African-American colleagues never seemed to eat lunch together. After a diversity training program, they came to realize that the African-American managers felt that if they ate together, their white colleagues would be overly curious about what they might be talking about. Thus, they avoided close associations with one another because they feared calling attention to themselves.[32]

Some organizations even go so far as to provide language training for their employees as a vehicle for managing diversity and multiculturalism. Motorola, for example, provides English language training for its foreign employees on assignment in the United States. At Pace Foods in San Antonio, with a total payroll of over four hundred employees, staff meetings and employee handbooks are translated into Spanish for the benefit of the company's two hundred or so Hispanic employees.

Organizational Culture The ultimate test of an organization's commitment to managing diversity and multiculturalism, as discussed earlier in this chapter, is its culture.[33] Regardless of what managers say or put in writing, unless there is a basic and fundamental belief that diversity and multiculturalism are valued, it can never become truly an integral part of an organization. An organization that really wants

to promote diversity and multiculturalism must shape its culture so that it clearly underscores top management commitment to and support of diversity and multiculturalism in all of its forms throughout every part of the organization. With top management support, however, and reinforced with a clear and consistent set of organizational policies and practices, diversity and multiculturalism can become a basic and fundamental part of an organization.[34]

MANAGEMENT IMPLICATIONS Managers need to appreciate the fact that diversity and multiculturalism can be managed. They should understand, for example, that such individual strategies as understanding, empathy, tolerance, and a willingness to communicate can help promote diversity. Similarly, managers should also be quite familiar with such organizational strategies as organizational policies and practices, training, and organizational culture.

■ Toward the Multicultural Organization

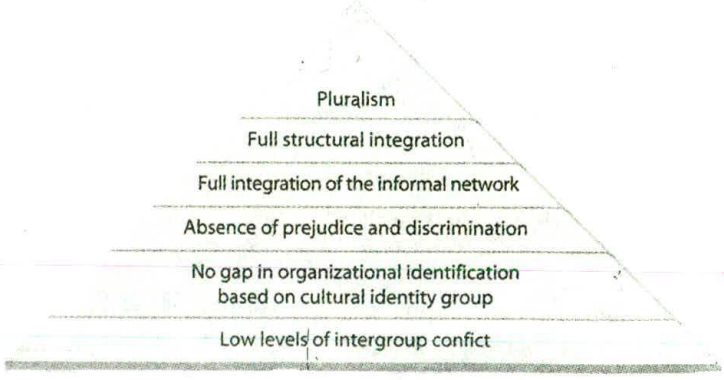
multicultural organization An organization that has achieved high levels of diversity, is able to capitalize fully on the advantages of diversity, and has few diversity-related problems

Many organizations today are grappling with cultural diversity. We noted in Chapter 5 that, whereas many organizations are becoming increasingly global, no truly global organization exists. In similar fashion, although organizations are becoming ever more diverse, few are truly multicultural. The **multicultural organization** has achieved high levels of diversity, is able to capitalize fully on the advantages of diversity, and has few diversity-related problems. One recent article described the six basic characteristics of such an organization.[35] These characteristics are illustrated in Figure 6.5.

Figure 6.5

The Multicultural Organization

Few, if any, organizations have become truly multicultural. At the same time, more and more organizations are moving in this direction. When an organization becomes multicultural, it reflects the six basic characteristics shown here.



Source: Based on Taylor H. Cox, "The Multicultural Organization," *Academy of Management Executive*, May 1991, pp. 34–47. Reprinted with permission.

First, the multicultural organization is characterized by *pluralism*: every group represented in an organization works to understand every other group. Thus, African-American employees try to understand white employees, and white employees try just as hard to understand their African-American colleagues. In addition, every group represented within an organization has the potential to influence the organization's culture and its fundamental norms.

Second, the multicultural organization achieves *full structural integration.* Full structural integration suggests that the diversity within an organization is a complete and accurate reflection of the organization's external labor market. If around half of the labor market is female, then about half of the organization's employees are female. Moreover, this same proportion is reflected at all levels of the organization. There are no glass ceilings or other subtle forms of discrimination.

Third, the multicultural organization achieves *full integration of the informal network.* This characteristic suggests that there are no barriers to entry and participation in any organizational activity. For example, people enter and exit lunch groups, social networks, communication grapevines, and other informal aspects of organizational activity without regard to age, gender, ethnicity, or other dimension of diversity.

Fourth, the multicultural organization is characterized by an *absence of prejudice and discrimination.* No traces of bias exist, and prejudice is eliminated. Discrimination is not practiced in any shape, form, or fashion. And discrimination is nonexistent, not because it is illegal but because of the lack of prejudice and bias. People are valued, accepted, and rewarded purely on the basis of their skills and what they contribute to the organization.

Fifth, in the multicultural organization there is *no gap in organizational identification based on cultural identity group.* In many organizations today people tend to make presumptions about organizational roles based on group identity. For example, many people walking into an office and seeing a man and woman conversing tend to assume that the woman is the secretary and the man is the manager. No such tendencies exist in the multicultural organization. People recognize that men and women are equally likely to be managers and secretaries.

Finally, there are *low levels of intergroup conflict* in the multicultural organization. We noted earlier that conflict is a likely outcome of increased diversity. The multicultural organization has evolved beyond this point to a state of virtually no conflict among people who differ. People within the organization fully understand, empathize with, have tolerance for, and openly communicate with everyone else. Values, premises, motives, attitudes, and perceptions are so well understood by everyone that any conflict that does arise is over meaningful and work-related issues as opposed to differences in age, gender, ethnicity, or other dimensions of diversity.

MANAGEMENT IMPLICATIONS Managers should be aware of the fact that no truly multicultural organization yet exists. At the same time, though, they should be familiar with the qualities and characteristics that would typify such an organization.

Summary of Key Points

Organization culture is the set of values, beliefs, behaviors, customs, and attitudes that helps the members of the organization understand what it stands for, how it does things, and what it considers important. When the people comprising an organization represent different cultures, their differences in values, beliefs, behaviors, customs, and attitudes reflect multiculturalism. Diversity exists in a community of people when its members differ from one another along one or more important dimensions.

Organization culture is an important environmental concern for managers. Managers must understand that culture is an important determinant of how well their organization will perform. Culture can be determined and managed in several different ways.

Diversity and multiculturalism are increasing in organizations today because of changing demographics, the desire by organizations to improve their workforce, legal pressures, and increased globalization. There are several important dimensions of diversity, including age, gender, and ethnicity. The overall age of the workforce is increasing. More women are also entering the workplace, although there is still a glass ceiling in many settings. In the United States, more Hispanics are also entering the workplace and the percentage of whites is gradually declining.

Diversity and multiculturalism can affect an organization in a number of different ways. For example, they can be sources of competitive advantage (i.e., cost, resource acquisition, marketing, creativity, problem solving, and systems flexibility arguments). On the other hand, diversity and multiculturalism can also be sources of conflict in an organization.

Managing diversity and multiculturalism in organizations can be done by both individuals and the organization itself. Individual approaches include understanding, empathy, tolerance, and willingness to communicate. Major organizational approaches are through policies, practices, diversity training, and culture.

Few, if any, organizations have become truly multicultural. The major dimensions that characterize organizations as they eventually achieve this state are pluralism, full structural integration, full integration of the informal network, an absence of prejudice and discrimination, no gap in organizational identification based on cultural identity group, and low levels of intergroup conflict attributable to diversity.

Discussion Questions

Questions for Review

1. How is organization culture usually created?
2. Why is diversity and multiculturalism increasing in many organizations today?
3. Summarize the basic impact of diversity and multiculturalism on organizations.
4. Discuss the four basic individual approaches and the four basic organizational approaches to diversity and multiculturalism.

Questions for Analysis

5. Compare and contrast organization culture and the culture of a country.
6. The text outlines many different advantages of diversity and multiculturalism in organizations. Can you think of any disadvantages?
7. What are the basic dimensions of diversity that most affect you personally?

Questions for Application

8. Visit the registrar's office or admissions office at your college or university. Using its enrollment statistics, determine the relative diversity on your campus. Is the student population more or less diverse than the faculty?
9. Assume that you are starting a new organization that is likely to grow rapidly. Develop a plan for becoming a multicultural organization.
10. Assume that you work for a large multinational organization. You have just learned that you are being transferred to India. You also know that you will be the first person of your ethnicity to work there. What steps might you take before you go to minimize problems that your presence might cause?

BUILDING EFFECTIVE *technical* SKILLS

Exercise Overview

Technical skills are the skills necessary to accomplish or understand the specific kind of work being done in an organization. This exercise will enable you to develop Internet skills as they relate to dealing with multicultural issues.

Exercise Background

One of the most important multicultural challenges facing managers today involves language skills. Assume you are the human resource manager for a large domestic company. Your firm has recently decided to enter into a joint venture with three foreign companies, one each from France, Germany, and Korea.

The terms of this joint venture involve your three partners each sending a team of managers to your corporate headquarters for a period of two years. You must make sure that your own top management team has the basic language skills in each of the three languages represented among your partners.

Exercise Task

With the background information above as context, do the following:

1. Use the Internet to obtain information about language training programs and methods.
2. Obtain information about one or more of each such program or method and make a decision about how you should proceed.

BUILDING EFFECTIVE *diagnostic* SKILLS

Exercise Overview

Diagnostic skills are the skills that enable a manager to visualize the most appropriate response to a situation. This exercise will enable you to practice your diagnostic skills as they relate to organization culture and multicultural issues and challenges.

Exercise Background

Your firm has recently undergone a significant increase in its workforce. Many of the new workers you have hired are immigrants from Eastern Europe and Asia. Several do not speak English very well, but all are hard workers who appear to be trying very hard to be successful and to fit in with their coworkers.

Recently, however, some problems have come to your attention. For one thing, several of your female workers have begun to complain about an increase in sexual harassment. For another, your supervisors have noticed an increase in tardiness and absenteeism among all of your workers.

You have decided that some action is clearly needed. However, you are unsure how to proceed. Consequently, you have decided to spend a few days thinking about what to do.

Exercise Task

With the background information above as context, do the following:

1. Think of as many causes as you can to explain each of the two problems you are facing.
2. Determine how you might address each problem, given the potential array of factors that might have contributed to them.
3. What role might organization culture be playing in this situation, apart from issues of multiculturalism?
4. What role might multiculturalism be playing in this situation, apart from issues of organization culture?

BUILDING EFFECTIVE *decision-making* SKILLS

Exercise Overview

Decision-making skills refer to the manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action for solving problems and capitalizing on opportunities. This exercise focuses on decision making about issues related to diversity and multiculturalism.

Exercise Background

For years your firm had relatively little diversity. The one-thousand-member workforce was almost exclusively white and male. But in recent years you have succeeded in increasing diversity substantially. Almost one-third of your employees are now female, while over 40 percent are Hispanic or African American.

Unfortunately, your firm has recently met with some unfortunate financial setbacks. You feel that you have no choice but to lay off about three hundred employees for a period of at least six months. If everything goes well, you also expect to be able to bring them back after six months.

Exercise Task

With the background information above as context, do the following:

1. Develop a layoff plan that will not substantially reduce your firm's diversity.
2. Decide how you will communicate your decision to the workforce.
3. What obstacles do you foresee in implementing your decision?

CHAPTER CLOSING CASE

A World of Diversity at IBM

In the mid-1990s, CEO Louis V. Gerstner made two decisions that changed the course of IBM. Big Blue (IBM's popular nickname) was struggling to redefine itself as more than a manufacturer of giant mainframe computers, and its profits were sagging. Gerstner's first major decision was to keep the company intact, despite intense pressure to slim it down by selling selected units. He believed that, with proper management and focus, IBM's many parts could collaborate effectively for more profitable synergy.

Gerstner's second major decision was to make the Internet the focal point of every part of the business. Many technology firms were eyeing the Internet but taking one step at a time, racing to build better web browsers or faster search engines. In contrast, the IBM CEO was looking a few steps beyond, seeing the Internet as an innovative way of expediting transactions and serving customers in every business area. Based on this view of the future, Gerstner decided to invest hundreds of millions of dollars to move IBM onto the Internet. But he realized that reshaping IBM into an Internet-savvy organization required a shift away from the company's traditional straight-laced, buttoned-down culture.

To become a thoroughly Internet-driven company, IBM needed to attract, motivate, and retain the best and brightest talent around the world. Management therefore developed a three-pronged approach to workforce diversity: equal opportunity programs ensure nondiscrimination, affirmative action programs eliminate barriers to opportunities and promote equality among employees, and work/life programs help employees balance their professional and personal responsibilities.

As part of this cultural shift, IBM created a series of task forces to examine relations with specific employee groups, including African-American, Hispanic, gay and lesbian, female, and Native-American employees. Ted Childs, IBM's vice president for global workforce diversity, recalls, "We asked [the task forces] to look at IBM through their constituency and answer, 'What was required for your group to feel welcome and valued throughout IBM?' and 'What could we do in partnership to maximize your productivity?'" These task forces were so valuable that IBM went on to form local diversity network groups and councils to encourage communication among employees with similar concerns and characteristics. There are currently eighty such network groups, including seventeen for African-American employees.

Grooming managers from all backgrounds for higher-level management positions became another priority. IBM began providing mentors and growth opportunities to fast-track managers through its Executive Resource Program and its Mentoring and Employee Development Program. Women infotech (IT) managers find such programs particularly helpful, according to Diane Hill, a manager at IBM Learning Services. "IT customers are typically male, and sometimes they second-guess women," she explains. "It's important for women to have positive role models in leadership positions."

IBM is also remaking its culture by aggressively recruiting creative tech types to work in special web design centers. Located in hip areas such as near the MTV studio in Los Angeles, the web design centers seem more like dot-com start-ups than IBM outposts. The design centers sport billiard and Ping-Pong tables, and employees are encouraged to bring their dogs (or iguanas) to work. Even employees' business cards look different, with titles such as "concept architect and paradoxiologist" (meaning that the employee works on complex Internet strategies).

As part of a decade-long global effort to attract and keep skilled employees at all levels, IBM has invested $150 million in dependent-care programs, establishing and expanding child-care and elder-care facilities in Canada, the United States, Mexico, Germany, Ireland, and other countries. The goal is to help employees and managers care for children and parents by establishing camps, day-care centers, elder-care programs, and nurseries on or near IBM offices and plants.

IBM's diversity programs are making a difference. Its management ranks are more diverse than ever, and the

company has become a recognized leader in Internet activities. But Gerstner and his management team are still feeling pressure. Amid slower revenue growth and more intense competition, some analysts are again calling for plans to refocus or sell parts of the business. So, despite its past successes, Big Blue must prove itself—again.

Case Questions

1. From a cultural standpoint, why would IBM maintain web design centers separate from other non-Internet facilities?
2. Which specific dimensions of diversity are being addressed by IBM's dependent-care programs?
3. What organizational culture and/or multicultural challenges might IBM have to face in the future?

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PART THREE

Planning and Decision Making



CHAPTER 7

Basic Elements of Planning and Decision Making

CHAPTER 8

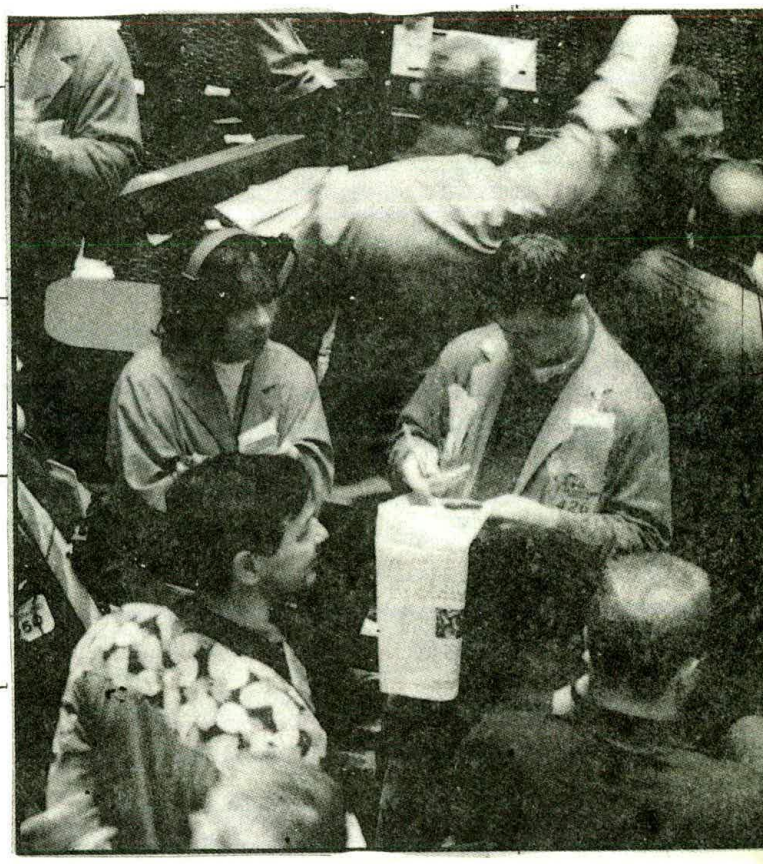
Managing Strategy and Strategic Planning

CHAPTER 9

Managing Decision Making and Problem Solving

CHAPTER 10

Managing New Venture Formation and Entrepreneurship



CHAPTER 7

Basic Elements of Planning and Decision Making

OPENING INCIDENT

For decades Procter & Gamble has been seen as one of the preeminent marketing companies in the world. Popular P&G brands such as Tide laundry detergent, Crisco shortening, Ivory soap, Crest toothpaste, and Pampers disposable diapers, for example, long ruled their respective markets. And P&G seemed like an unstoppable juggernaut as its flagship products and brands became increasingly entrenched as icons around the world.

One key to P&G's heritage of success has been a finely tuned set of procedures for developing new products, getting them to market, and then promoting them with relentless efficiency. All told, the firm sells more than three hundred brands in 140 countries. And there is at least one P&G product tucked away in virtually every kitchen cabinet or under every bathroom sink in the United States. Its annual revenues—about $37 billion—are four times those of Colgate-Palmolive and three times those of Kimberly-Clark, its nearest domestic rivals.

Indeed, P&G executives were so bullish in 1997 that they promised investors the firm would double its annual revenues from that year's $35 billion to a stunning $70 billion by the year 2006. And when that goal was announced, Wall Street analysts responded by encouraging investors to buy the firm's stock, and the business press lauded the company for its aggressive and forward-looking leadership. But almost before the ink had dried, observers began to identify chinks in the P&G armor and, within a short time, the firm's growth seemed to grind to a halt.

How could such a well-oiled marketing machine lose its momentum so quickly? As it turns out, P&G's problems had actually started years before but had simply not become apparent until much more recently. In a nutshell, what had been a major advantage for the firm had become a major liability—it had stopped innovating and was taking far too long to make changes and get new products to market. And its long-standing internal policies and procedures were to blame.

Perhaps most symptomatic of the firm's adherence to the "P&G way" is its internal system for writing memos. All internal memos have to follow a precise format. Managers are taught to follow this format, and they are encouraged to return any they receive that don't follow it. One former P&G manager indicated that the average memo had been revised or changed fifteen times before it was ever seen by a brand manager. Another exaggerated that "there's a P&G way for using the bathroom." And this rigid adherence to formula and procedure caused the firm to

"Colgate'll give you a project—and in a week it's out the door. . . . a P&G project can take years."

—unidentified packing supplier for Colgate-Palmolive and Procter & Gamble

LEARNING OBJECTIVES

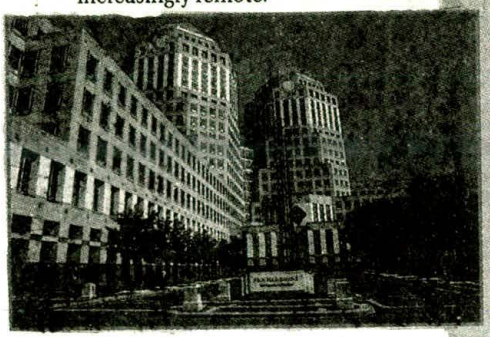
After studying this chapter, you should be able to:

- Summarize the function of decision making and the planning process.
- Discuss the purposes of organizational goals, identify different kinds of goals, discuss who sets goals, and describe how to manage multiple goals.
- Identify different kinds of organizational plans, note the time frames for planning, discuss who plans, and describe contingency planning.
- Discuss how tactical plans are developed and executed.
- Describe the basic types of operational plans used by organizations.
- Identify the major barriers to goal setting and planning, how organizations overcome those barriers, and how to use goals to implement plans.

become increasingly less responsive to shifts in its market.

Whereas competitors like Colgate were busily creating new products and nimbly getting them in the hands of consumers, P&G stuck with its tried-and-true approach to simply reformulating existing products and relaunching them as "improved." Tide, for instance, has undergone more than sixty product upgrades since its initial launch. Because the firm had enjoyed such a long period of sustained dominance, the company's culture acquired a pervasive and unerring adherence to precedent. Managers had come to believe they had to do things the way they had always been done, and individuals were criticized or even fired when they tried something new or different.

Looking back over the last decade, P&G's decline becomes more apparent. Its Ivory soap lost the market leadership position in 1991 to Unilever's Dove, and today has less than 5 percent of the market. Pampers disposable diapers have experienced a 50 percent drop in market share and lost the market leadership position to Kimberly-Clark's Huggies in 1993. And Crest toothpaste, perhaps P&G's most entrenched product, was passed by a new Colgate toothpaste in 1998. While Crest was still focusing on cavities—its hallmark since being introduced in 1955—Colgate and other competitors had started stressing not only cavity prevention but also fighting tartar, plaque, bad breath, and gingivitis. And because of these and other setbacks, P&G's hopes of reaching its lofty revenue goal seem increasingly remote.[1]



CHAPTER OUTLINE

- **Decision Making and the Planning Process**
- **Organizational Goals**
  - Purposes of Goals
  - Kinds of Goals
  - Responsibilities for Setting Goals
  - Managing Multiple Goals
- **Organizational Planning**
  - Kinds of Organizational Plans
  - Time Frames for Planning
  - Responsibilities for Planning
  - Contingency Planning
- **Tactical Planning**
  - Developing Tactical Plans
  - Executing Tactical Plans
- **Operational Planning**
  - Single-Use Plans
  - Standing Plans
- **Managing Goal-Setting and Planning Processes**
  - Barriers to Goal Setting and Planning
  - Overcoming the Barriers
  - Using Goals to Implement Plans

Procter & Gamble's managers have set an ambitious target for the firm's future revenue growth. One risk that they now face, though, is the criticism they can expect and the sense of disappointment that will result if this goal is not met. No matter how well the company performs otherwise, many observers will say the company failed to reach its goal. At the same time, however, the goal focuses attention on what the firm anticipates doing and provides guidance and direction to managers throughout the firm, with clear indicators of how they should manage their operations. In addition, the firm's plans for achieving its goal should help guide day-to-day activities toward growth and expansion.

As we noted in Chapter 1, planning and decision making comprise the first managerial function that organizations must address. This chapter is the first of four that explore the planning process in detail. We begin by briefly relating decision making and planning and then explaining the planning process that most organizations follow. We then discuss the nature of organizational goals and introduce the basic concepts of planning. Next we discuss tactical and operational planning more fully. We conclude with a discussion of how to manage the goal-setting and planning processes.

■ Decision Making and the Planning Process

Decision making is the cornerstone of planning. Consider, for example, Procter & Gamble's goal of doubling its revenues. The firm's top managers could have adopted an array of alternative options, including increasing revenues by only 25 percent or increasing revenues threefold. The time frame included for the projected revenue growth could also have been somewhat shorter or longer than the ten-year period that was actually specified. Alternatively, the goal could have included diversifying into new markets, cutting costs, or buying competing businesses. Thus, P&G's exact mix of goals and plans for growth rate and time frame reflect choices from among a variety of alternatives.

Clearly, then, decision making is the catalyst that drives the planning process. An organization's goals follow from decisions made by various managers. Likewise, deciding on the best plan for achieving particular goals also reflects a decision to adopt one course of action as opposed to others. We discuss decision making per se in Chapter 9. Our focus here is on the planning process itself. As we discuss goal setting and planning, however, keep in mind that decision making underlies every aspect of setting goals and formulating plans.[2]

The planning process itself can best be thought of as a generic activity. All organizations engage in planning activities, but no two organizations plan in exactly the same fashion. Figure 7.1 is a general representation of the planning process that many organizations attempt to follow. Although most firms follow this general framework, each also has its own nuances and variations.[3]

As Figure 7.1 shows, all planning occurs within an environmental context. If managers do not understand this context, they are unable to develop effective plans. Thus, understanding the environment is essentially the first step in planning. The four previous chapters cover many of the basic environmental issues

that affect organizations and how they plan. With this understanding as a foundation, managers must then establish the organization's mission. The mission outlines the organization's purpose, premises, values, and directions. Flowing from the mission are parallel streams of goals and plans. Directly following the mission are strategic goals. These goals and the mission help determine strategic plans. Strategic goals and plans are primary inputs for developing tactical goals. Tactical goals and the original strategic plans help shape tactical plans. Tactical plans, in turn, combine with the tactical goals to shape operational goals. These goals and the appropriate tactical plans determine operational plans. Finally, goals and plans at each level can also be used as input for future activities at all levels. This chapter discusses goals and tactical and operational plans. Chapter 8 covers strategic plans.

Figure 7.1

The Planning Process

The planning process takes place within an environmental context. Managers must develop a complete and thorough understanding of this context to determine the organization's mission and to develop its strategic, tactical, and operational goals and plans.



MANAGEMENT IMPLICATIONS Managers should recognize that decision making is the cornerstone of planning. They should also understand that, while all organizations engage in planning activities, no two organizations plan in exactly the same fashion. Consequently, every manager must understand the environmental context that provides the framework for planning within the unique organizational setting.

■ Organizational Goals

Goals are critical to organizational effectiveness, and they serve a number of purposes. Organizations can have several different kinds of goals, all of which must be appropriately managed. And several different kinds of managers must be involved in setting goals.

Purposes of Goals

Goals serve four important purposes.[4] First, they provide guidance and a unified direction for people in the organization. Goals can help everyone understand where the organization is going and why getting there is important.[5] Several years ago Jack Welch, CEO of General Electric Co., set a goal that every business owned by the firm will be either number one or number two in its industry. This goal still helps set the tone for decisions made by GE managers as the company competes with other firms like Whirlpool and Electrolux.[6] Likewise, the goal set for P&G of

doubling revenues by the year 2006 helps everyone in the firm recognize the strong emphasis on growth and expansion that is driving the firm.

Second, goal-setting practices strongly affect other aspects of planning. Effective goal setting promotes good planning, and good planning facilitates future goal setting. For example, the ambitious revenue goal set for P&G demonstrates how setting goals and developing plans to reach them should be seen as complementary activities. The strong growth goal should encourage managers to plan for expansion by looking for new market opportunities, for example. Similarly, they must also always be alert for competitive threats and new ideas that will help facilitate future expansion.

Third, goals can serve as sources of motivation to employees of the organization. Goals that are specific and moderately difficult can motivate people to work harder, especially if attaining the goal is likely to result in rewards. The Italian furniture manufacturer Industrie Natuzzi SpA uses goals to motivate its workers. Each craftsperson has a goal for how long it should take to perform her or his job, such as sewing leather sheets together to make a sofa cushion or building wooden frames for chair arms. At the completion of assigned tasks, workers enter their ID numbers and job numbers into the firm's computer system. If they get a job done faster than their goal, a bonus is automatically added to their paycheck.[8]

Finally, goals provide an effective mechanism for evaluation and control. This means that performance can be assessed in the future in terms of how successfully today's goals are accomplished. For example, suppose that officials of the United Way of America set a goal of collecting $250,000 from a particular community. If midway through the campaign they have raised only $50,000, they know that they need to change or intensify their efforts. If they raise only $100,000 by the end of their drive, they will need to study carefully why they did not reach their goal and what they need to do differently next year. On the other hand, if they succeed in raising $265,000, evaluations of their efforts will take on an entirely different character.

Kinds of Goals

Organizations establish many different kinds of goals. In general, these goals vary by level, area, and time frame. Figure 7.2 provides examples of each type of goal for a fast-food chain.

Level Goals are set for and by different levels within an organization. As we noted earlier, the four basic levels of goals are the mission and strategic, tactical, and operational goals. An organization's **mission** is a statement of its "fundamental, unique purpose that sets a business apart from other firms of its type and identifies the scope of the business's operations in product and market terms."[9] For example, the CEO of Monsanto is attempting to reshape his firm's mission by transforming it into what he calls a "life sciences" firm.[10]

mission A statement of an organization's fundamental purpose

strategic goal A goal set by and for top management of the organization

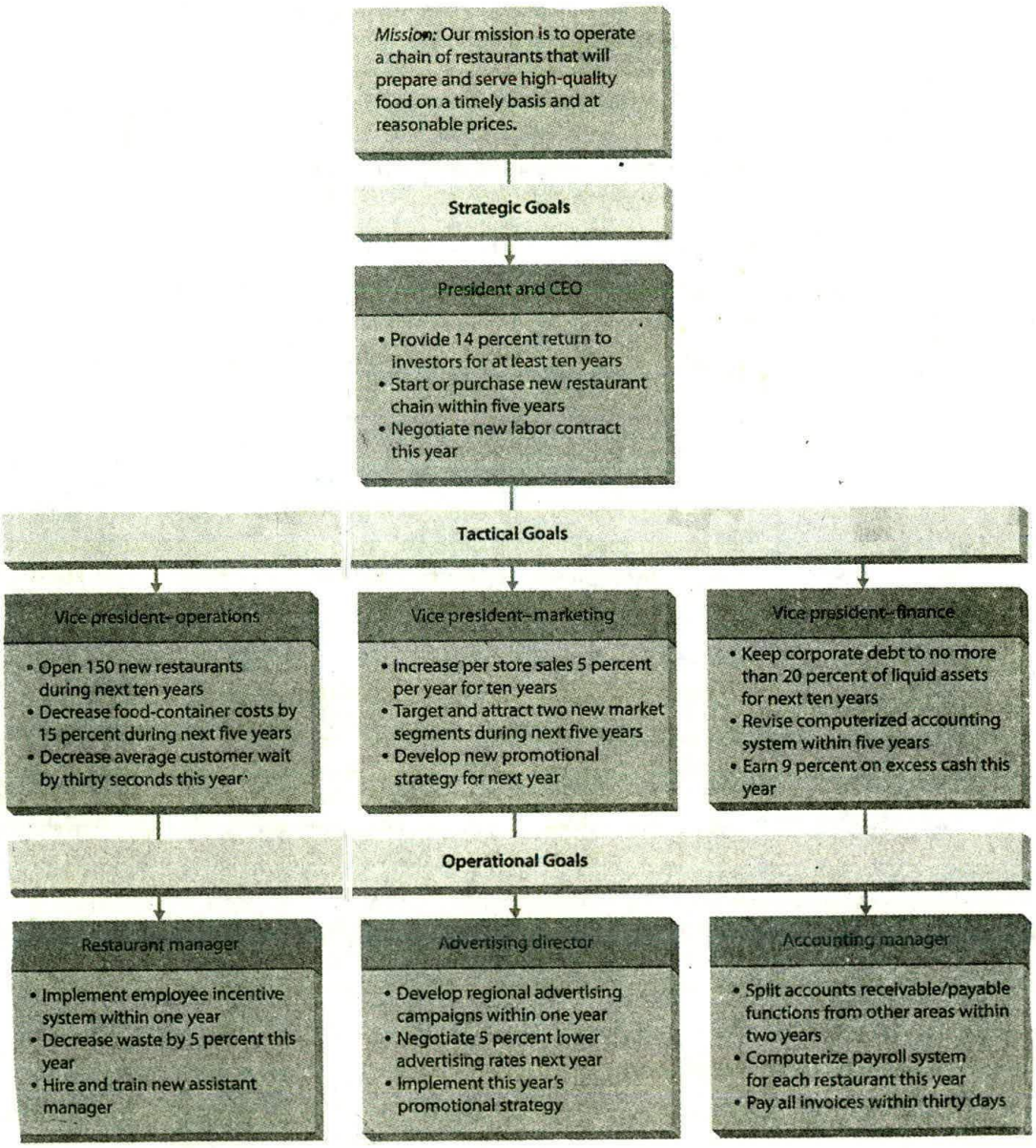
tactical goal A goal set by and for middle managers of the organization

Strategic goals are goals set by and for top management of the organization. They focus on broad, general issues. For example, Procter & Gamble's goal of doubling sales revenues is a strategic goal. **Tactical goals** are set by and for middle managers. Their focus is on how to operationalize actions necessary to achieve

Figure 7.2

Kinds of Organizational Goals for a Regional Fast-Food Chain

Organizations develop many different types of goals. A regional fast-food chain, for example, might develop goals at several different levels and for several different areas.



the strategic goals. Tactical goals at P&G might center around which new products to launch, which existing products to revise, and so forth.

operational goal A goal set by and for lower-level managers of the organization

Operational goals are set by and for lower-level managers. Their concern is with shorter-term issues associated with the tactical goals. An operational goal for P&G might be a target number of new products to launch each of the next five years. (Some managers use the words *objective* and *goal* interchangeably. When they are differentiated, however, the term *objective* is usually used instead of *operational goal*.)

Area Organizations also set goals for different areas. The restaurant chain shown in Figure 7.2 has goals for operations, marketing, and finance. Hewlett-Packard routinely sets production goals for quality, productivity, and so forth. By keeping activities focused on these important areas, H-P has managed to remain competitive against organizations from around the world. Human resource goals might be set for employee turnover and absenteeism. 3M and Rubbermaid set goals for product innovation. Similarly, Beth Pritchard, CEO of Bath & Body works, has a goal that 30 percent of the products sold in the retail outlets each year will be new.[11]

Time Frame Organizations also set goals across different time frames. In Figure 7.2, three goals are listed at the strategic, tactical, and operational levels. The first is a long-term goal, the second an intermediate-term goal, and the third a short-term goal. Some goals have an explicit time frame (i.e., open 150 new restaurants during the next ten years) and others have an open-ended time horizon (i.e., maintain 10 percent annual growth).

Finally, we should also note that the meaning of different time frames varies by level. For example, at the strategic level, long-term often means ten years or longer; intermediate term, around five years or so; and short-term, around one year. But two or three years may be long-term at the operational level, and short-term may mean a matter of weeks or even days.

Responsibilities for Setting Goals

Who sets goals? The answer is actually quite simple: all managers should be involved in the goal-setting process. Each manager, however, generally has responsibilities for setting goals that correspond to his or her level in the organization. The mission and strategic goals are generally determined by the board of directors and top managers. Top and middle managers then work together to establish tactical goals. Finally, middle and lower-level managers are jointly responsible for operational goals. Many managers also set individual goals for themselves. These goals may involve career paths, informal work-related goals outside the normal array of official goals, or just about anything of interest or concern to the manager.

Managing Multiple Goals

Organizations set many different kinds of goals and sometimes experience conflicts or contradictions among goals. Nike had problems with inconsistent goals a few years ago. The firm was producing high-quality shoes (a manufacturing

goal), but they were not particularly stylish (a marketing goal). As a result, the company lost substantial market share when Reebok International started making shoes that were both high quality and fashionable. When Nike management recognized and corrected the inconsistencies, Nike regained its industry standing.

To address such problems, managers must understand the concept of optimizing. **Optimizing** involves balancing and reconciling possible conflicts among goals. Because goals may conflict with one another, the manager must look for inconsistencies and decide whether to pursue one goal to the exclusion of another or to find a midrange target between the extremes. For example, The Home Depot has achieved dramatic success in the retailing industry by offering do-it-yourselfers high-quality home improvement products at low prices and with good service. The firm has recently announced a goal of doubling its revenues from professional contractors. Among its plans are to set up separate checkout areas and to provide special products for contractors. The challenge, however, will be to keep loyal individual customers while also satisfying professional contractors.[12]

optimizing Balancing and reconciling possible conflicts among goals

MANAGEMENT IMPLICATIONS Managers need to appreciate the various purposes that goals play in an organization. They should also appreciate the various kinds of goals that exist. No manager can avoid the goal-setting process because all managers share responsibility for this activity. Finally, managers should also understand that, because some goals may be in conflict with one another, they must be carefully optimized to serve the best overall interests of the organization.

■ Organizational Planning

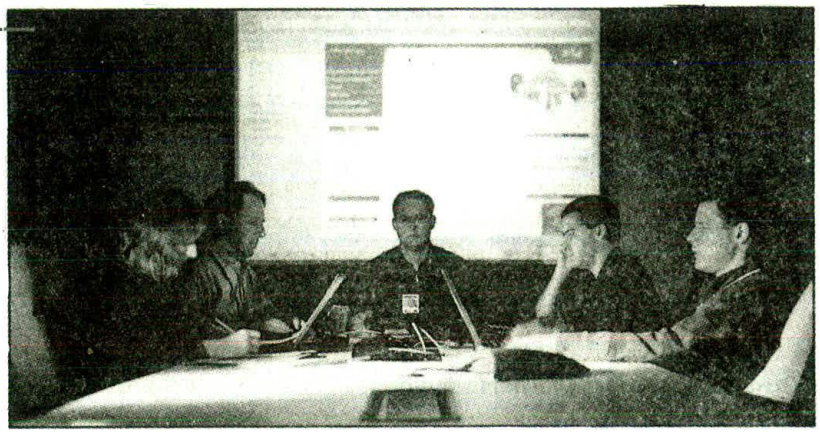
Given the clear link between organizational goals and plans, we now turn our attention to various concepts and issues associated with planning itself. In particular, this section identifies kinds of plans, time frames for planning, who is responsible for planning, and contingency planning.

Kinds of Organizational Plans

Organizations establish many different kinds of plans. At a general level, these include strategic, tactical, and operational plans.

Strategic Plans Strategic plans are the plans developed to achieve strategic goals. More precisely, a **strategic plan** is a general plan outlining decisions of resource allocation, priorities, and action steps necessary to reach strategic goals.[13] These plans are set by the board of directors and top management; generally have an extended time horizon; and address questions of scope, resource deployment, competitive advantage, and synergy. We discuss strategic planning further in Chapter 8.

strategic plan A general plan outlining decisions of resource allocation, priorities, and action steps necessary to reach strategic goals



The processes of setting goals and developing plans involve ongoing and sustained efforts by a variety of managers. Take Intel, for example. Each of the firm's 40,000 employees is equipped with a laptop computer, pager, and cell phone, plus a home PC. Using this technology, Intel employees like these can work together on group projects from anywhere in the world. Hence, they are continuously involved in identifying and developing new business opportunities, seeking new solutions, and enhancing the firm's abilities to compete in an ever-changing world.

tactical plan A plan aimed at achieving tactical goals and developed to implement specific parts of a strategic plan

Tactical Plans A **tactical plan**, aimed at achieving tactical goals, is developed to implement specific parts of a strategic plan. Tactical plans typically involve upper and middle management and, compared with strategic plans, have a somewhat shorter time horizon and a more specific and concrete focus. Thus, tactical plans are concerned more with actually accomplishing tasks than with deciding what to do. Tactical planning is covered in detail in a later section.

operational plan A plan that focuses on carrying out tactical plans to achieve operational goals

Operational Plans An **operational plan** focuses on carrying out tactical plans to achieve operational goals. Developed by middle and lower-level managers, operational plans have a short-term focus and are relatively narrow in scope. Each one deals with a fairly small set of activities. We cover operational planning in more detail later.

Time Frames for Planning

As we previously noted, strategic plans tend to have a long-term focus; tactical plans an intermediate-term focus; and operational plans, a short-term focus. The sections that follow address these time frames in more detail. Of course, we should also remember that time frames vary widely from industry to industry, as discussed more fully in *Working with Diversity.*

long-range plan A plan that covers many years, perhaps even decades; common long-range plans are for five years or more

Long-Range Plans A **long-range plan** covers many years, perhaps even decades. The founder of Matsushita Electric (maker of Panasonic and JVC electronic products), Konosuke Matsushita, once wrote a 250-year plan for his company.[14] Today, however, most managers recognize that environmental change makes it unfeasible to plan too far ahead, but large firms like General Motors and Exxon still routinely develop plans for ten- to twenty-year intervals. GM executives, for example, have a pretty good idea today about new car models that they plan to introduce for at least a decade in advance. The time span for long-range planning

WORKING WITH DIVERSITY

PLANNING AND DECISION MAKING AT INTERNET SPEED

Managers who move from traditional companies to Internet companies must learn how to develop plans and make decisions faster than ever before—working with a mixed management team of web veterans and newcomers. That's what Barbara Hyder found out when she made the transition from international regional president at Mary Kay Cosmetics to CEO of Gloss.com. Although both companies sell cosmetics and personal-care products, Gloss.com's approach to planning and decision making is markedly different, as is the composition of its management team.

When Hyder was at Mary Kay, making a decision to alter a multimillion-dollar advertising campaign would have taken many weeks of discussion and analysis as the issue worked its way through the hierarchy in a series of meetings. In contrast, after Hyder spent five minutes huddling with Gloss.com's president and vice president of marketing, the group agreed to change the company's $20 million advertising plan entirely. Another major decision Hyder faced was whether to launch a new version of the firm's web site, despite some glitches and missing features, or postpone the launch until everything was ready. After listening to both sides during an impromptu twenty-minute management meeting, the CEO decided to go ahead with the launch, citing the highly competitive environment and the opportunity to gain additional consumer feedback.

Although Hyder had years of management and decision-making experience at Mary Kay and earlier at Maybelline, she had no experience with e-commerce before joining Gloss.com. Now she heads a team with managers who are, in some cases, more than a decade younger. She also has to learn their language, the lingo of Internet business that is sprinkled with phrases such as "click-through rates," referring to how many people click on banner advertisements. Just as important, she is bringing with her the language of traditional business that is sprinkled with phrases such as "P&L," referring to profit and loss statements. After all, profitability is the ultimate goal for Gloss.com and its management team.

You have to act quickly; speed is of the essence.

*—Barbara Hyder, CEO, Gloss.com**

Reference: Melanie Warner, "Getting Up to Internet Speed," *Fortune,* January 10, 2000, pp. 185–186 (*quote on p. 185).

varies from one organization to another. For our purposes, we regard any plan that extends beyond five years as long-range. Managers of organizations in complex, volatile environments face a special dilemma. These organizations probably need a longer time horizon than do organizations in less dynamic environments, yet the complexity of their environment makes long-range planning difficult. Managers at these companies therefore develop long-range plans but must also constantly monitor their environment for possible changes.

Intermediate Plans An **intermediate plan** is somewhat less tentative and subject to change than is a long-range plan. Intermediate plans usually cover periods from one to five years and are especially important for middle and first-line managers. Thus, they generally parallel tactical plans. For many organizations intermediate planning has become the central focus of planning activities. Nissan, for example, has fallen far behind its domestic rivals Toyota and Honda in areas like profitability and productivity. To turn things around, the firm has developed

intermediate plan A plan that usually covers periods from one to five years

several plans ranging in duration from two to four years, each intended to improve some part of the company's operations. One plan (three years in duration) involves updating the manufacturing technology used in each Nissan assembly factory. Another (four years in duration) calls for shifting more production to foreign plants to lower labor costs.[15]

short-range plan A plan that generally covers a span of one year or less

action plan A plan used to operationalize any other kind of plan

Short-Range Plans A manager also develops a short-range plan, which has a time frame of one year or less. **Short-range plans** greatly affect the manager's day-to-day activities. There are two basic kinds of short-range plans. An **action plan** operationalizes any other kind of plan. When a specific Nissan plant is ready to have its technology overhauled, its managers focus their attention on replacing the existing equipment with new equipment as quickly and as efficiently as possible to minimize lost production time. In most cases this can be done in a matter of a few months, with actual production being halted only for a few weeks. An action plan thus coordinates the actual changes at a given factory. A **reaction plan**, in turn, is a plan designed to allow the company to react to an unforeseen circumstance. At one Nissan factory the new equipment arrived earlier than expected and plant managers had to shut down production more quickly than expected. These managers thus had to react to events beyond their control in ways that still allowed their goals to be achieved. In fact, reacting to any form of environmental turbulence, as described in Chapter 3, is a form of reaction planning.

reaction plan A plan designed to allow the company to react to an unforeseen circumstance

Responsibilities for Planning

We earlier noted briefly who is responsible for setting goals. We can now expand that initial perspective a bit and examine more fully how different parts of the organization participate in the overall planning process. All managers engage in planning to some degree. Marketing sales managers develop plans for target markets, market penetration, and sales increases. Operations managers plan cost-cutting programs and better inventory control methods. As a general rule, however, the larger an organization becomes, the more the primary planning activities become associated with groups of managers rather than with individual managers.

Planning Staff Some large organizations develop a professional planning staff. Tenneco, General Motors, Disney, Caterpillar, Raytheon, NCR, Ford, and Boeing all have planning staffs.[16] And although the planning staff was pioneered in the United States, foreign firms like Nippon Telegraph & Telephone have also started using them. Organizations might use a planning staff for a variety of reasons. In particular, a planning staff can reduce the workload of individual managers, help coordinate the planning activities of individual managers, bring to a particular problem many different tools and techniques, take a broader view than individual managers, and go beyond pet projects and particular departments.

Planning Task Force Organizations sometimes use a planning task force to help develop plans. Such a task force often comprises line managers with a special interest in the relevant area of planning. The task force may also have members

from the planning staff if the organization has one. A planning task force is most often created when the organization wants to address a special circumstance. For example, when Electronic Data Systems (EDS) decided to expand its information management services to Europe, managers knew that the firm's normal planning approach would not suffice, and top management created a special planning task force. The task force included representatives from each of the major units within the company, the corporate planning staff, and the management team that would run the European operation. Once the plan for entering the European market was formulated and implemented, the task force was eliminated.[17]

Board of Directors Among its other responsibilities, the board of directors establishes the corporate mission and strategy. In some companies the board takes an active role in the planning process. At CBS, for example, the board of directors has traditionally played a major role in planning. In other companies the board selects a competent chief executive and delegates planning to that individual.

Chief Executive Officer The chief executive officer (CEO) is usually the president or the chair of the board of directors. The CEO is probably the single most important individual in any organization's planning process. The CEO plays a major role in the complete planning process and is responsible for implementing the strategy. The board and CEO, then, assume direct roles in planning. The other organizational components involved in the planning process have more of an advisory or consulting role.

Executive Committee The executive committee is usually composed of the top executives in the organization working together as a group. Committee members usually meet regularly to provide input to the CEO on the proposals that affect their own units and to review the various strategic plans that develop from this input. Members of the executive committee are frequently assigned to various staff committees, subcommittees, and task forces to concentrate on specific projects or problems that might confront the entire organization at some time in the future.

Line Management The final component of most organizations' planning activities is line management. Line managers are those persons with formal authority and responsibility for the management of the organization. They play an important role in an organization's planning process for two reasons. First, they are a valuable source of inside information for other managers as plans are formulated and implemented. Second, the line managers at the middle and lower levels of the organization usually must execute the plans developed by top management. Line management identifies, analyzes, and recommends program alternatives, develops budgets and submits them for approval, and finally sets the plans in motion.

Contingency Planning

Another important type of planning is **contingency planning**, or the determination of alternative courses of action to be taken if an intended plan of action is

contingency planning The determination of alternative courses of action to be taken if an intended plan of action is unexpectedly disrupted or rendered inappropriate

unexpectedly disrupted or rendered inappropriate.[18] An excellent example of contingency planning is what was for a while called the Y2K problem. Concerns about the impact of technical glitches in computers stemming from their internal clocks changing from 1999 to 2000 resulted in contingency planning for most organizations. Many banks and hospitals, for example, had extra staff available; some organizations created backup computer systems; and some even stockpiled inventory in case they couldn't purchase new products or materials.[19]

The mechanics of contingency planning are shown in Figure 7.3. In relation to an organization's other plans, contingency planning comes into play at four action points. At action point 1, management develops the basic plans of the organization. These may include strategic, tactical, and operational plans. As part of this development process, managers usually consider various contingency events. Some management groups even assign someone the role of devil's advocate to ask, "But what if . . ." about each course of action. A variety of contingencies are usually considered.

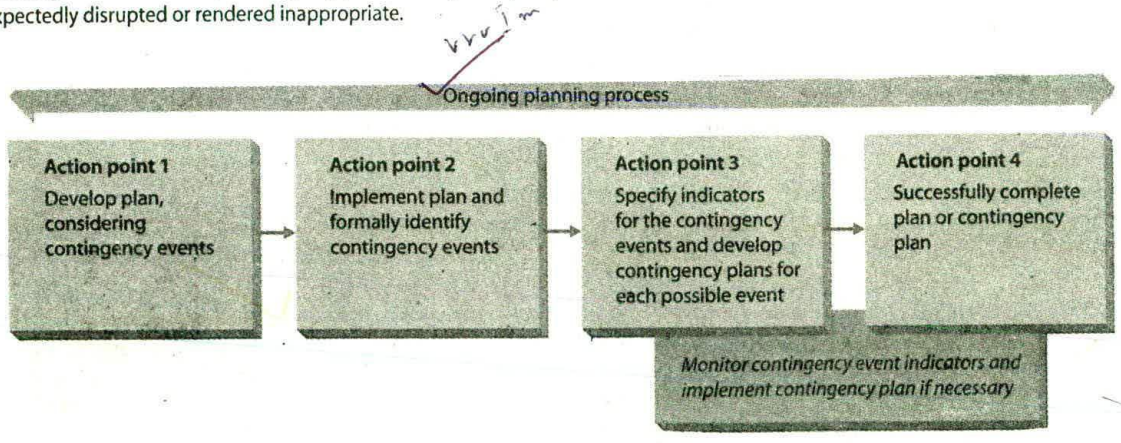
At action point 2, the plan that management chooses is put into effect. The most important contingency events are also defined. Only the events that are likely to occur and whose effects will have a substantial impact on the organization are used in the contingency-planning process. Next, at action point 3, the company specifies certain indicators or signs that suggest that a contingency event is about to take place. A bank might decide that a 2-percent drop in interest rates should be considered a contingency event. An indicator might be two consecutive months with a drop of 0.5 percent in each. As indicators of contingency events are being defined, the contingency plans themselves should also be developed. Examples of contingency plans for various situations are delaying plant construction, developing a new manufacturing process, and cutting prices.

After this stage, the managers of the organization monitor the indicators identified at action point 3. If the situation dictates, a contingency plan is implemented.

Figure 7.3

Contingency Planning

Most organizations develop contingency plans. These plans specify alternative courses of action to be taken if an intended plan is unexpectedly disrupted or rendered inappropriate.



Otherwise the primary plan of action continues in force. Finally, action point 4 marks the successful completion of either the original or a contingency plan.

Contingency planning is becoming increasingly important for most organizations and especially for those operating in particularly complex or dynamic environments. Few managers have such an accurate view of the future that they can anticipate and plan for everything. Contingency planning is a useful technique for helping managers cope with uncertainty and change.

MANAGEMENT Managers should understand that organizations rely on several different kinds of plans that span different levels and different time frames. Similarly, they should also recognize that different managers are responsible for different kinds of planning activities, and they should be ready and prepared to play an appropriate role. In addition, all managers should understand that the potential for unexpected events makes it important to develop contingency plans.

■ Tectical Planning

As we noted earlier, tactical plans are developed to implement specific parts of a strategic plan. You have probably heard the saying about winning the battle but losing the war. Tactical plans are to battles what strategy is to a war: an organized sequence of steps designed to execute strategic plans. Strategy focuses on resources, environment, and mission, whereas tactics focus primarily on people and action.[20] Figure 7.4 identifies the major elements in developing and executing tactical plans.

Developing Tactical Plans

Although effective tactical planning depends on many factors that vary from one situation to another, we can identify some basic guidelines. First, the manager needs to recognize that tactical planning must address a number of tactical goals derived from a broader strategic goal.[21] An occasional situation may call for a stand-alone tactical plan, but most of the time tactical plans flow from and must be consistent with a strategic plan.

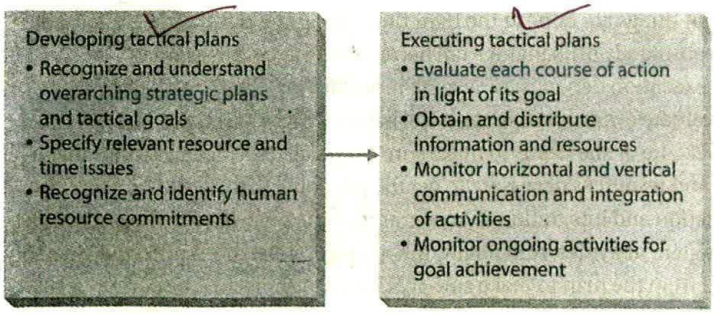


Figure 7.4

Developing and Executing Tactical Plans

Tactical plans are used to accomplish specific parts of a strategic plan. Each strategic plan is generally implemented through several tactical plans. Effective tactical planning involves both development and execution.

For example, a few years ago top managers at Coca-Cola developed a strategic plan for maintaining the firm's dominance of the soft-drink industry. As part of developing the plan, they identified a critical environmental threat—considerable unrest and uncertainty among the independent bottlers who packaged and distributed Coca-Cola's products. To counter this threat and strengthen the company's position simultaneously, Coca-Cola bought several large independent bottlers and combined them into one new organization called Coca-Cola Enterprises. Selling half of the new company's stock reaped millions in profits while still effectively keeping control of the enterprise in Coca-Cola's hands. Thus, the creation of the new business was a tactical plan developed to contribute to the achievement of an overarching strategic goal.[22]

Second, although strategies are often stated in general terms, tactics must specify resources and time frames. A strategy can call for being number one in a particular market or industry, but a tactical plan must specify precisely what activities will be undertaken to achieve that goal. Consider the Coca-Cola example again. Another element of its strategic plan involves increased worldwide market share. To facilitate additional sales in Europe, managers developed tactical plans for building a new plant in the south of France to make soft-drink concentrate and for building another canning plant in Dunkirk. Building these plants represents a concrete action involving measurable resources (i.e., funds to build the plants) and a clear time horizon (i.e., a target date for completion).

Finally, tactical planning requires the use of human resources. Managers involved in tactical planning spend a great deal of time working with other people. They must be in a position to receive information from others in and outside the organization, process that information in the most effective way, and then pass it on to others who might make use of it. Coca-Cola executives have been intensively involved in planning the new plants, setting up the new bottling venture noted earlier, and exploring a joint venture with Cadbury Schweppes in the United Kingdom. Each activity has required considerable time and effort from dozens of managers. One manager, for example, crossed the Atlantic twelve times while negotiating the Cadbury deal.

Executing Tactical Plans

Regardless of how well a tactical plan is formulated, its ultimate success depends on the way it is carried out. Successful implementation, in turn, depends on the astute use of resources, effective decision making, and insightful steps to ensure that the right things are done at the right time and in the right ways. A manager can see an absolutely brilliant idea fail because of improper execution.

Proper execution depends on several important factors. First, the manager needs to evaluate every possible course of action in light of the goal it is intended to reach. Next, he or she needs to make sure that each decision maker has the information and resources necessary to get the job done. Vertical and horizontal communication and integration of activities must be present to minimize conflict and inconsistent activities. And finally, the manager must monitor ongoing activities derived from the plan to make sure that they are achieving the desired results.

This monitoring typically takes place within the context of the organization's ongoing control systems.

For example, managers at The Walt Disney Company recently developed a new strategic plan aimed at spurring growth and profits from foreign markets. One tactical plan developed to stimulate growth involves expanding the cable Disney Channel into more and more foreign markets; another involves building a new theme park near Hong Kong. Although expanding cable television and building a new theme park are big undertakings in their own right, they are still tactical plans within the overall strategic plan focusing on international growth.[23]

MANAGEMENT IMPLICATIONS While strategic planning is, of course, critical to the success of any organization, tactical planning often makes the difference in how well strategies actually work. Thus, tactical plans should be developed and executed with as much care as the organization devotes to other kinds of planning.

■ Operational Planning

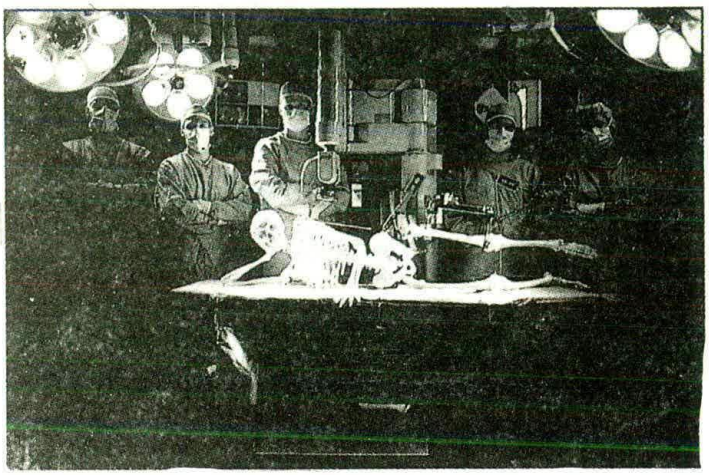
Another critical element in effective organizational planning is the development and implementation of operational plans. Operational plans are derived from tactical plans and are aimed at achieving operational goals. Thus, operational plans tend to be narrowly focused, have relatively short time horizons, and involve lower-level managers. The two most basic forms of operational plans and specific types of each are summarized in Table 7.1.

Table 7.1

Types of Operational Plans

Organizations develop various operational plans to help achieve operational goals. In general, there are two types of single-use plans and three types of standing plans.

Plan	Description
Single-use plan	Developed to carry out a course of action not likely to be repeated in the future
Program	Single-use plan for a large set of activities
Project	Single-use plan of less scope and complexity than a program
Standing plan	Developed for activities that recur regularly over a period of time
Policy	Standing plan specifying the organization's general response to a designated problem or situation
Standard operating procedure	Standing plan outlining steps to be followed in particular circumstances
Rules and regulations	Standing plans describing exactly how specific activities are to be carried out



Many surgeons rely heavily on standard operating procedures. For example, these doctors specialize in hip replacement surgeries. A modified industrial robot, shown above the skeleton, is used to drill a precise hole in a femur so that the implant can be fitted exactly as the doctors want it. A clearly defined set of procedures guides the team through every surgery it conducts. At the same time, however, the doctors are also prepared to deviate from established procedures as circumstances warrant.

Single-Use Plans

A **single-use plan** is developed to carry out a course of action that is not likely to be repeated in the future. As Disney proceeds with its new theme park in Hong Kong, it will develop numerous single-use plans for individual rides, attractions, and hotels. The two most common forms of single-use plans are programs and projects.

Programs A **program** is a single-use plan for a large set of activities. It might consist of identifying procedures for introducing a new product line, opening a new facility, or changing the organization's mission. As part of its own strategic plans for growth, Black & Decker bought General Electric's small-appliance business. The deal involved the largest brand-name switch in history: 150 products were converted from GE to the Black & Decker label. Each product was carefully studied, redesigned, and reintroduced with an extended warranty. A total of 140 steps were used for each product. It took three years to convert all 150 products over to Black & Decker. The total conversion of the product line was a program.

single-use plan Developed to carry out a course of action that is not likely to be repeated in the future

program A single-use plan for a large set of activities

project A single-use plan of less scope and complexity than a program

Projects A **project** is similar to a program but is generally of less scope and complexity. A project may be part of a broader program, or it may be a self-contained single-use plan. For Black & Decker, the conversion of each of the 150 products was a separate project in its own right. Each product had its own manager, its own schedule, and so forth. Projects are also used to introduce a new product within an existing product line or to add a new benefit option to an existing salary package.

Standing Plans

standing plan Developed for activities that recur regularly over a period of time

Whereas single-use plans are developed for nonrecurring situations, a **standing plan** is developed for activities that recur regularly over a period of time. Standing plans can greatly enhance efficiency by routinizing decision making. Policies, standard operating procedures, and rules and regulations are three kinds of standing plans.

policy A standing plan that specifies the organization's general response to a designated problem or situation

Policies As a general guide for action, a policy is the most general form of standing plan. A **policy** specifies the organization's general response to a designated problem or situation. For example, McDonald's has a policy that it will not grant a franchise to an individual who already owns another fast-food restaurant. Similarly, Starbucks' has a policy that it will not franchise at all, instead, retaining own-



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ership of all Starbucks' coffee shops. Likewise, a university admissions office might establish a policy that admission will be granted only to applicants with a minimum SAT score of 1,000 and a ranking in the top quarter of their high-school classes. Admissions officers may routinely deny admission to applicants who fail to reach these minimum requirements. A policy is also likely to describe how exceptions are to be handled. The university's policy statement, for example, might create an admissions appeals committee to evaluate applicants who do not meet minimum requirements but may warrant special consideration.

Standard Operating Procedures Another type of standing plan is the **standard operating procedure**, or **SOP**. An SOP is more specific than a policy because it outlines the steps to be followed in particular circumstances. The admissions clerk at the university, for example, might be told that when an application is received, he or she should (1) set up a file for the applicant; (2) add test-score records, transcripts, and letters of reference to the file as they are received; and (3) give the file to the appropriate admissions director when it is complete. Gallo Vineyards in California has a three-hundred-page manual of standard operating procedures. This planning manual is credited with making Gallo one of the most efficient wine operations in the United States. McDonald's has SOPs explaining exactly how Big Macs are to be cooked, how long they can stay in the warming rack, and so forth.

Standard operating procedures, rules, and regulations can all be useful methods for saving time, improving efficiency, and streamlining decision making and planning. But it is also helpful to review SOPs, rules, and regulations periodically to ensure that they remain useful. For example, as shown in this cartoon, an SOP for regularly ordering parts and supplies may become less effective if the demand for those parts and supplies changes or disappears.

standard operating procedure (SOP) A standing plan that outlines the steps to be followed in particular circumstances

Rules and Regulations The narrowest of the standing plans, **rules and regulations** describe exactly how specific activities are to be carried out. Rather than guiding decision making, rules and regulations actually take the place of decision making in various situations. Each McDonald's restaurant has a rule prohibiting customers from using its telephones, for example. The university admissions office might have a rule stipulating that if an applicant's file is not complete two months before the beginning of a semester, the student cannot be admitted until the next semester. Of course, in most organizations a manager at a higher level can suspend or bend the rules. If the high-school transcript of the child of a prominent university alumnus and donor arrives a few days late, the director of admissions might waive the two-month rule. Rules and regulations can become problematic if they are excessive or enforced too rigidly.

rules and regulations Describe exactly how specific activities are to be carried out

Rules and regulations and SOPs are similar in many ways. They are both relatively narrow in scope, and each can serve as a substitute for decision making. An SOP typically describes a sequence of activities, whereas rules and regulations focus on one activity. Recall our examples: the admissions-office SOP consisted of three activities, whereas the two-month rule related to one activity only. In an industrial setting, the SOP for orienting a new employee could involve enrolling the person in various benefit options, introducing him or her to coworkers and supervisors, and providing a tour of the facilities. A pertinent rule for the new employee might involve the starting time for work each day.

MANAGEMENT IMPLICATIONS Managers need to understand the various kinds of operating plans that organizations use. This understanding should enable them to assess when to use operating plans. At the same time, managers should be flexible about how they use operating plans.

■ Managing Goal-Setting and Planning Processes

Obviously, all the elements of goal setting and planning discussed to this point involve managing these processes in some way or another. In addition, however, because major barriers sometimes impede effective goal setting and planning, knowing how to overcome some of the barriers is important.

Barriers to Goal Setting and Planning

Several circumstances can serve as barriers to effective goal setting and planning; the more common ones are listed in Table 7.2. The *World of Management* also discusses barriers to goal setting and planning.

Table 7.2

Barriers to Goal Setting and Planning

As part of managing the goal-setting and planning processes, managers must understand the barriers that can disrupt them. Managers must also know how to overcome the barriers.

Major barriers	Inappropriate goals Improper reward system Dynamic and complex environment Reluctance to establish goals Resistance to change Constraints
Overcoming the barriers	Understanding the purposes of goals and planning Communication and participation Consistency, revision, and updating Effective reward systems

WORLD OF MANAGEMENT

PLANNING FOR OPEN COMPETITION IN CHINA

As the date approaches for China to open its doors to international competition, managers of many local companies are worried about their ability to fight off foreign rivals. Not Tsingtao Brewery. After years of battling U.S., German, and other beer brands that have targeted internal Chinese markets, Tsingtao's top managers have become seasoned veterans in developing plans for managing the beer business at home and abroad.

Tsingtao's planning process was less formal in the days before foreign competition. Domestic beer consumption was on the rise, so management mostly cranked up production in response to orders that came in from distributors around the country. The company was also exporting to the United States, where its beer is sold in Chinese restaurants. Once experienced global giants such as Anheuser-Busch and Heineken began selling their beers in China, however, Tsingtao was forced to tighten its planning procedures. Even so, sales and profits plummeted during the first few years of all-out competition. Then new management came in, bringing new ideas and a more disciplined approach to setting and meeting goals for matching production to demand. In this way, Tsingtao could lower its inventory costs and keep fresh beer on store shelves.

Thanks to better planning and implementation, Tsingtao's output, sales, and profits have risen dramatically in recent years. At the same time, the company is planning for future growth by buying up struggling breweries all over China. Now the once-robust domestic beer market is showing signs of going flat, which means Tsingtao's managers will have to sharpen their planning skills yet again to stay ahead of non-Chinese beer makers.

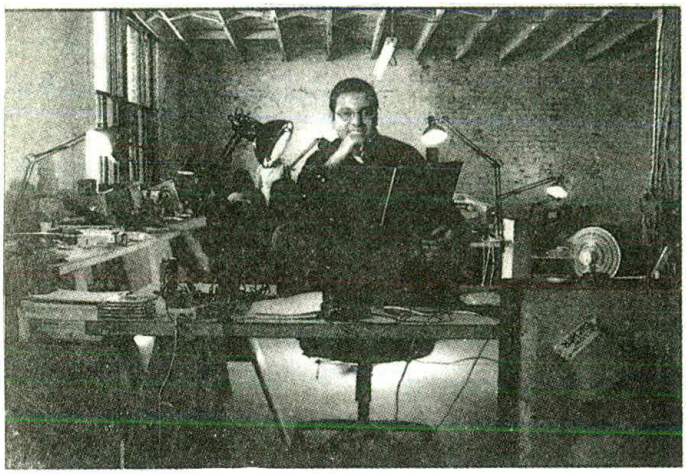
Some industries are afraid of foreign competition. Competing with foreign brands, we learned how markets worked.

—Peng Zuo Yi, CEO, Tsingtao Brewery*

Reference: Paul Wiseman, "Chinese Beer Barrels Up to the World's Bar," *USA Today*, January 18, 2000, pp. 1B, 2B (*quote on p. 1B).

Inappropriate Goals Inappropriate goals come in many forms. Paying a large dividend to stockholders may be inappropriate if it comes at the expense of research and development. Goals may also be inappropriate if they are unattainable. If Kmart were to set a goal of having more revenues than Wal-Mart next year, employees at the company would probably be embarrassed because achieving such a goal would be impossible. Goals may also be inappropriate if they place too much emphasis on either quantitative or qualitative measures of success. Some goals, especially those relating to financial areas, are quantifiable, objective, and verifiable. Other goals, such as employee satisfaction and development, are difficult if not impossible to quantify. Organizations are asking for trouble if they put too much emphasis on one type of goal to the exclusion of the other.

Improper Reward System In some settings, an improper reward system acts as a barrier to goal setting and planning. For example, people may inadvertently be rewarded for poor goal-setting behavior or be unrewarded or even punished for proper goal-setting behavior. Suppose that a manager sets a goal of decreasing turnover next year. If turnover is decreased by even a fraction, the manager can claim success and perhaps be rewarded for the accomplishment. In contrast, a



A dynamic and complex environment is one of the most challenging barriers to effective goal-setting and planning. Consider, for example, the situation faced by Salim Teja, co-founder and chief strategist of Accompany, a Silicon Valley-based online buying club. He took Accompany from an abstract concept to a going concern in less than three months. Teja has had to shift his firm's strategy several times, sometimes within a matter of hours, because of environmental shifts and changes. He uses e-mail to communicate these shifts to Accompany workers immediately, in part so they can better perform their jobs and in part so that they feel more invested in the outcome.

manager who attempts to decrease turnover by 5 percent but actually achieves a decrease of only 4 percent may receive a smaller reward because of her or his failure to reach the established goal. And if an organization places too much emphasis on short-term performance and results, managers may ignore longer-term issues as they set goals and formulate plans to achieve higher profits in the short-term.

Dynamic and Complex Environment The nature of an organization's environment is also a barrier to effective goal setting and planning. Rapid change, technological innovation, and intense competition can each increase the difficulty of an organization accurately assessing future opportunities and threats. For example, when an electronics firm like IBM develops a long-range plan, it tries to take into account how much technological innovation is likely to occur during that interval. But forecasting such events is extremely difficult. During the early boom years of personal computers, data were stored primarily on floppy disks. Because these disks had a limited storage capacity, hard disks were developed. Whereas the typical floppy disk can hold hundreds of pages of information, a hard disk can store thousands of pages. Today computers increasingly store information on optical disks that hold millions of pages. The manager attempting to set goals and plan in this rapidly changing environment faces a truly formidable task. *Management InfoTech* presents several pertinent examples illustrating how hard it is to predict the future, especially where technology is concerned!

Reluctance to Establish Goals Another barrier to effective planning is the reluctance of some managers to establish goals for themselves and their units of responsibility. The reason for this reluctance may be lack of confidence or fear of failure. If a manager sets a goal that is specific, concise, and time related, then whether he or she attains it is obvious. Managers who consciously or unconsciously try to avoid this degree of accountability are likely to hinder the organization's planning efforts. Pfizer, a large pharmaceutical company, ran into problems because its managers did not set goals for research and development. Consequently, the organization fell further and further behind because managers had no way of knowing how effective their R&D efforts actually were.

Resistance to Change Another barrier to goal setting and planning is resistance to change. Planning essentially involves changing something about the organization. As we will see in Chapter 13, people tend to resist change. Avon Products almost drove itself into bankruptcy several years ago because it insisted on contin-

MANAGEMENT INFOTECH

A Few Poorly Chosen Words from the Past

Today is full of blind spots. So was yesterday, the year before, the century before that, the millennium before that. The future is perpetually around the corner, invisible to mere mortals, no matter how wise.

To wit, these pratfalls (culled from the Internet, various media, and Herb London, publisher of *American Outlook* magazine):

"Drill for oil? You mean drill into the ground to try and find oil? You're crazy."

—Workers to railroad conductor Edwin Drake before he drilled the first successful U.S. oil, 1859

"Well-informed people know it is impossible to transmit the voice over wires and that were it possible to do so, the thing would be of no practical value."

—Boston Post, *1865*

"Heavier-than-air flying machines are impossible."

*—**Lord Kelvin** of the British Royal Society, one of the nineteenth century's top experts on thermodynamics, 1890s*

"The world is coming to an end in 1950."

*—Historian **Henry Adams**, 1903*

"There is no likelihood man can ever tap the power of the atom."

*—Nobel Prize–winning physicist **Robert Milliken**, 1923*

"Who the hell wants to hear actors talk?"

*—**H. M. Warner**, Warner Bros., 1927*

"A rocket will never be able to leave the earth's atmosphere."

—The New York Times, *1936*

"I think there is a world market for maybe five computers."

*—IBM's **Thomas Watson**, 1943*

"Television won't last because people will soon get tired of staring at a plywood box every night."

*—Producer **Darryl Zanuck**, 20th Century Fox, 1946*

"If excessive smoking actually plays a role in the production of lung cancer, it seems to be a minor one."

*—**W. C. Heuper**, National Cancer Institute, 1954*

"You ain't going nowhere, son. You ought to go back to driving a truck."

*—The Grand Ole Opry's **Jim Dunny** to **Elvis Presley**, 1954*

Everything that can be invented has been invented.

—Charles Duell, director of the U.S. patent office, 1899

"By 2000, politics will simply fade away. We will not see any political parties."

*—Visionary and inventor **R. Buckminster Fuller**, 1966*

"There is no need for any individual to have a computer in their home."

*—**Ken Olson**, president of Digital Equipment Corp., 1977*

"640K ought to be enough for anybody."

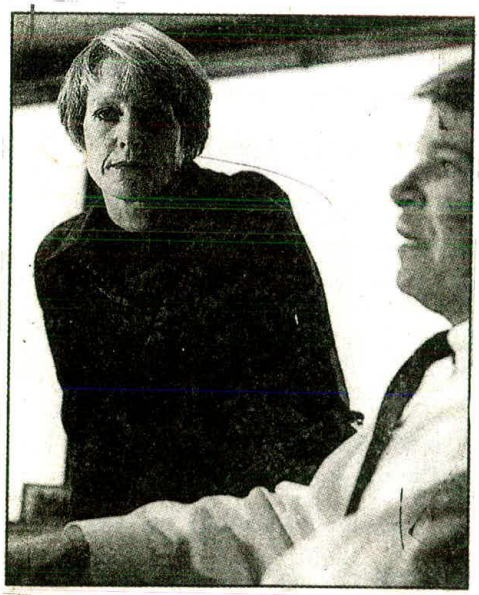
*—Microsoft's **Bill Gates**, 1981, whose computers now offer more than five hundred times that much memory*

Reference: *USA Today*, Tuesday, November 23, 1999, p. 5D. Copyright 1999, *USA Today*. Reprinted with permission.

uing a policy of large dividend payments to its stockholders. When profits started to fall, managers resisted cutting the dividends and started borrowing to pay them. The company's debt grew from $3 million to $1.1 billion in eight years. Eventually, managers were forced to confront the problem and cut dividends.

Constraints Constraints that limit what an organization can do are another major obstacle. Common constraints include a lack of resources, government restrictions, and strong competition. For example, Owens-Corning Fiberglass Corp. took on an enormous debt burden as part of its fight to avoid a takeover by Wickes Companies. The company then had such a large debt that it was forced to cut back on capital expenditures and research and development. Those cutbacks greatly constrained what the firm can plan for the future. Time constraints are also a factor. It's easy to say, "I'm too busy to plan today; I'll do it tomorrow." Effective planning takes time, energy, and an unwavering belief in its importance.

Establishing goals and then working to achieve them play very important roles in organizational success. Some managers, however, have difficulty in setting meaningful goals. To enhance their abilities to set and achieve goals, some managers are starting to rely on executive coaches—essentially personal consultants who help them function more effectively. When Cheryl Weir started working with Charles Cleary at AT&T, she was unimpressed with his vague goal for his unit of "being number 1" or achieving what she saw as unambitious growth of 5 percent. She led him to set a growth goal of 16 percent and develop a plan for achieving it; and when they met this goal, Cleary's unit was among the top three in the company.



Overcoming the Barriers

Fortunately, there are several guidelines for making goal setting and planning effective. Some of the guidelines are also listed in Table 7.2.

Understand the Purposes of Goals and Plans One of the best ways to facilitate goal-setting and planning processes is to recognize their basic purposes. Managers should also recognize that there are limits to the effectiveness of setting goals and making plans. Planning is not a panacea that will solve all of an organization's problems, nor is it an iron-clad set of procedures to be followed at any cost. And effective goals and planning do not necessarily ensure success; adjustments and exceptions are to be expected over time. For example, Coca-Cola once followed a logical and rational approach to setting goals and planning a few years ago when it introduced a new formula to combat Pepsi's increasing market share. But all the plans proved to be wrong as consumers rejected the new version of Coca-Cola. Managers quickly reversed the decision and reintroduced the old formula as Coca-Cola Classic. And it has a larger market share today than before. Even though careful planning resulted in a big mistake, the company came out ahead in the long run.

Communication and Participation Although goals and plans may be initiated at high levels, they must also be communicated to others in the organization. Everyone involved in the planning process should know what the overriding organizational strategy is, what the various functional strategies are, and how they are all to be integrated and coordinated. People responsible for achieving goals and implementing plans must have a voice in developing them from the outset. These individuals almost always have valuable information to contribute, and because they will be implementing the plans, their involvement is critical: people are usually more committed to plans that they have helped shape. Even when an organization is

somewhat centralized or uses a planning staff, managers from a variety of levels in the organization should be involved in the planning process. When Compaq Computer set a strategic goal of moving from the number five to the number three position in the computer industry, it developed a detailed brochure explaining the goal and how it was to be achieved and distributed it to every employee in the company.

Consistency, Revision, and Updating Goals should be consistent both horizontally and vertically. Horizontal consistency means that goals should be consistent across the organization, from one department to the next. Vertical consistency means that goals should be consistent up and down the organization: strategic, tactical, and operational goals must agree with one another. Because goal setting and planning are dynamic processes, they must also be revised and updated regularly. Many organizations are seeing the need to revise and update on an increasingly frequent basis. Citicorp, for example, once used a three-year planning horizon for developing and providing new financial services. That cycle has been cut to two years, and the bank hopes to reduce it to one year very soon.

Effective Reward Systems In general, people should be rewarded both for establishing effective goals and plans and for successfully achieving them. Because failure sometimes results from factors outside the manager's control, however, people should also be assured that failure to reach a goal will not necessarily bring punitive consequences. Frederick Smith, founder and CEO of Federal Express, has a stated goal of encouraging risk. Thus, when Federal Express lost $233 million on an unsuccessful new service called ZapMail, no one was punished. Smith believed that the original idea was a good one but was unsuccessful for reasons beyond the company's control.

Using Goals to Implement Plans

Goals are often used to implement plans. Formal goal-setting programs represent one widely used method for managing the goal-setting and planning processes concurrently to ensure that both are done effectively. Some firms call this approach *management by objectives*, or *MBO*. We should also note, however, that while many firms use this basic approach, they frequently tailor it to their own special circumstances and use a special term or name for it.[24] For example, Tenneco uses an MBO-type system but calls it the Performance Agreement System, or PAS.

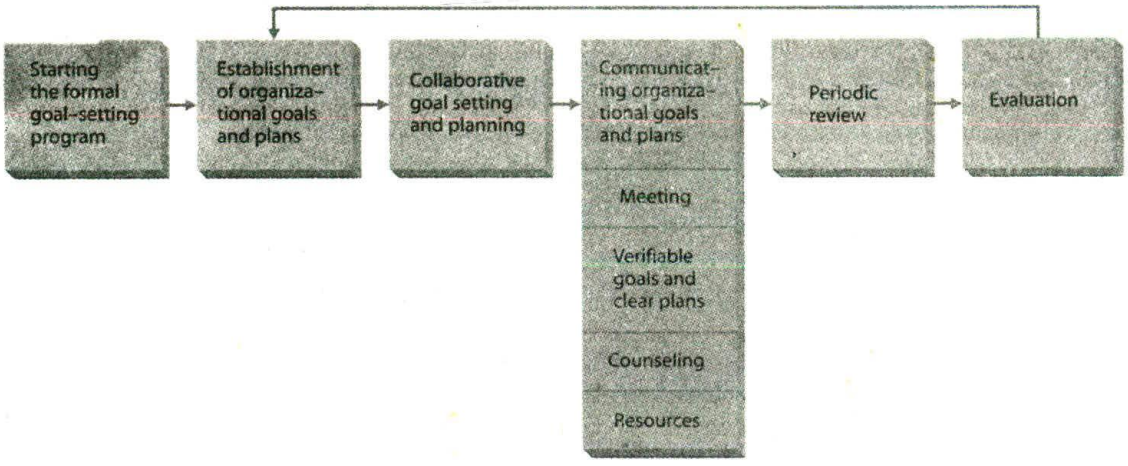
The Nature and Purpose of Formal Goal Setting The purpose of formal goal setting is generally to give subordinates a voice in the goal-setting and planning processes and to clarify for them exactly what they are expected to accomplish in a given time span. Thus, formal goal setting is often concerned with goal setting and planning for individual managers and their units or work groups.

The Formal Goal-Setting Process The basic mechanics of the formal goal-setting process are shown in Figure 7.5. This process is described here from an

Figure 7.5

The Formal Goal-Setting Process

Formal goal-setting is an effective technique for integrating goal setting and planning. This figure portrays the general steps that most organizations use when they adopt formal goal-setting. Of course, most organizations adapt this general process to fit their own unique needs and circumstances.



ideal perspective. In any given organization, the steps of the process are likely to vary in importance and may even take a different sequence. As a starting point, however, most managers believe that if a formal goal-setting program is to be successful, it must start at the top of the organization. Top managers must communicate why they have adopted the program, what they think it will do, and that they have accepted and are committed to formal goal setting. Employees must also be educated about what goal setting is and what their role in it will be. Having committed to formal goal setting, managers must implement it in a way that is consistent with overall organizational goals and plans. The idea is that goals set at the top will systematically cascade down throughout the organization.

Although establishing the organization's basic goals and plans is extremely important, collaborative goal setting and planning are the essence of formal goal setting. The collaboration involves a series of distinct steps. First, managers tell their subordinates what organizational and unit goals and plans top management has established. Then managers meet with their subordinates on a one-to-one basis to arrive at a set of goals and plans for each subordinate that both the subordinate and the manager have helped develop and to which both are committed. Next the goals are refined to be as verifiable (quantitative) as possible and to specify a time frame for their accomplishment. They should also be written. Further, the plans developed to achieve the goals need to be stated as clearly as possible and must relate directly to each goal. Managers must play the role of counselors in the goal-

setting and planning meeting. For example, they must ensure that the subordinate's goals and plans are attainable and workable and that they will facilitate both the unit's and the organization's goals and plans. Finally, the meeting should spell out the resources that the subordinate will need to implement his or her plans and work effectively toward goal attainment.

Conducting periodic reviews as subordinates are working toward their goals is advisable. If the goals and plans are for a one-year period, meeting quarterly to discuss progress may be a good idea. At the end of the period, the manager meets with each subordinate again to review the degree of goal attainment. They discuss which goals were met and which were not met in the context of the original plans. The reasons for both success and failure are explored, and the employee is rewarded on the basis of goal attainment. In an ongoing goal setting program, the evaluation meeting may also serve as the collaborative goal-setting and planning meeting for the next time period.

The Effectiveness of Formal Goal Setting Many organizations, including Cypress Semiconductor, Alcoa, Tenneco, Du Pont, General Motors, Boeing, Caterpillar, Westinghouse Electric, and Black & Decker, all use some form of goal setting. As might be expected, goal setting has both strengths and weaknesses. A primary benefit of goal setting is improved employee motivation. By clarifying exactly what is expected, by allowing the employee a voice in determining expectations, and by basing rewards on the achievement of those expectations, organizations create a powerful motivational system for their employees.

Communication is also enhanced through the process of discussion and collaboration. And performance appraisals may be done more objectively, with less reliance on arbitrary or subjective assessment. Goal setting focuses attention on appropriate goals and plans, helps identify superior managerial talent for future promotion, and provides a systematic management philosophy that can have a positive effect on the overall organization. Goal setting also facilitates control, The periodic development and subsequent evaluation of individual goals and plans helps keep the organization on course toward its own long-run goals and plans.

On the other hand, goal setting occasionally fails because of poor implementation. Perhaps the major problem that can derail a goal-setting program is lack of top-management support. Some organizations decide to use goal setting, but then its implementation is delegated to lower management. This approach limits the program's effectiveness because the goals and plans cascading throughout the organization may not actually be the goals and plans of top management and because others in the organization are not motivated to accept and become committed to them. Another problem with goal setting is that some firms overemphasize quantitative goals and plans and burden their systems with too much paperwork and record keeping. Some managers will not or cannot sit down and work out goals and plans with their subordinates. Rather, they "suggest" or even "assign" goals and plans to people. The result is resentment and a lack of commitment to the goal-setting program.[25]

MANAGEMENT IMPLICATIONS Managers need to understand that various barriers to effective goal setting and planning can exist in any organization. They should also, of course, know how to overcome these barriers. Finally, they should recognize that goals can be used to implement plans, especially through a comprehensive goal-setting system.

Summary of Key Points

The planning process is the first basic managerial function that organizations must address. With an understanding of the environmental context, managers develop several different types of goals and plans. Decision making is the underlying framework of all planning because every step of the planning process involves a decision.

Goals serve four basic purposes: to provide guidance and direction, to facilitate planning, to inspire motivation and commitment, and to promote evaluation and control. Goals can be differentiated by level, area, and time frame. All managers within an organization need to be involved in the goal-setting process. Managers need to pay special attention to the importance of managing multiple goals through optimizing and other approaches.

Goals are closely related to planning. The major types of plans are strategic, tactical, and operational. Plans are developed across a variety of time horizons, including long-range, intermediate, and short-range time frames. Essential people in an organization responsible for effective planning are the planning staff, planning task forces, the board of directors, the CEO, the executive committee, and line management. Contingency planning helps managers anticipate and plan for unexpected changes.

After plans have been developed, the manager must address how they will be achieved. This implementation often involves tactical and operational plans. Tactical plans occur at the middle of the organization and have an intermediate time horizon and moderate scope. Tactical plans are developed to implement specific parts of a strategic plan. They must flow from strategy, specify resource and time issues, and commit human resources. Tactical plans must be effectively executed.

Operational plans occur at the lower levels of the organization, have a shorter time horizon, and are narrower in scope. Operational plans are derived from a tactical plan and are aimed at achieving one or more operational goals. Two major types of operational plans are single-use and standing plans. Single-use plans are designed to carry out a course of action that is not likely to be repeated in the future. Programs and projects are examples of single-use plans. Standing plans are designed to carry out a course of action that is likely to be repeated several times. Policies, standard operating procedures, and rules and regulations are all standing plans.

Several barriers exist to effective goal setting and planning. These barriers include inappropriate goals, an improper reward system, a dynamic and complex environment, reluctance to establish goals, resistance to change, and various constraints. Methods for overcoming these barriers include understanding the purposes of goals and plans; communication and participation; consistency, revision, and updating; and an effective reward system. One particularly useful technique for managing goal setting and planning is formal goal setting, a process of collaborative goal setting and planning.

Discussion Questions

Questions for Review

1. Describe the nature of organizational goals. Be certain to include both the purposes and kinds of goals.
2. What is contingency planning? Is being flexible about your plans the same as contingency planning? Why or why not?
3. What is tactical planning? What is operational planning? What are the similarities and differences between them?
4. What are the barriers to goal setting and planning? How can they be overcome? Can you think of any ways to overcome the barriers other than the ways identified in the text?

Questions for Analysis

5. Almost by definition, organizations cannot accomplish all of their goals. Why?
6. Which kind of plan—tactical or operational—should an organization develop first? Why? Does the order of development really make a difference as long as plans of both types are made?
7. Think of examples of each type of operational plan you have used at work, in your school work, or even in your personal life.

Questions for Application

8. Interview the head of the department in which your major exists. What kinds of goals exist for the department and for the members of the department? Share your findings with the rest of the class.
9. Interview a local small-business manager about the time frames for planning that he or she uses. How do your results compare with what you might have expected from the presentation in the textbook?
10. Interview a college or university official to determine the use of single-use and standing plans at your institution. How were these plans developed?

BUILDING EFFECTIVE *conceptual* SKILLS

Exercise Overview

Conceptual skills refer to a person's abilities to think in the abstract. This exercise will help you develop your conceptual skills by relating your own personal goals and plans across different time frames.

Exercise Background

Most people have a general idea of what they want their future to be like. However, few people actually take the time to formulate specific goals and plans for their future. To do so might provide a useful blueprint for achieving those goals while simultaneously helping people better understand the likelihood of various goals actually coming to fruition.

Exercise Task

With the background information above as context, do the following:

1. List ten goals that you would like to have achieved in ten years. These goals might relate to work, family, or anything else you see as important.
2. Next, outline a five-year plan of the goals that you think are necessary to be at the halfway point in achieving your long-term goals.

3. Now do the same thing for each one of the next five years.
4. Evaluate the likelihood of actually being able to achieve each one-year goal, the five-year goals, and the ten-year goals.
5. How might this process be similar to and different from a manager doing the same thing for business goals?

BUILDING EFFECTIVE *time-management* SKILLS

Exercise Overview

Time-management skills refer to the manager's ability to prioritize work, to work efficiently, and to delegate appropriately. This exercise will help you develop your time-management skills by relating them to the process of goal optimization.

Exercise Background

All managers face a myriad of goals, challenges, opportunities, and demands on their time. Juggling all requires a clear understanding of priorities, time availability, and related factors. Assume that you are planning to open your own business, a retail store in a local shopping mall. You are starting from scratch, with no prior business connections. You do, however, have a strong and impressive business plan that you know will work.

In planning your business, you know that you need to meet with the following parties:

1. The mall manager, to negotiate a lease.
2. A local banker, to arrange partial financing.
3. An attorney, to incorporate your business.
4. An accountant, to set up a bookkeeping system.
5. Suppliers, to arrange credit terms and delivery schedules.
6. An advertising agency, to start promoting your business.
7. A staffing agency, to hire employees.
8. A design firm, to plan the physical layout of the store.

Exercise Task

With the background information above as context, do the following:

1. Develop a schedule listing the sequence in which you need to meet with the eight parties noted above. Your schedule should be developed to minimize backtracking (i.e., seeing one party and then having to see her or him again after seeing someone else).
2. Compare your schedule with that of a classmate and discuss differences.
3. Are there different schedules that are equally valid?

BUILDING EFFECTIVE *communication* SKILLS

Exercise Overview

Communication skills refer to the manager's abilities both to convey ideas and information to others effectively and to receive ideas and information effectively from others. Communicating goals is an important part of management and requires strong communication skills.

Exercise Background

Assume that you are the CEO of a large discount retailing company. You have decided that your firm needs to change its strategy to survive. Specifically, you want the firm to move away from discount retailing and move more into specialty retailing.

To do this, you know that you will need to close four hundred of your twelve hundred discount stores within the next year. You also need both to increase the expansion rate of your two existing specialty chains and to launch one new chain. Your tentative plans call for opening three hundred new specialty stores in one business and 150 in the other next year. You also want the basic concept for the new chain to be finalized and to have ten stores open next year as well. Finally, while you will be able to transfer some discounting employees to specialty retail jobs, there will still be a few hundred people put out of work.

Exercise Task

With the background information above as context, do the following:

1. Develop a press release that outlines these goals.
2. Determine the best way to communicate the goals to your employees.
3. Develop a contingency plan for dealing with problems.

CHAPTER CLOSING CASE

ROYAL CARIBBEAN PLANS THE LARGEST LUXURY LINER

Top management at Royal Caribbean did not actually set out to create the largest passenger ship in the world. But by the time *Voyager of the Seas* set sail, it had become by far the largest ship in Royal Caribbean's seventeen-ship fleet—triple the size of the fabled *Titanic* and one-quarter larger than any competing ship. At a cost of $700 million, *Voyager* is not just another luxury liner—it represents a huge step toward the future by opening an entirely new portion of the vacation market. It also represents a long-term investment, because cruise ships generally stay in service for at least twenty-five years.

CEO Richard Fain and his managers started planning this ship more than three years before the anticipated launch. Their first step was establishing a challenging mission: to attract vacationers who have never taken a cruise. Because a mere 11 percent of U.S. vacationers have ever taken a cruise, this was a huge potential market as well as a huge gamble. But Fain and his team knew they were planning not for the next year or two but for the next decade, when lifestyles and vacations could be vastly different. For this reason, Royal Caribbean commissioned extensive research into consumer attitudes toward vacation activities. These attitudes became the basis for many of the special features built into *Voyager,* such as a state-of-the-art nightclub and a wedding chapel. Fain and his team also envisioned facilities for other activities not normally found on cruise ships, such as in-line skating, rock climbing, and ice skating.

With this broad outline of features in hand, Royal Caribbean managers began hiring companies to design and build everything, from the chandeliers above, to the dance floors below. Rather than hire only architects and designers with experience working on cruise ships, Fain and his managers invited some proposals from talented designers who had never worked on ships. Although other cruise lines keep costs low and simplify the planning process by hiring the same designer for all ships, Royal Caribbean was more interested in innovation than in saving money. As a result, different parts of the ship were individually designed and often constructed in different parts of the world, then assembled in the shipyard in Turku, Finland. For example, the huge saltwater aquarium tanks were made in Colorado, while the fish came from Florida;

the English pub was designed by a Rhode Island firm; and the Egyptian-theme dance lounge was designed by a British firm.

Planning and coordinating the construction of such a huge ship required careful attention to detail. So Fain created a steering committee of key managers to oversee the entire process. In regular one- to two-day sessions, the committee listened to progress reports and considered ideas for overcoming potential pitfalls. The CEO, known for his sharp memory, frequently asked hard questions that resulted in small and large changes, from moving some light fixtures (to improve the look of the room) to widening the ten-story atrium (to enhance the feeling of spaciousness). Fain and other committee members made numerous trips to Finland to examine the ship under construction and make on-the-spot decisions where necessary, knowing that details such as the noise level in the dining room can make or break the cruise experience for passengers.

Before the launch date, *Voyager* sailed a series of trial runs so managers could check that everything operated properly. Although nearly all of the 1,186 crew members were drawn from other Royal Caribbean ships, they each received ninety-two hours of training about the intricacies of the ship and its equipment. By the time *Voyager* was officially launched, it was more than the world's largest and most expensive passenger ship—it was a major part of Royal Caribbean's future.

Case Questions

1. What kind of operational plan did Royal Caribbean create for the building of *Voyager of the Seas*?
2. What kinds of problems might Royal Caribbean encounter when working on the design and construction of a unique ship such as *Voyager*? What role would contingency planning play in this situation?
3. What constraints might Royal Caribbean have faced when designing and building *Voyager*?

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CHAPTER 8

Managing Strategy and Strategic Planning

OPENING INCIDENT

January 2000 brought with it global celebrations of the new millennium. It also marked one of the most significant mergers in the history of business—the joining of America Online (AOL) and Time Warner into a new enterprise that some observers predicted would rewrite the rules of business for years to come. AOL launched nationwide service in 1989 and went public in 1992. It grew rapidly over the rest of the decade, attracting millions of subscribers and swallowing rival CompuServe and premier Internet portal Netscape along the way.

Time Warner, on the other hand, is an old-line company tracing its roots back almost one hundred years. Time, Inc. was founded in 1922 with the launch of its namesake magazine *Time*. Over the decades Time also began publication of such periodicals as *Fortune*, *Sports Illustrated*, and *People*, and created the cable television network HBO. Warner Brothers was born alongside the Hollywood movie industry when it produced such classics as *Little Caesar* and *Casablanca*. Warner eventually grew to encompass a movie studio, television studios, cable television operations, and a publishing business headlined by such properties as *Superman* comics and *Mad* magazine. These two firms merged in 1989 to create Time Warner; the combined firm subsequently acquired TBS (consisting of CNN and other cable networks), launched numerous new magazines, and started a new broadcast television network.

As the 1990s drew to a close, managers at both AOL and Time Warner realized that their firms had some major strategic weaknesses. AOL, for example, lacked two key competitive assets. For one thing, most of its services were carried by and delivered through telephone wire; many experts, though, were predicting that the future of this industry rests on so-called broadband technology such as cable television. And for another, AOL itself had precious little "content" to deliver—it simply connected information sources with users who wanted access to that information.

Time Warner, meanwhile, had both of the things AOL desperately needed. Time Warner cable, for example, has over thirteen million subscribers. And information content—magazines, books, music, movies, and television programming—was the very thing Time Warner was based on. But the venerable media company, like so

"This is a merger of equals."

—Stephen Case, CEO of AOL, and Gerald Levin, CEO of Time Warner

LEARNING OBJECTIVES

After studying this chapter, you should be able to:

- **Discuss the components of strategy, types of strategic alternatives, and the distinction between strategy formulation and strategy implementation.**
- **Describe how to use SWOT analysis in formulating strategy.**
- **Identify and describe various alternative approaches to business-level strategy formulation.**
- **Describe how business-level strategies are implemented.**
- **Identify and describe various alternative approaches to corporate-level strategy formulation.**
- **Describe how corporate-level strategies are implemented.**

CHAPTER OUTLINE

- **The Nature of Strategic Management**
  - The Components of Strategy
  - Types of Strategic Alternatives
  - Strategy Formulation and Implementation
- **Using SWOT Analysis to Formulate Strategy**
  - Evaluating an Organization's Strengths
  - Evaluating an Organization's Weaknesses
  - Evaluating an Organization's Opportunities and Threats
- **Formulating Business-Level Strategies**
  - Porter's Generic Strategies
  - The Miles and Snow Typology
  - Strategies Based on the Product Life Cycle
- **Implementing Business-Level Strategies**
  - Implementing Porter's Generic Strategies
  - Implementing Miles and Snow's Strategies
- **Formulating Corporate-Level Strategies**
  - Single-Product Strategy
  - Related Diversification
  - Unrelated Diversification
- **Implementing Corporate-Level Strategies**
  - Becoming a Diversified Firm
  - Managing Diversification

many of its old-line brethren, had failed to figure out for itself how to make the transformation to the e-world. At the time the merger was announced, Time Warner had already made a commitment of $500 million to develop a digital division, but most observers were unenthusiastic or downright skeptical about its ability to become a player.

The idea for a partnership was hatched in September 1999 at an international meeting of high-level CEOs in Paris; the players kept talking and met again two weeks later in Shanghai at a similar event. In October, a merger was formally proposed. Serious negotiations began in November. Two key AOL executives traveled to New York to meet with a senior vice president from Time Warner. The three managers locked themselves in a conference room and used poster-sized sheets of paper to sketch how a combined firm might look. These sheets were then taken back to AOL headquarters for further examination. Finally, all the details were worked out, and a final accord was reached in January 2000. When the deal was announced, the business community was stunned. One observer went so far as to call it the most transformational event in his career. And indeed, the merger was so intriguing that many experts were simply at a loss to figure out what it truly means.[1]



The actions taken by AOL and Time Warner reflect one of the most critical functions that managers perform for their businesses: strategy and strategic planning. Executives at each firm recognized that their respective firms had both significant strengths and worrisome weaknesses. They also saw that by combining their firms they could use the strengths of each firm to offset the weaknesses of the other. And they further recognized that a combined firm would be well positioned to capitalize on the emerging commercial potential of the Internet. Hence, the merger of the two firms represents a significant strategic decision by managers at the two firms.

This chapter discusses how organizations manage strategy and strategic planning. We begin by examining the nature of strategic management, including its components and alternatives. We then describe the kinds of analyses needed for firms to formulate their strategies. Next we examine how organizations first formulate and then implement business-level strategies, followed by a parallel discussion at the corporate level.

■ The Nature of Strategic Management

strategy A comprehensive plan for accomplishing an organization's goals

strategic management A comprehensive and ongoing management process aimed at formulating and implementing effective strategies; it is a way of approaching business opportunities and challenges

effective strategy A strategy that promotes a superior alignment between the organization and its environment and between the organization and the achievement of its strategic goals

distinctive competence An organizational strength possessed by only a small number of competing firms

scope When applied to *strategy*, it specifies the range of markets in which an organization will compete

resource deployment How an organization will distribute its resources across the areas in which it competes

A **strategy** is a comprehensive plan for accomplishing an organization's goals. **Strategic management**, in turn, is a way of approaching business opportunities and challenges—it is a comprehensive and ongoing management process aimed at formulating and implementing effective strategies. Finally, **effective strategies** are those that promote a superior alignment between the organization and its environment and the achievement of its strategic goals.[2]

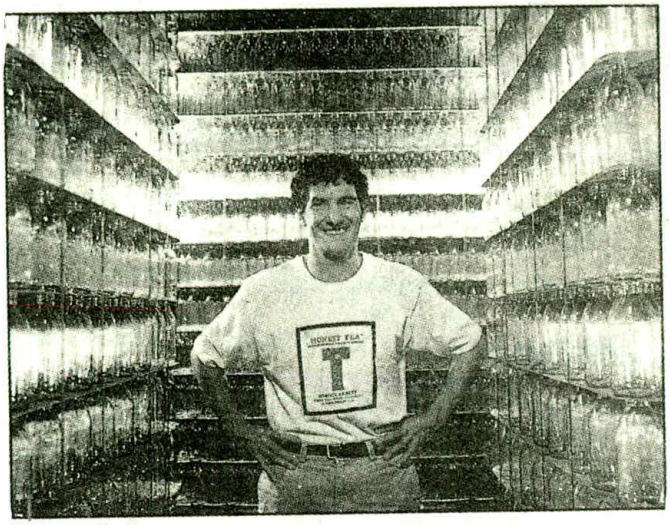
The Components of Strategy

In general, a well-conceived strategy addresses three areas: distinctive competence, scope, and resource deployment. A **distinctive competence** is something the organization does exceptionally well. (We discuss distinctive competencies more fully later.) A distinctive competence of The Limited is speed in moving inventory. It tracks consumer preferences daily with point-of-sale computers, transmits orders to suppliers in Hong Kong electronically, charters 747s to fly products to the United States, and has products in stores forty-eight hours later. Because other retailers take weeks or sometimes months to accomplish the same things, The Limited relies on this distinctive competence to stay ahead of its competition.[3]

The **scope** of a strategy specifies the range of markets in which an organization will compete. Hershey Foods has essentially restricted its scope to the confectionery business, with a few related activities in other food-processing areas. In contrast, its biggest competitor, Mars, has adopted a broader scope by competing in the pet-food business and the electronics industry, among others. Some organizations, called *conglomerates*, compete in dozens or even hundreds of markets.

A strategy should also include an outline of the organization's projected **resource deployment**—how it will distribute its resources across the areas in which it com-

petes. General Electric, for example, has been using profits from its highly successful U.S. operations to invest heavily in new businesses in Europe and Asia. Alternatively, the firm might have chosen to invest in different industries in its domestic market and/or to invest more heavily in Latin America. The choices it made about where and how much to invest reflect issues of resource deployment.[4]



Effective business strategies generally spell out such things as distinctive competencies, resource deployment, and scope. Consider, for instance, the success currently being enjoyed by Seth Goldman, owner and "Tea-EO" of Honest Tea. The distinctive competence of Honest Tea is its brewing technology: it uses real tea leaves and spring water and adds only a minimum amount of sweetener. It invests heavily in building strong relations with key partners such as socially conscious suppliers and retailers. And it limits operations to packaged tea beverages. Honest Tea has more than doubled its revenues each of the last three years and seems headed toward long-term "prosperi-tea."

Types of Strategic Alternatives

Most businesses today also develop strategies at two distinct levels. These levels provide a rich combination of strategic alternatives for organizations. The two general levels are business strategies and corporate strategies. **Business-level strategy** is the set of strategic alternatives that an organization chooses from as it conducts business in a particular industry or a particular market. Such alternatives help the organization focus its competitive efforts for each industry or market in a targeted manner.

Corporate-level strategy is the set of strategic alternatives that an organization chooses from as it manages its operations simultaneously across several industries and several markets.[5] As we discuss later, most large companies today compete in a variety of industries and markets. Although they develop business-level strategies for each industry or market, they also develop an overall strategy that helps define the mix of industries and markets that are of interest to the firm.

business-level strategy The set of strategic alternatives that an organization chooses from as it conducts business in a particular industry or a particular market

corporate-level strategy The set of strategic alternatives that an organization chooses from as it manages its operations simultaneously across several industries and several markets

Strategy Formulation and Implementation

Drawing a distinction between strategy formulation and strategy implementation is also instructive. **Strategy formulation** is the set of processes involved in creating or determining the strategies of the organization, whereas **strategy implementation** is the methods by which strategies are operationalized or executed within the organization. The primary distinction is along the lines of content versus process: the formulation stage determines what the strategy is, and the implementation stage focuses on how the strategy is achieved.

Sometimes the process of formulating and implementing strategies is rational, systematic, and planned and is often referred to as a **deliberate strategy**—a plan chosen and implemented to support specific goals.[6] Texas Instruments (TI) excels at formulating and implementing deliberate strategies. TI uses a planning

strategy formulation The set of processes involved in creating or determining the strategies of the organization; it focuses on the content of strategies

strategy implementation The methods by which strategies are operationalized or executed within the organization; it focuses on the processes through which strategies are achieved

deliberate strategy A plan chosen and implemented to support specific goals

process that assigns most senior managers two distinct responsibilities: an operational, short-term responsibility and a strategic, long-term responsibility. Thus, one manager may be responsible for both increasing the efficiency of semiconductor operations over the next year (operational, short-term) and investigating new materials for semiconductor manufacture in the twenty-first century (strategic, long-term). TI's objective is to help managers make short-term operational decisions while keeping in mind longer-term goals and objectives.

emergent strategy A pattern of action that develops over time in an organization in the absence of missions and goals, or despite missions and goals

Other times, however, organizations use an **emergent strategy**—a pattern of action that develops over time in an organization in the absence of missions and goals, or despite missions and goals.[7] Implementing emergent strategies involves allocating resources even though an organization has not explicitly chosen its strategies. 3M has at times benefited from emergent strategies. The invention of invisible tape, for instance, provides a good example. Entrepreneurial engineers working independently took the invention to their boss, who concluded that it did not have major market potential because it was not part of an approved research and development plan. Only when the product was evaluated at the highest levels in the organization was it accepted and made part of 3M's product mix. Of course, 3M's Scotch tape became a major success, despite the fact that it arose outside the firm's established practices. 3M now counts on emergent strategies to help expand its numerous businesses.

MANAGEMENT IMPLICATIONS Managers need to appreciate the importance of strategy and strategic management in directing their organization through its competitive environment. Part of this appreciation rests on knowing the difference between business- and corporate-level strategy, and part rests on knowing the difference between deliberate and emergent strategy.

■ Using SWOT Analysis to formulate Strategy

SWOT An acronym that stands for strengths, weaknesses, opportunities, and threats

The starting point in formulating strategy is usually SWOT analysis. **SWOT** is an acronym that stands for strengths, weaknesses, opportunities, and threats. As shown in Figure 8.1, SWOT analysis is a careful evaluation of an organization's internal strengths and weaknesses as well as its environmental opportunities and threats. In SWOT analysis, the best strategies accomplish an organization's mission by (1) exploiting an organization's opportunities and strengths while (2) neutralizing its threats and (3) avoiding (or correcting) its weaknesses.

Evaluating an Organization's Strengths

organizational strength A skill or capability that enables an organization to conceive of and implement its strategies

Organizational strengths are skills and capabilities that enable an organization to conceive of and implement its strategies. Sears, for example, has a nationwide network of trained service employees who repair Sears appliances. Jane Thompson, a Sears executive, conceived of a plan to consolidate repair and home-improvement

services nationwide under the well-known Sears brand name and to promote it as a general repair operation for all appliances, not just those purchased from Sears. Thus, the firm is capitalizing on existing capabilities and the strength of its name to launch a new operation.[8] Different strategies call on different skills and capabilities. For example, Matsushita Electric has demonstrated strengths in manufacturing and selling consumer electronics under the brand name Panasonic. Matsushita's strength in electronics does not ensure success, however, if the firm expands into insurance, swimming-pool manufacture, or retail. Different strategies such as these require different organizational strengths. SWOT analysis divides organizational strengths into two categories: common strengths and distinctive competencies. *Working with Diversity* also describes how some firms effectively use diversity to build organizational strength.

Common Organizational Strengths A **common strength** is an organizational capability possessed by numerous competing firms. For example, all the major Hollywood film studios possess common strengths in lighting, sound recording, set and costume design, and makeup. *Competitive parity* exists when large numbers of competing firms can implement the same strategy. In this situation organizations generally attain only average levels of performance. Thus, a film company that exploits only its common strengths in choosing and implementing strategies is not likely to go beyond average performance.

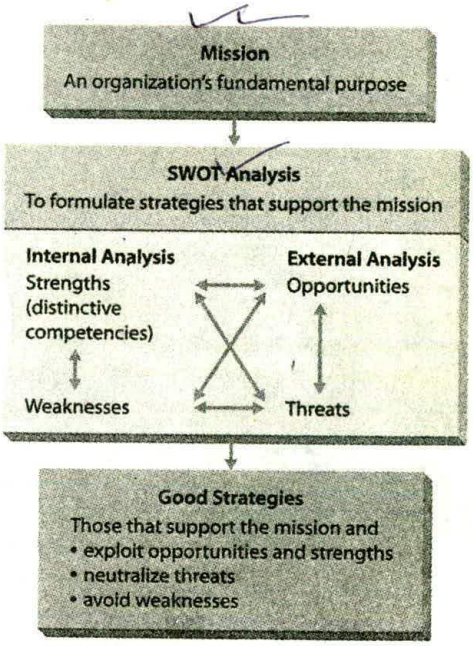
Distinctive Competencies A distinctive competency is a strength possessed by only a small number of competing firms. Distinctive competencies are rare among a set of competitors. George Lucas's Industrial Light and Magic (ILM), for example, has brought the cinematic art of special effects to new heights. Some of ILM's special effects can be produced by no other organization; these rare special effects are thus ILM's distinctive competencies. Organizations that exploit their distinctive competencies often obtain a *competitive advantage* and attain above-normal economic performance.[9] Indeed, a main purpose of SWOT analysis is to discover an organization's distinctive competencies so that the organization can choose and implement strategies that exploit its unique organizational strengths.

Imitation of Distinctive Competencies An organization that possesses distinctive competencies and exploits them in the strategies it chooses can expect to obtain a competitive advantage and above-normal economic performance. However, its success will lead other organizations to duplicate these advantages. **Strategic imitation** is the practice of duplicating another firm's distinctive competency and thereby

Figure 8.1

SWOT Analysis

SWOT analysis is one of the most important steps in formulating strategy. Using the organization's mission as a context, managers assess internal strengths (distinctive competencies) and weaknesses as well as external opportunities and threats. The goal is then to develop good strategies that exploit opportunities and strengths, neutralize threats, and avoid weaknesses.



common strength An organizational capability possessed by numerous competing firms

strategic imitation The practice of duplicating another organization's distinctive competency and thereby implementing a valuable strategy

WORKING WITH DIVERSITY

DIVERSITY AS A COMPETITIVE ADVANTAGE

When leading organizations such as SBC Communications, Hyatt, and Public Service Company of New Mexico conduct a SWOT analysis, they can count diversity among their competitive strengths. In today's multicultural environment, a diverse workforce and diversity in the ranks of management and the board of directors can help companies attract talented employees and better serve all kinds of customers.

At Texas-based SBC Communications, for example, diversity among employees and managers helps the telecommunications company understand and respond to the needs of its multicultural customer base. Representatives at SBC's call center speak twenty languages. The company also donates to programs that help minority-owned suppliers obtain financing for business operations.

Hyatt, the hotel chain headquartered in Chicago, has one of the most diverse workforces in the United States. More than 60 percent of its employees and 35 percent of its managers come from Asian, African American, Hispanic, or Native American backgrounds. Hyatt is so committed to diversity that it built a full-size industrial kitchen in Chicago's Roberto Clemente High School to encourage the mainly Latino student body to consider cooking as a career. Already, one Clemente graduate has risen through the ranks to become head banquet chef at a Hyatt hotel.

Diversity is also a priority at the Public Service Company of New Mexico, where Hispanic employees make up more than 40 percent of the workforce. The company goes out of its way to nurture talent through an innovative program in which promising managers serve for four months as the chairman's executive assistant. In addition to arranging the chairman's schedule, the assistants accompany him to a variety of meetings—including sessions with state regulators and corporate directors. Along the way, the assistants soak up valuable knowledge while showing what they can do. So far, three assistants have used the program as a springboard to higher management, adding to the diversity at senior levels and expanding the organization's strengths through their insights and experience.

This is a way to find young, talented people in the middle ranks—particularly women and minorities.

*—Benjamin Montoya, chairman, Public Service Company of New Mexico**

Reference: Christine Y. Chen and Jonathan Hickman, "America's 50 Best Companies for Minorities," *Fortune*, July 10, 2000, pp. 190–200 (*quote on p. 200).

implementing a valuable strategy. Although some distinctive competencies can be imitated, others cannot. When a distinctive competency cannot be imitated, strategies that exploit these competencies generate sustained competitive advantages. A **sustained competitive advantage** is a competitive advantage that exists after all attempts at strategic imitation have ceased.[10]

sustained competitive advantage A competitive advantage that exists after all attempts at strategic imitation have ceased

A distinctive competency might not be imitated for three reasons. First, the acquisition or development of the distinctive competency may depend on unique historical circumstances that other organizations cannot replicate. Caterpillar, for example, obtained a sustained competitive advantage when the U.S. Army granted it a long-term contract during World War II. The Army felt obligated to offer this contract because of the acute international construction requirements necessary to meet the army's needs. Caterpillar's current competitors, including Komatsu and Deere & Company, cannot re-create these circumstances.

Second, a distinctive competency might be difficult to imitate because its nature and character might not be known or understood by competing firms. Procter & Gamble, for example, considers that its sustained competitive advantage is based on its manufacturing practices. Large sections of Procter & Gamble's plants are screened off to keep this information secure. Industrial Light & Magic also refuses to disclose how it creates some of its special effects.

Finally, a distinctive competency can be difficult to imitate if it is based on complex social phenomena, like organizational teamwork or culture. Competing organizations may know, for example, that a firm's success is directly traceable to the teamwork among its managers but may not be able to imitate this distinctive competency because teamwork is a difficult thing to create.

Evaluating an Organization's Weaknesses

Organizational weaknesses are skills and capabilities that do not enable an organization to choose and implement strategies that support its mission. An organization has essentially two ways of addressing weaknesses. First, it may need to make investments to obtain the strengths required to implement strategies that support its mission. Second, it may need to modify its mission so that it can be accomplished with the skills and capabilities that the organization already possesses.

organizational weakness A skill or capability that does not enable an organization to choose and implement strategies that support its mission

In practice, organizations have a difficult time focusing on weaknesses, in part because organization members are often reluctant to admit that they do not possess all the skills and capabilities needed. Evaluating weaknesses also calls into question the judgment of managers who chose the organization's mission in the first place and who failed to invest in the skills and capabilities needed to accomplish it.

Organizations that fail either to recognize or overcome their weaknesses are likely to suffer from competitive disadvantages. An organization has a **competitive disadvantage** when it is not implementing valuable strategies that are being implemented by competing organizations. Organizations with a competitive disadvantage can expect to attain below-average levels of performance.

competitive disadvantage A situation in which an organization is not implementing valuable strategies that are being implemented by competing organizations

Evaluating an Organization's Opportunities and Threats

Whereas evaluating strengths and weaknesses focuses attention on the internal workings of an organization, evaluating opportunities and threats requires analyzing an organization's environment. **Organizational opportunities** are areas that may generate higher performance. **Organizational threats** are areas that increase the difficulty of an organization performing at a high level. Porter's five forces model of the competitive environment, as discussed in Chapter 3, can be used to characterize the extent of opportunity and threat in an organization's environment.

organizational opportunity An area in the environment that, if exploited, may generate higher performance

organizational threat An area in the environment that increases the difficulty of an organization performing at a high level

Recall that Porter's five forces are level of rivalry, power of suppliers, power of customers, threat of substitutes, and threat of new entrants. In general, when the level of rivalry, the power of suppliers and customers, and the threat of substitutes and new entrants are all high, an industry has relatively few opportunities and

numerous threats. Firms in these types of industries typically have the potential to achieve only normal economic performance. On the other hand, when the level of rivalry, the power of suppliers and customers, and the threat of substitutes and new entrants are all low, then an industry has numerous opportunities and relatively few threats. These industries hold the potential for above-normal performance for member organizations.[11]

MANAGEMENT IMPLICATIONS Managers need to understand how to perform a SWOT analysis. Understanding the differences between common organizational strengths and distinctive competencies can help managers avoid competitive parity and achieve a competitive advantage. Assessing organizational strengths and weaknesses is also a difficult—but very important—part of this process.

Formulating Business-Level Strategies

Several frameworks have been developed for identifying the major strategic alternatives that organizations should consider when choosing their business-level strategies. Three important classification schemes are Porter's generic strategies, the Miles and Snow typology, and strategies based on the product life cycle.

Porter's Generic Strategies

According to Michael Porter, organizations may pursue a differentiation, overall cost leadership, or focus strategy at the business level.[12] Table 8.1 summarizes each of these strategies. An organization that pursues a **differentiation strategy** seeks to distinguish itself from competitors through the quality of its products or services. Firms that successfully implement a differentiation strategy can charge more than competitors because customers are willing to pay more to obtain the extra value they perceive.[13] Rolex pursues a differentiation strategy. Rolex watches are hand made of gold and stainless steel and are subjected to strenuous tests of quality and reliability. The firm's reputation enables it to charge thousands of dollars for its watches. Other firms that use differentiation strategies are Lexus, Nikon, Cross, and Ralph Lauren.

differentiation strategy A strategy in which an organization seeks to distinguish itself from competitors through the quality of its products or services

An organization implementing an **overall cost leadership strategy** attempts to gain a competitive advantage by reducing its costs below the costs of competing firms. By keeping costs low, the organization can sell its products at low prices and still make a profit. Timex uses an overall cost leadership strategy. For decades, this firm has specialized in manufacturing relatively simple, low-cost watches for the mass market. The price of Timex watches, starting around $39.95, is low because of the company's efficient high-volume manufacturing capacity. Other firms that implement overall cost leadership strategies are Hyundai, Eastman Kodak, and Bic.

overall cost leadership strategy A strategy in which an organization attempts to gain a competitive advantage by reducing its costs below the costs of competing firms

A firm pursuing a **focus strategy** concentrates on a specific regional market, product line, or group of buyers. This strategy may have either a differentiation focus, whereby the firm differentiates its products in the focus market, or an overall

focus strategy A strategy in which an organization concentrates on a specific regional market, product line, or group of buyers

Strategy Type	Definition	Examples
Differentiation	Distinguish products or services	Rolex (watches) Mercedes-Benz (automobiles) Nikon (cameras) Cross (writing instruments) Hewlett-Packard (handheld calculators)
Overall cost leadership	Reduce manufacturing and other costs	Timex Hyundai Kodak Bic Texas Instruments
Focus	Concentrate on specific regional market, product market, or group of buyers	Tag Heuer Fiat, Alpha Romeo Polaroid Waterman Pens Fisher Price

Table 8.1

Porter's Generic Strategies
Michael Porter has proposed three generic strategies. These strategies, called differentiation, overall cost leadership, and focus, are each presumed to be widely applicable to many different competitive situations.

cost leadership focus, whereby the firm manufactures and sells its products at low cost in the focus market. In the watch industry, Tag Heuer follows a focus differentiation strategy by selling only rugged waterproof watches to active consumers. Fiat follows a focus cost leadership strategy by selling its automobiles only in Italy and in selected regions of Europe; Alpha Romeo uses focus differentiation to sell its high-performance cars in these same markets. Fisher-Price uses focus differentiation to sell electronic calculators with large, brightly colored buttons to the parents of preschoolers; stockbroker Edward Jones focuses on small town settings. General Mills is focusing new product development on consumers who eat meals while driving—their slogan is, "Can we make it 'one-handed'?" so that drivers can eat or drink it safely.[14]

The Miles and Snow Typology

A second classification of strategic options was developed by Raymond Miles and Charles Snow.[15] These authors suggested that business-level strategies generally fall into one of four categories: prospector, defender, analyzer, and reactor. Table 8.2 summarizes each of these strategies. Of course, different businesses within the same company might pursue different strategies.

A firm that follows a **prospector strategy** is a highly innovative firm that is constantly seeking new markets and new opportunities and is oriented toward growth and risk taking. Over the years, 3M has prided itself on being one of the most innovative major corporations in the world. Employees at 3M are constantly encouraged to develop new products and ideas in a creative and entrepreneurial way. This focus on innovation has led 3M to develop a wide range of new products and markets, including invisible tape and antistain fabric treatments. Amazon.com is also following a prospector strategy because it constantly seeks new market opportunities for selling different kinds of products through its web sites.

prospector strategy A strategy in which the firm is constantly seeking new markets and new opportunities and is oriented toward growth and risk taking

Table 8.2

The Miles and Snow Typology

The Miles and Snow typology identifies four strategic types of organizations. Three of these—the prospector, the defender, and the analyzer—can each be effective in certain circumstances. The fourth type—the reactor—represents an ineffective approach to strategy.

Strategy Type	Definition	Examples
Prospector	Is innovative and growth oriented, searches for new markets and new growth opportunities, encourages risk taking	Amazon.com 3M Rubbermaid
Defender	Protects current markets, maintains stable growth, serves current customers	Bic eBay.com Mrs. Fields
Analyzer	Maintains current markets and current customer satisfaction with moderate emphasis on innovation	DuPont IBM Yahoo!
Reactor	No clear strategy, reacts to changes in the environment, drifts with events	International Harvester in the 1960s and 1970s, Joseph Schlitz Brewing Co., W. T. Grant

The *World of Management* provides a bit more detail about Amazon.com's strategy in Europe.

defender strategy A strategy in which the firm concentrates on protecting its current markets, maintaining stable growth, and serving current customers

Rather than seeking new growth opportunities and innovation, a company that follows a **defender strategy** concentrates on protecting its current markets, maintaining stable growth, and serving current customers. With the maturity of the market for writing instruments, Bic has used this approach—it has adopted a less aggressive, less entrepreneurial style of management and has chosen to defend its substantial market share in the industry. It emphasizes efficient manufacturing and customer satisfaction. While eBay is expanding aggressively into foreign markets, the on-line auctioneer is still pursuing what amounts to a defender strategy because it is keeping its focus primarily on the auction business. Thus, while it is prospecting for new markets, its defending its core business focus.[16]

analyzer strategy A strategy in which the firm attempts to maintain its current businesses and to create new market opportunities

A business that uses an **analyzer strategy** combines elements of prospectors and defenders. Most large companies use this approach because they want both to protect their base of operations and to create new market opportunities. IBM uses analyzer strategies. DuPont is currently using an analyzer strategy. The firm is relying heavily on its existing chemical and fiber operations to fuel its earnings for the foreseeable future. At the same time, though, DuPont is also moving systematically into new business areas such as biotech agriculture and pharmaceuticals. Yahoo! is also using this strategy by keeping its primary focus on its role as an Internet portal while simultaneously seeking to extend that portal into more and more applications.[17]

reactor strategy A strategy in which a firm has no consistent approach to strategy

Finally, a business that follows a **reactor strategy** has no consistent strategic approach; it drifts with environmental events, reacting to but failing to anticipate or influence those events. Not surprisingly, these firms usually do not perform as well as organizations that implement other strategies. Although most organizations would deny using reactor strategies, during the 1970s International Harvester Co. (IH) clearly was a reactor. At a time when IH's market for trucks, construction equipment, and agricultural equipment was booming, IH failed to keep pace with

WORLD OF MANAGEMENT

U.S. E-BUSINESSES PROSPECT FOR GROWTH IN EUROPE

U.S. Internet innovators are seeking aggressive growth by building on their successful domestic strategies to enter global markets. Leading e-tailer Amazon.com, for example, used its innovative web technology to fuel an invasion of the British market. Much of the content on Amazon's British site (http://www.amazon.co.uk) is local—CDs by local artists, books by local authors—and is supported by the U.S. parent's on-line shopping technology and marketing expertise. The company used the same strategy to expand in France with a mix of local and global content supported by back-office technology imported from the U.S. parent. In addition, Amazon expanded by buying locally operated Internet bookstores. Despite competition from European e-businesses, Amazon's on-line cash registers have been ringing: its European sales have already outdistanced those of Bertelsmann's BOL, its closest European rival, by 500 percent.

On-line auction innovator eBay has also pursued growth by crossing the Atlantic to open country-specific web sites in Germany (http://www.ebay.de), Great Britain, and France. By initially concentrating on just three new markets, eBay sought to establish a strong customer base and to build economies of scale for higher profitability and future expansion. Despite intense competition, eBay attracted far more users than QXL, its largest European rival, in less than a year.

Taking risks to support aggressive growth and to ensure long-term viability is what helps U.S. e-businesses such as VacationSpot.com, which lists foreign vacation home rentals, compete more effectively against European rivals such as Belgium's Rent-a-Holiday. Although Rent-a-Holiday had a nine-month head start, VacationSpot (http://vacationspot.com) went beyond merely listing rental properties to allow customers to finalize and pay for rental arrangements on-line. VacationSpot also took financial risks, such as arranging expensive promotion deals with Expedia, Travelocity, and other popular travel web sites to gain wider exposure and to increase market share. Rent-a-Holiday was soon bought by VacationSpot. Then the combined company merged with Expedia, gaining more financial backing and building the on-line clout to become an even more formidable force in the growing market for on-line vacation home rentals.

You're not going to get scale by being number one in Norway.

—Michael van Swaiij, European managing director for eBay*

References: William Echikson, "American E-tailers Take Europe by Storm," *Business Week*, August 7, 2000, pp. 54–55 (*quote on p. 55); William Echikson, "Home Field Disadvantage," *Business Week*, December 13, 1999, pp. EB72–EB74; "Rough Crossing for eBay," *Business Week*, February 7, 2000, p. EB48.

its competitors. By the time a recession cut demand for its products, it was too late for IH to respond, and the company lost millions of dollars. The firm was forced to sell off virtually all of its businesses except its truck-manufacturing business. IH, now renamed Navistar, moved from being a dominant firm in trucking, agriculture, and construction to a medium-size truck manufacturer because it failed to anticipate changes in its environment.

Strategies Based on the Product Life Cycle

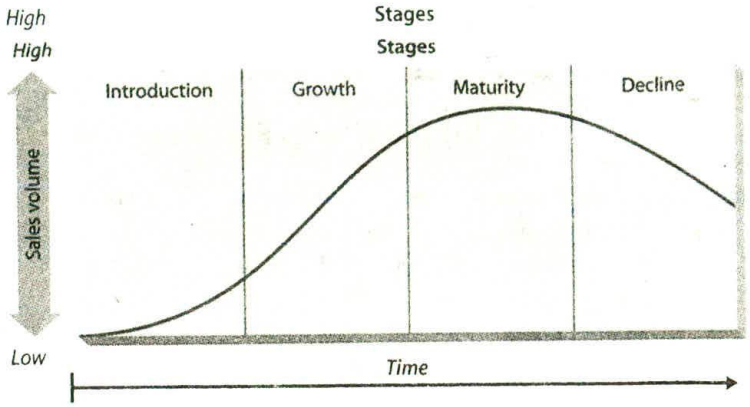
The **product life cycle** is a model that shows how sales volume changes over the life of products. Understanding the four stages in the product life cycle helps managers recognize that strategies need to evolve over time. As Figure 8.2 shows, the

product life cycle A model that shows how sales volume changes over the life of products

Figure 8.2

The Product Life Cycle

Managers can use the framework of the product life cycle—introduction, growth, maturity, and decline—to plot strategy. For example, management may decide on a differentiation strategy for a product in the introduction stage and a prospector approach for a product in the growth stage. By understanding this cycle and where a particular product falls within it, managers can develop more effective strategies for extending product life.



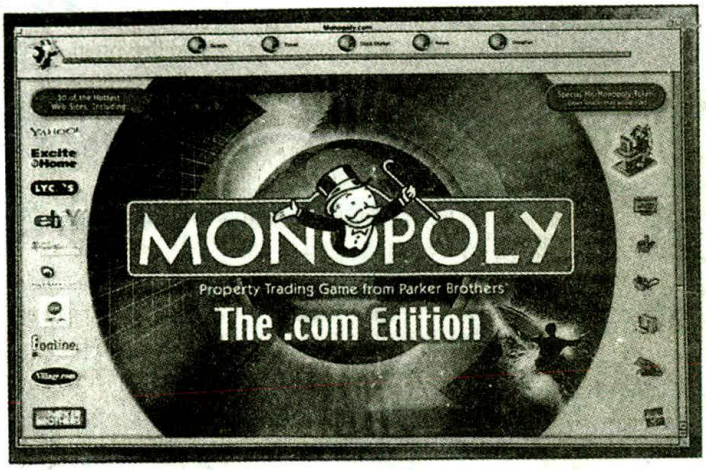
cycle begins when a new product or technology is first introduced. In this *introduction stage*, demand may be very high and sometimes outpaces the firm's ability to supply the product. Managers need to focus their efforts on getting product out the door without sacrificing quality. Managing growth by hiring new employees and managing inventories and cash flow are also concerns during this stage.

During the *growth stage*, more firms begin producing the product, and sales continue to grow. Important management issues include ensuring quality and delivery and beginning to differentiate an organization's product from competitors' products. Entry into the industry during the growth stage may threaten an organization's competitive advantages; thus, strategies to slow the entry of competitors are important.

After a period of growth, products enter a third phase. During this *mature stage*, overall demand growth for a product begins to slow down and the number of new firms producing the product begins to decline. The number of established firms producing the product may also begin to decline. This period of maturity is essential if an organization is going to survive in the long run. Product differentiation concerns are still important during this stage, but keeping costs low and beginning the search for new products or services are also important strategic considerations.

In the *decline stage*, demand for the product or technology decreases, the number of organizations producing the product drops, and total sales drop. Demand often declines because all those who were interested in purchasing a particular product have already done so. Organizations that fail to anticipate the decline stage in earlier stages of the life cycle may go out of business. Those that differentiate their product, keep their costs low, or develop new products or services may do well during this stage.

MANAGEMENT IMPLICATIONS Managers who formulate business-level strategies can adopt one of three competitive strategies advocated by Porter or one of the three strategies described by Miles and Snow. However, they should avoid using a reactor strategy. Managers can also use product life cycles as part of their strategy formulation process.



Firms can sometimes extend the life cycle of their products so as to continue to generate new revenues. Introducing existing products to new consumers or modernizing existing products are common methods for doing this. For example, the venerable Monopoly board game, owned and distributed by the Parker Brothers game company, is one of the most successful game products of all time. But today's game players might not relate to such properties as the Reading Railroad and Water Works or to such institutions as the Community Chest. So, Parker Brothers recently launched a new-economy version of Monopoly in which players buy properties like eBay, Lycos, and Nokia and receive "good news" and "bad news" e-mails.

■ Implementing Business-Level Strategies

As noted earlier, after business strategies are formulated, they must then be implemented. To do implement business strategies effectively, managers must integrate the activities of several different functions. *Marketing* and *sales*, for example, are used to promote products or services and the overall public image of the organization (often through various types of advertising), price products or services, contact customers directly, and make sales. *Accounting* and *finance* control the flow of money both within the organization and from outside sources to the organization, and *manufacturing* creates the organization's products or services. Organizational *culture*, as discussed in Chapter 6, also helps firms implement their strategies.

Implementing Porter's Generic Strategies

Differentation and cost leadership can each be implemented via these basic organizational functions. (Focus is implemented via the same approaches, depending on which one it is based.)

Differentiation Strategy In general, to support differentiation, marketing and sales must emphasize the high-quality, high-value image of the organization's products or services. Neiman-Marcus, a department store for financially secure consumers, has excelled at using marketing to support its differentiation strategy. People do not go to Neiman-Marcus just to buy clothes or to shop for home electronics. Instead, a trip to Neiman-Marcus is advertised as a "total shopping experience." Customers who want to shop for $3,000 pet houses, $50,000 mink coats, and $7,000 exercise machines recognize that the store caters to their needs. Other organizations that have used their marketing function to implement a differentiation strategy include Chanel, Calvin Klein, and Bloomingdale's.



Implementing business-level strategy can be complicated, especially when it's necessary to make a change. A few years ago, Jeffrey Bezos launched Amazon.com, an Internet-based book retailer. Amazon.com built its business using a differentiation strategy, billing itself as "Earth's biggest bookstore," offering a huge selection of books, stressing ease-of-use, and relying on mail delivery service. But as other big firms, like Barnes & Noble and Amazon.com's own wholesaler, have launched Internet book selling operations themselves, Bezos has found it necessary to shift to a cost leadership strategy to protect his marketshare and fend off these new competitors.

The function of accounting and finance in a business that is implementing a differentiation strategy is to control the flow of funds without discouraging the creativity needed to develop new products and services constantly to meet customer needs. If keeping track of and controlling the flow of money become more important than determining how money and resources are best spent to meet customer needs, then no organization, whether high-technology firm or fashion designer, will be able to implement a differentiation strategy effectively. In manufacturing, a firm implementing a differentiation strategy must emphasize quality and meeting specific customer needs rather than simply reducing costs. Manufacturing may sometimes have to keep inventory on hand so that customers will have access to products when they want them. Manufacturing may also have to engage in costly customization to meet customer needs.

The culture of a firm implementing a differentiation strategy, like the firm's other functions, must also emphasize creativity, innovation, and response to customer needs. Lands' End's culture puts the needs of customers ahead of all other considerations. This firm, which sells men's and women's leisure clothes through a catalog service, offers a complete guarantee on merchandise. Dissatisfied customers may return clothes for a full refund or exchange, no questions asked. Lands' End takes orders twenty-four hours a day and will ship most orders within twenty-four hours. Lost buttons and broken zippers are replaced immediately. The priority given to customer needs is typical of an organization that is successfully implementing a differentiation strategy.

Overall Cost Leadership Strategy To support cost leadership, marketing and sales are likely to focus on simple product attributes and how these product attributes meet customer needs in a low-cost and effective manner. These organizations are very likely to engage in advertising. Throughout this effort, however, emphasis is on the value that an organization's products provide for the price, rather than on the special features of the product or service. Advertising for Bic pens ("Writes first time, every time"), Timex watches ("Takes a licking and keeps on ticking"), and Wal-Mart stores ("Always low prices—always") helps these firms implement cost leadership strategies.

Proper emphasis in accounting and finance is also pivotal. Because the success of the organization depends on having costs lower than the competitors', management must take care to reduce costs wherever possible. Tight financial and accounting controls at Wal-Mart, Costco, and MCI have helped these organizations

implement cost leadership strategies. Manufacturing typically helps with large runs of highly standardized products. Products are designed both to meet customer needs and to be manufactured easily. Manufacturing emphasizes increased volume of production to reduce the per-unit costs of manufacturing. Organizations such as Toshiba (a Japanese semiconductor firm) and Texas Instruments have used this type of manufacturing to implement cost leadership strategies.

The culture of organizations implementing cost leadership strategies tends to focus on improving the efficiency of manufacturing, sales, and other business functions. Managers in these organizations are almost fanatical about keeping their costs low. Wal-Mart appeals to its customers to leave shopping carts in its parking lot with signs that read "Please—help us keep *your* costs low." Fujitsu Electronics, in its Tokyo manufacturing facilities, operates in plain, unpainted cinder-block and cement facilities to keep its costs as low as possible.

Implementing Miles and Snow's Strategies

Similarly, various issues must be considered when implementing any of Miles and Snow's strategic options. (Of course, no organization would purposefully choose to implement a reactor strategy.)

Prospector Strategy An organization implementing a prospector strategy is innovative, seeks new market opportunities, and takes numerous risks. To implement this strategy, organizations need to encourage creativity and flexibility. Creativity helps an organization perceive, or even create, new opportunities in its environment; flexibility enables it to change quickly to take advantage of these new opportunities. Organizations often increase creativity and flexibility by adopting a decentralized organization structure. An organization is decentralized when major decision-making responsibility is delegated to middle- and lower-level managers. Johnson & Johnson links decentralization with a prospector strategy. Each of the firm's different businesses is organized into a separate unit, and the managers of these units hold full decision-making responsibility and authority. Often these businesses develop new products for new markets. As the new products develop and sales grow, Johnson & Johnson reorganizes so that each new product is managed in a separate unit.

Defender Strategy An organization implementing a defender strategy attempts to protect its market from new competitors. It tends to downplay creativity and innovation in bringing out new products or services and focus its efforts instead on lowering costs or improving the performance of current products. Often a firm implementing a prospector strategy will switch to a defender strategy. This happens when the firm successfully creates a new market or business and then attempts to protect its market from competition. A good example is Mrs. Fields. One of the first firms to introduce high-quality, high-priced cookies, Mrs. Fields sold its product in special cookie stores and grew very rapidly. This success, however, encouraged numerous other companies to enter the market. Increased competition, plus reduced

demand for high-priced cookies, has threatened Mrs. Fields's market position. To maintain its profitability, the firm has slowed its growth and is now focusing on making its current operation more profitable. This behavior is consistent with the defender strategy.

Analyzer Strategy An organization implementing an analyzer strategy attempts to maintain its current business and to be somewhat innovative in new businesses. Because the analyzer strategy falls somewhere between prospector strategy (with a focus on innovation) and defender strategy (with a focus on maintaining and improving current businesses), the attributes of organizations implementing the analyzer strategy tend to be similar to both of these other types of organizations. They have tight accounting and financial controls, high flexibility, efficient production and customized products, and high creativity and low costs. Organizations maintain these multiple and contradictory processes with difficulty.

Starbucks is implementing an analyzer strategy. While the firm is growing rapidly, its fundamental business is still coffee. At the same time, however, the firm is cautiously branching out into music and ice cream and other food products, and is experimenting with restaurants with more comprehensive menu selections. This approach is allowing Starbucks to remain focused on its core coffee business but still explore new business opportunities at the same time.

MANAGEMENT IMPLICATIONS Managers should understand the basic concepts inherent in marketing and sales, accounting and finance, manufacturing, and organization culture. Each function or characteristic plays an important role in implementing any of the business-level strategies.

■ Formulating Corporate-Level Strategies

Most large organizations are engaged in several businesses, industries, and markets. Each business or set of businesses within such an organization is frequently referred to as a *strategic business unit,* or *SBU.* An organization such as General Electric Co. operates hundreds of different businesses, making and selling products as diverse as jet engines, nuclear power plants, and light bulbs. GE organizes these businesses into approximately twenty SBUs. Even organizations that sell only one product may operate in several distinct markets.

diversification The number of different businesses that an organization is engaged in and the extent to which these businesses are related to one another

Decisions about which businesses, industries, and markets an organization will enter, and how to manage these different businesses, are based on an organization's corporate strategy. The most important strategic issue at the corporate level concerns the extent and nature of organizational diversification. **Diversification** describes the number of different businesses that an organization is engaged in and the extent to which these businesses are related to one another. There are three types of diversification strategies: single-product strategy, related diversification, and unrelated diversification.[18]

Single-Product Strategy

An organization that pursues a **single-product strategy** manufactures just one product or service and sells it in a single geographic market. The WD-40 Company, for example, manufactures only a single product, WD-40 spray lubricant, and sells it in just one market, North America. WD-40 has considered broadening its market to Europe and Asia, but it continues to center all manufacturing, sales, and marketing efforts on one product.

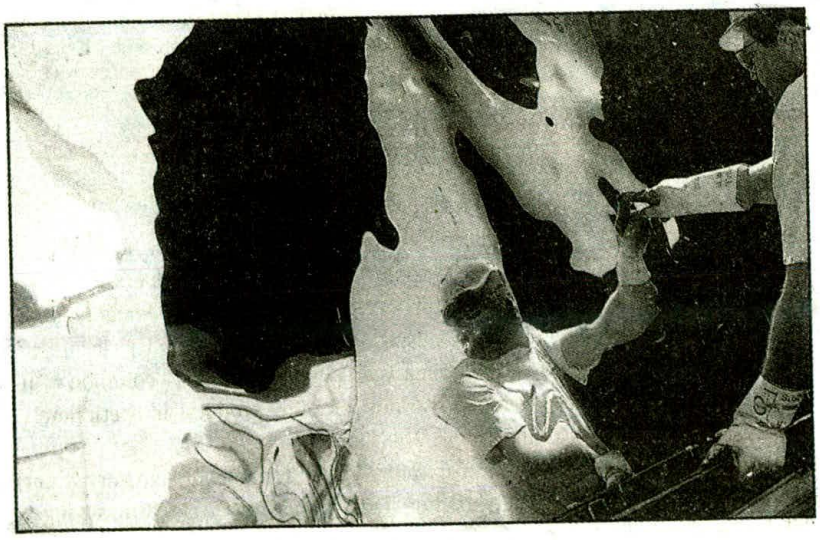
single-product strategy A strategy in which an organization manufactures just one product or service and sells it in a single geographic market

The single-product strategy has one major strength and one major weakness. By concentrating its efforts so completely on one product and market, a firm is likely to be very successful in manufacturing and marketing the product. Because it has staked its survival on a single product, the organization works very hard to make sure that the product is a success. Of course, if the product is not accepted by the market or is replaced by a new one, the firm will suffer. This happened to slide-rule manufacturers when electronic calculators became widely available and to companies that manufactured only black-and-white televisions when low-priced color televisions were first mass-marketed. Similarly, Wrigley has long practiced what amounts to a single-product strategy with its line of chewing gums. But because younger consumers are buying less gum than earlier generations, Wrigley is facing declining revenues and lower profits.[19]

Related Diversification

Given the disadvantage of the single-product strategy, most large businesses today operate in several different businesses, industries, or markets.[20] If the businesses are somehow linked, that organization is implementing a strategy of **related diversification**. Virtually all larger businesses in the United States use related diversification. *Managing in an E-business World* discusses how Cisco is using this strategy.

related diversification A strategy in which an organization operates in several different businesses, industries, or markets that are somehow linked



Formulating corporate strategy often involves making decisions about diversification. Alcoa's senior managers recently decided the firm needed to begin diversifying if it is to meet the CEO's goal of becoming a $40 billion enterprise by 2004. In recent months, then, the firm has bought Cordant Technologies (a firm that builds engines for the Space Shuttle), Reynolds Metals (a competing aluminum company), and two small aluminum companies in Britain. But since additional acquisitions in the aluminum industry might raise antitrust concerns, Alcoa is now considering additional acquisitions in other industries.

MANAGING IN AN *e*-BUSINESS WORLD

Cisco Uses Acquisitions to Strengthen Its E-business Backbone

Making acquisitions work is an important strength in the e-business world, where companies often grow by following a strategy of related diversification. But few companies have the acquisitions expertise or experience of Cisco Systems, which acquired fifty-one firms in six and a half years to add the latest web-related connection products and reshape its strategic direction. Cisco's sophisticated routers and networking equipment serve as the e-business backbone for many Internet companies—a strength the company enhances by buying smaller firms with complementary technology.

Consider Cisco's acquisition of Cerent, which makes fiber-optic equipment. A year before the acquisition, Cisco bought a 9 percent stake in Cerent so it could learn more about the firm and its products. As Cisco's CEO got to know the company better, he saw two key reasons why it would be a good acquisition. First, acquiring Cerent would give Cisco access to the fast-growing market for fiber optics and to Cerent's burgeoning customer base. Second, Cerent's hard-driving, frugal organization culture was similar to Cisco's. Once the decision was made, Cisco negotiated the $6.3 billion acquisition in just two and a half hours spread over three days.

Next, Cisco's integration team stepped in to plan the details before the public announcement. In the two weeks following the agreement, the Cisco team met with Cerent's management to work out differences between the companies' personnel practices and to prepare a package of transition information. Only then did Cerent's CEO announce the acquisition to his employees. Cisco staffers immediately gave every Cerent employee the transition package showing how Cerent's benefits compared with Cisco's benefits. In many cases, Cisco raised salaries and boosted benefits to bring compensation in line with Cisco's compensation. Most important, Cerent's 266 employees were assured that they could never be fired or reassigned without their CEO's permission.

You must get on the Net and find new ways to add value.

—John Chambers, CEO, Cisco Systems*

Thanks to Cisco's advance planning, the acquisition went smoothly, and Cerent's employees were able to focus on their jobs rather than being distracted by uncertainty. E-business is humming, so Cisco will be relying on its acquisition expertise again and again as it aims for as many as twenty-five acquisitions per year.

References: Scott Thurm, "Joining the Fold: Under Cisco's System, Mergers Usually Work; That Defies the Odds," *Wall Street Journal*, March 1, 2000, pp. A1, A12; Andy Serwer, "There's Something About Cisco," *Fortune*, May 15, 2000, pp. 114–138 (*quote on p. 138).

Bases of Relatedness Organizations link their different businesses, industries, or markets in different ways. Table 8.3 gives some typical bases of relatedness. In companies such as Philips, a European consumer electronics company, a similar type of electronics technology underlies all the businesses. A common technology in aircraft design links Boeing's commercial and military aircraft divisions, and a common computer design technology links Compaq's various computer products and peripherals.

Organizations such as Philip Morris, RJR Nabisco, and Procter & Gamble operate multiple businesses related by a common distribution network (grocery stores) and common marketing skills (advertising). Disney and Universal rely on strong brand names and reputations to link their diverse businesses, which include movie studios and theme parks. Pharmaceutical firms such as Merck sell numerous products to a single set of customers: hospitals, doctors, patients, and drug-

Table 8.3

Bases of Relatedness in Implementing Related Diversification

Firms that implement related diversification can do so using any number of bases of relatedness. Four frequently used bases of related uses for diversification are similar technology, common distribution and marketing skills, common brand name and reputation, and common customers.

Basis of Relatedness	Examples
Similar technology	Philips, Boeing, Westinghouse, Compaq
Common distribution and marketing skills	RJR Nabisco, Philip Morris, Procter & Gamble
Common brand name and reputation	Disney, Universal
Common customers	Merck, IBM, AMF-Head

stores. Similarly, AMF-Head sells snow skis, tennis rackets, and sportswear to active, athletic customers.

Advantages of Related Diversification Pursuing a strategy of related diversification has three primary advantages. First, it reduces an organization's dependence on any one of its business activities and thus reduces economic risk. Even if one or two of a firm's businesses lose money, the organization as a whole may still survive because the healthy businesses will generate enough cash to support the others.[21] At The Limited, sales declines at Lerners of New York may be offset by sales increases at Express.

Second, by managing several businesses at the same time, an organization can reduce the overhead costs associated with managing any one business. In other words, if the normal administrative costs required to operate any business, such as legal services and accounting, can be spread over a large number of businesses, then the overhead costs *per business* will be lower than they would be if each business had to absorb all costs itself. Thus, the overhead costs of businesses in a related, diversified firm are usually lower than those of similar businesses that are not part of a larger corporation.[22]

Third, related diversification allows an organization to exploit its strengths and capabilities in more than one business. When organizations do this successfully, they capitalize on synergies, which are complementary effects that exist among their businesses. *Synergy* exists among a set of businesses when the businesses' economic value together is greater than their economic value separately. McDonald's is using synergy as it diversifies into other restaurant and food businesses. For example, its McCafé premium coffee stands in some McDonald's restaurants and its acquisitions of Donatos Pizza, Chipotle Mexican Grill, and Boston Market allow the firm to create new revenue opportunities while utilizing the firm's existing strengths in food-products purchasing and distribution.[23]

Unrelated Diversification

unrelated diversification A strategy in which an organization operates multiple businesses that are not logically associated with one another

Firms that implement a strategy of **unrelated diversification** operate multiple businesses that are not logically associated with one another. At one time, for example,

Quaker Oats owned clothing chains, toy companies, and a restaurant business. Unrelated diversification was a very popular strategy in the 1970s. During this time, several conglomerates like ITT and Transamerica grew by acquiring literally hundreds of other organizations and then running these numerous businesses as independent entities. Even if there are important potential synergies between their different businesses, organizations implementing a strategy of unrelated diversification do not attempt to exploit them.

In theory, unrelated diversification has two advantages. First, a business that uses this strategy should have stable performance over time. During any given period, if some businesses owned by the organization are in a cycle of decline, others may be in a cycle of growth. Unrelated diversification is also thought to have resource allocation advantages. Every year, when a corporation allocates capital, people, and other resources among its various businesses, it must evaluate information about the future of those businesses so that it can place its resources where they have the highest return potential. Given that it owns the businesses in question and thus has full access to information about the future of those businesses, a firm implementing unrelated diversification should be able to allocate capital to maximize corporate performance.

Despite these presumed advantages, research suggests that unrelated diversification usually does not lead to high performance. First, corporate-level managers in such a company usually do not know enough about the unrelated businesses to provide helpful strategic guidance or to allocate capital appropriately. To make strategic decisions, managers must have complete and subtle understanding of a business and its environment. Because corporate managers often have difficulty fully evaluating the economic importance of investments for all the businesses under their wing, they tend to concentrate only on a business's current performance. This narrow attention at the expense of broader planning eventually hobbles the entire organization. Many of International Harvester's problems noted earlier grew from an emphasis on current performance at the expense of investments for the future success of the firm.

Second, because organizations that implement unrelated diversification fail to exploit important synergies, they are at a competitive disadvantage compared to organizations that use related diversification. Universal Studios has been at a competitive disadvantage relative to Disney because its theme parks, movie studios, and licensing divisions are less integrated and therefore achieve less synergy.

For these reasons, almost all organizations have abandoned unrelated diversification as a corporate-level strategy. Transamerica has sold off numerous businesses and now concentrates on a core set of related businesses and markets. Large corporations that have not concentrated on a core set of businesses eventually have been acquired by other companies and then broken up. Research suggests that these organizations are actually worth more when broken up into smaller pieces than they are when joined.[24]

MANAGEMENT IMPLICATIONS Managers should understand the various kinds of corporate strategies that can be adopted from the perspective of strategic business units, or SBUs. Although diversification is a very common corporate-level

strategy, managers should have a clear understanding of whether they should use related or unrelated diversification. Appreciating the bases for relatedness is also important.

■ Implementing Corporate-Level Strategies

In implementing a diversification strategy, organizations face two important questions. First, how will the organization move from a single-product strategy to some form of diversification? Second, once the organization diversifies, how will it manage diversification effectively?

Becoming a Diversified Firm

Most organizations do not start out completely diversified. Rather, they begin operations in a single business, pursuing a particular business-level strategy. Success in this strategy then creates resources and strengths that the organization can use in related businesses.

Internal Development of New Products Some firms diversify by developing their own new products and services within the boundaries of their traditional business operations. Honda followed this path to diversification. Relying on its traditional strength in the motorcycle market, over the years Honda learned how to make fuel-efficient, highly reliable small engines. Honda began to apply its strengths in a new business: manufacturing small, fuel-efficient cars for the Japanese domestic market. These vehicles were first sold in the United States in the late 1960s. Honda's success in U.S. exports led the company to increase the size and improve the performance of its cars. Over the years, Honda has introduced automobiles of increasing quality, culminating in the Acura line of luxury cars. While diversifying into the market for automobiles, Honda also applied its engine-building strengths to produce a line of all-terrain vehicles, portable electric generators, and lawn mowers. In each case, Honda was able to parlay its strengths and resources into successful new businesses.

Replacement of Suppliers and Customers Firms can also become diversified by replacing their former suppliers and customers. A company that stops buying supplies (either manufactured goods or raw materials) from other companies and begins to provide its own supplies has diversified through **backward vertical integration**. Campbell Soup once bought soup cans from several different manufacturers but later began manufacturing its own cans. In fact, Campbell is currently one of the largest can-manufacturing companies in the world, although almost all the cans it makes are used in its soup operations.

An organization that stops selling to one customer and sells instead to that customer's customers has diversified through **forward vertical integration**. G.H. Bass used forward vertical integration to diversify its operations. Bass once sold its

backward vertical integration An organization's beginning the business activities formerly conducted by its suppliers

forward vertical integration An organization stops selling to one customer and sells instead to that customer's customers

shoes and other products only to retail outlets. More recently, however, Bass opened numerous factory outlet stores, which now sell products directly to consumers. Nevertheless, Bass has not abandoned its former customers, retail outlets. Many firms are also employing forward vertical integration today when they use the Internet to market their products and services directly to consumers.

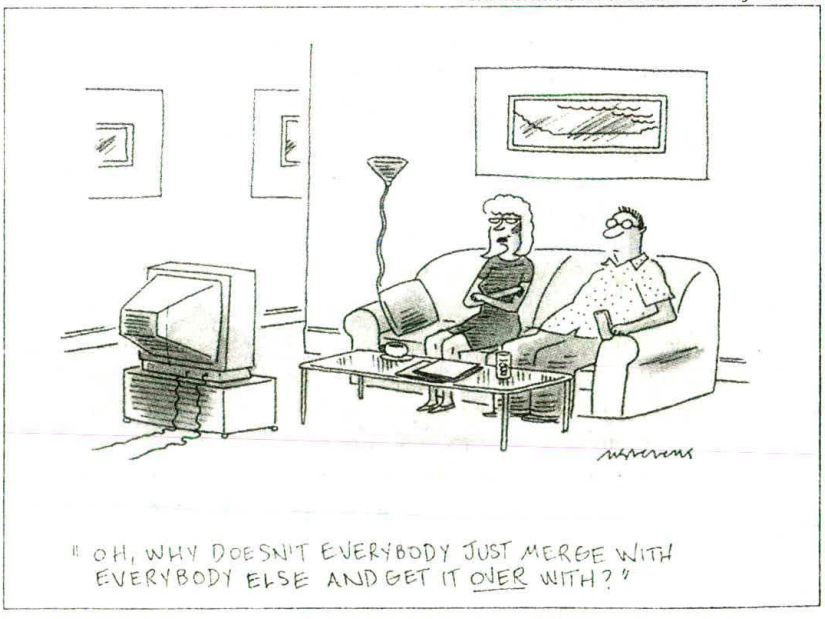
Mergers and Acquisitions Another common way for businesses to diversify is through mergers and acquisitions—that is, through purchasing another organization. Such a purchase is called a **merger** when the two organizations being combined are approximately the same size. It is called an **acquisition** when one of the organizations involved is considerably larger than the other. Organizations engage in mergers and acquisitions to diversify through vertical integration by acquiring former suppliers or former customers. Mergers and acquisitions are also becoming more common in other countries such as Germany and China.[25]

merger The purchase of one firm by another firm of approximately the same size

acquisition The purchase of a firm by another firm that is considerably larger

Most organizations use mergers and acquisitions to acquire complementary products or complementary services, which are products or services linked by a common technology and common customers. The objective of most mergers and acquisitions is the creation or exploitation of synergies.[26] Synergy can reduce the combined organizations' costs of doing business, it can increase revenues, and it may open the way to entirely new businesses for the organization to enter. For example, in early 2000 MGM Grand paid $4.4 billion for its largest competitor in the gambling industry, Mirage Resorts. The deal will allow MGM Grand to compete with other firms more efficiently while eliminating a major rival.[27] The cartoon illustrates another interesting perspective on mergers and acquisitions.

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Mergers and acquisitions are becoming an increasingly popular way to implement corporate-level strategies. Of course, as illustrated in this cartoon, there is at least theoretically a limit to the extent to which mergers and acquisitions can occur. For example, in recent years the U.S. government has blocked the merger of Staples and Office Depot and fought the merger of American Online and Time Warner. The reasons in each case have involved concerns about reduced competition that might, in turn, lead to higher consumer prices.

Managing Diversification

However an organization implements diversification—whether through internal development, vertical integration, or mergers and acquisitions—it must monitor and manage its strategy. The two major tools for managing diversification are (1) organization structure and (2) portfolio management techniques. How organization structure can be used to manage a diversification strategy is discussed in detail in Chapter 12.[28] **Portfolio management techniques** are methods that diversified organizations use to make decisions about what businesses to engage in and how to manage these multiple businesses to maximize corporate performance. Two important portfolio management techniques are the BCG matrix and the GE Business Screen.

portfolio management technique A method that diversified organizations use to make decisions about what businesses to engage in and how to manage these multiple businesses to maximize corporate performance

BCG matrix A method of evaluating businesses relative to the growth rate of their market and the organization's share of the market

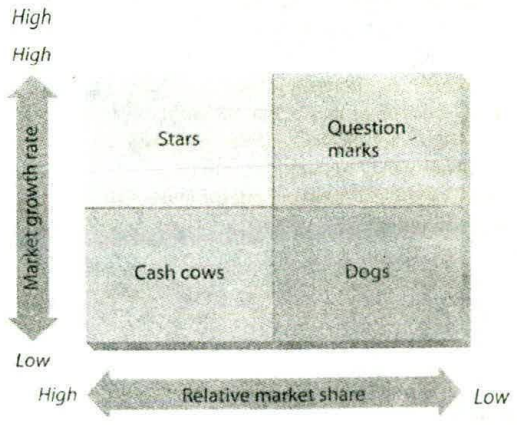
BCG Matrix The **BCG** (for Boston Consulting Group) **matrix** provides a framework for evaluating the relative performance of businesses in which a diversified organization operates. It also prescribes the preferred distribution of cash and other resources among these businesses.[29] The BCG matrix uses two factors to evaluate an organization's set of businesses: the growth rate of a particular market and the organization's share of that market. The matrix suggests that fast-growing markets in which an organization has the highest market share are more attractive business opportunities than slow-growing markets in which an organization has small market share. Dividing market growth and market share into two categories (low and high) creates the simple matrix shown in Figure 8.3.

The matrix classifies the types of businesses that a diversified organization can engage in as dogs, cash cows, question marks, and stars. *Dogs* are businesses that have a very small share of a market that is not expected to grow. Because these businesses do not hold much economic promise, the BCG matrix suggests that organizations either should not invest in them or should consider selling them as soon as possible. *Cash cows* are businesses that have a large share of a market that is not expected to grow substantially. These businesses characteristically generate high profits that the organization should use to support question marks and stars. (Cash cows are "milked" for cash to support businesses in markets that have greater growth potential.) *Question marks* are businesses that have only a small share of a quickly growing market. The future performance of these businesses is uncertain. A question mark that can capture increasing amounts of this growing market may be very profitable. On the other hand, a question mark unable to keep up with market growth is likely to have low profits. The BCG matrix suggests that organizations should carefully invest in question marks. If their performance does not live up to expectations, question marks should be reclassified as dogs and divested. *Stars* are businesses that have the largest share of a rapidly

Figure 8.3

The BCG Matrix

The BCG matrix helps managers develop a better understanding of how different strategic business units contribute to the overall organization. By assessing each SBU on the basis of its market growth rate and relative market share, managers can make decisions about whether to commit further financial resources to the SBU or to sell or liquidate it.



Source: Perspectives, No. 66, "The Product Portfolio." Adapted by permission from The Boston Consulting Group, Inc., 1970.

growing market. Cash generated by cash cows should be invested in stars to ensure their pre-eminent position. For example, when BMW bought Rover a few years ago, experts thought its products would help the German auto maker reach new consumers. But the company was not able to capitalize on this opportunity, so it ended up selling Rover's car business to a British firm and Land Rover to Ford.[30]

GE Business Screen A method of evaluating businesses along two dimensions: (1) industry attractiveness and (2) competitive position; in general, the more attractive the industry and the more competitive the position, the more an organization should invest in a business

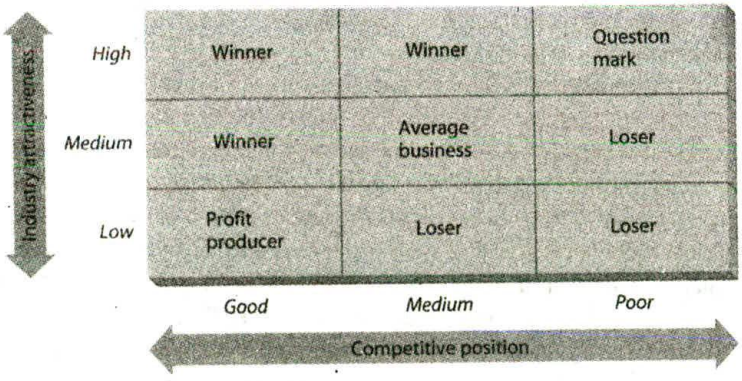
GE Business Screen Because the BCG matrix is relatively narrow and overly simplistic, General Electric (GE) developed the **GE Business Screen**, a more sophisticated approach to managing diversified business units. The Business Screen is a portfolio management technique that can also be represented in the form of a matrix. Rather than focusing solely on market growth and market share, however, the GE Business Screen considers industry attractiveness and competitive position. These two factors are divided into three categories to make the nine-cell matrix shown in Figure 8.4.[31] These cells, in turn, classify business units as winners, losers, question marks, average businesses, or profit producers.

As Figure 8.4 shows, both market growth and market share appear in a broad list of factors that determine the overall attractiveness of an industry and the overall quality of a firm's competitive position. Other determinants of an industry's attractiveness (in addition to market growth) include market size, capital requirements, and competitive intensity. In general, the greater the market growth, the larger the market, the smaller the capital requirements, and the less the competitive intensity, the more attractive an industry will be. Other determinants of an

Figure 8.4

The GE Business Screen

The GE Business Screen is a more sophisticated approach to portfolio management than the BCG matrix. As shown here, several factors combine to determine a business's competitive position and the attractiveness of its industry. These two dimensions, in turn, can be used to classify businesses as winners, question marks, average businesses, losers, or profit producers. Such a classification enables managers to allocate the organization's resources more effectively across various business opportunities.



Competitive position
1. Market share
2. Technological know-how
3. Product quality
4. Service network
5. Price competitiveness
6. Operating costs

Industry attractiveness
1. Market growth
2. Market size
3. Capital requirements
4. Competitive intensity

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organization's competitive position in an industry (besides market share) include technological know-how, product quality, service network, price competitiveness, and operating costs. In general, businesses with large market share, technological know-how, high product quality, a quality service network, competitive prices, and low operating costs are in a favorable competitive position.

Think of the GE Business Screen as a way of applying SWOT analysis to the implementation and management of a diversification strategy. The determinants of industry attractiveness are similar to the environmental opportunities and threats in SWOT analysis, and the determinants of competitive position are similar to organizational strengths and weaknesses. By conducting this type of SWOT analysis across several businesses, a diversified organization can decide how to invest its resources to maximize corporate performance. In general, organizations should invest in winners and in question marks (where industry attractiveness and competitive position are both favorable), should maintain the market position of average businesses and profit producers (where industry attractiveness and competitive position are average), and should sell losers. For example, Unilever recently assessed its business portfolio using a similar framework and, as a result, decided to sell off several specialty chemical units that were not contributing to the firm's profitability as much as other businesses. The firm then used the revenues from these divestitures and bought more related businesses such as Ben & Jerry's Homemade and Slim-Fast.[32]

MANAGEMENT IMPLICATIONS Diversification can be achieved through the internal development of new products, replacement of suppliers and customers, and mergers and acquisitions. Managers who are pursuing a diversification strategy should know the advantages and disadvantages of each type of diversification. In addition, they should understand how to manage multiple business units by using such frameworks as the BCG matrix or the GE Business Screen.

Summary of Key Points

A strategy is a comprehensive plan for accomplishing the organization's goals. Strategic management is a comprehensive and ongoing process aimed at formulating and implementing effective strategies. Effective strategies address three organizational issues: distinctive competency, scope, and resource deployment. Most large companies have both business-level and corporate-level strategies. Strategy formulation is the set of processes involved in creating or determining the strategies of an organization. Strategy implementation is the process of executing strategies.

SWOT analysis considers an organization's strengths, weaknesses, opportunities, and threats. Using SWOT analysis, an organization chooses strategies that support its mission and (1) exploit its opportunities and strengths, (2) neutralize its threats, and (3) avoid its weaknesses. Common strengths cannot be ignored, but distinctive competencies hold the greatest promise for superior performance.

A business-level strategy is the plan an organization uses to conduct business in a particular industry or market. Porter suggests that businesses may formulate a differentiation strategy, an overall cost leadership strategy, or a focus strategy at this level. According to Miles and Snow, organizations may choose one of four business-level strategies: prospector, defender, analyzer, or reactor. Business-level strategies may also take into account the stages in the product life cycle.

Strategy implementation at the business level takes place in the areas of marketing, sales, accounting and finance, and manufacturing. Organization culture also influences strategy implementation. Implementation of Porter's generic strategies requires different emphases in each of these organizational areas. Implementation of Miles and Snow's strategies affects organization structure and practices.

A corporate-level strategy is the plan an organization uses to manage its operations across several businesses. A firm that does not diversify is implementing a single-product strategy. An organization pursues a strategy of related diversification when it operates a set of businesses that are somehow linked. Related diversification reduces the financial risk associated with any particular product, reduces the overhead costs of each business, and enables the organization to create and exploit synergy. An organization pursues a strategy of unrelated diversification when it operates a set of businesses that are not logically associated with one another.

Strategy implementation at the corporate level addresses two issues: how the organization will go about its diversification and the way that an organization is managed once it has diversified. Businesses accomplish strategy implementation in three ways: developing new products internally, replacing suppliers (backward vertical integration) or customers (forward vertical integration), and engaging in mergers and acquisitions. Organizations manage diversification through the organization structure that they adopt and through portfolio management techniques. The BCG matrix classifies an organization's diversified businesses as dogs, cash cows, question marks, or stars according to market share and market growth rate. The GE Business Screen classifies businesses as winners, losers, question marks, average businesses, or profit producers according to industry attractiveness and competitive position.

Discussion Questions

Questions for Review

1. What are the two main types of strategic alternatives available to an organization?
2. How does a deliberate strategy differ from an emergent strategy?
3. List and describe Porter's generic strategies and the Miles and Snow typology of strategies.
4. What are the differences among a single-product strategy, a related diversification strategy, and an unrelated diversification strategy?

Questions for Analysis

5. Common strengths among firms cannot give one firm a competitive advantage. Does this mean that an organization should ignore its common strengths in choosing and implementing its strategies? Why or why not?

6. Suppose that an organization does not have any distinctive competencies. If the organization can acquire some distinctive competencies, how long are these strengths likely to remain distinctive competencies? Why?
7. Suppose that an organization moves from a single-product strategy to a strategy of related diversification. How might the organization use SWOT analysis to select attributes of its current business to serve as bases of relatedness among its newly acquired businesses?
8. For decades, Ivory Soap advertised that it is 99 percent pure. Ivory refused to add deodorants, facial creams, or colors to its soap. It also packages its soap in plain paper wrappers—no foil or fancy printing. Is Ivory implementing a product differentiation, low cost, or focus strategy, or some combination of the three? Explain your answer.

Questions for Application

9. Interview a manager and categorize the business- and corporate-level strategies of his or her organization according to Porter's generic strategies, the Miles and Snow typology, and extent of diversification.
10. Will implementing a differentiation strategy always improve an organization's performance? Give three real-world examples in which differentiation did not seem to improve an organization's performance, and describe why it did not. What do these "errors" have in common?

BUILDING EFFECTIVE *decision-making* SKILLS

Exercise Overview

Decision-making skills refer to the manager's ability to recognize and define problems and opportunities correctly and then to select an appropriate course of action to solve problems and capitalize on opportunities. As noted in the chapter, many organizations use SWOT analysis as part of the process of strategy formulation. This exercise will help you better understand how managers obtain the information they need to perform such an analysis and use it as a framework for making decisions.

Exercise Background

SWOT is an acronym for strengths, weaknesses, opportunities, and threats. Good strategies are those that exploit an organization's opportunities and strengths while neutralizing threats and avoiding or correcting weaknesses.

Assume that you have just been hired to run a medium-size manufacturing company. The firm has been manufacturing electric motors, circuit breakers, and similar electronic components for industrial use. In recent years, the firm's financial performance has gradually eroded. You have been hired to turn things around.

Meetings with both current and former top managers of the firm have led you to believe that a new strategy is needed. In earlier times the firm was successful in part because its products were of top quality, which allowed the company to charge premium prices for them. Recently, however, various cost-cutting measures have resulted in a decrease in quality. Competition has also increased. As a result, your firm no longer has a reputation for top quality products, but your manufacturing costs are still relatively high. The next thing you want to do now is to conduct a SWOT analysis.

Exercise Task

With the situation described above as context, do the following:

1. List the sources you will use to obtain information about the firm's strengths, weaknesses, opportunities, and threats.
2. Rate each source in terms of its probable reliability.
3. Rate each source in terms of how easy or difficult it will be to access.
4. How confident should you be in making decisions based on the information obtained?

BUILDING EFFECTIVE *conceptual* SKILLS

Exercise Overview

Conceptual skills refer to the manager's ability to think in the abstract. This exercise gives you some experience in using your conceptual skills on real business opportunities and potential.

Exercise Background

Many successful managers have had at one time or another an idea for using an existing product for new purposes or in new markets. For example, Arm & Hammer baking soda (a food product used in cooking) is now also widely used to absorb odors in refrigerators. Commercials advise consumers simply to open a box of Arm & Hammer and place it in their refrigerators. This has led to a big increase in the sales of the baking soda.

In other situations, managers have extended product life cycles by taking the products into new markets. The most common example today involves products that are becoming obsolete in more industrialized countries but are being introduced in less industrialized countries.

Exercise Task

Apply your conceptual skills by doing each of the following:

1. List ten simple products that have relatively straightforward purposes (i.e., a pencil, which is used for writing).
2. Next, try to identify two or three alternative uses for each product (i.e., a pencil can be used as a splint for a broken finger in an emergency).
3. Evaluate the market potential for each alternative product use as high, moderate, or low (i.e., the market potential for pencils used as splints is low).
4. Form small groups of two or three members and pool your ideas. Each group should choose two or three ideas to present to the class.

BUILDING EFFECTIVE *technical* SKILLS

Exercise Overview

Technical skills are necessary for the manager to accomplish or understand the specific kind of work being done in an organization. This exercise will enable you to sharpen your technical skills with regard to using the Internet and to see how the Internet can facilitate strategic planning.

Exercise Background

Select a company in which you have some interest. It might be a firm that you would like to work for, one where someone you know works, or a firm that is simply in the news a lot. Next, identify the two or three firms that you see as being the firm's biggest competitors. Visit the web sites of the company you originally se-

lected and the competitors you subsequently identified.

Exercise Task

With the preceding background information as context, do the following:

1. Analyze the business and corporate strategies being used by the firm you originally selected.
2. Analyze the business and corporate strategies being used by its competitors.
3. Evaluate the effectiveness of each firm's strategies.

CHAPTER CLOSING CASE

PEPSI'S NEW STRATEGIC FORMULA

The high stakes rivalry between Pepsi-Cola and Coca-Cola is being played out in supermarkets, restaurants, and convenience stores all over the world. Pepsi-Cola has worked for years, with limited success, to catch up to market-leader Coca-Cola, trying strategy after strategy to regain ground in the United States and abroad. In 1965, Pepsi sought growth through diversification by acquiring Frito-Lay, which makes popular snacks such as Lay's Potato Chips and Doritos. This diversification proved so lucrative that the company, renamed PepsiCo, decided to diversify into fast-food restaurants—thought to be good outlets for soft drinks and snacks—through the purchase of Pizza Hut, Taco Bell, and Kentucky Fried Chicken.

By the mid-1990s, however, snack sales were increasing but growth in the fast-food business had slowed, as had growth in soft drinks. So in 1997, PepsiCo changed its strategy, spinning off the restaurants as a separate business to concentrate on exploiting the synergy between its snacks and its soft drinks. By now, snacks had become PepsiCo's main source of profits—a complete reversal from the early days of diversification, when profits from soft drinks had dwarfed profits from snacks.

Next, PepsiCo introduced its "Power of One" strategy to boost both beverage and snack sales in U.S. supermarkets. Visiting with the CEOs of the twenty-five top chains, PepsiCo's CEO compared the stores' 9 percent profit margins on PepsiCo products with the typical 2 percent margins earned on other items. He stressed that the stores could increase sales and profits by giving PepsiCo products more shelf space and displaying PepsiCo drinks with Frito-Lay snacks. "Power of One" paid off, giving Frito-Lay and Pepsi-Cola more domestic market share. It also gave PepsiCo drinks a huge sales boost in smaller grocery stores throughout Mexico. There, Frito-Lay's Sabritas brand is the runaway market leader, thanks to a low-cost strategy that keeps retail prices as low as sixteen cents per snack.

PepsiCo continued to diversify by buying Tropicana, the leading orange juice brand, and Cracker Jack, a perennial favorite that had lost profitability. By adding more peanuts and offering a four-ounce bag in addition to smaller single-serving and larger family-size packages, PepsiCo returned Cracker Jack to profitability within a year. In addition, through aggressive marketing, the company made best-sellers of its bottled waters and bottled teas. Now PepsiCo's Lipton Iced Tea holds a commanding lead over Coca-Cola's Nestea bottled teas. Pepsi-Cola's sales still lag Coca-Cola's sales in the United States, but PepsiCo's Mountain Dew recently pulled ahead of Diet Coke to become the country's third-largest-selling soda.

Outside the United States, PepsiCo's new soft-drink strategy is to focus on building sales and share in developing countries such as India, where Coca-Cola is not

yet the undisputed market leader. This strategy reverses PepsiCo's previous strategy of doggedly battling Coca-Cola in every market. Populous Asian nations such as China and Japan are particular targets for PepsiCo's snack business. Although Frito-Lay holds just a tiny share of the snack market in those countries today, PepsiCo's CEO sees them as the cornerstone of future growth.

Case Questions

1. Where in the Miles and Snow typology does the "Power of One" strategy fit?
2. Which of Porter's generic strategies is Frito-Lay's Sabritas brand pursuing in Mexico? Which is PepsiCo pursuing with its soft-drink strategy?
3. What should PepsiCo consider before implementing its "Power of One" strategy around the world?

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