

Organizational Structure

Chapter 9 = Chapter 14 on Connect



What Is Organizational Architecture?

- **Organizational architecture** is the totality of a firm's organization including

1. Organizational structure

- the formal division of the organization into subunits
- the location of decision-making responsibilities within that structure
 - centralized versus decentralized
- the establishment of integrating mechanisms to coordinate the activities of subunits including cross-functional teams or pan-regional committees

What Is Organizational Architecture?

2. Control systems and incentives

- **control systems** - the metrics used to measure performance of subunits
- **incentives** - the devices used to reward managerial behavior

What Is Organizational Architecture?

3. Processes, organizational culture, and people

- **processes** - how decisions are made and work is performed within the organization
- **organizational culture** - norms and values that are shared among the employees of an organization
- **people** - the employees and the strategy used to recruit, compensate, and retain those individuals and the type of people they are in terms of their skills, values, and orientation

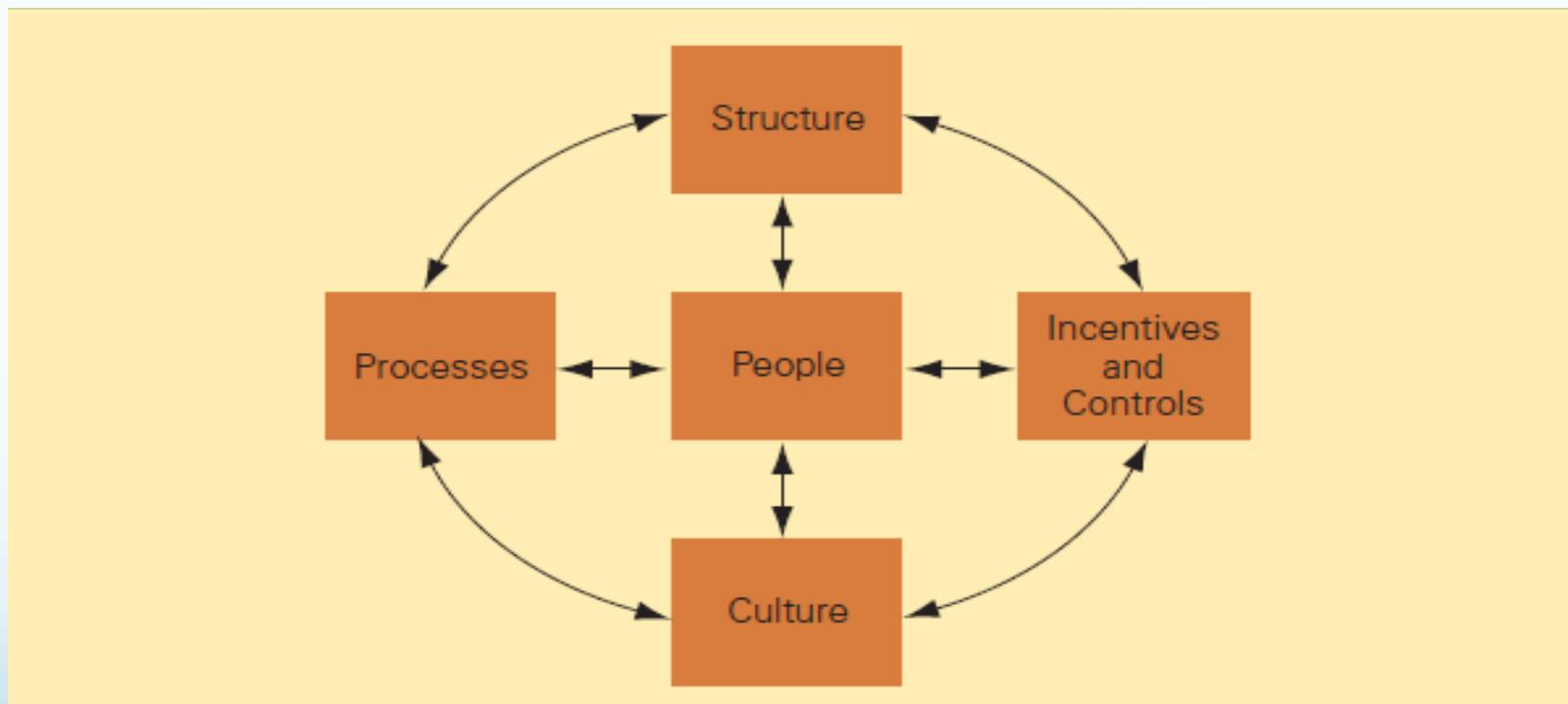


What Is Organizational Architecture?

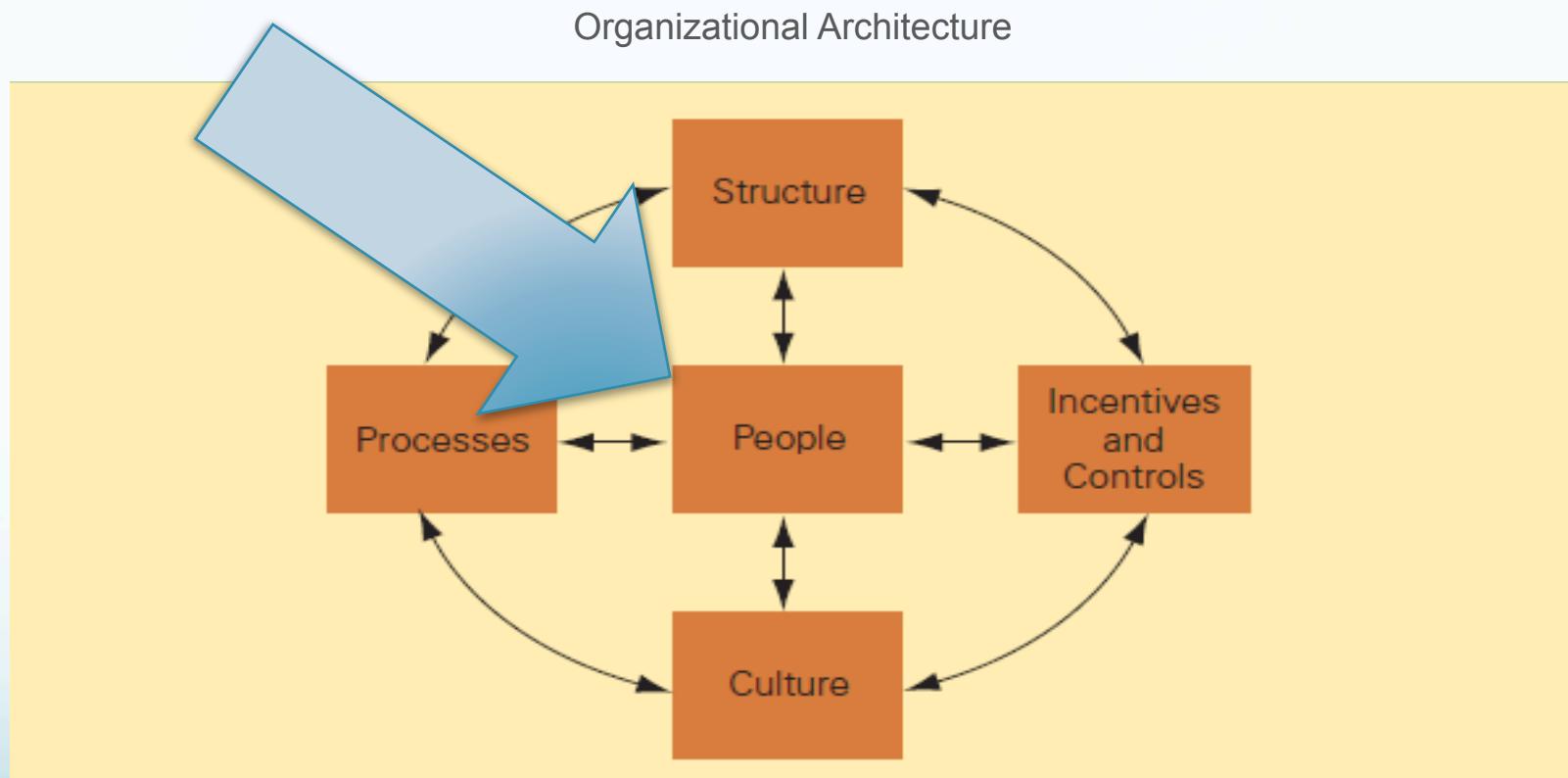
- To be the most profitable
 - the elements of the organizational architecture must be internally consistent
 - the organizational architecture must fit the strategy
 - the strategy and architecture must be consistent with each other, and consistent with competitive conditions

What Is Organizational Architecture?

Organizational Architecture



What Is Organizational Architecture?



What Are the Dimensions of Organizational Structure?

- Organizational structure has three dimensions
 1. **Vertical differentiation** - the location of decision-making responsibilities within a structure
 2. **Horizontal differentiation** - the formal division of the organization into subunits
 3. **Integrating mechanisms** - the mechanisms for coordinating subunits

Why Is Vertical Differentiation Important?

- Vertical differentiation determines where decision-making power is concentrated
- **Centralized decision making**
 - facilitates coordination
 - ensures decisions are consistent with the organization's objectives
 - gives managers the means to bring about organizational change
 - avoids duplication of activities

Why Is Vertical Differentiation Important?

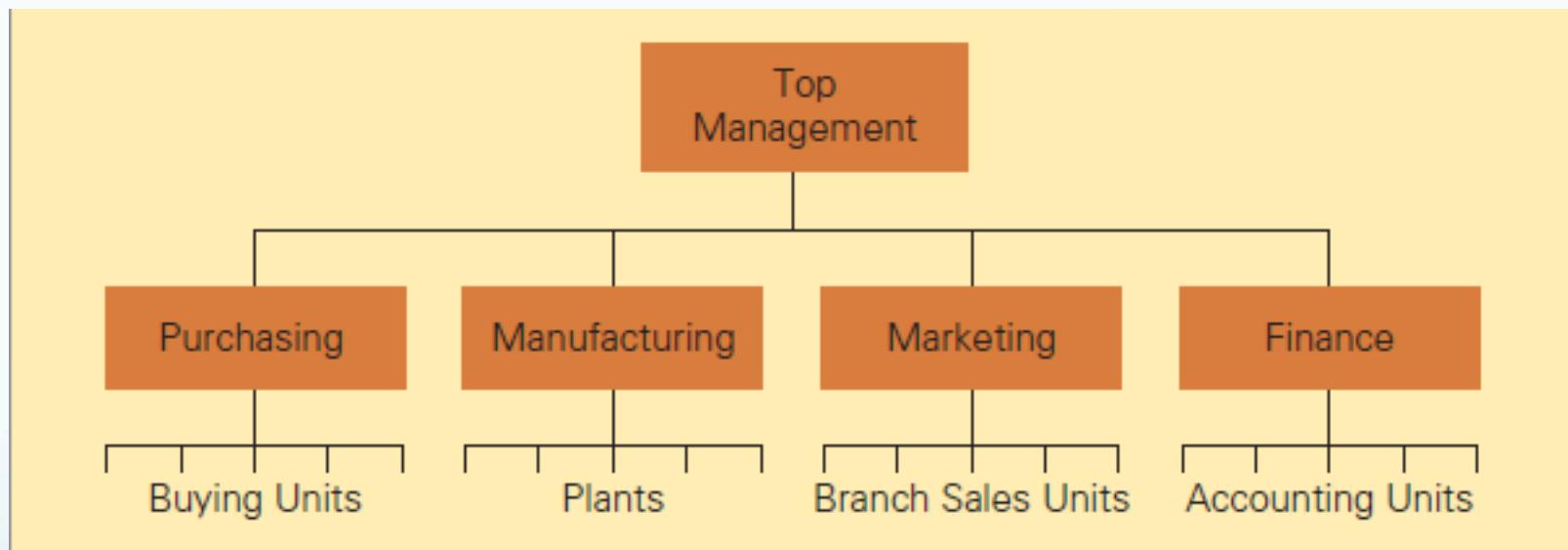
- Decentralized decision making
 - relieves the burden of centralized decision making
 - has been shown to motivate individuals
 - permits greater flexibility
 - can result in better decisions
 - can increase control

Why Is Horizontal Differentiation Important?

- Horizontal differentiation refers to how the firm divides into subunits
 - usually based on function, type of business, or geographical area
- Most firms begin with no formal structure, but as they grow, split into functions reflecting the firm's value creation activities - **functional structure**
 - functions are coordinated and controlled by top management
 - decision making is centralized
 - product line diversification requires further horizontal differentiation

What Is a Functional Structure?

A Typical Functional Structure

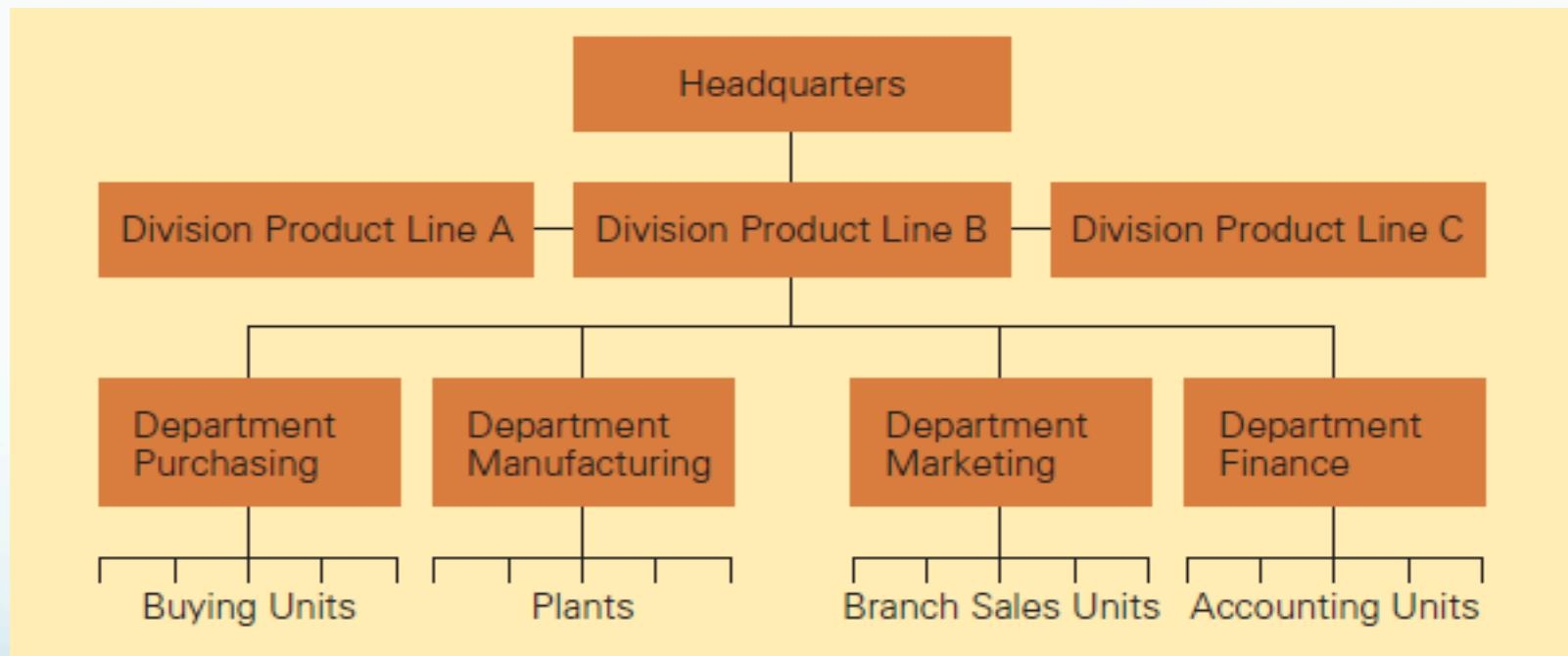


Why Is Horizontal Differentiation Important?

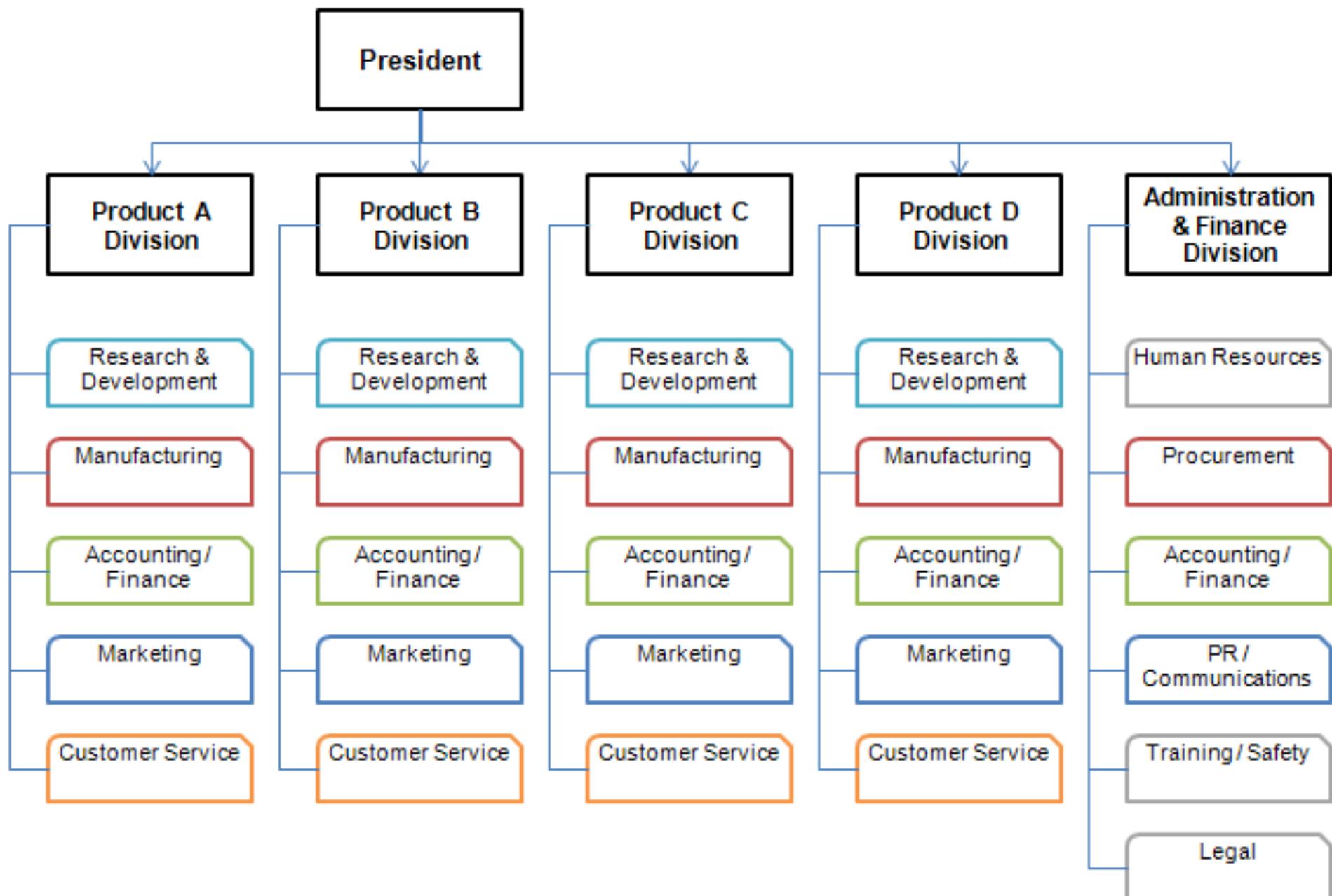
- Firms may switch to a product divisional structure
 - each division is responsible for a distinct product line
 - headquarters retains control for the overall strategic direction of the firm and for the financial control of each division

What Is a Product Divisional Structure?

A Typical Product Divisional Structure



Sample Divisional Organizational Structure

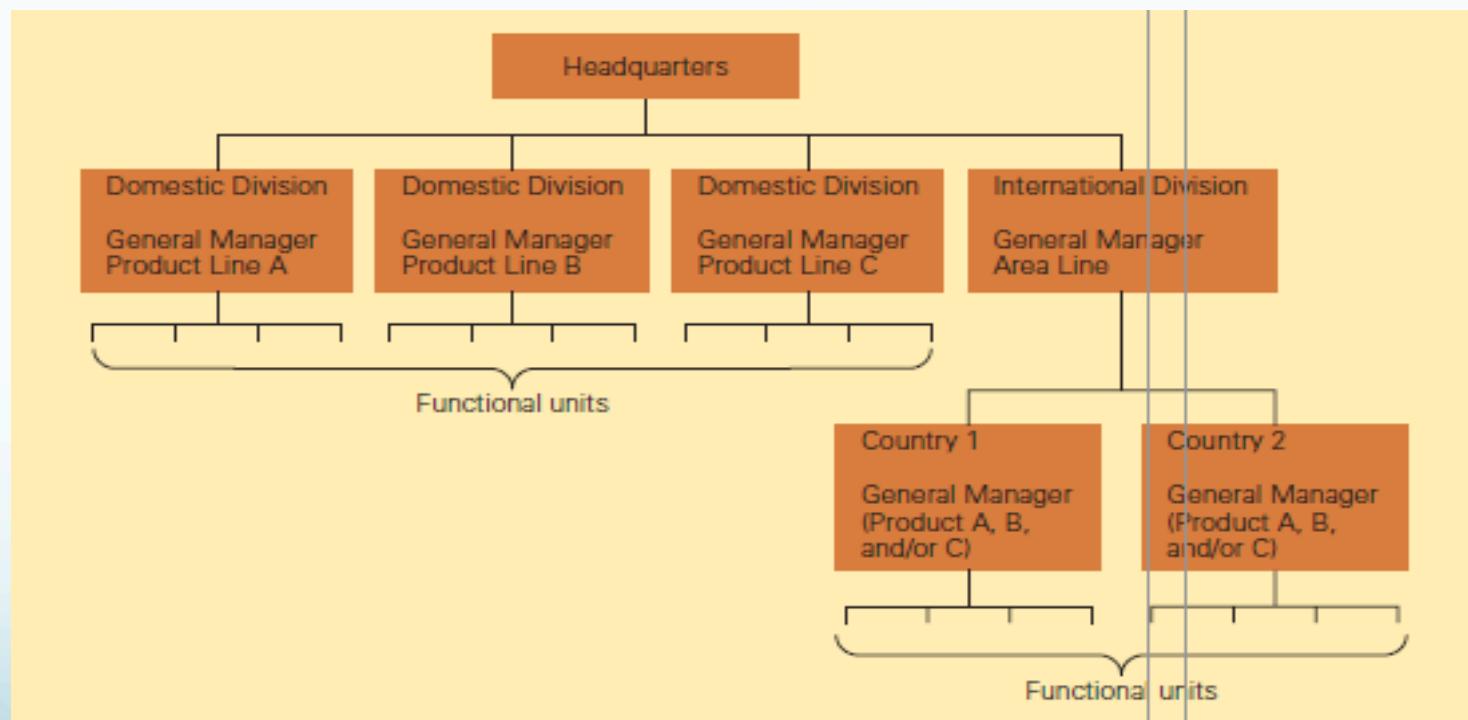


What Happens When Firms Expand Globally?

- When firms expand internationally, they often group all of their international activities into an **international division**
- Over time, manufacturing may shift to foreign markets
 - firms with a functional structure at home would replicate the functional structure in the foreign market
 - firms with a divisional structure would replicate the divisional structure in the foreign market
- In either case, there is the potential for conflict and coordination problems between domestic and foreign operations

What Is an International Division Structure?

One Company's International Division Structure

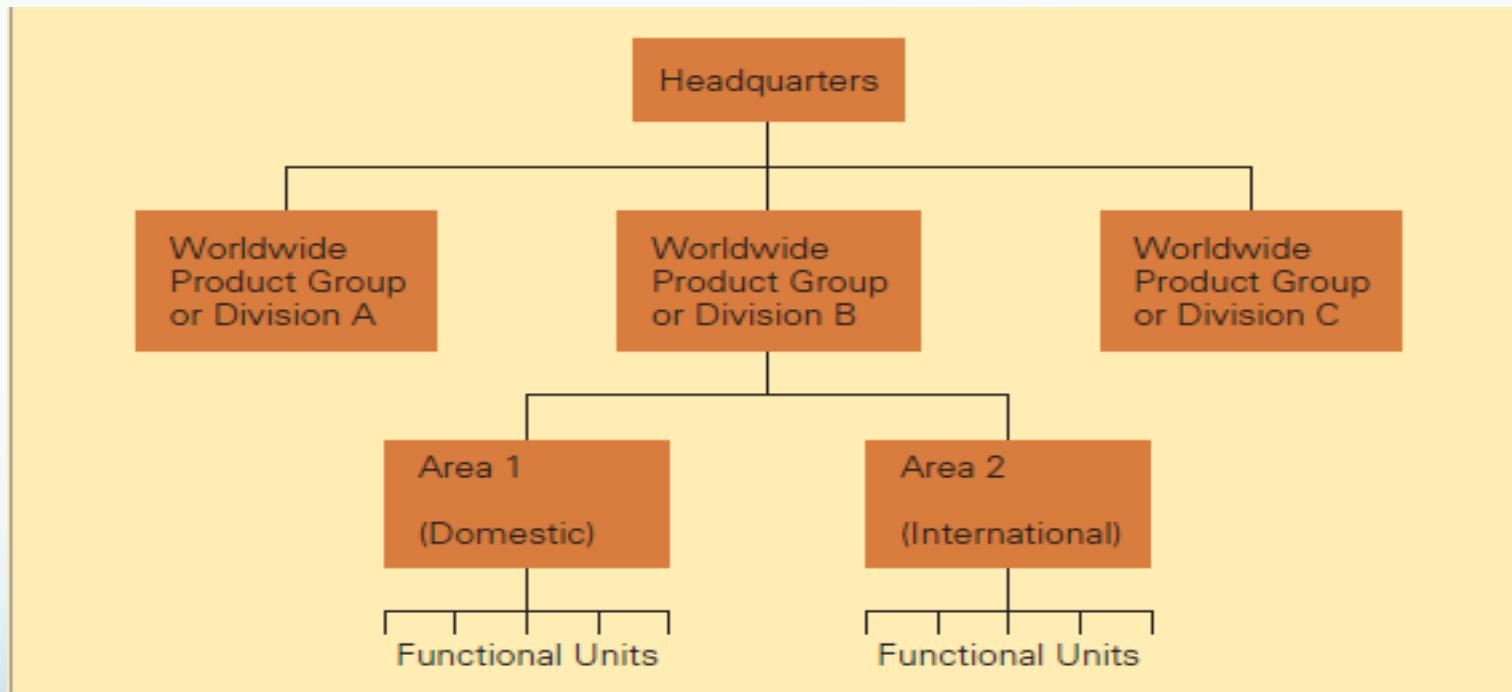


What Happens Next?

- Firms that continue to expand will move to either a
 1. **Worldwide product division structure** - adopted by firms that are reasonably diversified
 - allows for worldwide coordination of value creation activities of each product division
 - helps realize location and experience curve economies
 - facilitates the transfer of core competencies
 - does not allow for local responsiveness

What Is a Worldwide Product Division Structure?

A Worldwide Product Divisional Structure

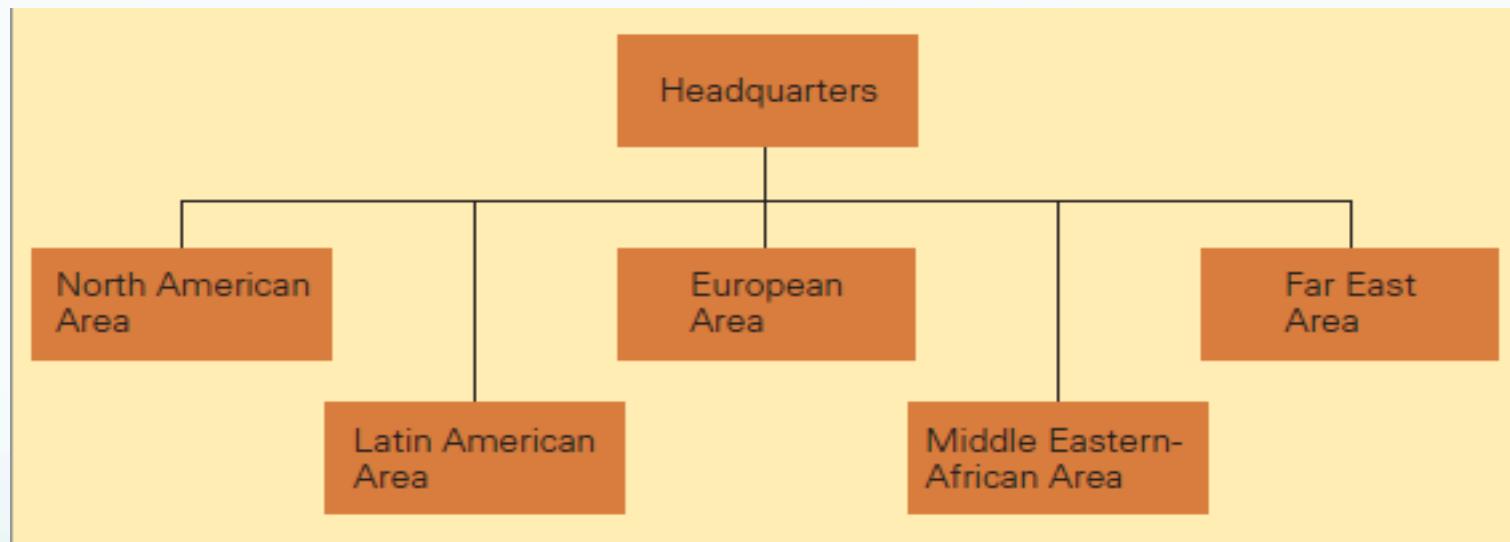


What Happens Next?

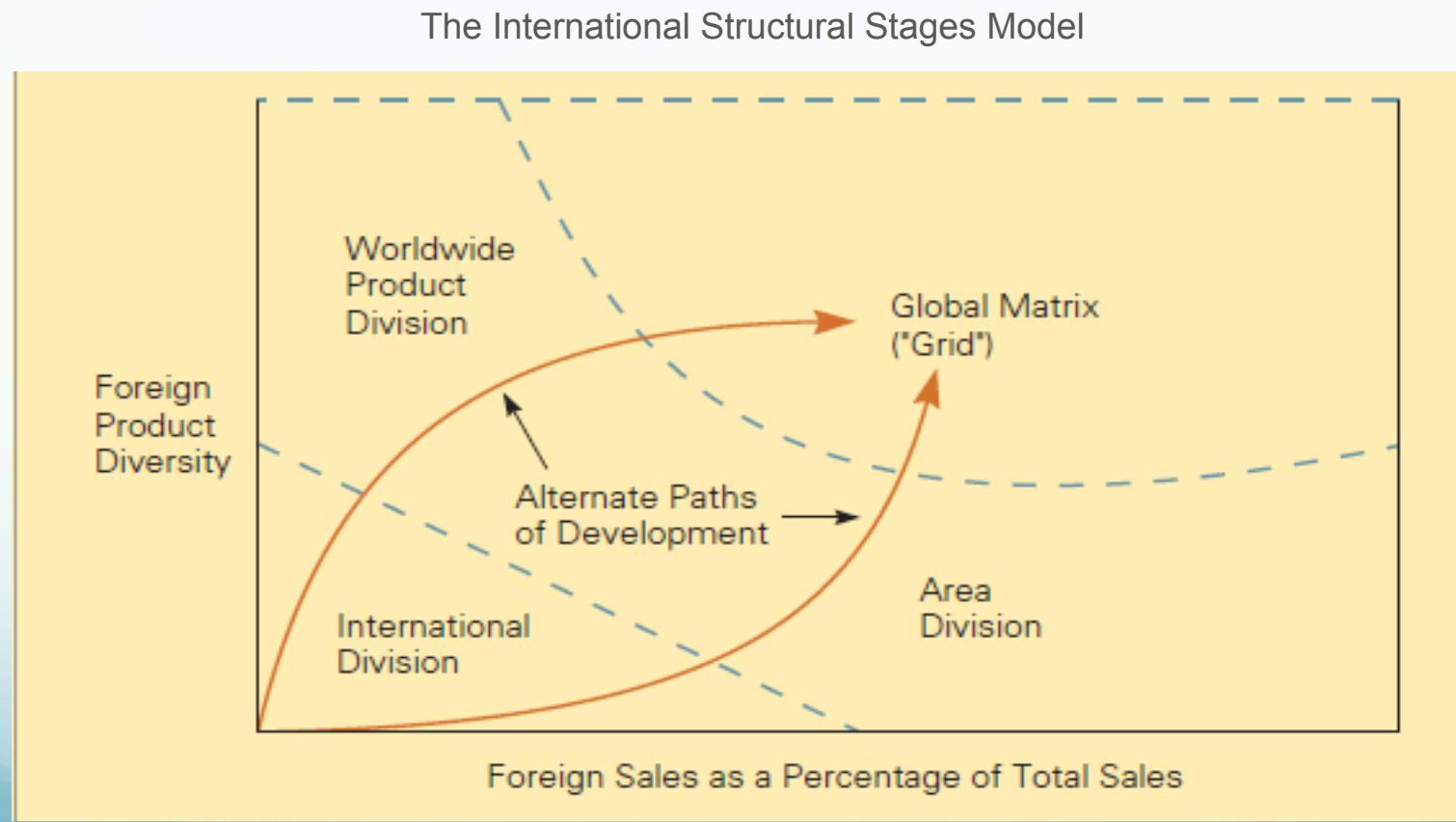
2. Worldwide area structure - favored by firms with low degree of diversification and a domestic structure based on function
 - divides the world into autonomous geographic areas
 - decentralizes operational authority
 - facilitates local responsiveness
 - can result in a fragmentation of the organization
 - is consistent with a localization strategy

What Is a Worldwide Area Structure?

A Worldwide Area Structure



How Does Organizational Structure Change over Time?

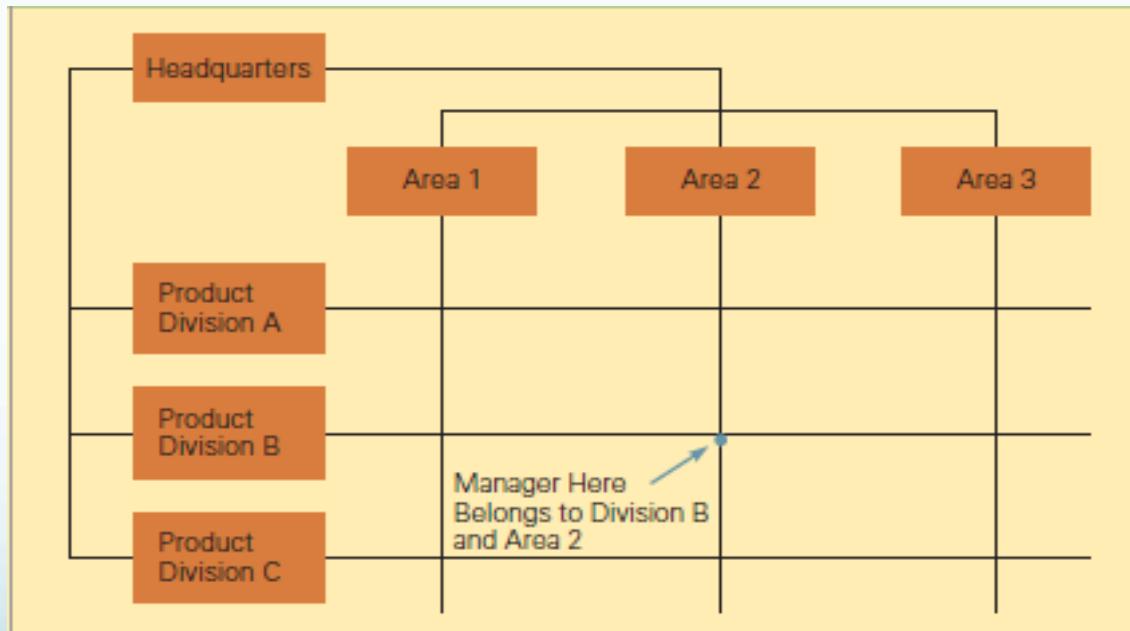


What Is the Global Matrix Structure?

- The **global matrix structure** – tries to minimize the limitations of the worldwide area structure and the worldwide product divisional structure
 - allows for differentiation along two dimensions - product division and geographic area
 - has dual decision making - product division and geographic area have equal responsibility for operating decisions
 - can be bureaucratic and slow
 - can result in conflict between areas and product divisions
 - can result in finger-pointing between divisions when something goes wrong

What Is the Global Matrix Structure?

A Global Matrix Structure

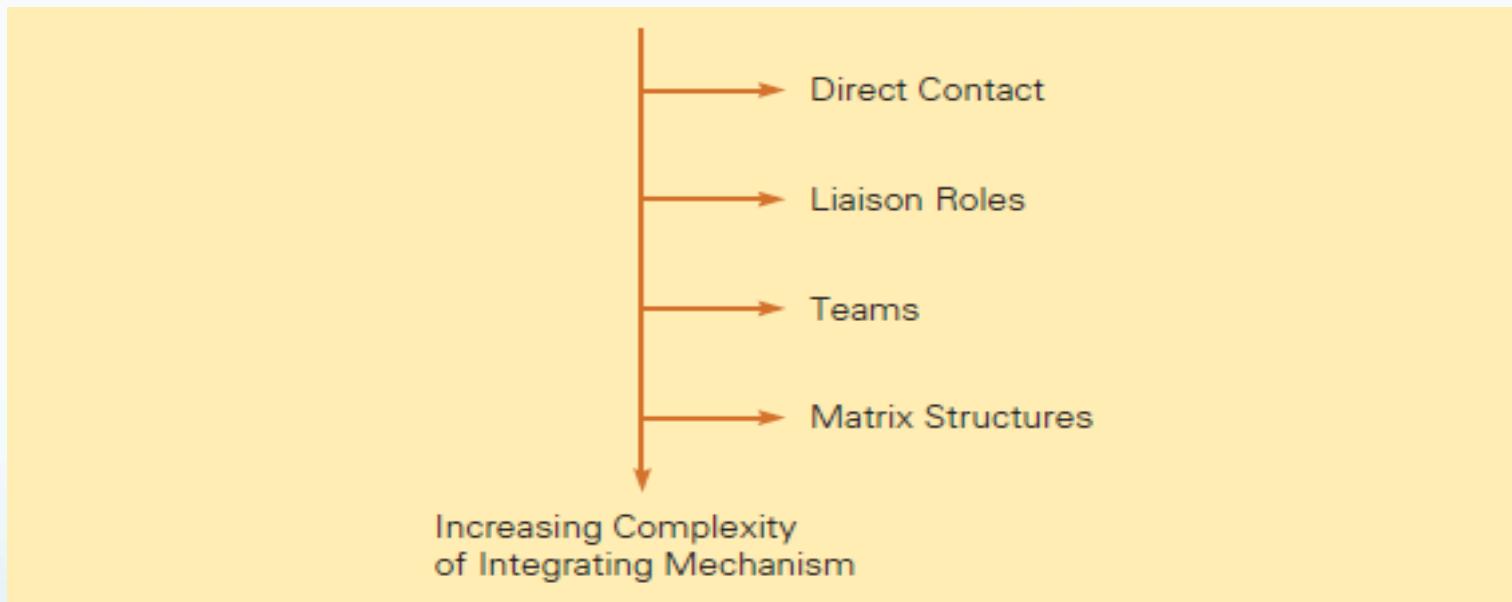


How Can Subunits Be Integrated?

- Regardless of the type of structure, firms need a mechanism to integrate subunits
 - need for coordination is lowest in firms with a localization strategy and highest in transnational firms
 - coordination can be complicated by differences in subunit orientation and goals
 - simplest formal integrating mechanism is direct contact between subunit managers, followed by liaisons
 - temporary or permanent teams composed of individuals from each subunit is the next level of formal integration
 - the matrix structure allows for all roles to be integrating roles

How Can Subunits Be Integrated?

Formal Integrating Mechanisms

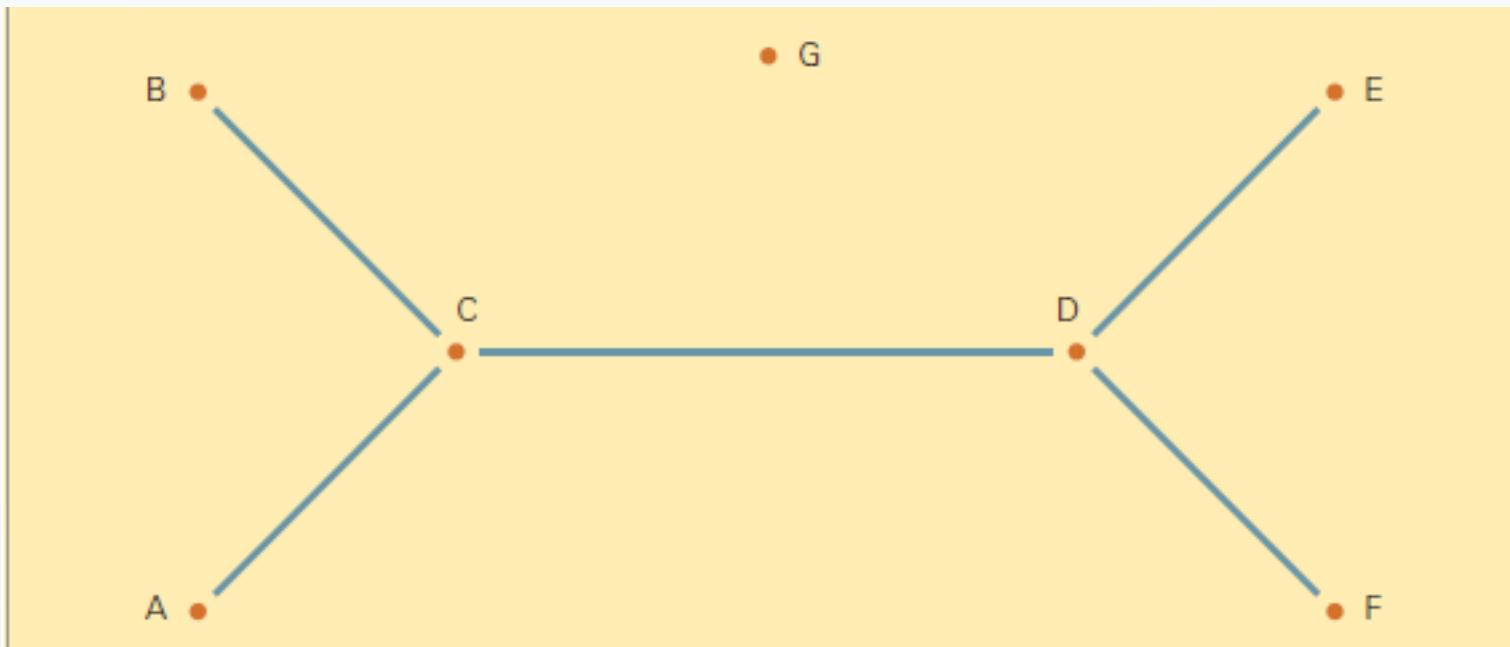


How Can Subunits Be Integrated?

- Many firms use informal integrating mechanisms
- A knowledge network - network for transmitting information within an organization that is based not on informal contacts between managers and on distributed information systems
 - a non-bureaucratic conduit for knowledge flows
 - must embrace as many managers as possible and managers must adhere to a common set of norms and values that override differing subunit orientations

How Can Subunits Be Integrated?

A Simple Management Network



What Are the Different Types of Control Systems?

1. **Personal controls** –personal contact with subordinates
 - most widely used in small firms
2. **Bureaucratic controls** –a system of rules and procedures that directs the actions of subunits
 - budgets and capital spending rules

What Are the Different Types of Control Systems?

3. **Output controls** – setting goals for subunits to achieve and expressing those goals in terms of objective performance metrics
 - compare actual performance against targets and intervene selectively to take corrective action
4. **Cultural controls** – exist when employees “buy into” the norms and value systems of the firm
 - strong culture implies less need for other forms of control

What Are Incentive Systems?

- Incentives - devices used to reward behavior
 - usually closely tied to performance metrics used for output controls
 - should vary depending on the employee and the nature of the work being performed
 - should promote cooperation between managers in sub-units
 - should reflect national differences in institutions and culture
 - can have unintended consequences

What Is Performance Ambiguity?

- **Performance ambiguity** exists when the causes of a subunit's poor performance are not clear
 - is common when a subunit's performance is dependent on the performance of other subunits
 - is lowest in firms with a localization strategy
 - is higher in international firms
 - is still higher in firms with a global standardization strategy
 - is highest in transnational firms

What Is the Link Between Control, Incentives, And Strategy?

Interdependence, Performance Ambiguity, and the Costs of Control for the Four International Business Strategies

Strategy	Interdependence	Performance Ambiguity	Costs of Control
Localization	Low	Low	Low
International	Moderate	Moderate	Moderate
Global	High	High	High
Transnational	Very high	Very high	Very high

What Are Processes?

- **Processes** refer to the manner in which decisions are made and work is performed
 - many processes cut across national boundaries as well as organizational boundaries
 - processes can be developed anywhere within a firm's global operations network
 - formal and informal integrating mechanisms can help firms leverage processes

What Is Organizational Culture?

- **Organizational culture** - the values and norms that employees are encouraged to follow
- Evolves from
 - founders and important leaders
 - national social culture
 - the history of the enterprise
 - decisions that resulted in high performance

What Is Organizational Culture?

- Organizational culture can be maintained through
 - hiring and promotional practices
 - reward strategies
 - socialization processes
 - communication strategies
- Organizational culture tends to change very slowly

What Is Organizational Culture?

- Managers in companies with a “strong” culture share a relatively consistent set of values and norms that have a clear impact on the way work is performed
- A “strong” culture
 - is not always good
 - may not lead to high performance
 - could be beneficial at one point, but not at another
- Companies with adaptive cultures have the highest performance

What Is the Link Between Strategy And Architecture?

A Synthesis of Strategy, Structure, and Control Systems

Structure and Controls	Strategy			
	Localization	International	Global Standardization	Transnational
Vertical differentiation	Decentralized	Core competency more centralized; rest decentralized	Some centralization	Mixed centralization and decentralization
Horizontal differentiation	Worldwide area structure	Worldwide product divisions	Worldwide product divisions	Informal matrix
Need for coordination	Low	Moderate	High	Very high
Integrating mechanisms	None	Few	Many	Very many
Performance ambiguity	Low	Moderate	High	Very high
Need for cultural controls	Low	Moderate	High	Very high

What Is the Link Between Strategy And Architecture?

1. Firms pursuing a **localization strategy** focus on local responsiveness
 - they do not have a high need for integrating mechanisms
 - performance ambiguity and the cost of control tend to be low
 - the worldwide area structure is common

What Is the Link Between Strategy And Architecture?

2. Firms pursuing an **international strategy** create value by transferring core competencies from home to foreign subsidiaries
 - the need for control is moderate
 - the need for integrating mechanisms is moderate
 - performance ambiguity is relatively low and so is the cost of control
 - the worldwide product division structure is common

What Is the Link Between Strategy And Architecture?

3. Firms pursuing a **global standardization** strategy focus on the realization of location and experience curve economies
 - headquarters maintains control over most decisions
 - the need for integrating mechanisms is high
 - strong organizational cultures are encouraged
 - the worldwide product division is common

What Is the Link Between Strategy And Architecture?

4. Firms pursuing a **transnational strategy** focus on simultaneously attaining location and experience curve economies, local responsiveness, and global learning
 - some decisions are centralized and others are decentralized
 - the need for coordination and cost of control is high
 - an array of formal and informal integrating mechanism are used
 - a strong culture is encouraged
 - matrix structures are common

How Are the Environment, Strategy, Architecture and Performance Related?

- For a firm to succeed
 - 1. The firm's strategy must be consistent with the environment in which the firm operates
 - 2. The firm's organization architecture must be consistent with its strategy
 - firms need to change their architecture to reflect changes in the environment in which they are operating and the strategy they are pursuing



How Can Firms Implement Organizational Change?

- To implement organization change
1. Unfreeze the organization through shock therapy
 - requires taking bold actions like plant closures or dramatic structural reorganizations
 2. Move the organization to a new state through proactive change in architecture
 - requires a substantial and quick change in organizational architecture so that it matches the desired new strategic posture
 3. Refreeze the organization in its new state
 - requires that employees be socialized into the new way of doing things

How Can Firms Implement Organizational Change?

- Organizations can be difficult to change because of
 - the existing distribution of power and influence
 - the current culture
 - managers' preconceptions about the appropriate business model or paradigm
 - institutional constraints

