STRATEGIC MANAGEMENT
Concepts and Cases

FIFTEENTH EDITION

A COMPETITIVE ADVANTAGE APPROACH

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Implementing Strategies: Management and Operations Issues

CHAPTER OBJECTIVES

After studying this chapter, you should be able to do the following:

1. Construct an effective organizational chart.
2. Explain why corporate wellness has become so important in strategic planning.
3. Explain why strategy implementation is more difficult than strategy formulation.
4. Discuss the importance of annual objectives and policies in achieving organizational commitment for strategies to be implemented.
5. Explain why organizational structure is so important in strategy implementation.
6. Compare and contrast restructuring and reengineering.
7. Describe the relationship between production/operations and strategy implementation.
8. Explain how a firm can effectively link performance and pay to strategies.
9. Discuss employee stock ownership plans (ESOPs) as a strategic-management concept.
10. Describe how to modify an organizational culture to support new strategies.

David + David
2015

ASSURANCE OF LEARNING EXERCISES

The following exercises are found at the end of this chapter.

EXERCISE 7A Critique Corporate Organizational Charts

EXERCISE 7B Draw an Organizational Chart for PepsiCo Using a Free, Online Template

EXERCISE 7C Do Organizations Really Establish Objectives?

EXERCISE 7D Understanding Your University's Culture

The strategic-management process does not end on deciding what strategy or strategies pursue. There must be a translation of strategic thought into strategic action. This trans tion is much easier if managers and employees of the firm understand the business, f a part of the company, and through involvement in strategy-formulation activities have beco committed to helping the organization succeed. Without understanding and commitme strategy-implementation efforts face major problems. Vince Lombardi said: "The best game pl in the world never blocked or tackled anybody."

Implementing strategy affects an organization from top to bottom, including all the fu tional and divisional areas of a business. This chapter focuses on management issues m central to implementing strategies in 2014–2015 and Chapter 8 focuses on marketing, finan accounting, R&D, and management information systems issues. TJX Companies is an exam firm with excellent management practices.

> Even the most technically perfect strategic plan will serve little purpose if it is not implemented. Many organizations tend to spend an inordinate amount of time, money, and effort on developing the strategic plan, treating the means and circumstances under which it will be implemented as afterthoughts! Change comes through implementation and evaluation, not through the plan. A technically imperfect plan that is implemented well will achieve more than the perfect plan that never gets off the paper on which it is typed.[1]

The Nature of Strategy Implementation

The strategy-implementation stage of strategic management is revealed in Figure 7-1, illustrated with white shading. Successful strategy formulation does not guarantee success strategy implementation. It is always more difficult to do something (strategy implementatio than to say you are going to do it (strategy formulation)! Although inextricably linked, strate

EXCELLENT STRATEGIC MANAGEMENT SHOWCASED

The TJX Companies Inc.

Have you every shopped at the largest two discount clothing retailers in the USA, T. J. Maxx and Marshalls? The parent company of those clothing stores, TJX Companies, has formulated and is implementing excellent strategies. T. J. Maxx sells brand-name family apparel, accessories, women's shoes, domestics, giftware, and jewelry "at discount prices" at more than 1,010 stores nationwide. Marshalls offers a full line of shoes and a broader selection of menswear through about 900 stores. The company's HomeGoods chain of 399 stores in the USA focuses exclusively on home furnishings. T. K. Maxx is the company's European retail arm with more than 350 stores in the UK, Ireland, Germany, and now Poland, including 339 T. K. Maxx and 24 HomeSense stores. The company also operates about 310 stores in Canada, including 222 Winners, 87 HomeSense, and 13 Marshalls.

Same-store sales at TJX climbed 8.0 percent year-over-year in the 4-week period ended August 25, 2012. This rate of increase was in line with the year-ago period's growth. TJX's total sales climbed 10.0 percent for the aforementioned period to $1.9 billion from $1.7 billion in the year-ago period. As for the 30-week period ended August 25, 2012, comparable sales climbed 8 percent from the year-ago period. Total sales for the same period went up 10.0 percent year over year to $12.4 billion. TJX's sales exceeded even management's expectations partly as a result of higher customer tra in its USA, Canadian, and European divisions. At TJX's largest divisi Marmaxx Group, comparable store sales growth of 9 percent duri the 4-week period ended August 25, 2012.

TJX has reported increased comparable store sales and custom traffic for the past several quarters. TJX has an excellent, flexible c price business model that allows the firm to react quickly and capit ize on market trends. TJX has a lower cost structure than many ot traditional retailers.

Source: Based on a variety of sources.

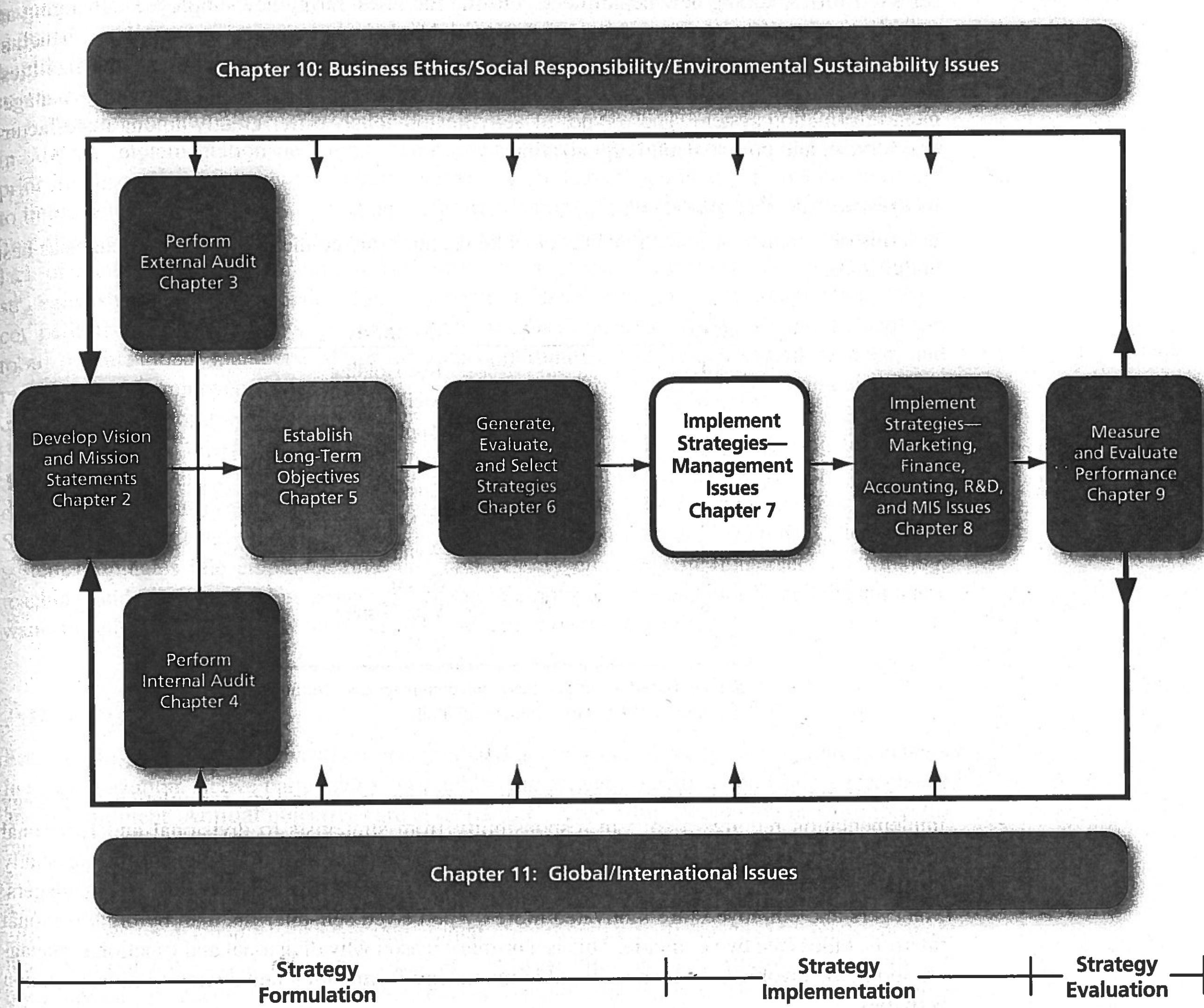


FIGURE 7-1
Comprehensive Strategic-Management Model

Source: Fred R. David, "How Companies Define Their Mission," *Long Range Planning* 22, no. 3 (June 1988): 40.

implementation is fundamentally different from strategy formulation. Strategy formulation and implementation can be contrasted in the following ways:

- Strategy formulation is positioning forces before the action.
- Strategy implementation is managing forces during the action.
- Strategy formulation focuses on effectiveness.
- Strategy implementation focuses on efficiency.
- Strategy formulation is primarily an intellectual process.
- Strategy implementation is primarily an operational process.
- Strategy formulation requires good intuitive and analytical skills.
- Strategy implementation requires special motivation and leadership skills.
- Strategy formulation requires coordination among a few individuals.
- Strategy implementation requires coordination among many individuals.

Strategy-formulation concepts and tools do not differ greatly for small, large, for-profit, or nonprofit organizations. However, strategy implementation varies substantially among different types and sizes of organizations. Implementing strategies requires such actions as altering sales territories, adding new departments, closing facilities, hiring new employees, changing an organization's pricing strategy, developing financial budgets, developing new employee benefits, establishing cost-control procedures, changing advertising strategies, building new facilities, training new employees, transferring managers among divisions, and building a better management information system. These types of activities obviously differ greatly among manufacturing, service, and governmental organizations.

Management Perspectives

In terms of "Quality of Management," *Fortune* recently ranked the following companies as best in the world:

Rank	Company
1	Koc Holding
2	McDonald's
3	Apple
4	Philip Morris International
5	Costco Wholesale
6	JP Morgan Chase
7	Wyndham Worldwide
8	Sysco
9	Walt Disney
10	TJX

Source: Based on: http://money.cnn.com/magazines/fortune/mostadmired/2012/best_worst/best5.html.

In all but the smallest organizations, the transition from strategy formulation to strategy implementation requires a shift in responsibility from strategists to divisional and functional managers. Implementation problems can arise because of this shift in responsibility, especially if strategy-formulation decisions come as a surprise to middle- and lower-level managers. Managers and employees are motivated more by perceived self-interests than by organizational interests, unless the two coincide. This is a primary reason why divisional and functional managers should be involved as much as possible in strategy-formulation and strategy-implementation activities.

As indicated in Table 7-1, management issues central to strategy implementation include establishing annual objectives, devising policies, allocating resources, altering an existing organizational structure, restructuring and reengineering, revising reward and incentive plans,

TABLE 7-1 Some Management Issues Central to Strategy Implementation

Establish annual objectives
Devise policies
Allocate resources
Alter an existing organizational structure
Restructure and reengineer
Revise reward and incentive plans
Minimize resistance to change
Match managers with strategy
Develop a strategy-supportive culture
Adapt production and operations processes
Develop an effective human resources function
Downsize and furlough as needed
Link performance and pay to strategies

minimizing resistance to change, matching managers with strategy, developing a strategy-supportive culture, adapting production and operations processes, developing an effective human resources function, and, if necessary, downsizing. Management changes are necessarily more extensive when strategies to be implemented move a firm in a major new direction.

Managers and employees throughout an organization should participate early and directly in strategy-implementation decisions. Their role in strategy implementation should build on prior involvement in strategy-formulation activities. Strategists' genuine personal commitment to implementation is a necessary and powerful motivational force for managers and employees. Too often, strategists are too busy to actively support strategy-implementation efforts, and their lack of interest can be detrimental to organizational success. The rationale for objectives and strategies should be understood and clearly communicated throughout an organization. Major competitors' accomplishments, products, plans, actions, and performance should be apparent to all organizational members. Major external opportunities and threats should be clear, and managers' and employees' questions should be answered. Top-down flow of communication is essential for developing bottom-up support.

Firms need to develop a competitor focus at all hierarchical levels by gathering and widely distributing competitive intelligence; every employee should be able to benchmark her or his efforts against best-in-class competitors so that the challenge becomes personal. For example, Starbucks Corp. recently instituted "lean production/operations" at its 11,000+ U.S. stores. This system eliminates idle employee time and unnecessary employee motions, such as walking, reaching, and bending. Starbucks says 30 percent of employees' time is motion and the company wants to reduce that. They say "motion and work are two different things."

Annual Objectives

Establishing annual objectives is a decentralized activity that directly involves all managers in an organization. Active participation in establishing annual objectives can lead to acceptance and commitment. **Annual objectives** are essential for strategy implementation because they (a) represent the basis for allocating resources; (b) are a primary mechanism for evaluating managers; (c) are the major instrument for monitoring progress toward achieving long-term objectives; and (d) establish organizational, divisional, and departmental priorities. Considerable time and effort should be devoted to ensuring that annual objectives are well conceived, consistent with long-term objectives, and supportive of strategies to be implemented. Approving, revising, or rejecting annual objectives is much more than a rubber-stamp activity. The purpose of annual objectives can be summarized as follows:

> Annual objectives serve as guidelines for action, directing and channeling efforts and activities of organization members. They provide a source of legitimacy in an enterprise by justifying activities to stakeholders. They serve as standards of performance. They serve as an important source of employee motivation and identification. They give incentives for managers and employees to perform. They provide a basis for organizational design.[2]

Clearly stated and communicated objectives are critical to success in all types and sizes of firms. Annual objectives, stated in terms of profitability, growth, and market share by business segment, geographic area, customer groups, and product, are common in organizations. Figure 7-2 illustrates how the Stamus Company could establish annual objectives based on long-term objectives. Table 7-2 reveals associated revenue figures that correspond to the objectives outlined in Figure 7-2. Note that, according to plan, the Stamus Company will slightly exceed its long-term objective of doubling company revenues between 2012 and 2014.

Figure 7-2 also reflects how a hierarchy of annual objectives can be established based on an organization's structure. Objectives should be consistent across hierarchical levels and form a network of supportive aims. **Horizontal consistency of objectives** is as important as **vertical consistency of objectives**. For instance, it would not be effective for manufacturing to achieve more than its annual objective of units produced if marketing could not sell the additional units.

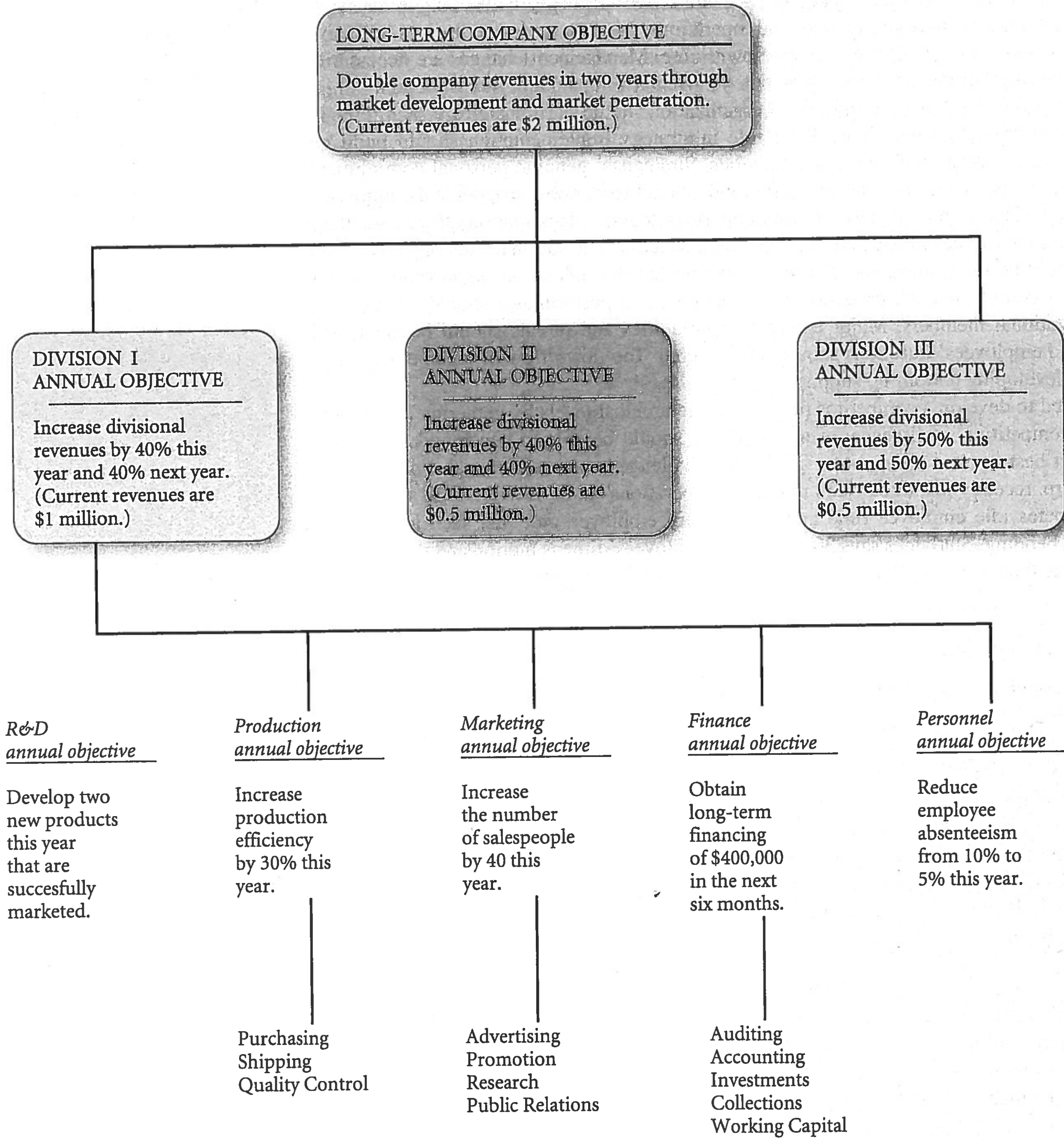


FIGURE 7-2
The Stamus Company's Hierarchy of Aims

Annual objectives should be measurable, consistent, reasonable, challenging, clear, communicated throughout the organization, characterized by an appropriate time dimension, and accompanied by commensurate rewards and sanctions. Too often, objectives are stated in generalities, with little operational usefulness. Annual objectives, such as "to improve communication" or "to improve performance," are not clear, specific, or measurable. Objectives should state quantity, quality, cost, and time—and also be verifiable. Terms and phrases such as *maximize*, *minimize*, *as soon as possible*, and *adequate* should be avoided.

Annual objectives should be compatible with employees' and managers' values and supported by clearly stated policies. More of something is not always better. Improved quality or

TABLE 7-2 The Stamus Company's Revenue Expectations (in $millions)

	2012	2013	2014
Division I Revenues	1.0	1.400	1.960
Division II Revenues	0.5	0.700	0.980
Division III Revenues	0.5	0.750	1.125
Total Company Revenues	**2.0**	**2.850**	**4.065**

reduced cost may, for example, be more important than quantity. It is important to tie rewards and sanctions to annual objectives so that employees and managers understand that achieving objectives is critical to successful strategy implementation. Clear annual objectives do not guarantee successful strategy implementation, but they do increase the likelihood that personal and organizational aims can be accomplished. Overemphasis on achieving objectives can result in undesirable conduct, such as faking the numbers, distorting the records, and letting objectives become ends in themselves. Managers must be alert to these potential problems.

Policies

Changes in a firm's strategic direction do not occur automatically. On a day-to-day basis, policies are needed to make a strategy work. Policies facilitate solving recurring problems and guide the implementation of strategy. Broadly defined, **policy** refers to specific guidelines, methods, procedures, rules, forms, and administrative practices established to support and encourage work toward stated goals. Policies are instruments for strategy implementation. Policies set boundaries, constraints, and limits on the kinds of administrative actions that can be taken to reward and sanction behavior; they clarify what can and cannot be done in pursuit of an organization's objectives. For example, Carnival's *Paradise* ship has a no smoking policy anywhere, anytime aboard ship. It was the first cruise ship to ban smoking comprehensively. Another example of corporate policy relates to surfing the Web while at work. About 40 percent of companies today do not have a formal policy preventing employees from surfing the Internet, but software is being marketed now that allows firms to monitor how, when, where, and how long various employees use the Internet at work.

Policies let both employees and managers know what is expected of them, thereby increasing the likelihood that strategies will be implemented successfully. They provide a basis for management control, allow coordination across organizational units, and reduce the amount of time managers spend making decisions. Policies also clarify what work is to be done and by whom. They promote delegation of decision making to appropriate managerial levels where various problems usually arise. Many organizations have a policy manual that serves to guide and direct behavior. Walmart has a policy that it calls the "10 Foot" Rule, whereby customers can find assistance within 10 feet of anywhere in the store. This is a welcomed policy in Japan, where Walmart is trying to gain a foothold; 58 percent of all retailers in Japan are mom-and-pop stores and consumers historically have had to pay "top yen" rather than "discounted prices" for merchandise.

Policies can apply to all divisions and departments (for example, "We are an equal opportunity employer"). Some policies apply to a single department ("Employees in this department must take at least one training and development course each year"). Whatever their scope and form, policies serve as a mechanism for implementing strategies and obtaining objectives. Policies should be stated in writing whenever possible. They represent the means for carrying out strategic decisions. Examples of policies that support a company strategy, a divisional objective, and a departmental objective are given in Table 7-3.

Some example issues that may require a management policy are provided in Table 7-4.

TABLE 7-3 A Hierarchy of Policies

Company Strategy
Acquire a chain of retail stores to meet our sales growth and profitability objectives.
Supporting Policies
1. "All stores will be open from 8 a.m. to 8 p.m. Monday through Saturday." (This policy could increase retail sales if stores currently are open only 40 hours a week.)
2. "All stores must submit a Monthly Control Data Report." (This policy could reduce expense-to-sales ratios.)
3. "All stores must support company advertising by contributing 5 percent of their total monthly revenues for this purpose." (This policy could allow the company to establish a national reputation.)
4. "All stores must adhere to the uniform pricing guidelines set forth in the Company Handbook." (This policy could help assure customers that the company offers a consistent product in terms of price and quality in all its stores.)

Divisional Objective
Increase the division's revenues from $10 million in 2014 to $15 million in 2015.
Supporting Policies
1. "Beginning in January 2014, each one of this division's salespersons must file a weekly activity report that includes the number of calls made, the number of miles traveled, the number of units sold, the dollar volume sold, and the number of new accounts opened." (This policy could ensure that salespersons do not place too great an emphasis in certain areas.)
2. "Beginning in January 2014, this division will return to its employees 5 percent of its gross revenues in the form of a Christmas bonus." (This policy could increase employee productivity.)
3. "Beginning in January 2014, inventory levels carried in warehouses will be decreased by 30 percent in accordance with a just-in-time (JIT) manufacturing approach." (This policy could reduce production expenses and thus free funds for increased marketing efforts.)

Production Department Objective
Increase production from 20,000 units in 2014 to 30,000 units in 2015.
Supporting Policies
1. "Beginning in January 2014, employees will have the option of working up to 20 hours of overtime per week." (This policy could minimize the need to hire additional employees.)
2. "Beginning in January 2014, perfect attendance awards in the amount of $100 will be given to all employees who do not miss a workday in a given year." (This policy could decrease absenteeism and increase productivity.)
3. "Beginning in January 2014, new equipment must be leased rather than purchased." (This policy could reduce tax liabilities and thus allow more funds to be invested in modernizing production processes.)

TABLE 7-4 Some Issues That May Require a Management Policy

- To offer extensive or limited management development workshops and seminars
- To centralize or decentralize employee-training activities
- To recruit through employment agencies, college campuses, or newspapers
- To promote from within or to hire from the outside
- To promote on the basis of merit or on the basis of seniority
- To tie executive compensation to long-term or annual objectives
- To offer numerous or few employee benefits
- To negotiate directly or indirectly with labor unions
- To delegate authority for large expenditures or to centrally retain this authority
- To allow much, some, or no overtime work
- To establish a high- or low-safety stock of inventory
- To use one or more suppliers
- To buy, lease, or rent new production equipment
- To greatly or somewhat stress quality control
- To establish many or only a few production standards
- To operate one, two, or three shifts
- To discourage using insider information for personal gain
- To discourage sexual harassment
- To discourage smoking at work
- To discourage insider trading
- To discourage moonlighting

Resource Allocation

Resource allocation is a central management activity that allows for strategy execution. In organizations that do not use a strategic-management approach to decision making, resource allocation is often based on political or personal factors. Strategic management enables resources to be allocated according to priorities established by annual objectives.

All organizations have at least four types of resources that can be used to achieve desired objectives: financial resources, physical resources, human resources, and technological resources. Allocating resources to particular divisions and departments does not mean that strategies will be successfully implemented. A number of factors commonly prohibit effective resource allocation, including an overprotection of resources, too great an emphasis on short-run financial criteria, organizational politics, vague strategy targets, a reluctance to take risks, and a lack of sufficient knowledge.

Below the corporate level, there often exists an absence of systematic thinking about resources allocated and strategies of the firm. Yavitz and Newman explain why:

> Managers normally have many more tasks than they can do. Managers must allocate time and resources among these tasks. Pressure builds up. Expenses are too high. The CEO wants a good financial report for the third quarter. Strategy formulation and implementation activities often get deferred. Today's problems soak up available energies and resources. Scrambled accounts and budgets fail to reveal the shift in allocation away from strategic needs to currently squeaking wheels.[3]

The real value of any resource allocation program lies in the resulting accomplishment of an organization's objectives. Effective resource allocation does not guarantee successful strategy implementation because programs, personnel, controls, and commitment must breathe life into the resources provided. Strategic management itself is sometimes referred to as a "resource allocation process."

Managing Conflict

Interdependency of objectives and competition for limited resources often leads to conflict. **Conflict** can be defined as a disagreement between two or more parties on one or more issues. Establishing annual objectives can lead to conflict because individuals have different expectations and perceptions, schedules create pressure, personalities are incompatible, and misunderstandings between line managers (such as production supervisors) and staff managers (such as human resource specialists) occur. For example, a collection manager's objective of reducing bad debts by 50 percent in a given year may conflict with a divisional objective to increase sales by 20 percent.

Establishing objectives can lead to conflict because managers and strategists must make trade-offs, such as whether to emphasize short-term profits or long-term growth, profit margin or market share, market penetration or market development, growth or stability, high risk or low risk, and social responsiveness or profit maximization. Trade-offs are necessary because no firm has sufficient resources to pursue all strategies that would benefit the firm. Table 7-5 reveals some important management trade-off decisions required in strategy implementation.

Conflict is unavoidable in organizations, so it is important that conflict be managed and resolved before dysfunctional consequences affect organizational performance. Conflict is not always bad. An absence of conflict can signal indifference and apathy. Conflict can serve to energize opposing groups into action and may help managers identify problems. General George Patton once said: "If everyone is thinking alike, then somebody isn't thinking."

Various approaches for managing and resolving conflict can be classified into three categories: avoidance, defusion, and confrontation. **Avoidance** includes such actions as ignoring the problem in hopes that the conflict will resolve itself or physically separating the conflicting individuals (or groups). **Defusion** can include playing down differences between conflicting parties while accentuating similarities and common interests, compromising so that there is neither a clear winner nor loser, resorting to majority rule, appealing to a higher authority, or redesigning present positions. **Confrontation** is exemplified by exchanging members of conflicting parties so that each can gain an appreciation of the other's point of view or holding a meeting at which conflicting parties present their views and work through their differences.

TABLE 7-5 Some Management Trade-Off Decisions Required in Strategy Implementation

To emphasize short-term profits or long-term growth
To emphasize profit margin or market share
To emphasize market development or market penetration
To lay off or furlough
To seek growth or stability
To take high risk or low risk
To be more socially responsible or more profitable
To outsource jobs or pay more to keep jobs at home
To acquire externally or to build internally
To restructure or reengineer
To use leverage or equity to raise funds
To use part-time or full-time employees

Matching Structure with Strategy

Changes in strategy often require changes in the way an organization is structured, for two major reasons. First, structure largely dictates how objectives and policies will be established. For example, objectives and policies established under a geographic organizational structure are couched in geographic terms. Objectives and policies are stated largely in terms of products in an organization whose structure is based on product groups. The structural format for developing objectives and policies can significantly impact all other strategy-implementation activities.

The second major reason why changes in strategy often require changes in structure is that structure dictates how resources will be allocated. If an organization's structure is based on customer groups, then resources will be allocated in that manner. Similarly, if an organization's structure is set up along functional business lines, then resources are allocated by functional areas. Unless new or revised strategies place emphasis in the same areas as old strategies, structural reorientation commonly becomes a part of strategy implementation.

Alfred Chandler promoted the notion that "changes in strategy lead to changes in organizational structure." Structure should be designed to facilitate the strategic pursuit of a firm and, therefore, follow strategy. Without a strategy or reasons for being (mission), companies find it difficult to design an effective structure. Chandler found a particular structure sequence to be repeated often as organizations grow and change strategy over time.

There is no one optimal organizational design or structure for a given strategy or type of organization. What is appropriate for one organization may not be appropriate for a similar firm, although successful firms in a given industry do tend to organize themselves in a similar way. For example, consumer goods companies tend to emulate the divisional structure-by-product form of organization. Small firms tend to be functionally structured (centralized). Medium-sized firms tend to be divisionally structured (decentralized). Large firms tend to use a **strategic business unit (SBU) structure** or matrix structure. As organizations grow, their structures generally change from simple to complex as a result of concatenation, or the linking together of several basic strategies.

Numerous external and internal forces affect an organization; no firm could change its structure in response to every one of these forces because to do so would lead to chaos. However, when a firm changes its strategy, the existing organizational structure may become ineffective. As indicated in Table 7-6, symptoms of an ineffective organizational structure include too many levels of management, too many meetings attended by too many people, too much attention being directed toward solving interdepartmental conflicts, too large a span of control, and too many unachieved objectives. Changes in structure can facilitate strategy-implementation efforts, but changes in structure should not be expected to make a bad strategy good, to make bad managers good, or to make bad products sell.

TABLE 7-6 Symptoms of an Ineffective Organizational Structure

1. Too many levels of management
2. Too many meetings attended by too many people
3. Too much attention being directed toward solving interdepartmental conflicts
4. Too large a span of control
5. Too many unachieved objectives
6. Declining corporate or business performance
7. Losing ground to rival firms
8. Revenue or earnings divided by number of employees or number of managers is low compared to rival firms

Structure undeniably can and does influence strategy. Strategies formulated must be workable, so if a certain new strategy required massive structural changes it would not be an attractive choice. In this way, structure can shape the choice of strategies. But a more important concern is determining what types of structural changes are needed to implement new strategies and how these changes can best be accomplished. There are seven basic types of organizational structure: functional, divisional by geographic area, divisional by product, divisional by customer, divisional process, strategic business unit (SBU), and matrix.

The Functional Structure

The most widely used structure is the functional or centralized type because this structure is the simplest and least expensive of the seven alternatives. A **functional structure** groups tasks and activities by business function, such as production and operations, marketing, finance and accounting, research and development, and management information systems. A university may structure its activities by major functions that include academic affairs, student services, alumni relations, athletics, maintenance, and accounting. Besides being simple and inexpensive, a functional structure also promotes specialization of labor, encourages efficient use of managerial and technical talent, minimizes the need for an elaborate control system, and allows rapid decision making.

Some disadvantages of a functional structure are that it forces accountability to the top, minimizes career development opportunities, and is sometimes characterized by low employee morale, line or staff conflicts, poor delegation of authority, and inadequate planning for products and markets.

A functional structure often leads to short-term and narrow thinking that may undermine what is best for the firm as a whole. For example, the research and development department may strive to overdesign products and components to achieve technical elegance, whereas manufacturing may argue for low-frills products that can be mass produced more easily. Thus, communication is often not as good in a functional structure. Schein gives an example of a communication problem in a functional structure:

> The word "marketing" will mean product development to the engineer, studying customers through market research to the product manager, merchandising to the salesperson, and constant change in design to the manufacturing manager. Then when these managers try to work together, they often attribute disagreements to personalities and fail to notice the deeper, shared assumptions that vary and dictate how each function thinks.[4]

Most large companies have abandoned the functional structure in favor of decentralization and improved accountability. However, a large company that still operates from a functional type organizational design is Southwest Airlines, headquartered in Dallas, Texas. As illustrated in Figure 7-3, Southwest has only five top executives and no divisions, even though the firm operates 700 aircraft serving 72 cities in 37 states.

Table 7-7 summarizes the advantages and disadvantages of a functional organizational structure.

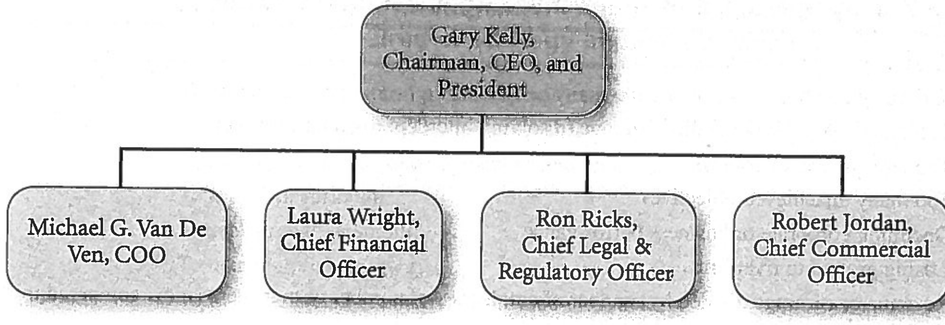


FIGURE 7-3
Southwest Airlines' Functional Organizational Chart

Source: Based on company documents.

The Divisional Structure

The **divisional structure** or **decentralized structure** is the second most common type used by U.S. businesses. As a small organization grows, it has more difficulty managing different products and services in different markets. Some form of divisional structure generally becomes necessary to motivate employees, control operations, and compete successfully in diverse locations. The divisional structure can be organized in one of four ways: *by geographic area*, *by product* or *service*, *by customer*, or *by process*. With a divisional structure, functional activities are performed both centrally and in each separate division.

Sun Microsystems recently reduced the number of its business units from seven to four. Kodak recently reduced its number of business units from seven by-customer divisions to five by-product divisions. As consumption patterns become increasingly similar worldwide, a by-product structure is becoming more effective than a by-customer or a by-geographic type divisional structure. In the restructuring, Kodak eliminated its global operations division and distributed those responsibilities across the new by-product divisions.

A divisional structure has some clear advantages. First and perhaps foremost, accountability is clear. That is, divisional managers can be held responsible for sales and profit levels. Because a divisional structure is based on extensive delegation of authority, managers and employees can easily see the results of their good or bad performances. As a result, employee morale is generally higher in a divisional structure than it is in a centralized structure. Other advantages of the divisional design are that it creates career development opportunities for managers, allows local control of situations, leads to a competitive climate within an organization, and allows new businesses and products to be added easily.

The divisional design is not without some limitations, however. Perhaps the most important limitation is that a divisional structure is costly, for a number of reasons. First, each division requires functional specialists who must be paid. Second, there exists some duplication of staff

TABLE 7-7 Advantages and Disadvantages of a Functional Organizational Structure

Advantages	Disadvantages
1. Simple and inexpensive	1. Accountability forced to the top
2. Capitalizes on specialization of business activities such as marketing and finance	2. Delegation of authority and responsibility not encouraged
3. Minimizes need for elaborate control system	3. Minimizes career development
4. Allows for rapid decision making	4. Low employee and manager morale
	5. Inadequate planning for products and markets
	6. Leads to short-term, narrow thinking
	7. Leads to communication problems

TABLE 7-8 Advantages and Disadvantages of a Divisional Organizational Structure

Advantages	Disadvantages
1. Accountability is clear	1. Can be costly
2. Allows local control of local situations	2. Duplication of functional activities
3. Creates career development chances	3. Requires a skilled management force
4. Promotes delegation of authority	4. Requires an elaborate control system
5. Leads to competitive climate internally	5. Competition among divisions can become so intense as to be dysfunctional
6. Allows easy adding of new products or regions	6. Can lead to limited sharing of ideas and resources
7. Allows strict control and attention to products, customers, or regions	7. Some regions, products, or customers may receive special treatment

services, facilities, and personnel; for instance, functional specialists are also needed centrally (at headquarters) to coordinate divisional activities. Third, managers must be well qualified because the divisional design forces delegation of authority; better-qualified individuals require higher salaries. A divisional structure can also be costly because it requires an elaborate, headquarters-driven control system. Fourth, competition between divisions may become so intense that it is dysfunctional and leads to limited sharing of ideas and resources for the common good of the firm. Table 7-8 summarizes the advantages and disadvantages of divisional organizational structure.

Ghoshal and Bartlett, two leading scholars in strategic management, note the following:

> As their label clearly warns, divisions divide. The divisional model fragments companies' resources; it creates vertical communication channels that insulate business units and prevents them from sharing their strengths with one another. Consequently, the whole of the corporation is often less than the sum of its parts. A final limitation of the divisional design is that certain regions, products, or customers may sometimes receive special treatment, and it may be difficult to maintain consistent, companywide practices. Nonetheless, for most large organizations and many small firms, the advantages of a divisional structure more than offset the potential limitations.[5]

A *divisional structure by geographic area* is appropriate for organizations whose strategies need to be tailored to fit the particular needs and characteristics of customers in different geographic areas. This type of structure can be most appropriate for organizations that have similar branch facilities located in widely dispersed areas. A divisional structure by geographic area allows local participation in decision making and improved coordination within a region. Hershey Foods is an example company organized using the divisional-by-region type of structure, as illustrated in Figure 7-4. Analysts contend that this type of structure may not be best for Hershey because consumption patterns for candy are quite similar worldwide. An alternative—and perhaps better—type of structure for Hershey would be divisional by product because the company produces, and sells three types of products worldwide: (1) chocolate, (2) nonchocolate, and (3) grocery.

The *divisional structure by product (or services)* is most effective for implementing strategies when specific products or services need special emphasis. Also, this type of structure is widely used when an organization offers only a few products or services or when an organization's products or services differ substantially. The divisional structure allows strict control over and attention to product lines, but it may also require a more skilled management force and reduced top management control. General Motors, DuPont, Microsoft, and Procter & Gamble use a divisional structure by product to implement strategies. Microsoft introduced its new Surface Tablet for $499 in late 2012. The Surface is being sold online and in Microsoft retail stores, but not in stores such as Best Buy or Walmart, or even Amazon. Microsoft's divisional-by-product organizational structure is illustrated in Figure 7-5.

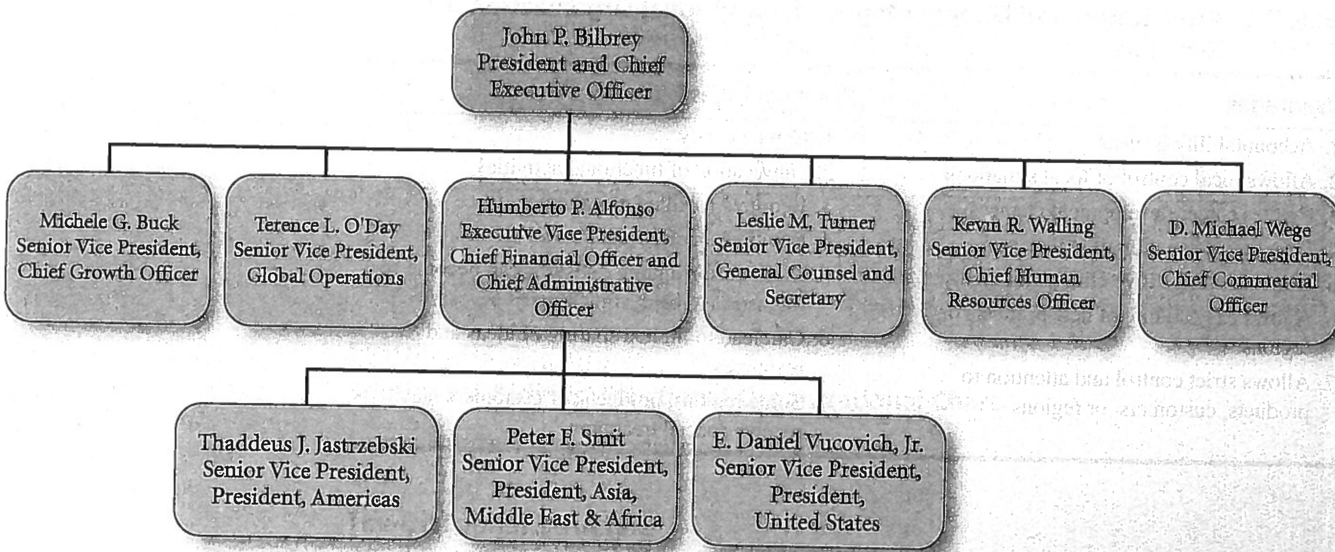


FIGURE 7-4
Hershey Foods' Divisional-by-Region Organizational Chart

Source: Based on company documents.

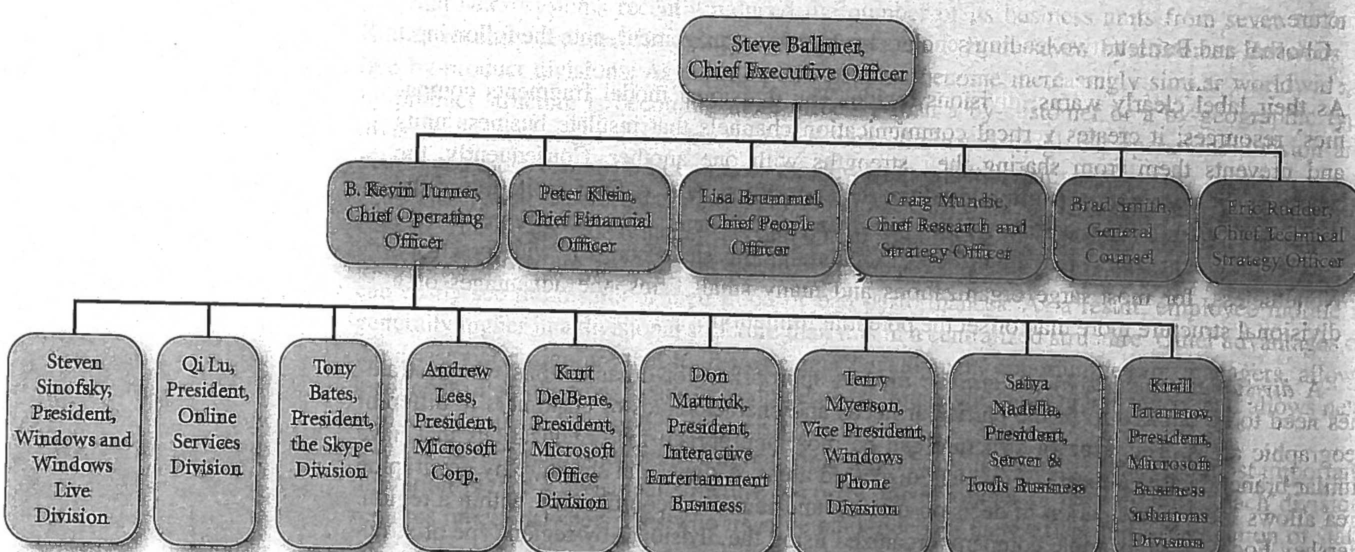


FIGURE 7-5
Microsoft's Divisional-by-Product Organizational Structure

Source: Based on company documents.

When a few major customers are of paramount importance and many different services are provided to these customers, then a *divisional structure by customer* can be the most effective way to implement strategies. This structure allows an organization to cater effectively to the requirements of clearly defined customer groups. For example, book publishing companies often organize their activities around customer groups, such as colleges, secondary schools, and private commercial schools. Some airline companies have two major customer divisions: passengers and freight or cargo services. Utility companies often use (1) commercial, (2) residential, and (3) industrial as their divisions by customer.

A *divisional structure by process* is similar to a functional structure, because activities are organized according to the way work is actually performed. However, a key difference between these two designs is that functional departments are not accountable for profits or revenues, whereas divisional process departments are evaluated on these criteria. An example of a divisional structure by process is a manufacturing business organized into six divisions: electrical work, glass cutting, welding, grinding, painting, and foundry work. In this case, all operations related to these specific processes would be grouped under the separate divisions. Each process (division) would be responsible for generating revenues and profits. The divisional structure by process can be particularly effective in achieving objectives when distinct production processes represent the thrust of competitiveness in an industry. Halliburton's organizational chart illustrated on the next page features aspects of the division-by-process design.

The Strategic Business Unit (SBU) Structure

As the number, size, and diversity of divisions in an organization increase, controlling and evaluating divisional operations become increasingly difficult for strategists. Increases in sales often are not accompanied by similar increases in profitability. The span of control becomes too large at top levels of the firm. For example, in a large conglomerate organization composed of 90 divisions, such as ConAgra, the chief executive officer could have difficulty even remembering the first names of divisional presidents. In multidivisional organizations, an SBU structure can greatly facilitate strategy-implementation efforts. ConAgra has put its many divisions into three primary SBUs: (1) food service (restaurants), (2) retail (grocery stores), and (3) agricultural products.

The SBU structure groups similar divisions into SBUs and delegates authority and responsibility for each unit to a senior executive who reports directly to the chief executive officer. This change in structure can facilitate strategy implementation by improving coordination between similar divisions and channeling accountability to distinct business units. In a 100-division conglomerate, the divisions could perhaps be regrouped into 10 SBUs according to certain common characteristics, such as competing in the same industry, being located in the same area, or having the same customers.

Two disadvantages of an SBU structure are that it requires an additional layer of management, which increases salary expenses. Also, the role of the group vice president is often ambiguous. However, these limitations often do not outweigh the advantages of improved coordination and accountability. Another advantage of the SBU structure is that it makes the tasks of planning and control by the corporate office more manageable.

News Corp. recently reorganized its operations into two SBUs: (1) Entertainment, which includes 20th Century Fox, Fox Broadcast News, and the Fox News Channel, and (2) Publishing, which includes The *Wall Street Journal*, *Times of London*, *The Sun* newspaper, *The Australian* newspaper, and HarperCollins book publishing. News Corp.'s Chairman and CEO, Rupert Murdoch, is retaining his family's 40 percent voting stake in what may result in two separate companies. Estimated 2014 revenue in billions of dollars by division within the Publishing SBU is as follows:

Australia newspapers (2.19)
Dow Jones (2.07)
U.K. newspapers (1.34)
Book publishing (1.25)
Marketing services (0.97)
Fox Sports (0.62)
REA Group (0.37)
NY Post, other (0.30)
Education business (0.12)

Apparently to groom a new CEO, Coca-Cola recently streamlined its organizational structure by converting to three SBUs: (1) The Americas Beverages headed by Cahillane, (2) Outside-The-Americas Beverages headed by Bozer, and (3) Outside-The-Americas Bottlers headed by Finan. Coke CEO Muhtar Kent said "Consolidating leadership under the three groups

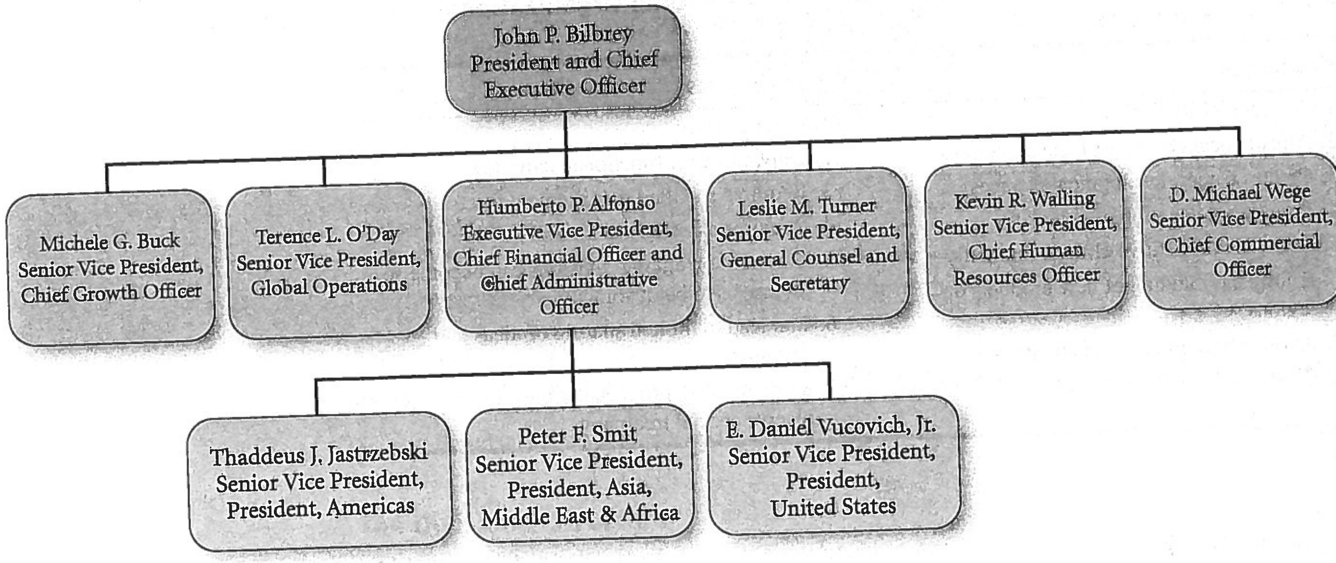
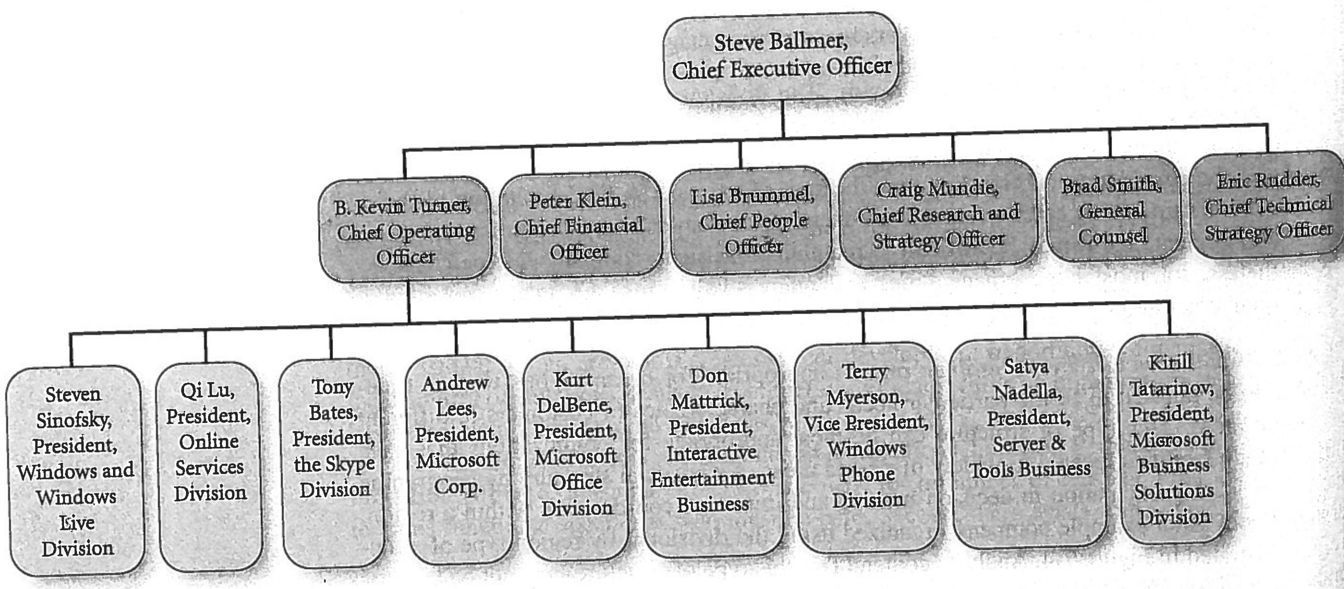


FIGURE 7-4
Hershey Foods' Divisional-by-Region Organizational Chart

Source: Based on company documents.



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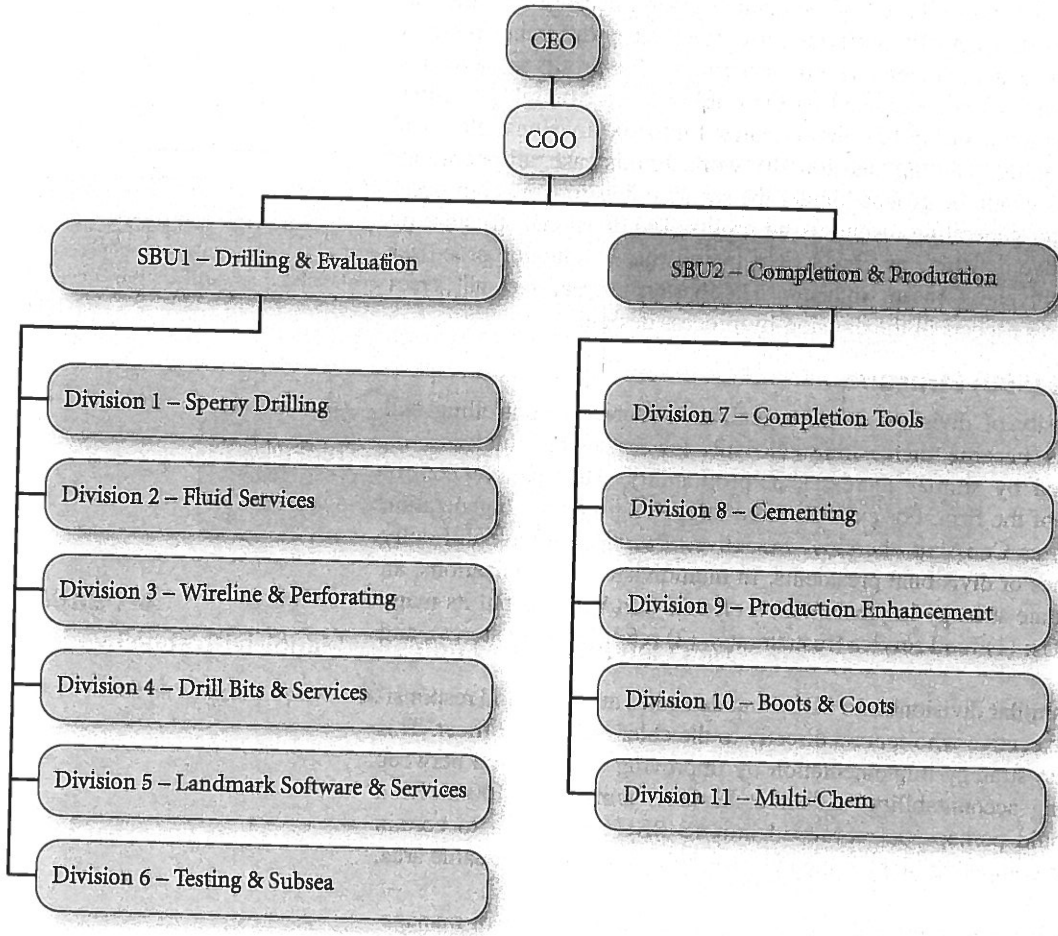

FIGURE 7-6

Halliburton Company's SBU Organizational Chart

Source: Based on http://www.halliburton.com/AboutUs/default.aspx?pageid=2458&navid=966.

will streamline reporting lines and intensify our focus on key markets." Either Mr. Cahillane and Mr. Bozer are expected to replace Mr. Kent as CEO sometime in the future, although Mr. Kent says: "As long as I'm having fun, my health allows me to continue and I'm generating good returns for our shareholders, and importantly as long as I'm smiling, which is important in anything you do, then I will continue."[6]

An excellent example of an SBU organizational chart is the one posted at the Halliburton Company website and shown in Figure 7-6. Note that six division executives report to the Drilling and Evaluation top executive, whereas five division heads report to the Completion and Production top executive. It is interesting and somewhat unusual that the 11 Halliburton divisions are organized by process rather than by geographic region or product.

The Matrix Structure

A **matrix structure** is the most complex of all designs because it depends on both vertical and horizontal flows of authority and communication (hence the term *matrix*). In contrast, functional and divisional structures depend primarily on vertical flows of authority and communication. A matrix structure can result in higher overhead because it creates more management positions. Other disadvantages of a matrix structure that contribute to overall complexity include dual lines of budget authority (a violation of the unity-of-command principle), dual sources of reward and punishment, shared authority, dual reporting channels, and a need for an extensive and effective communication system.

Despite its complexity, the matrix structure is widely used in many industries, including construction, health care, research, and defense. As indicated in Table 7-9, some advantages of a

TABLE 7-9 Advantages and Disadvantages of a Matrix Structure

Advantages	Disadvantages
1. Project objectives are clear	1. Requires excellent vertical and horizontal flows of communication
2. Employees can clearly see results of their work	2. Costly because creates more manager positions
3. Shutting down a project is easily accomplished	3. Violates unity of command principle
4. Facilitates uses of special equipment, personnel, and facilities	4. Creates dual lines of budget authority
5. Functional resources are shared instead of duplicated as in a divisional structure	5. Creates dual sources of reward and punishment
	6. Creates shared authority and reporting
	7. Requires mutual trust and understanding

matrix structure are that project objectives are clear, there are many channels of communication, workers can see the visible results of their work, and shutting down a project can be accomplished relatively easily. Another advantage of a matrix structure is that it facilitates the use of specialized personnel, equipment, and facilities. Functional resources are shared in a matrix structure, rather than duplicated as in a divisional structure. Individuals with a high degree of expertise can divide their time as needed among projects, and they in turn develop their own skills and competencies more than in other structures.

A typical matrix structure is illustrated in Figure 7-7. Note that the letters (A through Z4) refer to managers. For example, if you were manager A, you would be responsible for financial aspects of Project 1, and you would have two bosses: the Project 1 Manager on site and the CFO off site.

For a matrix structure to be effective, organizations need participative planning, training, clear mutual understanding of roles and responsibilities, excellent internal communication, and mutual trust and confidence. The matrix structure is being used more frequently by U.S. businesses because firms are pursuing strategies that add new products, customer groups, and technology to their range of activities. Out of these changes are coming product managers, functional managers, and geographic-area managers, all of whom have important strategic responsibilities. When several variables, such as product, customer, technology, geography, functional area, and line of business, have roughly equal strategic priorities, a matrix organization can be an effective structural form.

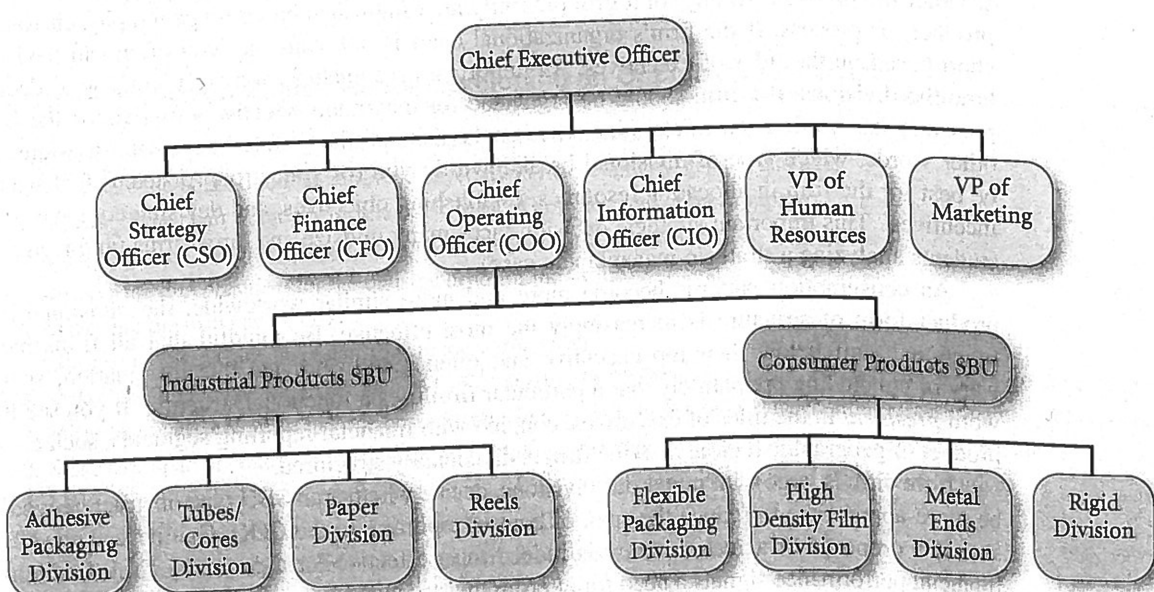

FIGURE 7-7
An Example Matrix Structure