Chapter - 1

Management: Science, Theory, and Practice

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

1. Explain the nature and purpose of management.
2. Understand that management, as used in this book, applies to all kinds of organizations and to managers at all organizational levels.
3. Recognize that the aim of all managers is to create a surplus.
4. Identify the trends in information technology and globalization.
5. Explain the concepts of productivity, effectiveness, and efficiency.
6. Describe the evolution of management and some recent contributions to management thought.
7. Describe the various approaches to management, their contributions, as well as their limitations.
8. Show how the management process, or operational, approach to management theory and science has a basic core of its own and draws from other approaches.
9. Realize that managing requires a systems approach and that practice must always take into account situations and contingencies.
10. Define the managerial functions of planning, organizing, staffing, leading, and controlling.

One of the most important human activities is managing. Ever since people began forming groups to accomplish aims they could not achieve as individuals, managing has been essential to ensure the coordination of individual efforts. As society has come to rely increasingly on group effort, and as many organized groups have become large, the task of managers has been rising in importance. The purpose of this book is to promote excellence among all persons in organizations, especially among managers, aspiring managers, and other professionals.*

Definition of Management: Its Nature and Purpose

Management The process of designing and maintaining an environment in which individuals, working together in groups, efficiently accomplish selected aims.

Management is the process of designing and maintaining an environment in which individuals, working together in groups, efficiently accomplish selected aims. This basic definition needs to be expanded:

- As managers, people carry out the managerial functions of planning, organizing, staffing, leading, and controlling.
- Management applies to any kind of organization.
- It applies to managers at all organizational levels.
- The aim of all managers is the same: to create a surplus.
- Managing is concerned with productivity, which implies effectiveness and efficiency.

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Here are some managers you may know: Steve Jobs at Apple Computer; Bill Ford, Jr., at Ford Motor Company; Scott McNealy of Sun Microsystems; Jack Welch of General Electric and his successor, Jeff Immelt; Cisco's John Chambers; and Bill Gates of Microsoft. One of the most powerful managers is George W. Bush, President of the United States. The Governor of the State of California is also a manager and, in some ways, so is Pope John Paul II, the head of the Roman Catholic Church, one of the largest global organizations. But middle-level managers and first-line supervisors also make important contributions to the goal of their organizations.

All manage organizations. We define an **organization** as a group of people working together to create a surplus. In business organizations,

* At times, the term *nonmanager* is used in reference to persons who have no subordinates. Thus, nonmanagers include professionals who may have a high status in organizations.

this surplus is profit. In nonprofit organizations, such as charitable organizations, it may be satisfaction of needs. Universities also create a surplus through generation and dissemination of knowledge as well as providing service to the community or society.

The Functions of Management

Five managerial functions around which managerial knowledge is organized in this book: planning, organizing, staffing, leading, controlling.

Many scholars and managers have found that the analysis of management is facilitated by a useful and clear organization of knowledge. In studying management, therefore, it is helpful to break it down into five managerial functions—planning, organizing, staffing, leading, and controlling—around which the knowledge that underlies those functions can be organized. Thus, the concepts, principles, theory, and techniques of management are grouped into these five functions in this book.

This framework has been used and tested for many years. Although there are different ways of organizing managerial knowledge, most textbook authors today have adopted this or a similar framework even after experimenting at times with alternative ways of structuring knowledge.

External elements that affect operation: economic, technological, social, ecological, political, and ethical factors.

Although the emphasis in this book is on managers' tasks that pertain to designing an internal environment for performance within an organization, it must never be overlooked that managers must operate in the external environment of an enterprise as well. Clearly, managers cannot perform their tasks well unless they have an understanding of, and are responsive to, the many elements of the external environment—economic, technological, social, ecological, political, and ethical factors—that affect their areas of operation. Moreover, many organizations now operate in different countries. Therefore, this book takes a global perspective of managing.

Management as an Essential for Any Organization

Enterprise A business, government agency, hospital, university, or any other type of organization.

Managers are charged with the responsibility of taking actions that will enable individuals to make their best contributions to group objectives. Management thus applies to small and large organizations, to profit and not-for-profit enterprises, to manufacturing as well as service industries. The term **enterprise** refers to a business, government agency, hospital, university, and any other type of organization, since almost everything said in this book refers to business as well as nonbusiness organizations. Effective management is the concern of the corporation president, the hospital administrator, the government first-line supervisor, the Boy Scout

leader, the church bishop, the baseball manager, and the university president.

Managerial Functions at Different Organizational Levels

In this book, no basic distinction is made between managers, executives, administrators, and supervisors. To be sure, a given situation may differ considerably between various levels in an organization or between various types of enterprises. Similarly, the scope of authority held may vary and the types of problems dealt with may be considerably different. Furthermore, the person in a managerial role may be directing people in the sales, engineering, or finance department. But the fact remains that, as managers, all obtain results by establishing an environment for effective group endeavor.

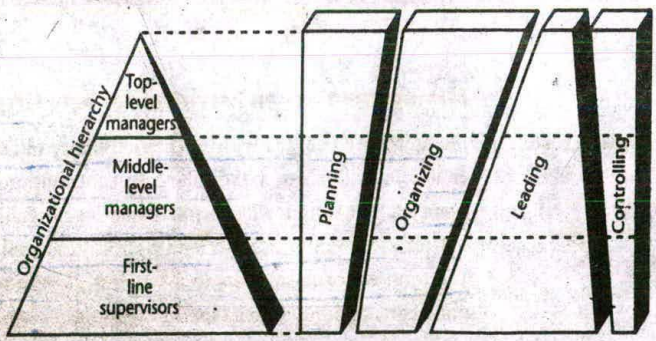
All managers carry out managerial functions, but the time spent for each function may differ.

All managers carry out managerial functions. However, the time spent for each function may differ. Figure 1-1 shows an approximation of the relative time spent for each function. Thus, top-level managers spend more time on planning and organizing than do lower-level managers. Leading, on the other hand, takes a great deal of time for first-line supervisors. The difference in time spent on controlling varies only slightly for managers at various levels.

Managerial Skills and the Organizational Hierarchy

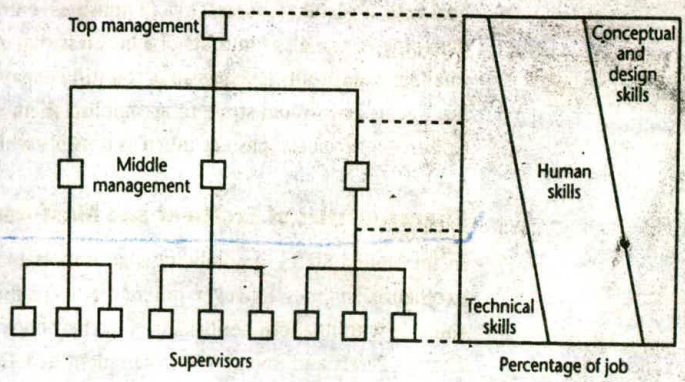
Robert L. Katz identified three kinds of skills for administrators.[1] To these may be added a fourth—the ability to design solutions.

FIGURE 1-1 Time spent in carrying out managerial functions



Partly based on and adapted from Thomas A. Mahoney, Thomas H. Jerdee, and Stephen J. Carroll, "The Job(s) of Management," *Industrial Relations* (February 1965), pp. 97–110.

FIGURE 1-2 Skills and management levels



Four skills required of administrators: technical, human, conceptual, and design skills.

The relative importance of these skills may differ at various levels in the organizational hierarchy. As shown in Figure 1-2, *technical skills* are of greatest importance at the supervisory level, and *human skills* are helpful in the frequent interactions with subordinates. *Conceptual and design skills*, on the other hand, are usually not critical for lower-level supervisors. At the middle management level, the need for technical skills decreases, human skills are still essential, while conceptual skills gain in importance. At the top management level, conceptual and design abilities and human skills are especially valuable, but there is relatively little need for technical abilities. It is assumed, especially in large companies, that chief executive officers (CEOs) can utilize the technical abilities of their subordinates. In smaller firms, however, technical experience may still be quite important.

The Goals of All Managers and Organizations

The aim of all managers should be to create a surplus, by establishing an environment in which people can accomplish group goals with the least amount of time, money, materials, and personal dissatisfaction.

Nonbusiness executives sometimes say that the aim of business managers is simple—to make a profit. But profit is really only a measure of a surplus of sales receipts over expenses. For many businesses, an important goal is the long-term increase in the value of their common stock. Michael Porter at Harvard is critical about the emphasis of shareholder value when he wrote that "we lost sight of profitability as the goal and substituted shareholder value measured by stock price."[2] This, Porter suggests, has destroyed many enterprises. In a very real sense, in all kinds of organizations, whether business or nonbusiness, the logical and publicly desirable aim of all managers should be a *surplus*. Thus, managers must establish an environment in which people can accomplish group goals with the least amount of time, money, materials, and personal

dissatisfaction or in which they can achieve as much as possible of a desired goal with available resources. In a nonbusiness enterprise such as a police department, as well as in units of a business that are not responsible for total business profits (such as an accounting department), managers still have goals and should strive to accomplish them with the minimum of resources or to accomplish as much as possible with available resources.

Characteristics of Excellent and Most Admired Companies

In the United States, profitability is an important measure of company excellence. At times, however, other criteria are also used that frequently coincide with financial performance. In their book *In Search of Excellence*, Thomas Peters and Robert Waterman identified 43 companies that they regarded as excellent.[3] In choosing the firms, they considered factors such as growth of assets and equity, average return on total capital, and similar measures. They also asked industry experts about the innovativeness of the companies.

The authors identified eight characteristics of excellent enterprises. Specifically, these firms

1. were oriented toward action
2. learned about the needs of their customers
3. promoted managerial autonomy and entrepreneurship
4. achieved productivity by paying close attention to the needs of their people
5. were driven by a company philosophy often based on the values of their leaders
6. focused on the business they knew best
7. had a simple organization structure with a lean staff
8. were centralized as well as decentralized, depending on appropriateness

Two years after *In Search of Excellence* was published, *Business Week* took a second look at the companies that Peters and Waterman had considered excellent.[4] The magazine's survey revealed that at least 14 of the 43 companies did not measure up very well to several of the eight characteristics of excellence. Nine companies showed a great decline in earnings. While Peters and Waterman have been criticized in several respects (e.g., their methods of collecting and interpreting the data, such as extensive use of anecdotes and quotations from leaders in the field rather than using more scientific research sources), the performance review of the firms indicated that success may be only transitory and that it demands continuing hard work to adapt to the changes in the environment.[5]

International Perspective

The Most Admired Companies in America[6]

In *Fortune*'s annual survey of 530 companies, 10,000 executives, directors, and security analysts were asked to rate the companies in their own industry. The following eight attributes were used in the ranking: innovativeness, quality of management, talents of the employees, financial soundness, the way corporate assets were used, long-term investment value, social responsibility, and the quality of the companies' products/services.

The ten most admired companies listed in *Fortune*'s March 4, 2002, issue were [the figures in brackets indicate the ranking during the previous year]:

1 [1] General Electric (electronics)
2 [4] Southwest Airlines
3 [3] Wal-Mart (general merchandise)
4 [5] Microsoft (computer software)
5 [7] Berkshire Hathaway (financial)
6 [6] Home Depot (specialty retailer)
7 [12] Johnson & Johnson (pharmaceuticals)
8 [16] FedEx (delivery)
9 [11] Citigroup (megabank)
10 [9] Intel (semiconductors)

General Electric topped this list for the fifth straight year. FedEx and Johnson & Johnson improved considerably in the ranking. Of course, notorious companies such as Enron, Tyco, and Global Crossing were not on this list. Those companies have been accused of questionable activities.

Advances in Information Technology and Globalization: Adapting to Changes in the 21st Century

To be successful in the 21st century, companies must take advantage of information technology—especially the Internet—and globalization.

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Information technology[7]

The World Wide Web has a pervasive impact on both organizations and individuals. The Internet connects people and organizations through a global network. Electronic commerce (e-commerce) is increasingly used for transactions between individuals and companies (B2C), but especially between businesses (B2B). The number of people connecting to the Internet varies between countries. At this time, the United States, Canada, the Nordic countries in Europe, and Australia have the highest network

access rates. But other countries, including developing countries, are rapidly connecting to the global network.

Another trend (especially in Europe and Japan) is the use of m-commerce, that is, mobile or wireless commerce. Increasingly, people can communicate without computers by using wireless devices. In Japan, for example, NTT DoCoMo has developed an Internet service called i-mode, which has already many million subscribers. These services will increase as soon as third-generation wireless technology makes the speedy transmission of data (including video) possible. These technology trends are so important that they will be further discussed in Chapter 19 and in Part 6 closing.

Globalization[8]

The second major trend is globalization. Most major corporations have an international presence. The World Trade Organization (WTO), an umbrella organization, was established in 1995 to govern international trade. Despite street protests at WTO meetings, globalization continues. The gains from globalization not only benefit Western corporations but also result in higher incomes for people in other countries, such as China.[9] Clearly, managers must develop an international perspective. Chapter 3 will address several global issues in detail.

Productivity, Effectiveness, and Efficiency

Another way to view the aim of managers is that they must raise productivity. After World War II, the United States became the world leader in productivity. But in the late 1960s, productivity growth began to decelerate. Today, the urgent need for productivity improvement is recognized around the world by governments, industry, and universities. Often one looks to Japan to find answers to our productivity problem (a subject to be considered later in Chapter 3), but what tends to be overlooked is the importance of effectively performing basic managerial and nonmanagerial activities.

Definition of productivity

Productivity The output–input ratio within a time period with due consideration for quality.

Successful companies create a surplus through productive operations. Although there is no complete agreement on the true meaning of **productivity**, let us define it as the output–input ratio within a time period with due consideration for quality. It can be expressed as follows:

$$\text{Productivity} = \frac{\text{Outputs}}{\text{Inputs}} \text{ (within a time period, quality considered)}$$

The formula indicates that productivity can be improved by (1) increasing outputs with the same inputs, (2) decreasing inputs but maintaining the same outputs, or (3) increasing outputs and decreasing inputs to change the ratio favorably. Companies use several kinds of inputs, such as labor, materials, and capital. Total-factor productivity combines various inputs to arrive at a composite input. In the past, productivity improvement programs were mostly aimed at the worker level. Yet, as Peter F. Drucker, one of the most prolific writers in management, observed, "The greatest opportunity for increasing productivity is surely to be found in knowledge work itself, and especially in management."[10]

Effectiveness The achievement of objectives.

Efficiency The achievement of the ends with the least amount of resources.

Definitions of effectiveness and efficiency

Productivity implies effectiveness and efficiency in individual and organizational performance. **Effectiveness** is the achievement of objectives. **Efficiency** is the achievement of the ends with the least amount of resources. Managers cannot know whether they are productive unless they first know their goals and those of the organization, a topic that will be discussed in Chapter 4.

Managing: Science or Art?

Managing as practice is an art; the organized knowledge underlying the practice is a science.

Managing, like all other practices—whether medicine, music composition, engineering, accountancy, or even baseball—is an art. It is know-how. It is doing things in light of the realities of a situation. Yet managers can work better by using the organized knowledge about management. It is this knowledge that constitutes a science. Thus, managing as practice is an *art*; the organized knowledge underlying the practice may be referred to as a *science*. In this context, science and art are not mutually exclusive; they are complementary.

As science improves, so should art, as has happened in the physical and biological sciences. To be sure, the science underlying managing is fairly crude and inexact because the many variables that managers deal with are extremely complex. Nevertheless, such management knowledge can certainly improve managerial practice. Physicians without the advantage of science would be little more than witch doctors. Executives who attempt to manage without management science must trust to luck, intuition, or what they did in the past.

In managing, as in any other field, unless practitioners are to learn by trial and error (and it has been said that managers' errors are their subordinates' trials), there is no place they can turn to for meaningful guidance other than the accumulated knowledge underlying their practice.

The Evolution of Management Thought

Many different contributions of writers and practitioners have resulted in different approaches to management, and these make up a "management theory jungle." Later in this chapter, you will learn about the different patterns of management analysis and what can be done to untangle the jungle. Table 1-1 summarizes the major contributions of management writers and practitioners.[11] We will highlight Frederick Taylor's scientific management, Henri Fayol's modern operational management theory, and Elton Mayo and F. J. Roethlisberger's Hawthorne studies.

TABLE 1-1 The emergence of management thought

Name and year of major work	Major contribution to management
	Scientific management
Frederick W. Taylor *Shop Management* (1903) *Principles of Scientific Management* (1911) *Testimony before the Special House Committee* (1912)	Acknowledged as the father of scientific management. His primary concern was to raise productivity through greater efficiency in production and increased pay for workers, by applying the scientific method. His principles emphasize using science, creating group harmony and cooperation, achieving maximum output, and developing workers.
Henry L. Gantt (1901)	Called for scientific selection of workers and "harmonious cooperation" between labor and management. Developed the Gantt chart (Chapter 19). Stressed the need for training.
Frank and Lillian Gilbreth (1900)	Frank is known primarily for his time and motion studies. Lillian, an industrial psychologist, focused on the human aspects of work and the understanding of workers' personalities and needs.
	Modern operational management theory
Henri Fayol *Administration Industrielle et Générale* (1916)	Referred to as the father of modern management theory. Divided industrial activities into six groups: technical, commercial, financial, security, accounting, and managerial. Recognized the need for teaching management. Formulated 14 principles of management, such as authority and responsibility, unity of command, scalar chain, and esprit de corps.

TABLE 1.1 continued

Name and year of major work	Major contribution to management
	Behavioral sciences
Hugo Münsterberg (1912)	Application of psychology to industry and management.
Walter Dill Scott (1910, 1911)	Application of psychology to advertising, marketing, and personnel.
Max Weber (translations 1946, 1947)	Theory of bureaucracy.
Vilfredo Pareto (books 1896–1917)	Referred to as the father of the social systems approach to organization and management.
Elton Mayo and F. J. Roethlisberger (1933)	Famous studies at the Hawthorne plant of the Western Electric Company on the influence of social attitudes and relationships of work groups on performance.
	Systems theory
Chester Barnard *The Functions of the Executive* (1938)	The task of managers is to maintain a system of cooperative effort in a formal organization. Suggested a comprehensive social systems approach to managing.
	Modern management thought
Many authors are discussed in this book. Major contributors include Chris Argyris, Robert R. Blake, C. West Churchman, Ernest Dale, Keith Davis, Mary Parker Follett, Frederick Herzberg, G. C. Homans, Harold Koontz, Rensis Likert, Douglas McGregor, Abraham H. Maslow, Lyman W. Porter, Herbert Simon, George A. Steiner, Lyndall Urwick, Norbert Wiener, and Joan Woodward.	
Peter F. Drucker (1974)	Very prolific writer on many general management topics.
W. Edwards Deming (after World War II)	Introduced quality control in Japan.
Laurence Peter (1969)	Observed that eventually people get promoted to a level where they are incompetent.
William Ouchi (1981)	Discussed selected Japanese managerial practices adapted in the U.S. environment.
Thomas Peters and Robert Waterman (1982)	Identified characteristics of companies they considered excellent.

Source: Some information in this table is based on Claude S. George, Jr., *The History of Management Thought* (Englewood Cliffs, NJ: Prentice Hall, 1972).

Frederick Taylor and Scientific Management[12]



Frederick W. Taylor
1856–1915
(Historical Pictures Service, Chicago)

Frederick Winslow Taylor gave up going to college and started out as an apprentice pattern maker and machinist in 1875, joined the Midvale Steel Company in Philadelphia as a machinist in 1878, and rose to the position of chief engineer after earning a degree in engineering through evening study. He invented high-speed steel-cutting tools and spent most of his life as a consulting engineer. Taylor is generally acknowledged as the father of scientific management. Probably no other person has had a greater impact on the early development of management. His experiences as an apprentice, a common laborer, a foreman, a master mechanic, and then the chief engineer of a steel company gave Taylor ample opportunity to know first-hand the problems and attitudes of workers and to see the great possibilities for improving the quality of management.

Taylor's famous work *Principles of Scientific Management* was published in 1911. The fundamental principles that Taylor saw underlying the scientific approach to management are as follows:

- Replacing rules of thumb with science (organized knowledge).
- Obtaining harmony, rather than discord, in group action.
- Achieving cooperation of human beings, rather than chaotic individualism.
- Working for maximum output, rather than restricted output.
- Developing all workers to the fullest extent possible for their own and their company's highest prosperity.

You will notice that these basic precepts of Taylor's are not far from the fundamental beliefs of the modern manager.

Henri Fayol, the Father of Modern Management Theory[13]



Henri Fayol
1841–1925
(Ronald T. Greenwood)

Perhaps the real father of modern management theory is the French industrialist Henri Fayol. He recognized a widespread need for principles and management teaching. Consequently, he identified 14 such principles, noting that they are flexible, not absolute, and must be usable regardless of changing conditions. Let us look at some of these principles:

Authority and responsibility. Fayol suggests that authority and responsibility are related, with the latter arising from the former. He sees authority as a combination of official factors, deriving from the manager's position, and personal factors, "compounded of intelligence, experience, moral worth, past service, etc."

- *Unity of command.* Employees should receive orders from one superior only.
- *Scalar chain.* Fayol thinks of this as a "chain of superiors" from the highest to the lowest ranks, which, while not to be departed from needlessly, should be short-circuited when following it scrupulously would be detrimental.
- *Esprit de corps.* This is the principle that "in union there is strength," as well as an extension of the principle of unity of command, emphasizing the need for teamwork and the importance of communication in obtaining it.

Fayol regarded the elements of management as the functions of planning, organizing, commanding, coordinating, and controlling.

Elton Mayo and F. J. Roethlisberger and the Hawthorne Studies



Elton Mayo
1880–1949
(Baker Library, Harvard University Graduate School of Business Administration)

www.thoemmes.com/encyclopedia/mayo.htm

Elton Mayo, F. J. Roethlisberger, and others undertook the famous experiments at the Hawthorne plant of the Western Electric Company between 1927 and 1932.[14] Earlier, from 1924 to 1927, the National Research Council made a study in collaboration with Western Electric to determine the effect of illumination and other conditions on workers and their productivity. Finding that productivity improved when illumination was either increased or decreased for a test group, the researchers were about to declare the whole experiment a failure. However, Mayo of Harvard saw in it something unusual and, with Roethlisberger and others, continued the research.

What Mayo and his colleagues found, partly on the basis of the earlier thinking of Vilfredo Pareto, was to have a dramatic effect on management thought. Changing illumination for the test group, modifying rest periods, shortening workdays, and varying incentive pay systems did not seem to explain changes in productivity. Mayo and his researchers then came to the conclusion that other factors were responsible. They found, in general, that the improvement in productivity was due to such social factors as morale, satisfactory interrelationships between members of a work group (a sense of belonging), and effective management—a kind of managing that takes into account human behavior, especially group behavior, and serves it through such interpersonal skills as motivating, counseling, leading, and communicating. This phenomenon, arising basically from people being "noticed," has been named the Hawthorne effect.

Recent Contributors to Management Thought

Among the contributors to management thought are public administrators, business managers, and behavioral scientists, whose important works are discussed throughout this book. We will mention only a few here.

Peter F. Drucker has written on a variety of general management topics.[15] Keith Davis helped us understand the informal organization. The late W. Edwards Deming[16] and Joseph M. Juran,[17] two Americans, did much to improve the quality of Japanese products. The late Laurence Peter suggested that eventually people get promoted to a level where they are incompetent and no further promotion is possible. Unfortunately, this may result in organizations with incompetent people. William Ouchi, who wrote the best-selling book *Theory Z*, showed how selected Japanese management practices may be adapted in the United States. Finally, Thomas Peters and Robert Waterman discussed characteristics of excellent companies. Most of these works are discussed in greater detail in other parts of this book.

Patterns of Management Analysis: A Management Theory Jungle?

Although academic writers and theorists contributed notably little to the study of management until the early 1950s—previous writings having come largely from practitioners—the past four to five decades have seen a veritable deluge of writing from the academic halls. The variety of approaches to management analysis, the amount of research, and the great number of differing views have resulted in much confusion as to what management is, what management theory and science is, and how managerial events should be analyzed. As a matter of fact, Harold Koontz many years ago called this situation "the management theory jungle."[18] Since that time, the vegetation in this jungle has changed somewhat—new approaches have developed and older approaches have taken on some new meanings with some new words attached, but the developments of management science and theory still have the characteristics of a jungle.

The various approaches to management analysis are summarized in Figure 1-3, where they are grouped into 14 categories. The characteristics, contributions, and limitations of each approach are shown in the figure. We will focus here on the managerial roles approach and the management process (or operational) approach.

FIGURE 1.3 Approaches to management

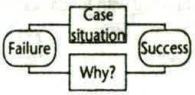
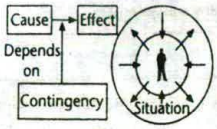
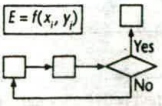
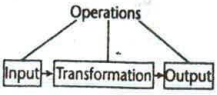
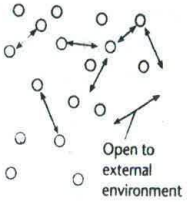
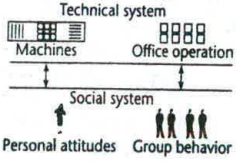
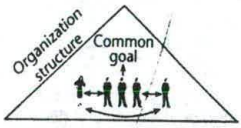
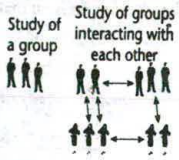
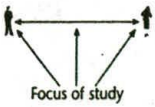
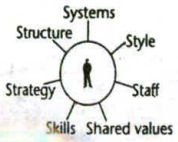
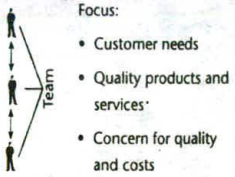
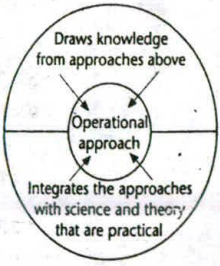
Characteristics/Contributions	Limitations	Illustration
Empirical, or case, approach		
Studies experience through cases. Identifies successes and failures.	Situations are all different. No attempt to identify principles. Limited value for developing management theory.	
Managerial roles approach		
Original study consisted of observations of five chief executives. On the basis of this study, ten managerial roles were identified and grouped into interpersonal, informational, and decision roles.	Original sample was very small. Some activities are not managerial. Many activities are evidence of planning, organizing, staffing, leading, and controlling. Some important managerial activities are left out (e.g., appraising managers).	
Contingency, or situational, approach		
Managerial practice depends on circumstances (i.e., a contingency or a situation). Contingency theory recognizes the influence of given solutions on organizational behavior patterns.	Managers have long realized that there is no one best way to do things. Difficult to determine all relevant contingency factors and to show their relationships. Can be very complex.	
Mathematical, or "management science," approach		
Sees managing as mathematical processes, concepts, symbols, and models. Looks at management as a purely logical process, expressed in mathematical symbols and relationships.	Preoccupation with mathematical models. Many aspects in managing cannot be modeled. Mathematics is a useful tool, but hardly a school or an approach to management.	
Decision theory approach		
Focuses on the making of decisions, persons or groups making decisions, and the decision-making process. Some theorists use decision making as a springboard to study all enterprise activities. The boundaries of study are no longer clearly defined.	There is more to managing than making decisions. The focus is at the same time too narrow and too wide.	

FIGURE 1.3 continued

Characteristics/Contributions	Limitations	Illustration
Reengineering approach		
Concerned with fundamental rethinking, process analysis, radical redesign, and dramatic results.	Neglects external environment. Possibly ignores customers' needs. Neglects human needs. Ignores total management system, unlike the management process, or operational, approach.	
Systems approach		
Systems concepts have broad applicability. Systems have boundaries, but they also interact with the external environment; that means organizations are open systems. Recognizes the importance of studying interrelatedness of planning, organizing, and controlling in an organization as well as in the many subsystems.	Can hardly be considered a new approach to management, as claimed by some proponents of this approach.	
Sociotechnical systems approach		
Technical system has a great effect on social system (personal attitudes, group behavior). Focuses on production, office operations, and other areas with close relationships between the technical system and people.	Emphasizes only blue-collar and lower-level office work. Ignores much of other managerial knowledge.	
Cooperative social systems approach		
Concerned with both interpersonal and group behavioral aspects leading to a system of cooperation. Expanded concept includes any cooperative group with a clear purpose.	Too broad a field for the study of management. At the same time, it overlooks many managerial concepts, principles, and techniques.	
Group behavior approach		
Emphasizes behavior of people in groups. Based on sociology and social psychology. Primarily studies group behavior patterns. The study of large groups is often called organizational behavior.	Often not integrated with management concepts, principles, theory, and techniques. Need for closer integration with organizational structure design, staffing, planning, and controlling.	

Characteristics/Contributions	Limitations	Illustration
Interpersonal behavior approach		
Focuses on interpersonal behavior, human relations, leadership, and motivation. Based on individual psychology.	Ignores planning, organizing, and controlling. Psychological training is not enough for becoming an effective manager.	
McKinsey's 7-S framework		
The seven S's are (1) strategy, (2) structure, (3) systems, (4) style, (5) staff, (6) shared values, and (7) skills.	Although this experienced consulting firm uses a framework similar to that found useful by Koontz and colleagues since 1955 and confirms its practicality, the terms used are not precise and topics are not discussed in depth.	
Total quality management approach		
Focuses on providing dependable, satisfying products and services (Deming) or products or services that are fit for use (Juran), as well as conforming to quality requirements (Crosby). The general concepts are continuous improvement, attention to details, teamwork, and quality education.	No complete agreement on what total quality management is.	
Management process, or operational, approach		
Draws together concepts, principles, techniques, and knowledge from other fields and managerial approaches. The attempt is to develop science and theory with practical application. Distinguishes between managerial and nonmanagerial knowledge. Develops a classification system built around the managerial functions of planning, organizing, staffing, leading, and controlling.	Does not, as some authors do, identify representing or coordination as a separate function. Coordination, for example, is the essence of managership and is the purpose of managing.	

The Managerial Roles Approach

One widely discussed approach to management theory is the managerial roles approach, popularized by Henry Mintzberg of McGill University.[19] Essentially, his approach is to observe what managers actually do and from such observations come to conclusions as to what managerial activities (or roles) are. Although many researchers have studied the actual work of managers—from CEOs to line supervisors—Mintzberg has given this approach higher visibility.

After systematically studying the activities of five CEOs in a variety of organizations, Mintzberg came to the conclusion that executives do not perform the classical managerial functions of planning, organizing, commanding, coordinating, and controlling. Instead, they engage in a variety of other activities. From his research and the research of others who had studied what managers actually did, Mintzberg concluded that managers really fill a series of ten roles:

Interpersonal roles

1. The figurehead role (performing ceremonial and social duties as the organization's representative)
2. The leader role
3. The liaison role (particularly with outsiders)

Informational roles

4. The recipient role (receiving information about the operation of an enterprise)
5. The disseminator role (passing information to subordinates)
6. The spokesperson role (transmitting information to those outside the organization)

Decision roles

7. The entrepreneurial role
8. The disturbance-handler role
9. The resource-allocator role
10. The negotiator role (dealing with various persons and groups of persons)

Mintzberg's approach has also been criticized. In the first place, the sample of five CEOs used in his research is far too small to support so sweeping a conclusion. In the second place, in analyzing the actual activities of managers—from CEOs to supervisors—any researcher must realize that all managers do some work that is not purely managerial; one would expect

even presidents of large companies to spend some of their time in public and stockholder relations, in fund-raising, and perhaps in dealer relations, marketing, and so on. In the third place, many of the activities Mintzberg found are in fact evidence of planning, organizing, staffing, leading, and controlling. For example, what is resource allocation but planning? The entrepreneurial role is certainly an element of planning. And the interpersonal roles are mainly instances of leading. In addition, the informational roles can be fitted into a number of the functional areas.

Nevertheless, looking at what managers really do can have considerable value. In analyzing activities, an effective manager might wish to ascertain how activities and techniques fall into the various fields of knowledge reflected by the basic functions of managers. However, the roles Mintzberg identified appear to be incomplete. Where does one find such unquestionably important managerial activities as structuring an organization, selecting and appraising managers, and determining major strategies? Omissions such as these make one wonder whether the executives in his sample were really effective managers. They certainly raise a serious question as to whether the managerial roles approach, at least as put forth here, is an adequate one on which to base a practical, operational theory of management.

The Management Process, or Operational, Approach

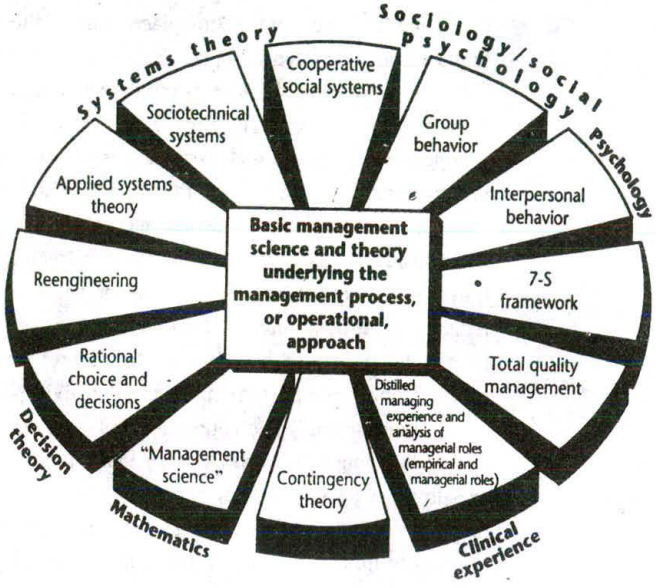
The management process, or operational, approach draws together the pertinent knowledge of management by relating it to the managerial job.

The process, or operational, approach to management theory and science draws together the pertinent knowledge of management by relating it to the managerial job—what managers do. Like other operational sciences, it tries to integrate the concepts, principles, and techniques that underlie the task of managing.

This approach recognizes that there is a central core of knowledge about managing that is pertinent only to the field of management. Such matters as line and staff, departmentation, managerial appraisal, and various managerial control techniques involve concepts and theories found only in situations involving managers. In addition, this approach draws on and absorbs knowledge from other fields, including systems theory, quality and reengineering concepts, decision theory, theories of motivation and leadership, individual and group behavior, social systems, and cooperation and communications, as well as the application of mathematical analyses and concepts.

The nature of this approach can be seen in Figure 1-4. As this diagram shows, the management process, or operational, school recognizes the

FIGURE 1-4 The management process, or operational, approach

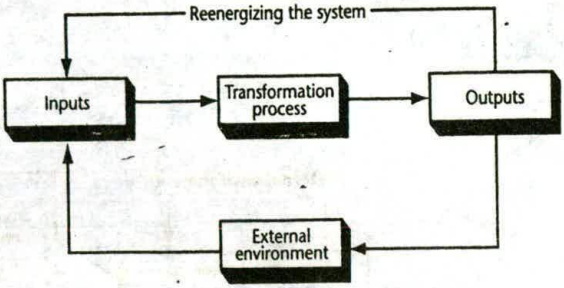


existence of a central core of science and theory peculiar to managing and also draws important contributions from various other schools and approaches. In addition, the management process theorist is interested not in all the important knowledge in these various fields but only in that which is deemed most useful and relevant to managing.

The Systems Approach to the Management Process

An organized enterprise does not, of course, exist in a vacuum. Rather, it is dependent on its external environment; it is a part of larger systems, such as the industry to which it belongs, the economic system, and society. Thus, the enterprise receives inputs, transforms them, and exports the outputs to the environment, as shown by the very basic model in Figure 1-5. However, this simple model needs to be expanded and developed into a model of process, or operational, management that indicates how the various inputs are transformed through the managerial functions of planning, organizing, staffing, leading, and controlling, as shown in Figure 1-6. When Peter Senge, the author of *The Fifth Discipline: The Art and Practice of the Learning Organization*, was asked what the most important issue is that faces domestic and international businesses today,

FIGURE 1-5 Input–output model



he said, "I would say the system of management."[20] This book is about the systems approach to the management process. Not only is the concern about the internal functioning of the enterprise, but it must include the interactions between the enterprise and its external environment.

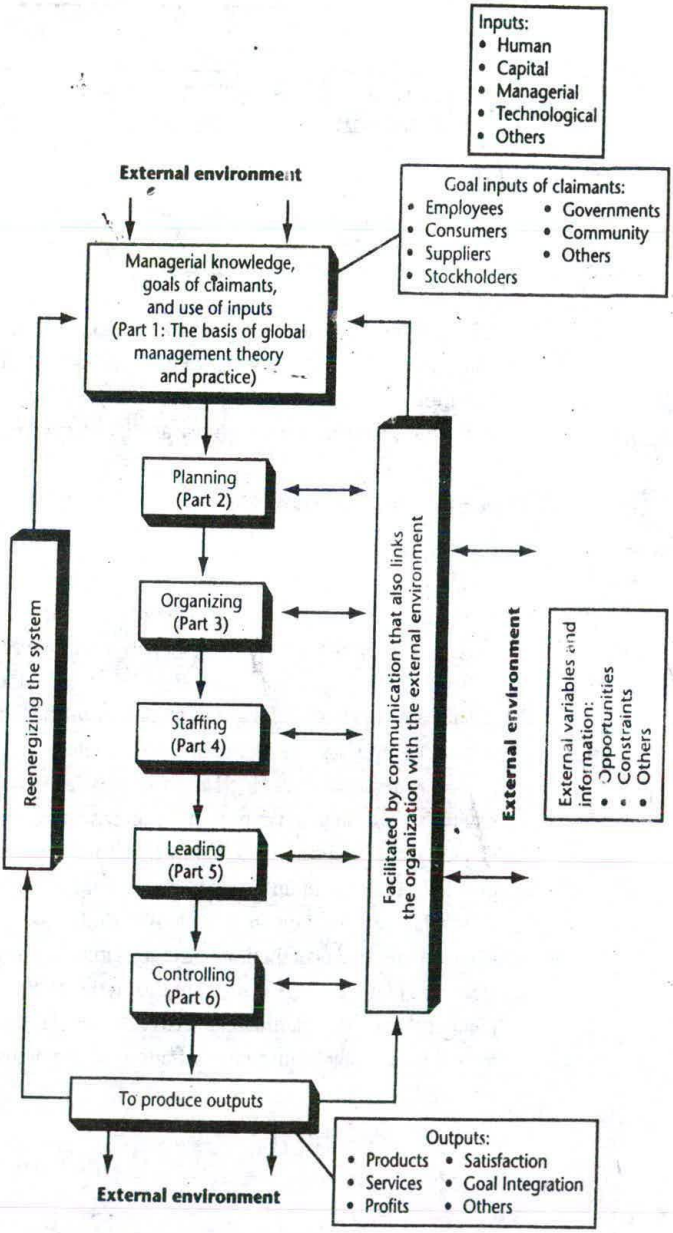
Inputs and Claimants*

Inputs: people, capital, managerial skills, technical knowledge and skills.

The inputs from the external environment (see Figure 1-6) may include people, capital, managerial skills, as well as technical knowledge and skills. In addition, various groups of people make demands on the enterprise. For example, employees want higher pay, more benefits, and job security. Consumers demand safe and reliable products at reasonable prices. Suppliers want assurance that their products will be bought. Stockholders want not only a high return on their investment but also security for their money. Federal, state, and local governments depend on taxes paid by the enterprise, but they also expect the enterprise to comply with their laws. Similarly, the community demands that enterprises be "good citizens," providing the maximum number of jobs with a minimum of pollution. Other claimants to the enterprise may include financial institutions and labor unions; even competitors have a legitimate claim for fair play. It is clear that many of these claims are incongruent, and it is the manager's job to integrate the legitimate objectives of the claimants. This may need to be done through compromises, trade-offs, and denial of the manager's own ego.

* Claimants may also be called stakeholders.

FIGURE 1-6 Systems approach to management



The Managerial Transformation Process

The task of managers is to transform the inputs, in an effective and efficient manner, into outputs.

- It is the task of managers to transform the inputs, in an effective and efficient manner, into outputs. Of course, the transformation process can be viewed from different perspectives. Thus, one can focus on such diverse enterprise functions as finance, production, personnel, and marketing. Writers on management look at the transformation process in terms of their particular approaches to management. Specifically, writers belonging to the human behavior school focus on interpersonal relationships, social systems theorists analyze the transformation by concentrating on social interactions, and those advocating decision theory see the transformation as sets of decisions. However, the most comprehensive and useful approach for discussing the job of managers is to use the managerial functions of planning, organizing, staffing, leading, and controlling as a framework for organizing managerial knowledge. Therefore, this is the approach used as the framework of this book (see Figure 1-6).

The Communication System

Communication is essential to all phases of the managerial process for two reasons. First, it integrates the managerial functions. For example, the objectives set in planning are communicated so that the appropriate organization structure can be devised. Communication is essential in the selection, appraisal, and training of managers to fill the roles in this structure. Similarly, effective leadership and the creation of an environment conducive to motivation depend on communication. Moreover, it is through communication that one determines whether events and performance conform to plans. Thus, it is communication that makes managing possible.

The second purpose of the communication system is to link the enterprise with its external environment, where many of the claimants are. For example, one should never forget that customers, who are the reason for the existence of virtually all businesses, are outside a company. It is through the communication system that the needs of customers are identified; this knowledge enables the firm to provide products and services at a profit. Similarly, it is through an effective communication system that the organization becomes aware of competition and other potential threats and constraining factors.

External Variables

Effective managers will regularly scan the external environment. While it is true that managers may have little or no power to change the external environment, they have no alternative but to respond to it. The forces acting in the external environment are discussed in various chapters, especially in chapters 2, 3, and 5.

Outputs

Outputs: products, services, profits, satisfaction, integration of the goals of claimants to the enterprise.

It is the task of managers to secure and utilize inputs to the enterprise to transform them through the managerial functions—with due consideration for external variables—into outputs. Although the kinds of outputs will vary with the enterprise, they usually include many of the following: products, services, profits, satisfaction, and integration of the goals of various claimants to the enterprise. Most of these outputs require no elaboration, and only the last two will be discussed.

The organization must indeed provide many "satisfactions" if it hopes to retain and elicit contributions from its members. It must contribute to the satisfaction not only of basic material needs (e.g., employees' needs to earn money for food and shelter or to have job security) but also of the needs for affiliation, acceptance, esteem, and perhaps even self-actualization so that one can realize one's potential at the workplace.

Another output is goal integration. As noted earlier, the different claimants to the enterprise have very divergent—and often directly opposing—objectives. It is the task of managers to resolve conflicts and integrate these aims.

Reenergizing the System

Finally, it is important to note that, in the systems model of the management process, some of the outputs become inputs again. Thus, the satisfaction and new knowledge or skills of employees become important human inputs. Similarly, profits, the surplus of income over costs, are reinvested in cash and capital goods, such as machinery, equipment, buildings, and inventory. You will see shortly that the model shown in Figure 1-6 will serve as a framework in this book for organizing managerial knowledge. But let us first look closer at the managerial functions.

The Functions of Managers

The functions of managers provide a useful structure for organizing management knowledge (see the central part of Figure 1-6). There have been no new ideas, research findings, or techniques that cannot readily be placed in the classifications of planning, organizing, staffing, leading, and controlling.

Planning

Planning Selecting missions and objectives as well as the actions to achieve them, which requires decision making.

Planning involves selecting missions and objectives as well as the actions to achieve them; it requires decision making, that is, choosing future courses of action from among alternatives. As Chapter 4 will show, there are various types of plans, ranging from overall purposes and objectives to the most detailed actions to be taken, such as ordering a special stainless steel bolt for an instrument or hiring and training workers for an assembly line. No real plan exists until a decision—a commitment of human or material resources—has been made. Before a decision is made, all that exists is a planning study, an analysis, or a proposal; there is no real plan. The various aspects of planning are discussed in Part 2 of this book.

Organizing

People working together in groups to achieve some goal must have roles to play, much like the parts actors fill in a drama, whether these roles are the ones they develop themselves, are accidental or haphazard, or are defined and structured by someone who wants to make sure that they contribute in a specific way to group effort. The concept of a role implies that what people do has a definite purpose or objective; they know how their job objective fits into the group effort, and they have the necessary authority, tools, and information to accomplish the task. This can be seen in as simple a group effort as setting up camp on a fishing expedition. Everyone could do anything he or she wants to do, but activity would almost certainly be more effective and certain tasks would be less likely to be left undone if one or two persons were given the job of gathering firewood, some the assignment of getting water, others the task of starting a fire, yet others the job of cooking, and so on.

Organizing Establishing an intentional structure of roles for people to fill in an organization.

Organizing, then, is that part of managing which involves establishing an intentional structure of roles for people to fill in an organization. It is intentional in the sense of making sure that all the tasks necessary to accomplish goals are assigned and, it is hoped, assigned to people who can do them best.

The purpose of an organization structure is to help create an environment for human performance. It is then a management tool and not an end in and of itself. Although the structure must define the tasks to be done, the roles so established must also be designed in light of the abilities and motivations of the people available.

Designing an effective organization structure is not an easy managerial task. Many problems are encountered in making structures fit situations, including both defining the kinds of jobs that must be done and finding the people to do them. These problems and the essential theory, principles, and techniques of handling them are the subjects of Part 3.

Staffing

Staffing Filling, and keeping filled, the positions in the organization structure.

Staffing involves filling, and keeping filled, the positions in the organization structure. This is done by identifying work-force requirements; inventorying the people available; and recruiting, selecting, placing, promoting, appraising, planning the careers of, compensating, and training or otherwise developing both candidates and current jobholders so that tasks are accomplished effectively and efficiently. This subject is dealt with in Part 4.

Leading

Leading Influencing people so that they will contribute to organizational and group goals.

Leading is influencing people so that they will contribute to organizational and group goals; it has to do predominantly with the interpersonal aspect of managing. All managers would agree that their most important problems arise from people—their desires and attitudes as well as their behavior as individuals and in groups—and that effective managers also need to be effective leaders. Since leadership implies followership and people tend to follow those who offer a means of satisfying their own needs, wishes, and desires, it is understandable that leading involves motivation, leadership styles and approaches, and communication. The essentials of these subjects are dealt with in Part 5.

Controlling

Controlling Measuring and correcting individual and organizational performance to ensure that events conform to plans.

Controlling is measuring and correcting individual and organizational performance to ensure that events conform to plans. It involves measuring performance against goals and plans, showing where deviations from standards exist, and helping to correct deviations from standards. In short, controlling facilitates the accomplishment of plans. Although planning

must precede controlling, plans are not self-achieving. Plans guide managers in the use of resources to accomplish specific goals; then activities are checked to determine whether they conform to the plans.

Control activities generally relate to the measurement of achievement. Some means of controlling, like the budget for expenses, inspection records, and the record of labor-hours lost, are generally familiar. Each of them measures, and each shows, whether plans are working out. If deviations persist, correction is indicated. But what is corrected? Activities, through persons. Nothing can be done about reducing scrap, for example, or buying according to specifications, or handling sales returns unless one knows who is responsible for these functions. Compelling events to conform to plans means locating the persons who are responsible for results that differ from planned action and then taking the necessary steps to improve performance. Thus, outcomes are controlled by controlling what people do. This subject is treated in Part 6.

Coordination, the Essence of Managership

Some authorities consider coordination to be a separate function of the manager. It seems more accurate, however, to regard it as the essence of managership, for achieving harmony among individual efforts toward the accomplishment of group goals. Each of the managerial functions is an exercise contributing to coordination.

Even in the case of a church or a fraternal organization, individuals often interpret similar interests in different ways, and their efforts toward mutual goals do not automatically mesh with the efforts of others. It thus becomes the central task of the manager to reconcile differences in approach, timing, effort, or interest and to harmonize individual goals to contribute to organizational goals.

The Systems Model of Management and the Organization of This Book

The model of the systems approach to management is also the foundation for organizing managerial knowledge. Note that in Figure 1-6 the numbers shown in the model correspond to the parts of this book. Part 1 covers the basis of management and the interactions between the organization and its environment. This part cuts across all managerial functions. It deals with basic managerial knowledge, such as theory, science, and practice. It also discusses the evolution of management and the various approaches

to management. Since organizations are open systems, they interact with the external environment: domestic and international.

The figure also shows that Part 2 deals with the various aspects of planning (chapters 4 to 6). Part 3 is concerned with organizing (chapters 7 to 10), while Part 4 deals with staffing (chapters 11 to 13), Part 5 with leading (chapters 14 to 17), and Part 6 with controlling (chapters 18 to 20).

This book has a global perspective of management. Increasingly, organizations operate in the global market. Therefore, comparative and international management aspects are discussed not only in Chapter 3 but also throughout the book.

The model shown in Figure 1-6 is repeated at the beginning of parts 2 to 6, but with the appropriate part highlighted. This feature of an integrative model shows the relationships of the topics in this book.

Summary

Management is the process of designing and maintaining an environment for efficiently accomplishing selected aims. Managers carry out the functions of planning, organizing, staffing, leading, and controlling. Managing is an essential activity at all organizational levels; however, the managerial skills required vary with the organizational level. The goal of all managers is to create a surplus. Enterprises must take advantage of the 21st century trends in information technology and globalization. They must also focus on productivity, that is, to achieve a favorable output–input ratio within a specific time period with due consideration for quality. Productivity implies effectiveness (achieving of objectives) and efficiency (using the least amount of resources). Managing as practice is an art; organized knowledge about management is a science.

Many writers and practitioners have contributed to the development of management thought. The major contributors and their works are shown in Table 1-1. Many theories about management have been proposed, and each contributes something to our knowledge of what managers do. The characteristics and contributions as well as the limitations of the various approaches to management are summarized in Figure 1-3. The management process (or operational) approach draws from other theories of management and integrates them into a total system of managing.

The organization is an open system that operates within and interacts with the environment. The systems approach to management includes

inputs from the external environment and from claimants, the transformation process, the communication system, external factors, outputs, and a way to reenergize the system. The transformation process consists of the managerial functions, which also provide the framework for organizing knowledge in this book. Throughout the book, but especially in Chapter 3, international aspects of managing are emphasized.

KEY IDEAS AND CONCEPTS FOR REVIEW

Management
Managerial functions
Managerial skills in the organizational hierarchy
The goal of all managers
Characteristics of excellent and most admired companies
Two major trends in the 21st century
Productivity, effectiveness, and efficiency
Managing: science or art?
Major contributors to management thought
Contributors to scientific management
Fayol's operational management theory
Mayo and Roethlisberger
Recent contributors to management thought
Management theory jungle
Managerial roles approach
Management process, or operational, approach
Systems approach to the management process
Five managerial functions

FOR DISCUSSION

1. How would you define management? Does your definition differ from the one offered in this book? Explain.
2. What are the managerial functions?
3. How do the required managerial skills differ in the organizational hierarchy?
4. In what fundamental way are the basic goals of all managers at all levels and in all kinds of enterprises the same?
5. What are some of the characteristics of excellent companies (according to Peters and Waterman)? Do the companies you know have these characteristics?
6. What are the differences between productivity, effectiveness, and efficiency?
7. Is managing a science or an art? Could the same explanation apply to engineering or accounting?
8. Why has Frederick Taylor been called the father of scientific management and Henri Fayol the father of modern management theory?
9. What is meant by the term *management theory jungle*?
10. Identify the various approaches to management analysis. Discuss their characteristics and contributions as well as their limitations.

EXERCISES/ACTION STEPS

1. Interview two local business managers and ask them how they learned about managing. Ask what kind of books they might have read on management (e.g., textbooks or popular books). Here are examples of management books: Gary Hamel and C. K. Prahalad, *Competing for the Future*; Michael Hammer and James Champy, *Reengineering the Corporation*; Charles Handy, *The Age of Paradox*; John P. Kotter, *The New Rules: How to Succeed in Today's Post-Corporate World*; Peter M. Senge, *The Fifth Discipline*. Probe to what extent these books have helped them to manage. You may also find it interesting to read one of the best-selling books on management and mention it in the class discussion.
2. Interview two public administrators and ask them how their job differs from that of business managers. How do they know how well their department, agency, or organization is performing since profit is probably not one of their criteria for measuring effectiveness and efficiency? Do they consider management an art or a science?

INTERNET RESEARCH

1. Review three of the following Web sites for current topics of management: *www.businessweek.com, www.economist.com, www.fortune.com, www.forbes.com, www.industryweek.com, http://public.wsj.com/home.html, www.hbsp.harvard.edu/products/hbr/index.html, http://mitsloan.mit.edu/smr/index.html.*
2. Read the cover stories of *Business Week*, *Fortune*, and *The Economist* on the Web (*www.businessweek.com, www.fortune.com, www.economist.com*) and identify any section in this book that relates to these stories.

International Case

McDonald's: Serving Fast Food around the World[21]

Ray Kroc opened the first McDonald's restaurant in 1955 in the United States. He offered a limited menu of high-quality, moderately priced food served fast in spotless surroundings. McDonald's QSC&V (quality, service, cleanliness, and value) was a hit. The chain expanded into every state in the nation. By 1983 it had more than 6,000 restaurants in the United States, and by 1995 it had more than 18,000 restaurants in 89 countries, located in six continents. In 1995 alone, the company built 2,400 restaurants, and by 2001 it had more than 29,000 restaurants in 121 countries.

In 1967, McDonald's opened its first restaurant outside the United States—in Canada. Since then, its international growth accelerated. In 1995, the "Big Six" countries that provided about 80 percent of the international operating income were Canada, Japan, Germany, Australia, France, and Britain. Yet fast food has barely touched many cultures. The opportunities for expanding the market are great, as 99 percent of the world population are not yet McDonald's customers. For example, in China, with a population of 1.2 billion people, there were only 62 McDonald's

restaurants in 1995. McDonald's vision is to be the major player in food services around the world.

In Europe, McDonald's maintains a small percentage of restaurant sales but commands a large share of the fast-food market. It took the company 14 years of planning before it opened a restaurant in Moscow in 1990. But the planning paid off. After the opening, people were standing in line for up to two hours for a hamburger. It has been said that McDonald's restaurant in Moscow attracts more visitors (on average 27,000 daily) than Lenin's mausoleum (about 9,000 people), which used to be *the* place to see. The Beijing opening in 1992 attracted some 40,000 people to the largest (28,000 square foot) McDonald's restaurant in China at a location where some 800,000 pedestrians pass by every day. Food is prepared in accordance with local laws. For example, the menus in Arab countries comply with Islamic food preparation laws. In 1995, McDonald's opened its first kosher restaurant in Jerusalem, where it does not serve dairy products. The taste for fast food, American style, is growing more rapidly abroad than at home. McDonald's international sales have been increasing by a large percentage every year. Every day, more than 33 million people eat at McDonald's around the world, with 18 million of them in the United States.

Prices vary considerably around the world, ranging from $3.81 in Switzerland to $0.78 in Argentina for the Big Mac, which costs in the United States $2.49.* *The Economist* magazine even devised a Big Mac index to estimate whether a currency is over- or undervalued.[22] For example, the $1.27 Chinese Mac translates into an implied purchasing power parity of $4.22. The inference is that the Chinese currency is undervalued. Here are other price comparisons for the $2.49 U.S. Big Mac: Chile $2.16, Euro area $2.37, Hong Kong $1.40, Japan $2.01, Mexico $2.37, Peru $2.48, Singapore $1.81, and Thailand $1.27.

McDonald's traditional menu has been surprisingly successful. People with diverse dining habits have adopted burgers and fries wholeheartedly. Before McDonald's introduced the Japanese to french fries, potatoes were used in Japan only to make starch. The Germans thought hamburgers were people from the city of Hamburg. Now McDonald's also serves chicken, sausage, and salads. Another item, a very different product, is pizza. In Norway, McDonald's serves grilled salmon sandwich, in the Philippines pasta in a sauce with frankfurter bits, and in Uruguay hamburger with a poached egg. Any new venture is risky and can be either a very profitable addition or a costly experiment.

Despite the global operations, McDonald's stays in close contact with its customers, who want good taste, fast and friendly service, clean surroundings, and quality. To attain quality, so-called quality assurance centers are located in the United States, Europe, and Asia. In addition, training plays an important part in customer service. Besides day-to-day coaching, Hamburger universities in the United States, Germany, Britain, Japan, and Australia teach the necessary skills in 22 languages with the aim of providing 100 percent customer satisfaction. It is interesting that

* All dollar values are in U.S. dollars in this book.

McDonald's was one of the first restaurants in Europe to welcome families with children. Not only are children welcomed, but in many restaurants they are also entertained with crayons and paper, a playland, and the clown Ronald McDonald, who can speak 20 languages.

With generally aging populations, McDonald's takes aim at the adult market. With heavy advertising (it has been said that McDonald's will spend $200 million to promote the new burger), the company introduced Arch Deluxe on a potato-flower bun with lettuce, onions, ketchup, tomato slices, American cheese, grainy mustard, and mayonnaise. Although McDonald's considers the over-50 adult burger a great success, a survey conducted five weeks after its introduction showed mixed results.

McDonald's golden arches promise the same basic menu and QSC&V in every restaurant. Its products, handling and cooking procedures, and kitchen layouts are standardized and strictly controlled. McDonald's revoked the first French franchise because the franchisee failed to meet its standards for fast service and cleanliness, even though their restaurants were highly profitable. This may have delayed its expansion in France.

McDonald's restaurants are run by local managers and crews. Owners and managers attend the Hamburger University near Chicago or in other places around the world to learn how to operate a McDonald's restaurant and maintain QSC&V. The main campus library and modern electronic classrooms (which include simultaneous translation systems) are the envy of many universities. When McDonald's opened in Moscow, a one-page advertisement resulted in 30,000 inquiries about the jobs; 4,000 people were interviewed and some 300 were hired. The pay is about 50 percent higher than the average Soviet salary.

McDonald's ensures consistent products by controlling every stage of the distribution. Regional distribution centers purchase products and distribute them to individual restaurants. The centers will buy from local suppliers if the suppliers can meet detailed specifications. McDonald's has had to make some concessions to available products. For example, it is difficult to introduce the Idaho potato in Europe because of special soil requirements.

McDonald's uses essentially the same competitive strategy in every country: be first in a market and establish its brand as rapidly as possible by advertising very heavily. New restaurants are opened with a bang. So many people attended the opening of one Tokyo restaurant that the police closed the street to vehicles. The strategy has helped McDonald's develop a strong market share in the fast-food market, even though its U.S. competitors and new local competitors quickly enter the market.

McDonald's advertising campaigns are based on local themes and reflect the different environments. In Japan, where burgers are a snack, McDonald's competes against confectioneries and new "fast sushi" restaurants. Many of the charitable causes McDonald's supports abroad have been recommended by its local restaurants.

McDonald's business structures take a variety of forms, with 66 percent of the restaurants being franchises. The development licenses are similar to franchising, but they do not require

McDonald's investment. Joint ventures are undertaken when understanding of the local environment is critically important. The McDonald's Corporation operates about 21 percent of the restaurants. McDonald's has been willing to relinquish the most control to its Far Eastern operations, where many restaurants are joint ventures with local entrepreneurs, who own 50 percent or more of the restaurant.

European and South American restaurants are generally company-operated or franchised (although there are many affiliates, or joint ventures, in France). Like the U.S. franchises, restaurants abroad are allowed to experiment with their menus. In Japan, hamburgers are smaller because they are considered a snack. The Quarter Pounder does not make much sense to people on a metric system, so it is called a Double Burger. Some German restaurants serve beer; some French restaurants serve wine. Some Far Eastern McDonald's restaurants offer oriental noodles. In Canada, the menu includes cheese, vegetables, pepperoni, and deluxe pizza. However, these new items must not disrupt the existing operation.

Despite its success, McDonald's faces tough competitors, such as Burger King, Wendy's, Kentucky Fried Chicken (KFC), and now also Pizza Hut. Moreover, fast food in reheatable containers is now also sold in supermarkets, delicatessens, convenience stores, and even gas stations. McDonald's has done very well, with a great percentage of profits coming now from international operations. For example, McDonald's dominates the Japanese market with 1,860 outlets (half the Japanese market) in 1996 compared to only 43 Burger King restaurants. However, the British food conglomerate Grand Metropolitan PLC, which owns Burger King, has an aggressive strategy for Asia. Although McDonald's has been in a very favorable competitive position, since 2001 the customer satisfaction level has been below that of its competitors Wendy's and Burger King. In China, KFC is more popular than McDonald's.[21] Some observers suggest that McDonald's has expanded too fast and that Burger King and Wendy's have tastier meals. It is Mr. Jack Greenberg's (McDonald's top manager) task to change things around.

Questions

1. What opportunities and threats did McDonald's face? How did it handle them? What alternatives could it have chosen?
2. Before McDonald's entered the European market, few people believed that fast food could be successful in Europe. Why do you think McDonald's succeeded? What strategies did it follow? How did these differ from its strategies in Asia?
3. What is McDonald's basic philosophy? How does it enforce this philosophy and adapt to different environments?
4. Should McDonald's expand its menu? If you say no, then why not? If you say yes, what kinds of products should it add?
5. Why is McDonald's successful in many countries around the world?

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Chapter -2

Management and Society: The External Environment, Social Responsibility, and Ethics

CHAPTER OBJECTIVES

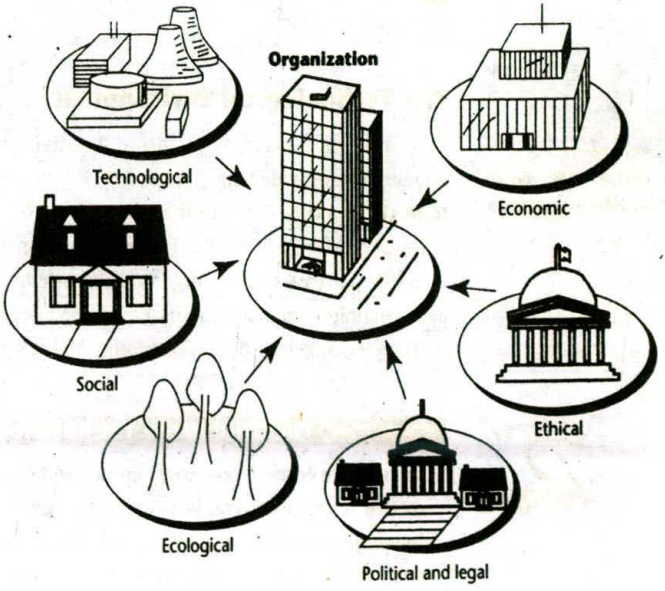
After studying this chapter, you should be able to:

1. Describe the nature of the pluralistic society and selected environments.
2. Explain the social responsibility of managers and the arguments for and against the social involvement of business.
3. Understand the nature and importance of ethics in managing and ways to institutionalize ethics and raise ethical standards.
4. Recognize that some ethical standards vary in different societies.
5. Realize that trust is the basis for human interaction.

Every time managers plan, they take into account the needs and desires of members of society outside the organization, as well as the needs for material and human resources, technology, and other requirements in the external environment. They do likewise to some degree with almost every other kind of managerial activity.

All managers, whether they operate in a business, a government agency, a church, a charitable foundation, or a university, must, in varying degrees, take into account the elements and forces of their external environment. While they may be able to do little or nothing to change these forces, they have no alternative but to respond to them. They must identify, evaluate, and react to the forces outside the enterprise that may affect its operation. The impact of the external environment on the organization is illustrated in Figure 2-1. The constraining influences of external factors on the enterprise are even more crucial in international management (a fact to be discussed in Chapter 3).

FIGURE 2-1 The organization and its external environment



This chapter deals with the impact of the external environment on the organization—with a focus on the technological and ecological environment—and the relationships between business and the society in which it operates. First, the focus is on the nature of the pluralistic society. Then the discussion expands to the topics of social responsibility and ethical behavior.

Operating in a Pluralistic Society

Pluralistic society A society where many organized groups represent various interests.

Managers operate in a **pluralistic society**, in which many organized groups represent various interests. Each group has an impact on other groups, but no one group exerts an inordinate amount of power. Many groups exert some power over business. As explained in Chapter 1, there are many stakeholders or claimants on the organization, and they have divergent goals. It is the task of the manager to integrate their aims.

Working within a pluralistic society has several implications for business. First, various groups, such as environmental groups, keep business power in balance. Second, business interests can be expressed by joining groups such as the Chamber of Commerce. Third, business can participate in projects with other responsible groups for the purpose of bettering society; an example is working toward the renewal of inner cities. Fourth, in a pluralistic society, there can be conflict as well as agreement among groups. Finally, in such a society, one group is quite aware of what other groups are doing.

The Technological Environment

Technology The sum total of the knowledge we have of ways to do things.

One of the most pervasive factors in the environment is technology. It is science that provides knowledge, and it is technology that uses it. The term **technology** refers to the sum total of the knowledge we have of ways to do things. It includes inventions, it includes techniques, and it includes the vast store of organized knowledge about everything from aerodynamics to zoology. But its main influence is on ways of doing things, on how we design, produce, distribute, and sell goods as well as services.

International Perspective

The Third Wave: The Knowledge Age[1]

The first-wave economy was based on land and farm labor. The second wave centered on machines and large industries. The third-wave economy is the knowledge age, which encompasses data, images, symbols, culture, ideology, values, and information. Being at the frontiers of the new technologies, society

must rethink the way it structures itself and how it strikes a balance between freedom and restrictions (e.g., how to manage or control the massive amount of information available on the Internet). Cyberspace is a bioelectronic environment that exists wherever one can find telephone and coaxial cables, fiber-optic lines, or electromagnetic waves. It will require a rethinking of centralization versus decentralization, organizational hierarchy versus empowerment, and vertical versus horizontal organization structures, just to mention a few.

The Ecological Environment

Ecology The relationship of people and other living things with their environment.

Managers must take into account the ecological factors in their decision making. By **ecology** we mean the relationship of people and other living things with their environment, such as soil, water, and air. Land, water, and air pollution is of great concern to all people. Land may be polluted by industrial waste such as packaging. Water pollution may be caused, for example, by hazardous waste and sewage. Air pollution can be caused by a variety of sources, such as acid rain, vehicle exhaust fumes, and carcinogens from manufacturing processes.

A variety of legislation has been passed dealing with solid waste, water, and air pollution. Managers must be keenly aware of these laws and regulations and must incorporate ecological concerns into their decision making.

International Perspective

The Bhopal Plant in India and Union Carbide

www.bhopal.net

In December 1984, lethal vapors from Union Carbide's pesticide plant in India killed over 2,000 people and injured 30,000 to 40,000 others. It was the worst industrial disaster, which was at first attributed to failed safety devices and procedures. A subsequent investigation theorized that the disaster was due to sabotage by a disgruntled employee.

In 1975, Carbide obtained permission from the Ministry of Industry in New Delhi to build a plant for producing methyl isocyanate. After 1982, the plant was turned over to Indian personnel because of governmental pressure to make Indian industry self-sufficient. Safety inspections became the responsibility of UCIL, the Indian subsidiary of Union Carbide, which maintained majority ownership of UCIL. After the accident, Warren Anderson, Carbide's chairman, accepted the moral responsibility for the tragedy. Various theories developed about the real cause of the accident.

American experts and relief were sent to India, followed by American lawyers who wanted to represent the victims. After many arguments, the suit was tried in India, where U.S. lawyers were not allowed to represent the victims. In 1989, the lawsuit was settled in which Union Carbide agreed to pay $470 million.

Still, the issue remains as to who should be held accountable? Top management at Union Carbide? Managers at UCIL? Operators responsible for the methyl isocyanate unit? The Indian government issuing the permit? These are difficult questions indeed for multinational corporations and governments.

In order to protect the environment, European countries developed the ISO 14001 standard to assure that company policies address a variety of public concerns, including pollution prevention and compliance with relevant laws and regulations. Since the adoption of ISO 14001 in 1996, some 10,000 companies had registered by the year 2000. Although the standard had a slow start in the United States, it received a boost when Ford Motor Company certified all its facilities around the world as conforming to ISO 14001.[3] Other companies such as General Motors, IBM, and Xerox followed. The standard was valuable to Ford for reducing water consumption, disposed paint sludge, and disposable packing materials.

International Perspective

The Greening of Toshiba[4]

Toshiba Corporation, a leader in high technology, takes environmental protection seriously by considering how its products are disposed when their usefulness diminishes and they need to be discarded or recycled.

www.toshiba.com

In 1988, the company set up the Environment Protection Center at the corporate level. The efforts since then have not gone unnoticed. In 1997, Toshiba achieved ISO 14001 certification, which recognizes efforts for creating a friendly environment. Environmental accounting is used to quantify the economic benefits, such as reduction of waste and in water and electricity usage. These efforts require environmental education of its employees as well as its partners and suppliers. Environmental management is more than a slogan at Toshiba; it is a systematic effort to reduce the undesirable impact of its operation on the environment.

The Social Responsibility of Managers

In the early 1900s, the mission of business firms was exclusively economic. Today, partly owing to the interdependencies of the many groups in our

society, the social involvement of business has increased. As pointed out in the model of the systems approach to management in Chapter 1, there are many stakeholders or claimants to the organization. There is indeed a question as to what the social responsibility of business really is. Moreover, the question of social responsibility, originally associated with businesses, is now being posed with increasing frequency in regard to governments, universities, nonprofit foundations, charitable organizations, and even churches. Thus, we are talking about the social responsibility and social responsiveness of all organizations, although the focus of this discussion is on business. Society, awakened and vocal with respect to the urgency of social problems, is asking managers, particularly those at the top, what they are doing to discharge their social responsibilities and why they are not doing more.

Social Responsibility and Social Responsiveness

Corporate social responsibility The serious consideration of the impact of the company's actions on society.

The concept of social responsibility is not new. Although the idea was already considered in the early part of the 20th century, it received a major impetus with the 1953 book *Social Responsibilities of the Businessman* by Howard R. Bowen, who suggested that businesses should consider the social implications of their decisions.[5] As might be expected, there is no complete agreement on the definition. In a survey of 439 executives, 68 percent of the managers who responded agreed with the following definition: **corporate social responsibility** is "seriously considering the impact of the company's actions on society."[6]

Social responsiveness The ability of a corporation to relate its operations and policies to the social environment in ways that are mutually beneficial to the company and to society.

A concept that is newer, but very similar to social responsibility, is **social responsiveness**, which in simple terms means "the ability of a corporation to relate its operations and policies to the social environment in ways that are mutually beneficial to the company and to society."[7] Both definitions focus on corporations, but these concepts should be expanded to include enterprises other than businesses and to encompass relationships within an enterprise. The main difference between social responsibility and social responsiveness is that the latter implies actions and the "how" of enterprise responses. In this discussion, the terms will be used interchangeably.

Arguments For and Against Business Involvement in Social Actions

Although there are arguments for business involvement in social activities, there are also arguments against it, as shown in Table 2-1.

TABLE 2.1 Arguments for and against social involvement of business

Arguments *for* social involvement of business
1. Public needs have changed, leading to changed expectations. Business, it is suggested, received its charter from society and consequently has to respond to the needs of society.
2. The creation of a better social environment benefits both society and business. Society gains through better neighborhoods and employment opportunities; business benefits from a better community, since the community is the source of its workforce and the consumer of its products and services.
3. Social involvement discourages government regulation and intervention. The result is greater freedom and more flexibility in decision making for business.
4. Business has a great deal of power that, it is reasoned, should be accompanied by an equal amount of responsibility.
5. Modern society is an interdependent system, and the internal activities of the enterprise have an impact on the external environment.
6. Social involvement may be in the interests of stockholders.
7. Problems can become profits. Items that may once have been considered waste (e.g., empty soft-drink cans) can be profitably used again.
8. Social involvement creates a favorable public image. As a result, the firm may attract customers, employees, and investors.
9. Business should try to solve the problems that other institutions have not been able to solve. After all, business has a history of coming up with novel ideas.
10. Business has the resources. Specifically, business should use the talents of its managers and specialists, as well as its capital resources, to solve some of society's problems.
11. It is better to prevent social problems through business involvement than to cure them. It may be easier to help the hard-core unemployed than to cope with social unrest.
Arguments *against* social involvement of business
1. The primary task of business is to maximize profit by focusing strictly on economic activities. Social involvement could reduce economic efficiency.
2. In the final analysis, society must pay for the social involvement of business through higher prices. Social involvement would create excessive costs for business, which cannot commit its resources to social action.
3. Social involvement can create a weakened international balance-of-payment situation. The cost of social programs, the reasoning goes, would have to be added to the price of the product. Thus, socially involved companies selling in international markets would be at a disadvantage when competing with companies from other countries that do not have these social costs to bear.
4. Business has enough power, and additional social involvement would further increase its power and influence.
5. Businesspeople lack the social skills to deal with the problems of society. Their training and experience are with economic matters, and their skills may not be pertinent to social problems.
6. There is a lack of accountability of business to society. Unless accountability can be established, business should not get involved.
7. There is not full support for involvement in social actions. Consequently, disagreements among groups with different viewpoints will cause friction.

Based on a variety of sources, including William C. Frederick, Keith Davis, and James E. Post, *Business and Society*, 6th ed. (New York: McGraw-Hill, 1988), chap. 2.

Today, many businesses are involved in social actions. A good example is the Ben & Jerry ice-cream company, which contributes to the conservation of the rainforest. The company also purchases nuts from tribes in the rainforest so that they do not rely on cutting trees for survival. Furthermore, it opened an ice-cream store in Harlem to provide employment for homeless people. A decision as to whether companies should extend their social involvement requires careful examination of the arguments for and against such actions. Certainly, society's expectations are changing, and the trend seems to be toward greater social responsiveness.

Reaction or Proaction?

To live within an environment and be responsive to it does not mean that managers should merely react in the face of stress. Since no enterprise can be expected to react very quickly to unforeseen developments, an enterprise must practice ways of anticipating developments through forecasts. An alert company, for example, does not wait until its product is obsolete and sales have fallen off before coming out with a new or improved product. A government agency should not wait until its regulations are obsolete and discredited before looking for another way to achieve its objectives. No enterprise should wait for problems to develop before preparing to face them. Proaction is an essential part of the planning process.

The Role of the Government

There are many instances in which social changes can be implemented only by the enactment of legislation. However, many managers in business and elsewhere have found it to their advantage to do something about pressing social problems. For example, many businesses have profited by filtering smokestack pollutants and selling or utilizing these recovered wastes. Some companies have made a profit by building low-cost apartment buildings in ghetto areas. In other words, contributing to the solution of social problems does not always involve net expenses. But society may need the bludgeoning force of legislation to get improvements underway.

International Perspective

Bill Gates and Microsoft a Monopoly?[8]

www.microsoft.com

This was the contention of Judge Thomas Penfield Jackson in a document released on November 5, 1999: "Through its conduct toward Netscape, IBM, Compaq, Intel and others, Microsoft has demonstrated that it will use its prodigious market power and immense profits to harm any firm that insists on pursuing initiatives that could intensify competition against one of Microsoft's core products."[9] It is suggested that Microsoft's behavior is harming consumers and competitors.

Microsoft had a humble beginning. In 1975, the company was started in Albuquerque, New Mexico. In the early 1980s, Bill Gates and his colleagues wrote the operating system that runs the personal computer for IBM. Later, this system, MS-DOS, became the dominating operating system. It was followed by Windows, which is now installed in most personal computers. Eventually, the company became so successful that the government engaged in a two-year "fact-finding" mission to demonstrate monopolistic behavior by Microsoft. Judge Jackson's position was that Microsoft's pattern of behavior was intended to destroy Netscape and pressure other firms to bend to the company's wishes. Microsoft's internal e-mail seemed to support this behavior. However, Microsoft contended that its aim was to serve its customers and protect its intellectual property. Moreover, it was suggested that technological change would eventually act against monopolies anyway. For example, the Internet changes the "rules of the game" by providing open standards, which reduce Microsoft's influence in the personal computer market. The company also contended that it did not harm consumers nor stifle innovation.

Ethics in Managing

Ethics The discipline dealing with what is good and bad and with moral duty and obligation.

Business ethics is concerned with truth and justice.

All persons, whether in business, government, university, or any other enterprise, are concerned with ethics. In *Webster's Ninth New Collegiate Dictionary*, **ethics** is defined as "the discipline dealing with what is good and bad and with moral duty and obligation." **Business ethics** is concerned with truth and justice and has a variety of aspects, such as the expectations of society, fair competition, advertising, public relations, social responsibility, consumer autonomy, and corporate behavior in the home country as well as abroad.

International Perspective

Scandals and Corporate Governance[10]

In July 2002, WorldCom filed the largest bankruptcy claim in U.S. history. While the investors of WorldCom, Global Crossing, and other telecommunication companies were suffering, top managers of many of these companies got rich.

Jack Grubman of Citigroup's Salomon Smith Barney seemed to have misled "outsiders," resulting in losses and bankruptcies that could hurt not only investors but also the U.S. telecommunication industry in the global competition with firms in countries such as South Korea and Japan, which already are technologically ahead of U.S. companies in certain areas.

Corporate scandals such as those of Enron and WorldCom have shaken the confidence of investors. In response to the disclosure of alleged improprieties, the United States initiated new legislation.

Starting from August 2002, chief executive officers (CEOs) and chief financial officers (CFOs) of many of the largest U.S. companies are required to state under oath that to the best of their knowledge the latest financial reports are true. Under the Sarbanes–Oxley law, CEOs and CFOs are required to certify the correctness of the reports to regain the confidence of investors. This legislation also stipulates that subsidized personal loans to executives be banned.

Business Week suggests several ideas for the creation of the ideal corporation, which must be built on integrity, ethics, fairness, and trust.[11] The new corporate model must be more transparent for investors, suppliers, customers, and employees. Performance data need to be accurate so that investors can trust the numbers. Executive pay must be perceived as being fair. The more open corporate culture needs to emphasize accountability, and employees must feel free to report unethical and unfair practices.

Ethical Theories[12]

Utilitarian theory Plans and actions should be evaluated by their consequences.

Theory based on rights All people have basic rights.

Theory of justice Decision makers must be guided by fairness and equity, as well as impartiality.

In organizations, managers compete for information, influence, and resources. The potential for conflicts in selecting the ends as well as the means to the ends is easy to understand, and the question of what criteria should guide ethical behavior becomes acute.

Three basic types of moral theories in the field of normative ethics have been developed. First, the **utilitarian theory** suggests that plans and actions should be evaluated by their consequences. The underlying idea is that plans or actions should produce the greatest good for the greatest number of people. Second, the **theory based on rights** holds that all people have basic rights. Examples are the rights to freedom of conscience, free speech, and due process. A number of those rights can be found in the Bill of Rights in the Constitution of the United States. Third, the **theory of justice** demands that decision makers be guided by fairness and equity, as well as impartiality.

Institutionalizing Ethics

Business ethics are increasingly addressed in seminars and at conferences.[13] Managers, especially top managers, do have a responsibility to create an organizational environment that fosters ethical decision making by institutionalizing ethics. This means applying and integrating ethical concepts with daily actions. Theodore Purcell and James Weber suggest that this can be accomplished in three ways: (1) by establishing an appropriate company policy or a code of ethics, (2) by using a formally appointed ethics committee, and (3) by teaching ethics in management development programs.[14] The most common way to institutionalize ethics is to establish a code of ethics; much less common is the use of ethics committees. Management development programs dealing with ethical issues are seldom used, although companies such as Allied Chemical, IBM, and General Electric have instituted such programs.

The publication of a code of ethics is not enough. Some companies require employees to sign the code and include ethics criteria in performance appraisal. Moreover, certain firms connect compensation and rewards to ethical behavior. Managers should also take any opportunity to encourage and publicize ethical behavior. At the same time, employees should be encouraged to report unethical practices. Most important, managers must set a good example through ethical behavior and practices.

Code A statement of policies, principles, or rules that guide behavior.

A **code** is a statement of policies, principles, or rules that guide behavior. Certainly, codes of ethics do not apply only to business enterprises; they should guide the behavior of persons in all organizations and in everyday life.

International Perspective

Code of Ethics for Government Service

The U.S. federal government has established the following code.[15] Any person in government service should:

1. Put loyalty to the highest moral principles and to country above loyalty to persons, party, or Government department.
2. Uphold the Constitution, laws, and regulations of the United States and of all governments therein and never be a party to their evasion.
3. Give a full day's labor for a full day's pay; giving earnest effort and best thought to the performance of duties.
4. Seek to find and employ more efficient and economical ways of getting tasks accomplished.

5. Never discriminate unfairly by the dispensing of special favors or privileges to anyone, whether for remuneration or not; and never accept, for himself or herself or for family members, favors or benefits under circumstances which might be construed by reasonable persons as influencing the performance of governmental duties.
6. Make no private promises of any kind binding upon the duties of office, since a Government employee has no private word that can be binding on public duty.
7. Engage in no business with the Government, either directly or indirectly, which is inconsistent with the conscientious performance of governmental duties.
8. Never use any information gained confidentially in the performance of governmental duties as a means of making private profit.
9. Expose corruption wherever discovered.
10. Uphold these principles, ever conscious that public office is a public trust.

Simply stating a code of ethics is not enough to ensure compliance, and the appointment of an ethics committee, consisting of internal and external directors, is considered essential for institutionalizing ethical behavior.[16] The functions of such a committee may include (1) holding regular meetings to discuss ethical issues, (2) dealing with "gray areas," (3) communicating the code to all members of the organization, (4) checking for possible violations of the code, (5) enforcing the code, (6) rewarding compliance and punishing violations, (7) reviewing and updating the code, and (8) reporting activities of the committee to the board of directors.

Factors that Raise Ethical Standards

The two factors that raise ethical standards the most, according to the respondents in one study, are (1) public disclosure and publicity and (2) the increased concern of a well-informed public. These factors are followed by government regulations and by education to raise the professionalism of business managers.[17]

For ethical codes to be effective, provisions must be made for their enforcement. Unethical managers should be held responsible for their actions. This means that privileges and benefits should be withdrawn and sanctions should be applied. Although the enforcement of ethical codes may not be easy, the mere existence of such codes can increase ethical

behavior by clarifying expectations. On the other hand, one should not expect ethical codes to solve all problems. In fact, they can create a false sense of security. Effective code enforcement requires demonstration of consistent ethical behavior and support from top management. Another factor that could raise ethical standards is the teaching of ethics and values in higher education institutions.

Whistle-blowing

Whistle-blowing Making known to outside agencies unethical company practices.

Another way of encouraging ethical corporate behavior is through **whistle-blowing**, which means making known to outside agencies unethical company practices. Black's Law Dictionary defines a whistle-blower as "an employee who refuses to engage in and/or reports illegal or wrongful activities of his employer or fellow employees." There is even a whistle-blower Web site that discusses whistle-blowing issues, including legal matters and protection.[18] This whistle-blowing center is a nonprofit organization that helps enforce environmental laws and works for the accountability of business and government organizations. Its primary objective is to protect and defend persons who disclose actions harmful to the environment and public health.

As we will discuss later in this book in greater detail, Roger Boisjoly, an engineer at Morton Thiokol, the contractor for the rocket booster in the Challenger space shuttle, pointed out the problem with the O-rings, which became ineffective at low temperatures. His fears and concerns were largely ignored by management and eventually led to the Challenger disaster. Another example is that of Mr. Ruud, a whistle-blower who was fired from his job at the nuclear plant operator Westinghouse Hanford Company. He sued the company and was awarded by a federal judge an entitlement for lifetime front pay.[19] In America, legislation now gives greater protection to government whistle-blowers. There is some evidence that after the September 11, 2001, World Trade Center suicide attacks more employees have come forward to disclose security issues.[20]

Differing Ethical Standards between Societies

Ethical, as well as legal, standards differ, particularly between nations and societies. For example, certain nations permit privately owned companies to make monetary contributions to political parties, campaigns, and candidates (which is prohibited in the United States). In some countries, payments to government officials and other persons with political influence

to ensure favorable handling of a business or other transaction are regarded not as bribes but as payments for services rendered. In some cases, payments made in order to win a contract are even looked upon as a normal and acceptable way of doing business. Consider the Quaker Oats Company, which faced a situation in which foreign officials threatened to close its operation if the demand for "payouts" was not met; or a company may find itself in a predicament where its plant manager's safety will be in jeopardy if payoffs are not made.[21] The question facing responsible foreign business managers is: What ethical standards should they follow?[22] For example, *guanxi*, which pertains to informal relationships and exchange of favors, influences business activities in China and East Asia. There is no question of what to do in similar situations in the United States: executives have to refuse the suggestion of putting money in a "paper bag." But in a country where such practices are expected and are common, American executives are faced with a difficult problem. With the passage of laws by the U.S. Congress and the adoption of regulations by the Securities and Exchange Commission, not only must American firms report anything that could be called a payoff but also anything else that can be construed as a bribe is unlawful. The Foreign Corrupt Practices Act (FCPA) Antibribery Provisions state: "U.S. firms seeking to do business in foreign markets must be familiar with the FCPA. In general, the FCPA prohibits corrupt payments to foreign officials for the purpose of obtaining or keeping business."[23] Thus, the United States has attempted to export its standards for doing business to other countries, which can improve ethical standards abroad.

www.quakeroats.com

www.sec.gov

Trust as the Basis for Change Management

Managers are bombarded with new managerial concepts, and old ones often are disguised by new terminology—all designed for coping with managerial change demanded by global competition, customer expectations, and the need to respond quickly to environmental changes. Although various approaches to managing change in the New Age will be discussed throughout the book, one often-overlooked concept is trust. Professor Salvatore Belardo points out that trust is at the center of communication, collaboration, and the willingness to change.[24] Traditionally, the concept of trust is equated with integrity, loyalty, caring, and keeping promises in the relationships between and among individuals. But Belardo points out that trust should go beyond individual relationships and extend to the organization through the creation of a culture of trust

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that transcends individual leadership. Leaders come and go; the organization continues. For example, David Packard of Hewlett-Packard left as his legacy the HP Way, a philosophy that emphasizes a code of ethics, which permeates the whole organization and continues after his death.

In this book, many managerial concepts, principles, theories, and practices will be introduced for managing change in the New Age. But an enterprise is essentially a human organization, which functions well only when it is based on trust, ethical behavior, and the recognition of human dignity.

Summary

Managers operate in a complex environment. They are affected by—and to some extent influence—the environment. Managers operate in a pluralistic society in which many organized groups represent various interests.

In their decision making, managers must consider the external environment. Technology provides many benefits but also some problems. Increasingly, firms are considering the impact of managerial actions on the ecological environment. Many business corporations and other organizations are making serious efforts to establish an environment that is beneficial to individuals, business, and society.

Corporate social responsibility requires that organizations consider seriously the impact of their actions on society. Similarly, social responsiveness is relating corporate operations and policies to the social environment in ways that are beneficial to both the company and society. Determining the appropriate relationships between various types of organizations and society is not an easy task, and one can make arguments for and against business involvement in social activities. However, there is now a general recognition that the responsibility of business goes beyond profit maximization.

Ethics deals with what is good and bad as well as with moral duty and obligation. There are three moral theories in normative ethics: the utilitarian theory, the theory based on rights, and the theory of justice. Some authors have suggested that businesses institutionalize ethics and develop a code of ethics. There are also other factors that raise ethical standards, including whistle-blowing. Managers have to make difficult choices when the standards differ in other societies. Trust is the foundation for human relations and modern management approaches.

KEY IDEAS AND CONCEPTS FOR REVIEW

Pluralistic society
Technological environment
Ecological environment
Corporate social responsibility
Social responsiveness
Arguments for and against social involvement of business
Government's role in enforcing ethical behavior
Ethics
Utilitarian theory of ethics
Ethical theory based on rights
Ethical theory of justice
Institutionalizing ethics
Code of ethics
Factors raising ethical standards
Whistle-blowing
Differing ethical standards
Trust as a critical factor for change

FOR DISCUSSION

1. Why is the environment external to an enterprise so important to all managers? Can any manager avoid being influenced by the external environment?
2. Identify the elements of the external environment that are likely to be the most important to each of the following: a company president, a sales manager, a production manager, a controller, and a personnel manager.
3. What are the major social responsibilities of business managers? of public administrators? Have these responsibilities changed over the years? How?
4. If you were the chief executive of a large corporation, how would you institutionalize ethics in the organization?
5. What ethical codes would you recommend for your university, your class, and your family? How should these codes be enforced?

EXERCISES/ACTION STEPS

1. The class should select and read an article published in a recent issue of the *Wall Street Journal*, *Business Week*, or *Fortune* that raises some ethical issues. Divide the class into groups and analyze the situation using the ethical theories discussed in this chapter.
2. Interview one business manager and one administrator in the local government and ask how they perceive their social responsibilities. Do these responsibilities relate primarily to the environment external to the organization, or do they also include internal aspects?

INTERNET RESEARCH

1. Search the Internet for "business ethics" and select two articles for class discussion.
2. Cars do pollute the air. Search the Internet for "ecology" and "cars" to find out what car makers are doing to reduce pollution.
3. Search the Internet for "knowledge age" and describe three developments that might affect you or provide opportunities for you.

International Case

Spirituality in the Workplace[25]

Traditionally, the workplace and spirituality did not mix in America. But things are changing. Andre Delbecq, a professor at Santa Clara University, a Jesuit institution, said, "There were two things I thought I'd never see in my life, the fall of the Russian empire and God being spoken about in a business school." Now management books and conferences (including the annual meeting of the Academy of Management) deal with the various aspects of how God can be brought into the organizational environment. To be sure, people who want to integrate spiritual dimensions into the workplace are still considered rebels. But ServiceMaster, a Fortune 500 company with some 75,000 employees, created a spiritual organization culture many years ago. Indeed, Peter Drucker, one of the most prolific writers on management, had high regard for the company that is known for its products such as Terminix, TruGreen, and Merry Maids.

When people in the United States were asked if they believe in God, some 95 percent said yes. It is in a spiritual context that businesspeople under the daily pressure of work can discuss their inner feelings. As the baby boomers, now in their 50s, are reaching the top in their corporate life, they begin to wonder what life is all about. They lived through the youth culture of the 1960s and the greed-dominated 1980s. They are now questioning the real meaning of life and the ethical dimension of work. Jose Zeilstra, an executive at PriceWaterhouseCoopers, worked around the world, practicing her Christian principles in different cultures. During her assignment in China, she strongly argued against the practice of giving "very expensive gifts." As a result, the business deal did not work out. Yet, in the long run, integrating her personal beliefs with her work resulted in a very successful career. Academic institutions such as the University of St. Thomas, University of Denver, and Harvard Divinity School are following and studying the movement of spirituality. Other American schools such as Antioch University, University of New Haven, University of Scranton, and Santa Clara University, as well as institutions abroad such as the University of Bath in England and the Indian Center for Encouraging Excellence in India, are conducting research, conferences, or lectures on spirituality.

The cover story of *Business Week* (November 1, 1999) discussed how companies such as Taco Bell, Pizza Hut, McDonald's, and Xerox pay attention to the spiritual needs of their employees. Some companies claim an increase in productivity, decrease in turnover, and reduction in fear. A research study by the consulting firm McKinsey in Australia found that firms with spiritual programs showed reduced turnover and improved productivity. Professor Ian I. Mitroff at the University of Southern California even stated, "Spirituality could be the ultimate competitive advantage." But there is also the concern that cult members and groups with a radical perspective could use the workplace for their own aims. Still, employees in companies that integrate spirituality in their workplace count on the potential benefits of greater respect for individuals, more humane treatment of their fellow workers, and an environment with greater trust that permeates their organization.

Questions

1. What is spirituality?
2. Is this topic appropriate for business?
3. What are the arguments for and against inclusion of spirituality in business?

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Chapter -3

Global, Comparative, and Quality Management

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

1. Discuss the nature and purpose of international business and multinational corporations.
2. Understand country alliances that form trade blocs.
3. Appreciate cultural and country differences and their implications for managing.
4. Recognize the differences in managing in selected countries.
5. Describe the managerial practices in Japan and Theory Z.
6. Understand the factors that influence the competitive advantages of nations, according to Michael Porter.
7. Recognize the major contributions to quality management and describe the Baldrige quality award, ISO 9000, and the European Quality Award.

The previous chapter focused on the external factors that are present especially in the domestic environment. The constraining factors on managing are likely to be more severe for international firms. Executives operating in a foreign country need to learn a great deal about the country's educational, economic, legal, and political systems and especially its sociocultural environment.

The first section in this chapter deals with international management and the role of multinational corporations. Then the environmental impact on managing in selected countries is examined, with special attention given to Japanese managerial practices. Finally, the competitive advantage of nations and quality management are discussed.

International Management and Multinational Corporations

International management focuses on the operation of international firms in host countries.

The study of **international management** focuses on the operation of international firms in host countries. It is concerned with managerial issues related to the flow of people, goods, and money, with the ultimate aim of managing better in situations that involve crossing national boundaries.

The environmental factors that affect domestic firms usually are more critical for international corporations operating in foreign countries. As illustrated in Table 3-1, managers involved in international business are faced with many factors that are different from those of the domestically oriented firm. They have to interact with employees who have different educational and cultural backgrounds and value systems; they also must cope with different legal, political, and economic factors. These environments understandably influence the way managerial and enterprise functions are carried out.

The Nature and Purpose of International Business

International businesses engage in transactions across national boundaries.

Although business had been conducted on an international scale for a long time, international business gained greater visibility and importance because of the growth of large multinational corporations. **International businesses** engage in transactions across national boundaries. These

TABLE 3-1 Managing domestic and international enterprises

Managerial function	Domestic enterprise (in industrialized country)	International enterprise
Planning		
• Scanning the environment for threats and opportunities	• National market	• Worldwide market
Organizing		
• Organization structure	• Structure for domestic operations	• Global structure
• View of authority	• Similar	• Different
Staffing		
• Sources of managerial talent	• National labor pool	• Worldwide labor pool
• Manager orientation	• Often ethnocentric	• Geocentric
Leading		
• Leadership and motivation	• Influenced by similar culture	• Influenced by many different cultures
• Communication lines	• Relatively short	• Network with long distances
Controlling		
• Reporting system	• Similar requirements	• Many different requirements

transactions include the transfer of goods, services, technology, managerial knowledge, and capital to other countries.

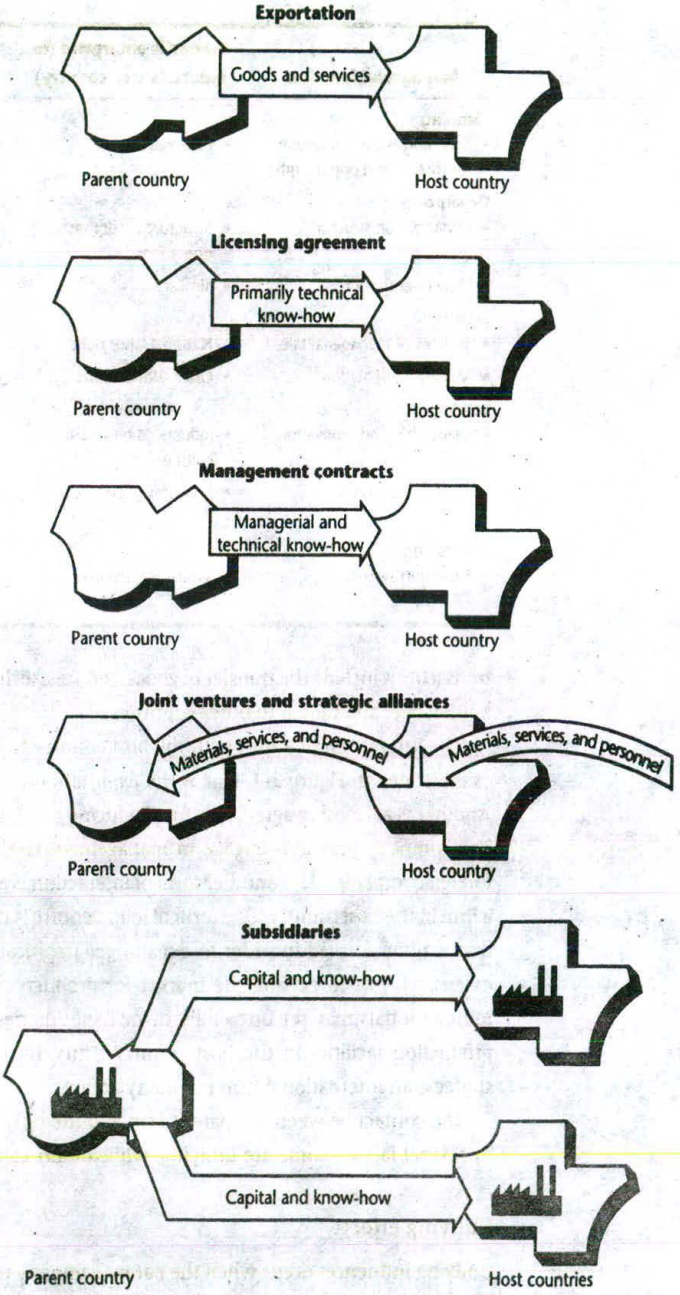
The interaction of a firm with the host country can take many forms, as illustrated in Figure 3-1. One is the exportation of goods and services. Another is a licensing agreement for producing goods in another country. The company may also engage in management contracts for operating foreign companies. Still another form of interaction is a joint venture with a firm in the host country. One form of joint venture is the strategic alliance that is often formed in order to expand geographically (airlines do this extensively) or to expand the market for products or services. Finally, multinationals may set up wholly owned subsidiaries or branches with production facilities in the host country. Thus, in developing a global strategy, an international firm has many options.

The contact between the parent firm and the host country is affected by several factors; some are unifying, while others can cause conflicts.

Unifying effects

Unifying influences occur when the parent company provides and shares technical and managerial know-how, thus assisting the local company in

FIGURE 3.1 Forms of international business



the development of human and material resources. Moreover, both partners may find it advantageous to be integrated into a global organization structure. Whatever the interaction, organizational policies must provide for equity and result in benefits for both the parent firm and the local company. Only then can one expect a long-lasting relationship.

Potentials for conflict

Many factors can cause conflicts between the parent firm and the host country. Nationalistic self-interest may overshadow the benefits obtained through cooperation. Similarly, sociocultural differences can lead to breakdown in communication and subsequent misunderstandings. Also, a large multinational firm may have such overpowering economic effects on a small host country that the latter feels overwhelmed. Some international corporations have been charged with making excessive profits, hiring the best local people away from local firms, and operating contrary to social customs. International corporations must develop social and diplomatic skills in their managers to prevent such conflicts and to resolve those that unavoidably occur.

Multinational Corporations

Multinational corporations have their headquarters in one country but operate in many countries.

Multinational corporations (MNCs) have their headquarters in one country but operate in many countries. *Fortune* magazine annually identifies the 500 largest global companies. Of the ten largest corporations ranked by revenues in 2000, five were American, one German/American, one British/Dutch, one British, and two Japanese. These companies were (1) Exxon Mobil, (2) Wal-Mart Stores, (3) General Motors, (4) Ford, (5) DaimlerChrysler, (6) Royal Dutch/Shell Group, (7) BP (British Petroleum), (8) General Electric, (9) Mitsubishi, and (10) Toyota.[1]

In 2000, among the top 25 Asian companies, most were from Japan. Specifically, 21 were Japanese, 3 Chinese, and 1 South Korean.

Fortune also ranked the most admired global companies. In 2002, American companies took the top 23 positions (with General Electric ranking number 1). Of the top firms outside the United States, four were in Japan (Toyota Motor, Sony, Honda Motor, Canon), two in Britain/Netherlands (BP and Royal Dutch/Shell), and one from each of the following countries: Finland (Nokia), Switzerland (Néstle), Singapore (Singapore Airlines), and France (L'Oreal).[2]

From ethnocentric to geocentric orientation[3]

Ethnocentric orientation The style of the foreign operations is based on that of the parent company.

Polycentric orientation The foreign subsidiaries are given a great deal of managerial freedom.

Regiocentric orientation The foreign operations are staffed on a regional basis.

Geocentric orientation The entire organization is viewed as an interdependent system operating in many countries.

In its early stages, international business was conducted with an **ethnocentric** outlook, with the orientation of the foreign operation based on that of the parent company.[4] The **polycentric** attitude, on the other hand, is based on the notion that it is best to give the foreign subsidiaries, staffed by local nationals, a great deal of managerial freedom. It is assumed that local nationals understand the local environment best. A **regiocentric** orientation favors the staffing of foreign operations on a regional basis. Thus, a European view may be composed of British, French, German, Italian, and other European influences. The modern MNC has a **geocentric** orientation. This means that the entire organization is viewed as an interdependent system operating in many countries. The relationships between headquarters and subsidiaries are collaborative, with communication flowing in both directions. Furthermore, key positions are filled by managers of different nationalities. In short, the orientation of the MNC is truly international and goes beyond a narrow nationalistic viewpoint.

Advantages of multinationals

MNCs have several advantages over firms that have a domestic orientation. Obviously, the MNC can take advantage of business opportunities in many different countries. It can also raise money for its operations throughout the world. Moreover, it benefits by being able to establish production facilities in countries where its products can be produced most cost-effectively and efficiently. Companies with worldwide operations sometimes have better access to natural resources and materials that may not be available to domestic firms. Finally, large MNCs can recruit managers and other personnel from a worldwide labor pool.

Challenges for multinationals

The advantages of multinational operations must be weighed against the challenges and risks associated with operating in foreign environments. One problem is the increasing nationalism in many countries. Years ago, developing countries lacked managerial, marketing, and technical skills. Consequently, they welcomed MNCs. But the situation is changing, with people in developing countries also acquiring those skills. In addition, countries have not only become aware of the value of their natural resources but have also become more skilled in international negotiations. Finally, MNCs must maintain good relations with the host country, a task

that may prove difficult in some countries because their governments frequently change and corporations must deal with, and adapt to, these changes.

From Multinational to Global, or Transnational, Corporations

Global, or transnational, corporations view the whole world as one market.

Just operating in different countries is not enough for large corporations; nor is the establishment of manufacturing plants in several countries (as Exxon and General Motors have done) sufficient to be competitive in the world market. The shift is toward the **global, or transnational, corporation**, which views the whole world as one market. This means, however, that a corporation also has to adapt to national and even local needs.

www.exxon.com
www.gm.com

Domestic markets have become too small. Developing a drug may cost several hundred million dollars and may take more than ten years. To recover the costs requires selling the drug in a world market. Moreover, global companies have to keep abreast of technological developments around the world. Ford Motor Company decided in the latter half of the 1980s to become a global corporation. Previous attempts to build the "world car" (named the Escort) were not very successful. However, the use of modern communication technology, such as teleconferencing, establishes now a much closer link between Ford's headquarters and its European operations. While Ford was aiming at becoming a global corporation, it had no plants in Japan. To compensate for this void, Ford bought a 25 percent share in Mazda, which was later increased to 33.4 percent. After Ford gained a controlling interest, Henry Wallace was appointed president, the first foreigner to lead a major Japanese firm.[5] Moreover, the company has another project with Nissan in Japan that designed the minivan built by Ford and marketed as the Villager and as the Quest that is sold by Nissan dealerships.

www.ford.com

www.mazda.com

While many firms are aiming at becoming global, only a few have really done so. It requires developing products with the whole world in mind, especially the markets in North America, Asia, and Western Europe. Similarly, strategic decisions must take into account the whole world, but tactics must be adapted to the national and local environments. In staffing, opportunities must be opened for nonnationals to move into upper management ranks. In countries where the global corporation cannot enter, strategic alliances may need to be formed with local companies.

Country Alliances and Economic Blocs

At one time, countries in a region were competing against each other (and they still do). But now, countries are forming regional alliances that have regions compete with each other. Examples are the European Union, the North American Free Trade Agreement (NAFTA), the Association of Southeast Asian Nations (ASEAN), and Mercosur.

European Union

Europe 1992 marked the completion of the first stage of European economic ties. The European Community (EC) 1992 program caused dramatic shifts in economic power. Some saw the new program as the New Europe, while others, especially outsiders, saw it as a fortress that could provide serious challenges to other countries, including the United States. In order to compete effectively, North American and Asian countries prepared for the New Europe by forming NAFTA and ASEAN.

The European Commission worked on some 300 legislative actions for removing trade barriers and creating an internal market. The new measures were intended to increase market opportunities, escalate competition within the EC, and boost competition from companies outside the EC. The abolition of transnational trade restrictions and the relaxation of border controls had a considerable impact on U.S. companies doing business in Europe. Moreover, strong European companies have become formidable competitors in the U.S. market, as illustrated by Siemens, the German global company.

www.siemens.com

The objective of Europe 1992 was to create a single market through the removal of trade barriers and through free movement of goods, people, service, and capital. The changes go beyond economic interests and encompass many social changes as well. Educational qualifications, for example, are also affected. The Council of Ministers submitted a directive that recognizes diplomas of higher education across national boundaries, making it easier for professionals to work in different countries. It is clear, then, that the EC is more than an economic community: it is a state of mind with political power.

www.europa.eu.int

The original EC 1992 (which later became the European Union) consisted of 12 member nations: Belgium, Denmark, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, and the United Kingdom. It expanded in 1995 to include Austria, Finland, and Sweden. Since then, Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia have been admitted.

North American Free Trade Agreement and Other Latin American Free Trade Blocs[6]

www.nafta-sec-alena.org

In 1994, NAFTA, which included agreements among the United States, Canada, and Mexico, went into effect. Since then, trade among those countries has increased greatly. The objectives of NAFTA are to eliminate trade barriers and facilitate cross-border movements of goods and services, promote fair trade, increase investment opportunities, protect intellectual property, provide for resolution of disputes, and present opportunities to improve the benefits of this agreement. The agreement covers a variety of areas, such as market access, rules governing the origin of goods, customs procedures, energy, agriculture, and measures to be taken in emergencies.

Other Latin American and Caribbean countries have also formed their own trade blocs. Argentina, Brazil, Bolivia, Chile, Paraguay, and Uruguay are members of the Mercosur group.[7] The European Union has extensive trade with Mercosur members, which was further strengthened by the Fifth Round of Association negotiations held in July 2001. In addition, the Caribbean and Central and South American countries consider reductions in trade barriers through the Free Trade Area of the Americas (FTAA), which some consider an extension of NAFTA.[8]

www.mercosur.org

www.ftaa-alca.org

These trade agreements, however, do not go unchallenged, as shown by the protests at World Trade Organization meetings. Critics see them as benefiting only developed nations.

Association of Southeast Asian Nations (ASEAN)[9]

www.aseansec.org

The ten countries of Brunei Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam formed a trading bloc that will increasingly counter NAFTA and the European Union, not only economically but also politically.

During the ASEAN summit conference in October 2003 in Bali, the leaders discussed political security, sociocultural cooperation, and economic issues with the leaders of China, Japan, India, and South Korea. Also, ASEAN economic ministers meet frequently to discuss economic issues and strategies. The 35th such meeting was held in Phnom Penn in September 2003. The following month, ASEAN ministers held the inaugural meeting on culture and arts in Kuala Lumpur, Malaysia. The goal of the meeting was to improve cooperation among ASEAN countries, enhance understanding among their people, and promote a regional identity. More recently, the countries also begin to cooperate to fight

terrorism. Eventually, the ASEAN alliance could rival NAFTA and the European Union.

International Management: Cultural and Country Differences

It is interesting to know some of the differences in managerial practices. A comprehensive study by Geert Hofstede provides a good framework for studying cultural differences between countries. Our discussion will focus on selected countries. It is illustrative, rather than comprehensive, and is based on generalizations. We have to bear in mind that there are, for example, great differences between the managers in any country. Furthermore, a society is not static, and changes do occur over time. For instance, the traditional authoritarian style of German managers is slowly giving way to a more participative approach.

Behaviors in Different Cultures[10]

The study by Geert Hofstede, a Dutch researcher, found that a country's culture impacts on the behavior of employees. In his initial study of more than 110,000 people, he identified four dimensions and later added a fifth. They are (1) individualism versus collectivism, (2) large versus small power distance, (3) uncertainty tolerance versus avoidance, (4) masculinity versus femininity or aggressive versus passive goal behavior, and (5) short- versus long-term orientation. The behaviors in the five dimensions are summarized in Table 3-2.

The results of Hofstede's research showed that, for example, individualism prevailed in the United States, Australia, Britain, and Canada. In contrast, collectivism prevailed in countries such as Guatemala, Ecuador, and Panama. Among the 50 countries studied, India ranked 21, close to the Japanese ranking (22/23). On the other hand, Hong Kong, Singapore, Thailand, and Taiwan ranked between 37 and 44, indicating a tendency toward collectivism.[11] On the masculinity/femininity index, Japan, Austria, Italy, and Switzerland ranked high, while Sweden, Norway, the Netherlands, and Denmark ranked low, meaning that these countries are skewed toward feminism.[12]

These findings suggest that managers need to understand the cultural environments and their implications in order to be successful in the country in which they do business. We shall now discuss the management styles in selected countries.

TABLE 3-2 Five dimensions of behavior

Individualism	Collectivism
People focus on their own interests and the people close to them. Tasks more important than relationships.	Emphasis on the group, with group support expected. Relationships more important than task orientation.
Large power distance	**Small power distance**
Society accepts unequal distribution of power. Respect for authority. Emphasis on titles and ranks. Subordinates expect to be told what to do. Centralization emphasized.	Society less accepting of power. Employees more open to the idea of dialogue with their superior. Less emphasis on authority, titles, and ranks. Inequality minimized. Decentralization emphasized.
Uncertainty tolerance	**Uncertainty avoidance**
People accept uncertainty and are open to risk taking. Willing to take risks.	Afraid of ambiguity and uncertainty. Structure and formal rules preferred.
Masculinity*	**Femininity**
Aggressive and assertive behavior. Emphasis on material things, success, and money.	Relationship-oriented. Quality of life favored. Concern for the welfare of others; caring. Emphasis on modesty.
Long-term orientation	**Short-term orientation**
Characterized by hard work and perseverance. Savings-driven.	Less emphasis on hard work and perseverance. Consumption-driven.

* Some authors prefer to use the terms *quantity versus quality of life* or *aggressive versus passive goal orientation* instead of *masculinity versus femininity*, the terms Hofstede used originally.

France: *Le Plan* and the *Cadre*

In France, government planning on a national scale (legal–political environment factor) helps coordinate the plans of individual industries and companies (managerial function of planning). The government's aim is to utilize most effectively the country's resources and to avoid expansion in uneconomic areas. Although government planning—which is also extended to regional areas—is carried out by relatively few, but competent, people, other government departments, employers' organizations, unions, and consumers provide cooperation and assistance.

At times, the plan becomes a global strategy helping specific industries. For example, the government attempts to integrate the electronics industry into a whole so that it can overcome its weaknesses in information processing, consumer electronics, microelectronics, and automation. To

implement the strategy, the government plans to support several national projects, such as speech synthesis, mini- and microcomputers, and mainframe computers. Clearly, there is a close relationship between government planning and firms, especially those that are owned and directly aided by the government.

The heavy involvement of government in economic and social activities resulted in a large civil service with some 4.5 million workers.[13] Civil servants have advantages over private-sector workers: higher pay, shorter hours, more holidays, better pension, more bonuses, almost complete job security, and other perks. In France, in contrast to other European countries, the government work force grew some 20 percent between 1979 and 1999 so that about one in four French workers received their pay from the government. It is no surprise then that many French people would like to become civil servants, or "functionaries."

Jean-Louis Barsoux and Peter Lawrence noted not only the close relationship between government and industry but also the impact of the elite universities, the Grandes Écoles, on forming the French managerial mind, which is considered essential for managing in both government and business organizations.[14] These schools supply the *cadre*, the managerial elite. Moreover, the schools' connections are vital for managerial success. What is valued in these managers is analytical ability, independence, and proficiency in synthesizing facts. While written communication is considered very important, oral communication is de-emphasized. These managers exhibit intellectual ability rather than action. Rationality, problem solving, and numerical analysis are important for obtaining high managerial posts in government as well as in business. Indeed, it is not unusual for managers to work for both alternately.

The French managerial model also has drawbacks. It may limit managers in dealing with nonquantifiable and "nonrational" data and in responding quickly to changes in the environment, and it may not result in the selection of the best managers because school ties may be more important than performance. Although the managerial characteristics may also be limiting in terms of obtaining a global outlook, French managers, in general, are quite supportive of the European Union. They see it as an opportunity to restructure the New Europe.

Germany: Authority and Codetermination

In the past, and to a lesser extent today, the German cultural environment favored reliance on authority in directing the work force, although it was

Codetermination requires labor membership in the supervisory board and the executive committee of the corporation.

often benevolent authoritarianism (managerial function of leading). Even today, while managers may show concern for subordinates, they also expect obedience. In 1951, a law was passed that provided for **codetermination**, which requires labor membership in the supervisory board and the executive committee of certain large corporations. Furthermore, a labor director is elected as a member of the executive committee. This position is a difficult one. Labor directors supposedly must represent the interests of the employees and, at the same time, must make managerial decisions that are in the best interest of the enterprise.

Selected Factors Influencing Managing in Other Western Countries

Managing in Australia is influenced by the country's moralistic stance and its emphasis on political and social values, achievement, and risk taking.

Italian managers operate in an environment of low tolerance for risks. Italians are very competitive, but at the same time they like group decision making.

Management in Austria (and Germany) is characterized by self-realization and leadership. Independence and competitiveness are valued. Tolerance for risk taking is rather low.

In Britain, job security is important, and so are resourcefulness, adaptability, and logic. Individualism is also highly valued.



Is There a European Management Model?[15]

Managers in European countries manage in different ways. Yet there are some commonalities, as interviews with top managers from European firms found:

- European managers think of themselves as being more people-oriented than American managers are.
- A great deal of negotiation takes place within European firms, such as between management and workers or unions and between headquarters and subsidiaries. The practice of codetermination in large German firms may be an illustration of such extensive negotiations. European managers perceive the American style as more top-down.
- Europeans also have developed great skills in managing international diversity. Managing across borders is achieved more through people than through structures and procedures. The ability of most European managers to speak several languages facilitates the "people approach."
- European managers operate between the extremes of short-term profit

orientation (of American managers, as perceived by European managers), and the long-term growth orientation of Japanese managers.

European managers, on the other hand, have adopted many managerial techniques from the Americans, and they also could learn from American entrepreneurship. In the global environment, with free flow of information and with MNCs operating in many countries, there may be some convergence of managerial approaches.

Korean Management

Chaebol is characterized by a tight collusion between government and industrial conglomerates.

Japanese management receives a great deal of attention, partly because of the economic success of Japanese companies in the past. The Republic of Korea (South Korea, referred to here as Korea) has also shown remarkable economic growth, but the Asian economic crisis that began in 1997 resulted in a dramatic downturn of its economy. Korean management practices are not well known. It would be incorrect to assume that Korean management is simply an extension of Japanese management. It is not, although there are some cultural and structural similarities, such as the dominance of powerful conglomerate companies. The Korean model has been characterized by the ***chaebol***, a tight collusion between government and industrial conglomerates. However, Kim Young Sam, when he was the Korean President, suggested: "We need a better balance between big and small companies. We cannot just let the chaebol grow by taking over small businesses."[16] He even declared: "The chaebol system, which puts the emphasis on outward expansion that burdens the people, has come to an end."[17]

Inhwa Korean concept of harmony.

In Japan, managers emphasize group harmony and cohesion expressed in the concept of *wa*; the Korean concept of ***inhwa*** also translates into harmony, but with less accent on group values. Korean organizations are quite hierarchical, with family members occupying key positions. Beyond blood relationships, the factors affecting hiring decisions often include the school attended or being from the same geographic region as the top person. The leadership style can best be described as top-down, or autocratic/paternalistic. This approach enables the firm to adjust quickly to demands in the environment by issuing commands. Lifetime employment does not prevail. Indeed, the labor turnover rates are high when compared with the low rates in Japan. Turnover is primarily attributable to resignations rather than dismissals. All in all, Korean management is different from both Japanese and American management practices.

Japanese Management and Theory Z

Japan, one of the leading industrial nations in the world, has adopted managerial practices that are quite different from those of other economically advanced countries in the Western world. The discussion here deals with two common Japanese practices: lifetime employment and consensus decision making. Then it compares and contrasts Japanese and U.S. managerial practices, including Theory Z. In the closing sections of parts 2 to 6 of this book, other managerial practices in Japan are discussed and compared with those in the United States and China.

Lifetime employment

Important features of Japanese management are lifelong employment for permanent employees (related to the managerial function of staffing), great concern for the individual employee, and emphasis on seniority.

Wa Japanese concept of harmony.

Typically, employees spend their working life with a single enterprise, which in turn gives employees security and a feeling of belonging. This practice brings the culturally induced concept of ***wa*** (harmony) to the enterprise, resulting in employee loyalty and close identification with the aims of the company. However, it also adds to business costs because employees are kept on the payroll even when there is insufficient work. Consequently, firms are beginning to question this practice. Indeed, changes appear to be in the making, but they are slow. What is often overlooked, however, is that this permanent employment practice is used primarily by large firms. In fact, it is estimated that the job security system applies to only about one-third of the labor force.

International Perspective

Are Japanese Workers Happy?[18]

Japanese workers endured long working hours and sometimes poor working conditions in exchange for lifetime employment. While this practice still prevails in many companies, some companies do not provide their workers with a sufficient safety net of employment. This insecurity may have contributed to making Japanese workers the least satisfied among seven countries surveyed.

www.isrsurveys.com

A study conducted by International Survey Research found that the Japanese were the least satisfied and the Swiss workers the most satisfied. Specifically, in response to the question "Taking everything into account, how satisfied are you with your company as an employer?", the following results were obtained. In Switzerland 82 percent of the workers were satisfied, in Canada 73 percent,

in Mexico 72 percent, in Germany 66 percent, in the United States 65 percent, in the United Kingdom 63 percent, and in Japan only 44 percent.

Moreover, only 33 percent of the Japanese workers felt that their company was managed well. Among the respondents, 60 percent felt that they were not fairly appraised; only 37 percent felt that their pay was fair.

The often admired disciplined Japanese work force appears to think that their contributions to Japan's economic success have not been sufficiently recognized and rewarded, as shown by the low satisfaction of its workers.

Closely related to lifelong employment is the seniority system, which provides privileges for older employees who have been with the enterprise for a long time. But there are indications that this system may be superseded by a more open approach that provides opportunities for advancement for young people. For example, the relatively new Sony Corporation has team leaders (a point is made of not calling them supervisors) who are often young women 18 or 19 years of age. There is practically no age difference between these leaders and the operators they lead.

www.world.sony.com

Decision making in Japan

The managerial practice of decision making in Japan is also considerably different from that in the United States. It is built on the concept that change and new ideas should come primarily from below. Thus, lower-level employees prepare proposals for higher-level personnel. Supervisors, rather than simply accepting or rejecting the proposals, tactfully question them, make suggestions, and encourage subordinates. If necessary, proposals are sent back to the initiator for more information. Still, in major decisions, top management retains its power.

Japanese management, then, uses decision making by consensus to deal with everyday problems. Lower-level employees initiate an idea and submit it to the next higher level, until it reaches the desk of the top executive. If the proposal is approved, it is returned to the initiator for implementation.

Theory Z

Theory Z The adaptation of selected Japanese managerial practices to the U.S. environment.

In **Theory Z**, selected Japanese managerial practices are adapted to the environment of the United States. This approach is practiced by companies such as IBM, Hewlett-Packard, and the diversified retail company Dayton-Hudson. One of the characteristics of Type Z organization, as suggested by Professor William Ouchi, is an emphasis on the interpersonal skills needed

www.ibm.com
www.hp.com

for group interaction.[19] Yet, despite the emphasis on group decision making, responsibility remains with the individual (which is quite different from the Japanese practice, which emphasizes collective responsibility). There is also an emphasis on informal and democratic relationships based on trust. Yet the hierarchical structure remains intact, as illustrated by IBM, where not only goals but also authority, rules, and discipline guide corporate behavior.

Porter's Competitive Advantage of Nations[20]

Besides appreciating cultural differences in management style, managers should also understand the economic situations of other countries. Michael Porter, a Harvard Business School professor, questions the economic theory of comparative advantage. He suggests four sets of factors that contribute to a nation's well-being. The first set pertains to factor conditions such as a nation's resources, its labor costs, and the skills and education of its people. The second factor set consists of the demand conditions of a nation, such as the market size, the way products may be advertised, and the degree of consumer sophistication. The third set of factors concerns the suppliers: a company prospers when supporting companies are located in the same area. The fourth factor set consists of the firm's strategy and structure as well as rivalry among competitors.

A favorable combination of the four sets of factors leads to competitive advantage. When only two sets are favorable, competitive advantage usually cannot be sustained. On the other hand, the availability of resources is not always necessary. Japan, for example, lacks natural resources, yet the country prospered in the past. In fact, economic hardship may stimulate economic activity and success, as illustrated by Japan and Germany after World War II. However, these two countries have consumers who demand sophisticated products of high quality. Similarly, Japanese and German companies have good relationships with their suppliers. They also benefit from good education systems and a skilled labor force. Despite cooperation among Japanese companies on certain levels, they are also fiercely competitive.

Gaining a Global Competitive Advantage through Quality Management

Quality has become a strategic weapon in the global marketplace. American companies, once the acknowledged world leaders in productivity, have become under siege from firms around the globe. One reason is that many

American companies became complacent and failed to see the changing needs of the global market, which increasingly demanded quality products. This complacency and the lack of foresight enabled competitors, especially those from Japan, to use a powerful weapon to increase their market shares in the U.S. and European markets. This weapon is quality.

Before managers can revolutionize the production process, they must first revolutionize the way they think about quality. The need for a new philosophy of quality is paramount. The old philosophy of adequacy—maintaining the status quo for as long as a product turns a profit—is no longer acceptable. Now the aim of companies must be nothing short of excellence. To attain excellence, however, managers must be willing to put the needs of their customers first. They must never forget that customers are indispensable: they are the reason the company exists.

Traditional Quality Management Gurus[21]

Although the concern for quality may seem like a recent phenomenon, there were several quality gurus who tried to introduce their theories to American companies in the 1950s. But U.S. managers did not listen. This, however, is beginning to change. In fact, early quality management pioneers have now been joined by many new advocates of quality. We will briefly review the contributions of three quality champions: Deming, Juran, and Crosby. Each has taken a different approach to quality management, yet each has helped to shape its direction.

There are several interesting parallels between the career paths of the two American professors: Dr. Deming and Dr. Juran. Both men taught in the business department at New York University in the 1950s. During the post–World War II economic boom, Deming and Juran made unsuccessful attempts to persuade American managers to focus on quality. When Americans ignored their teachings, the two scholars decided to take their message to a more receptive audience—the Japanese.

Their pilgrimage to Japan could not have occurred at a more favorable time. Before the 1950s, Japan's export trade suffered because their domestic goods had a reputation for shoddy workmanship and inferior quality. Japanese-made cars, for example, were poorly designed and manufactured, were unreliable, and featured unattractive styling. With such a combination of undesirable product features, it is not surprising that American consumers were uninterested in Japanese-made vehicles.

But over the last three decades, Japanese auto makers have steadily captured a market share in the United States by selling quality cars. This

transformation from inferior to superior quality was, to a great extent, made possible by the teachings of Deming and Juran. They helped to revolutionize the quality of Japan's industries, and they have become the quality heroes. Partly because of their work, consumers all over the world now equate Japanese products with high quality. As a tribute to his contributions, the most coveted quality award in Japan is named in honor of the late Dr. Deming. Today, many years after Deming and Juran showed Japanese managers how to produce quality products, they are finally getting some much-deserved attention from American managers.

The last of this trio of quality gurus is Phil Crosby. Unlike Deming and Juran, Crosby did not cross the Pacific to instruct the Japanese, nor did his approach originate within the university setting. Crosby was not an academic. He formulated practical ideas for improving quality while working in a variety of U.S. corporations. His hands-on style enabled him to put his ideas into action at Martin Marietta and ITT, where he worked before becoming a corporate consultant.

www.deming.org
www.juran.com
www.philipcrosby.com

While all three experts—Deming, Juran, and Crosby—view quality as an imperative for survival, each of them defines quality differently. For Deming, quality meant providing customer-satisfying products and services at a low cost. It also meant a commitment to continual innovation and improvement that the Japanese call *kaizen*. For Juran, a key element in the definition of quality is a product's "fitness for use." Finally, Crosby explains quality from an engineering perspective as the conformance to precise standards and requirements. His motto is "Do it right the first time [and] achieve zero defects." All three experts consider statistics a valuable tool for measuring quality, although Deming is perhaps the best known for commitment to statistical analysis.

Other Quality Approaches and Awards[22]

As mentioned earlier, the Deming Award recognizes companies that have achieved superior quality in Japan. A similar award, but one with a different emphasis, is the Malcolm Baldrige National Quality Award established by the U.S. Congress in 1987. Another approach is known as ISO 9000, pioneered by the Europeans. There is also the European Quality Award given by the European Foundation for Quality Management.[23]

Malcolm Baldrige National Quality Award 1996[24]

www.quality.nist.gov

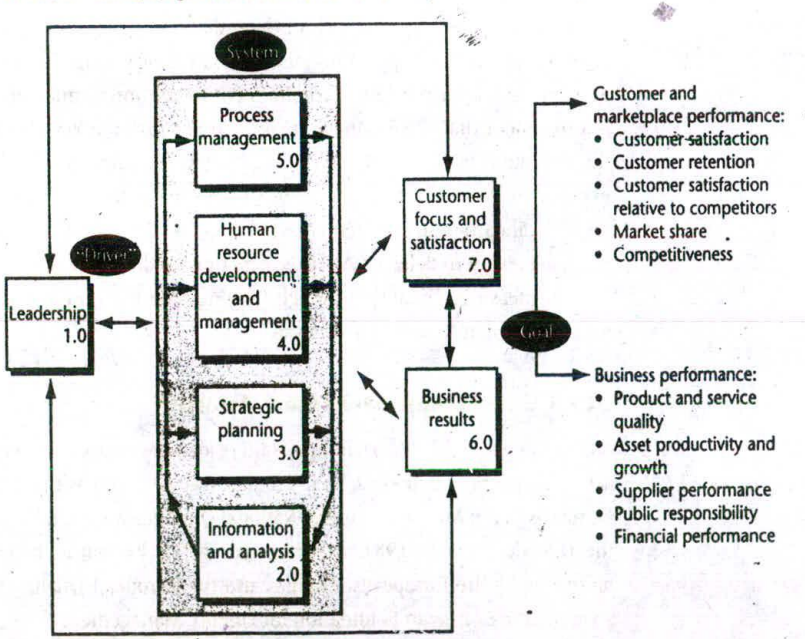
The Malcolm Baldrige award is the highest national recognition a U.S. company can receive for business excellence. The award helps the

understanding of performance requirements of excellence and competitiveness. The three categories for participation are (1) manufacturing firms, (2) service companies, and (3) small businesses. Applicants for the award are expected to share information about the company's improvement processes and the results so that this information can be used by other organizations. Each company benefits by getting feedback from the examiners.

Participants in the award program must show results and improvements in a variety of areas. Specifically, the criteria are grouped into seven categories with 24 items. The assessment, however, is tailored to the requirements of key success factors of the specific company, depending on the kind of business, its size, its strategy, and its stage of development. The seven categories, illustrated in Figure 3-2, are as follows:[25]

1. The *leadership* category requires that senior executives set direction and build and maintain the leadership required for high performance.

FIGURE 3-2 The Baldrige award criteria framework: dynamic relationships



Source: *Malcolm Baldrige National Quality Award 1996 Award Criteria* (Gaithersburg, MD: U.S. Department of Commerce, Technology Administration, National Institute of Standards and Technology, undated).

This criterion also demands leadership in creating an effective organization and management system as well as demonstrating public responsibility and corporate citizenship.

2. The *information and analysis* category examines the company's effectiveness and use of management information (financial and nonfinancial). It not only requires the analysis of company data but also includes competitive analysis and benchmarking, comparing performance with the best firms.
3. *Strategic planning* includes business planning with an emphasis on translating the plans into customer and operational requirements. Planning has to be driven by customer needs and operational improvement.
4. The category of *human resource development and management* includes criteria for all key aspects of human resources.
5. *Process management* focuses on all key work processes, including the design, introduction, production, and delivery of products and services. It also includes criteria for support services and supplier performance.
6. Organizations are results-oriented. This category looks at *results*: quality results in products and services as well as company operational and financial results; it also includes human resource and supplier performance results.
7. The final category is *customer focus and satisfaction*. Specifically, the criteria in this category require excellence in customer and market knowledge, relationships with customers, and customer satisfaction compared with that of the firm's competitors.

The award criteria focus on business results. They are nonprescriptive, which means the requirements can be met in a variety of ways. As shown in the seven categories, the criteria are comprehensive, involving interrelated processes and results that focus on improvement and continuous learning. They also emphasize a systems approach in which all parts of the organization are aligned with each other. Moreover, the criteria serve as a diagnostic tool, pointing out the strengths and weaknesses of the company.

The award criteria are not static but evolve toward a comprehensive system. For example, the 1996 award criteria discussed above had a new "business results" category added. At any rate, the Malcolm Baldrige award is designed to make U.S. companies more competitive in the global environment. Its criteria are congruent with the discussions in this book.

ISO 9000[26]

www.iso.ch

ISO 9000 has become so popular that some have termed it ISOmania. ISO, which is derived from the Greek *isos*, meaning equal, was founded in 1946 in Geneva, Switzerland. The ISO 9000 document was first published in 1987 and consists actually of five related standards numbered from 9000 to 9004 (and expanding). Although the ISO movement originated in Europe, now more than 100 countries participate in ISO, including Japan, the United States, and European Union nations. Most large companies, such as General Electric, Du Pont, British Telecom, and Philips Electronic, urge and even demand suppliers to be ISO 9000 certified.

ISO 9000 requires that the company document its processes and quality system, assure that all employees understand and follow the guidelines of the document, continually monitor and check the quality system through internal and external audits, and make any necessary changes. The internal benefits of ISO 9000 are the documentation of processes, a greater quality awareness of the company's employees, a possible change in organization culture resulting in increased productivity, and the installation of an overall quality system. The external benefits include an advantage over nonregistered competitors, meeting the requirements set forth by customers and the European Union, higher perceived quality and possible greater customer satisfaction, and meeting, for example, the demands of purchasing agents.

The Malcolm Baldrige award and ISO 9000 differ in focus, purpose, and content. ISO 9000 focuses on the adherence to the practices specified by the company. Its purpose is to assure buyers that certain practices and documentation are in conformance with the quality system identified by the firm. ISO 9000 does not evaluate the efficiency of the operation, nor improvement trends, nor the product quality. It does not ensure quality products or services, does not emphasize continuous improvement, and is not concerned with empowerment or teamwork. But ISO 9000 does provide the documentation to show customers how the company trains employees, tests its products, and corrects problems. Purchasing agents like to see proof that the registered company has a documented quality system and follows it. Documentation is a central aspect of ISO 9000. Therefore, ISO registration cannot be compared with Baldrige award scores.

European model for total quality management

www.efqm.org

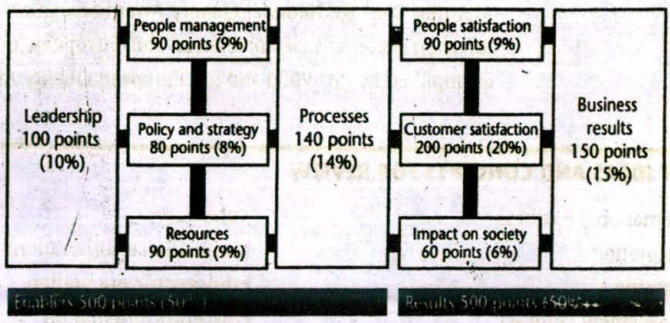
Another quality program is the European Quality Award bestowed upon excellent companies by the European Foundation for Quality Management

(EFQM).[27] The 1996 European model for total quality management, shown in Figure 3-3, is built on the following premise: "Customer Satisfaction, People (employee) Satisfaction, and Impact on Society are achieved through Leadership driving Policy and Strategy, People Management, Resources and Processes, leading ultimately to excellence in Business Results."[28] The percentages shown in the figure are used for assigning weights in the award.

The European total quality management model is built on the American Baldrige award but contains some new aspects, as a comparison of the two models reveals. Still, the models are very similar. For example, the "impact on society" variable in the European model is considered in the "leadership" concept of the Baldrige award as "public responsibility and corporate citizenship." Similarly, "people satisfaction" in the European model is part of "human resource development and management" in the Baldrige model. What is interesting in the European model is that the first five variables (leadership, people management, policy and strategy, resources, and processes) are called "enablers." This means that they deal with *how* an organization achieves the results. The four other criteria (people satisfaction, customer satisfaction, impact on society, and business results) are called "results" and deal with *what* an organization has achieved.

In conclusion, then, the American Malcolm Baldrige National Quality Award model and the European model for total quality management are similar, but both are very different from ISO 9000.

FIGURE 3-3 The European Foundation for Quality Management model for business excellence



Used with permission. "The EFQM Model for Business Excellence," in *Self-Assessment 1997 Guidelines for Companies* (Brussels: European Foundation for Quality Management, 1997), p. 8.

Summary

International businesses, which extend their operations across national boundaries, are particularly affected by the educational, sociocultural–ethical, political–legal, and economic environments of the host countries. Multinational corporations have developed different orientations for operating in foreign countries, ranging from ethnocentric (the foreign operation's views are based on those of the parent company) to geocentric (the organization is viewed as an interdependent system operating in many countries, that is, it is truly international).

Countries are forming regional alliances, such as the European Union, NAFTA, ASEAN, and Mercosur. Hofstede studied the impact of a country's culture on the behavior of its people.

Managerial practices differ between countries. In France, for example, government planning greatly influences the planning and direction of enterprises. In Germany, the use of authority and the concept of co-determination shape managerial practices. South Korea has developed managerial practices that are different from those in Japan and the United States. Japanese managerial practices differ greatly from those in the United States. Theory Z, which involves selected Japanese managerial practices, has been adopted by some U.S. companies.

International business managers also need to understand the economic situations of other countries. Porter identified four sets of factors that contribute to the competitive advantage of a nation.

Quality is a strategic weapon in the global marketplace. The traditional contributors to quality management are Deming, Juran, and Crosby. The Malcolm Baldrige National Quality Award recognizes U.S. organizations for their excellent performance. The European quest for quality is exemplified by ISO 9000 and the European Quality Award.

KEY IDEAS AND CONCEPTS FOR REVIEW

International business
Exportation
Licensing
Management contract
Joint venture
Subsidiary
Multinational corporation
Ethnocentric orientation
Polycentric orientation
Regiocentric orientation

Geocentric orientation
Global, or transnational, corporation
Country alliance and trade bloc
Hofstede's five dimensions of behavior
Management practices in France, Germany, and South Korea
Management practices in Japan and Theory Z
Porter's competitive advantage of nations
Contributions to quality management by Deming, Juran, and Crosby
Malcolm Baldrige National Quality Award criteria
ISO 9000
European Quality Award model

FOR DISCUSSION

1. What advantages do multinational corporations have? What challenges must they meet? Give examples.
2. What are the five cultural dimensions identified by Hofstede?
3. What are some key characteristics of French, German, Korean, and Japanese management practices?
4. What is Theory Z?
5. Do you think the managerial concepts and practices applied in the United States can be transferred to Britain, France, Germany, or any other country that you know?
6. Take any country with which you are familiar and discuss how factors in the educational environment impact on managing an enterprise.
7. Discuss how a company with a geocentric orientation may manage. Compare these practices with a company having an ethnocentric outlook.
8. Do you think that the way managerial decisions are made in Japan could work in the United States? Why or why not?
9. From the various approaches to quality management, which model do you find most useful? Why?

EXERCISE/ACTION STEPS

Interview the managers of a company that is known for excellent products or services. Ask how they achieved the high level of quality.

INTERNET RESEARCH

1. Search the Internet for Geert Hofstede and identify his articles and books. Discuss the cultural characteristics of any three countries.
2. Use the Internet to find out the economic conditions of the Eastern European countries that have been admitted to the European Union. Select one country to discuss in detail.

International Case

Woman CEO Manages by the Textbook[29]

The demand for managers with an international background is great. Consider Marisa Bellisario, who was one of the most sought-after executives in Europe. She was the first woman to head a major industrial firm in Italy, the state-controlled ITALTEL Societa Italiana. This company is the largest telecommunication equipment manufacturer in Italy. Bellisario's background, however, was international. After receiving her degree in economics and business administration from Turin University, she worked at Olivetti in the electronics division. When Olivetti sold its data processing unit to General Electric (GE), she spent time in Miami working on GE's worldwide marketing strategy for computers. She left GE to head corporate planning at Olivetti. As the chief executive officer (CEO) at ITALTEL, she turned the company around to show a small profit. (The firm had experienced huge losses in the past.) Her managerial approach had been characterized as "straight out of the textbook," and companies such as GTE Corporation, IBM, AT&T, and other European and Japanese firms were interested in recruiting her.

Questions

1. Why was Ms. Bellisario a much sought-after CEO? What was her career path?
2. What special problems may she have encountered as a woman heading a major company in Italy?
3. If she was successful managing by the textbook, why do some managers still think that management cannot be taught?

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Part - 1 closing

The Basis of Global Management

Management transcends national boundaries. In Chapter 1, the emphasis was on viewing organizations as open systems that interact with the external environment. But the external environment is not limited by national boundaries. Indeed, modern managers have to operate in a global environment. Even firms operating in one country will be affected by international competitive forces. For example, U.S. companies will have to compete more vigorously not only with Pacific Rim companies but also with those belonging to the European Union. In addition, China (referring to the People's Republic of China in this book) is becoming an economic power, especially since it was admitted to the World Trade Organization (WTO) in 2001.

International FOCUS

China—The New Economic Giant?[1]

During the past 25 years, China has been transformed from a Marxist system to an entrepreneurial force. It has been a breathtaking transformation since the country opened its doors. The hypergrowth of 9 to 10 percent annually during the 1990s was achieved without excessive inflation. By 2001, however, the gross domestic product fell to around 7 percent.[2] China will soon have one of the biggest economies in the world. With this growth rate and a population of about one-fifth of the world total, China attracts much foreign investment. It has been estimated that the economy will grow 7 percent annually until 2005 and then even 9 percent between 2006 and 2012. But there is also concern that official statistics may be overstated.[3]

The revolutionary economic development, spearheaded first by the late Deng Xiaoping (who, by the way, was not an economist) and continued by the then President Jiang Zemin, was accompanied by rising expectations. It was only in 1992 that the goal of the market economy (although a socialistic one) was declared.

In his path-setting speech on September 12, 1997, to the 15th Party Congress, Mr. Jiang announced some sweeping changes. His plan was to convert most of the 305,000 state-owned companies to shareholding firms that would be exposed to international competition. Although

the issue of ownership was only vaguely mentioned, some companies declared bankruptcy. At that time, state-owned companies still produced about 40 percent of industrial output; but they used most of the available capital, thus constraining more productive, flexible, privately owned firms. Still, the 1,000 largest firms remained under the control of the government; however, most of them would have to compete in the marketplace. Thus, Mr. Jiang had to deal with the industry dinosaurs on which 100 million workers depended for their living.

Although the 1997 speech may have laid the basis for the future direction of China, Mr. Jiang made an even bolder statement at the July 1, 2001, party meeting when he suggested that the party should engage capitalists to increase its "influence and cohesiveness."[4]

The plan was to form large corporations operating in industries such as high-tech electronics, telecommunication, and petrochemicals. China is already a major exporter of appliances, garments, and several lower-end products. To implement the ambitious plan, China has to reduce the tariffs on many goods to operate in the WTO. Shanghai and Hong Kong can become financial centers rivaling those in London, Tokyo, and New York.

However, the ambitious plans are accompanied by the risk of massive unemployment, which in turn could result in political unrest. So if many firms close down in the transformation process, those adversely affected must be taken care of. Provisions have to be made for helping them meet housing and medical expenses as well as for pensions, benefits that were previously granted by their employers. Besides providing a social safety net, workers also need to be trained for the demands created by the market economy.

China is facing some tough questions of how to proceed. While some politicians hold on to the communist philosophy, others forge ahead with Western ideas. The country has many strengths but also faces many challenges. Among the strengths are the relative openness toward reform, advances in technology, reunification with Hong Kong, educational progress through partnerships with Western universities, and access to modern technology through joint ventures. For example, in 1984, Volkswagen, the German car maker, signed a joint venture agreement with a consortium of Chinese partners. The new venture of Shanghai Volkswagen produced the VW Santana model, which now has the largest market share in China.

The leading Chinese industrial companies are engaged in petrochemicals, automobiles, electric power, iron and steel, and tobacco products. Among the multinational corporations, we find in car manufacturing Shanghai Volkswagen, Beijing Jeep, General Motors, and others; in chemicals we find BASF as the biggest investor in China; in consumer electronics, Matsushita invested heavily; in consumer goods are companies such as Unilever, SC Johnson, Henkel, Gillette, and Nike; in food, beverages, and restaurants are firms such as Cadbury, Kentucky Fried Chicken, and Pizza Hut, just to mention a few. Many multinational firms can also be found in oil, gas, pharmaceuticals, telecommunication, and a variety of services.

In management education, the China Europe International Business School (CEIBS), a joint project between the Chinese government and the European Union, offers a variety of management

programs, including an Executive MBA (Master of Business Administration) degree. The school, funded by the Shanghai municipal government and the European Union, introduces executives to management theories and practical skills necessary to integrate the Chinese economy into the global economy.

But China also faces formidable challenges, such as internal political opposition and the possibility of social unrest. The situation is aggravated by the migration of people to the already overcrowded urban areas, which are plagued by pollution and other urban ailments. Furthermore, inconsistent government regulation could discourage foreign investment.

Outside its boundaries, China has great opportunities. It is a major force in the Pacific Rim region. It also has access to Western technology, enabling it to catch up rapidly with developed countries. The eagerness of foreign firms to enter the market enables the Chinese to negotiate favorable terms.

On the other hand, China also faces considerable threats from abroad. The reduction of trade barriers may help the country as a whole but will hurt individual firms as they will have to compete with quality products from abroad. Although the economic crisis that started in 1997 in Pacific Rim countries, such as Thailand, Indonesia, and South Korea, has crippled those countries, their recovery poses significant competition for China.

In all, then, China has much strength not only to overcome its weaknesses but also to take advantage of its opportunities and to cope with threats. The challenges are to keep the economy growing (although at a lower rate than in the 1990s) without inflation and to deal with the social forces that may become restless during the transformation at a time of rising expectations. The relationship with Taiwan remains an issue that may need to be resolved later in the 21st century. China also needs to provide a political and legal environment free from corruption to attract foreign investors and to become a major force in the global community.[5]

After 15 years of negotiations, China has become a member of WTO. The signing of the membership agreement with WTO on November 11, 2001, and the ratification of its membership a month later as WTO's 143rd member certainly will create opportunities and challenges (e.g., it will drastically reduce the barriers for importing agricultural products from the United States), for China as well as for President Hu Jintao, Mr. Jiang's successor.[6]

Figure C1-1 summarizes the competitive position of China showing its internal strengths and weaknesses as well as the external opportunities and threats from other countries. The figure also indicates possible Chinese strategies by combining the internal and external factors, shown as Maxi–Maxi (maximizing internal strengths to take advantage of external opportunities), Mini–Maxi (minimizing weaknesses and maximizing opportunities), Maxi–Mini (maximizing strengths and minimizing threats), and Mini–Mini (minimizing both weaknesses and threats) strategies. These alternative strategies are driven by China's culture, purpose, and objectives, shown in the first box in the figure.

Asian economic conditions are also linked to Europe, and one of the driving forces in the European Union is the car industry, which is illustrated by the following case.

FIGURE C1.1 TOWS Matrix for the competitive situation of China

Country culture, values, purpose, objectives, etc.	**Internal strengths (S)**	**Internal weaknesses (W)**
• To be a powerful member of the international community (World Trade Organization, WTO) • To move toward a market economy • To improve the living standard of its people • To unify a diverse culture • To gain political and economic power	• Aggressive government reforms • Ability to change regulations (government intervention) • Strong bargaining position with interested investors • Large domestic market • Growing strength in high-tech, wireless, and electronics products • Low labor costs and Confucian ethics (loyalty, duty, etc.) • Vast natural resources (coal, iron ore, petroleum, etc.) • High growth with low inflation • Vastly improved socioeconomic conditions in last decade (health, nutrition, life expectancy, education) • Competitive advantage in clothing, consumer goods, fabric, toys, electrical machinery, and switch gear • Scholars educated abroad • WTO member	• Unemployment: risk of labor unrest • High poverty level • Regional economic development gap • Lack of trained managers • Political uncertainty • Poor legal system; lack of copyright/patent protection • Unprofitable state-owned enterprises (SOEs) • Despite natural resources, insufficient energy supply • Outdated banking system • Oversupply of expensive housing and office buildings • Consumer demand dropping • Variety of dialects hinders communication • Excessive bureaucracy and corruption • High inventory with deflationary tendencies
External opportunities (O)	**SO: Maxi–Maxi**	**WO: Mini–Maxi**
• Export light industrial goods to high-cost, high-priced markets and attract foreign investors • Technological developments demand for low-cost goods in high-priced and poor countries • Asia and Pacific Rim: traditional ties to these economies; financing from Hong Kong, Singapore, other countries or regions • USA: eagerness to access Chinese economy allows Chinese business access to its market with very little resistance; improved political relations	• Attract investment by reducing trade barriers and introducing clear long-term policies • Continue policy of constructive engagement with USA • Expand presence throughout Asia by bolstering large and competitive SOEs • Introduce protectionism by setting up new barriers and changing rules • Export items where China has a competitive advantage (electrical machinery, toys, footwear, apparel, power generation equipment, textiles, iron and steel)	• Improve management education by continuing to establish and promote linkages with Western universities and offering MBA at state universities • Provide a social safety net • Reform legal system and eliminate corruption; strengthen and enforce laws protecting intellectual property • Assist transition of unprofitable SOEs through absorption by larger SOEs or privatization (East German model)

• European Union (EU): same eagerness as USA; Hong Kong's traditional tie to EU economies creates natural links for China, especially in the banking industry • WTO membership allows China even more access to the U.S., EU, and Japanese markets		• Encourage foreign direct investment in the less-developed western regions to promote growth and reduce migration into the eastern cities • Raise money from other Asian countries for restructuring • Reduce bureaucracy and introduce policies that reduce arbitrary restrictions for foreigners • Attract foreign companies that are willing to share technology
External threats (T)	**ST: Maxi–Mini**	**WT: Mini–Mini**
• Asian financial crisis • Competition for exports and foreign investment due to falling labor costs and devalued currencies in other Asian countries • Hesitation of foreign investors due to Asian crisis along with political and legal uncertainties • Antidumping investigations	• Invest in high-tech industries • Lower tariffs and other barriers to free trade • Provide a stable legal system for foreign investors • Continue to move toward a market economy and reform of SOEs and reduction of government subsidies • Consider investing in emerging economies • Consider devaluing currency as a last resort	• Meet the requirements for WTO membership • Increase social reforms to reduce poverty and improve quality of life for workers

The TOWS Matrix is described in Chapter 5. The authors would like to acknowledge the assistance of Chris Capistran in conducting the research. The information is based on a forthcoming paper "An Analysis of China's Competitive Environment with the TOWS Matrix: An Alternative to Porter's Model" by Heinz Weihrich and Chunguan Ma; Michael E. Porter, *The Competitive Advantage of Nations* (New York: Free Press, 1990), p. 71; Heinz Weihrich, "The TOWS Matrix: A Tool for Situational Analysis," *Long Range Planning*, 1982, pp. 54–66; World Bank, *China Country Brief* (Washington, DC, 1998), p. 1; Dexter Roberts and Mark L. Clifford, "The Engine Is Misfiring," *Business Week*, October 1, 2001, pp. 80–81; "China Opens Up," *The Economist*, November 20, 1999, pp. 17–18; "China's Future: A Dampened Blaze," *The Economist*, March 9, 2002, pp. 46–47; "Systemic Corruption: Something Rotten in the State of China," *The Economist*, February 16, 2002, pp. 37–38; "Corruption in China: Rocking the Boat," *The Economist*, November 24, 2001; "China's Economy: East Asia's Whirlwind Hits the Middle Kingdom," *The Economist*, February 14, 1998, pp. 37–39; Roger Chen, "An Analysis of China's Economic Development Policies and Prospects," *Business Economics*, July 1998, pp. 29–34; "Chinese Companies, Silicon Valley, PRC," *The Economist*, June 27, 1998, pp. 64–65; data released by the International Data Company, January 21, 2003, by the Chinese Ministry of Information Technology, January 21, 2003, and by the Chinese Ministry of Foreign Trade and Economic Cooperation, January 23, 2003; "China in Transition," *Far Eastern Economic Review*, January 29, 1998, p. 26; Greg Mastel, *The Rise of the Chinese Economy* (Armonk, NY: M. E. Sharpe, 1997), p. 44; John Bryan Starr, *Understanding China* (New York: Hill and Wang, 1997), p. 61; U.S. Census Bureau, Foreign Trade Division, Data Dissemination Branch, *www.census.gov/foreign-trade*, accessed May 22, 2002; "Bush's Asian Challenge," *The Economist*, March 17, 2002, pp. 13–14; "China, America and Japan," *The Economist*, March 17, 2001, pp. 21–23; "Crashing to Earth," *The Economist*, April 7, 2002, p. 29; "China Complains to WTO," *Far Eastern Economic Review*, April 4, 2002; Catherine Gelb, "Are You Ready?" *China Business Review*, January–February 2002; *www.BIMBA.edu.cn*, accessed March 9, 2003; "Cars in China: Leave It to the Locals," *The Economist*, April 13, 2002, pp. 60–61.

Global Car Industry Case

The Car Market in the New Europe[7]

The European car market is at a crossroads—and the European Union (EU) is the reason. Certain European countries, especially Italy and France, had their car market protected from Japanese cars. The question is how the European Community (EC) 1992 provisions, which call for the elimination of trade barriers, will affect European car makers.

In the late 1980s, European manufacturers had excellent sales. Italian Fiat, French Peugeot Citroen, and German Volkswagen did very well in Europe, the largest market in the world. But in the 1990s, car sales slowed. In the luxury class, Mercedes and BMW maintained a strong market position. However, both firms are being challenged by Japanese upscale models, such as Nissan's Infiniti and Toyota's Lexus. The German car makers can hardly argue for Japanese import restrictions unless they are willing to risk constraints from the Japanese, who enjoy the luxury of driving BMW and Mercedes cars in their own country.

However, other car manufacturers argued before the EU Commission for indefinite transition of the EC 1992 rulings. Italy had established the most stringent barriers to Japanese imports by limiting them to 1 percent of the Italian market. Similarly, France had restricted imports of Japanese cars to 3 percent of the total market. In the late 1980s, Italy's car manufacturers Alfa Romeo, Fiat, and Lancia registered 60 percent of the home market, and Peugeot and Renault of France had more than 60 percent of the French market. EU countries other than Italy and France are less restrictive with respect to Japanese car imports. The elimination of all trade barriers would increase the Japanese share of the car market, which has been protected by a variety of overt and covert trade barriers.

There is no agreement on which companies would benefit most from a free market. While some think that Fiat, Peugeot Citroen, and Volkswagen would gain the most, others suggest that Ford, General Motors, and Volkswagen would be the winners. Ford may indeed be in a unique position. Several years ago, the company began integrating its 22 plants in the various EC countries into a truly European firm. In turn, this integrated network could result in increased productivity, and it has the potential of making Ford cars competitive. However, in 1996, Ford, Peugeot Citroen, Renault (45 percent of which is owned by the state), and Fiat were in weak positions in Europe, with Volkswagen (17.3 percent of market share) and General Motors (12.6 percent) being the market leaders.

To understand the European car industry in the 21st century, one must recognize the overcapacity in the industry. The European market shows fierce competition by companies such as Volkswagen, BMW, DaimlerChrysler, General Motors, Ford, Peugeot Citroen, and Renault. While Volkswagen leads the passenger car market with almost 19 percent in sales volume in 2001, General Motors, Ford, and Renault are struggling. One key factor in remaining competitive is to shorten the product development cycle.[8] The industry average is about four years, and extending the cycle can result in market share loss. However, developing new products can be very costly. Volkswagen has addressed this issue through platform sharing by various models.

Ford seems to have learned from Volkswagen's experience, as shown in a later version of the Mondeo. Fiat, which lost market share even in Italy, addresses the new-product/cost issue with a new production technology called space-frame technology, which allows a model to be made narrower or wider, shorter or longer, without requiring heavy investment on new product development. The aim is to assure a flow of new products at reasonable costs. New models helped Peugeot Citroen improve its market share from 11 percent to 14 percent. To the fierce competition among European car makers comes the threat from Japanese firms.

Traditionally, Japanese cars sold in Europe are imported from Japan. However, concerned about EU barriers, Japanese car makers are positioning themselves to circumvent import restrictions and other indirect barriers such as local content requirements. Toyota, for example, is setting up a manufacturing plant in Britain, but it is concerned about the 80 percent European-parts content requirement. Honda has been building a factory in Swindon, England, which in turn could increase Honda's European market share. Nissan is even more ambitious: it has been assembling cars in a factory in northern England since 1986.

Mazda, which is number 4 in Japan, is formulating a global strategy through alliances around the world. Cooperation is particularly strong with Ford, which owns a considerable part of Mazda. In fact, many cars with the Ford nameplate are made by Mazda. Mazda also has business ties with the Japanese company Suzuki and with the French Peugeot Citroen. In the meantime, it is shopping for other European partners.

Japanese car makers will find it more difficult to penetrate the market in Europe than in America. Lee Iacocca, Chrysler's former chief executive, stated in an interview: "Europe has gone to school in [on] the U.S. They will not allow the Japanese to do what they've done here, getting nearly 35 percent of the industry in a decade. There will be competition, but it will be honest competition."[9]

As it turned out, Japan did not exhaust its 1995 quota and consequently accepted a cut of its 1996 quota from 1.071 million in 1995 to 1.066 million vehicles. This cut was agreed upon in Tokyo during regular consultations in early 1996. While an official from the Japanese Ministry of International Trade and Industry indicated that the reduced quota would not be a drag on Japan's exports, Mr. Jacques Calvet, head of France's Peugeot Citroen group, again took the opportunity to demand an indefinite extension of the five-year-old quota system scheduled to end in 1999. He also wanted the quotas on Japanese vehicles expanded to include cars made by Japanese manufacturers in the European Union.

In addition to competition from Japan, imported cars from South Korea pose a new threat to the European car industry, from Hyundai and Daewoo (some of whose cars are made in Poland)

Questions

1. What would be the arguments for EU policies for opening the European car market?
2. If you were an Italian or French representative, how would you argue before the EU Commission for special rules restricting Japanese imports to Italy or France?

3. As a representative from France, what special rules or policies would you like to see to protect your home market?
4. What would be your position before the EU Commission if you were a representative of Great Britain, where many Japanese firms have invested heavily?
5. As a representative of Germany, what position would you take before the EU Commission?
6. How would you argue your case as a representative of the Japanese car industry?

Suggestion for role playing. Imagine a meeting of the EU Commission in Brussels with each country presenting their concern. The following roles can be assigned: EU commissioner directs the meeting and presents the goals of the European Union. Country and car representatives from Germany, Britain, France, and Italy present their positions. Also one representative from Japan should be invited to participate in the discussion as a guest.

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Part - 2

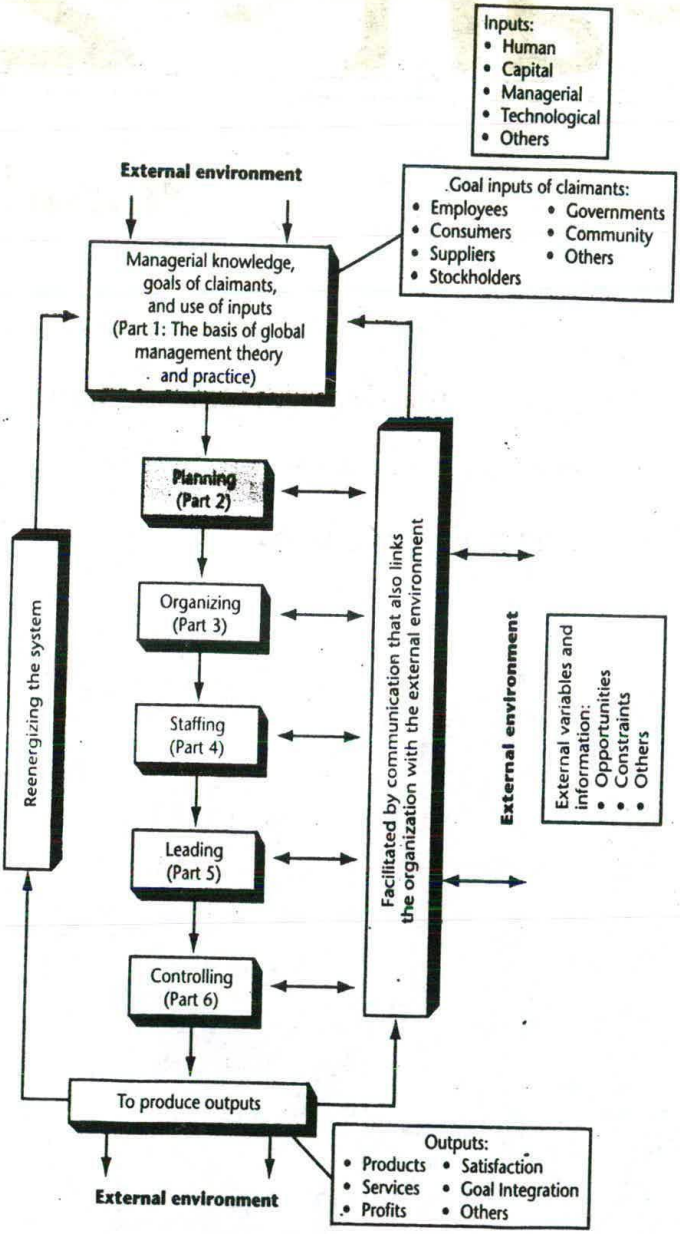
Planning

Chapter 4 *Essentials of Planning and Managing by Objectives*

Chapter 5 *Strategies, Policies, and Planning Premises*

Chapter 6 *Decision Making*

Part 2 Closing *Global Planning*



Systems approach to management

Chapter -4

Essentials of Planning and Managing by Objectives

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

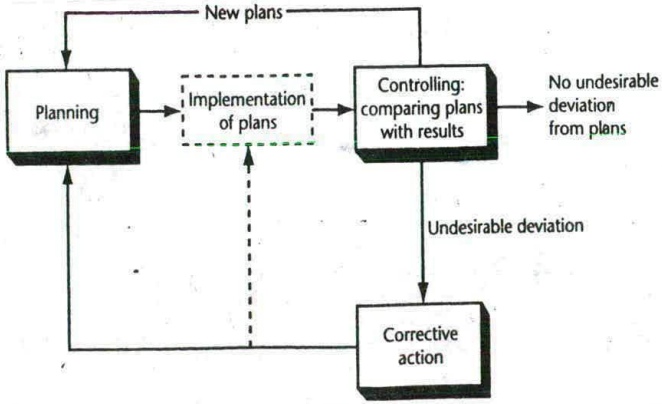
1. Understand what managerial planning is and why it is important.
2. Identify and analyze the various types of plans and show how they relate to one another.
3. Outline and discuss the logical steps in planning and see how these steps are essentially a rational approach to setting objectives and selecting the means of reaching them.
4. Explain the nature of objectives.
5. Describe how verifiable objectives can be set for different situations.
6. Outline the evolving concepts in management by objectives (MBO).
7. Understand the model of the systems approach to MBO.
8. Describe the benefits of MBO.
9. Recognize the weaknesses of MBO and suggest ways to overcome them.

You are now familiar with the basic management theory and have been introduced to the five essential managerial functions: planning, organizing, staffing, leading, and controlling. In Part 2 of this book, we shall discuss planning.

Planning Selecting missions and objectives as well as the actions to achieve them, which requires decision making, that is, choosing a course of action from among alternatives.

In designing an environment for the effective performance of individuals working together in a group, a manager's most essential task is to see that everyone understands the group's mission and objectives and the methods for attaining them. If group effort is to be effective, people must know what they are expected to accomplish. This is the function of planning. It is the most basic of all the managerial functions. **Planning** involves selecting missions and objectives and deciding on the actions to achieve them; it requires decision making, that is, choosing a course of action from among alternatives. Plans thus provide a rational approach to achieving preselected objectives. Planning also strongly implies managerial innovation, as will be discussed in Chapter 6. Planning bridges the gap from where we are to where we want to go. It is also important to point out that planning and controlling are inseparable—the Siamese twins of management (see Figure 4-1). Any attempt to control without plans is meaningless, since there is no way for people to tell whether they are going where they want to go (the result of the task of control) unless they

FIGURE 4-1 Close relationship of planning and controlling



first know where they want to go (part of the task of planning). Plans thus furnish the standards of control.



Types of Plans

Plans can be classified as (1) missions or purposes, (2) objectives or goals, (3) strategies, (4) policies, (5) procedures, (6) rules, (7) programs, and (8) budgets.

Missions or Purposes*

Mission or purpose The basic purpose or function or tasks of an enterprise or agency or any part of it.

The **mission**, or **purpose** (the terms are often used interchangeably), identifies the basic purpose or function or tasks of an enterprise or agency or any part of it. Every kind of organized operation has, or at least should have if it is to be meaningful, a mission or purpose. In every social system, enterprises have a basic function or task assigned to them by society. For example, the purpose of a business generally is the production and distribution of goods and services. The purpose of a state highway department is the design, building, and operation of a system of state highways. The purpose of the courts is the interpretation of laws and their application. The purpose of a university is teaching, research, and providing services to the community.

Although we do not do so, some writers distinguish between mission and purpose. While a business, for example, may have a social purpose of producing and distributing goods and services, it can accomplish this by fulfilling a mission of producing certain lines of products. The mission of an oil company, like Exxon, is to search for oil and to produce, refine, and market petroleum and petroleum products, from diesel fuel to chemicals. The mission of Du Pont has been expressed as "better things through chemistry," and Kimberly-Clark (noted for its Kleenex trademark) regards its business mission as the production and sale of paper and paper products. In the 1960s, the mission of the National Aeronautics Space Administration (NASA) was to get a person to the moon before the Russians. It is true

www.exxon.com
www.dupont.com
www.kimberly-clark.com
www.nasa.gov

* Often the term *vision* is mentioned in connection with the discussion of mission. Popular books on management discuss concepts such as goal setting, team management, and orientation toward the future, in connection with the discussion of vision. A recent study found no agreement among executives of the meaning of vision. Seven factors, however, were identified in the structure and content of vision statements. They were "formulation, implementation, innovative realism, general, degree of detail, risk propensity, and profit orientation."[1]

Synergy means that the whole is greater than its parts.

that in some businesses and other enterprises, the purpose or mission often becomes fuzzy. For example, many conglomerates have regarded their mission as **synergy,*** which is accomplished through the combination of a variety of companies.

Objectives or Goals

Objectives or goals The ends toward which activity is aimed.

Objectives, or **goals** (the terms are used interchangeably in this book), are the ends toward which activity is aimed. They represent not only the end point of planning but also the end toward which organizing, staffing, leading, and controlling are aimed. The nature of objectives and management by objectives will be discussed in greater detail later in this chapter.

Strategies

Strategy The determination of the basic long-term objectives of an enterprise and the adoption of courses of action and allocation of resources necessary to achieve these goals.

For years, the military used the word *strategies* to mean grand plans made in light of what it was believed an adversary might or might not do. While the term still usually has a competitive implication, managers increasingly use it to reflect broad areas of an enterprise's operation. In this book, **strategy** is defined as the determination of the basic long-term objectives of an enterprise and the adoption of courses of action and allocation of resources necessary to achieve these goals.

Policies

Policies General statements or understandings that guide or channel thinking in decision making.

Policies also are plans in that they are general statements or understandings that guide or channel thinking in decision making. Not all policies are "statements"; they are often merely implied from the actions of managers. The president of a company, for example, may strictly follow—perhaps for convenience rather than as policy—the practice of promoting from within; the practice may then be interpreted as policy and carefully followed by subordinates. In fact, one of the problems of managers is to make sure that subordinates do not interpret as policy minor managerial decisions that are not intended to serve as patterns.

Policies define an area within which a decision is to be made and ensure that the decision will be consistent with, and contribute to, an objective. Policies help decide issues before they become problems, make it

* The concept of synergy can be expressed simply as a situation in which 2 plus 2 becomes equal to 5, or in which the whole is greater than the sum of the parts.

unnecessary to analyze the same situation every time it comes up, and unify other plans, thus permitting managers to delegate authority and still maintain control over what their subordinates do.

There are many types of policies. Examples include policies of hiring only university-trained engineers, encouraging employee suggestions for improved cooperation, promoting from within, conforming strictly to a high standard of business ethics, setting competitive prices, and insisting on fixed, rather than cost-plus, pricing.



Policies for Market Leadership[2]

Michael Treacy and Fred Wiersema suggest that market leaders must excel in at least one of the three disciplines of (1) operational leadership, (2) product leadership, and (3) customer closeness. Companies usually do not excel in all three areas. *Operational excellence* means providing a good product or service at a low cost. For example, the warehouse store Costco has a limited selection of products but at low prices because of its operational effectiveness and efficiency. Similarly, Southwest Airlines offers no-frills flights at low fares. *Product leadership* may be illustrated by companies that develop a stream of new products faster than their competitors do. Intel, for example, develops microchips that are more powerful and faster than those of its formidable competitors such as Motorola, Texas Instruments, NEC, Toshiba, and Hitachi. *Customer intimacy* requires being close to the customers, learning about their goals and requirements. Thus, the entire company focuses on serving its customers, as illustrated by the close relationship between Airborne Express and Xerox.

www.costco.com
www.iflyswa.com
www.intel.com
www.airborne.com
www.xerox.com

Procedures

Procedures Plans that establish a required method of handling future activities.

Procedures are plans that establish a required method of handling future activities. They are chronological sequences of required actions. They are guides to action, rather than to thinking, and they detail the exact manner in which certain activities must be accomplished. For example, Case Western University outlines three steps for its appraisal process: (1) setting performance objectives, (2) performing a mid-year review of the objectives, and (3) conducting a performance discussion at the end of the period.[3] Procedures often cut across departmental lines. For example, in a manufacturing company, the procedure for handling orders may involve the sales department (for the original order), the finance department (for acknowledgment of receipt of funds and for customer credit approval), the accounting department (for recording the transaction), the production

department (for the order to produce the goods or the authority to release them from stock), and the shipping department (for determination of shipping means and route).[4]

A few examples illustrate the relationship between procedures and policies. Company policy may grant employees vacations; procedures established to implement this policy will provide for scheduling vacations to avoid disruption of work, setting rates of vacation pay and methods for calculating them, maintaining records to ensure each employee of a vacation, and spelling out the means for applying for leave.

Rules

Rules spell out specific required actions or nonactions, allowing no discretion.

Rules spell out specific required actions or nonactions, allowing no discretion. They are usually the simplest type of plan. "No smoking" is a rule that allows no deviation from a stated course of action. The essence of a rule is that it reflects a managerial decision that a certain action must—or must not—be taken. Rules are different from policies in that policies are meant to guide decision making by marking off areas in which managers can use their discretion, while rules allow no discretion in their application.



Procedures and Rules Imposed by the Outside

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At times, rules and procedures are set up because of unfavorable publicity. General Dynamics, one of the largest defense contractors, had been accused of improprieties.[5] In order not to be suspended from bidding on defense contracts, the company had to agree to a list of rules and procedures imposed by the U.S. Defense Department.

These new requirements were designed to prevent the shifting of costs from one contract to another. For example, workers have to prepare and sign their own time cards. The supervisor has to check each card; if one is incorrectly filled out, the worker involved has to make the correction, which then has to be initialed by the worker and the boss. The original entry must not be erased so that it can be checked later. Also, General Dynamics was required to establish tight rules for charging overhead expenses. Employees are not allowed to accept gifts—not even a pen or a calendar.

Thus, rules and procedures can be imposed by an important customer and are examples not only of planning but also of controlling, showing the close relationship between the two functions.

Programs

Program A complex of goals, policies, procedures, rules, task assignments, steps to be taken, resources to be employed, and other elements necessary to carry out a given course of action.

Programs are a complex of goals, policies, procedures, rules, task assignments, steps to be taken, resources to be employed, and other elements necessary to carry out a given course of action; they are ordinarily supported by budgets. They may be as major as an airline's program to acquire a $400 million fleet of jets or a five-year program to improve the status and quality of its thousands of supervisors. Or they may be as minor as a program formulated by a single supervisor to improve the morale of workers in the parts manufacturing department of a farm machinery company.

Budgets

Budget A statement of expected results expressed in numerical terms.

A **budget** is a statement of expected results expressed in numerical terms. It may be called a "quantified" plan. In fact, the financial operating budget is often called a *profit plan*. A budget may be expressed in financial terms; in terms of labor-hours, units of product, or machine-hours; or in any other numerically measurable terms. It may deal with operation, as the expense budget does; it may reflect capital outlays, as the capital expenditure budget does; or it may show cash flow, as the cash budget does. One of the most comprehensive budgets is prepared by the Office of Management and Budget of the White House.[6] The budget proposal is then presented to the Congress by the President of the United States.

Since budgets are also control devices, we reserve our principal discussion of them for Chapter 19 on control techniques. However, making a budget is clearly planning. The budget is the fundamental planning instrument in many companies. It forces a company to make in advance—whether for a week or for five years—a numerical compilation of expected cash flow, expenses and revenues, capital outlays, or labor- or machine-hour utilization. The budget is necessary for control, but it cannot serve as a sensible standard of control unless it reflects plans.

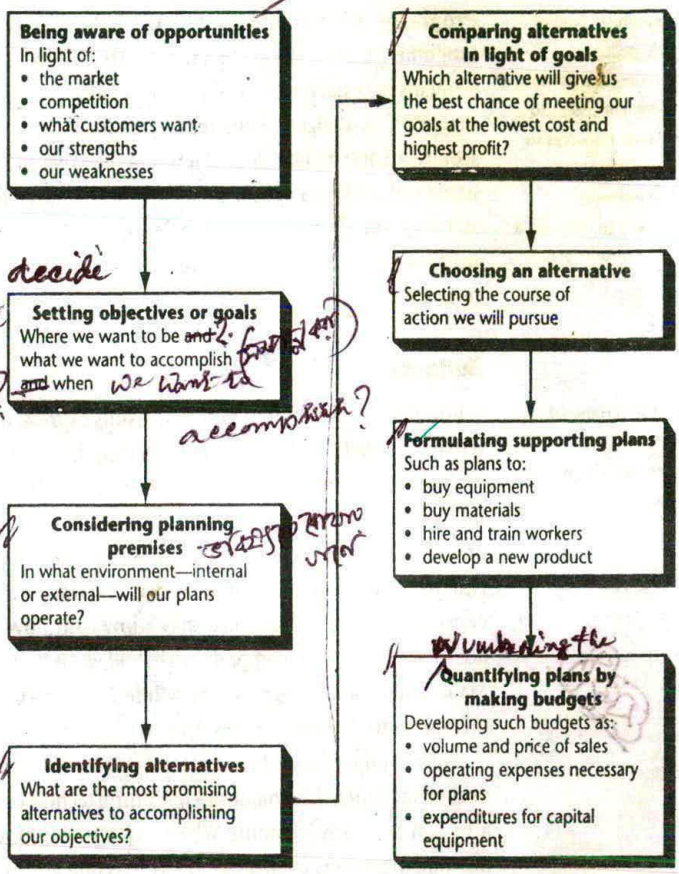
Steps in Planning

The practical steps listed below, and diagramed in Figure 4-2, are of general application. In practice, however, one must study the feasibility of possible courses of action at each stage.

1. Being Aware of Opportunities

Although it precedes actual planning and is therefore not strictly a part of

FIGURE 4-2 Steps in planning



the planning process, an awareness of opportunities* in the external environment as well as within the organization is the real starting point for planning. All managers should take a preliminary look at possible future opportunities and see them clearly and completely, know where their company stands in light of its strengths and weaknesses, understand what problems it has to solve and why, and know what it can expect to gain. Setting realistic objectives depends on this awareness. Planning requires a realistic diagnosis of the opportunity situation.

* The word *problems* might be used instead of *opportunities*. However, a state of disorder or confusion and a need for a solution to achieve a given goal can more constructively be regarded as an opportunity. In fact, one very successful and astute company president does not permit his colleagues to speak of problems; they must speak only of opportunities.

2. Establishing Objectives

The second step in planning is to establish objectives for the entire enterprise and then for each subordinate work unit. This is to be done for the long term as well as for the short range. Objectives specify the expected results and indicate the end points of what is to be done, where the primary emphasis is to be placed, and what is to be accomplished by the network of strategies, policies, procedures, rules, budgets, and programs.

Enterprise objectives give direction to the major plans, which, by reflecting these objectives, define the objective of every major department. Major departmental objectives in turn control the objectives of subordinate departments, and so on down the line. In other words, objectives form a hierarchy. The objectives of lesser departments will be more accurate if subdivision managers understand the overall enterprise objectives and the derivative goals. Managers should also have the opportunity to contribute ideas for setting their own goals and those of the enterprise.

3. Developing Premises

Premises Assumptions about the environment in which the plan is to be carried out.

Principle of planning premises The more thoroughly individuals charged with planning understand and agree to utilize consistent planning premises, the more coordinated enterprise planning will be.

The next logical step in planning is to establish, circulate, and obtain agreement to utilize critical planning premises such as forecasts, applicable basic policies, and existing company plans. **Premises** are assumptions about the environment in which the plan is to be carried out. It is important for all the managers involved in planning to agree on the premises. In fact, the major **principle of planning premises** is this: the more thoroughly individuals charged with planning understand and agree to utilize consistent planning premises, the more coordinated enterprise planning will be.

Forecasting is important in premising: What kinds of markets will there be? What volume of sales? What prices? What products? What technical developments? What costs? What wage rates? What tax rates and policies? What new plants? What policies with respect to dividends? What political or social environment? How will expansion be financed? What are the long-term trends?

4. Determining Alternative Courses

The fourth step in planning is to search for and examine alternative courses of action, especially those not immediately apparent. There is seldom a plan for which reasonable alternatives do not exist, and quite often an alternative that is not obvious proves to be the best.

The more common problem is not finding alternatives but reducing the number of alternatives so that the most promising may be analyzed. Even with mathematical techniques and the computer, there is a limit to the number of alternatives that can be thoroughly examined. The planner must usually make a preliminary examination to discover the most fruitful possibilities.

5. Evaluating Alternative Courses

After seeking out alternative courses and examining their strong and weak points, the next step is to evaluate the alternatives by weighing them in light of premises and goals. One course may appear to be the most profitable but may require a large cash outlay and have a slow payback; another may look less profitable but may involve less risk; still another may better suit the company's long-range objectives.

There are so many alternative courses in most situations and so many variables and limitations to be considered that evaluation can be exceedingly difficult. Because of these complexities, the newer methodologies and applications and analysis are discussed in Part 6 on controlling.

6. Selecting a Course

This is the point at which the plan is adopted—the real point of decision making. Occasionally, an analysis and evaluation of alternative courses will disclose that two or more are advisable, and the manager may decide to follow several courses rather than the one best course.

7. Formulating Derivative Plans

When a decision is made, planning is seldom complete, and a seventh step is indicated. Derivative plans are almost invariably required to support the basic plan.

8. Quantifying Plans by Budgeting

After decisions are made and plans are set, the final step in giving them meaning, as was indicated in the discussion on types of plans, is to quantify them by converting them into budgets. The overall budget of an enterprise represents the sum total of income and expenses, with resultant profit or surplus, and the budgets of major balance sheet items such as cash and capital expenditures. Each de[illegible]r program of a business or some

other enterprise can have its own budgets, usually of expenses and capital expenditures, which tie into the overall budget.

If done well, budgets become a means of adding the various plans and set important standards against which planning progress can be measured.

International Perspective

Applying the Planning Steps in Preparing for College[7]

The planning steps can be applied to most planning situations. High school students probably follow these steps to some degree when planning for college. First, they are aware of opportunities to attend college and the benefits derived from a college education. Then they set objectives in a variety of areas, such as the area of study and completion of the degree within four years. They also develop planning premises. Thus, they may make the assumption that scholarships are available or that they may have to work while attending college. Some students may assume that they want to stay in the same area, or the same state, while others may want to study abroad. In each situation, there are usually several alternatives available that should then be carefully evaluated. Thus, students may assess the advantages and disadvantages of applying for admission at different schools. After receiving several acceptance letters, they have to select the appropriate college. This is an important decision point. After making a choice, they need to formulate derivative plans, which may include selecting housing, moving to the new location, or finding a job near the college. Then the students need to quantify their plans by converting them into budgets, which may include tuition, moving and housing costs, clothing and entertainment expenses, and so on.

These steps do not always follow the same sequence. For example, when evaluating alternative courses, one may have to go back and make new assumptions for the various alternatives. Or one may develop different courses of action based on different assumptions. One course may be based on the assumption of obtaining a scholarship, another course on the premise that one has to work through college. Clearly, then, planning is not a linear process but a reiterative one.

Coordination of Short- and Long-Range Plans

Often short-range plans are made without reference to long-range plans. This is plainly a serious error. The importance of integrating the two types can hardly be overemphasized, and no short-run plan should be made unless it contributes to the achievement of the relevant long-range plan.

Much waste arises from decisions about immediate situations that fail to consider their effect on more remote objectives.

Responsible managers should continually review and revise immediate decisions to determine whether they contribute to long-range programs, and subordinate managers should be regularly briefed on long-range plans so that they will make decisions consistent with the company's long-range goals. Doing this is far easier than to correct inconsistencies later, especially since short-term commitments tend to lead to further commitments along the same line.

Objectives

An objective is **verifiable** when at the end of the period one can determine whether or not it has been achieved.

Objectives were defined earlier as the important ends toward which organizational and individual activities are directed. Since writers and practitioners make no clear distinction between the terms *goals* and *objectives*, they are used interchangeably in this book. Within the context of the discussion, it will become clear whether the objectives are long term or short term, broad or specific. The emphasis is on **verifiable** objectives, which means at the end of the period it should be possible to determine whether or not the objective has been achieved. The goal of every manager is to create a surplus (in business organizations, this means profit). Clear and verifiable objectives facilitate measurement of the surplus as well as the effectiveness and efficiency of managerial actions.

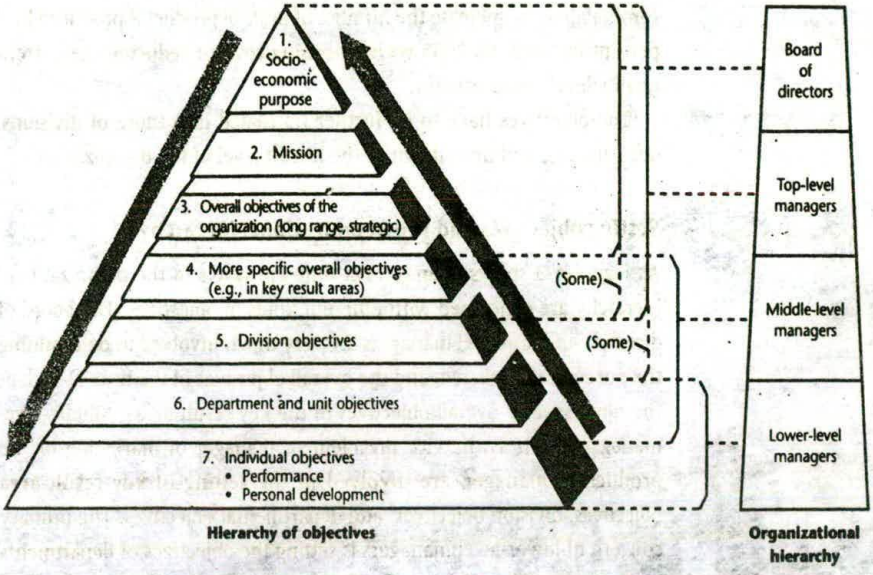
The Nature of Objectives

Objectives state end results, and overall objectives need to be supported by subobjectives. Th[illegible] objectives form a hierarchy as well as a network. Moreover, organizations and managers have multiple goals that are sometimes incompatible and may lead to conflicts within the organization, within the group, and even within individuals. A manager may have to choose between short-term and long-term performance, and personal interests may have to be subordinated to organizational objectives.

Hierarchy of objectives

As Figure 4-3 shows, objectives form a hierarchy, ranging from the broad aim to specific individual objectives. The zenith of the hierarchy is the purpose or mission, which has two dimensions. First, there is the social purpose, such as contributing to the welfare of people by providing goods and services at a reasonable price. Second, there is the mission or purpose

FIGURE 4-3 Relationship of objectives and the organizational hierarchy



Adapted from H. Weihrich and J. Mendleson, *Management: An MBO Approach* (Dubuque, IA: Wm. C. Brown Co., 1978), p. xi. Used with permission.

of the business, which might be to furnish convenient, low-cost transportation for the average person. The stated mission might be to produce, market, and service automobiles. As you will notice, the distinction between purpose and mission is a fine one, and therefore many writers and practitioners do not differentiate between the two terms. At any rate, these aims are in turn translated into general objectives and strategies, such as designing, producing, and marketing reliable, low-cost, fuel-efficient automobiles.

Key result area An area in which performance is essential for the success of the enterprise.

The next level of the hierarchy contains more specific objectives, such as those in the **key result areas**. These are the areas in which performance is essential for the success of the enterprise.

Although there is no complete agreement on what the key result areas of a business should be—and they may differ between enterprises—Peter F. Drucker suggests the following: market standing, innovation, productivity, physical and financial resources, profitability, manager performance and development, worker performance and attitude, and public responsibility.[8] More recently, however, two other key result areas have become of strategic importance: service and quality.

Examples of objectives for key result areas are the following: to obtain a 10 percent return on investment by the end of calendar year 2005 (profitability); to increase the number of units of product X produced by 7 percent by June 30, 2005 without raising costs or reducing the current quality level (productivity).

The objectives have to be further translated into those of divisions, departments, and units down to the lowest level of the organization.

Setting objectives and the organizational hierarchy[9]

As Figure 4-3 shows, managers at different levels in the organizational hierarchy are concerned with different kinds of objectives. The board of directors and top-level managers are very much involved in determining the purpose, the mission, and the overall objectives of the firm, as well as the more specific overall objectives in the key result areas. Middle-level managers, such as the vice president or manager of marketing or the production manager, are involved in the setting of key-result-area objectives, division objectives, and departmental objectives. The primary concern of lower-level managers is setting the objectives of departments and units as well as of their subordinates. Although individual objectives, consisting of performance and development goals, are shown at the bottom of the hierarchy, managers at higher levels also should set objectives for their own performance and development.

There are different views about whether an organization should use the top-down or the bottom-up approach in setting objectives, as indicated by the arrows in Figure 4-3. In the top-down approach upper-level managers determine the objectives for subordinates, while in the bottom-up approach subordinates initiate the setting of objectives for their positions and present them to their superior.

Proponents of the top-down approach suggest that the total organization needs direction through corporate objectives provided by the chief executive officer (in conjunction with the board of directors). Proponents of the bottom-up approach, on the other hand, argue that top management needs to have information from lower levels in the form of objectives. In addition, subordinates are likely to be highly motivated by, and committed to, goals that they initiate. Personal experience has shown that the bottom-up approach is underutilized but that either approach alone is insufficient.

Multiplicity of objectives

Objectives are normally multiple. For example, merely stating that a university's mission is education and research is not enough. It would be much more accurate (but still not verifiable) to list the overall objectives, which might be the following:

- Attracting students of high quality
- Offering basic training in the liberal arts and sciences as well as in certain professional fields
- Granting postgraduate degrees to qualified candidates
- Attracting highly regarded professors
- Discovering and organizing new knowledge through research
- Operating as a private school supported principally through tuition and gifts of alumni and friends

Likewise, at every level in the hierarchy of objectives, goals are likely to be multiple. Some people think that a manager cannot effectively pursue more than two to five objectives. The argument is that too many objectives tend to dilute the drive for their accomplishment. But the limit of two to five objectives seems too arbitrary; managers might pursue more significant objectives. It would be wise to state the relative importance of each objective so that major goals receive more attention than lesser ones. At any rate, the number of objectives managers should realistically set for themselves depends on how much they will do themselves and how much they can assign to subordinates, thereby limiting their role to one of assigning, supervising, and controlling.

How to Set Objectives[10]

Without clear objectives, managing is haphazard. No individual and no group can expect to perform effectively and efficiently unless there is a clear aim. Table 4-1 illustrates some objectives and how they can be restated in a way that allows measurement.

Quantitative and qualitative objectives

To be measurable, objectives must be verifiable. This means that one must be able to answer this question: At the end of the period, how do I know if the objective has been accomplished? For example, the objective of

TABLE 4-1 Examples of nonverifiable and verifiable objectives

Nonverifiable objective	Verifiable objective
1. To make a reasonable profit	1. To achieve a return on investment of 12% at the end of the current fiscal year
2. To improve communication	2. To issue a two-page monthly newsletter beginning July 1, 2005, involving not more than 40 working hours of preparation time (after the first issue)
3. To improve productivity of the production department	3. To increase production output by 5% by December 31, 2005, without additional costs while maintaining the current quality level
4. To develop better managers	4. To design and conduct a 40-hour in-house program on the "fundamentals of management," to be completed by October 1, 2005, involving not more than 200 working hours of the management development staff and with at least 90% of the 100 managers passing the exam (specified)
5. To install a computer system	5. To install a computerized control system in the production department by December 31, 2005, requiring not more than 500 working hours of systems analysis and operating with not more than 10% downtime during the first three months or 2% thereafter

making a reasonable profit (see Table 4-1) does not state how much profit is to be made, and what is reasonable to the subordinate may not be at all acceptable to the superior. In the case of such a disagreement, it is of course the subordinate who loses the argument. In contrast, a return on investment of 12 percent at the end of the current fiscal year can be measured; it answers these questions: how much or what? when?

At times, stating results in verifiable terms is more difficult. This is especially true when it involves the objectives for staff personnel and in government. For example, installing a computer system is an important task, but "to install a computer system" is not a verifiable goal. However, suppose the objective is "to install a computerized control system (with certain specifications) in the production department by December 31, 2005, with an expenditure of not more than 500 working hours." Then, goal accomplishment can be measured. Moreover, quality can also be specified in terms of computer downtime, such as "the system shall be operational 90 percent of the time during the first two months of operation."

Guidelines for setting objectives

Setting objectives is indeed a difficult task. It requires intelligent coaching by the superior and extensive practice by the subordinate. The guidelines shown in Table 4-2 will help managers in setting their objectives.

The list of objectives should not be too long, yet it should cover the main features of the job. As this chapter has emphasized, objectives should

TABLE 4.2 Checklist of manager objectives

If the objectives meet the criterion, write "+" in the box on the right of the statement. If they do not, mark "–" in the box.

1. Do the objectives cover the main features of my job?	☐
2. Is the list of objectives too long? If so, can I combine some objectives?	☐
3. Are the objectives verifiable, that is, will I know at the end of the period whether they have been achieved?	☐
4. Do the objectives indicate:	
(a) quantity (how much)?	☐
(b) quality (how well, or specific characteristics)?	☐
(c) time (when)?	☐
(d) cost (at what cost)?	☐
5. Are the objectives challenging yet reasonable?	☐
6. Are priorities assigned to the objectives (ranking, weight, etc.)?	☐
7. Does the set of objectives also include:	
(a) improvement objectives?	☐
(b) personal development objectives?	☐
8. Are the objectives coordinated with those of other managers and organizational units?	☐
Are they consistent with the objectives of my superior, my department, and the company?	☐
9. Have I communicated the objectives to all who need to be informed?	☐
10. Are the short-term objectives consistent with the long-term aims?	☐
11. Are the assumptions underlying the objectives clearly identified?	☐
12. Are the objectives expressed clearly, and are they in writing?	☐
13. Do the objectives provide for timely feedback so that I can take any necessary corrective steps?	☐
14. Are my resources and authority sufficient for achieving the objectives?	☐
15. Have I given the individuals who are expected to accomplish the objectives a chance to suggest their objectives?	☐
16. Do my subordinates have control over aspects for which they are assigned responsibility?	☐

be verifiable and should state what is to be accomplished and when. If possible, the quality desired and the projected cost of achieving the objectives should be indicated. Furthermore, objectives should present a challenge, indicate priorities, and promote personal and professional growth and development. These and other criteria for good objectives are

summarized in Table 4-2. Testing objectives against the criteria shown in the checklist is a good exercise for managers and aspiring managers.

Evolving Concepts in Management by Objectives[11]

Management by objectives A comprehensive managerial system that integrates many key managerial activities in a systematic manner and is consciously directed toward the effective and efficient achievement of organizational and individual objectives.

Management by objectives (MBO) is now practiced around the world. Yet, despite its wide application, it is not always clear what is meant by MBO. Some still think of it as an appraisal tool; others see it as a motivational technique; still others consider MBO a planning and control device. In other words, definitions and applications of MBO differ widely. We define **management by objectives** as a comprehensive managerial system that integrates many key managerial activities in a systematic manner and is consciously directed toward the effective and efficient achievement of organizational and individual objectives. This view of MBO as a system of managing is not shared by all. While some still define MBO in a very narrow, limited way, we prefer to see it as a comprehensive goal-driven, success-oriented management system as shown in Figure 4-4. Besides being used for performance appraisal, as an instrument for motivating individuals, and in strategic planning, there are still other managerial subsystems that can be integrated into the MBO process. They include human resource planning and development (staffing as well as individual and organization development), career planning (building on personal strengths and overcoming weaknesses), the reward system (paying for performance), budgeting (planning and controlling), and other managerial activities important for a specific position. These various managerial activities need to be integrated into a system. In short, MBO, to be effective, must be considered a way of managing as shown in Figure 4-4, and not an addition to the managerial job.[12]

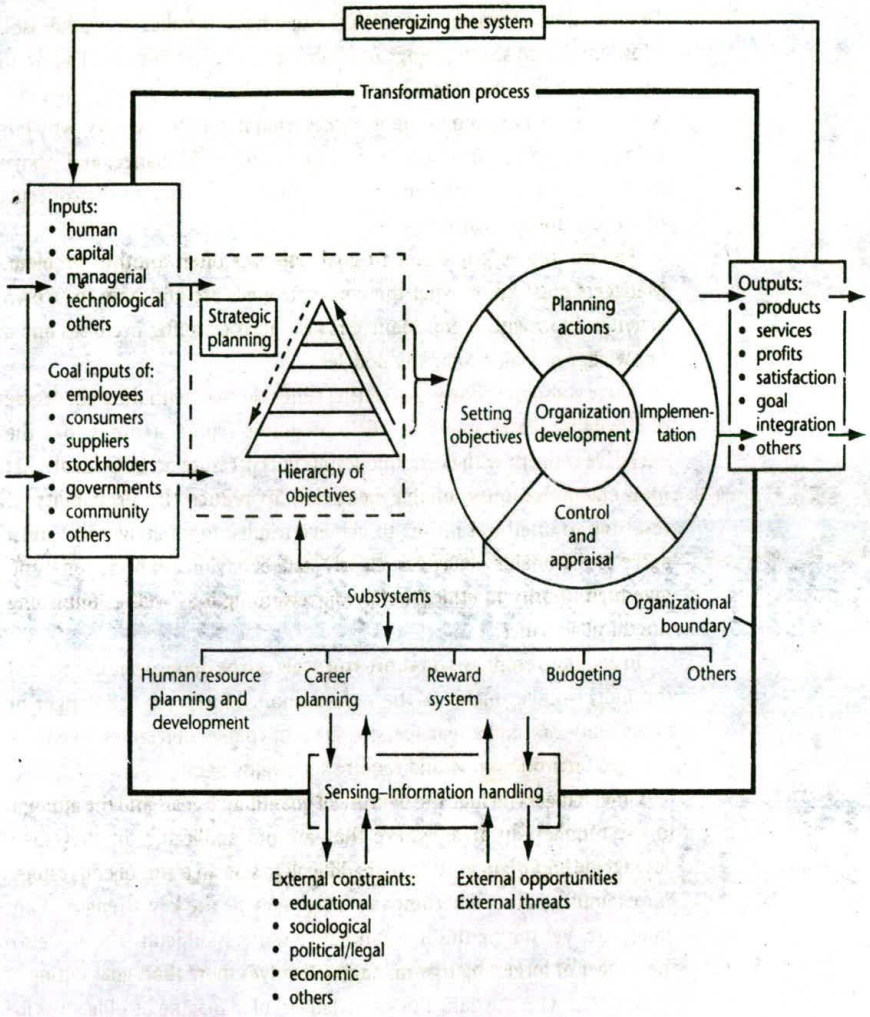
Benefits and Weaknesses of Management by Objectives

Although goal-oriented management is now one of the most widely practiced managerial approaches, its effectiveness is sometimes questioned. Faulty implementation is often blamed, but another reason is that MBO may be applied as a mechanistic technique focusing on selected aspects of the managerial process without integrating them into a system.

Benefits of management by objectives

There is considerable evidence, much of it from laboratory studies, that shows the motivational aspects of clear goals. But there are other benefits, such as the following:

FIGURE 4-4 Systems approach to management by objectives



Adapted from Heinz Weihrich, *Management Excellence: Productivity through MBO* (New York: McGraw-Hill, 1985), p. 18.

- Improvement of managing through results-oriented planning
- Clarification of organizational roles and structures as well as delegation of authority according to the results expected of the people occupying the roles
- Encouragement of commitment to personal and organizational goals
- Development of effective controls that measure results and lead to corrective actions

Failures of management by objectives and some recommendations

Despite all its advantages, an MBO system has a number of weaknesses. Most are due to shortcomings in applying the MBO concepts. Failure to teach the philosophy of MBO is one of the weaknesses of certain programs. Managers must explain to subordinates what it is, how it works, why it is being done, what part it will play in appraising performance, and, above all, how participants can benefit. The philosophy is built on the concepts of self-control and self-direction.

Failure to give guidelines to goal setters is often another problem. Managers must know what the corporate goals are and how their own activities fit in with them. Managers also need planning premises and a knowledge of major company policies.

There is also the difficulty of setting verifiable goals with the right degree of flexibility. Participants in MBO programs report at times that the excessive concern with economic results puts pressure on individuals that may encourage questionable behavior. To reduce the probability of resorting to unethical means to achieve results, top management must agree to reasonable objectives, clearly state behavioral expectations, and give high priority to ethical behavior, rewarding it as well as punishing unethical activities.

In addition, emphasis on short-run goals can be done at the expense of the longer-range health of the organization. Moreover, the danger of inflexibility can make managers hesitate to change objectives, even if a changed environment would require such adjustments.

Other dangers include the overuse of quantitative goals and the attempt to use numbers in areas where they are not applicable, or they may downgrade important goals that are difficult to state in terms of end results. For example, a favorable company image may be the key strength of an enterprise, yet stating this in quantitative terms is difficult. There is also the danger of forgetting that managing involves more than goal setting.

But even with the difficulties and dangers of managing by objectives in certain situations, this system emphasizes in practice the setting of goals long known to be an essential part of planning and managing.

Summary

Planning involves selecting the missions and objectives as well as the actions to achieve them. It requires decision making, which means choosing a future course of action from among alternatives. Planning and controlling are closely interrelated, although they are discussed separately in this book.

There are many types of plans, such as missions or purposes, objectives or goals, strategies, policies, procedures, rules, programs, and budgets. Once an opportunity is recognized, a manager plans rationally by establishing objectives, making assumptions (premises) about the present and future environment, finding and evaluating alternative courses of action, and choosing a course to follow. Next, the manager must make supporting plans and devise a budget. These activities must be carried out with attention to the total environment. Short-range plans must of course be coordinated with long-range plans.

Objectives are the end points toward which activities are aimed. Objectives are verifiable if it is possible, at the end of the period, to determine whether they have been accomplished. Objectives form a hierarchy, starting from corporate missions or purposes going down to individual goals. Managers can best determine the number of objectives they should realistically set for themselves by analyzing the nature of the job and how much they can do themselves and how much they can delegate. In any case, managers should know the relative importance of each of their goals.

Management by objectives (MBO) has been widely used for performance appraisal and employee motivation, but it is really a system of managing. Among its benefits, MBO results in better managing, often forces managers to clarify the structure of their organizations, encourages people to commit themselves to their goals, and helps develop effective controls.

Some of its weaknesses are that managers sometimes fail to explain the philosophy of MBO (which emphasizes self-control and self-direction) to subordinates or give them guidelines for their goal setting. In addition, goals themselves are difficult to set, tend to be short-term, and may become inflexible despite changes in the environment. People, in their search for verifiability, may overemphasize quantifiable goals.

KEY IDEAS AND CONCEPTS FOR REVIEW

Planning
Mission or purpose
Objective or goal
Strategy
Policy
Procedure
Rule
Program
Budget
Planning steps
Hierarchy of objectives
Key result areas
Quantitative and qualitative objectives
Verifiability

Evolving concepts in management by objectives (MBO)
Systems approach to MBO
Benefits of MBO
Weaknesses of MBO
Recommendations for improving MBO

FOR DISCUSSION

1. "Planning is looking ahead, and control is looking back." Comment.
2. Draw up a statement of policy and devise a brief procedure that might be useful in implementing it. Are you sure your policy is not a rule?
3. Take an organization that you know and identify its purpose or mission, even if it is not formally stated by the enterprise.
4. To what extent do you believe that managers you have known in business or elsewhere have a clear understanding of their objectives? If you think they do not, how would you suggest that they go about setting their objectives?
5. Some people object to defining long-term goals because they think that knowing what will happen over a long period is impossible. Do you believe this is an intelligent position to take? Why or why not?
6. Do you think that managing by objectives could be introduced in a government agency? A university? A college fraternity or sorority?
7. What are your five most important personal objectives? Are they long- or short-range? Are the objectives verifiable?
8. In your organization, what does your superior expect from you in terms of performance? Is it stated in writing? If you wrote down your job objective and your boss wrote down what he or she expects of you, would the two be consistent?

EXERCISE/ACTION STEPS

In this chapter, the overall objectives of a university were identified. Develop overall objectives for your university, for your college, and for the various departments in your college. Show how these objectives are interrelated to form a network.

INTERNET RESEARCH

1. Use a search engine to look for "management by objectives" and identify how MBO is used: as a planning tool? for managerial appraisal? for motivating people? in conjunction with strategic planning? for developing managers?
2. Search the Internet for the term "budget" and discuss your findings with the class.

International Case

Developing Verifiable Goals

The division manager had recently heard a lecture on management by objectives. His enthusiasm, kindled at that time, grew the more he thought about it. He finally decided to introduce the concept and see what headway he could make at his next staff meeting.

He recounted the theoretical developments in this technique, cited the advantages to the division of its application, and asked his subordinates to think about adopting it.

It was not as easy as everyone had thought. At the next meeting, several questions were raised. "Do you have division goals assigned by the president to you for next year?" the finance manager wanted to know.

"No, I do not," the division manager replied. "I have been waiting for the president's office to tell me what is expected, but they act as if they will do nothing about the matter."

"What is the division to do then?" the manager of production asked, rather hoping that no action would be indicated.

"I intend to list my expectations for the division," the division manager said. "There is not much mystery about them. I expect $30 million in sales; a profit on sales before taxes of 8 percent; a return on investment of 15 percent; an ongoing program in effect by June 30, with specific characteristics I will list later, to develop our own future managers; the completion of development work on our XZ model by the end of the year; and stabilization of employee turnover at 5 percent."

The staff were stunned that their superior had thought through to these verifiable objectives and stated them with such clarity and assurance. They were also surprised about his sincerity in wanting to achieve them.

"During the next month, I want each of you to translate these objectives into verifiable goals for your own functions. Naturally, they will be different for finance, marketing, production, engineering, and administration. However you state them, I will expect them to add up to the realization of the division goals."

Questions

1. Can a division manager develop verifiable goals, or objectives, when they have not been assigned to him or her by the president? How? What kind of information or help do you believe is important for the division manager to have from headquarters?
2. Did the division manager set the goals in the best way? What would you have done?

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Chapter -5

Strategies, Policies, and Planning Premises

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

1. Explain the nature and purpose of strategies and policies.
2. Describe the strategic planning process.
3. Understand the TOWS Matrix and the business portfolio matrix.
4. Describe some major kinds of strategies and policies and the hierarchy of strategies.
5. Identify Porter's generic strategies.
6. Discuss the nature of premises and forecasts.

Today, most business enterprises engage in strategic planning, although the degree of sophistication and formality varies considerably. Conceptually, strategic planning is deceptively simple: analyze the current and expected future situation, determine the direction of the firm, and develop means for achieving the mission. In reality, this is an extremely complex process that demands a systematic approach for identifying and analyzing factors external to the organization and matching them with the firm's capabilities.

Planning is done in an environment of uncertainty. No one can be sure if the external as well as the internal environment will be the same even next week, much less several years from now. Therefore, people make assumptions or forecasts about the anticipated environment. Some of the forecasts become assumptions for other plans. For example, the gross national product forecast becomes the assumption for sales planning, which in turn becomes the basis for production planning, and so on.

In this chapter, you will learn about the nature and purpose of strategies and policies, the strategic planning process (which identifies the critical aspects of formulating a strategy), the TOWS Matrix (a tool for systematically integrating external and internal factors), the business portfolio matrix (a tool for allocating resources), some major kinds of strategies and policies, the hierarchy of strategies, and generic strategies. Since plans are made in an environment of uncertainty, you will also learn about premising and forecasting.

The Nature and Purpose of Strategies and Policies

Strategy The determination of the mission or purpose and the basic long-term objectives of an enterprise, followed by the adoption of courses of action and allocation of resources necessary to achieve these aims.

Strategies and policies are closely related. Both give direction, both are the framework for plans, both are the basis of operational plans, and both affect all areas of managing.

The term *strategy* (which is derived from the Greek word *strategos*, meaning "general") has been used in different ways. Authors differ in at least one major aspect. Some writers focus on both the end points (mission/purpose and goals/objectives) and the means of achieving them (policies and plans). Others emphasize the means to the ends in the strategic process rather than the ends per se. As pointed out in Chapter 4, **strategy** refers

to the determination of the mission (or the fundamental purpose) and the basic long-term objectives of an enterprise, followed by the adoption of courses of action and allocation of resources necessary to achieve these aims. Therefore, objectives are part of strategy formulation.

Policies General statements or understandings that guide managers' thinking in decision making.

Policies are general statements or understandings that guide managers' thinking in decision making. They ensure that decisions fall within certain boundaries. They usually do not require action but are intended to guide managers in their commitment to the decision they ultimately make.

The essence of policy is discretion. Strategy, on the other hand, concerns the direction in which human and material resources will be applied in order to increase the chance of achieving selected objectives.



Value- and Policy-driven Samsung Strives for Global Recognition[1]

The Samsung Group is a large Korean conglomerate that focuses on electronics and financial services. In the past, many Korean companies encountered difficulties because they diversified into unrelated fields. In its new approach to management, Samsung tries to avoid the pitfalls of other companies. At the turn of the century, Samsung initiated a policy designed to make the company a leader in its field, competing against firms such as Sony of Japan.

The company is driven by its values and its philosophy, which states: "We will devote our people and technologies to create superior products and services, thereby contributing to a better global society."[2] Samsung realizes the importance of its people and the use of the latest technologies for achieving success in the marketplace. At the same time, it is aware of the responsibility to contribute to society, not only in Korea but also worldwide.

Chairman Lee Kun-Hee laid the groundwork for a new approach to management that considers defects as a crime. Quality, superior products, and excellent customer service are considered key factors for success in the very competitive environment that has been dominated by Japanese firms. With its "digital management" approach, Samsung attempts to exploit the opportunities created by the information age technologies.

Samsung's values, philosophies, and policies, as well as its goal of becoming a global leader in its field, have attracted many Korean university students. Will these young people help the company to successfully compete in the global environment?

To be effective, strategies and policies must be put into practice by means of plans, with increasing details until they get down to the nuts and bolts

of operation. The action plans through which strategies are executed are known as *tactics*. Strategies must be supported by effective tactics.

The Strategic Planning Process

Although specific steps in the formulation of a strategy may vary, the process can be built, at least conceptually, around the key elements shown in Figure 5-1 and elaborated in the following.

Inputs to the Organization

The various organizational inputs, including the goal inputs of the claimants, were discussed in Chapter 1 and need no elaboration.

Industry Analysis

As will be pointed out later in this chapter, Michael Porter suggests that the formulation of a strategy requires the evaluation of the attractiveness of an industry by analyzing the external environment. The focus should be on the kind of competition within an industry, the possibility of new firms entering the market, the availability of substitute products or services, and the bargaining positions of the suppliers as well as the buyers or customers.

Enterprise Profile

The enterprise profile is usually the starting point for determining where the company is and where it should go. Thus, top managers determine the enterprise's mission and clarify its geographic orientation, such as whether it should operate in selected regions, throughout the home country, or even in different countries. In addition, managers assess the competitive position of their firm.

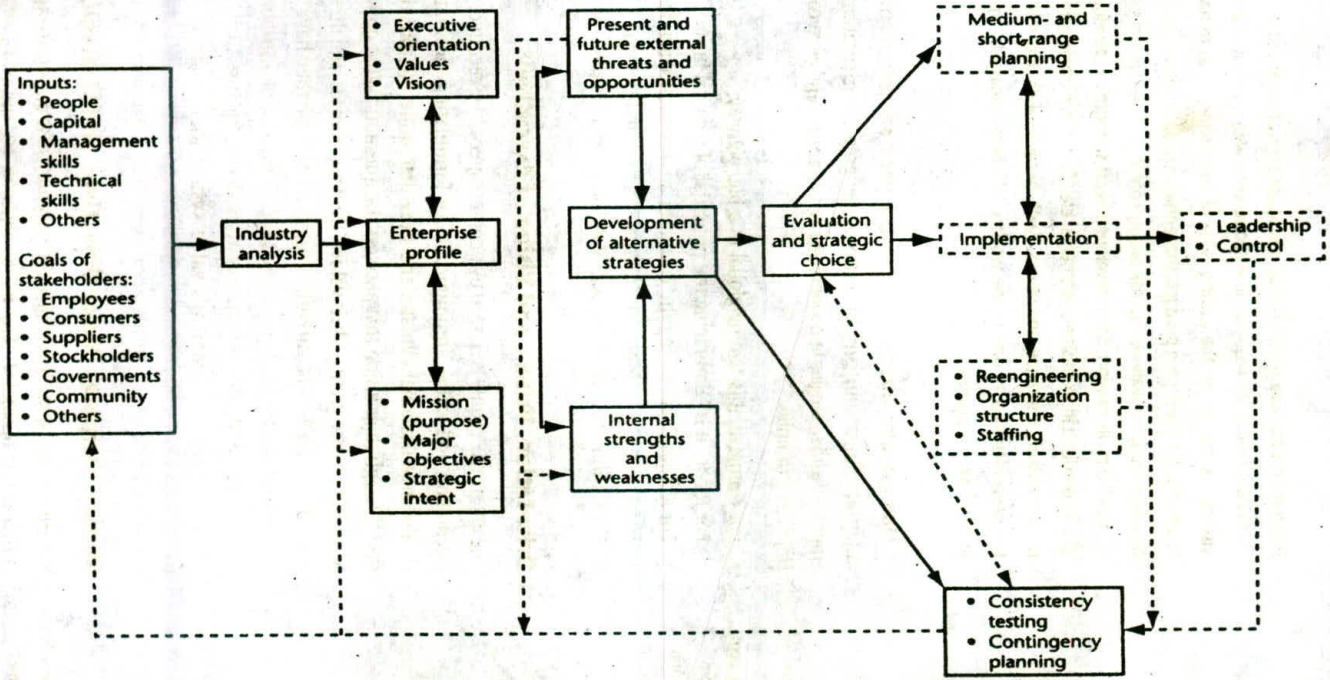
International Perspective

Sony's Mission Leads to Strengths[1]

The Japanese Sony Corporation, founded after World War II, has become a leading manufacturer of a variety of products, such as audio, video, and information technology products. It is also one of the most recognized producers of entertainment, including music, motion picture, television, and electronic games.

The company is driven by its mission, stated in the founding prospectus, which emphasizes open-mindedness and an environment with a great deal of

FIGURE 5.1 Strategic planning process model



Adapted and modified from Heinz Weihrich, "The TOWS Matrix: A Tool for Situational Analysis," *Long Range Planning*, vol. 15, no. 2 (1982), pp. 54–66.

freedom that encourages innovation and application of advanced technologies. Promoting innovation requires close cooperation with universities and research institutions that are on the cutting edge of knowledge, so as to harness that knowledge for developing products that enhance people's lives. Sony's emphasis on adaptation, innovation, and risk taking contributed to the firm's success.

Guided by its mission, Sony developed great strengths in developing high-quality products in six business segments: electronics, electronic games, music, motion picture, insurance, and others. Partly because of its clear mission, Sony has been identified as one of the world's 100 best-managed companies by *Industry Week* magazine.[4]

One can also often infer from company advertisements what is important for a company in terms of geographic orientation, product emphasis, and strategies in cooperating with partners and even competitors. Here are examples:[5]

www.komatsu.com
www.ricoh.com
www.konica.com
www.amway.com
www.canon.com

- For Komatsu, it is "Going global in a big, big way."
- For Ricoh, it is "Embracing the potential of a digital future."
- For Konica, it is "Giving the customer a voice in product design."
- For Amway, it is "Made in America, sold around the world."
- For Canon, it is "Working both with partners and competitors."

Orientation, Values, and Vision of Executives[6]

The enterprise profile is shaped by people, especially executives; and their orientation and values are important for formulating the strategy. They set the organizational climate, and they determine the direction of the firm through their vision that answers the question "What do we want to become?"[7] Consequently, their values, their preferences, and their attitudes toward risks have to be carefully examined because they have an impact on the strategy. For example, even if the alternative of distributing spirits may appear profitable, executives may decide against such a strategy because of top management's value system that condemns alcoholic beverages.

Mission (Purpose), Major Objectives, and Strategic Intent[8]

Mission A statement that answers the question "What is our business?"

The *mission*, also sometimes called the purpose, is the answer to the question "What is our business?" The major *objectives* are the end points toward which the activities of the enterprise are directed. These topics were discussed in the previous chapter.

Strategic intent The commitment to win in the competitive environment.

Strategic intent is the commitment to win in the competitive environment. Professors Gary Hamel and C. K. Prahalad analyzed companies that had achieved global leadership.[9] They found that those firms had an obsession with winning, not only at the top level but also throughout the organization. This obsession is called strategic intent and is illustrated by Komatsu's intent to "encircle Caterpillar," its main rival, or Canon's idea to "beat Xerox," or Honda's intent to become an automotive pioneer, "a second Ford." The authors point out that strategic intent requires personal effort and commitment. The intent statement is stable over time and focuses on the essence of winning.

www.caterpillar.com
www.xerox.com
www.honda.com
www.ford.com

Present and Future External Environment

The present and future external environment must be assessed in terms of threats and opportunities. The evaluation focuses on the competitive situation as well as on economic, social, political, legal, demographic, and geographic factors. In addition, the environment is scanned for technological developments, for products and services on the market, and for other pertinent factors in determining the competitive situation of the enterprise.

Internal Environment[10]

Similarly, the firm's internal environment should be audited and evaluated with respect to its resources and its weaknesses and strengths in research and development, production, operation, procurement, marketing, products, and services. Other internal factors that are important for formulating a strategy should be assessed, including human and financial resources, as well as the company image, organization structure and climate, planning and control system, and relations with customers.

Development of Alternative Strategies

Strategic alternatives are developed on the basis of an analysis of the external and internal environments. An organization may pursue many different kinds of strategies.[11] It may *specialize* or *concentrate*, as the Korean Hyundai did by producing lower-priced cars (in contrast to General Motors, for example, which has a complete product line ranging from inexpensive to luxury cars). Under the leadership of its chief executive, Chung Mong Koo, the company introduced the competitively priced sport utility vehicle Santa Fe, which was well received by the market.[12]

www.hyundai.com
www.gm.com

www.kmart.com
www.bordersgroupinc.com (Walden)
www.paylessdrug.com
www.toyota.com
www.nummi.com

Alternatively, a firm may *diversify*, extending the operation into new and profitable markets. Kmart Corporation formed a Specialty Retailing Group that included stores such as Walden Book Company, Builders Square, Designer Depot, and PayLess Drug Stores. Still another strategy is *international expansion* to other countries, as described in Chapter 3. Other examples of possible strategies are *joint ventures* and *strategic alliances*, which may be appropriate for some firms.[13] They are especially suitable for big undertakings in which firms have to pool their resources, as illustrated by the joint venture of General Motors and Toyota to produce small cars in California.[14]

Under certain circumstances, a company may have to adopt a *liquidation* strategy by terminating an unprofitable product line or even dissolving the firm, as illustrated by the Savings and Loan Associations, or declare bankruptcy, as exemplified by the energy company Enron. But in some cases, liquidation may not be necessary, but a *retrenchment* strategy may be sufficient. In such a situation, the company may curtail its operation temporarily.

These are just a few examples of possible strategies. In practice, companies, especially large ones, pursue a combination of strategies.

Evaluation and Choice of Strategies[15]

The various strategies have to be carefully evaluated before the choice is made. Strategic choices must be considered in light of the risks involved in a particular decision. Some profitable opportunities may not be pursued because failure in a risky venture could result in bankruptcy of the firm. Another critical element in choosing a strategy is timing. Even the best product may fail if it is introduced to the market at an inappropriate time. Moreover, the reaction of competitors must be taken into consideration. When IBM reduced the price of its personal computer in reaction to the success of Apple's Macintosh computer, firms producing IBM-compatible computers had little choice but to reduce their prices as well. This illustrates the interconnection of the strategies of firms in the same industry.

Medium- and Short-Range Planning, Implementation through Reengineering, Staffing, Leadership, and Control

Although not a part of the strategic planning process (and therefore shown by broken lines in Figure 5-1), medium- and short-range planning as well as implementation of the plans must be considered during all phases of

the process. Implementation of the strategy often requires reengineering the organization, staffing, and providing leadership. Controls must also be installed for monitoring performance against plans. The importance of feedback is shown by the loops in the model. These aspects of strategy implementation are discussed later in the book.

Consistency Testing and Contingency Planning

The last key aspect of the strategic planning process is testing for consistency and preparing for contingencies. During all phases of the strategic planning process, consistency testing is essential. Since the future cannot be predicted with a high degree of certainty, contingency plans need to be prepared. For example, a strategy may be prepared with the assumption that the gross national product may increase 3 percent annually over the next three years. A contingency plan may also be made in which the scenario includes a major recession.

The TOWS Matrix: A Modern Tool for Analysis of the Situation

Today, strategy designers are aided by a number of matrices that show the relationships of critical variables, such as the Boston Consulting Group's business portfolio matrix, which will be discussed later. For many years, the SWOT analysis has been used to identify a company's strengths, weaknesses, opportunities, and threats. However, this kind of analysis is static and seldom leads to the development of distinct alternative strategies based on it. Therefore, the TOWS Matrix has been introduced for analyzing the competitive situation of the company or even of a nation that leads to the development of four distinct sets of strategic alternatives.[16]

The TOWS Matrix has a wider scope and a different emphasis from the business portfolio matrix. The former does not replace the latter. The TOWS Matrix is a conceptual framework for a systematic analysis that facilitates matching of the external threats and opportunities with the internal weaknesses and strengths of the organization.

It is common to suggest that companies should identify their strengths and weaknesses, as well as the opportunities and threats in the external environment, but what is often overlooked is that combining these factors may require distinct strategic choices. To systematize these choices, the TOWS Matrix has been proposed, where *T* stands for threats, *O* for opportunities, *W* for weaknesses, and *S* for strengths. The TOWS model

starts with the threats (*T* in TOWS) because in many situations a company undertakes strategic planning as a result of a perceived crisis, problem, or threat.

Four Alternative Strategies

Figure 5-2 presents the four alternative strategies of the TOWS Matrix. The strategies are based on the analysis of the external environment (threats and opportunities) and the internal environment (weaknesses and strengths):

1. The *WT strategy* aims to minimize both weaknesses and threats and may be called the Mini–Mini (for "minimize–minimize") strategy. It may require that the company, for example, form a joint venture, retrench, or even liquidate.
2. The *WO strategy* attempts to minimize the weaknesses and maximize the opportunities. Thus, a firm with weaknesses in some areas may either develop those areas within the enterprise or acquire the needed competencies (such as technology or persons with needed skills) from outside in order to enable it to take advantage of opportunities in the external environment.

FIGURE 5-2 TOWS Matrix for strategy formulation

Internal factors / **External factors**	**Internal strengths (S)** e.g., strengths in management, operations, finance, marketing, research and development, engineering	**Internal weaknesses (W)** e.g., weaknesses in areas shown in the "strengths" box
External opportunities (O) (consider risks also) e.g., current and future economic conditions; political and social changes; new products, services, and technology	**SO strategy: Maxi–Maxi** potentially the most successful strategy, utilizing the organization's strengths to take advantage of opportunities	**WO strategy: Mini–Maxi** e.g., development strategy to overcome weaknesses in order to take advantage of opportunities
External threats (T) e.g., energy shortage, competition, and areas similar to those shown in the "opportunities" box above	**ST strategy: Maxi–Mini** use of strengths to cope with threats or to avoid threats	**WT strategy: Mini–Mini** e.g., retrenchment, liquidation,or joint venture to minimize both weaknesses and threats

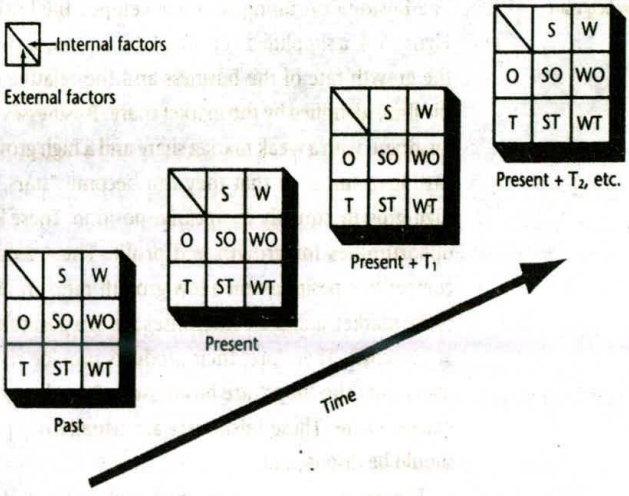
* Although the emphasis is on strategies in this discussion, similar analyses can be made for developing more detailed tactics or action plans.

3. The *ST strategy* is based on using the organization's strengths to deal with threats in the environment. The aim is to maximize the former while minimizing the latter. Thus, a company may use its technological, financial, managerial, or marketing strengths to cope with the threats of a new product introduced by its competitor.
4. The *SO strategy*, which capitalizes on a company's strengths to take advantage of opportunities, is the most desirable. Indeed, it is the aim of enterprises to move from other positions in the matrix to this one. If they have weaknesses, they will strive to overcome them, making them strengths. If they face threats, they will cope with them so that they can focus on opportunities.

Time Dimension and the TOWS Matrix

So far, the factors displayed in the TOWS Matrix pertain to analysis at a particular point in time. However, external and internal environments are dynamic: some factors change over time, while others change very little. Hence, strategy designers must prepare several matrices at different points in time, as shown in Figure 5-3. Thus, one may start with a TOWS analysis of the past, continue with an analysis of the present, and, perhaps most important, focus on different time periods (T1, T2, etc.) in the future.

FIGURE 5-3 Dynamics of the TOWS Matrix



Application of the TOWS Merger Matrix for Mergers, Acquisitions, Joint Ventures, and Alliances

Companies around the world now use the TOWS Matrix; the matrix has also been included in several modern textbooks on strategic management.[17] Recently, the TOWS Matrix concept has been introduced for planning mergers, acquisitions, joint ventures, and alliances.[18] Whenever two partners consider joint activities, it is prudent to analyze the strengths and weaknesses for each partner as well as their opportunities and threats. Moreover, their alternative strategies *before* their association should be considered: these two TOWS Matrices provide a better understanding of the prospective partners before the actual linkage. For example, complementary strengths and weaknesses could result in a competitive advantage for both companies. On the other hand, repetition and overlap may result in duplication of efforts. After the two matrices are evaluated, a third matrix should be developed for the partnership. This is especially important for acquisitions and mergers because of the relative permanency of the resulting entity. Preparing the three TOWS Matrices can also allow potential problems to be identified in more loosely coupled partnerships such as a strategic alliance. The TOWS Merger Matrix will be illustrated by the Daimler–Chrysler merger in the closing section of Part 2.

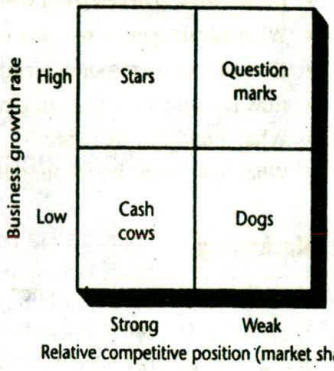
The Portfolio Matrix: A Tool for Allocating Resources

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The Boston Consulting Group developed the business portfolio matrix.[19] Figure 5-4, a simplified version of the matrix, shows the linkages between the growth rate of the business and the relative competitive position of the firm, identified by the market share. Businesses in the "question marks" quadrant, with a weak market share and a high growth rate, usually require cash investment so that they can become "stars," the businesses in the high-growth, strongly competitive position. These kinds of businesses have opportunities for growth and profit. The "cash cows," with a strong competitive position and a low growth rate, are usually well established in the market, and such enterprises are in a position to make their products at low costs. Therefore, their products provide the cash needed for their operation. The "dogs" are businesses with a low growth rate and a weak market share. These businesses are usually not profitable and generally should be disposed of.

The portfolio matrix was developed for large corporations with several divisions that are often organized around strategic business units (a topic to be discussed in Chapter 8). While portfolio analysis was popular in the

FIGURE 5.1 Business portfolio matrix



Adapted from *The Product Portfolio Matrix*, copyright © 1970, the Boston Consulting Group, Inc.

1970s, it is not without its critics, who contend that it is too simplistic. Also, the growth rate criterion has been considered insufficient for the evaluation of an industry's attractiveness. Similarly, the market share as a yardstick for estimating the competitive position may be inadequate.

Major Kinds of Strategies and Policies

For a business enterprise (and, with some modification, for other kinds of organizations as well), the major strategies and policies that give an overall direction to operation are likely to be in the areas of growth, finance, organization, personnel, public relations, products or services, and marketing. We will elaborate on the last two areas.

Products or Services

A business exists to furnish products or services. In a very real sense, profits are merely a measure—although an important one—of how well a company serves its customers. New products or services, more than any other single factor, determine what an enterprise is or will be.

The key questions in this area can be summarized as follows:

- What is our business?
- Who are our customers?
- What do our customers want?
- How much will our customers buy and at what price?
- Do we wish to be a product leader?

- What is our competitive advantage?
- Do we wish to develop our own new products?
- What advantages do we have in serving customer needs?
- How should we respond to existing and potential competition?
- How far can we go in serving customer needs?
- What profits can we expect?
- What basic form should our strategy take?

Marketing

Marketing strategies are designed to guide managers in getting products or services to customers and in encouraging customers to buy. Marketing strategies are closely related to product strategies; they must be interrelated and mutually supportive. As a matter of fact, Peter Drucker regards the two basic business functions as innovation (e.g., the creation of new goods or services) and marketing. A business can scarcely survive without at least one of these functions and preferably both.

The key questions that serve as guides for establishing a marketing strategy are these:

- Where are our customers, and why do they buy?
- How do our customers buy?
- How is it best for us to sell?
- Do we have something to offer that competitors do not?
- Do we wish to take legal steps to discourage competition?
- Do we need, and can we supply, supporting services?
- What are the best pricing strategy and policy for our operation?
- How can we best serve our customers?

Hierarchy of Company Strategies

In large, diversified companies, the overall strategy may take the form of a hierarchy. At the top of the pyramid is the *corporate-level strategy*. At this level, executives craft the overall strategy for a diversified company. Decisions are made as to the industries in which the company wants to compete. A portfolio of businesses is often selected to achieve synergies among the business units.

The second level in the hierarchy is *business strategies*, which are usually developed by the general manager of a business unit. These strategies are reviewed and approved or rejected by the chief executive. The aim of the business strategy is to gain a competitive advantage in a particular area of

On the third hierarchical level, *functional strategies* (or policies) are developed. These strategies are devised for departments or other organizational units, such as finance, production, marketing, service, and personnel. The aim is to support the business and corporate strategies.

Porter's Industry Analysis and Generic Competitive Strategies[20]

Professor Michael Porter suggests that strategy formulation requires an analysis of the attractiveness of an industry and the company's position within that industry. This analysis becomes the basis for formulating generic strategies.

Industry Analysis[21]

In the analysis of the industry, Porter identified five forces: (1) the competition among companies, (2) the threat of new companies entering the market, (3) the possibility of using substitute products or services, (4) the bargaining power of suppliers, and (5) the bargaining power of buyers or customers. On the basis of the industry analysis, a company may adopt generic strategies. These strategies are generic because they may be suitable on a broad level for different kinds of organizations. Any enterprise, however, may use more than one strategy.

Overall Cost Leadership Strategy

This strategic approach aims at reduction in costs, based to a great extent on experience. Thus, the emphasis may be on keeping a close watch on costs in areas such as research and development, operation, sales, and service. The objective is for a company to have a low-cost structure compared with its competitors. This strategy often requires a large relative market share and cost-efficient operation, as illustrated by the low-cost Ivory soap sold in a broad market.

Differentiation Strategy

A company following a differentiation strategy attempts to offer something unique in the industry in terms of products or services. Porsche sports cars are indeed special; so is the Caterpillar Company, which is known for its prompt service and availability of spare parts. In the broad consumer market, Dial soap is differentiated from other brands of soap by its use of deodorants.

Focused Strategy

A company adopting a focused strategy concentrates on special groups of customers, a particular product line, a specific geographic region, or other aspects that become the focal point of the firm's efforts. Rather than serving the entire market with its products or services, an enterprise may emphasize a specific segment of the market. A low-cost strategy, differentiation, or both may accomplish this. Porter illustrates the *focused low-cost strategy* with the example of La Quinta Inns, a motel chain that operates in a certain region of the United States and appeals to traveling business representatives, such as salespeople. The *focused differentiation strategy* may be exemplified by Cray Research Inc., which specializes in very powerful and sophisticated supercomputers. The differentiation allows the company to charge premium prices.

In general, a company needs to choose a generic strategy and should not "get stuck in the middle," according to Porter. A company that gets stuck in the middle needs to decide on a low-cost strategy in a broad or narrow market or offer a differentiated (i.e., unique) product or service in a broad or narrow market.

Premising and Forecasting

Planning premises The anticipated environment in which plans are expected to operate.

One of the essential and often overlooked steps in effective and coordinated planning is premising, which is the establishment of and the agreement by managers and planners to utilize consistent assumptions critical to plans under consideration. **Planning premises** are defined as the anticipated environment in which plans are expected to operate. They include assumptions or forecasts of the future and known conditions that will affect the operation of plans.[22] Examples are prevailing policies and existing company plans that control the basic nature of supporting plans.

A distinction should be drawn between forecasts that are planning premises and forecasts that are translated into future expectancies, usually in financial terms, from actual plans developed. For example, a forecast to determine future business conditions, sales volume, or political environment furnishes premises on which to develop plans. However, a forecast of the costs or revenues from a new capital investment translates a planning program into future expectations. In the first case, the forecast is a prerequisite of planning; in the second case, the forecast is a result of planning.

At the same time, plans themselves and forecasts of their future effects often become premises for other plans. The decision by an electricity

company to construct a nuclear generating plant, for example, creates conditions that give rise to premises for transmission line plans and other plans necessarily dependent on the generating plant being built.

Environmental Forecasting

If the future could be forecast with accuracy, planning would be relatively simple. Managers would need only to take into account their human and material resources and their opportunities and threats, compute the optimum method of reaching their objective, and proceed with a relatively high degree of certainty toward it. In practice, forecasting is much more complicated.

Values and areas of forecasting

Forecasting has values aside from its use. First, the making of forecasts and their review by managers compel thinking ahead, looking to the future, and providing for it. Second, preparation of the forecast may disclose areas where necessary control is lacking. Third, forecasting, especially when there is participation throughout the organization, helps unify and coordinate plans. By focusing attention on the future, it assists in bringing a singleness of purpose to planning.

The environmental areas that are frequently chosen for making forecasts include the economic, social, political/legal, and technological environments.

Forecasting with the Delphi technique

www.rand.org

One of the attempts to make technological forecasting more accurate and meaningful is the Delphi technique. This technique, developed by Olaf Helmer and his colleagues at the RAND Corporation, has a degree of scientific respectability and acceptance. A typical process of the Delphi technique is as follows:

1. A panel of experts on a particular problem area is selected, usually from both inside and outside the organization.
2. The experts are asked to make (anonymously, so that they will not be influenced by others) a forecast as to what they think will happen, and when, in various areas of new discoveries or developments.
3. The answers are compiled, and the composite results are fed back to the panel members.
4. With this information at hand (but still with individual anonymity), further estimates of the future are made.

5. This process may be repeated several times.
6. When a convergence of opinion begins to evolve, the results are then used as an acceptable forecast.

Note that the purpose of the successive opinions and feedback is not to force the experts to compromise but rather, by bringing additional informational inputs to bear, to make opinions more informed. It is thus hoped, and experience has verified this hope, that an informed consensus among experts will be arrived at.

Summary

There are different definitions of strategy. A comprehensive one refers to the determination of the firm's mission or purpose and its basic long-term objectives, followed by the adoption of courses of action and allocation of resources necessary to achieve these aims. Policies are general statements or understandings that guide managers' thinking in decision making. Both strategies and policies give direction to plans. They provide the framework for plans and serve as a basis for the development of tactics and other managerial activities.

The strategic planning model shows how the process works. It identifies the critical elements of this process and indicates how they relate to each other. The TOWS Matrix is a modern tool for analyzing the threats and opportunities in the external environment and their relationships to the organization's internal weaknesses and strengths. Three TOWS Matrices have to be developed for mergers, acquisitions, joint ventures, and alliances. The portfolio matrix is a tool for allocating resources, linking the business growth rate with the relative competitive position (measured by market share) of the firm.

Major kinds of strategies and policies need to be developed in areas such as growth, finance, organization, personnel, public relations, products or services, and marketing. Strategies form a hierarchy from the corporate level to the business level and the functional level. Porter identified three generic competitive strategies related to overall cost leadership, differentiation, and focus.

Planning premises are the anticipated environment. They include assumptions or forecasts of the future and known conditions. More recently, environmental forecasting has become important. One approach to forecasting is the Delphi technique developed by the RAND Corporation.

KEY IDEAS AND CONCEPTS FOR REVIEW

Strategy
Policy
Tactic
Key elements in the strategic planning process
TOWS Matrix by Weihrich
TOWS Merger Matrix
Portfolio matrix by the Boston Consulting Group
Major kinds of strategies
Hierarchy of strategies
Porter's generic strategies
Planning premises
Environmental forecasting
Delphi technique

FOR DISCUSSION

1. How can you distinguish between strategies and policies?
2. Are strategies and policies as important in a nonbusiness enterprise (such as a labor union, a government department, a hospital, or a city fire department) as they are in a business? Why and how?
3. Why are contingency plans important?
4. Choose an organization that you know and identify its strengths and weaknesses. What are its special opportunities and threats in the external environment?
5. How would you make an organizational appraisal of your college or university? What kind of "business" is the school in?
6. How can strategies be implemented effectively?
7. Identify major premises that, in your judgment, Honda Motor Company would need in order to forecast its sales of automobiles for the next two years.

EXERCISES/ACTION STEPS

1. Read two articles that deal with strategy in magazines such as *Fortune* or *Business Week*. List the strengths and weaknesses of a company reported as well as the opportunities and threats faced by the firm.
2. Take a major decision problem facing you and outline the more critical planning premises surrounding it. How many of these are matters of knowledge and how many are matters of forecast? How many are qualitative and how many are quantitative? How many are within your control?

INTERNET RESEARCH

1. The TOWS Matrix has been used for developing alternative strategies for organizations, for analyzing the competitive advantages of nations, as well as for developing a career strategy. Search the Internet for the "TOWS Matrix" and identify the application of the matrix.

2. Search the Internet for the term "strategic intent" and compare the intents of four organizations.
3. Search the Internet for "competing for the future" and find reviews of the book by that name by Hamel and Prahalad.

International

Case The Road Ahead for Shanghai Volkswagen[23]

Shanghai Volkswagen is a joint venture between the German Volkswagen AG and a consortium of Chinese partners. The 25-year agreement signed by the partners in the middle of 1980s provided for 50 percent Volkswagen AG equity in the venture. By 2001, this cooperation was the most successful automobile venture in China. Attempts by the U.S. AMC Jeep Corporation and other car makers failed. While other companies were attracted by the potential of swift, huge returns because of the large Chinese population of 1.2 billion people (certainly only a very small percentage would be customers), Volkswagen built the venture gradually over the years. By 2001, it had achieved a market share of over 50 percent as a result of introducing "hot" models and assuring reliable service. But a great deal of effort was necessary to build up this market.

The early years were not without difficulties. For example, Volkswagen had to develop suppliers for quality components, train the work force, work under constraints imposed by the host government, and share its latest engine technology. The Santana model, which proved successful in Brazil, was the primary vehicle that suited the Chinese market. By 1995, the improved Santana 2000 was introduced. The ultimate aim of the Chinese partners, however, is to design and eventually develop cars by themselves. The factory, not far away from Shanghai, has one of the most modern engine plants. Chinese engineers and managers were sent to the factory in Wolfsburg, Germany, for training. Moreover, Chinese managers and technicians attended German universities to gain engineering expertise. One of the major difficulties was the lack of suppliers of quality components. Therefore, Volkswagen introduced an incentive system that paid its suppliers handsomely for quality car parts. At the same time, the company worked hard to build relationships not only with the suppliers but also with the community. The Chinese government, on the other hand, provided tax incentives and protected the car market for Volkswagen during the early years. For example, from 1993 to 1996, it did not permit other car makers to set up joint ventures for passenger car assembly.

The combination of hot models and reliable service resulted in an 8 percent sales increase in 2000 and expected sales of more than 14 percent in 2001. Besides the popular Santana model, Volkswagen also produces Jettas, Passats, and Polos, which should result in the production of more than 400,000 cars in 2001. But the competition is not sleeping, with Ford introducing a budget car and Toyota a compact car. With 90 percent of the parts produced in China, Volkswagen

was able to keep the price lower than its competitors could. Still, the Passat at $29,000 is expensive for a person earning $1,200 a month. In comparison, the midsize Buick by General Motors costs $44,000, partly because only 60 percent of the parts are locally made. With China's entrance to the World Trade Organization in 2001, competition is likely to increase, putting pressure on prices. Volkswagen could counteract by bringing the low-priced Czech Skoda (which is wholly owned by Volkswagen) to China. Although successful in the past, Volkswagen cannot rest on its laurels but must prepare for the future global competition.

Questions

1. Why was Volkswagen so successful in China while other companies failed?
2. What would you recommend to Shanghai Volkswagen to remain successful in the future?
3. Was it wise of Volkswagen AG in Germany to share its latest engine technology with the Chinese?

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Chapter -6

Decision Making

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

1. Analyze decision making as a rational process.
2. Develop alternative courses of action with consideration of the limiting factor.
3. Evaluate alternatives and select a course of action from among them.
4. Differentiate between programmed and nonprogrammed decisions.
5. Understand the differences between decisions made under conditions of certainty, uncertainty, and risk.
6. Recognize the importance of creativity and innovation in managing.

Decision making The selection of a course of action from among alternatives.

Decision making is defined as the selection of a course of action from among alternatives; it is at the core of planning. A plan cannot be said to exist unless a decision—a commitment of resources, direction, or reputation—has been made. Until that point, there are only planning studies and analyses. Managers sometimes see decision making as their central job because they must constantly choose what is to be done, who is to do it, and when, where, and occasionally even how it will be done. Decision making is, however, only a step in planning. Even when it is done quickly and with little thought or when it influences action for only a few minutes, it is part of planning. It is also part of everyone's daily life. A course of action can seldom be judged alone because virtually every decision must be geared to other plans.

The Importance and Limitations of Rational Decision Making

In the discussion of the steps in planning in Chapter 4, decision making was considered a major part of planning. As a matter of fact, given an awareness of an opportunity and a goal, the decision-making process is really the core of planning. Thus, in this context, the process leading to making a decision might be thought of as (1) premising, (2) identifying alternatives, (3) evaluating alternatives in terms of the goal sought, and (4) choosing an alternative, that is, making a decision.

Although this chapter emphasizes the logic and techniques of choosing a course of action, the discussion will show that decision making is really one of the steps in planning.

Rationality in Decision Making

It is frequently said that effective decision making must be rational. But what is rationality? When is a person thinking or deciding rationally?

People acting or deciding rationally are attempting to reach some goal that cannot be attained without action. They must have a clear understanding of alternative courses by which a goal can be reached under existing circumstances and limitations. They also must have the information and the ability to analyze and evaluate alternatives in light of the goal

sought. Finally, they must have a desire to come to the best solution by selecting the alternative that most effectively satisfies goal achievement.

People seldom achieve complete rationality, particularly in managing.[1] In the first place, since no one can make decisions affecting the past, decisions must operate for the future, and the future almost invariably involves uncertainties. In the second place, it is difficult to recognize all the alternatives that might be followed to reach a goal; this is particularly true when decision making involves doing something that has not been done before. Moreover, in most instances, not all alternatives can be analyzed, even with the newest analytical techniques and computers available.

Limited, or "Bounded," Rationality

A manager must settle for limited or "bounded," rationality. In other words, limitations of information, time, and certainty limit rationality, even if a manager tries earnestly to be completely rational. Since managers cannot be completely rational in practice, they sometimes allow their dislike of risk—their desire to "play it safe"—to interfere with the desire to reach the best solution under the circumstances. Herbert Simon[2] called this **satisficing**, that is, picking a course of action that is satisfactory or good enough under the circumstances. Although many managerial decisions are made with a desire to "get by" as safely as possible, most managers do attempt to make the best decisions they can within the limits of rationality and in light of the degree and nature of the risks involved.

Satisficing Picking a course of action that is satisfactory or good enough under the circumstances.

We will now consider the steps of the decision-making process in detail.

Development of Alternatives and the Limiting Factor

Assuming that we know what our goals are and agree on clear planning premises, the first step of decision making is to develop alternatives. There are almost always alternatives to any course of action; indeed, if there seems to be only one way of doing a thing, that way is probably wrong. If we can think of only one course of action, clearly we have not thought hard enough.

The ability to develop alternatives is often as important as being able to select correctly from among them. On the other hand, ingenuity, research, and common sense will often unearth so many choices that none of them can be adequately evaluated. The manager needs help in this situation, and this help, as well as assistance in choosing the best alternative, is found in the concept of the limiting or strategic factor.

Principle of the limiting factor By recognizing and overcoming factors that stand critically in the way of a goal, the best alternative course of action can be selected.

A **limiting factor** is something that stands in the way of accomplishing a desired objective. Recognizing the limiting factors in a given situation makes it possible to narrow the search for alternatives to those that will overcome the limiting factors. The **principle of the limiting factor** states that, by recognizing and overcoming those factors that stand critically in the way of a goal, the best alternative course of action can be selected.

International Perspective

www.graniterock.com

The Decision to Speed up the Decision-making Process at Granite Rock Co.[3]

The Granite Rock Company is a Watsonville, California, company that produces rocks, sand, gravel aggregates, and a variety of other products. The company was the 1992 winner of the much-coveted Malcolm Baldrige award, which recognizes outstanding performance in quality improvement.

Established in 1900, the company's focus was on the "bottom line." Employees knew it, and so did customers, who also felt that it was an inflexible, centralized, bureaucratic firm. Bruce Woolpert, the company's president and chief executive, recognized that it took too long to make decisions. Indeed, it was felt that bureaucracy was killing the company. That started to change with the 1986 decision to turn the organization chart upside down. Traditional organization charts show the president at the top and the customer contact people at the bottom. The change put the customers in charge and on top. Three things turned the company around. First, all its employees discussed the current operation, and it was decided that special requests from customers would be granted, with the exception of illegal or immoral requests. Second, through surveys, customers were asked to rate the company from grade A to F together with written comments. Third, the company empowered customers to decide whether the company earned its pay. Specifically, the invoices stated: "If you're not satisfied with the Granite Rock service or construction services you just received, then don't pay us for it." Because of it, the company became very much aware of what was wrong and consequently could make improvements. Many other companies go out of business without knowing the reason because most customers do not complain. At Granite Rock, the key 1986 decision of empowering the customer set the stage for the prestigious 1992 Malcolm Baldrige National Quality Award.

Evaluation of Alternatives

Once appropriate alternatives have been found, the next step in planning is to evaluate them and select the one that will best contribute to the goal.

This is the point of ultimate decision making, although decisions must also be made in the other steps of planning—in selecting goals, in choosing critical premises, and even in selecting alternatives.

Quantitative and Qualitative Factors

Quantitative factors Factors that can be measured in numerical terms.

In comparing alternative plans for achieving an objective, people are likely to think exclusively of **quantitative factors**. These are factors that can be measured in numerical terms, such as time or various fixed and operating costs. No one would question the importance of this type of analysis, but the success of the venture would be endangered if intangible, or qualitative, factors were ignored. **Qualitative, or intangible, factors** are factors that are difficult to measure numerically, such as the quality of labor relations, the risk of technological change, or the international political climate. There are all too many instances in which an excellent quantitative plan was destroyed by an unforeseen war, a fine marketing plan made inoperable by a long transportation strike, or a rational borrowing plan hampered by an economic recession. These illustrations point out the importance of giving attention to both quantitative and qualitative factors when comparing alternatives.

Qualitative, or intangible, factors Factors that are difficult to measure numerically.

To evaluate and compare the intangible factors in a planning problem and make decisions, managers must first recognize these factors and then determine whether a reasonable quantitative measurement can be given to them. If not, they should find out as much as possible about the factors, perhaps rate them in terms of their importance, compare their probable influence on the outcome with that of the quantitative factors, and then come to a decision. This decision may give predominant weight to a single intangible.

Marginal Analysis

Marginal analysis Comparing the additional revenue and the additional cost arising from increasing output.

Evaluating alternatives may involve utilizing the technique of **marginal analysis** to compare the additional revenue and the additional cost arising from increasing output. Where the objective is to maximize profit, this goal will be reached, as elementary economics teaches, when the additional revenue and additional cost are equal. In other words, if the additional revenue of a larger quantity is greater than its additional cost, more profit can be made by producing more. However, if the additional revenue of the larger quantity is less than its additional cost, a larger profit can be made by producing less.

Marginal analysis can be used in comparing factors other than cost and revenue. For example, to find the best output of a machine, input could be varied against output until the additional input equals the additional output. This would then be the point of maximum efficiency of the machine. Or the number of subordinates reporting to a manager might conceivably be increased to the point at which additional cost savings, better communication and morale, and other factors equal additional losses in the effectiveness of control, leadership, and similar factors.

Cost-Effectiveness Analysis

Cost-effectiveness analysis seeks the best ratio of benefit and cost.

An improvement on, or variation of, traditional marginal analysis is cost-effectiveness, or cost–benefit, analysis. **Cost-effectiveness analysis** seeks the best ratio of benefit and cost; this means, for example, finding the least costly way of reaching an objective or getting the greatest value for a given expenditure.

International Perspective

Cost–Benefit Analysis in Managing Risks to Health, Safety, and the Environment[1]

www.house.gov

The U.S. Congress, like businesses, faces the decision of allocating resources. What are the government's priorities? Increased airport security? Pesticide residue regulation? Protecting the public from nuclear power plant radiation? Managing health risks from smoking? Some suggest using cost–benefit analysis for ranking the risks to health, safety, and the environment. But politics and the question of values also enter decisions. Too often, decisions are made by public officials without the participation of the stakeholders affected by the regulation. But this does not need to be so.

In Florida, a decision had to be made on where to locate a needed coal-fired power plant. Through public participation, criteria for an ideal site were identified. During the discussion between the power company and a committee consisting of community leaders, a site away from the populated area was identified, a site the company had not even considered.

In the San Francisco Bay area, a citizen task force developed a long-term plan for dealing with solid waste disposal, air pollution, and water pollution and to ensure adequate water supply. The task force collected data from experts and citizens and developed a plan that resulted in what is considered now—after more than 18 years—one of the best-managed environmental areas in the country.

Selecting an Alternative: Three Approaches

When selecting from among alternatives, managers can use three basic approaches: (1) experience, (2) experimentation, and (3) research and analysis (Figure 6-1).

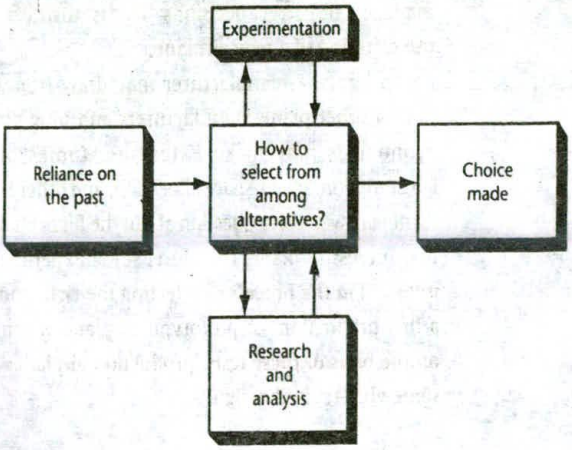
Experience

Reliance on past experience probably plays a larger part than it deserves in decision making. Experienced managers usually believe, often without realizing it, that the things they have successfully accomplished and the mistakes they have made furnish almost infallible guides to the future. This attitude is likely to be more pronounced the more experience a manager has had and the higher he or she has risen in an organization.

To some extent, experience is the best teacher. The very fact that managers have reached their position appears to justify their past decisions. Moreover, the process of thinking problems through, making decisions, and seeing programs succeed or fail does make for a degree of good judgment (at times bordering on intuition). Many people, however, do not learn from their errors, and there are managers who seem never to gain the seasoned judgment required by the modern enterprise.

Relying on past experience as a guide for future action can be dangerous. In the first place, most people do not recognize the underlying reasons for their mistakes or failures. In the second place, the lessons of experience may be entirely inapplicable to new problems. Good decisions must be evaluated against future events, while experience belongs to the past.

FIGURE 6-1 Bases for selecting from among alternative courses of action



On the other hand, if a person carefully analyzes experience, rather than blindly following it, and if he or she distills from experience the fundamental reasons for success or failure, then experience can be useful as a basis for decision analysis. A successful program, a well-managed company, a profitable product promotion, or any other decision that turns out well may furnish useful data for such distillation. Just as scientists do not hesitate to build upon the research of others and would be foolish indeed merely to duplicate it, managers can learn much from others.

Experimentation

An obvious way to decide among alternatives is to try one of them and see what happens. Experimentation is often used in scientific inquiry. People often argue that it should be employed more often in managing and that the only way a manager can make sure some plans are right—especially in view of the intangible factors—is to try the various alternatives and see which is best.

The experimental technique is likely to be the most expensive of all techniques, especially if a program requires heavy expenditures of capital and personnel and if the firm cannot afford to vigorously attempt several alternatives. Besides, after an experiment has been tried, there may still be doubt about what it proved, since the future may not duplicate the present. This technique, therefore, should be used only after considering other alternatives.

On the other hand, there are many decisions that cannot be made until the best course of action can be ascertained by experiment. Even reflections on experience or the most careful research may not assure managers of correct decisions. This is nowhere better illustrated than in the planning of a new airplane.

An airplane manufacturer may draw from personal experience and that of other plane manufacturers and new plane users. Engineers and economists may make extensive studies of stress, vibration, fuel consumption, speed, space allocation, and other factors. But all these studies do not answer every question about the flight characteristics and economics of a successful plane; therefore, some experimentation is almost always involved in the process of selecting the right course to follow. Ordinarily, a first-production, or prototype, airplane is constructed and tested; and on the basis of these tests, production airplanes are made according to a somewhat revised design.

Experimentation is used in other ways. A firm may test a new product in a certain market before expanding its sale nationwide. Organizational techniques are often tried in a branch office or plant before being applied over an entire company. A candidate for a management job may be tested in the job during the incumbent's vacation.

Research and Analysis

One of the most effective techniques for selecting from alternatives when major decisions are involved is research and analysis. This approach means solving a problem by first comprehending it. It thus involves a search for relationships among the more critical of the variables, constraints, and premises that bear upon the goal sought. It is the pencil-and-paper (or, better, the computer-and-printout) approach to decision making.

Solving a planning problem requires breaking it into its component parts and studying the various quantitative and qualitative factors. Study and analysis is likely to be far cheaper than experimentation. The hours of time and reams of paper used for analyses usually cost much less than trying the various alternatives. In manufacturing airplanes, for example, if careful research did not precede the building and testing of the prototype airplane and its parts, the resulting costs would be enormous.

A major step in the research-and-analysis approach is to develop a model simulating the problem. Thus, architects often make models of buildings in the form of extensive blueprints or three-dimensional renditions. Engineers test models of airplane wings and missiles in a wind tunnel. But the most useful simulation is likely to be a representation of the variables in a problem situation by mathematical terms and relationships. Conceptualizing a problem is a major step toward its solution. The physical sciences have long relied on mathematical models to do this, and it is encouraging to see this method being applied to managerial decision making.



Boeing's Decision to Go Digital in Developing the 777

www.boeing.com

Boeing's 777 airliner may be one of the most advanced aircraft in the world. The most innovative aspect, however, is the way the airliner was built: 100 percent three-dimensional digital design using CAD/CAM technology. To go digital was a critical decision for Boeing. Using the new system, engineers could see on the screen the design and preassemble the plane's more than 3 million parts and its 132,500 uniquely engineered parts. This new approach, a paradigm

shift, required completely new relationships with suppliers and customers. For example, the company requested ideas for the 777 from eight airlines. Internally, planners, engineers, and toolers worked together as a team, and they had current information on the development process. Previously, engineers and mechanics had had to work on some full-scale mockups to see whether parts did or did not fit, and problems would result in costly reworks. More recently, Boeing has begun using an advanced, intelligent CAD (called ICAD) system that makes major changes in the design possible. Now, and in the future, emerging technologies aid decision making.

Programmed and Nonprogrammed Decisions

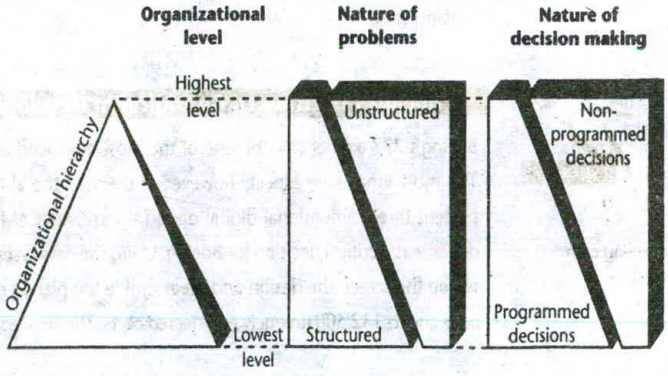
Programmed decisions are used for structured or routine work.

A distinction can be made between programmed and nonprogrammed decisions. A **programmed decision**, as shown in Figure 6-2, is applied to structured or routine problems. Lathe operators, for instance, have specifications and rules that tell them whether the part they made is acceptable, has to be discarded, or should be reworked. Another example of a programmed decision is the reordering of standard inventory items. This kind of decision is used for routine and repetitive work; it relies primarily on previously established criteria. It is, in effect, decision making by precedent.

Nonprogrammed decisions are used for unstructured, novel, and ill-defined situations of a nonrecurring nature.

Nonprogrammed decisions are used for unstructured, novel, and ill-defined situations of a nonrecurring nature. Examples are the introduction of the Macintosh computer by Apple Computer or the development of the four-wheel-drive passenger car by Audi. In fact, strategic decisions, in general, are nonprogrammed decisions, since they require subjective judgments.

FIGURE 6-2 The nature of problems and decision making in the organization



Most decisions are neither completely programmed nor completely nonprogrammed; they are a combination of both. As Figure 6-2 indicates, most nonprogrammed decisions are made by upper-level managers; this is because upper-level managers have to deal with unstructured problems. Problems at lower levels of the organization are often routine and well structured, requiring less decision discretion by managers and nonmanagers.

International Perspective

IBM's Louis Gerstner as Decision Maker[6]

At first, it might seem unlikely that a manager with a career at RJR Nabisco and American Express would be the person who could lead a technically oriented company like IBM out of its difficult 1993 position. Yet this was precisely what Louis Gerstner did with two key decisions: first, he did not break up the company; and second, he focused on the service business. By 2001, its global business was the area with the fastest growth. Despite the demands on his time, he still took time for social causes, especially those related to schooling.

One of Gerstner's strategic decisions was in the server market, where Sun Microsystems had been dominant with its UNIX servers. IBM was able to lower its prices and therefore put its competitors such as Sun, Hewlett-Packard, and Compaq under extreme pressure.

Thus, as a top-level manager, Gerstner had to balance his time resources between making strategic and tactical decisions, deciding on products and services, global and domestic planning, and strategy formulation and implementation, as well as balancing his energy between organizational and socially responsible actions.

Decision Making under Certainty, Uncertainty, and Risk

Virtually all decisions are made in an environment of at least some uncertainty. However, the degree will vary from relative certainty to great uncertainty. There are certain risks involved in making decisions.

In a situation involving certainty, people are reasonably sure about what will happen when they make a decision. The information is available and is considered to be reliable, and the cause and effect relationships are known.

In a situation of uncertainty, on the other hand, people have only a meager database, they do not know whether or not the data are reliable, and they are very unsure about whether or not the situation may change.

Moreover, they cannot evaluate the interactions of the different variables. For example, a corporation that decides to expand its operation to an unfamiliar country may know little about the country's culture, laws, economic environment, and politics. The political situation may be so volatile that even experts cannot predict a possible change in government.

In a situation with risks, factual information may exist, but it may be incomplete. To improve decision making, one may estimate the objective probability of an outcome by using, for example, mathematical models. On the other hand, subjective probability, based on judgment and experience, may be used.

All intelligent decision makers dealing with uncertainty like to know the degree and nature of the risk they are taking in choosing a course of action. One of the deficiencies in using the traditional approaches of operations research for problem solving is that many of the data used in a model are merely estimates and others are based on probabilities. The ordinary practice is to have staff specialists come up with "best estimates."

Virtually every decision is based on the interaction of a number of important variables, many of which have an element of uncertainty but, perhaps, a fairly high degree of probability. Thus, the wisdom of launching a new product might depend on a number of critical variables: the cost of introducing the product, the cost of producing it, the capital investment that will be required, the price that can be set for the product, the size of the potential market, and the share of the total market that it will represent.

International Perspective

Was Disneyland Paris Built on the Wrong Assumptions?[7]

www.disneylandparis.com

Assumptions are critical for making strategies; their importance can be illustrated by the decision to build Euro Disney, which was later called Disneyland Paris. The venture was planned in an uncertain environment and based on wrong assumptions. In the early days of this undertaking, from 1992 to 1994, the company lost more than $1 billion. Disney initially owned 49 percent of the venture, but its share was later reduced to 39 percent. So what went wrong? After all, the earlier move into Japan was very successful. Using the experiences with other ventures as the premises for the French Disneyland was precisely the problem. In the United States and Japan, the admission price was gradually raised after initial interest had been built. In contrast, Euro Disney started with an unsustainable entrance price of more than $40. This was very high in comparison with other theme parks. Consequently, the admission price had to be drastically reduced and then gradually increased. In 1996, the one-day adult

admission was about $38. Nevertheless, the initial high price may have resulted in the loss of customers in the early years of operation.

Another flawed assumption was that people would stay on average four days in Disney's hotels. However, in 1993, the average stay was only two days. The theme park opened with about one-third of the rides found at Disney World in America. Thus, all the rides could be done in one day, requiring a shorter hotel stay.

The European tradition of having the main meal at noontime was not taken into consideration either. The available eating places were overcrowded at noon and underutilized at other times. Rather than wait, visitors left to eat outside the park. In the United States and Japan, people eat throughout the day, thus avoiding long lines in the restaurants.

The mix of merchandise purchases is also different in France from that in the United States: Europeans buy fewer high-margin items.

These few illustrations seem to indicate that Disney did not sufficiently test its premises for the Euro Disney venture. Using assumptions based on previous successes may prove to be very costly. A careful analysis of cultural habits and observations of other theme parks may have prevented making plans based on incorrect assumptions.

While Euro Disney was suffering, certain competitors prospered. Euro Park was one of them. It is a theme park smaller than Euro Disney, located in Germany close to the French and Swiss borders. While Euro Disney may not have considered the cultural differences, management at Euro Park was very familiar with European customs. In surveys, visitors were asked to rate cleanliness, price, hours, rides, special shows, and so on. The surveys indicated, for example, that French visitors like to bring their baskets with bread, cheese, and wine. So patrons are allowed to bring their own food to the park (which is not allowed at Disney). The admission price was also substantially lower than at Euro Disney. Euro Park was considering building a hotel, but management realized that this would be a risky undertaking because it is a different kind of business, requiring competencies that are different from managing a theme park.

Creativity and Innovation

Creativity The ability and power to develop new ideas.

Innovation The use of new ideas.

An important factor in managing people is creativity. A distinction can be made between creativity and innovation. The term **creativity** usually refers to the ability and power to develop new ideas. **Innovation**, on the other hand, usually means the use of these ideas. In an organization, this can mean a new product, a new service, or a new way of doing things.

Although this discussion centers on the creative process, it is implied that organizations not only generate new ideas but also translate them into practical applications.

The Creative Process

Four phases of the **creative process:** unconscious scanning, intuition, insight, and logical formulation or verification.

The creative process is seldom simple and linear. Instead, generally it consists of four overlapping and interacting phases: (1) unconscious scanning, (2) intuition, (3) insight, and (4) logical formulation.

The first phase, *unconscious scanning,* is difficult to explain because it is beyond consciousness. This scanning usually requires an absorption in the problem, which may be vague in the mind. Yet managers working under time constraints often make decisions prematurely rather than dealing thoroughly with ambiguous, ill-defined problems.

The second phase, *intuition,* connects the unconscious with the conscious. This stage may involve a combination of factors that may seem contradictory at first. For example, Donaldson Brown and Alfred Sloan of General Motors conceived the idea of a decentralized division structure with centralized control, concepts that seem to contradict each other. Yet the idea makes sense when one recognizes the underlying principles of (1) giving responsibility for the operations to the general manager of each division and (2) maintaining centralized control in headquarters over certain functions. It took the intuition of two great corporate leaders to see that these two principles could interact in the managerial process.

www.gm.com

Intuition needs time to work. It requires that people find new combinations and integrate diverse concepts and ideas. Thus, one must think through the problem. Intuitive thinking is promoted by several techniques, such as brainstorming.

Insight, the third phase of the creative process, is mostly the result of hard work. For example, many ideas are needed in the development of a usable product, a new service, or a new process. What is interesting is that insight may come at times when the thoughts are not directly focused on the problem at hand. Moreover, new insights may last for only a few minutes, and effective managers may benefit from having paper and pencil ready to make notes of their creative ideas.

The last phase in the creative process is *logical formulation or verification.* Insight needs to be tested through logic or experiment. This may be accomplished by continuing to work on an idea or by inviting critiques from others. Brown and Sloan's idea of decentralization, for example, needed to be tested against organizational reality.

Brainstorming

Creativity can be taught. Creative thoughts are often the fruits of extensive efforts. Some techniques focus on group interactions, others on individual actions.

One of the best-known techniques for facilitating creativity was developed by Alex F. Osborn, who has been called the father of brainstorming.[8] The purpose of this approach is to improve problem solving by finding new and unusual solutions. In the brainstorming session, a multiplication of ideas is sought. The rules are as follows:

- No ideas are ever criticized.
- The more radical the ideas are, the better.
- The quantity of idea production is stressed.
- The improvement of ideas by others is encouraged.

Brainstorming, which emphasizes group thinking, was widely accepted after its introduction. However, the enthusiasm was dampened by research which showed that individuals could develop better ideas working by themselves than they could working in groups. Additional research, however, showed that in some situations the group approach may work well. This may be the case when the information is distributed among various people or when a poorer group decision is more acceptable than a better individual decision that, for example, may be opposed by those who have to implement it. Also, the acceptance of new ideas is usually greater when the decision is made by the group charged with its implementation.

Limitations of Traditional Group Discussion

Although the technique of brainstorming may result in creative ideas, it would be incorrect to assume that creativity flourishes only in groups. Indeed, the usual group discussion can inhibit creativity. For example, group members may pursue an idea to the exclusion of other alternatives. Experts on a topic may not be willing to express their ideas in a group for fear of being ridiculed. Also, lower-level managers may be inhibited in expressing their views in a group with higher-level managers. Pressures to conform can discourage the expression of deviant opinions. The need for getting along with others can be stronger than the need for exploring creative but unpopular alternatives to the solution of a problem. Finally, because they need to arrive at a decision, groups may not make the effort of searching for data relevant to a decision.

International Perspective

www.jnj.com
www.rubbermaid.com
www.hp.com
www.dowcorning.com
www.ge.com
www.3m.com

How 3M Fosters Innovation[9]

Companies have different strategies for fostering innovation. At Johnson & Johnson, autonomous operating units are encouraged to innovate. The organization culture allows failure. At Rubbermaid, 30 percent of its sales are derived from products that are less than five years old. Hewlett-Packard encourages researchers to spend 10 percent of their time on their pet projects, and Merck allocates time and resources to its researchers for working on high-risk products with a potential for high payouts. Dow Corning and General Electric engage in joint projects with customers to develop new products. One of the masters in innovation is Minnesota Mining & Manufacturing (3M).

When one hears of 3M, one thinks of innovation. The organizational environment of 3M fosters creative thinking and a tolerance for new ideas. Although the financial performance in 1995 was not as good as before, the company met its goal of obtaining at least 30 percent of its sales from products that were less than four years old. Continual innovation is fostered by the 15 percent rule, which suggests that researchers spend 15 percent of their time on things that are not related to their main project.

The company is very decentralized. Its 8,300 researchers work in many different laboratories. This results in redundancy. In theory, the main labs and development centers should do research, while the others do the development. Often, however, it does not work this way. The company operates with few rules and does not have a strategy in the traditional sense. Instead, it is guided by two things: (1) to be very innovative and (2) to satisfy the customer in every respect. Anything that hampers innovation, such as excessive planning or intolerance for mistakes, is eliminated. On the other hand, information sharing is required. Although financial measures act as a control, the real control comes from peers, who review each other's work.

The typical innovative process at 3M works as follows: When a person in the organization has an idea for a new product, he or she forms a team consisting of individuals from the functional areas, such as the technical department, manufacturing, marketing, sales, and, at times, finance. The company also encourages customers to contribute their ideas. The team works on product design, production, and marketing. Moreover, various uses of the product are explored. Team members are rewarded for the success of the product.

Rules or guidelines are rather simple: develop a tolerance for failure; reward those who have a good product idea and who can form an effective action team to promote the product; establish close relationships with customers; share technology with others in the company; keep the project alive by allocating time or financial grants; keep the divisions small.

The future will tell whether innovation will continue to be a key success factor for 3M.

The Creative Manager[10]

All too often, it is assumed that most people are noncreative and have little ability to develop new ideas. This assumption, unfortunately, can be detrimental to the organization, for in the appropriate environment virtually all people are capable of being creative, although the degree of creativity varies considerably between individuals.

Generally speaking, creative people are inquisitive and come up with many new and unusual ideas; they are seldom satisfied with the status quo. Although intelligent, they not only rely on the rational process but also involve the emotional aspects of their personality in problem solving. They appear to be excited about solving a problem, even to the point of tenacity. Creative individuals are aware of themselves and capable of independent judgment. They object to conformity and see themselves as being different.

It is beyond question that creative people can make great contributions to an enterprise. At the same time, however, they may also cause difficulties in organizations. Change—as any manager knows—is not always popular. Moreover, change frequently has undesirable and unexpected side effects. Similarly, unusual ideas, pursued stubbornly, may frustrate others and inhibit the smooth functioning of an organization. Finally, creative individuals may be disruptive by ignoring established policies, rules, and regulations. John Kao, who teaches at Harvard Business School, suggests that creative people should have enough freedom to pursue their ideas, but not too much that they waste their time or do not find enough time to collaborate with others in working toward common goals. He suggests that managers should view themselves as jazz musicians who follow a set of scores but have enough freedom for variations.[11]

As a result, the creativity of most individuals is probably underutilized in many cases, despite the fact that unusual innovations can be of great benefit to the firm. However, individual and group techniques can be effectively used to nurture creativity, especially in the area of planning. Nonetheless, creativity is not a substitute for managerial judgment. It is the manager who must determine and weigh the risks involved in pursuing unusual ideas and translating them into innovative practices.

Summary

Decision making is the selection of a course of action from among alternatives; it is the core of planning. Managers must make choices on the basis of limited, or bounded, rationality—that is, in light of everything they can learn about a situation, which may not be everything they should know. *Satisficing* is a term sometimes used to describe picking a course of action that is satisfactory under the circumstances.

Because there are almost always alternatives—usually many—to a course of action, managers need to narrow them down to those few that deal with the limiting factors. These are the factors that stand in the way of achieving a desired objective. Alternatives are then evaluated in terms of quantitative and qualitative factors. Other techniques for evaluating alternatives include marginal analysis and cost-effectiveness analysis. Experience, experimentation, and research and analysis come into play in selecting an alternative.

Programmed and nonprogrammed decisions are different. The former are suited for structured or routine problems. These kinds of decisions are made especially by lower-level managers and nonmanagers. Nonprogrammed decisions, on the other hand, are used for unstructured and nonroutine problems and are made especially by upper-level managers.

Virtually all decisions are made in an environment of at least some uncertainty involving the interaction of a number of important variables, and there are certain risks involved in making decisions. Managers dealing with uncertainty should know the degree and nature of the risk they are taking in choosing a course of action.

Creativity, the ability and power to develop new ideas, is important for effective managing. Innovation is the use of these ideas. The creative process consists of four overlapping phases: unconscious scanning, intuition, insight, and logical formulation. A popular technique for enhancing creativity is brainstorming. Creative individuals can make a great contribution to the enterprise. At the same time, they can be disruptive by not following commonly accepted rules of behavior.

KEY IDEAS AND CONCEPTS FOR REVIEW

Decision making
Limited or bounded rationality
Satisficing
Principle of the limiting factor
Quantitative factors
Qualitative factors
Marginal analysis
Cost-effectiveness analysis

Three approaches to selecting an alternative
Programmed decisions
Nonprogrammed decisions
Decision making under certainty, uncertainty, and risk
Creativity
Innovation
Creative process
Brainstorming
Creative manager

FOR DISCUSSION

1. Why is experience often referred to not only as an expensive basis for decision making but also as a dangerous one? How can a manager make the best use of experience?
2. In a decision problem you now know of, how and where would you apply the principle of the limiting factor? Did you apply this principle in selecting the class or section of the class you are attending? In what ways?
3. Identify five decision problems and recommend programmed or nonprogrammed decisions. If the examples are from an organizational setting, did they occur at upper or lower levels?
4. "Decision making is the primary task of the manager." Comment.
5. Think of a problem that was creatively solved. Did the solution come from group discussion, or was it the result of an individual effort? Reconstruct the phases of the creative process.

EXERCISE/ACTION STEPS

Your boss offers you a promotion to a position in a location that your family does not like. Make the necessary assumptions and then state how and what you would decide.

INTERNET RESEARCH

1. Search the Internet for "creativity" and illustrate how creativity can be applied to decision making.
2. Find three applications of brainstorming on the Internet.

International Case

Coke's European Scare

What seemed like an isolated incident of a few bad cans of Coca-Cola at a school in Belgium turned into near disaster for the soft-drink giant's European operations. In June 1999, Coke experienced its worst nightmare—a contamination scare resulting in the recall of 14 million cases of Coke products in five European countries and a huge blow to consumer confidence in the quality and safety of the world's most recognizable brand.

After the initial scare in Bornem, Belgium, Coke and Coca-Cola Enterprises, a bottler 40 percent owned by Coca-Cola, thought they had isolated the problem. Scientists at the bottling

plant in Antwerp, Belgium, found that lapses in quality control had led to contaminated carbon dioxide being used in the bottling of a recent batch of Coke. Company officials saw the contamination as a minor problem and they issued an apology to the school.

At the same time that the problem was being dealt with in Antwerp, things were breaking down at Coke's bottling plant in Dunkirk, France. In Belsele, ten miles from Bornem, children and teachers were complaining of illnesses related to drinking Coke products. The vending machines at the school were stocked with Coke from the company's Dunkirk plant and was thought to be safe. Now a second bottling plant's practices were being questioned. What initially seemed like an isolated incident was now a crisis.

Immediately following the second scare, Belgium's Health Minister banned the sale of all products produced in the Antwerp and Dunkirk plants. Things got worse when Coke gave an incomplete set of recall codes to a school in Lochristi, Belgium, resulting in 38 children being rushed to the hospital. Immediately following this incident, French officials banned the sale of soft drinks produced in the Dunkirk plant. It was believed that fungicide on wooden shipping pallets was the cause of the illnesses linked to the drinks from that plant.

On June 15, 1999, 11 days after the initial scare in Bornem, Coke finally issued an explanation to the public. Most Europeans were not satisfied. Coca-Cola officials used vague language and often contradicted one another when making statements. The French Health Minister, Bernard Kouchner, stated, "That a company so very expert in advertising and marketing should be so poor in communicating on this matter is astonishing."[12]

After three weeks of testing by both Coke officials and French government scientists, it was concluded that the plants were safe and that there was no immediate threat to the health of consumers. Coke destroyed all of the pallets in Dunkirk and tightened quality control on carbon dioxide.

How could this happen to a company that is revered worldwide for its quality control and the superiority of its products? Coke has spent decades building its reputation overseas, and the European market now represents 73 percent of total profits.[13] While the scare has had some effect on Coke's profits in Europe, the company is more concerned with damages to its reputation and consumer confidence in its products.

Many critics say that Coke's slow response, insisting that no real problem existed, and belated apology have severely damaged the company's reputation in Europe. Some would disagree and feel that Coke handled the situation as best as it could. "I think that Coke acted in a responsible, diligent way," says John Sitcher, editor of *Beverage Digest*. "Their first responsibility was to ascertain the facts in a clear and unequivocal way. And as soon as Coke knew what the facts were, they put out a statement to the Belgium people."[14]

The character and quality of a company can often be measured by how it responds to adversity. Coca-Cola believes that this crisis has forced the company to reexamine both its marketing and management strategies in Europe. Coke executives in Brussels are predicting that the company

will double its European sales in the next decade and that this setback will only make the company stronger. Wall Street analysts seem to agree. Only time will tell.

Questions

1. What are the management issues in this case?
2. What did Coke do and what could have been done differently?
3. What were the key factors that were or should have been considered by management?

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Part - 2 closing

Global Planning

This part closing focuses on the global dimension of planning. First, managerial practices in Japan, the United States, and China are discussed.[1] Second, the competitive advantages and disadvantages of Germany are identified. The global car industry case discusses the merger between the German Daimler and the American Chrysler corporations.

Planning Practices in Japan, the United States, and China[2]

Productivity is of great concern to all nations. Many U.S. enterprises have looked to Japan to learn about managerial practices, such as that used by Toyota Motor. On the other hand, many Japanese scholars attend universities in the United States to learn about management and to earn their MBA. Japan's phenomenal success in increasing productivity is often attributed to its managerial approach.[3] But external forces shaping these practices, such as culture and philosophies, should not be overlooked. It should also be pointed out that managerial practices are changing rapidly. Japanese firms, for example, are moving toward Western styles of managing because of experiences gained by managers through strategic alliances with Western companies. There is an abundance of literature on both U.S. and Japanese management. One such book even made the bestseller list,[4] and there are many other books[5] and many more articles. But the literature on Chinese management is very sparse.[6] Since Japan and the United States present contrasting managerial approaches, Chinese managers probably could adopt aspects from either approach to make their enterprises more effective and efficient. The purpose of this discussion is to compare and contrast the Japanese and U.S. managerial models and evaluate them with current practices used by large, state-owned enterprises in China.

This section focuses on planning in these three countries, as summarized in Table C2-1. The discussions in the closing sections of parts 3 to 6 are on organizing, staffing, leading, and controlling in these nations. At the outset, a word of caution is in order. It is obvious that not all American firms are managed the same way as discussed in this text. The same is true for Japanese and Chinese managerial practices. Managerial practices change over time, and Japanese and Chinese approaches are moving closer to practices in the West. This is true not only for planning, but also for the other managerial functions that will be discussed later in the book.

TABLE 6.1 Comparison of Japanese, U.S., and Chinese planning

Japanese	American	Chinese*
• Long-term orientation	• Primarily short-term orientation	• Long-term and short-term orientations (five-year and annual plans)
• Collective decision making (*ringi*) with consensus	• Individual decision making	• Decision making by committees; at the top, often individual
• Involvement of many people in preparing and making the decision	• Involvement of a few people in making the decision and "selling" it to colleagues with divergent values	• Top-down; participation at lower levels
• Flow of critical decisions from top to bottom and back to top; flow of noncritical decisions often from bottom to top (in either case, emphasis is on consensus)	• Decisions initiated at the top, flowing down	• Top-down, initiated at the top
• Slow decision making; fast implementation of decision	• Fast decision making; slow implementation requiring compromise, often resulting in suboptimal decisions	• Slow decision making; slow implementation (but changes are taking place)

* As practiced by state-owned enterprises.

Planning in Japan

In Japan, planning is greatly aided by the cooperation between government and business. After World War II, Japan developed policies for promoting economic growth and strength as well as international competitiveness. These policies harmonized monetary and fiscal policies within the industrial structure. In this kind of relatively stable economic predictability, environment planning is less risky. Planning is choosing the purpose and objectives of the organization as a whole or a part of it and selecting the means to achieve those ends; it requires making decisions. The Japanese, in general, have a longer-term orientation in planning than American managers. There are several reasons. In Japan, for example, banks are the primary providers of capital, and their interest is in the long-term health of enterprises. Furthermore, the Ministry of International Trade and Industry develops five-year plans that promote and provide guides for industry planning. Moreover, business conglomerates, known as *keiretsu*, are often linked to large banks, which are interested in the long-term performance of the companies. These keiretsu offer opportunities for large-scale economics, networks that inhibit competition, vertical integration, and influence over governmental decisions.

Planning in the United States

In contrast, U.S. managers are often under pressure by stockholders to show favorable financial ratios each time they report them. This, unfortunately, may not encourage investments that have a payout in the more distant future. Also, Americans usually stay in their managerial positions for only a relatively short time, so a myopic decision can seldom be traced to the manager who made it but has already been promoted or has even changed companies.

Planning in China[7]

In China, the situation is quite different. Most of the enterprises are state-owned, and it is only more recently that private firms have come into existence. In our comparison, however, we focus only on the former. In these enterprises, both long- and short-term plans are prepared. The five-year plan is prepared at the top (the State Planning Commission), while more detailed plans are made at lower levels. The orientation is to meeting objectives and achieving the assigned plan rather than to being successful in the market. While strategy formulation may not be practiced widely in a formal manner, strategic thinking in military terms is a part of the Chinese culture. The book *Bing-Fa* is one of the most complete books on military strategy. Thus, certain principles from the book may be applied by managers in dealing with Western corporations. For example, the best strategy is considered to be that of winning without a war. The next best is to win through alliances. There is also the difficulty of integrating organizational and personal goals because the achievement of organizational objectives has little bearing on individual benefits.

Decision Making in Japan[8]

One of the most interesting aspects of Japanese management is the way decisions are made. In a typical organization, several levels are involved in making a decision. Actually, the most important part of the process is the understanding and analysis of the problem and the development of various alternative solutions. Critical decisions may flow from top management to lower levels and back to the top. Noncritical decisions may originate at the bottom and be submitted to top managers. The final authority for making a decision still rests with top management. However, before a proposal reaches the executive's desk, the problem and the possible solutions have been discussed at various levels in the organizational hierarchy. Top management still has the option to accept or reject a decision, but it is more likely that a decision will be returned to subordinates for further study rather than being rejected outright.

A proposal is confirmed through the *ringi* process. The *ringi-sho* is a proposal document prepared by a staff member. It is circulated among various managers before it goes to top management for formal approval. The document, which is usually initialed by those involved in or affected by the decision, elicits the cooperation and participation of many people. This in turn assures that the problem or the decision is examined from different perspectives. That this decision-making process is time-consuming is obvious. However, after a consensus is reached, implementation of the plan is rather swift because of the understanding of the plan, the clarification of the problem, the

evaluation of the different alternatives, and the involvement of those people who will implement the decision. Critics accuse Japanese companies of being too slow and ambiguous in making decisions. The sharing of decision power and responsibilities can also result in a situation where no one feels individually responsible for the decision. On the other hand, assuming collective responsibility is congruent with Japanese values.

Decision Making in the United States

In U.S. organizations, decisions are made primarily by individuals, and usually only a few people are involved. Consequently, after a decision has been made, it has to be sold to others, often to people with different values and different perceptions of what the problem really is and how it should be solved. In this way, the making of a decision is rather fast, but its implementation is very time-consuming and requires compromises with those managers holding different viewpoints. The result is that the decision that is eventually implemented may be suboptimal because of the compromises necessary to appease those with divergent opinions. It is true that decision responsibility can be traced to individuals as long as they remain in the same position, but at the same time this may result in the practice of finding scapegoats for wrong decisions. All in all, in U.S. companies, decision power and responsibility are vested in designated individuals, while in Japan several people share both decision power and responsibility.

Decision Making in China

In China, individuals at the top make major decisions, but many people are involved in operational decisions.[9] Still, lower-level managers have very little authority to make decisions. Decision making through the central planning bureau is under the direct control of the state. This, unfortunately, results in a lack of flexibility in the implementation of decisions. Although the need to change is realized, managers in the upper echelons of the hierarchy resist reforms because reforms would mean giving up some of the privileges they have as officials.



A TOWS Analysis of the Competitive Advantages and Disadvantages of Germany

Every nation is concerned with competing effectively in the global market. Competitiveness does not depend only on the effectiveness of individual companies, but also on the industries and the socioeconomic system of a nation. The rapidly changing environments of the free world markets dictate that nations fully use their comparative advantages to remain or become prosperous in the future. Political, economic, and business leaders must evaluate the opportunities in and threats from the external environment in order to build appropriate strategies that take advantage of their nation's and industry's strengths and shore up weaknesses.

The TOWS Matrix for the Analysis of Germany[10]

In Chapter 5, you have been introduced to the TOWS Matrix for analyzing the competitive position of a company. Now the TOWS concepts will be used for determining the competitive advantage of Germany. The TOWS Matrix in Figure C2-1 shows selected aspects of German industries that have had a significant impact—either positively or negatively—on the country's economy and its position in the European Union (EU) and the world. Intrinsic national forces in the social, economic, political, and technological areas are considered in determining the origin of Germany's industrial strengths and weaknesses. External opportunities for and threats to these industries can then be analyzed. After an analysis of a wide array of forces, strategies by German industries can be delineated and alternative industrial strategies developed. Because the former West Germany differs very much from the former East Germany, the analysis will focus on what used to be called West Germany before reunification; it will be referred to in this discussion simply as Germany. The figure summarizes the competitive situation of this part of Germany.

Germany's Internal Environment: Its Strengths and Weaknesses

Germany is often considered an economic power. Yet, from a global perspective, multinational corporations from Japan and the United States dominate the global markets. Among the largest Fortune 500 global corporations, only a relatively few firms were German in the year 2000 ranking. Germany's Volkswagen ranked only 21st and Siemens 23rd.[11] DaimlerChrysler, the merged German–American company, ranked 5th. On the global scale, then, large German corporations make up a much smaller portion than their Japanese and U.S. counterparts.

As shown in Figure C2-1, Germany's strengths range from the educated and skilled labor force to relatively stable labor–management relations and the strengths gained through the reunification of the former East and West Germany. But the reunification also involved a high cost, so it is also shown as an internal weakness in the figure. Other weaknesses range from the high labor and social costs to the relatively high unemployment rate.

External Opportunities and Threats

The external opportunities for Germany extend from the European Union to East European countries, the Americas, and the Pacific Rim and Asia. While opportunities abound, threats also come from some industries in the global market, as shown in the figure. For example, high-quality consumer electronic products from Japan have replaced many German products.

Four Sets of Strategies for Germany

Considering the nation's internal strengths and weaknesses and the opportunities and threats from other countries, four sets of alternative strategies should be considered.

FIGURE C2-1 TOWS Matrix for Germany

Internal factors / External factors	**Internal strengths (S)**	**Internal weaknesses (W)**
	• Educated, skilled labor force; pride in workmanship and quality • Experience in global market (e.g., export) • Strengths in engineering, machinery, chemicals (e.g., BASF Bayer, Hoechst), banking (e.g., Deutsche Bank), electromechanical (e.g., Siemens), cars (e.g., Mercedes-Benz, BMW, Volkswagen) • Strong small/midsize companies (*Mittelstand*) • Stable labor–management relations • German reunification • Common EU currency	• High labor and social costs • Slow in responding to changes • High cost of German reunification • Slow in innovation • Few natural resources • Relative lack of skills in new sciences (semiconductors, electronics, computers, software, biotechnology) • Problems in certain industries (shipbuilding, electronics, steel) • Weak in service • Relatively high unemployment rate • Some strengths become weaknesses (e.g., labor relations)
External opportunities (O) • Europe: increased trade within EU and EFTA; crossborder trade; standardization (e.g., ISO 9000); banking and insurance without borders in EU • North America: strong deutsche mark (now euro) favors German investments in USA • Eastern Europe: former East Germany's relations with COMECON countries • Former Soviet republics: industrial expansion; pent-up demand; relations with former East Germany	**SO: Maxi–Maxi** • Regulation and standardization within European banking industry will make EU more accessible to German bank expansion (e.g., through establishment of branches) • ISO certification will raise productivity and quality • Technological advancements in telecommunication, aviation, and manufacturing through cooperation, alliances, and mergers with U.S. companies (e.g., Daimler–Chrysler merger)	**WO: Mini–Maxi** • Set up steel plants in Spain and Portugal to exploit cheap labor and cut costs • Invest in USA in car manufacturing plants (e.g., BMW and Mercedes) • Move operations to countries with lower labor costs (e.g., Asia, USA) • Expand into China with caution

• Pacific Rim and Asia: growing wealth and investment opportunities; opening of China	• Expansion to Eastern Europe of automotive, power generation, and consumer markets • Capitalize on Asian interest in Germany through alliances	
External threats (T) • EU: price competition from other EU countries; economic instability in other EU countries • Eastern Europe: massive immigration (also from non-European countries) • Former Soviet republics: political and economic uncertainties; poor legal and economic structures • Pacific Rim and Asia: low costs (e.g., China); high-quality products (e.g., Japan); vigorous economic activities (e.g., South Korea)	**ST: Maxi–Mini** • Promote Mittelstand exports • More guarantees from German government and G-7 before German banks write off any more loans to aid Eastern bloc and prevent mass immigration • Establish wider banking in Asia • Establish joint ventures with Asian car makers • Adopt Japan's just-in-time and total quality control philosophies to increase worker commitment	**WT: Mini–Mini** • Concerted efforts among government, business, and labor sectors to cope with problems of overvalued currency, high wages and greedy labor unions, high social taxes, government inaction, and competition from "Asian Tigers" • Establish production bases in Eastern Europe to reduce effects of a strong deutsche mark (and euro) on costs and export prices

COMECON: Council for Mutual Economic Assistance, a trade organization of Communist countries; EFTA: European Free Trade Association; EU: European Union.

SO strategies (Maxi–Maxi)

The potentially most successful strategies for Germany would make use of its strengths to take advantage of opportunities, not only within the European Union but also in North America, Eastern Europe, Asia, and the Pacific Rim countries.

Opportunities created through the European Union allow the free flow of capital, guided by common regulations governing financial transactions. Regulation and standardization within the European banking industry will make the European Union more accessible to expansion by German banks. For example, Deutsche Bank's strategy of EU-wide expansion revolves around the establishment of branches throughout the European Union and cooperation with foreign banks. In addition, the bank has more freedom to expand aggressively in the United States.

ST strategies (Maxi–Mini)

Maxi–Mini strategies aim at maximizing the country's strengths and minimizing external threats. For example, Germany's export-driven economy relies upon gaining and maintaining market shares in foreign markets.[12] German exports account for a large percentage of its gross domestic product, much coming from small and midsize *Mittelstand* companies. Mittelstand exports are promoted by the German government, which helps these companies to obtain export insurance for countries such as Thailand. Several other strategies are summarized in the figure.

WO strategies (Mini–Maxi)

Mini–Maxi strategies aim at overcoming German industry's weaknesses so that it can take advantage of opportunities, as illustrated by the following two examples. The German steel industry could consider setting up steel plants in Spain and Portugal to exploit cheaper labor. Because of high labor and social costs in Germany, Mercedes-Benz has invested in a plant in Alabama in the United States to produce a sport utility vehicle. This vehicle is marketed not only in the United States but also abroad.[13]

WT strategies (Mini–Mini)

The Mini–Mini strategy is an attempt to minimize both internal weaknesses and external threats. While some Germans concede that the country is in trouble, most people do not realize it. In fact, different groups blame each other for some current problems, which include high wages, greedy labor unions, high social taxes, inaction by the government, and competition from the "Asian Tigers."[14] Coping with these problems will require a concerted effort among the government, business, and labor sectors of Germany. One such strategy relates to Germany's strong currency, which hinders export. Therefore, German industries may consider the establishment of production bases in Eastern Europe to reduce costs and barriers.

Selecting a Set of Strategies

Undoubtedly, the educated and skilled labor force has helped Germany gain and maintain its competitiveness. Furthermore, Germany's industrial strengths in chemicals, automobiles, machinery, and banks are important factors to the nation's success. However, the relative strengths in many of these industries have now started to diminish. Moreover, internal weaknesses, such as high labor and social costs, the relative slowness in innovation, and problems in certain industries, such as electronics, steel, and shipbuilding, indicate the need for transformation. Additionally, Germany has insufficient skills in the new sciences of semiconductors, computers, software, and biotechnology.

The TOWS Matrix approach generates various alternatives for gaining a competitive advantage for a nation. However, these alternatives are descriptive and not prescriptive. Nonetheless, they do help policy makers in the systematic analysis of internal and external factors and in combining them to achieve a synergistic effect. Although we illustrated the practical application of the TOWS Matrix for Germany, other countries may also benefit from generating strategies for maintaining or gaining competitive advantages in the global market.[15]

Global Car Industry

Case

The Daimler–Chrysler Merger: A New World Order?[16]

In May 1998, Daimler-Benz, the largest industrial firm in Europe, and Chrysler, the third largest car maker in the United States, merged. The carefully planned merger seemed to be a "strategic fit." Chrysler, with its lower-priced cars, light trucks, pickups, and its successful minivans, appeared to complement Daimler's luxury cars, commercial vehicles, and sport utility vehicles (SUVs). There was hardly any product-line overlap.

The merger followed a trend of other consolidations. General Motors (GM) owns 50 percent of Swedish Saab AB and has subsidiaries Opel in Germany and Vauxhall in England. Ford acquired British Jaguar and Aston Martin. The German car maker BMW acquired British Rover (but later got rid of it and kept only the Mini model), and Rolls Royce successfully sold its interests to Volkswagen and BMW. On the other hand, the attempted merger of Volvo and Renault failed, and Ford later acquired Volvo.

The Daimler–Chrysler cross-cultural merger had the advantage that the chief executive officers (CEOs) of both companies had international experience and knowledge of both German and American cultures. Chrysler's Robert Eaton had experience in restyling Opel cars in GM's European operation. Mr. Lutz, the co-chair at Chrysler, speaks fluent German, English, French, and Italian and had past work experience with BMW, GM, and Ford. Daimler's CEO, Jürgen Schrempp, had worked in the United States and South Africa, giving him a global perspective.

Background

Lee Iacocca, the colorful Chrysler chairman, left Ford for Chrysler because of a clash with Henry Ford II in 1978. He is credited with saving Chrysler from bankruptcy in 1979/1980 when he negotiated a loan guaranty from the U.S. government. Iacocca also led Chrysler's acquisition of American Motors in 1987, which added the Jeep to the Chrysler line. Robert Eaton, Chrysler's CEO who negotiated the 1998 merger with Daimler, replaced Iacocca in 1992.

At the time of the merger, Daimler was selling fewer vehicles than Chrysler but had higher revenues. Daimler's 300,000 employees worldwide produced 715,000 cars and 417,000 trucks and commercial vehicles in 1997. The company was also in the business of airplanes, trains, and helicopters, and two-thirds of its revenue came from outside Germany.

So, why would Daimler in Stuttgart, Germany, go to Chrysler in Detroit, USA? The companies had complementary product lines and Chrysler saw the merger as an opportunity to overcome some of the European trade barriers. However, the primary reasons for mergers in the auto industry are technology (which has high fixed costs) and overcapacity (which is estimated at 20 percent). Only those companies with economies of scale can survive. Mr. Park, the president of Hyundai Motor Company, stated that production lines in South Korea operated at about 50 percent of capacity in 1998. The auto industry could produce about one-third more cars. It has been predicted that only six or seven major car makers will be able to survive in the 21st century. This makes a merger more of a competitive necessity than a competitive or strategic advantage.

Daimler + Chrysler = New Car Company*

In the late 1980s and the early 1990s, the Japanese made great strides in the auto industry through efficient production methods and high-quality products. However, a new trend was set by the German car maker that changed the car industry with the Daimler–Chrysler merger, in which the former has 53 percent ownership and the latter the rest. The new car company is now the fifth largest in the world and could become the volume producer in the whole product range.

The respective strengths are that Daimler is known for its luxury cars and its innovation in small cars (A-Class, Smart car[17]). Chrysler, on the other hand, has an average profit per vehicle that is the highest among the Big 3 (GM, Ford, and Chrysler) in Detroit, thanks to high margins derived from the sale of minivans and Jeeps. It is also known for its highly skilled management and efficient production. Low costs and simplicity (e.g., the Neon model) are other hallmarks of Chrysler.

Figure C2-2 shows the strengths and weaknesses of Chrysler before the merger with Daimler-Benz. It also lists the external opportunities and threats for the company as well as alternative strategies. Essentially, Chrysler continued its strategy of strengthening its SUV and minivan market in the countries under the North American Free Trade Agreement (NAFTA). At the same time,

*This discussion shows the application of the TOWS Merger Matrix introduced in Chapter 5.

FIGURE C2-2 TOWS Matrix for Chrysler Corporation before the merger

Internal environment / External environment	**Internal strengths (S)** • A tradition and brand image in NAFTA • Sales and service network in NAFTA • Balanced portfolio in USA • Jeep image and profitable minivans	**Internal weaknesses (W)** • Narrow focus on home market and NAFTA • Company little known outside NAFTA • Weak network outside NAFTA • Delicate overall financial situation
External opportunities (O) • Demand for high-margin minivans • Growing SUV market • Advances in information technology	**SO: Maxi–Maxi** • Strengthen SUV and minivan products in NAFTA • Seek merger with a high-tech company	**WO: Mini–Maxi** • Enter non-NAFTA markets • Develop sales and service networks outside NAFTA
External threats (T) • Saturation and stagnation of U.S. market • Increasing SUV and minivan competition (e.g., Nissan, Toyota) • Hostile takeover possibility • Competition (e.g., General Motors, Ford)	**ST: Maxi–Mini** • Use know-how to improve SUV and minivan position • Develop innovative cars • Explore a friendly merger	**WT: Mini–Mini** • Find partner to enter worldwide market

NAFTA: North American Free Trade Agreement; SUV: sport utility vehicle.

the company faced increasing competition and the need for expanding to non-NAFTA markets. Furthermore, there was the danger of an "unfriendly" takeover by another company, and exploring a friendly merger with a firm with good reputation that could supplement its product line and enable it to expand into new markets made a lot of sense.

Mercedes-Benz (a part of Daimler Corporation) was known for its excellence in engineering and product quality; the company's brand image was luxury cars. On the other hand, Mercedes lacked a product offering in the lower-priced, high-volume segment as shown in Figure C2-3. The high development costs and the need for gaining economies of scale called for finding a partner that would enable it to offer a complete product line from high-priced to low-priced vehicles.

The situational analysis after the merger shows that the strengths and weaknesses of the two companies complement each other (see Figure C2-4). They can now offer a full product line in all segments in their respective home markets. There is little product overlap with the exception of the Jeep Cherokee competing directly with the Mercedes M-Class SUV, which is produced in

FIGURE 6.3 TOWS Matrix for Daimler-Benz before the merger

Internal environment / External environment	**Internal strengths (S)** • Brand image for luxury cars • Engineering expertise • Product quality • Financial power	**Internal weaknesses (W)** • Focus only on worldwide luxury car market • Lack of high-volume segment • High prices • Weak presence in Asian markets
External opportunities (O) • Need for broad product line • Demand for small luxury cars • Need for new sales channels	**SO: Maxi–Maxi** • Use brand image to enter new area and broaden product line • Develop the Smart car • Use platform concepts to reduce costs • Develop minivans	**WO: Mini–Maxi** • Enter lower-priced segment • Develop products to increase volume • Utilize existing partners • Find new partners in lower-priced segment
External threats (T) • Saturation in home market • Economic problems in emerging markets • Competition in luxury car market (e.g., BMW, Lexus, Infiniti, Accord, Jaguar) • Broadened product line of competitors (e.g., Volkswagen, Audi)	**ST: Maxi–Mini** • Use technological know-how to fight competitors • Search for cooperating partners	**WT: Mini–Mini** • Establish a new brand for lower-priced segment

Alabama. Moreover, the partners can now utilize the innovation in both their particular areas of expertise. Their facilities in various countries can be used for the production and assembly of both low- and premium-priced cars. In all, the merged DaimlerChrysler Corporation may achieve synergy and cost savings.

Despite the potential advantages of the merger, challenges remain. The company has little experience in penetrating the worldwide market of lower-priced products. There is also the potential for conflicts in the integration of the operational and management systems of the merged companies. External threats remain and may get worse. Car markets in the European Union and NAFTA are becoming saturated, and economic deterioration in developed and emerging economies reduce and stagnate the growth in those countries. In addition, competition (especially in the luxury segments) becomes fiercer.

FIGURE C2.4 TOWS Matrix for DaimlerChrysler after the merger

Internal environment / External environment	**Internal strengths (S)**	**Internal weaknesses (W)**
	• Full product line; presence in all segments in home markets • Favorable image and brand perception of Mercedes and Jeep brands • Improved car sales in WEU and USA • Sales and service network in WEU and USA • Worldwide assembly and production • Innovation potential and technological know-how • Financial power; productivity	• Focus only on luxury segment worldwide • Lack of products for Asian volume segment • Little experience in lower-priced segment in certain regions • Lack of products to enter lower-priced segment • High-priced position • Weak performance in Asia, except in luxury segment • Potential conflicts in operational and management systems
External opportunities (O) • Establishing existing brands in new markets • Addressing needs in new segments • Developing and introducing new models • Entering niche segments • Utilizing new sales channels • Broadening service (mobility, financing) • Utilizing economies of scale (cost-saving potential in distribution, production, and administration) • Development of fuel cells powered by hydrogen	**SO: Maxi–Maxi** • Make use of brands and products • Utilize business systems and further improve sales performance and efficiency • Further improve reputation of entire brand portfolio and customer awareness • Make use of technological know-how in newly served segments • Make use of synergies to reduce development, production, and administrative costs • Research in fuel cell technology for car offerings around 2004	**WO: Mini–Maxi** • Buy or create brand for lower-priced segment • Acquire or cooperate with other firms to penetrate lower-priced segment, achieve economies of scale, and gain access to new markets (especially Asia) • Develop lower-priced products, especially for Asia • Market products outside home markets • Search for appropriate partners especially in insufficiently served markets
External threats (T) • Saturation and stagnation in WEU and NAFTA • Economic deterioration in emerging markets, reducing demand • Fiercer competition in luxury segment • Broadening product line of (new) competitors • Increasing concentration in automotive sector • Falling stock market value	**ST: Maxi–Mini** • Utilize innovation potential and technological know-how to achieve dominance in all segments • Scan all potential customers to find their needs and offer the "perfect" solution • Attract investors to back up and increase stock market value to protect against hostile investors	**WT: Mini–Mini** • Deliberate cooperation with Asian partners to further grow and improve worldwide setup

NAFTA: North American Free Trade Agreement; WEU: Western European Union.

Figure compiled with the assistance of K. U. Seidenfuss.

The challenge for Daimler's CEO, Jürgen Schrempp, is to integrate the two companies and achieve the efficiencies that were one of the important aims of the merger. In addition, integrating the organization cultures of the two companies will be a major challenge.

Jürgen Schrempp: A Shake-up Artist?

Besides arranging for the Daimler–Chrysler merger, Schrempp initiated many changes in the German operation. When he took office, he felt that the company was without purpose and direction. Consequently, he divested AEG and reduced the number of businesses from 35 to 23. His emphasis on shareholder value is counter to traditional German business culture. Schrempp models his managerial style after former General Electric CEO Jack Welch.[18] Welch believed that General Electric should be number 1 or 2 (or have a plan aimed at getting there) in a given market or business, or the company should get out of that market.

Many challenges await Schrempp. Mercedes faces tough competition in the luxury segment from the Japanese Lexus, Infiniti, and Acura as well as the European BMW and Jaguar. Germany's labor cost is the highest in the world; and it requires 60 to 80 labor-hours to build a Mercedes, while it takes only 20 labor-hours to build a Lexus. Schrempp needs to cut costs and improve productivity in order to survive. To remain competitive in a global market with fewer but larger car makers, DaimlerChrysler has to grow and introduce new models. At the Frankfurt Auto Show in 1999, the company announced that it would invest $48 billion to introduce 64 new models in the next five years. Similarly, Chrysler faces competition in the SUV and minivan product lines.

Strategy Implementation: The Achilles' Heel of the Merger?

The merger strategy was carefully planned and formulated. The global perspectives of Schrempp and Eaton as well as the product lines indicated a fit as shown in the TOWS Matrix of the combined company (Figure C2-4). Yet implementing a well-conceived strategy provides its own challenges. Some Chrysler designers and managers saw the merger more as a takeover by Daimler and consequently left the firm to join GM and Ford. Mr. Eaton, the American morale booster, retired soon after the merger. While there is mutual understanding of the country and corporate cultures at the highest organizational level (both CEOs having a global perspective), incorporating the different cultures and managerial styles at lower levels is much more difficult.

German top managers may rely on a 50-page report for discussion and decision making, while Americans prefer one-to-one communication. Below the board level, subordinates typically research an issue and present it to their German boss, who usually accepts the recommendation. American managers, on the other hand, frequently accept the report and file it away, which frustrates German subordinates. Also, Chrysler designers are frustrated with not being involved in the design of Mercedes cars. Although there are at this time two headquarters (Detroit and Stuttgart), a top manager predicted that in the near future there would be only one—in Germany.

Both the Americans and Germans can learn from each other. Germans need to write shorter reports, be more flexible, reduce bureaucracy, and speed up managerial decision making. American managers, on the other hand, hope to learn discipline from the Germans. As one Chrysler employee said: "One of the real benefits to us is instilling some discipline that we know we needed but weren't able to inflict on ourselves."[19]

This employee seemed to have been right because in 2001 Chrysler needed a dramatic shakeup. External threats had increased and the internal environment needed an overall revamp. Externally, demand for the very profitable Chrysler minivans and SUVs dropped, partly because of the slowing economies in the United States and Europe and partly because of increased competition from Toyota, Honda, and Volkswagen. Internally, the past extravagant spending became a drain on Chrysler's resources as well as on the DaimlerChrysler Corporation. To solve the internal problems, Dieter Zetsche from Mercedes took control at Auburn Hills in the United States. In his analysis of the situation, he noted that assumptions underlying the plans were incorrect. Perhaps even more important, the plans lacked proper assessments of Chrysler's strengths and weaknesses.[20] With Zetsche focusing on Chrysler's operation and Schrempp on the overall strategy of DaimlerChrysler, will the merger finally live up to its promise? That is the question!

Questions

1. Evaluate the formulation of the merger between Daimler and Chrysler. Discuss the strategic fit and the different product lines.
2. Assess the international perspectives of Eaton and Schrempp.
3. What are the difficulties in merging the organization cultures of the two companies?
4. What is the probability of success or failure of the merger? What other mergers do you foresee in the car industry?
5. Conduct library and Internet research to assess whether the DaimlerChrysler strategy shown in Figure C2-4 was successful. If not, what hindered the implementation of the strategy?

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Part - 3

Organizing

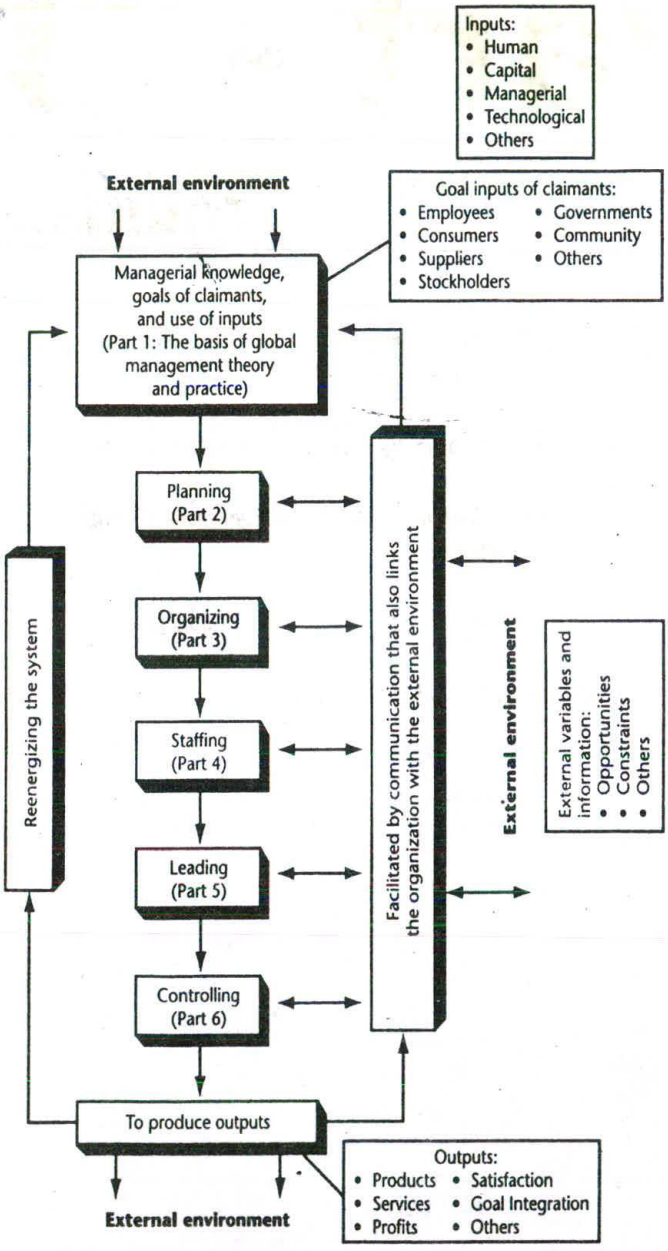
Chapter 7 The Nature of Organizing, Entrepreneuring, and Reengineering

Chapter 8 Organization Structure: Departmentation

Chapter 9 Line/Staff Authority, Empowerment, and Decentralization

Chapter 10 Effective Organizing and Organization Culture

Part 3 Closing Global Organizing



Systems approach to management

Chapter - 7

The Nature of Organizing, Entrepreneuring, and Reengineering

CHAPTER OBJECTIVES

After studying this chapter, you should be able to:

1. Realize that the purpose of an organization structure is to establish a formal system of roles.
2. Understand the meaning of *organizing* and *organization*.
3. Draw a distinction between formal and informal organization.
4. Show how organization structures and their levels are due to the limitation of the span of management.
5. Recognize that the exact number of people a manager can effectively supervise depends on a number of underlying variables and situations.
6. Describe the nature of entrepreneuring and intrapreneuring.
7. Understand the key aspects and limitations of reengineering.
8. Demonstrate the logic of organizing and its relationship to other managerial functions.
9. Appreciate that organizing requires taking situations into account.

It is often said that good people can make any organization structure work. Some people even assert that vagueness in organization is a good thing in that it forces teamwork, since people know that they must cooperate to get anything done. However, there can be no doubt that good people and those who want to cooperate will work together most effectively if they know the parts they are to play in any team operation and the way their roles relate to one another. This is as true in business or government as it is in football or in a symphony orchestra. Designing and maintaining these systems of roles is basically the managerial function of organizing.

For an **organizational role** to exist and be meaningful to people, it must incorporate (1) verifiable objectives, which, as indicated in Part 2, are a major part of planning; (2) a clear idea of the major duties or activities involved; and (3) an understood area of discretion or authority so that the person filling the role knows what he or she can do to accomplish goals. In addition, to make a role work out effectively, provision should be made for supplying needed information and other tools necessary for performance in that role.

It is in this sense that we think of **organizing** as:

- the identification and classification of required activities
- the grouping of activities necessary to attain objectives
- the assignment of each group to a manager with the authority (delegation) necessary to supervise it
- the provision for coordination horizontally (on the same or a similar organizational level) and vertically (e.g., between corporate headquarters, division, and department) in the organization structure

An organization structure should be designed to clarify who is to do what tasks and who is responsible for what results in order to remove obstacles to performance caused by confusion and uncertainty of assignment and to furnish decision-making and communication networks reflecting and supporting enterprise objectives.

Organization is a word many people use loosely. Some would say it includes all the behaviors of all participants. Others would equate it with the total system of social and cultural relationships. Still others refer to an

Organization A formalized intentional structure of roles or positions.

enterprise, such as the United States Steel Corporation or the Department of Defense, as an organization. But for most practicing managers, the term **organization** implies a formalized intentional structure of roles or positions. In this book, the term is generally used in reference to a formalized structure of roles, although it is sometimes used to denote an enterprise.

What does *intentional structure of roles* mean? In the first place, as already implied in the definition of the nature and content of organizational roles, people working together must fill certain roles. In the second place, the roles people are asked to fill should be intentionally designed to ensure that required activities are done and that activities fit together so that people can work smoothly, effectively, and efficiently in groups. Certainly, most managers believe they are organizing when they establish such an intentional structure.

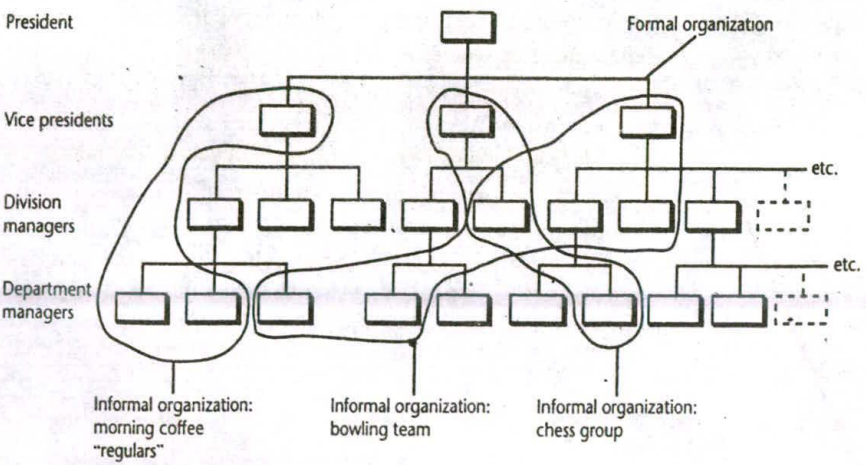
Formal and Informal Organization

Many writers on management distinguish between formal and informal organization. Both types are found in organizations, as shown in Figure 7-1. Let us look at them in more detail.

Formal Organization

In this book, generally, **formal organization** means the intentional structure of roles in a formally organized enterprise. Describing an

FIGURE 7-1 Formal and informal organization



Formal organization The intentional structure of roles in a formally organized enterprise.

organization as formal, however, does not mean there is anything inherently inflexible or unduly confining about it. If a manager is to organize well, the structure must furnish an environment in which individual performance, both present and future, contributes most effectively to group goals.

A formal organization must be flexible. There should be room for discretion, for beneficial utilization of creative talents, and for recognition of individual likes and capacities in the most formal of organizations. Yet individual effort in a group situation must be channeled toward group and organizational goals.

Informal Organization

Informal organization A network of interpersonal relationships that arise when people associate with each other.

Chester Barnard, author of the management classic *The Functions of the Executive*, described an informal organization as any joint personal activity without conscious joint purpose, although contributing to joint results.[1] It is much easier to ask for help on an organizational problem from someone you know personally, even if he or she may be in a different department, than from someone you know only as a name on an organization chart. The **informal organization** is a network of interpersonal relationships that arise when people associate with each other. Thus, informal organizations—relationships not appearing on an organization chart—might include the machine shop group, the sixth floor crowd, the Friday evening bowling gang, and the morning coffee "regulars."[2]

Organizational Division: The Department

Department A distinct area, division, or branch of an organization over which a manager has authority for the performance of specified activities.

One aspect of organizing is the establishment of departments. The word **department** designates a distinct area, division, or branch of an organization over which a manager has authority for the performance of specified activities. A department, as the term is generally used, may be the production division, the sales department, the West Coast branch, the market research section, or the accounts receivable unit. In some enterprises, departmental terminology is loosely applied; in others, especially large ones, a stricter terminology indicates hierarchical relationships. Thus, a vice president may head a division; a director, a department; a manager, a branch; and a chief, a section.

Organizational Levels and the Span of Management*

While the purpose of organizing is to make human cooperation effective, the reason for levels of organization is the limitation of the span of management. In other words, organizational levels exist because there is a limit to the number of persons a manager can supervise effectively, even though this limit varies depending on situations. The relationships between the span of management and organizational levels are shown in Figure 7-2. A wide span of management is associated with few organizational levels; a narrow span, with many levels.

Problems with Organizational Levels

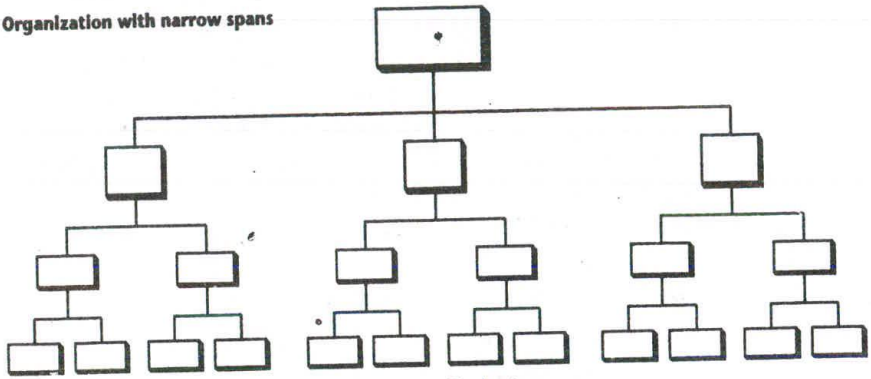
There is a tendency to regard organization and departmentation as ends in themselves and to gauge the effectiveness of organization structures in terms of clarity and completeness of departments and departmental levels. The division of activities into departments and the creation of multiple levels are not completely desirable in themselves.

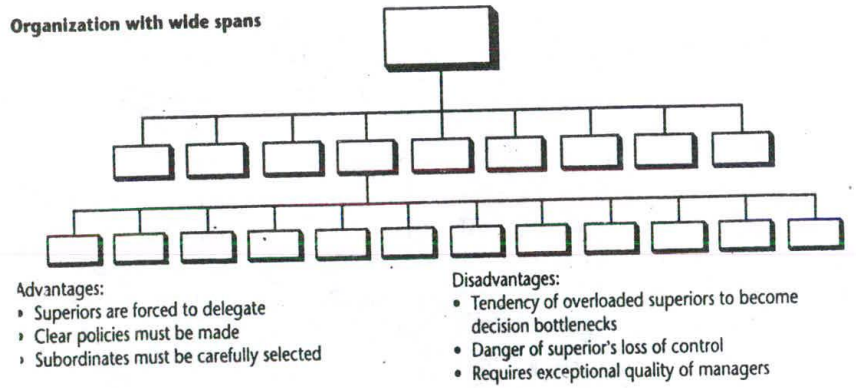
In the first place, levels are expensive. As they increase, more and more effort and money are devoted to managing because of the additional managers, the staff to assist them, and the necessity of coordinating departmental activities, as well as the cost of facilities for the personnel. Accountants refer to such costs as overhead, burden, or general and administrative, in contrast to so-called direct costs. Real production is accomplished by factory, engineering, or sales employees, who are, or could logically be accounted for as, "direct labor." Levels above the "firing line" are predominantly staffed with managers whose costs it would be desirable to eliminate, if that were possible.

In the second place, departmental levels complicate communication. An enterprise with many levels has greater difficulty communicating objectives, plans, and policies downward through the organization structure than does a firm in which the top manager communicates directly with employees. Omissions and misinterpretations occur as information

* In much of the literature on management, this is referred to as the *span of control*. Despite the widespread use of this term, in this book *span of management* will be used, since the span is one of management and not merely of control, which is only one function of managing.

FIGURE 7-2 Organization structures with narrow and wide spans





passes down the line. Levels also complicate communication from the "firing line" to the commanding superiors, which is every bit as important as downward communication. It has been well said that levels are "filters" of information.

Finally, numerous departments and levels complicate planning and control. A plan that may be definite and complete at the top level loses coordination and clarity as it is subdivided at lower levels. Control becomes more difficult as levels and managers are added; at the same time, the complexities of planning and difficulties of communication make this control more important.

The Operational Management Position: A Situational Approach

Principle of the span of management There is a limit to the number of subordinates a manager can effectively supervise, but the exact number will depend on the impact of underlying factors.

The classical school approach to the span of management deals with specifying the number of subordinates for an effective span. Operational management theorists have taken the position that there are too many underlying variables in a management situation for us to specify any particular number of subordinates that a manager can effectively supervise. Thus, the **principle of the span of management** states that there is a limit to the number of subordinates a manager can effectively supervise, but the exact number will depend on the impact of underlying factors.

In other words, the dominant current guideline is to look for the causes of limited span in individual situations rather than to assume that there is a widely applicable numerical limit. Examining what consumes the time of managers in their handling of superior–subordinate relationships and ascertaining devices that can be used to reduce these time pressures will be not only a helpful approach for determining the best span in individual cases but also a powerful tool for finding out what can be done to extend the span without destroying effective supervision. There can be no argument that the costs of levels of supervision make it highly desirable for every individual manager to have as many subordinates as can be effectively supervised.

Factors Determining an Effective Span

The number of subordinates a manager can effectively manage depends on the impact of underlying factors. Aside from such personal capacities as comprehending quickly, getting along with people, and commanding loyalty and respect, the most important determinant is a manager's ability to reduce the time he or she spends with subordinates. This ability naturally varies with managers and their jobs, but several factors materially influence the number and frequency of such contacts and therefore the span of management, as shown in Table 7-1.

Need for Balance

There can be no doubt that, despite the desirability of a flat organization structure, the span of management is limited by real and important restrictions. Managers may have more subordinates than they can manage effectively, even though they delegate authority, conduct training, formulate clear plans and policies, and adopt efficient control and communication techniques. It is equally true that, as an enterprise grows,

TABLE 7-1 Factors influencing the span of management

Narrow spans (a great deal of time spent with subordinates)	Wide spans (very little time spent with subordinates)
• Little or no training of subordinates	• Thorough training of subordinates
• Inadequate or unclear authority delegation	• Clear delegation and well-defined tasks
• Unclear plans for nonrepetitive operations	• Well-defined plans for repetitive operations
• Nonverifiable objectives and standards	• Verifiable objectives used as standards
• Fast changes in external and internal environments	• Slow changes in external and internal environments
• Use of poor or inappropriate communication techniques, including vague instructions	• Use of appropriate techniques, such as proper organization structure and written and oral communication
• Ineffective interaction of superior and subordinate	• Effective interaction between superior and subordinate
• Ineffective meetings	• Effective meetings
• Greater number of specialties at lower and middle levels	• Greater number of specialties at upper levels (top managers concerned with external environment)
• Incompetent and untrained manager	• Competent and trained manager
• Complex task	• Simple task
• Subordinates' unwillingness to assume responsibility and reasonable risks	• Subordinates' willingness to assume responsibility and reasonable risks
• Immature subordinates	• Mature subordinates

limitations of the span of management force an increase in the number of levels simply because there are more people to supervise.

What is required is more precise balancing, in a given situation, of all pertinent factors. Widening spans and reducing the number of levels may be the answer in some cases; the reverse may be true in others. One must balance all the costs of adopting one course or the other, not only the financial costs but also costs in morale, personal development, and attainment of enterprise objectives. In a military organization, perhaps the attainment of objectives quickly and without error would be most important. On the other hand, in a department store operation, the long-run objective of profit may be best served by forcing initiative and personal development at the lower levels of the organization.

An Organizational Environment for Entrepreneuring and Intrapreneuring[3]

At times, special organizational arrangements need to be made for fostering and utilizing entrepreneurship. Frequently, entrepreneurship is thought

to apply to managing small businesses, but some authors expand the concept to large organizations and to managers carrying out entrepreneurial roles through which they initiate changes to take advantage of opportunities. Although it is common to look for the "entrepreneurial personality" in people, Peter Drucker suggests that this search might not be successful.[4] Instead, one should look for a commitment to systematic innovation, which is a specific activity of entrepreneurs. The essence of entrepreneurship is innovation, that is, goal-oriented change to utilize the enterprise's potential. As entrepreneurs, managers try to improve the situation.

The Intrapreneur and the Entrepreneur

Intrapreneur A person who focuses on innovation and creativity and who transforms a dream or an idea into a profitable venture by operating within the organizational environment.

Entrepreneur A person who does similar things as the intrapreneur, but outside the organizational setting.

Gifford Pinchot makes a distinction between the intrapreneur and the entrepreneur.[5] Specifically, an **intrapreneur** is a person who focuses on innovation and creativity and who transforms a dream or an idea into a profitable venture by operating *within* the organizational environment. In contrast, the **entrepreneur** is a person who does similar things, but *outside* the organizational setting. Entrepreneurs have the ability to see an opportunity, obtain the necessary capital, labor and other inputs, and then put together an operation successfully. They are willing to take personal risk of success and failure. Other authors do not make the distinction between entrepreneur and intrapreneur. In this book, the term *entrepreneur* designates an enterprising person working either within or outside the organization.

Creating an Environment for Entrepreneurship

www.intrapreneur.com
www.entrepreneur.com

Since it is a managerial responsibility to create an environment for effective and efficient achievement of group goals, managers must promote opportunities for entrepreneurs to utilize their potential for innovation. Entrepreneurs take personal risks in initiating change, and they expect to be rewarded for it. The taking of reasonable risk will at times result in failure, but this must be tolerated. Finally, entrepreneurs need some degree of freedom to pursue their ideas; this in turn requires that sufficient authority be delegated. The personal risks for entrepreneurs who have their own business are of a different kind, and failure may mean bankruptcy.

Innovative persons often have ideas that are contrary to "conventional wisdom." It is quite common that these individuals are not well liked by their colleagues, and their contributions are often not sufficiently appreciated. It is therefore not surprising that entrepreneurs leave large

www.hp.com
www.apple.com
www.3m.com

companies and start their own business. When Steve Wozniak could not get his dream of building a small computer fulfilled at Hewlett-Packard, he left that prestigious firm to form—together with another entrepreneur, Steve Jobs—Apple Computer. Progressive companies, such as 3M, consciously try to develop an organizational environment that promotes entrepreneurship within the company.

www.wharton.upenn.edu

Becoming an entrepreneur is fashionable. Several universities teach entrepreneurship. The Wharton School in Philadelphia even has an entrepreneurial center. Some people do not want to work for a big company; they want to be their own boss and live the life they want. Other people lose their job (especially those working for dot-com companies) and decide to start their own business. Some companies even provide support so that these new firms could become suppliers. Women seem to be attracted to entrepreneurship. Feeling discriminated at the workplace, some go out on their own. Important requirements for becoming an entrepreneur are self-confidence, a willingness to work hard, experience with the product, a good general education, and some money to start.

International Perspective

What Is in Your Future?[6]

Harvard professor John P. Kotter in his book *The New Rules: How to Succeed in Today's Post-Corporate World* surveyed the careers of 115 Harvard business graduates of 1974. Some of the findings are surprising. Many of the graduates left big businesses and joined smaller companies. Some who started in large firms switched to smaller firms. They felt that large companies were not open to their creative ideas for change, nor were they receptive to radical changes. In short, traditional big business firms may be stultifying people with new ideas. Kotter suggests that those with unconventional ideas often succeed. In the rapidly changing environment, managers must search for new opportunities, but they must also avoid the hazards.

Small, entrepreneurial firms often present more opportunity for advancement, are more open to ambiguous situations, and provide the environment for exerting influence. Although many of the Harvard graduates surveyed preferred smaller firms, they may be connected to large firms as consultants, distributors, suppliers, financiers, or other roles.

What then are some of the implications for managers in carrying out managerial functions? Planning needs to be done in a less bureaucratic manner. A frequent scanning of the environment and a rapid response to changes are

essential. Small companies, with a smaller hierarchical structure than large firms, may be more willing to change. With respect to staffing, graduates may want to explore the opportunities in smaller companies. The Harvard graduates who worked for small companies were not only better rewarded financially than those in large firms, but they were also rewarded through job satisfaction.

Innovation and Entrepreneurship[7]

When talking about innovation and entrepreneurship, one thinks immediately of the success stories of people such as Steve Jobs of Apple Computer and Ross Perot of Electronic Data Processing (which was later acquired by General Motors). It may be an appealing thought to get rich and get rich fast, often by establishing new companies. Entrepreneurs have creative ideas; they use their management skills and resources to meet identifiable needs in the marketplace. If successful, an entrepreneur can become wealthy.

Peter Drucker suggests that innovation applies not only to high-tech companies but equally to low-tech, established businesses. Worthwhile innovation is not a matter of sheer luck; it requires systematic and rational work, well organized and managed for results.

What does entrepreneurship imply? It suggests dissatisfaction with how things are and an awareness of a need to do things differently. Innovation comes about because of some of the following situations:

- An unexpected event, failure, or success
- An incongruity between what is assumed and what really is
- A process or task that needs improvement
- Changes in the market or industry structure
- Changes in demographics
- Changes in meaning or in the way things are perceived
- Newly acquired knowledge

www.ge.com

Innovations based solely on bright ideas may be very risky and at times are not successful. General Electric's ambitious plans for the "factory of the future" may have been a costly mistake. These plans may have been based on unrealistic forecasts and unrealistic expectations for automating industry. The concept of the new factory expressed the wish of the chairperson, who wanted to promote entrepreneurship in an organization that was known to be highly structured.

The most successful innovations are often the mundane ones. Take the Japanese, who make minor innovations (e.g., providing little conveniences

that customers like) in their cars or in their electronic equipment. Research has shown that successful large companies listen carefully to the needs of their customers. They establish teams that search for creative alternatives to serve their customers—but within a limiting framework and with clear goals in mind.



Post-it Note Pads[8]

Even in companies with a policy of promoting entrepreneurship and innovation, the development of new products requires perseverance in transforming an idea into reality.

Art Fry was singing in a church choir. The bookmarks placed in his hymnal fell out after the first church service, making it difficult to find the relevant pages for the second service. The need was clear: an adhesive paper slip that could be easily removed without damaging the page. However, developing an adhesive with the right degree of stickiness was not an easy task. 3M, where Art Fry worked, was known for products with great adhesion. For Art's purpose, however, a material was needed that not only provides sufficient adhesion but also allows easy removal. The 3M laboratory did not provide much help in the research and development of such a product. Nor did the marketing department think a great deal of this idea. But being an inventor as well as an innovator, Art Fry pursued his goal with great perseverance. The result was the Post-it note pad, which turned out to be a very profitable product for 3M.

Reengineering the Organization[9]

Some time ago, a managerial concept called reengineering entered management literature. It is sometimes called "starting over" because Michael Hammer and James Champy, who popularized the concept, suggested that one asks this question: "If I were recreating this company today (from scratch), knowing what I know now and given current technology, what would it look like?"[10]

More specifically, Hammer and Champy define reengineering as "the *fundamental* rethinking and *radical* redesign of business *processes* to achieve *dramatic* improvements in critical contemporary measures of performance, such as cost, quality, service, and speed."[11] The words in italics are considered key aspects by the authors.

Key Aspects of Reengineering

Let us briefly consider these key aspects. First, hardly anyone would disagree on the need for a *fundamental rethinking* of what the organization is doing and why. One of the authors, while working as a systems analyst, found that systems and procedures were often outdated, inefficient, and completely unnecessary. Seldom did systems users question why the procedures were necessary and the purpose they served. So a fresh look, especially by a "systems outsider," can indeed reveal many inefficiencies. New thinking about management may provide a new perspective at what is being done and why.

The second key aspect in the definition is *radical redesign* of the business processes. In the original publication, the authors suggested that "radical" meant precisely that—not a modification but a reinvention. They also suggested that this is the most important aspect of their approach. Hammer and Champy, in a later paperback edition of the book, admit that they may have been wrong in suggesting that the most important key aspect is radical redesign.[12] Radical redesign often results in radical downsizing with detrimental effects to organizations.

Downsizing or "rightsizing" is not the primary purpose of reengineering, although in many cases it does result in fewer people being needed. Unfortunately, reengineering has primarily been used in a reactive way by managers intent on reducing costs, without necessarily addressing customer needs and expectations. Another result of radical redesigning is a business system based primarily on the engineering model without due considerations given to the human system. While radical redesign, accompanied by downsizing, may indeed result in short-term cost savings, it may also negatively affect the remaining work force. Teamwork has become increasingly important in the modern organization. But team efforts are built on trust, and trust has to be built over a long period of time. With radical redesign, trust can be destroyed.

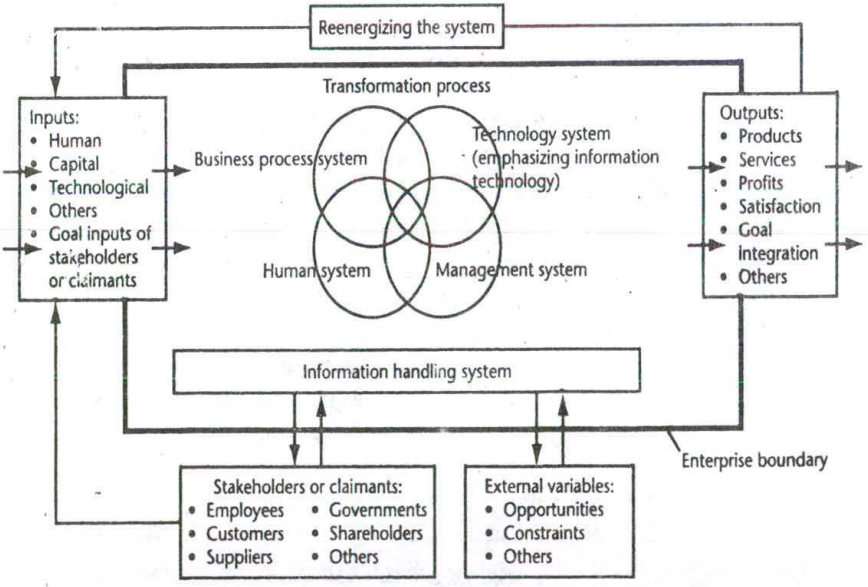
The third key term calls for *dramatic results*. Examples are often given to support this key aspect in the definition of reengineering that calls for dramatic improvements. Union Carbide cut $400 million from its fixed costs in three years. GTE, the Baby Bell telephone company, developed one-stop shopping; customers, who once had to deal with various departments, can now deal with one person, or they can connect directly with the department providing the specific service sought. But dramatic improvements are moderated by failures. Hammer and Champy admit

that "some 50 to 70 percent of reengineering efforts fail to deliver the intended dramatic results."[13]

The fourth key word in the reengineering definition is *processes*. The need for carefully analyzing and questioning business processes is indeed important. However, the process analysis must go beyond operations and must include the analysis and integration of technical systems, human systems, and the total management process including the linkage of the enterprise to the external environment. Engineers may focus on the business process; but to be truly effective, the various subsystems need to be integrated into a total system, as shown in Figure 7-3. The model indicates that the process of transforming the inputs into outputs must go beyond the business process system (the focus of reengineering) to include technological and human aspects, and indeed the total managerial system.

Despite the limitations, reengineering can be a powerful tool; but it is still only a tool. We suggest integrating reengineering with other systems through a new systems model called management by processes[14] to overcome some of the weaknesses of the narrowly focused reengineering approach.

FIGURE 7-3 Management by processes



The Structure and Process of Organizing

Looking at organizing as a process requires that several fundamentals be considered. In the first place, the structure must reflect objectives and plans because activities derive from them. In the second place, it must reflect the authority available to an enterprise's management. Authority in a given organization is a socially determined right to exercise discretion; as such, it is subject to change.

In the third place, an organization structure, like any plan, must reflect its environment. Just as the premises of a plan may be economic, technological, political, social, or ethical, so may be those of an organization structure. It must be designed to work, to permit contributions by members of a group, and to help people achieve objectives efficiently in a changing future. In this sense, a workable organization structure can never be static. There is no single organization structure that works best in all kinds of situations: an effective organization structure depends on the situation.

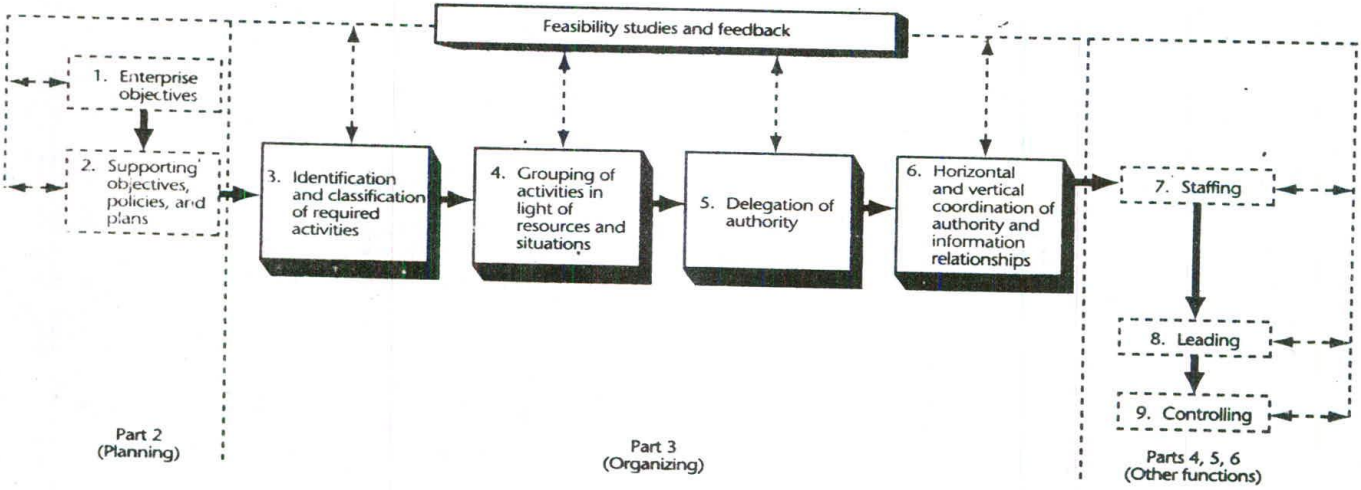
In the fourth place, since the organization is staffed with people, the grouping of activities and the authority relationships of an organization structure must take into account people's limitations and customs. This is not to say that the structure must be designed around individuals instead of around goals and accompanying activities. But an important consideration is the kinds of people who are to staff it.

The Logic of Organizing

There is a fundamental logic to organizing, as shown in Figure 7-4. The organizing process consists of the following six steps, although steps 1 and 2 are actually part of planning:

1. Establishing enterprise objectives
2. Formulating supporting objectives, policies, and plans
3. Identifying, analyzing, and classifying the activities necessary to accomplish these objectives
4. Grouping these activities in light of the human and material resources available and the best way, under the circumstances, of using them
5. Delegating to the head of each group the authority necessary to perform the activities
6. Tying the groups together horizontally and vertically, through authority relationships and information flows

FIGURE 7-4 The organizing process



Some Misconceptions

Organizing does not imply any extreme occupational specialization, which in many instances makes work uninteresting, tedious, and unduly restrictive. There is nothing in organization itself that dictates this. To say that tasks should be specific is not to say they must be limited and mechanical. In any organization, jobs can be defined to allow little or no personal leeway or, conversely, the widest possible discretion. One must not forget that there is no best way to organize and that the application of structural organization theory must take into account the situation.

Basic Questions for Effective Organizing

It is useful to analyze the managerial function of organizing by raising and answering the following questions:

- What determines the span of management and hence the levels of organization? (answered in this chapter)
- What determines the basic framework of departmentation, and what are the strengths and weaknesses of the basic forms? (answered in Chapter 8)
- What kinds of authority relationships exist in organizations? (answered in Chapter 9)
- How should authority be dispersed throughout the organization structure, and what determines the extent of this dispersion? (answered in Chapter 9)
- How should the manager make organization theory work in practice? (answered in Chapter 10)

The answers to these questions form a basis for a theory of organizing. When considered along with similar analyses of planning, staffing, leading, and controlling, they constitute an operational approach to management.

Summary

The term *organization* is often used loosely. Formal organization is the intentional structure of roles. Informal organization is a network of personal and social relations neither established nor required by formal authority but arising spontaneously. The span of management refers to the number of people a manager can effectively supervise. A wide span of management results in few organizational levels, and a narrow span results in many levels. There is no definite number of people a manager can always effectively supervise; the number depends on several underlying factors.

These include the degree of training of subordinates that is required and is possessed, the clarity of authority delegation, the clarity of plans, the use of objective standards, the rate of change, the effectiveness of communication techniques, the amount of personal contact needed, and the level in the organization.

Intrapreneurs and entrepreneurs focus on innovation and creativity. It is the manager's responsibility to create an environment that promotes entrepreneurship.

Reengineering that may require a redesign of business processes has become popular in some companies. The results of these efforts have shown positive but also some negative results.

The steps in organizing include formulating objectives and supporting objectives, policies, and plans to achieve the ends (strictly speaking, this is carried out in planning); identifying and classifying activities; grouping these activities; delegating authority; and coordinating authority as well as information relationships.

KEY IDEAS AND CONCEPTS FOR REVIEW

Organizational role
Organizing
Formal organization
Informal organization
Department
Principle of the span of management
Factors determining the span of management
Entrepreneuring and intrapreneuring
Innovation and entrepreneurship
Reengineering, key aspects
Logical steps of organizing
Basic questions for effective organizing

FOR DISCUSSION

1. Since the positions in an organization must be occupied by people, and since an effective organization depends on people, it is often said that the best organization arises when a manager hires good people and lets them do their jobs in their own way. Comment.
2. A formal organization is often conceived of as a communication system. Is it? How?
3. Construct a diagram depicting the formal organization of an enterprise or activity with which you are familiar. How does this organization chart help or hinder the establishment of an environment for performance?
4. Using the same enterprise or activity as in question 3, chart its informal organization. Does it help or hinder the formal organization? Why?
5. When you become a manager, what criteria will you favor to determine your span of management?

EXERCISES/ACTION STEPS

1. Organize a family picnic using the steps suggested in this chapter.
2. Interview a manager in your community and ask him or her how many subordinates he or she has. Are different numbers of subordinates supervised at the top, the middle, and the bottom of the organizational hierarchy? What really determines the span of management in this organization? Do you think the span is appropriate for the enterprise?

INTERNET RESEARCH

Use a search engine and type "post-it-notes" to find out more about the yellow stickers that have been very profitable for 3M.

International Case

Reengineering the Business Process at Procter & Gamble[15]

Procter & Gamble (P&G), a multinational corporation known for products such as diapers, shampoo, soap, and toothpaste, was committed to improving value to the customer. Its products were sold through various channels, such as grocery retailers, wholesalers, mass merchandisers, and club stores. The flow of goods in the retail grocery channel was from the factory's warehouse to the distributors' warehouses before going to the grocery stores where customers selected the merchandise from the shelves.

The improvement-driven company was not satisfied with its performance and developed a variety of programs to improve its service and the efficiency of its operation. One such program was electronic data interchange, which provided daily information from the retail stores to P&G. The installation of the system resulted in better service, reduced inventory levels, and labor-cost savings. Another approach, the continuous replenishment program, provided additional benefits for P&G as well as for its retailer customers. Eventually, the entire ordering system was redesigned, with the result of dramatic performance improvements.

The reengineering efforts also required restructuring of the organization. P&G had been known for its brand management for more than 50 years. But in the late 1980s and early 1990s, the brand management approach pioneered by the company in the 1930s required rethinking and restructuring. In a drive to improve efficiency and coordination, several brands were combined with authority and responsibility given to category managers. Such a manager would determine overall pricing and product policies. Moreover, the category managers had the authority to withdraw weak brands, thus avoiding conflict between similar brands. They were also held responsible for the profit of the product category they were managing. The switch to category management required not only new skills but also a new attitude.

Questions

1. The reengineering efforts of P&G focused on the business process system. Do you think other processes, such as the human system, or other managerial policies need to be considered in a process redesign?
2. What do you think was the reaction of the brand managers, who may have worked under the old system for many years, when the category management structure was installed?
3. As a consultant, would you have recommended a top-down or a bottom-up approach, or both, to process redesign and organizational change? What are the advantages and disadvantages of each approach?

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