CHAPTER 12

IMPLEMENTING STRATEGY THROUGH ORGANIZATION

Igor Sokolov (breeze)/Shutterstock.com

OPENING CASE

Organization at Microsoft

As is often the case with many start-ups, in its early days Microsoft's organization developed organically. Initially, when the company's main product was its MS-DOS operating system (the forerunner to Windows), the company had a functional organization. The two main functions were engineering, which was responsible for developing software products, and marketing and sales, which sold those products to computer manufacturers, business users, and consumers. The engineering function was initially headed by founder and CEO Bill Gates, while Steve Ballmer (who would ultimately succeed Gates as CEO), ran the marketing and sales function. Support functions included finance, human relations, and legal.

As the company grew and developed new products such as Office, Windows server software, development tools, X-Box, and Internet search, Microsoft developed into a de facto matrix organization. Each major product category was put into its own business division, while the engineering and sales functions cut across these divisions. The rational for the matrix structure was that it encouraged close coordination between the different businesses. This was seen as a key imperative at Microsoft, where various software products needed to work well with each other. For example, on the engineering side, Office needed to be optimized to run well on Windows; X-Box used a customized version of the Windows operating system, so development had to be synchronized; and the Windows operating system for desktop and laptop computers had to communicate seamlessly with the Windows server software that ran on servers. On the sales and marketing side, coordination was important to ensure that business users had one main point of contact with Microsoft, which was far preferable to having multiple salespeople from different divisions contact the company.

While the matrix organization achieved its main objectives of facilitating coordination between divisions and presenting a main point of contact for businesses, it did create some problems for the organization. In particular, there was a chronic lack of accountability within Microsoft.

LEARNING OBJECTIVES

12.1 Explain the concept of organizational architecture

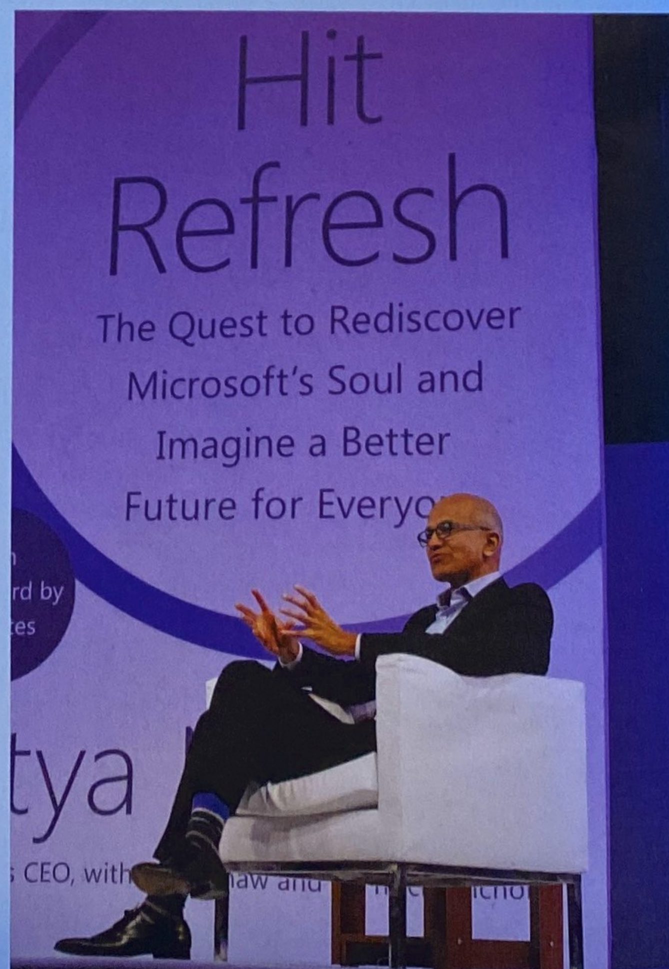
12.2 Articulate how strategy is implemented through the right combination of organizational structure, controls, incentives, process, culture, and people

12.3 Discuss how effective organizational design enables a company to implement its business-level strategy

12.4 Discuss how effective organization design enables a company to implement its corporate-level strategy

When things went wrong, it could be unclear whether this was due to management problems within the business divisions, or due to a lack of execution by the engineering function, or by sales and marketing. It was also the case that engineering was viewed as the premier cultural function within the organization. Most importantly, engineering took the lead in developing new products. This didn't always serve the company well, because its engineers, isolated from customers, were not as focused on the market as they should have been. Over time, the company also became increasingly bureaucratic and slow to respond to innovation by rivals such as Apple and Google.

When Satya Nadella became CEO of Microsoft in January 2014, one of his priorities was to increase accountability within the organization and make Microsoft more agile. By mid-2017, he had reorganized into three main business segments–Productivity and Business Processes (which included Office 365, Dynamics, and Linked-in), Intelligent Cloud (public, private, and hybrid server products and cloud services), and More Personal Computing (Windows, X-box, Surface, and search advertising). The heads of each segment report directly to Nadella, and they have primary profit-and-loss responsibility for their segments. The different product offerings within each segment are also profit centers, and the heads of those product divisions report to the head of each segment. Sales continues to operate as a separate function, but engineering and marketing responsibilities are now



Vipin Kumar/Hindustan Times/Getty Images embedded in each segment, and the product groups within each segment. In other words, Microsoft has moved significantly away from its de facto matrix structure. The articulated goal of these changes is to align structure with strategy, drive accountability, and eliminate obstacles to innovation. Judged by Microsoft's financial results and the rapid growth of its cloud offerings since Nadella took over, so far this seems to be working.

Sources: Discussions with Microsoft personnel by the author.

12-1 OVERVIEW

Earlier in this book, we noted that strategy is implemented through the organizational arrangements of a firm and through actions taken at the functional level. We discussed the functional actions required to implement different *business-level strategies* in Chapters 4 and 5. In this chapter, we look at how organizational arrangements are used to implement the business-, corporate-, and global-level strategies of an enterprise.

The Opening Case illustrates some of the issues that we shall be discussing in this chapter. Like most new enterprises, Microsoft started out with a functional organization. Over time, as it developed additional products, it grouped those products into business divisions. At the same time, its two core functions—engineering and marketing and sales—remained strong, resulting in a de facto matrix organization. This organization structure did help Microsoft ensure that all of its product offerings worked well with each other, which was a key competitive requirement, but it also resulted in problems of accountability and control, and a lack of agility. After Satya Nadella became CEO in January 2015, he instituted a number of changes to better align the structure of the organization with its strategy of growing its cloud computing business, increasing accountability, and removing barriers to product innovation. Microsoft is not the first company to wrestle with the problem of how best to organize the enterprise to implement its strategy. This is a major issue in all organizations, and accordingly it is the focus of the current chapter.

organizational architecture
The totality of a firm's organizational arrangements, including its formal organizational structure, control systems, incentive systems, organizational culture, organizational processes, and human capital.

12-2 ORGANIZATIONAL ARCHITECTURE

In this chapter, we use the term **organizational architecture** to refer to the totality of a firm's organizational arrangements, including its formal organizational structure, control systems, incentive systems, organizational culture, organizational processes, and people (or human capital).[1] Figure 12.1 illustrates these different elements.

organizational structure
The combination of the location of decision-making responsibilities, the formal division of the organization into subunits, and the establishment of integrating mechanisms to coordinate the activities of the subunits.

By **organizational structure**, we mean three things: First, the location of decision-making responsibilities in the firm (e.g., centralized or decentralized); second, the formal division of the organization into subunits such as functions, product divisions, and national operations; and third, the establishment of integrating mechanisms to coordinate the activities of subunits.