Organizational Theory, Design, and Change

Seventh Edition

Gareth R. Jones

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Organizational Theory, Design, and Change

SEVENTH EDITION
GLOBAL EDITION

Gareth R. Jones
Texas A&M University

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For Nicholas and Julia

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Preface

In the seventh edition of *Organizational Theory, Design, and Change*, I have kept to my theme of providing students with the most contemporary and up-to-date account of how the changing environment affects the way managers design and change organizational structure to increase organizational effectiveness. In revising my book, I have continued to focus on making the text relevant and interesting to students so it engages and encourages them to make the effort necessary to assimilate the text material—material being used every day by managers and consultants who are working to improve organizational performance. I have continued to mirror the changes taking place in the way organizations deal with their environments, such as the increasing use of outsourcing and the use of information technology, by incorporating recent developments in organizational theory and research into the text. Also, I have worked to provide vivid, current examples of the way managers of companies large and small have responded to such changes.

New to This Edition

- Over 65% of the in-chapter boxes and 90% of the closing cases are new and the rest have been updated.
- New material on the changing nature of problems involved in managing functional, product, and divisional structures and ways IT can be used to improve their performance.
- New material on the strategy–structure relationship, and new coverage about the reasons companies need to continuously examine and change their global strategies and structures.
- New material on online software development and craftswork technology and its importance in the growing services area.
- Expanded discussion of how to manage technology to create successful virtual organizational structures, such as those used by Accenture and PeopleSoft.
- A major focus is the recent ongoing changes in the mobile computing, smartphone, and software applications and the consequent effects on the changes in the competitive environment and the way companies have been changing their structures and control systems to manage these issues.
- Increased coverage of ethical issues involved in the stakeholder approach to organizations and their implications for organizational effectiveness, such as new "green" environmental coverage, and new coverage of disasters such as the BP oil spill, ethics in health care, and fraud in disguising the quality and price of goods and services.
- Explanations of the most recent developments in organizational structure, such as the product team structure, outsourcing, and network organizations because of advancements in IT.

The number and complexity of the strategic and organizational challenges confronting managers because of the changing global environment has continued to increase in the 2000s. In most companies, managers at all levels are playing catch-up as they work toward meeting these challenges by implementing new forms of organizational structure and by changing their existing structures, using the techniques and practices described in this book. Today, relatively small differences in performance between companies—the speed at which they can bring new products to market, for example, or in the way they choose to motivate their employees to find ways to increase effectiveness—can give one organization a significant competitive advantage over another. Managers and companies that use established organizational theory and design principles to change the way they operate can increase their effectiveness over time.

This is clearly evident by the way companies are continuously changing and reorganizing how they operate—at the functional, divisional, organizational, and global levels—to better compete and manage the ever-changing environment in the 2010s. Of course, the recession that began in the later 2000s, as well as continuously changing technological and economic conditions, offer new opportunities for agile companies that can adapt to meet these challenges while threatening the survival of those that cannot. Nowhere is this clearer than in the developing markets for mobile computing devices such as smartphones and tablet computers, where the performance of some companies like Apple and Samsung have soared, while those of others such as Motorola, Blackberry, and Dell have plunged.

Across all functions and levels, managers and employees must continuously search out ways to change organizational design to "work smarter" and increase performance. The challenges facing managers continue to mount as changing global forces such as increasing global outsourcing, rising commodity prices, and the emergence of new low-cost overseas competitors impact organizations large and small. Moreover, the revolution in information technology (IT) has transformed the way managers make decisions across all levels of an organization's hierarchy and across all of its functions and global divisions—and the rate of change in IT is accelerating.

The accelerated change in IT is changing the way organizations operate from top to bottom, a theme that has been extended and updated in the seventh edition. In today's world of video downloading, streaming media, text messaging, and tweeting without the use of any one type of mobile computing device, there is a need to understand how this affects organizational structure. The new edition offers up-to-date coverage of these issues throughout, peppered with examples that highlight the significant ways that advances in IT affect organizational decision making, change, and structure. For example, one issue covered in more depth is the pros and cons of global outsourcing and the new organizational problems that emerge when thousands of functional jobs in IT, customer service, and manufacturing are now being performed in countries overseas.

Encouraged by the increasing number of instructors and students who are using *Organizational Theory* with each new edition, and based on the reactions and suggestions of both users and reviewers, I have revised and updated the text in the following ways. First, just as pertinent new research concepts have been added to each chapter, outdated ideas and concepts have been omitted. As usual, my goal is to streamline the text content so students can avoid having to assimilate excessive material. Second, I am happy that the current content and arrangement of the chapters continues to be favorably received by its users. The organization of the book offers instructors many more hands-on ways in which they can help students to appreciate the power that people have over organizations to increase their effectiveness. As one student from New York City informed me in an email, "The book has given me a new vocabulary to understand the organization I work for and provided the conceptual tools needed to analyze and change it."

By bringing a discussion of organizational change and renewal to the center stage of organizational theory and design, this book stands alone. The organizational theory concepts the text describes are the same ones that firms of management consultants, chief operating officers, and the increasing number of managers responsible for organizational design and change use as they perform their roles and jobs.

Seventh Edition Content

The organization of the chapters in this edition is unchanged. Many textbooks lack a tight, integrated flow of topics from chapter to chapter. In this book, students will see beginning in Chapter 1 how the book's topics are related to one another. Integration has been achieved by organizing the material so that each chapter builds on the material of the previous chapters in a logical fashion. I also accomplish integration by focusing on one company, Amazon.com, and in several of the book's chapters I use boxed examples of this company, all of which have been updated, to illustrate organizational design and change issues.

Chapter 2, "Stakeholders, Managers, and Ethics," has proved to be popular, highlighting as it does the ethical issues that confront managers who seek to serve the interests of multiple stakeholders. I have expanded coverage of ethical issues in this edition in many chapters, offering more discussion and examples of all kinds of organizations—for-profit and nonprofit—that have benefited by the increased use of control systems to monitor their managers and their decision making. "The Ethical Dimension" exercise added to the "Organizational Theory in Action" section at the end of each chapter has also proved to be popular. Today, as corporate scandals proliferate, particularly insider trading and organizations created to defraud customers in the 2010s, it is important to ask students to think about and debate the ethical issues involved in organizational design and change.

A Focus on Managers

The managerial implications of organizational design and change are clearly articulated for the needs of students. Each chapter has one or more managerial summaries, in which the practical implications of organizational theories and concepts are clearly outlined. In addition, each chapter has several "Organizational Insight" boxes in which the experiences of a real company are tied to the chapter content to highlight the implications of the material. Each chapter also features two closing cases that allow a hands-on analysis by students.

Learning Features and Support Material

Each chapter ends with a section entitled "Organizational Theory in Action," which includes the following hands-on learning exercises/assignments:

- "Practicing Organizational Theory," which is an experiential exercise designed to give students hands-on experience doing organizational theory. Each exercise takes about 20 minutes of class time. The exercises have been class tested and work very well. Further details on how to use them can be found in the instructor's manual.
- An "Ethical Dimension" feature, where students individually or in groups can debate the ethical dilemmas that confront managers during the process of organizational design and change.
- A "Making the Connection" feature, where students collect examples of companies to illustrate organizational design and change issues.
- An ongoing "Analyzing the Organization" feature, where students select an organization to study and then complete chapter assignments that lead to an organizational theory analysis and a written case study of their organization. This case study is then presented to the class at the end of the semester. Complete details concerning the use of this and the other learning features are in the instructor's manual.
- A closing "Case for Analysis" with questions, which provides an opportunity for a short class discussion of a chapter-related theme.

In addition to these hands-on learning exercises, I have refined or added to the other learning features developed for previous editions of the book:

- Cases. At the end of the book are numerous cases to be used in conjunction with the book's chapters to enrich students' understanding of organizational theory concepts. Most cases are classical, in the sense that the issues they raise are always pertinent and provide a good learning experience for students. To preserve the teaching value of these cases, they should *not* be used for student write-ups; their value lies in the in-class discussion they generate. I have written detailed instructor notes for these cases to show how I use them in my course in organizational theory. These notes are found in the Instructor's Manual.
- "Organizational Insight" boxes relate directly to core chapter concepts.
- Chapter objectives and key terms are clearly defined and listed to aid learning.

- "Managerial Implications" sections provide students with lessons from organizational theory.
- Detailed end-of-chapter summaries facilitate learning.

Instructor Supplements

Instructors can access downloadable supplemental resources by signing in to the Instructor Resource Center at www.pearsonglobaleditions.com/jones.

It gets better. Once you register, you will not have additional forms to fill out or multiple user names and passwords to remember to access new titles and/or editions. As a registered faculty member, you can log in directly to download resource files and receive immediate access.

Need help? Our dedicated Technical Support team is ready to assist instructors with questions about the media supplements that accompany this text. Visit http://247pearsoned.custhelp.com/ for answers to frequently asked questions and toll-free user support phone numbers. The following supplements are available to adopting instructors.

PowerPoints: This presentation includes basic outlines and key points from each chapter. It includes figures from the text but no forms of rich media, which makes the file size manageable and easier to share online or via email. This set was also designed for the professor who prefers to customize PowerPoints and who wants to be spared from having to strip out animation, embedded files, and other media-rich features.

Instructor's Manual: Includes Teaching Objectives, Chapter Summaries, Outlines, Discussion Questions and Answers, Organizational Theory in Action, Cases for Analysis, Analyzing the Organization and Teaching Suggestions, and Ethical Dimensions.

Test Bank: Contains a detailed and comprehensive set of at least 60 multiple-choice questions and 15 true/false questions together with three short-answer and essay questions for each chapter.

Acknowledgments

Finding a way to coordinate and integrate the rich and diverse organizational theory literature is challenging. Nor is it easy to present the material in a way that students can readily understand. Across the last editions of *Organizational Theory*, I have been fortunate to have the assistance of several people who contributed greatly to the book's final form. My developmental editor, Jane Tufts, helped me decide how to present the material in the chapters on structure and culture, which was my most difficult task. Her efforts can be seen in the integrated flow of material both within and between the book's chapters. Brian Mickelson, my Pearson editor, provided me with timely feedback and information from professors and reviewers, which has allowed me to shape the book to meet the needs of its intended market. Ilene Kahn ably coordinated the book's progress through production. Their efforts can be seen in the comprehensiveness of the package of materials that constitutes *Organizational Theory.* I am also grateful to the following reviewers and colleagues who provided me with detailed feedback on the chapters in this and previous editions of the book:

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Part 1
The Organization and Its Environment

CHAPTER 1

Organizations and Organizational Effectiveness

Learning Objectives

Organizations exist in uncertain, changing environments and continually confront new challenges and problems. Managers must find solutions to these challenges and problems if organizations are to survive, prosper, and perform effectively.

After studying this chapter you should be able to:

1. Explain why organizations exist and the purposes they serve.
2. Describe the relationship between organizational theory and organizational design and change and differentiate between organizational structure and culture.
3. Understand how managers can utilize the principles of organizational theory to design and change their organizations to increase organizational effectiveness.
4. Identify the three principal ways in which managers assess and measure organizational effectiveness.
5. Appreciate the way in which several contingency factors influence the design of organizations.

What Is an Organization?

Few things in today's world are as important or as taken for granted as organizations. Although we routinely enjoy the goods and services that organizations provide, we rarely bother to wonder about how these goods and services are produced. We see online videos of manufacturing production lines churning out automobiles, PCs, or smartphones, and we watch on a local TV channel how our schools or hospitals are striving to use advances in new kinds of computer hardware and software, such as online learning programs, to help students improve their performance. Yet we rarely question how or why these organizations go about their business. Most often, we think about organizations only when they fail us in some way—for example, when we are forced to wait two hours in the emergency room to see a doctor, when our new smartphone crashes, or when we are at the end of a long line in a bank on a Friday afternoon. When such events happen, we wonder why the bank did not anticipate the rush of people and put on more tellers, why the hospital made us spend 30 minutes filling out paperwork in order to obtain service and then kept us waiting for an hour and a half, or why wireless phone companies don't insist on higher-quality hardware and bug-free software from their smartphone suppliers.

People have a casual attitude toward organizations because organizations are *intangible.* Even though most people in the world today are born, work, and die in organizations, nobody has ever seen or touched an organization. We see the products or services that an organization provides, and sometimes we see the people the organization employs, for example, as we go into a FedEx Kinko's store or doctor's office. But the reason an organization, such as FedEx Kinko's, is motivated to provide goods and services, and the way it controls and influences its members so that it can provide them, are not apparent to most people outside the organization. Nevertheless, grouping people and other resources to produce goods and services is the essence of organizing and of what an organization does.[1]

Organization
A tool people use to coordinate their actions to obtain something they desire or value.

An **organization** is a tool people use to coordinate their actions to obtain something they desire or value—that is, to achieve their goals. People who value security create an organization called a police force, an army, or a bank. People who value entertainment create organizations such as the Walt Disney Company, CBS, or a local club. People who desire spiritual or emotional support create churches, social service organizations, or charities. An organization is a response to and a means of satisfying some human need. New organizations are spawned when new technologies become available and new needs are discovered—such as social networking sites like Facebook—and organizations die or are transformed when the needs they satisfied are no longer important—such as video rental stores like Blockbuster. The need to invent improved drugs, for example, led to the creation of Amgen, Genentech, and other biotech companies. The need to handle increasing amounts of information and emerging new computer technologies led to the rise of IBM, Apple, Microsoft, Google, and other high-tech companies and the decline and failure of companies whose technology had become outdated, such as the typewriter company Smith Corona. Retail stores such as Walmart, Target, the Gap, and Sears are continually being transformed—not always successfully—as they seek to respond to the changing tastes and needs of consumers.

Entrepreneurship
The process by which people recognize opportunities to satisfy needs and then gather and use resources to meet those needs.

Who creates the organizations that arise to satisfy people's needs? Sometimes an individual or a few people believe they possess the necessary skills and knowledge and set up an organization to produce goods and services. In this way organizations like sandwich shops, Google, and software design studios are created. Sometimes several people form a group to respond to a perceived need by creating an organization. People with a lot of money may invest jointly to build a vacation resort. A group of people with similar beliefs may form a new church, or a nation's citizens may move to establish a new political party. In general, **entrepreneurship** is the term used to describe the process by which people recognize opportunities to satisfy needs and then gather and use resources to meet those needs.[2]

Today, many organizations being founded, and particularly those experiencing the fastest growth, are producing goods and services related in some way to new information

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Most of us don't think about the organizations that produce the products we use until we have a problem with those products.

technology (IT). The increasing use of mobile computing devices such as laptops, smartphones, and tablet computers linked to the World Wide Web (WWW) through wireless broadband connections are revolutionizing the way all organizations operate. This book examines this crucial issue by focusing on one company, Amazon.com, that has achieved explosive growth because of its development of IT products and services such as its Kindle book reader. In nine chapters of this book the story of this company is used to illustrate the many ways in which the IT revolution is improving the way organizations operate and create value today. We begin this analysis here by examining why and how Amazon.com was founded, which is discussed in the Focus on New Information Technology box.[3]

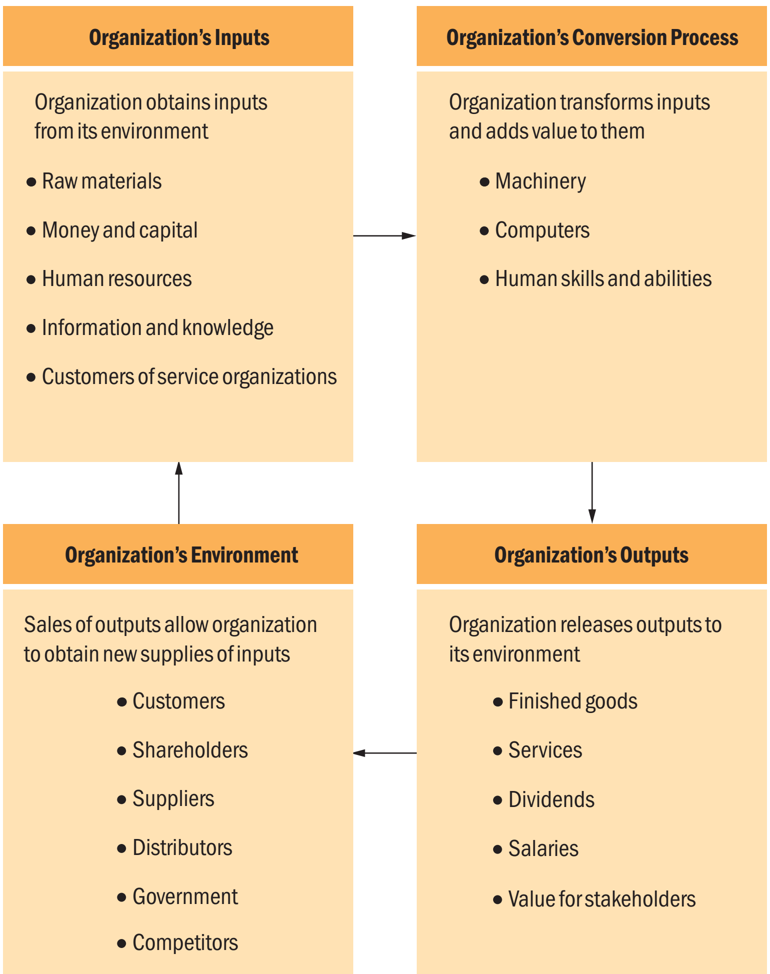
How Does an Organization Create Value?

The way in which an organization creates value is depicted in Figure 1.1. Value creation takes place at three stages: input, conversion, and output. Each stage is affected by the environment in which the organization operates. The **organizational environment** is the set of forces and conditions that operate beyond an organization's boundaries but affect its ability to acquire and use resources to create value.

Organizational environment The set of forces and conditions that operate beyond an organization's boundaries but affect its ability to acquire and use resources to create value.

Inputs include resources such as raw materials, machinery, information and knowledge, human resources, and money and capital. The way an organization chooses and obtains from its environment the inputs it needs to produce goods and services determines how much value the organization creates at the input stage. For example, Jeff Bezos chose to design software to make Amazon.com's website as simple and user friendly as he possibly could, and he only recruited people who could provide high-quality,

Figure 1.1 How an Organization Creates Value



Focus on New Information Technology

Amazon.com, Part 1

In 1994, Jeffrey Bezos, a computer science and electrical engineering graduate from Princeton University, was growing weary of working for a Wall Street investment bank. With his computer science background prompting him, he saw an entrepreneurial opportunity in the fact that use of the Internet was growing at over 2,300% a year as more and more people were becoming aware of its information advantages.

Searching for an opportunity to take advantage of his skills in the new electronic virtual marketplace, he concluded that the bookselling market would be a good place to invest his personal resources. Deciding to make a break, he packed up his belongings and drove to the West Coast, deciding en route that Seattle, Washington, a new mecca for high-tech software developers and the hometown of Starbucks coffee shops, would be an ideal place to begin his venture.

What was his vision for his new venture? To build an online bookstore that would be customer friendly, easy to navigate, and would offer the broadest possible selection of books. Bezos's mission? "To use the Internet to offer products that would educate, inform and inspire."[4] Bezos realized that compared to a real bricks-and-mortar bookstore, an online bookstore would be able to offer a much larger and more diverse selection of books. Moreover, online customers would be able to search easily for any book in print on a computerized online catalog, browse different subject areas, read reviews of books, and even ask other shoppers for online recommendations—something most people would hesitate to do in a regular bookstore.

With a handful of employees and operating from his garage in Seattle, Bezos launched his venture online in July 1995 with $7 million in borrowed capital. Word of his venture spread like wildfire across the Internet and book sales quickly picked up as satisfied customers spread the good word. Within weeks Bezos was forced to relocate to new larger premises and to hire new employees as book sales soared. Bezos's new venture seemed to be poised for success.

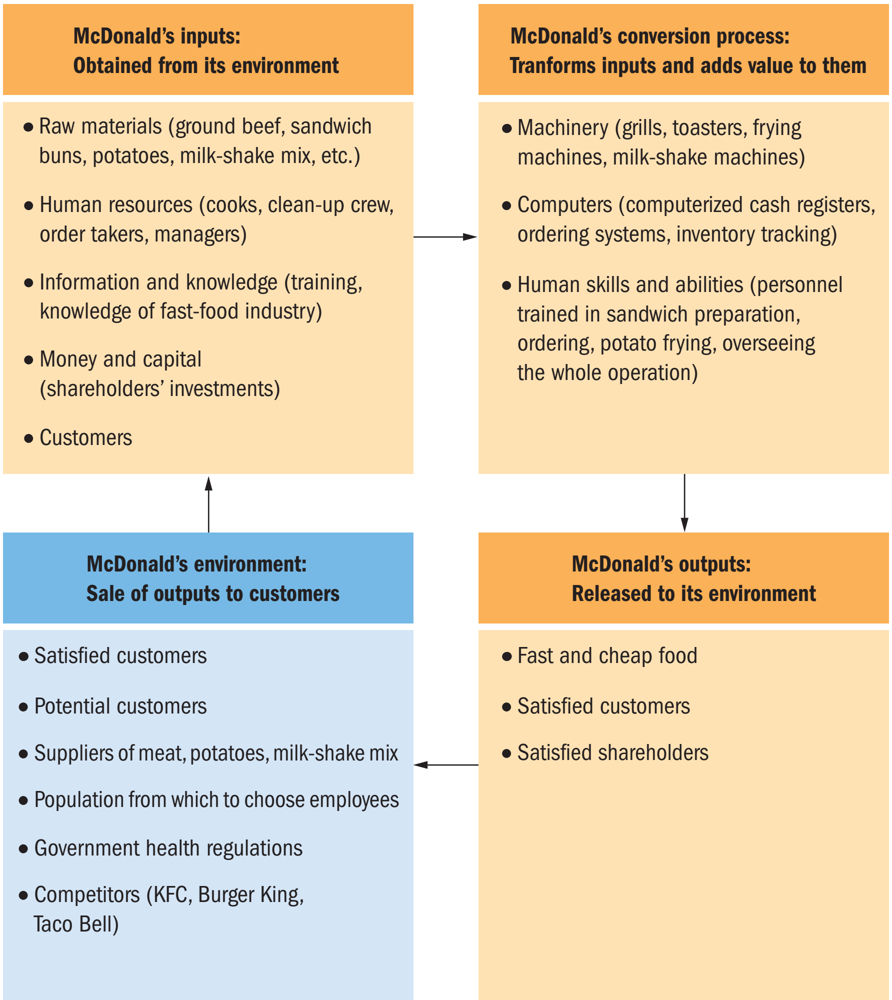
customer-friendly service that would most appeal to his Internet customers. If he had made poor choices and customers had not liked Amazon.com's website or customer service, his company would not have been successful.

The way the organization uses human resources and technology to transform inputs into outputs determines how much value is created at the conversion stage. The amount of value the organization creates is a function of the quality of its skills, including its ability to learn from and respond to the environment. For example, Jeff Bezos had to decide how best to sell and market his products to attract customers. His answer was to offer wide choice and low prices and to ship books quickly to customers. His skill at these activities created the value that customers saw in his concept.

The result of the conversion process is an output of finished goods and services that the organization releases to its environment, where they are purchased and used by customers to satisfy their needs—such as delivered books. The organization uses the money earned from the sale of its output to obtain new supplies of inputs, and the cycle begins again. An organization that continues to satisfy people's needs will be able to obtain increasing amounts of resources over time and will be able to create more and more value as it adds to its stock of skills and capabilities.[5] Amazon.com has grown from strength to strength because satisfied customers return to its online storefront and continue to provide the revenues it needs to continually improve its skills and expand its operations.

A value-creation model can be used to describe the activities of most kinds of organizations. Manufacturing companies, such as GE, GM, and IBM, take from the environment component parts, skilled or semiskilled labor, and technical knowledge and at the conversion stage create value by using their manufacturing skills to organize and assemble those inputs into outputs, such as cars and computers. Service organizations, such as McDonald's, Amazon.com, the Salvation Army, and your family doctor, interact directly with customers or clients, who are the "inputs" to their operations. Hungry people who go to McDonald's for a meal, needy families who go to the Salvation Army for assistance, and sick people who go to a doctor for a cure are all "inputs." In the conversion stage, service organizations create value by applying their skills to yield an output: satisfied hunger, a cared-for family, a cured patient. Figure 1.2 is a simplified model of how McDonald's creates value.

Figure 1.2 How McDonald's Creates Value



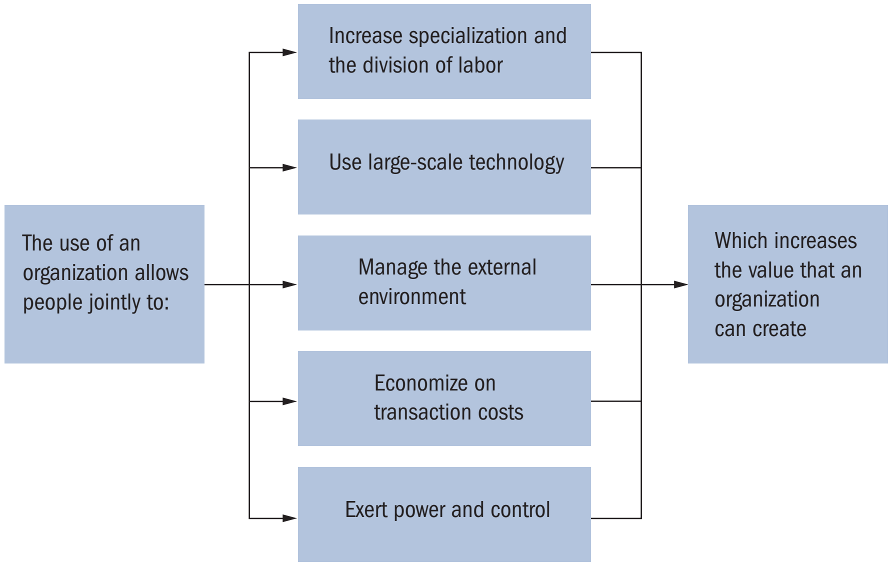
Why Do Organizations Exist?

The production of goods and services most often takes place in an organizational setting because people working together to produce goods and services usually can create more value than people working separately. Figure 1.3 summarizes five reasons for the existence of organizations.

To Increase Specialization and the Division of Labor

People who work in organizations may become more productive and efficient at what they do than people who work alone. For many kinds of productive work the use of an organization allows the development of specialization and a division of labor. The collective nature of organizations allows individuals to focus on a narrow area of expertise, which allows them to become more skilled or specialized at what they do. For example, engineers working in the engineering design department of a large car manufacturer like GM or Toyota might specialize in improving the design of fuel injection systems or other engine components. An engineer working for a small car manufacturer might be responsible for designing the whole engine. Because the engineer in the small company must perform many more tasks than the engineer in the large company, the degree of specialization in the small company is lower; there is less chance of discovering what makes for a great carburetor and thus creating more value for someone who desires high speed.

Figure 1.3 Why Organizations Exist



To Use Large-Scale Technology

Economies of scale
Cost savings that result when goods and services are produced in large volume on automated production lines.

Economies of scope
Cost savings that result when an organization is able to use underutilized resources more effectively because they can be shared across different products or tasks.

Organizations are able to take advantage of the economies of scale and scope that result from the use of modern automated and computerized technology. **Economies of scale** are cost savings that result when goods and services are produced in large volume on automated production lines.

Economies of scope are cost savings that result when an organization is able to use underutilized resources more effectively because they can be shared across several different products or tasks. Economies of scope (as well as of scale) can be achieved, for example, when it is possible to design an automated production line to produce several different types of products simultaneously. Toyota and Honda were the first carmakers to design assembly lines capable of producing three models of a car instead of just one. GM and Ford have followed suit and have achieved impressive gains in efficiency. Multimodel assembly lines give car companies lower manufacturing costs and greater flexibility to change quickly from making one model to another to meet varying customer needs.

To Manage the Organizational Environment

Pressures from the organizational environment in which they operate also make organizations the favored mode for transforming inputs into outputs. An organization's environment is the source of valuable input resources and is the marketplace into which it releases outputs. It is also the source of economic, social, and political pressures that affect an organization's ability to obtain these resources. Managing complex environments is a task beyond the abilities of most individuals, but an organization has the resources to develop specialists to anticipate or attempt to influence the many pressures from the environment. This specialization allows the organization to create more value for the organization, its members, and its customers. Large companies like IBM, AT&T, and Ford have whole departments of corporate executives who are responsible for monitoring, responding to, and attempting to manage the external environment, but those activities are just as important for small organizations. Although local stores and restaurants do not have whole departments to scan the environment, their owners and managers need to spot emerging trends and changes so that they can respond to changing customer needs, just as Jeff Bezos did; otherwise they will not survive.

To Economize on Transaction Costs

When people cooperate to produce goods and services, certain problems arise. As they learn what to do and how to work with others to perform a task effectively, people jointly have to decide who will do which tasks (the division of labor), who will get paid what amounts, and how to decide if each coworker is doing his or her share of the work. The costs associated with negotiating, monitoring, and governing exchanges between people to solve these kinds of transaction difficulties are called **transaction costs.** Organizations' ability to control the exchanges between people reduces the transaction costs associated with these exchanges. Suppose Intel bought the services of its scientists daily and thousands of scientists had to spend time every day discussing what to do and who should work with whom. Such a work system would be very costly and would waste valuable time and money. The structure and coordination imposed by the Intel organization, however, lets managers hire scientists on a long-term basis, assign them to specific tasks and work teams, and gives Intel the right to monitor their performance. The resulting stability reduces transaction costs and increases productivity.

Transaction costs
The costs associated with negotiating, monitoring, and governing exchanges between people.

To Exert Power and Control

Organizations can exert great pressure on individuals to conform to task and production requirements in order to increase production efficiency.[6] To get a job done efficiently, people must come to work in a predictable fashion, behave in the interests of the organization, and accept the authority of the organization and its managers. All these requirements make production less costly and more efficient but put a burden on individuals who must conform to organizational requirements. When individuals work for themselves, they need to address only their own needs. When they work for an organization, however, they must pay attention to the organization's needs as well as their own. Organizations can discipline or fire workers who fail to conform and can reward good performance with promotion and increased rewards. Because employment, promotion, and increased rewards are important and often scarce, organizations can use them to exert power over individuals.

Taken together, these five factors help explain why often more value can be created when people work together, coordinating their actions in an organized setting, than when they work alone. Over time, the stability created by an organization provides a setting in which the organization and its members can increase their skills and capabilities, and the ability of the organization to create value increases by leaps and bounds. By 2011, for example, Google grew to become the most valuable Internet software company in the world because Larry Page and Sergey Brin, its founders, created an organizational setting in which people are given freedom to develop their skills and capabilities to create innovative new products. In contrast, in the last decade other software companies like WordPerfect, Lotus, Novell, and even Microsoft have experienced major problems because they have not been able to create the Internet software customers want. Why does Google's organization allow it to create more and more value while these other organizations have actually reduced the value they can create? Before we can answer this question, we need to take a close look at organizational theory, design, and change.

Annette Shaff/Shutterstock.com

Giving the company's workers the freedom to innovate has helped Google stay ahead of its competition.

Organizational Theory, Design, and Change

Organizational theory
The study of how organizations function and how they affect and are affected by the environment in which they operate.

Organizational theory is the study of how organizations function and how they affect and are affected by the environment in which they operate. In this book, we examine the principles that underlie the design, operation, change, and redesign of organizations to maintain and increase their effectiveness. Understanding how organizations operate, however, is only the first step in learning how to control and change organizations so that they can create wealth and resources effectively. Thus the second aim of this book is to equip you with the conceptual tools to influence organizational situations in which you find yourself. The lessons of organizational design and change are as important at the level of first-line supervisor as they are at the level of chief executive officer, in small or large organizations, and in settings as diverse as the not-for-profit organization or the assembly line of a manufacturing company.

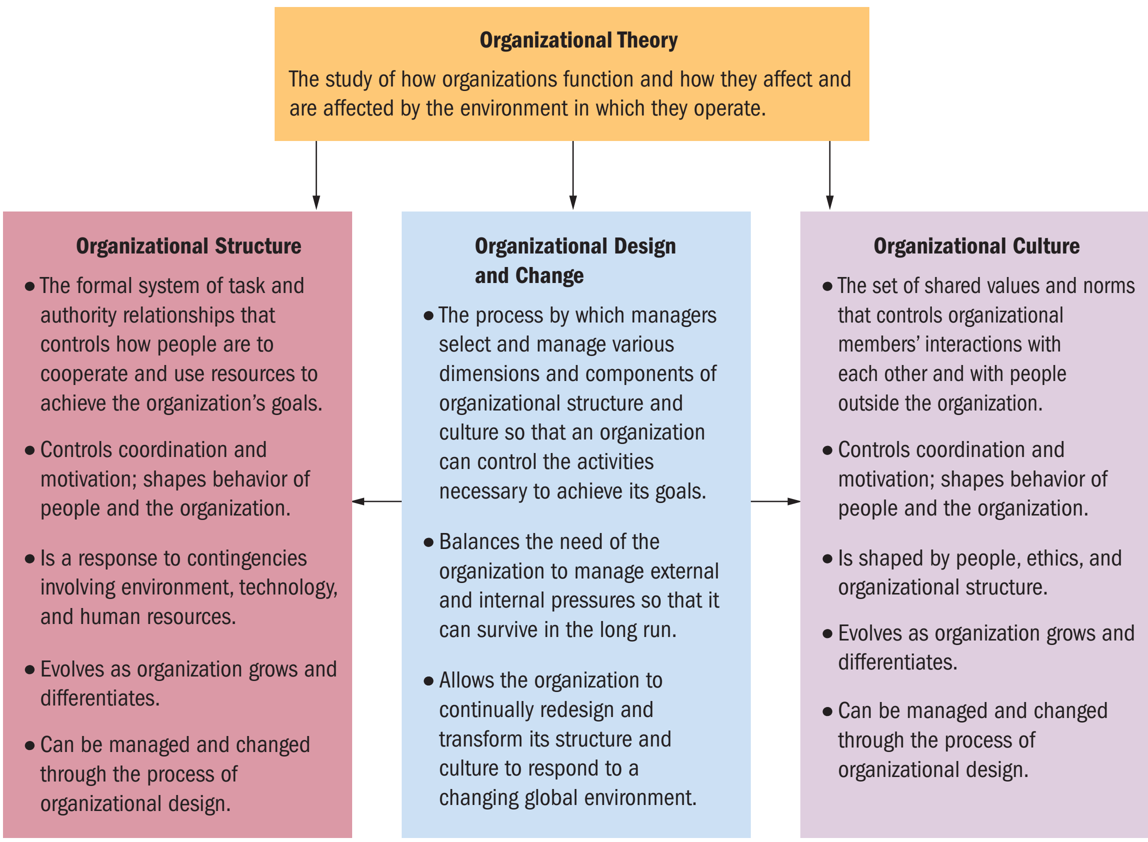
People and managers knowledgeable about organizational design and change are able to analyze the structure and culture of the organization for which they work (or which they wish to help, such as a charity or church), diagnose problems, and make adjustments that help the organization achieve its goals. Figure 1.4 outlines the relationship among organizational theory, structure, culture, design, and change.

Organizational Structure

Organizational structure
The formal system of task and authority relationships that control how people coordinate their actions and use resources to achieve organizational goals.

Once a group of people has established an organization to accomplish collective goals, organizational structure evolves to increase the effectiveness of the organization's control of the activities necessary to achieve its goals. **Organizational structure** is the formal system of task and authority relationships that control how people coordinate their actions and use resources to achieve organizational goals.[7] The principal purpose of organizational structure is one of control: to control the way people *coordinate* their actions

Figure 1.4 The Relationship among Organizational Theory and Organizational Structure, Culture, and Design, and Change



to achieve organizational goals and to control the means used to *motivate* people to achieve these goals. At Google, for example, the control problems facing Larry Page and Sergey Brin were how to coordinate their IT engineers' activities to make the best use of their talents, and how to reward them when they developed innovative products. Their solution was to place scientists in small self-contained teams and to reward them with stock in Google based on individual and team performance.

For any organization, an appropriate structure is one that facilitates effective responses to problems of coordination and motivation—problems that can arise for any number of environmental, technological, or human reasons.[8] As organizations grow and differentiate, the structure likewise evolves. Organizational structure can be managed through the process of organizational design and change.

Organizational Culture

At the same time that organizational structure is evolving, so is organizational culture. **Organizational culture** is the set of shared values and norms that controls organizational members' interactions with each other and with suppliers, customers, and other people outside the organization. An organization's culture is shaped by the people inside the organization, by the ethics of the organization, by the employment rights given to employees, and by the type of structure used by the organization. Like organizational structure, organizational culture shapes and controls behavior within the organization. It influences how people respond to a situation and how they interpret the environment surrounding the organization. At Google, Page and Brin attempted to create values that encouraged entrepreneurship and risk taking to build an organizational culture in which innovation was a valued activity. The small-team structure was helpful because scientists were continually meeting face to face to coordinate their activities and to learn from one another, which encouraged them to experiment and to find new ways of solving problems.

Organizational culture
The set of shared values and norms that controls organizational members' interactions with each other and with suppliers, customers, and other people outside the organization.

The cultures of organizations that provide essentially the same goods and services can be very different. For example, Coca-Cola and PepsiCo are the two largest and most successful companies in the soft drinks industry.[9] Because they sell similar products and face similar environments, we might expect their cultures to be similar. But they are not. Coca-Cola takes pride in its long-term commitment to employees; its loyal managers, many of whom spend their entire careers with the organization; and its cautious and cooperative approach to planning. By contrast, PepsiCo has a highly political and competitive culture in which conflicts over decision making cause frequent disputes, and often turnover, among top managers. Like organizational structure, organizational culture evolves and can be managed through organizational design and change.

Organizational Design and Change

Organizational design is the process by which managers select and manage aspects of structure and culture so an organization can control the activities necessary to achieve its goals. Organizational structure and culture are the *means* the organization uses to achieve its goals; organizational design is about how and why various means are chosen. An organization's behavior is the result of its design and the principles behind its operation. It is a task that requires managers to strike a balance between external pressures from the organization's environment and internal pressures from, for example, its choice of technology. Looking outward, the design can cause organizational members to view and respond to the environment in different ways. Looking inward, an organization's design puts pressure on work groups and individuals to behave in certain ways.

Organizational design
The process by which managers select and manage aspects of structure and culture so that an organization can control the activities necessary to achieve its goals.

Achieving the proper balance helps ensure that the organization will survive in the long run. The theories, concepts, and techniques covered in this book are intended to provide you with working models you can use to analyze organizational situations and to propose and implement suitable solutions to change an organization and increase its effectiveness.

High-tech organizations like Google, Apple, and Intel need to be flexible and capable of quick responses to the competitive moves of their rivals—Facebook, Samsung, and ARM—as they innovate new technology and introduce new products. At the same time, such organizations must have stable task relationships that allow their members to work together to create value, solve problems, and accomplish organizational objectives. In contrast, organizations like Nucor and Alcoa, which produce sheet steel and aluminium, respectively, face relatively stable environments in which customer needs are more predictable and technology changes more slowly. Consequently, their organizational design choices are likely to reflect the need for a structure and culture that reduces production costs rather than a structure and culture that promotes flexibility. In Chapters 4, 5, 6, and 7, we discuss the organizational structures and cultures that managers can design to help ensure their organizations' survival.

Organizational change
The process by which organizations redesign their structures and cultures to move from their present state to some desired future state to increase their effectiveness.

Organizational change is the process by which organizations move from their present state to some desired future state to increase their effectiveness. The goal of organizational change is to find new or improved ways of using resources and capabilities to increase an organization's ability to create value, and hence its performance.[10] Once again, organizational structure and culture are a principal means or fulcrum that managers use to change the organization so it can achieve its future desired state.

Organizational design and change are thus highly interrelated. Indeed, organizational change can be understood as the process of organizational redesign and transformation. As we discuss in later chapters, as organizations grow, their structure and culture is constantly evolving, changing, and becoming more complex. A large organization faces a different set of design and redesign problems than a small organization because its structure and culture are different from a small organization's. Managers need to recognize that their initial design choices will have important ramifications in the future as their organizations grow; indeed, it has been argued that initial choices are an important determinant of differences in long-run performance. For an example, consider how the way Steve Jobs designed the structure and culture of Apple changed over the years as he learned the principles behind organizational design, as illustrated in Organizational Insight 1.1.

Organizational Insight 1.1

How Steve Jobs Learned How to Organize and Control Apple

In 1976 Steven P. Jobs sold his Volkswagen van, and his partner Steven Wozniak sold his two programmable calculators, and they used the proceeds of $1,350 to build a circuit board in Jobs's garage. So popular was the circuit board, which developed into the Apple II personal computer (PC), that in 1977 Jobs and Wozniak founded Apple Computer to make and sell it. By 1985 Apple's sales had exploded to almost $2 billion, but in the same year Jobs was forced out of the company he founded. Jobs's approach to organizing was a big part of the reason he lost control of Apple.

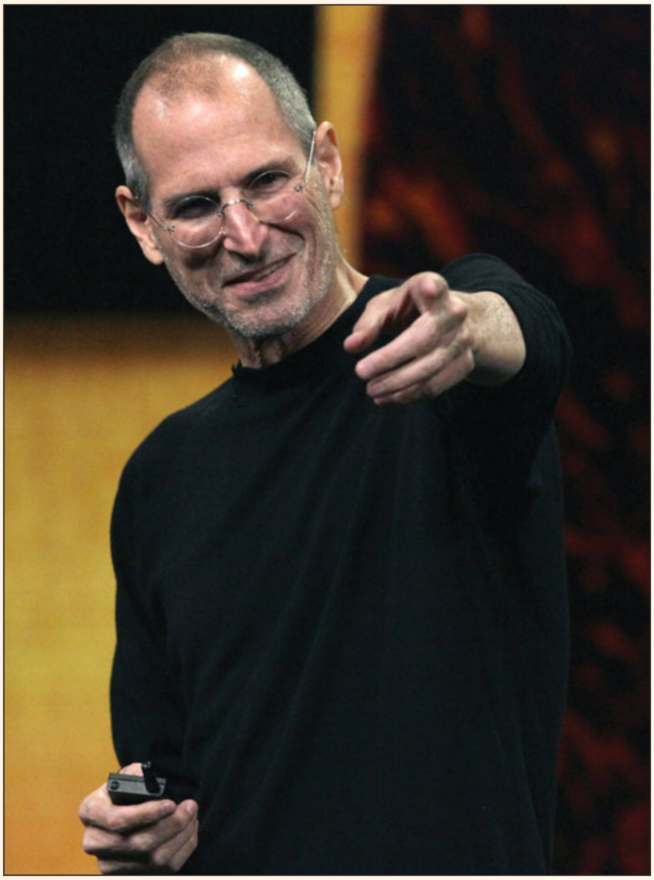
Jobs saw his main task as designing the organizational structure in ways that would lead to the rapid development of new and improved PCs, but his personal style was often arbitrary and overbearing. For example, Jobs often played favorites among the many different project teams he created that caused many conflicts and led to fierce competition, many misunderstandings, and growing distrust among members of the different teams. Jobs's abrasive management style also brought him into conflict with John Sculley, Apple's CEO. Employees became unsure whether Jobs (the chairman) or Sculley was in control of the company. Both managers were so busy fighting for control of Apple that the task of ensuring its resources were being used efficiently was neglected. Apple's costs soared, and its performance and profits fell.

Apple's directors became convinced Jobs's style was the heart of the problem and asked him to resign. After he left Apple, Jobs started new ventures. First he founded PC maker NEXT to develop a powerful new PC that would outperform Apple's PCs. Then he founded Pixar, a computer animation company, which become a huge success after it made blockbuster movies such as *Toy Story* and *Finding Nemo,* both distributed by Walt Disney, and Pixar was eventually sold to Disney.

In both these companies Jobs organizing approach changed. He built strong management teams to lead the project teams developing the new PCs and movies and kept his distance. Jobs saw his main task as organizing the companies' future product development strategies and he left the actual tasks of organizing and controlling to the managers who reported to him. He gave them the autonomy to put his vision into practice and in both companies he worked to create a culture based on values and norms of collaboration and creative thinking to promote innovation.

Meanwhile Apple was struggling to compete against Dell's low-cost PCs loaded with Microsoft's Windows software; its performance was plummeting and its future looked in doubt. To help the company he founded survive, in 1996 Jobs convinced Apple to buy NEXT for $400 million and use its powerful operating system in a new line of new Apple Mac PCs. Jobs worked inside Apple to lead its turnaround and he was so successful that in 1997 he was asked to become its new CEO.

His first step was to create a clear vision and goals to energize and motivate Apple employees. Jobs decided that Apple had to introduce state-of-the art, stylish PCs and related digital equipment. He created a team structure that allowed programmers and engineers to pool their



iStockphoto.com/Justin Sullivan

skills to develop new PCs. He delegated considerable authority to the teams, but he also established strict timetables and challenging "stretch" goals, such as bringing new products to market as quickly as possible, for these groups. One result of these efforts was Apple's sleek new line of iMac PCs, which were quickly followed by a wide range of futuristic PC-related products.[11]

In 2003 Jobs announced that Apple was starting a new service called iTunes, an online music store from which people could download songs for 99 cents. At the same time Apple introduced its iPod music player, which can store thousands of downloaded songs, and it quickly became a runaway success. Apple continually introduced new generations of the iPod, each more compact, powerful, and versatile than previous models. By 2006 Apple had gained control of 70% of the digital music player market and 80% of the online music download business, and its stock price soared to a new record level.

The next milestone in Jobs's managerial history came in 2007 when he announced that Apple would introduce the iPhone to compete directly with the popular Blackberry. Once again he organized Apple's engineers into teams, not only to develop the new phone but to create an online iPhone applications platform where users would be able to download iPhone applications—such as to interact with their friends—to make their phones more useful. By 2010 over two million iPhone applications had been developed, over two billion applications had been downloaded by iPhone users, and Apple was the leader in the smartphone market.

In 2010 Jobs announced that Apple planned to introduce its new iPad tablet computer, which he claimed would be the best way to experience the Web, email, and photos and would also have a wireless reading function to compete directly against Amazon.com's successful Kindle wireless reader.[12] As before, Jobs organized a new engineering unit to pioneer the development of applications for its new iPad, and after the iPad was released in spring 2010 analysts and customers swarmed to buy it, its stock rose to a high of $219. By 2011, Apple's stock had soared to over $350 as its product teams continuously brought out new and improved versions of its iPod, iPhone, and iPad and many analysts thought the company's stock would become the most valuable in the world.

As the example of the way Steve Jobs had changed his approach to organizing people and resources suggests, people who start new organizations may initially lack the kinds of skills or knowledge to manage an organization's structure and culture effectively but many of them can develop these skills over time. An understanding of the principles behind organizational design and change helps to speed this learning process and deepens appreciation for the many subtle technical and social processes that determine how organizations operate.

The Importance of Organizational Design and Change

Because of increased global competitive pressures and the increasing use of advanced IT, organizational design has become one of management's top priorities. Today, as never before, managers are searching for new and better ways to coordinate and motivate their employees to increase the value their organizations can create. There are several specific reasons why designing an organization's structure and culture, and changing them to increase its effectiveness, are such important tasks. Organizational design and change have important implications for a company's ability to deal with contingencies, achieve a competitive advantage, manage diversity effectively, and increase its efficiency and ability to innovate.

Dealing with Contingencies

A **contingency** is an event that might occur and must be planned for, such as a changing environment pressure like rising gas prices or the emergence of a new competitor like

Contingency
An event that might occur and must be planned for.

Amazon.com that decides to use new technology in an innovative way. The design of an organization determines how effectively an organization is able to respond to various pressures in its environment and so obtain scarce resources. For example, an organization's ability to attract skilled employees, loyal customers, or government contracts is a function of the degree to which the way it is designed gives it control over those three environmental factors.

An organization can design its structure in many ways to increase control over its environment. An organization might change employee task relationships so that employees are more aware of the environment, or it might change the way the organization relates to other organizations by establishing new contracts or joint ventures. For example, when Microsoft wanted to attract new customers for its Windows software in the United States and globally, it recruited large numbers of customer service representatives and created a new department to allow them to better meet customers' needs. The strategy was very successful, and the Windows platform is still used on over 90% of all desktop PCs globally.

As pressures from competitors, consumers, and the government increase, the environment facing all organizations is becoming increasingly complex and difficult to respond to, and more effective types of structure and culture are continually being developed and tried. We discuss how the changing nature of the environment affects organizations in Chapter 3 and how organizations can influence and control their environments in Chapter 8.

One part of the organizational environment that is becoming more important and more complex is the global environment. In the 2000s U.S. companies like Apple, IBM, and Walmart are constantly under pressure to expand their global presence and produce and sell more of their products in markets overseas to reduce costs, increase efficiency, and survive. Organizational design is important in a global context because to become a global competitor, a company often needs to create a new structure and culture. Chapter 8 also looks at the structures and cultures that a company can adopt as it engages in different kinds of global activities.

Changing technology is another contingency to which organizations must respond. Today, the Internet and other advanced IT have become one of the principal methods that organizations use to manage relationships with their employees, customers, and suppliers. The growing use of IT is fundamentally changing the design of organizational structure and has led to a huge round of organizational change as organizations have redesigned their structures to make most effective use of IT. We examine the effects of IT on organizational design and change in almost all the chapters of this book but particularly in Chapter 12.

In particular, a theme throughout the book is to examine how IT is changing the nature of the boundary of the organization, and the specific ways organizations coordinate people and tasks. The growth of outsourcing and the global network organizations whose members are linked primarily through electronic means has changed the way organizations operate in many ways. The pros and cons of this change in organizing—as organizations seek to increase their effectiveness and gain a competitive advantage—are discussed in depth in later chapters.

Gaining Competitive Advantage

Increasingly, organizations are discovering that organizational design, change, and redesign are a source of sustained competitive advantage. **Competitive advantage** is the ability of one company to outperform another because its managers are able to create more value from the resources at their disposal. Competitive advantage springs from **core competences,** managers' skills and abilities in value-creation activities such as manufacturing, R&D, managing new technology, or organizational design and change. Core competences allow a company to develop a strategy to outperform competitors and produce better products, or produce the same products but at a lower cost. **Strategy** is the specific pattern of decisions and actions that managers take to use core competences to achieve a competitive advantage and outperform competitors. Consider the way in which Groupon, profiled in Organizational Insight 1.2, has been rushing to develop its strategy to capture customers and keep its competitive advantage.

The *way* managers design and change organizational structure is an important determinant of how much value the organization creates because this affects how it

Competitive advantage
The ability of one company to outperform another because its managers are able to create more value from the resources at their disposal.

Core competences
Managers' skills and abilities in value-creating activities.

Strategy
The specific pattern of decisions and actions that managers take to use core competences to achieve a competitive advantage and outperform competitors.

Organizational Insight 1.2

Groupon Forges Ahead

iStockphoto.com/Christian Rummel

In 2010, Google offered to buy Groupon, the online "daily deal" newcomer, for $6 billion as it became obvious that Internet users liked the idea of online, continually changing coupons that offered them good deals by location. Groupon grew out of a website called The Point. Founded by Andrew Mason in 2007, it was designed to allow a sufficient number of people to get together online and participate as members in a joint endeavor, so that a "tipping point" was reached that allowed them to act as a *group* to take advantage of an opportunity that could not be obtained by any one individual. As Mason said in a letter to prospective investors in 2011, "I started The Point to empower the little guy and solve the world's unsolvable problems."[13]

Mason transformed The Point into Groupon, and began hiring employees who shared his collective vision, and by 2009 it launched its online coupon service. As Mason wrote, "As an antidote to a common ailment for us city-dwellers: there's so much cool stuff to do, but the choice can be overwhelming. With so many options, sometimes the easiest thing is to go to a familiar restaurant, or just stay at home and watch a movie. As a result, we miss out on trying all the cool things our cities have to offer."[14] Mason's idea was that by focusing on one specific good or service each day in a specific geographic location, Groupon could leverage its members' collective buying power to obtain deals from companies supplying goods and services that were hard to resist. Moreover, to protect its users, Groupon promises that because nothing is more important than treating customers well, if customers feel Groupon has let them down, all they have to do is call Groupon to get a refund.

Spearheaded by Mason's vision, Groupon has built a company that saw its revenues increase by 15 times between 2010 and 2011 and has successfully managed its explosive growth. Mason took advantage of the concept of online coupons to its full effect. In fact, while global sales were nonexistent in March 2010, they were 53% of its revenues by March 2011. Indeed, to grow his company so fast, Mason has taken major risks as he has invested all the money raised from private investors, and from its growing revenues, into aggressive expansion to stay ahead of competitors—including Google and LivingSocial, which also rushed to expand their own online coupon services.

After all, any new startup can easily imitate Groupon's strategy, but being the first mover is a major advantage. Hence Mason believes that pouring money into sales and marketing to make Groupon the global leader is worth it—in the same way that eBay and Amazon.com spent billions to become the online retail portals of choice and are currently reaping the benefits of their innovative strategies. However, Groupon still faces the prospect of cutthroat competition from giants like Google. For example, in 2011 Google announced the launch of an online coupon service that will offer discounts from restaurants and other merchants if enough people agree to buy the coupons. The service, called "Google Offers" is similar to the daily deals offered by Groupon. Google is testing its new online coupon service in Portland, Oregon, and will then rapidly expand it to large cities such as New York and San Francisco as a part of a new mobile payment service Google also unveiled recently that allows users to pay for products directly through their smartphones. So, only the future will tell if Groupon can maintain its leadership over this niche of the online market or will be crushed by Google, as well as Yahoo, AOL, and Facebook (which also announced its own coupon service for its 500,000 million users in 2011).

Despite these concerns and the fact in June 2011 Groupon had only 50 million users, its initial stock offering valued the company at $30 billion—a value higher than Google's when it went public! Only time will tell if Groupon can develop the organizational structure and culture it needs to control its explosive growth; so far it is succeeding as its laid-back founder has recruited people committed to following Mason's vision and making Groupon a force in which individuals can obtain the bargaining power they need to deal with large companies.

implements strategy. Many sources of competitive advantage, such as skills in research and development that result in novel product features or state-of-the-art technology, evaporate because they are relatively easy for competitors to imitate. It is much more difficult to imitate good organizational design and carefully managed change that brings into being a successful organizational structure and culture. Such imitation is difficult because structure and culture are embedded in the way people in an organization interact and coordinate their actions to get a job done. Moreover, because successful structures and cultures form early, as at Dell and Apple, and take a long time to establish and develop, companies that possess them can have a long-term competitive advantage.

An organization's strategy is always changing in response to changes in the environment; organizational design must be a continuously evolving managerial activity for a company to stay ahead of the competition. There is never a single optimal or "perfect" design to fit an organization's needs. Managers must constantly evaluate how well their organization's structure and culture work, and they should change and redesign them continually to improve them. In Chapter 8 we consider how organizations create value by means of their strategy.

Managing Diversity

Differences in the race, gender, and national origin of organizational members have important implications for the values of an organization's culture and for organizational effectiveness. The quality of organizational decision making, for example, is a function of the diversity of the viewpoints that get considered and of the kind of analysis that takes place. Similarly, in many organizations a large part of the workforce are minority employees whose needs and preferences must be taken into consideration. Also, changes in the characteristics of the workforce, such as an influx of immigrant workers or the aging of the current workforce, require attention and advance planning. An organization needs to design a structure and control system to make optimal use of the talents of a diverse workforce and to develop an organizational culture that encourages employees to work together. An organization's structure and culture determine how effectively managers are able to coordinate and motivate workers. Today, as companies increasingly operate in countries with widely disparate cultures around the globe, organizational design becomes even more important to harmonize national with organizational culture. Organizational Insight 1.3 discusses how the use of diverse—in this case female—manufacturing managers can promote high performance.

PROMOTING EFFICIENCY, SPEED, AND INNOVATION Organizations exist to produce goods and services that people value. The better that organizations function, the more value, in the form of more or better goods and services, they create. Historically, the capacity of organizations to create value has increased enormously as organizations have introduced better ways of producing and distributing goods and services. Earlier we discussed the importance of the division of labor and the use of modern technology in reducing costs, speeding work processes, and increasing efficiency. The design and use of new and more efficient organizational structures is equally important. In today's global environment, for example, competition from countries with low labor costs is pressuring companies all over the world to become more efficient in order to reduce costs or increase quality.

The ability of companies to compete successfully in today's competitive environment is increasingly a function of how well they innovate and how quickly they can introduce new technologies. Organizational design plays an important role in innovation. For example, the way an organization's structure links people in different specializations, such as research and marketing, determines how fast the organization can introduce new products. Similarly, an organization's culture can affect people's desire to be innovative. A culture based on entrepreneurial norms and values is more likely to encourage innovation than a culture that is conservative and bureaucratic because entrepreneurial values encourage people to learn how to respond and adapt to a changing situation.

Organizational design involves a constant search for new or better ways of coordinating and motivating employees. Different structures and cultures cause employees to behave in different ways. We consider structures that encourage efficiency and innovation in Chapters 4, 5, and 6 and cultures that do so in Chapter 7.

The Consequences of Poor Organizational Design

Many management teams fail to understand the important effects that organizational design and change can have on their company's performance and effectiveness. Although organizational structure and culture control behavior, managers are often unaware of the many factors that affect this relationship, paying scant attention to the way employees behave and their role in the organization—until something happens.

Ford, Sears, and Kodak have all experienced enormous problems in the last decade adjusting to the reality of modern global competition and have seen their sales and

Organizational Insight 1.3

How Diverse Manufacturing Managers Can Help Increase Product Quality

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Building cars remains primarily a male occupation; in 2011 roughly three out of four automotive manufacturing jobs are held by men, and women still number less than 20% of automotive manufacturing managers. Today, however, more women than men are buying new vehicles, and that shift, together with an increasing concern for diversity, has prompted major carmakers to promote more women into key management positions.[15] However, few women enroll in automotive and mechanical engineering programs because assembly plants have a reputation of being unpleasant, dirty, noisy places to work.

At Ford Motors, however, two of its female plant managers, Gloria Georger and Jan Allman, provide good examples of women who accepted the challenge of entering the manufacturing world. They embraced the opportunities such a job offers, and developed the skills that have allowed them to rise to become plant managers responsible for organizing and controlling billion-dollar manufacturing plants that employ thousands of employees.

Gloria Georger had no plans to pursue a manufacturing job and majored in accounting, but one recruiter commented on her outgoing personality and suggested she consider manufacturing where her interpersonal skills might be valuable—and manufacturing paid better than accounting. She took a job at U.S. Steel's plant in Gary, Indiana, and sure enough, her ability to motivate and work smoothly with employees led her to be promoted to production supervisor. Moreover, she claims the job helped develop the skills she needed to manage the unexpected contingencies that always arise on a fast-paced assembly line. She moved to Ford in 1986 when few women worked in manufacturing, but she quickly demonstrated the willingness to learn the cultural values and norms of its manufacturing operations and her personality allowed her to embrace and succeed in handling challenges from her mainly male colleagues and subordinates. She came to be regarded as a competent team leader and she steadily worked her way up the hierarchy of Ford's manufacturing function in different Ford plants until being promoted to her current position as the head manager of Ford's stamping plant in Chicago Heights, Illinois.[16]

Jan Allman is in charge of Ford's Torrence Avenue assembly plant, where in 2011 two-shifts of 2500 assembly line workers produce the new generation Ford Taurus, Lincoln MKS, and Explorer SUV. The parts produced by Georger's plant are assembled into the final vehicle at the Torrence Avenue plant, so close cooperation between the two plant managers is essential. Allman joined Ford in 1986 as a line engineer of an engine plant after receiving an engineering degree; she was one of two women out of 100 engineers Ford selected as interns to evaluate their performance before making hiring decisions. Allman rose to become the manufacturing engineering manager in charge of the engine plant, a position rarely held by a woman. Her hands-on organizing approach under difficult conditions impressed her colleagues, who noted her attention to detail of every aspect of the assembly process and the agreeable way in which she treated—and was treated by—employees. Hence, her promotion to become the manager of one of Ford's major assembly plants.

Both Allman and Georger agree that the growing number of women Ford has recruited into manufacturing over time has helped change the values and norms of its manufacturing culture.[17] Not only has it reduced the level of conflict between managers and workers, it has promoted cooperation and helped to promote Ford's focus on increasing product quality that is one of its major competitive advantages in the tough game of carmaking today. In 2011, for example, Ford reported its highest profits in 20 years and the company's new vehicles are increasingly ranked for their high quality.

profits fall dramatically. In response, they have slashed their workforces, reduced the number of products they make, and even reduced their investment in R&D. Why did the performance of these blue-chip companies deteriorate to such a degree? A major reason is that managers lost control of their organizational structures and cultures. These companies became so big and bureaucratic that their managers and employees were unable to change and adapt to changing conditions.

The consequence of poor organizational design or lack of attention to organizational design is the decline of the organization. Talented employees leave to take positions in strong growing companies. Resources become harder and harder to acquire, and the whole process of value creation slows down. Neglecting organizational design until crisis threatens forces managers to make changes in organizational structure and culture that derail the company's strategy. In the last decade, one major development at large companies has been the appointment of chief operating officers (COOs), who are made responsible for overseeing organizational structure and culture. COOs create and oversee teams of experienced senior managers who are responsible for organizational design and for orchestrating not only small and incremental but also organization-wide changes in strategy, structure, and culture.

How Do Managers Measure Organizational Effectiveness?

Because managers are responsible for utilizing organizational resources in a way that maximizes an organization's ability to create value, it is important to understand how they evaluate organizational performance. Researchers analyzing what CEOs and managers do have pointed to control, innovation, and efficiency as the three most important processes managers use to assess and measure how effective they, and their organizations, are at creating value.[18]

In this context, *control* means having control over the external environment and having the ability to attract resources and customers. *Innovation* means developing an organization's skills and capabilities so the organization can discover new products and processes. It also means designing and creating new organizational structures and cultures that enhance a company's ability to change, adapt, and improve the way it functions.[19] *Efficiency* means developing modern production facilities using new information technologies that can produce and distribute a company's products in a timely and cost-effective manner. It also means introducing techniques like Internet-based information systems, total quality management, and just-in-time inventory systems (discussed in Chapter 9) to improve productivity.

To evaluate the effectiveness with which an organization confronts each of these three challenges, managers can take one of three approaches (see Table 1.1). An organization is effective if it can (1) secure scarce and valued skills and resources from outside the organization (external resource approach); (2) coordinate resources with employee skills creatively to innovate products and adapt to changing customer needs (internal systems approach); and (3) convert skills and resources efficiently into finished goods and services (technical approach).

TABLE 1.1 Approaches to Measuring Organizational Effectiveness

Approach	Description	Goals to Set to Measure Effectiveness
External resource approach	Evaluates the organization's ability to secure, manage, and control scarce and valued skills and resources	• Lower costs of inputs • Obtain high-quality inputs of raw materials and employees • Increase market share • Increase stock price • Gain support of stakeholders such as government or environmentalists
Internal systems approach	Evaluates the organization's ability to be innovative and function quickly and responsively	• Cut decision-making time • Increase rate of product innovation • Increase coordination and motivation of employees • Reduce conflict • Reduce time to market
Technical approach	Evaluates the organization's ability to convert skills and resources into goods and services efficiently	• Increase product quality • Reduce number of defects • Reduce production costs • Improve customer service • Reduce delivery time to customer

The External Resource Approach: Control

The **external resource approach** allows managers to evaluate how effectively an organization manages and controls its external environment. For example, the organization's ability to influence stakeholders' perceptions in its favor and to receive a positive evaluation by external stakeholders is very important to managers and the organization's survival.[20] Similarly, an organization's ability to utilize its environment and to secure scarce and valuable resources is another indication of its control over the environment.[21]

External resource approach
A method managers use to evaluate how effectively an organization manages and controls its external environment.

To measure the effectiveness of their control over the environment, managers use indicators such as stock price, profitability, and return on investment, which compare the performance of their organization with the performance of other organizations.[22] Top managers watch the price of their company's stock very closely because of the impact it has on shareholder expectations. Similarly, in their attempt to attract customers and gauge the performance of their organization, managers gather information on the quality of their company's products as compared with their competitors' products.

Top management's ability to perceive and respond to changes in the environment or to initiate change and be first to take advantage of a new opportunity is another indicator of an organization's ability to influence and control its environment. For instance, the ability and willingness of the Walt Disney Company to manage its environment by seizing any chance to use its reputation and brand name to develop new products that exploit market opportunities—such as when it bought Pixar from Steve Jobs—are well known. Similarly, CEO Larry Page has stated that his goal is to be at the forefront of new developments in mobile computing software and hardware to increase Google's competitive advantage. By their competitive attitude, these companies signify that they intend to stay in control of their environment so they can continue to obtain scarce and valued resources such as customers and markets. Managers know that the organization's aggressiveness, entrepreneurial nature, and reputation are all criteria by which stakeholders (especially shareholders) judge how well a company's management is controlling its environment.

In fast-changing environments where customers' needs change and evolve and where new groups of customers emerge as new technologies result in new kinds of products and services, companies must learn to define and redefine their businesses to satisfy those needs. Companies have to listen closely to their customers and decide how best to meet their changing needs and preferences.

The Internal Systems Approach: Innovation

The **internal systems approach** allows managers to evaluate how effectively an organization functions and operates. To be effective, an organization needs a structure and a culture that foster adaptability and quick responses to changing conditions in the environment. The organization also needs to be flexible so it can speed up decision making and create products and services rapidly. Measures of an organization's capacity for innovation include the length of time needed to make a decision, the amount of time needed to get new products to market, and the amount of time spent coordinating the activities of different departments.[23] These factors can often be measured objectively. For example, in the spring of 2011 Netflix announced that its rapid moves to negotiate agreements with major movie studios to speed the launch of its new online movie streaming service had led to a record increase in the number of its customers—and its stock price soared. Similarly, Apple was able to announce record shipments of the new models of its iPhone and iPad in 2011 as a result of its ability to redesign and improve its products much more quickly than its rivals.

Internal systems approach
A method that allows managers to evaluate how effectively an organization functions and resources operate.

Improvements to internal systems that influence employee coordination or motivation have a direct impact on an organization's ability to respond to its environment. The reduction in product development time has allowed companies like Netflix and Apple to blow away competitors like Blockbuster, Comcast, and Blackberry and HP. The improved ability to get a product to market makes a company more attractive to customers who always want the product that contains the most recent technology available, such as the most advanced Intel chips, or software applications such as those in Apple's App Store.

The Technical Approach: Efficiency

Technical approach
A method managers use to evaluate how efficiently an organization can convert some fixed amount of organizational resources into finished goods and services.

The **technical approach** allows managers to evaluate how efficiently an organization can convert some fixed amount of organizational skills and resources into finished goods and services. Technical effectiveness is measured in terms of productivity and efficiency (the ratio of outputs to inputs).[24] Thus, for example, an increase in the number of units produced without the use of additional labor indicates a gain in productivity, and so does a reduction in the cost of labor or materials required to produce each unit of output.

Productivity measures are objective indicators of the effectiveness of an organization's production operations. Thus it is common for production line managers to measure productivity at all stages of the production process using indicators such as number of defective products or wasted material. When they find ways to increase productivity, they are then rewarded for reducing costs. In service organizations, where no tangible good is produced, line managers measure productivity using indicators such as amount of sales per employee or the ratio of goods sold to goods returned to judge employee productivity. For most work activities, no matter how complex, a way can be found to measure productivity or performance. In many settings the rewards offered to both employees and managers are closely linked to improvements in productivity, and it is critical to select the right measures to evaluate effectiveness.[25] Employee attitude and motivation and a desire to cooperate are also important factors influencing productivity and efficiency.[26]

The importance of continuously improving efficiency is very clear in the airline business. During the recent financial crisis, most major airlines were reporting billions of dollars in losses as a result of rising fuel prices, but one airline, Southwest Airlines, was only reporting *lower* profits. In fact, Southwest has long been the most profitable U.S. airline, even though its fares in the past have been 25% or more *below* those of its rivals. The major reason for its high performance is its never-ending quest to increase operating efficiency.[27]

From the beginning, under the direction of its founder, Herb Kelleher, the airline focused on developing an operating structure that lowers the cost of inputs and the cost of converting inputs into outputs, which are on-time flights that satisfy customers.

How does it do it? First, Southwest carefully selects its human resource inputs; only 3% of those who are interviewed each year are hired, and its existing employees are the ones who do the hiring—to make certain the new person fits in and is a team player with the right attitude. This is a vital strategy because employees are expected to have a positive, helping attitude not only toward passengers but also toward each other. To increase efficiency, all of Southwest's employees are expected to help each other out whenever needed to do everything necessary to speed the departure of its planes. Efficiency in the airline business is measured by the time each plane spends in the air, not stuck at the gate, and Southwest can turn a plane around and put it back in the air in 30 to 45 minutes—way ahead of its rivals. The bottom line is that Southwest needs fewer employees than other airlines to run its fleet of planes efficiently, which translates into major cost savings.

It also uses other inputs efficiently; for example, it only flies one kind of plane, the Boeing 737, which means that far less pilot training is required and maintenance costs are reduced. It also only flies mainly into low-cost airports, not the main city airports where landing charges and traffic congestion are usually much higher and plane turnaround much slower. It also operates what is called a "hub-and-spoke" network, meaning its planes typically touch down at least once before they reach the final destination, which allows it to fill its planes more easily and so make better use of its resources. Finally, Southwest never offered passengers meals and other free perks, a policy that all airlines have now copied to reduce costs as fuel prices soar. And, although it has experimented with assigned seating, boarding is on a first-come, first-served basis, which again simplifies its procedures.

In essence, Southwest tries to streamline and simplify all of its operating procedures to improve efficiency. Only the coordination between its employees makes it possible for its lean and simplified procedures to work, however. And as we discussed earlier, for its operating structure to work efficiently, coordination is not enough; employees must also be motivated to work hard and cooperate. From the beginning Southwest motivated employees with a generous profit-sharing plan whereby employees receive stock in the company as a function of how well the company performs. Because today employees own over 20% of Southwest's stock, this is a clear indicator that its continuous concern to design an operating structure that improves efficiency has paid off. In 2011, Southwest bought AirTran, its closest low-cost competitor, to expand its national route structure. Today Southwest's low-cost rival is JetBlue, which followed Southest's strategy and both these airlines are consistently rated as the highest in customer satisfaction.[28]

Another example of an airline that competes by improving efficiency in the global package shipping business is First Global Xpress, discussed in Organizational Insight 1.4.

Official goals
Guiding principles that the organization formally states in its annual report and in other public documents.

Measuring Effectiveness: Organizational Goals

Managers create goals that they use to assess how well the organization is performing. Two types of goals used to evaluate organizational effectiveness are official goals and operative goals. **Official goals** are guiding principles that the organization formally states in its annual report and in other public documents. Usually these goals lay out the **mission** of the organization: They explain why the organization exists and what it should be doing.

Mission
Goals that explain why the organization exists and what it should be doing.

Organizational Insight 1.4

First Global Xpress Delivers Packages Faster, Cheaper, and Greener

First Global Xpress (FGX) is a small, $10 million global package shipping company that claims it can ship packages from the 12 largest U.S. cities on the East Coast anywhere around the globe 24 hours faster and more reliably (its package loss rate is 1% to compared to the industry average of over 8%) than large competitors such as FedEx and UPS. Also, FGX claims it can ship its over 400 customers' packages at a 20% lower cost than its large rivals and in a "greener way" because it uses less fuel oil with a 30% savings in CO_2 emissions.[29] How has it been able to do become so efficient?

First, large shipping companies like FedEx and DHL rely on a "hub-and-spoke" package distribution system so that no matter where a package is collected or its destination, it has to go through a central hub first, where packages from all over the United States are sorted for shipment to their final destination. This means that a customer's shipment, say from New York to London, has to take two different flights—one to get to a hub, such as FedEx's hub in Memphis, Tennessee, and then another to get to England. FGX does not own aircraft; it has been rapidly forming alliances with over 100 different global airlines that can ship its customers' packages directly from city to city—from New York to London, for example—which saves time and money. Of course commercial airlines charge a fee for this service, but when demand for global air travel is declining and fuel costs are rising, forming an alliance with FGX is profitable for their bottom lines. As a result, airlines such as Continental, Virgin Atlantic, and Air France are willing to work closely with FGX to ensure that its packages are shipped directly and reliably to their destination cities. Because its flights are direct, FGX can also claim that it is providing this service "in a more socially responsible, greener way."

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FGX hopes to grow quickly and offer its service from other large U.S. cities such as Chicago, Houston, and Los Angeles. And its CEO claims, "Over the next five years FGX plans to keep growing, replicating its model for clients worldwide. Every day, FGX offers you the chance to save money, cut time off of your deliveries, and reduce your carbon footprint—all through the simple solution of shipping direct." The challenge facing its managers is to keep its value chain operations lean and efficient—just as Southwest does in the passenger segment of the airline business.[30]

TABLE 1.2 Amazon.com's Mission and Goals, 1998–2011

Where We Started

Amazon.com strives to be Earth's most customer-centric company where people can find and discover virtually anything they want to buy online. By giving customers more of what they want—low prices, vast selection, and convenience—Amazon.com continues to grow and evolve as a world-class e-commerce platform.

Where We Are Today

We seek to be Earth's most customer-centric company for three primary customer sets: consumer customers, seller customers and developer customers. . . . It is by design that technological innovation drives the growth of Amazon.com to offer customers more types of products, more conveniently, and at even lower prices.

Official goals include being a leading producer of a product, demonstrating an overriding concern for public safety, and so forth. Official goals are meant to legitimize the organization and its activities, to allow it to obtain resources and the support of its stakeholders.[31] Consider the way the mission and goals of Amazon.com have changed during the period 1998 to 2008 as its managers have changed its business activities to better manage its environment (Table 1.2). As these changes suggest, today Amazon.com serves the needs of three different kinds of customers because of the way it has grown and developed, and its organizational structure has become much more complex as a result, as we discuss in later chapters.

Operative goals
Specific long-term and short-term goals that guide managers and employees as they perform the work of the organization.

Operative goals are specific long- and short-term goals that guide managers and employees as they perform the work of the organization. The goals listed in Table 1.1 are operative goals that managers can use to evaluate organizational effectiveness. Managers can use operative goals to measure how well they are managing the environment. Is market share increasing or decreasing? Is the cost of inputs rising or falling? Similarly, they can measure how well the organization is functioning by measuring how long it takes to make a decision or the degree of conflict between organizational members. Finally, they can measure how efficient they are by creating operative goals that allow them to benchmark themselves against their competitors—that is, compare their competitors' cost and quality achievements with their own. UPS, FedEx, and First Global Xpress, for example, monitor one another's package delivery times and lost shipment rates to try to find ways to continuously improve their performance.

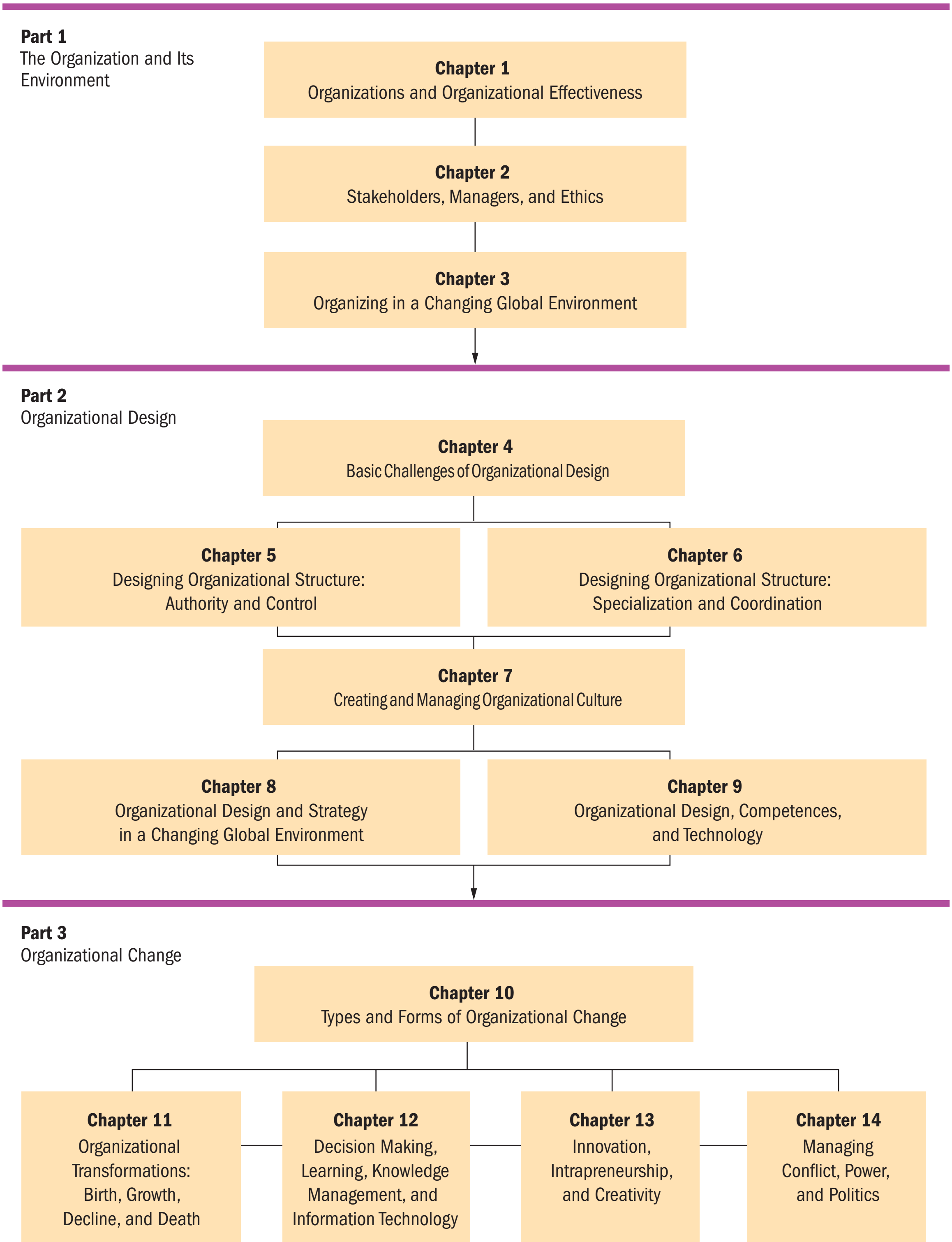
The Plan of This Book

To understand how to manage organizational design and change, it is first necessary to understand how organizations affect, and are affected by, their environments. Then the principles of organizational design and change that managers use to improve the match or fit of an organization with its environment can be better understood. To facilitate this learning process, the chapters in this book are organized so each builds on the ones that have come before. Figure 1.5 shows how the various chapters fit together and provides a model of the components involved in organizational design and change.

The number of major companies (e.g., Enron, Broadcom, and Computer Associates) whose top executives have engaged in unethical and often illegal kinds of corporate behavior, such as stock option backdating and "cooking the books," continues to increase. So it is more important than ever before that a clear link is made between ethics and organizational effectiveness because managers are responsible for protecting organizational resources and using them effectively. Chapter 2 examines the roles top managers perform in an organization, examines the claims and obligations of different organizational stakeholder groups, and examines the many ethical issues that managers face in dealing with the claims of these different groups.

The environment in which an organization operates is a principal source of uncertainty. If customers withdraw their support, if suppliers withhold inputs, if a global recession occurs, considerable uncertainty is created. Thus the organization must design its

Figure 1.5 **Components of Organizational Theory, Design, and Change**



structure to manage adequately the contingencies it faces in the external environment. Chapter 3 presents models that reveal why the environment is a source of uncertainty and theories about how and why organizations act to meet uncertainties in the environment. Resource dependence theory examines how organizations attempt to gain control over scarce resources. Transaction cost theory examines how organizations manage environmental relations to reduce transaction costs.

Organizational Design

Organizational design is complicated by the contingencies that must be considered as an organization makes its design choices. Several types of contingency—the organization's environment, its strategy, technology, and internal processes that develop in an organization over time—cause uncertainty and influence an organization's choice of structure and culture. Throughout the rest of this book we analyze the sources of this uncertainty and how organizations manage it. We also discuss how organizations can go about the process of changing and redesigning their structures and cultures as contingencies change and lead managers to develop new goals and strategies for their organizations.

Chapters 4 through 7 examine the principles on which organizations operate and the choices available for designing and redesigning their structures and cultures to match the environment. As these chapters show, the same basic organizational problems occur in all work settings, and the purpose of organizational design is to develop an organizational structure and culture that will respond effectively to these challenges.

Chapter 8 discusses organizations' attempts to manage their environment by using their structures and strategies to improve their fit with their environments. We discuss how organizations develop functional, business, and corporate strategies to increase their control over and share of scarce resources. We also discuss the global strategies managers can adopt as they expand and work to increase their presence overseas.

Organizations produce goods and services. The competences they develop to produce goods and services, and the uncertainty associated with different production methods or technologies, are major factors in the design of an organization. Chapter 9 discusses some theories that describe different competences and technologies, and explains the way in which they affect organizational structure and culture.

Organizational Change

The third part of this book deals with the many different but related issues involved in changing and redesigning organizations to improve their effectiveness. It also highlights the way for the need to foster innovation, utilize new information technologies effectively, and, in general, speed the rate at which organizations can adjust to their environments has been changing organizations.

Chapter 10 examines the nature of organizational change and outlines several important different kinds of organizational change processes, such as restructuring, reengineering, and innovation management. It also provides a model that explains the many different kinds of issues that must be confronted if managers are to succeed in their efforts to achieve a better fit with the environment.

When organizations are created and set in motion, various internal processes occur. As organizations grow and mature, many of them experience a predictable series of organizing crises, and as they attempt to change their strategies and structures, they confront similar problems. Chapter 11 presents a life cycle model of organizations and charts the typical problems they confront as they grow, mature, and decline.

Chapter 12 discusses organizational learning and decision making, and it relates these processes to the use of information technologies to show the many ways in which IT is changing organizations. First, the ways in which managers make decisions is examined. Then the increasingly important question of why managers make mistakes, both strategically and ethically, is examined. Ways in which managers can avoid these mistakes and speed the level of organizational learning to improve the quality of decision making is then described. Finally, we look at how new innovations in information technology, including the Internet, have been affecting organizations and changing organizational structure and culture.

Chapters 13 looks at the related issues of innovation and project management in organizations. Project management focuses on how project managers can use various techniques to speed and promote the development of new and improved goods and services. How to foster innovation and manage research and development is a pressing problem, particularly for organizations competing globally.

Finally, Chapter 14 covers problems of politics and conflict that arise as managers attempt to change and redesign organizational structure and culture. These chapters highlight the complex social and organizational processes that must be managed if an organization is to be able to manage the change process successfully and increase its effectiveness.

Summary

We have examined what organizations are, why they exist, the purpose of organizational theory, design, and change, and the different ways in which they can be evaluated. Organizations play a vital role in increasing the wealth of a society, and the purpose of managing organizational design and change is to enhance their ability to create value and thus organizational effectiveness. Chapter 1 has made the following main points:

1. An organization is a tool that people use to coordinate their actions to obtain something they desire or value—to achieve their goals.
2. Organizations are value-creation systems that take inputs from the environment and use skills and knowledge to transform these inputs into finished goods and services.
3. The use of an organization allows people jointly to increase specialization and the division of labor, use large-scale technology, manage the organizational environment, economize on transaction costs, and exert power and control—all of which increase the value the organization can create.
4. Organizational theory is the study of how organizations function and how they affect and are affected by the environment in which they operate.
5. Organizational structure is the formal system of task and authority relationships that control how people coordinate their actions and use resources to achieve an organization's goals.
6. Organizational culture is the set of shared values and norms that control organizational members' interactions with each other and with suppliers, customers, and other people outside the organization.
7. Organizational design is the process by which managers select and manage aspects of structure and culture so an organization can control the activities necessary to achieve its goals. Organizational design has important implications for a company's competitive advantage, its ability to deal with contingencies and manage diversity, its efficiency, its ability to generate new goods and services, its control of the environment, its coordination and motivation of employees, and its development and implementation of strategy.
8. Organizational change is the process by which organizations redesign and transform their structures and cultures to move from their present state to some desired future state to increase their effectiveness. The goal of organizational change is to find new or improved ways of using resources and capabilities to increase an organization's ability to create value and hence performance.
9. Managers can use three approaches to evaluate organizational effectiveness: the external resource approach, the internal systems approach, and the technical approach. Each approach is associated with a set of criteria that can be used to measure effectiveness and a set of organizational goals.

Discussion Questions

1. How do organizations create value? What is the role of entrepreneurship in this process?
2. What is the relationship among organizational theory, design, change, and organizational structure and culture?
3. What is organizational effectiveness? Discuss three approaches to evaluating effectiveness and the problems associated with each approach.
4. Draw up a list of effectiveness goals you would use to measure the performance of (a) a fast-food restaurant and (b) a school of business.

Organizational Theory in Action

Practicing Organizational Theory

Open Systems Dynamics

Form groups of three to five people and discuss the following scenario:

Think of an organization you are all familiar with, such as a local restaurant, store, or bank. Once you have chosen an organization, model it from an open systems perspective. For example, identify its input, conversion, and output processes.

1. Identify the specific forces in the environment that have the greatest opportunity to help or hurt this organization's ability to obtain resources and dispose of its goods or services.
2. Using the three views of effectiveness discussed in the chapter, discuss which specific measures are most useful to managers in evaluating this organization's effectiveness.

The Ethical Dimension #1

An ethical exercise is present in every chapter to help you understand the many ways in which organizations can help or harm the people and groups in their environments, especially when they are managed in ways that are unethical. This exercise can be done alone or in a small group.

Think of some examples of ways in which a hospital, and the doctors and nurses who work there, could act unethically toward patients. Also, think about behaviors that demonstrate a hospital has high ethical standards.

1. List examples of these ethical and unethical behaviors.
2. How do these behaviors relate to the attempts of doctors and nurses to increase organizational effectiveness in the ways discussed in the chapter? Or to attempts to pursue their own self-interest?

Making the Connection #1

At the end of every chapter you will find an exercise that requires you to search newspapers or magazines for an example of a real company that is dealing with some of the issues, concepts, challenges, questions, and problems discussed in the chapter.

Find an example of a company that is seeking to improve its effectiveness in some way. What dimension of effectiveness (control, innovation, or efficiency) is it seeking to improve? What changes is it making to address the issue?

Analyzing the Organization: Design Module #1

To give you insight into the way real-world organizations work, at the end of every chapter there is an organizational design module for which you must collect and analyze information about an organization you will select now and study all semester. You will write up the information you collect into a report to be presented to the class at the end of the semester.

Suppose you select General Motors. You will collect the information specified in each organizational design module, present and summarize your findings on GM for your class, and then produce a written report. Your instructor will provide the details of what will be required of you—for example, how long the presentation or report should be and whether you will work in a group or by yourself to complete the assignment. By the end of the semester, by completing each module, you will have a clear picture of how organizations operate and how they deal with problems and contingencies they face.

There are two approaches to selecting an organization. One is to choose a well-known organization about which a lot has been written. Large companies like IBM, Apple Computer, and Procter & Gamble receive extensive coverage in business periodicals such as *Fortune* and *Bloomberg/Business Week.* Every year, for example, in one of its April issues, *Fortune* magazine publishes a list of the Fortune 500 manufacturing companies, and in one of its May issues it publishes a list of the Fortune 500 service companies, the biggest companies in the United States. If you choose a company on the Fortune lists, you can be sure that considerable information is published about it.

The best sources of information are business periodicals and newspapers such as *Fortune*, *Business Week*, *Forbes,* the *Wall Street Journal*, *F&S Predicasts, Value Line Investment Survey,* and *Moody's Manuals on Investment*, and many other publications summarize articles written about a particular company. In addition, you should check industry and trade publications.

Finally, be sure to take advantage of the Internet and explore the Web to find information on your company. Most large companies have detailed websites that provide a considerable amount of information. You can find these websites using a search engine such as Yahoo or AltaVista and then download the information you need.

If you consult these sources, you will obtain a lot of information you can use to complete the design modules. You may not get all the specific information you need, but you will have enough to answer many of the design module questions.

The second approach to selecting an organization is to choose one located in your city or town—for example, a large department store, manufacturing company, hotel, or nonprofit organization (such as a hospital or school) where you or somebody you know works. You could contact the owners or managers of the organization and ask whether they would be willing to talk to you about the way they operate and how they design and manage their company.

Each approach to selecting a company has advantages and disadvantages. The advantage of selecting a local company and doing your own information gathering is that in face-to-face interviews you can ask for detailed information that may be unavailable from published sources. You will gain an especially rich picture of the way a company operates by doing your research personally. The problem is that the local organization you choose has to be big enough to offer you insight into the way organizations work. In general, it should employ at least 20 people and have at least three levels in its hierarchy.

If you use written sources to study a very large organization, you will get a lot of interesting information that relates to organizational theory because the organization is large and complex and is confronting many of the problems discussed in this book. But you may not be able to obtain all the detailed information you want.

Whichever selection approach you use, be sure you have access to enough interesting information to complete the majority of the organizational design modules. One module, for example, asks about the international or global dimension of your organization's strategy and structure. If you pick a local company that does not have an international dimension, you will be unable to complete that assignment. However, to compensate for this lack of information, you might have very detailed information about the company's structure or product lines. The issue is to make sure you can gain access to enough information to write an interesting report.

Assignment

Choose a company to study, and answer the following questions about it.

1. What is the name of the organization? Give a short account of the history of the company. Describe the way it has grown and developed.
2. What does the organization do? What goods and services does it produce/provide? What kind of value does it create? If the company has an annual report, what does the report describe as the company's organizational mission?
3. Draw a model of the way the organization creates value. Briefly describe its inputs, throughputs, outputs, and environment.
4. Do an initial analysis of the organization's major problems or issues. What challenges confront the organization today—for example, in its efforts to attract customers, to lower costs, to increase operating efficiency? How does its organizational design relate to these problems?
5. Read its annual report and determine which kinds of goals, standards, or targets the organization is using to evaluate performance. How well is the organization doing when judged by the criteria of control, innovation, and efficiency?

CASE FOR ANALYSIS

How Joe Coulombe Made Trader Joe's a Success Story

Trader Joe's, an upscale specialty supermarket chain, was founded in 1967 by Joe Coulombe, who then owned a few convenience stores that were fighting an uphill battle against the growing 7-11 chain. 7-11 offered customers a wider selection of lower-priced products and Coulombe could not compete. For his small business to survive, Coulombe decided to change his strategy and supply upscale specialty products such as wine, drinks, and gourmet foods to customers. Coulombe changed the name of his stores to Trader Joe's and stocked them with every variety and brand of California wine that was then being produced. He also began to offer fine foods like bread, crackers, cheese, fruits, and vegetables to complement and encourage wine sales. His planning paid off; customers loved his new upscale supermarket concept and the premium products he chose to stock sold quickly—and they were more profitable to sell.

From the beginning Coulombe realized that finding a new niche in the supermarket business was only the first step to help his small, growing company succeed. He knew that to encourage customers to visit his stores and buy more expensive gourmet products he needed to provide them with excellent customer service. So, he had to find ways to motivate his salespeople to perform at a high level. His approach to organizing was to decentralize authority and empower salespeople to take responsibility for meeting customer needs. Rather than instructing employees to follow strict operating rules and to get the approval of their supervisor before making customer-specific decisions, employees were given autonomy to make their own decisions and provide personalized customer service. Coulombe's approach led employees to feel they "owned" their supermarkets, and he worked to develop a culture based on values and norms about providing excellent customer service and developing personalized relationships with customers, who are often on first-name terms.

Coulombe led by example and created a store environment in which employees were treated as individuals and felt valued as people. For example, the theme behind the design of his stores was to create the feeling of a Hawaiian resort: employees wear loud Hawaiian shirts, store managers are called captains, and the store décor uses lots of wood and contains tiki huts, where employees provide customers with food and drink samples and interact with them. Once again, this helped to create strong values and norms that emphasize personalized customer service.

Finally, Joe Coulombe's approach was strongly influenced by the way he went about controlling salespeople. From the outset he created a policy of promotion from within the company so that the highest-performing salespeople could rise to become store captains and beyond in the organization. And, from the beginning, he recognized the need to treat employees in a fair and equitable way to encourage them to develop the customer-oriented values and norms needed to provide personalized customer service. He decided that full-time employees should earn at least the median household income for their communities, which averaged $7,000 a year in the 1960s and is $48,000 today—an astonishingly high amount compared to the pay of employees of regular supermarkets such as Kroger's and Safeway. Moreover, store captains, who are vital in helping create and reinforce Trader Joe's store culture, are rewarded with salaries and bonuses that can exceed $100,000 a year. And all salespeople know that as the store chain expands they may also be promoted to this level. In sum, Coulombe's approach to developing the right way to organize his small business created a solid foundation on which this upscale specialty supermarket has grown and prospered.[32]

Discussion Questions

1. What was Joe Coulombe's approach to organizational design?
2. What specific decisions did he make to create Trader Joe's organizational structure and culture?
3. Go online and see how Trader Joe's is performing today. What new problems of organizing has it been facing as it has grown?

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CHAPTER 2

Stakeholders, Managers, and Ethics

Learning Objectives

Organizations exist to create valuable goods and services that people need or desire. But who decides which goods and services an organization should provide or how to divide the value that an organization creates among different groups of people, such as employees, customers, or shareholders? If people behave self-interestedly, what mechanisms or procedures govern the way an organization uses its resources, and what is to stop the different groups from trying to maximize their share of the value created? In an age when the issue of corporate ethics, insider trading, and top-management greed has come under intense scrutiny, we must deal with these questions before we can address the issue of designing an organization to increase its effectiveness.

After studying this chapter you should be able to:

1. Identify the various stakeholder groups and their interests or claims on an organization.
2. Understand the choices and problems inherent in distributing the value an organization creates.
3. Appreciate who has authority and responsibility at the top of an organization, and distinguish between different levels of management.
4. Describe the agency problem that exists in all authority relationships and the various mechanisms, such as the board of directors and stock options, which can be used to help control illegal and unethical managerial behavior.
5. Discuss the vital role that ethics plays in constraining managers and employees to pursue the goals that lead to long-run organizational effectiveness.

Organizational Stakeholders

Stakeholders
People who have an interest, claim, or stake in an organization, in what it does, and in how well it performs.

Inducements
Rewards such as money, power, and organizational status.

Contributions
The skills, knowledge, and expertise that organizations require of their members during task performance.

Organizations exist because of their ability to create value and acceptable outcomes for various groups of **stakeholders,** people who have an interest, claim, or stake in an organization, in what it does, and in how well it performs.[1] In general, stakeholders are motivated to participate in an organization if they receive inducements that exceed the value of the contributions they are required to make.[2] **Inducements** include rewards such as money, power, and organizational status. **Contributions** include the skills, knowledge, and expertise that organizations require of their members during task performance.

The two main groups of organizational stakeholders are inside stakeholders and outside stakeholders. Table 2.1 summarizes the inducements and contributions of each group.[3]

Inside Stakeholders

Inside stakeholders are people who are closest to an organization and have the strongest or most direct claim on organizational resources: shareholders, managers, and the workforce.

TABLE 2.1 Inducements and Contributions of Organizational Stakeholders

Stakeholder	Contribution to the Organization	Inducement to Contribute
Inside		
Shareholders	Money and capital	Dividends and stock appreciation
Managers	Skills and expertise	Salaries, bonuses, status, and power
Workforce	Skills and expertise	Wages, bonuses, stable employment, and promotion
Outside		
Customers	Revenue from purchase of goods and services	Quality and price of goods and services
Suppliers	High-quality inputs	Revenue from purchase of inputs
Government	Rules governing good business practice	Fair and free competition
Unions	Free and fair collective bargaining	Equitable share of inducements
Community	Social and economic infrastructure	Revenue, taxes, and employment
General public	Customer loyalty and reputation	National pride

SHAREHOLDERS Shareholders are the owners of the organization, and, as such, their claim on organizational resources is often considered superior to the claims of other inside stakeholders. The shareholders' contribution to the organization is to invest money in it by buying the organization's shares or stock. The shareholders' inducement to invest is the prospective money they can earn on their investment in the form of dividends and increases in the price of stock. Investment in stock is risky, however, because there is no guarantee of a return. Shareholders who do not believe the inducement (the possible return on their investment) is enough to warrant their contribution (the money they have invested) sell their shares and withdraw their support from the organization.

During the recent recession that resulted because of the sub-prime mortgage problem, the resulting financial crisis led to a meltdown in the stock market during which most investors lost 40% or more of the value of their stock investments. As a result, more and more shareholders, who are most commonly mutual fund investors, are relying increasingly on the government and on large institutional investment companies to protect their interests and to increase their collective power to influence top managers. Large mutual fund companies like Fidelity or TIAA/CREF realize they have an increasing responsibility to their investors who lost billions in their pension funds as a result of the subprime crisis, as well as the earlier dot.com meltdown.[4] Also, mutual fund managers realize they have an increasing responsibility to monitor the performance of top managers to prevent the kinds of unethical and illegal behaviors that caused the collapse of Lehman brothers, Enron, Tyco, and many other companies whose dubious accounting practices led to a collapse in their stock price. If mutual fund companies are to protect the interests of their shareholders, they need to monitor and influence the behavior of the companies they invest in, to make sure the top managers pursue actions that do not threaten shareholders' interests while enhancing their own.

As a result of this concern for shareholders, mutual fund companies have become more vocal in trying to influence top managers. For example, they have sought to get companies to remove so-called poison pills, which are antitakeover provisions that make it much more difficult and expensive for another company to acquire it. Top managers like poison pills because it helps them protect their jobs, huge salaries, and other perks. Mutual fund companies are also showing increasing interest in controlling the huge salaries and bonuses that top managers give themselves that have reached record levels in recent years. They have also reacted to the accounting scandals that have led to the collapse of Enron and the poor performance of other companies such as Computer Associates by demanding that companies clarify their accounting procedures. And they have successfully lobbied for Congress to pass new laws such as the Sarbanes/Oxley and Dodd-Frank Acts, and to increase the power of government agencies such as the Federal Trade Commission (FTC)