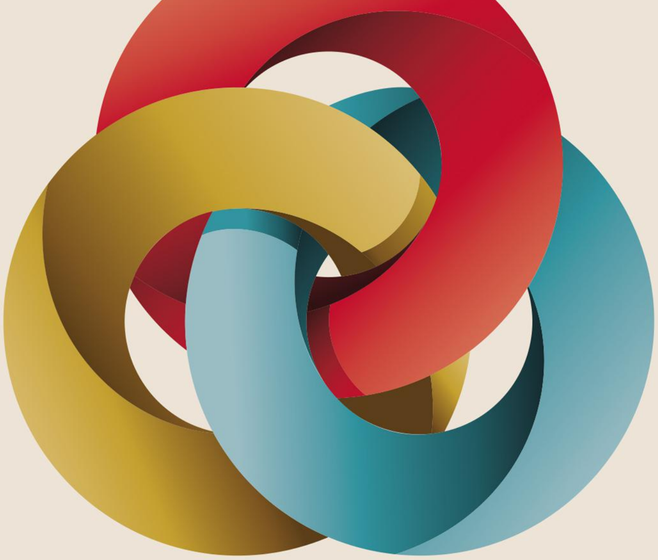
MANAGEMENT

AN INTEGRATED APPROACH



SECOND EDITION

GULATI MAYO NOHRIA

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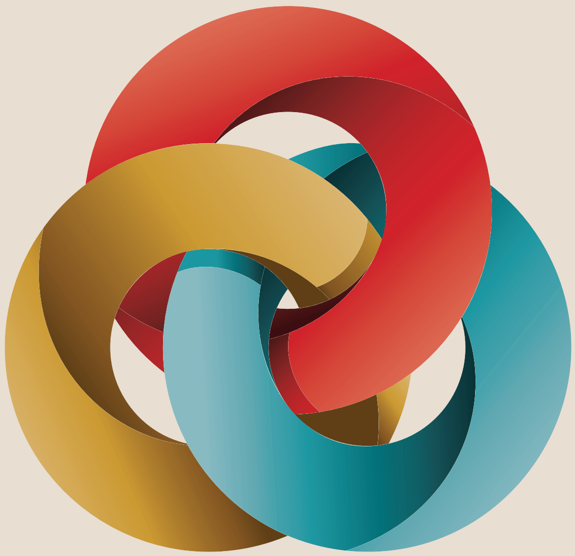
AN INTEGRATED APPROACH



SECOND EDITION

GULATI
Harvard Business School

MAYO
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NOHRIA
Harvard Business School

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***Management*, Second Edition**
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Brief Contents

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Preface

THE REALITIES OF MANAGEMENT

We are deeply grateful for the feedback, encouragement, and support that we received on our first edition. When we set out to write a new management textbook, we sought to capture the realities of managing in an ever-changing and dynamic environment. The speed of change and the global interconnectedness of business necessitate that managers and their companies be flexible, quick, and nimble. Effective change and sustainable performance require that managers understand the impact of strategic choices, the optimal design of organizations, and the power of leadership. In our first edition of the textbook, we called these three core components (strategy, organizational design, and leadership) the pillars of management. These pillars stand together to form a solid foundation of support, yet they are not stationary or immobile. As the contextual environment changes so too must a firm's strategy. The adaptation of strategy often requires a reexamination and deployment of new organizational structures and leadership approaches.

Today's managers need to understand the subtleties of strategy and the nuances of organizational design to carve out a defensible and sustainable position in an increasingly competitive and volatile marketplace. And managers need to know the key leadership levers that enable them to build, inspire, and nurture high-performing teams to implement that strategy. To be effective and relevant for a long period of time, managers must understand the co-evolutionary nature of these three pillars—strategy, organizational design, and leadership. This understanding provides managers with a holistic view of the ways in which strategy informs organizational design, organizational design impacts external competitiveness and internal motivation, and leadership ultimately influences performance.

In this second edition, we have continued to explore how strategy influences organizational design, how leaders shape and defend strategic positions, how organizations impact performance and drive motivation, how leaders lead, and how global forces impact the competitive landscape. The second edition includes both core foundational components of strategic and organizational theory as well as contemporary research that are useful and relevant for aspiring and experienced managers. As with the first edition, we employ a performance edge—demonstrating the impact and result of decisions regarding strategic choices, organizational alignment, and individual leadership approaches. Our aim is to help students prepare for leadership roles by addressing the integrated facets of leading businesses in today's complex and ever-changing environment.

TEXT ORGANIZATION

Our management textbook is organized into four main parts including (1) setting the context for management; (2) the strategic perspective; (3) the organizational perspective; and (4) the individual perspective. The chapters in each of the sections have been expanded and updated to highlight new research and to showcase contemporary examples from the world of practice. Through this book, we have tried to bridge the divide between theory and practice by presenting examples that are relevant, illustrative, and compelling.

The initial section of the book includes three chapters that are focused on the contextual landscape of business. We discuss the historical context of business and introduce the three pillars. This section also includes an overview of the internal and external components of the business environment with a specific focus on the global nature of business. This global focus is interwoven throughout the book including discussions on effective cross-cultural teams, market-entry strategies, global communication, and cross-boundary negotiations. In addition, this first section includes an in-depth discussion of ethics and corporate social responsibility. Similar to the focus on globalization, these themes are referenced throughout the textbook. In this second edition, we have provided a broader overview of the volatility in the business environment, including a discussion of the global financial crisis and its impact on companies, individuals, and countries. Alongside this discussion, we have included a deeper dive into the various stakeholders of a firm. The new edition also includes more examples of personal and corporate moral dilemmas and how individuals can successfully navigate them.

The second part of the textbook showcases the strategic perspective and includes three chapters—an introduction to strategy as well as overviews of business-level and corporate-level strategy. The second edition contains more global cases, a new section on the implementation of strategy, and a streamlined focus on related and unrelated diversification.

The third part of the textbook is focused on the organizational perspective of management and includes five chapters. In this section, we focus on the organization as an instrument for achieving strategic objectives, and we examine the way leaders make important decisions regarding organizational design, culture, human capital, and measurement. The second edition includes a broader discussion on different organizational forms, new content on delegation and empowerment, and a richer overview of the ways in which culture impacts organizational performance. The chapter on performance management has been extensively revised; it includes a new section on financial management, a streamlined overview of the balanced scorecard, and a review of new models of benchmarking. Finally, this section includes a deeper discussion on organizational change models and the role of innovation in shaping organizational and strategic evolution.

The final section of the textbook delves into the role of the individual. It includes a focus on how to manage oneself as well as how to manage others. This section includes nine chapters that provide a comprehensive overview of the important leadership levers that are needed to drive organizational performance, including the ability to motivate and inspire others, to effectively wield power and influence, to successfully navigate conflict, to reach win-win negotiations, and to communicate with passion and purpose. The second edition includes additional information about the effectiveness of different leadership styles, an integrated discussion on the use of power and how to channel personal power, and a broader overview of various cognitive biases that impact decision making. In addition, this section includes a new discussion on collective intelligence, extrinsic and intrinsic motivation, and network characteristics.

"ENGAGE. CONNECT. PERFORM. LEAD." ADDRESSING MAJOR COURSE NEEDS THROUGH INTERACTIVE LEARNING

Management, 2e seeks to effectively engage the student to think and act like a manager. *Management, 2e* follows a path to obtain these results and other key course goals through various learning activities: *Engage* (pulling the student into the content and establishing relevance), *Connect* (mastering a body of knowledge, connecting terms and concepts), *Perform* (real-world applications pertaining to concepts and theories), and *Lead* (higher level critical thinking and application that puts the student in the shoes of a manager). These assignment types are fully utilized in the MindTap/Aplia product, as described below.

TEXT FEATURES

The focus on relevance and performance will be demonstrated in the text through the use of timely and relevant case examples, reflective exercises showcasing the diverse business landscape, and personal assessments to help students discover the key factors that drive organizational and individual results. Specifically:

- A *Self-Reflection* starts each chapter, giving students a quick way to assess their sense of the content of the chapter.
- *The Leadership Development Journey* is a comprehensive skills-based activity that allows students to develop who they are, or will be, as managers. From chapter to chapter, this activity translates theory into action—the "what" into "how."
- *A Different View* showcases unique applications of chapter content including strategic corporate philanthropy (Chapter 3), culture in crisis (Chapter 8), servant leadership (Chapter 12), difficult conversations (Chapter 16), and crisis communication (Chapter 19).
- *Case in Point* activities ask students to further explore case examples and provide research opportunities based on text content.

INSTRUCTOR SUPPORT

- **Instructor's Resource CD**

  Discover all of the key instructor resources at your fingertips with this all-in-one resource. The Instructor's Resource CD (IRCD) offers chapter-by-chapter tools for instructors who are new to the course as well as innovative materials ideal for experienced professors who are developing strong managers. The Instructor's Resource contains the Instructor's Manual, Test Bank, Examview Testing Software, and PowerPoint Presentation Slides for both the instructor and student. The Instructor's Manual consists of lecture outlines, answers to pedagogical features, sample syllabi, and recommended teaching notes and additional case studies.

- **MindTap**

  MindTap®

  MindTap for Management is a personalized, fully online, digital learning platform. It is composed of authoritative Cengage Learning content, assignments, and services that engage your students with interactivity. The platform allows you to choose the configuration of coursework and to enhance the curriculum via complimentary web-apps known as MindApps. MindApps range from ReadSpeaker (which reads the text aloud to students) to Kaltura (allowing you to insert inline video and audio into your curriculum) to ConnectYard (allowing you to create digital "yards" through social media—all without "friending" your students). The Gulati interactive ebook is a media rich reader complete with figure animations, multiple choice concept checks, and drag and drop figures—all aimed at raising student comprehension. *Management, 2e* is well beyond an eBook, a homework solution or digital supplement, a resource center website, a course delivery platform or a Learning Management System. It is the first in a new category—the Personal Learning Experience.

- **Aplia**

  Have your students "think like managers" with Aplia's premium student engagement tool for management. This tool allows you to easily manage the subtle dynamics of teaching Principles of Management, with problem sets that engage students, help them connect class concepts to the real world, facilitate their skill performance, and show them how to lead others. Assignable exercises are designed to get students to Engage, Connect, Perform, and Lead with the content. Engage exercises show students how management is relevant to their lives; Connect takes management theories and applies them to real-world applications; Perform scenarios provide students an opportunity to apply management concepts; and Lead illustrates higher-level problem types, such as video cases, giving students a chance to practice and improve leadership decisions. Engaging media is seamlessly integrated throughout including video cases, interactive diagrams, self-assessments, and vivid examples. Holding students accountable for their own engagement becomes easy with Aplia's dynamic and flexible grading system, including grade analytics and easy grade book export tools that allow Aplia to work with any learning management system. Aplia™ assignments match the language, style, and structure of *Management*, *2e* allowing your students to apply what they learn directly to their work outside the classroom.

- **Write Experience**

  Cengage Learning's Write Experience helps students write effectively without adding to your workload! Write Experience utilizes artificial intelligence to score student writing instantly and accurately. It also provides students with detailed revision goals and feedback on their writing to help them improve written communication and critical thinking skills. Write Experience is the first product designed and created specifically for the higher education market through an exclusive agreement with McCann Associates, a Vantage Learning Affiliated operating company, and powered by e-Write IntelliMetric Within™.

Acknowledgments

First and foremost, we would like to thank the faculty who adopted the preliminary and first editions of our textbook. Adopting a new textbook is not an easy decision, and we greatly appreciate the trust and belief that was placed in us. We are also grateful for the feedback that we have received on the initial edition, and we have made a concerted effort to incorporate these invaluable suggestions. We would also like to acknowledge our partners at Cengage who have demonstrated a deep commitment and passion for this new approach to teaching the principles of management. In particular, we would like to thank Scott Person who has been a source of encouragement and support from the very beginning of this journey. In addition, we are indebted to the work of our colleagues at Cengage including Sara Ginn and Tara Singer for developmental editing support; Carol Moore, for her work on the digital side; and Joseph Malcolm for production support and oversight.

Over the last few years, we were fortunate to work with a team of dedicated individuals who provided thoughtful insights and relevant research support for various chapters including Sara Christopher, Stephanie Creary, Johnathan Cromwell, Alyssa Levy, Todd Maher, Lisa Riva, David Romney, William Russell, Franz Wohlgezogen, and Lara Zimmerman. We want to specifically acknowledge Samantha Cappelletti, Caroline de Lacvivier, Seah Lee, and Devlin McConnell who provided invaluable support for the second edition.

In launching this textbook on the principles of management, we sought the advice and counsel of several colleagues who provided thoughtful recommendations and input. In particular, we are extremely grateful for the thoughtful feedback and compelling insights of Bonita Austin (University of Utah), Francesca Gino (Harvard Business School), Geoffrey Love (University of Illinois), Svjetlana Madzar (University of Minnesota), and Lamar Pierce (Washington University, St. Louis). In addition, we are deeply indebted to Lynn Wooten (University of Michigan), who not only provided feedback on several chapters but also contributed key pedagogical elements to enhance the text.

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Ranjay Gulati

Ranjay Gulati is the Jaime and Josefina Chua Tiampo Professor of Business Administration and unit head of the Organizational Behavior Unit at the Harvard Business School. He is an expert on leadership, strategy, and organizational issues in firms. His recent work explores leadership and strategic challenges for building high-growth organizations in turbulent markets. Some of his prior work has focused on the enablers and implications of within-firm and inter-firm collaboration. He has looked at both when and how firms should leverage greater connectivity within and across their boundaries to enhance performance.

In his book, *Reorganize for Resilience: Putting Customers at the Center of Your Organization* (Harvard Business Press, 2009), he explores how "resilient" companies—those that prosper both in good times and bad—drive growth and increase profitability by immersing themselves in the lives of their customers. Based on more than a decade of research across a range of industries including manufacturing, retail, professional services, media, information technology, and healthcare, the book uncovers the path to resilience by showing companies how to break down internal barriers that impede action, build bridges across divisions, and create networks of collaborators. In another book, *Managing Network Resources: Alliances, Affiliations, and other Relational Assets* (Oxford University Press, 2007), he examines the implications of firms' growing portfolio of inter-firm connections. He demonstrates how firms are increasingly scaling back what they consider to be their core activities, and are at the same time expanding their array of offerings to customers by entering into a web of collaborations. He has also co-edited two books that focus on the dynamics of competition in emerging technology-intensive industries.

Professor Gulati is the past president of the Business Policy and Strategy Division at the Academy of Management and an elected fellow of the Strategic Management Society and the Academy of Management. He was ranked as one of the top 10 most cited scholars in Economics and Business over a decade by ISI-Incite. *The Economist*, *Financial Times*, and the *Economist Intelligence Unit* have listed him as among the top handful of business school scholars whose work is most relevant to management practice. He has been a Harvard MacArthur Fellow and a Sloan Foundation Fellow. His research has been published in leading journals such as *Administrative Science Quarterly, Harvard Business Review, American Journal of Sociology, Strategic Management Journal, Sloan Management Review, Academy of Management Journal*, and *Organization Science*. He has also written for the *Wall Street Journal*, *Forbes*, *strategy+business*, and the *Financial Times*. Professor Gulati sits on the editorial board of several leading journals. For the *Strategic Management Journal* he has been a co-editor of special issues including "Alliances and Strategic Networks" in 2000 and "Organizational Architecture" in 2011. He also co-edited a special issue of the *Academy of Management Journal* on "Multiplex Networks" that appeared in 2014.

Professor Gulati chairs the Harvard Business School's Advanced Management Program. He has directed several Executive Education programs on such topics as Building and Leading Customer Centric Organizations, Managing Customer Relationships, Managing Strategic Alliances, Mergers & Acquisitions, and Sustaining Competitive Advantage in Turbulent Markets. He is also active in custom executive education. He has received a number of awards for his teaching including the Best

Professor Award for his teaching in the MBA and executive MBA programs at the Kellogg School, where he was on the faculty prior to coming to Harvard.

Professor Gulati advises and speaks to corporations large and small around the globe. Some of his representative speaking and consulting clients include: GE, SAP, Novartis, Bank of China, Sanofi Aventis, Caterpillar, Allergan, Metlife, Target, Hitachi, Novartis, Honda, Qualcomm, Aetna, Future Brands, Ford, Seyfarth Shaw, LaFarge, McGraw-Hill, Rockwell Collins, Merck, General Mills, Abbott Laboratories, Baxter, Credit Suisse, and Microsoft. He has served on the advisory boards of several startup companies and has appeared as an expert witness in business litigations.

He has been a frequent guest on CNBC as well as a panelist on several of their series on topics that include: the *Business of Innovation, Collaboration*, and *Leadership Vision*. Professor Gulati holds a Ph.D. from Harvard University, a Master's Degree in Management from M.I.T.'s Sloan School of Management, and two Bachelor's Degrees, in Computer Science and Economics, from Washington State University and St. Stephens College, New Delhi, respectively. He lives in Newton, Massachusetts.

Anthony J. Mayo

Tony Mayo is the Thomas S. Murphy Senior Lecturer of Business Administration in the Organizational Behavior Unit of Harvard Business School (HBS) and the director of the HBS Leadership Initiative. He currently is the course head for FIELD, Field Immersion Experiences for Leadership Development, a required experiential, field-based course in the first year of the MBA Program which covers leadership, globalization, and entrepreneurship. Previously, he co-created and taught the course, "Great Business Leaders: The Importance of Contextual Intelligence." In addition, Tony teaches extensively in leadership-based executive education programs. He is the co-author of *In Their Time: The Greatest Business Leaders of the 20th Century*, which has been translated into 6 languages. He is also the co-author of *Paths to Power: How Insiders and Outsiders Shaped American Business Leadership* and *Entrepreneurs, Managers and Leaders: What the Airline Industry Can Teach Us About Leadership*. These books have been derived from the development of the Great American Business Leaders database that Dean Nitin Nohria and Tony created (see http://www.hbs.edu/ leadership/database/index.html).

As director of the Leadership Initiative, Tony oversees several comprehensive research projects on emerging, global, and legacy leadership and manages a number of executive education programs on leadership development. He was a co-creator of the High Potentials Leadership Development, Leadership for Senior Executives, Leading with Impact, Maximizing Your Leadership Potential, and Leadership Best Practices programs and has been a principal contributor to a number of custom leadership development initiatives. He launched the executive coaching component for the Program for Leadership Development and currently provides strategic support for a variety of executive coaching programs.

Prior to his current role, Tony pursued a career in database marketing where he held senior general management positions at advertising agency Hill Holliday, database management firm Epsilon, and full-service direct marketing company DIMAC Marketing Corporation. Most recently, Tony served as the General Manager of Hill Holliday's Customer Relationship Management Practice.

At Epsilon, he served as acting co-chief executive officer where he had full responsibility for the delivery and management of strategic and database marketing services for Fortune 1000 companies and national not-for-profit organizations. He also held senior management positions in Epsilon's sales and account management departments. At DIMAC Marketing Corporation, Tony served as vice president of strategic development and acting chief financial officer. In this capacity, Tony led the development of an integrated strategic plan for DIMAC's disparate business units and coordinated the ultimate sale of the company. Prior to his work in the database marketing industry, Tony served as the Director of MBA Program Administration at Harvard Business School.

Tony completed his MBA from Harvard Business School and received his Bachelor's Degree, *summa cum laude*, from Boston College. He lives in Needham, MA.

Nitin Nohria

Nitin Nohria became the 10th dean of Harvard Business School on July 1, 2010. He previously served as co-chair of the Leadership Initiative, senior associate dean of Faculty Development, and Head of the Organizational Behavior unit.

Dean Nohria's intellectual interests center on human motivation, leadership, corporate transformation and accountability, and sustainable economic and human performance. He is coauthor or coeditor of 16 books. The most recent, *Handbook of Leadership Theory and Practice*, is a compendium dedicated to advancing research on leadership based on a colloquium he organized during HBS's centennial celebrations. Dean Nohria is also the author of over 50 journal articles, book chapters, cases, working papers, and notes. He sits on the board of directors of Tata Sons and is on the board of trustees of Massachusetts General Hospital. He has served as an advisor and consultant to several large and small companies in different parts of the world. He has been interviewed by ABC, CNN, and NPR, and cited in *Business Week, Economist, Financial Times, Fortune, New York Times,* and *The Wall Street Journal.*

Prior to joining the Harvard Business School faculty in July 1988, Dean Nohria received his Ph.D. in management from the Sloan School of Management, Massachusetts Institute of Technology, and a B.Tech. in Chemical Engineering from the Indian Institute of Technology, Bombay (which honored him as a distinguished alumnus in 2007). He was a visiting faculty member at the London Business School in 1996.

PART 1

SETTING THE CONTEXT FOR MANAGEMENT

CHAPTER

1

Introduction to Management

Chapter Outline

Introduction

Management and Leadership

Historical Perspectives on Business

Changing Perspectives on the Purpose of Business

Stakeholder Approach

- Stakeholder Mapping
- Stakeholder Management Processes
- Managing Uncertainty

Summary

Key Terms

Assignments

Endnotes

Learning Objectives

After reading this chapter, you should be able to:

LO1 Differentiate among the three pillars of managing organizations: strategic positioning, organizational design, and individual leadership.

LO2 Describe the complementary components of management and leadership and the relative importance of technical, interpersonal, and conceptual skills at various managerial levels in the organization.

LO3 Articulate how the practice of management has evolved.

LO4 Explain the changing perspectives on the purpose of business and how the relationship between the firm and its business environment has changed over time.

LO5 Describe the stakeholder theory of management and how various stakeholder relationships are managed to enhance overall firm performance.

SELF-REFLECTION

What Are Your Managerial and Leadership Strengths?

Please respond True or False to the following statements to assess your leadership and managerial strengths.

1. I excel at planning projects.
2. When working with a group, I think strategically by creating a vision and setting goals to make that vision a reality.
3. I am skilled at budgeting and financial planning.
4. I encourage change by challenging the status quo.
5. I can organize people to get a job done by establishing structures and delegating tasks.
6. I understand how to motivate people.
7. I enjoy creating solutions for complex problems.
8. I have the ability to work with a diverse group of people to accomplish a goal.
9. I am a take-charge type of person who brings order to a variety of situations.
10. I influence people through passion and emotional connections.

If you answered True to the majority of the odd-numbered statements, you have a solid foundation of managerial strengths. If you answered True to the majority of the even-numbered statements, you have a solid foundation of leadership strengths. If both are true, you are adept at balancing the roles of managers and leaders.

INTRODUCTION

Now, more than ever, the world needs leaders who are versatile and flexible. The increasing pace of globalization, rapid deployment of technology, and constantly changing competitive landscape require leaders who can nimbly adapt themselves and their organizations to new realities. The one constant in business is that it is not constant. Change is a reality, and businesses that stand the test of time are led by individuals who not only embrace change, but proactively prepare their organizations for its impact. Sustaining relevance in a dynamic business environment requires leaders to confront difficult decisions on a daily basis. Do they expand product offerings to anticipate consumer demand? Or do they eliminate waste and focus the company's efforts on fewer products? Should they compete directly with rivals? Or do they invest money to innovate an entirely new product or service? How do they motivate their employees? How do they gain trust and commitment in the organization? Should they focus on learning and development or bottom-line results?

Leaders need to understand how to harness technological advancements, manage and lead a dispersed and diverse workforce, anticipate and react to constant competitive and geopolitical change and uncertainty, compete on a global scale, and operate in a socially responsible and accountable manner.[1] One increasingly popular acronym that captures the context in which today's organizations compete is **VUCA**, which stands for volatile, uncertain, complex, and ambiguous. A volatile situation is characterized by unpredictability and requires managers to be agile and flexible. An uncertain situation calls for managers to gather and decipher large amounts of information, some of which will be conflicting. This uncertainty is sometimes accompanied by complexity, a situation that is based on the interconnection of various business elements. Separating these interconnections and structuring individual responses to them helps managers cope with complexity. Finally, managers often face very ambiguous situations where the cause-and-effect relationships are not always clear. Experimentation helps managers to achieve a greater sense of clarity about ambiguous situations (see Table 1.1).[2] Success for organizations in this VUCA environment requires a strong knowledge of (1) strategic positioning, (2) organizational design, and (3) individual leadership (see Figure 1.1).

The interaction between the formulation of strategy, the design of the organization, and the leadership of the firm is not a functional or linear process; it is a dynamic and interactive one. Throughout this textbook on the principles, purpose, and perspectives of management, we demonstrate the mutual interdependence and interconnectivity between strategy, organizational design, and individual leadership action. The strategy of an organization depends on the nature and context of the competitive and environmental landscape as well as the skills and capabilities of the management team. The understanding of this contextual landscape is, in turn, dependent on the ability of the firm's management to recognize opportunities and threats as well as lead and organize the company's resources to effectively compete in the marketplace.

A firm needs to adapt and change its strategic choices and leadership approaches to retain its relevance. Strategy often dictates the organizational design and leadership required for success. The type of leaders and the organizational design of a business can also influence the strategic choices in which a business can credibly compete. In essence, strategy, organizational design, and leadership must work together in an integrative and dynamic fashion.

VUCA
An acronym for volatile, uncertain, complex, and ambiguous that captures the context in which today's organizations compete.

The chapters of this textbook are organized according to the three pillars of managing organizations—strategy, organization, and individual leadership. The strategic level or perspective will encompass an understanding of the environmental landscape in which businesses compete and the elements of strategy that help organizations align their resources for success in a changing context. Key questions that will be addressed in the strategic perspective include the following: How should a business compete? How does the competitive landscape shape the potential for its

		Situation Characterized by...	Response
V	**Volatility**	Unstable and unpredictable change	Be agile and flexible
U	**Uncertainty**	Lack of knowledge about significance of change	Seek knowledge and information
C	**Complexity**	Many interconnected parts	Adjust operations to match the environment
A	**Ambiguity**	Lack of knowledge about cause and effect	Experiment

Table 1.1 〉 Context in Which Businesses Operate: VUCA—Volatility, Uncertainty, Complexity, and Ambiguity

Source: Adapted from Nathan Bennett and G. James Lemoine, "What a Difference a Word Makes: Understanding Threats to Performance in a VUCA World," *Business Horizons*, Vol. 57, 2014, pp. 311–317.

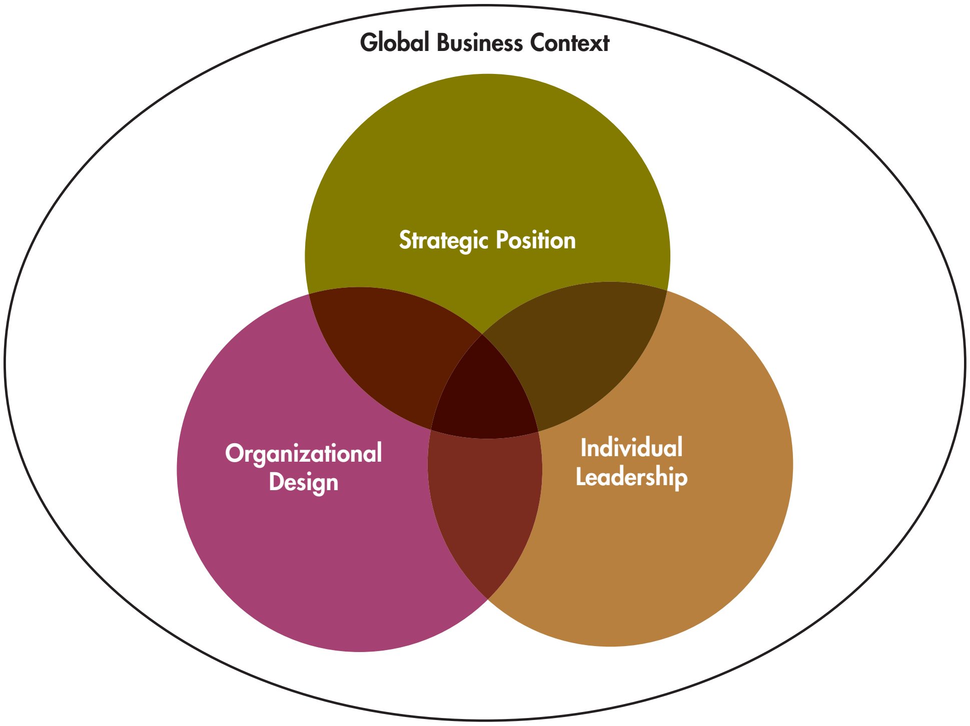

Figure 1.1 〉 The Pillars of Management

success or failure? What strategy will allow a firm to adapt as the context evolves? How has and will globalization impact the competitive positioning of a business?

Knowing what strategy to pursue is only the first part of the management puzzle. The next piece involves developing and aligning the organizational components (e.g., organizational design, culture, human resource practices, and performance management) to achieve these strategic objectives. Without this, no strategy will ever be properly implemented and all that thinking will come to nothing. To that end, the organizational perspective of the textbook will define the manner in which a business is structured to compete in its changing contextual landscape. Key questions include the following: What organizational structure will enable the firm to optimize its resources? How can the culture of the firm reinforce key values and lay the foundation for strong organizational performance? How will performance be measured? How does an organization remain relevant in a constantly changing competitive landscape?

Finally, an organization is nothing more than a collection of individuals who come together to achieve a common goal or objective. But how does one coordinate and motivate diverse individuals to work together? The answer is through effective leadership. The final section of the textbook addresses the key components and activities of leadership. This section is about you and how you can be a more effective leader in the global organizations of tomorrow. Leaders must first know who they are and what impels them to effectively motivate and influence others. Key questions addressed in the individual perspective section of the textbook include the following: How should managers wield power and influence? How do managers make critical decisions and navigate conflict? What motivates others, and how does one create and nurture effective teams? How do managers communicate with urgency and compassion?

The interplay of strategy, organizational design, and individual action operates within a broad contextual landscape. In fact, the context can directly impact the strategic opportunities open to a firm as well as the latitude of individual managerial action. That is why we have encircled the three perspectives of management in Figure 1.1 a contextual framing. While the context can shape the availability and viability of certain opportunities, managers can influence the context through a number of actions including their ability to commercialize technology, support or oppose government action, and capitalize on demographic movements.

In recent years, the growing importance of globalization and the expanding scope of corporate social responsibility have fundamentally impacted the business landscape. Chapters 2 and 3 of this opening section of the textbook will provide an overview of globalization and corporate responsibility, respectively, and how they have shaped the context for business.

In this first chapter, we will discuss how the perspective from which the firm is viewed has evolved over the years. As we'll see, the firm has shifted from owing a duty only to shareholders to owing a duty to various stakeholders. This view of a firm's purpose has changed as the complexity and turbulence in the marketplace have increased. We'll also discuss a firm's external and internal environments to demonstrate the various forces and stakeholders that a firm encounters in conducting its business. One thing that should become clear through the reading is that managing a firm's stakeholders and environments is a very difficult task, but doing so is critical to building a high-performing organization.[3] By responding to stakeholder concerns, the manager can drive the firm's performance and achieve a competitive advantage in the marketplace. Failing to understand the complexity of various stakeholders can have disastrous consequences, as evidenced by Walmart's attempt to enter the Inglewood, California, market.

Walmart's Business Environment

Walmart, the world's largest retailer, has followed a trajectory of growth and expansion since its inception in the 1960s. Started by the legendary Sam Walton, Walmart's historical strategy was to open stores in semirural markets to provide variety and competitive prices to customers who previously relied on a host of smaller stores for their shopping needs. Throughout the 1970s and 1980s, Walmart expanded aggressively across the United States, offering the lowest prices in many markets. As other retailing businesses such as K-Mart and Sears fell on hard times, Walmart continued to post ever-impressive results.[4]

In 2014, the company employed over 2.2 million people and earned net income of $16 billion on revenues of $476 billion.[5] Over the past two decades, Walmart has changed the mix of its retail stores, opening more Supercenters that offer groceries as well as traditional retail offerings (see Figure 1.2). Despite its growth, Walmart has struggled with expansion, especially in Vermont and California. Though rural Vermont would seem to be a natural fit for Walmart, the state has the fewest Walmarts per capita than any other state in the country. Several small Vermont communities have launched aggressive anti-Walmart campaigns in the state, concerned that the company's presence will erode the success of local retailers and irreparably damage the charm of the state's small towns.[6]

Andrew Nelles/Reuters

Walmart faced similar resistance in California. Following its first successful opening of a Supercenter in La Quinta, Walmart looked next to a market closer to Los Angeles. However, as the company drafted plans to open a Supercenter in Inglewood, it began to encounter serious opposition from the members of the city council, who had attempted to pass legislation in 2002 to prevent stores of Walmart's size from building new units in their town. Walmart executives were confused about why a town would not want a new commercial enterprise that could generate new jobs (estimated at 1,200) and additional tax revenue for the city (estimated at $5 million annually).

The company also faced typical competitive pressures as it sought to enter this new market. Like many markets in the United States, the grocery business in California was very competitive, with low gross margins prevalent across the industry. The California market was dominated by established grocers such as Safeway, Albertson's, and Kroger. Just as the Inglewood proposal hit the headlines, many of Walmart's grocery competitors in California responded to the chain's potential entry with a series of competitive actions. In many markets, a Walmart entry into the grocery business had resulted in prices dropping 3%–5% for certain products. As a result, many of the biggest grocery chains in California attempted to lower employees' wages and healthcare coverage in an effort to remain cost competitive with Walmart.[7] As rival grocery workers suffered from wage cuts, the United Food and Commercial Workers (UFCW) union continued to put pressure on the Inglewood city council to block Walmart's Supercenter. Many argued that Walmart's arrival would continue to cause wage decreases across the city. This was a grim prospect for a city that already suffered high unemployment rates and lower income levels relative to those in other areas around Los Angeles.

As Walmart executives watched these events unfold, they debated what course of action to take. To many, it seemed pointless to take the proposal before a city council that had made its intentions clear. So the company moved forward with its efforts to put the proposal to a vote by citizen referendum. Critics responded that Walmart would hurt local citizens because its wage and healthcare programs kept employees below the poverty line. The city of Los Angeles commissioned a study showing that Walmart Supercenters destroyed jobs and forced competitors to pay lower wages.[8] In contrast, a report issued by the Los Angeles County Economic Development Corporation and funded by Walmart came to opposite conclusions, claiming that households shopping at Walmart saved on groceries, which allowed consumers to spend more on other items, in turn leading to job growth.[9] In the end, voters soundly rejected the initiative and Walmart was forced to abandon Inglewood.

Until recently, Walmart faced little if any opposition to new store openings. Today, it seems as though the company encounters resistance at every turn when opening new stores. If you were a manager at Walmart, how would you have dealt with the situation? What could they have done differently?

Figure 1.2 〉 Growth of Supercenters, 1994–2014

Source: Wal-Mart Stores, Inc. annual reports for 1999, 2004, 2010, and 2014.

The Walmart case highlights the complexity of managing and leading in today's business environment. Effective management is responsible for more than generating a profit; management's job often requires the ability to understand the needs of a variety of key constituents including its employees and the broader community. In essence, success in the global business environment requires effective management and skillful leadership.

MANAGEMENT AND LEADERSHIP

The distinction between **management** and **leadership** is often very subtle. In fact, most people use the terms interchangeably when they refer to the operation of a business. In a seminal analysis on the difference between managers and leaders, John Kotter noted that leaders set a direction for a firm, align people to focus on the organization's vision, and motivate and inspire people (see Figure 1.3).[10] Conversely, he noted that managers generally focus their efforts on planning and budgeting, organizing and staffing resources, and controlling and problem solving.

Management
The act of working with and through a group of people to accomplish a desired goal or objective in an efficient and effective manner.

Leadership
The ability to drive change and innovation through inspiration and motivation.

Management has generally been defined as the act of working with and through a group of people to accomplish a desired goal or objective in an efficient and effective manner. Leadership has been defined as the ability to drive change and innovation through inspiration and motivation. The development and execution of strategy requires the skills and expertise of leaders and managers, and both are equally important to an organization's success. A vision or direction without a sound plan for execution is often merely a dream. The execution of a plan without a vision often lacks strategic or competitive advantage.

For instance, at Southwest Airlines, a vision was born when former chief executive officer (CEO) Herb Kelleher learned of a short-haul commuter airline in

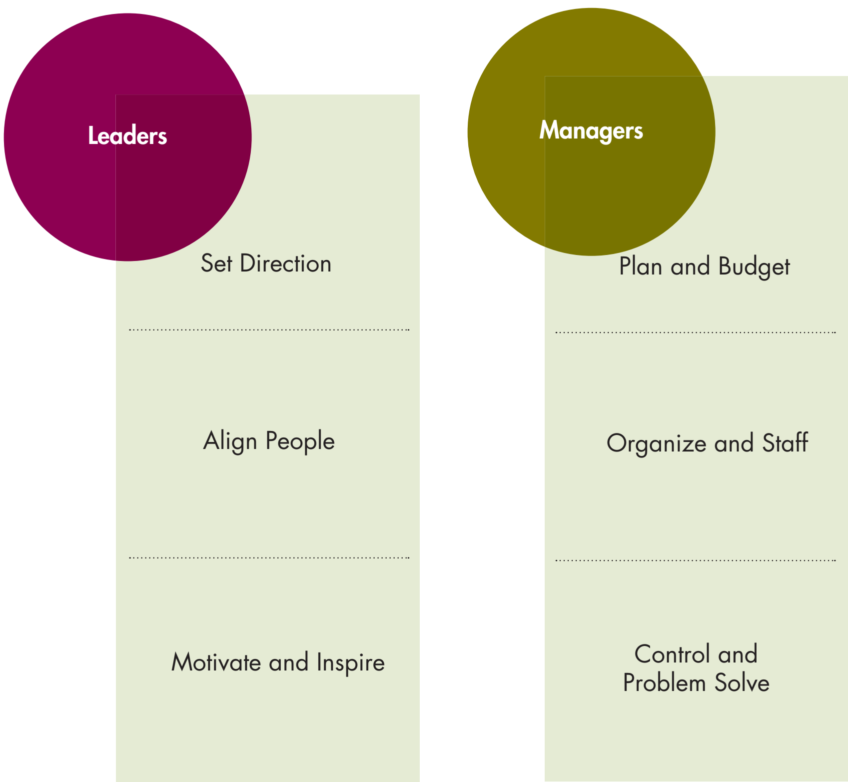

Figure 1.3 〉 The Roles of Leaders versus Managers

California that flew passengers over shorter distances than did major airlines. Kelleher surmised that many travelers were tired of driving long distances (between 500 and 1,000 miles) because the available flights were too expensive or not frequent enough. Kelleher's vision was to get passengers to trade their car trips for short flights. This vision of air travel competing with car travel differed greatly from the vision promoted by the major airlines that were more focused on long-distance flights. While Kelleher set forth the vision of the firm, his management team was able to execute it with precision and accuracy. They did so by organizing the resources of the company to focus on efficiency, consistency, speed, and cost-effectiveness.[11]

To be successful, organizations need to develop and nurture managers and leaders at all levels, not just at the top. In fact, organizations often evolve and innovate based on the suggestions and input of individuals who are several levels below the CEO.[12] The skills required for success in business are often different depending on a person's level and responsibilities in the organization.[13] While technical skills are very important early on, they tend to take a back seat to more strategic abilities as an individual advances in an organization. For instance, frontline supervisors must often focus on technical or process issues to ensure that operations are running smoothly, and new entry-level employees are often tasked with specific operational roles that require a certain level of proficiency and skills. While it is true that leadership skills become more critical as you move up in an organization, it is important to note that leadership is not just the monopoly of top management, and most organizations today expect even their lower-level managers to operate and think like leaders.

As individuals move up in an organization, they have to focus on managerial tasks such as financial reporting, planning, recruiting talent, and resource allocation. While technical skills are still important, middle-level managers sometimes have to spend more time applying their leadership skills such as motivating and developing teams while at the same time using managerial skills such as working with senior executives to provide analysis for the development or refinement of the organization's strategy.

And still higher up, senior executives are expected to set the vision and agenda for the organization as well as oversee strategic execution. They must balance short and long-term expectations while planning for certain expected and unexpected contingencies. To do so, they must leverage both leadership and management skills. If they lack one or the other they must ensure that someone with complementary skills is there to support them. To secure buy-in and support in the organization, senior leaders need to rely on strong communication and interpersonal skills.[14] The ability to think conceptually is vitally important at this level (see Figure 1.4).[15]

While an individual's abilities must transform as they go higher in an organization, it is important to note that each person can have a very unique style and still be successful. Some leaders are extroverted, while others make decisions by listening to their inner voice. Some are quick and impulsive, while others are cautious and take longer to make a decision. Some leaders are vain, some are humble. According to Peter Drucker, an effective leader is not someone who uses a specific leadership style; he or she is someone whose style enables him or her to obtain results.[16]

Technical, interpersonal, and conceptual skills are important and relevant for all individuals regardless of their place in the organization. The key difference is the level of intensity of each skill.[17] Conceptual skills consume more of a top executive's time, while technical skills are more important for new employees and frontline supervisors. This breakdown of skills is applicable to business and nonbusiness settings. Think about a soccer team. The players are focused on exercising their technical skills to the best of their abilities. They need to work as members of a team, and they need to know the team's plays (or strategies) but the players' primary concern is their own skills. The coaches are also focused on skills by providing instruction and training, but they must ensure that individual players work as a team. Coaches set strategy and create plays

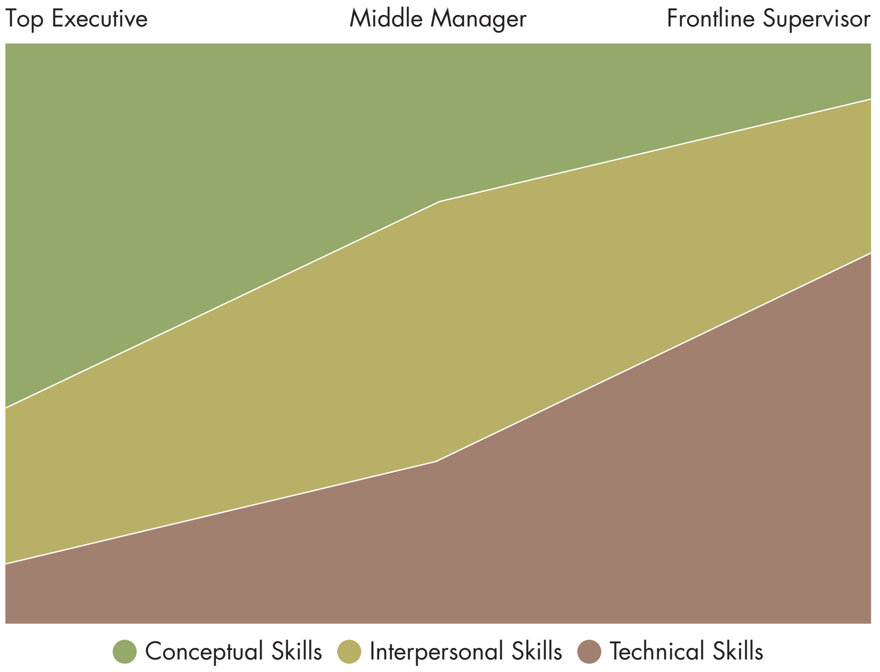

Figure 1.4 〉 Importance and Relevance of Skills by Managerial Level

Figure 1.5 〉 From Big Picture Strategy to Individual Action

to further develop the capacity of the team. Finally, the team's owners must be able to identify and support talent, but they spend the bulk of their time overseeing strategic issues such as revenue generation and long-term investment opportunities.

The primary skills of managers and leaders (conceptual, interpersonal, and technical) are aligned with the overall structure of this textbook (see Figure 1.5). In the strategic perspective, we will spend a considerable amount of time discussing ways in which business leaders develop strategies and positions to differentiate their operation in a competitive landscape. This ability to understand the landscape and one's position in it depends on the development of well-honed conceptual abilities.

The Leadership Development Journey

After you graduate from college and start your career, you will be expected to effectively incorporate fully developed technical, conceptual, and interpersonal skills needed for managing and leading. Identify your ideal career and consider the following questions:

- Can you identify the technical skills required for an entry-level job?
- What are the interpersonal skills needed to supervise a staff?
- How does a top executive use conceptual skills to set a vision and craft a strategy?

Based on your analysis of the skills needed for your ideal career, identify three goals that will enable you to succeed and to develop a career path.

Moving to the organizational perspective, our focus is on structural issues that involve conceptual as well as interpersonal and technical skills. For instance, how does one create an organizational structure that maximizes the talents of employees? In the final section of the textbook, we address the ways in which individuals can build the skills (technical, interpersonal, and conceptual) to develop as a leader and to prepare to make necessary organizational and strategic decisions.

We start with the big picture strategic perspective to define the company's position in the global business context. Once the strategy has been developed, it is important to move to execution and delivery. That's where organizational structure, design processes, and performance management come into play. What are the best structures and processes to support the desired strategic objectives? What resources are available? What resources must be acquired or developed? How can a business sustain its relevance in a changing contextual landscape? The answers to these questions define the organizational perspective.

Ultimately, managers must have the strategic abilities needed to understand a situation, the social skills to know what to do in that situation, and the behavioral skills to act.[18] Some leaders know what to do but can't do it, while others are less effective at recognizing the subtleties and complexities of nuanced situations. Still others treat all situations with the same managerial approach. Effective management requires the development of a broad set of skills and capabilities needed to act in a variety of situations. That's why it is so important to focus on the development of personal leadership skills.

HISTORICAL PERSPECTIVES ON BUSINESS

A formal theory of how large and complex organizations operate was first put forward in the early 1900s by German social scientist Max Weber. He was interested in explaining how organizations retain order and get things done as they get bigger. The underlying idea here was that as organizations get larger, they can become unwieldy as they tackle their internal division of labor. To maintain order, most organizations (in this case not just business but nonbusiness settings like the military and government) seek to implement systems and processes to create order. Weber's main contribution to the field was the conceptualization of the **bureaucratic organization structure**. According to Weber, the features of an ideal bureaucracy include the following: a clear differentiation of tasks and responsibilities among individuals; coordination through a strict hierarchy of authority and decision rights; standardized

Bureaucratic organization structure
A clear differentiation of tasks and responsibilities among individuals; coordination through a strict hierarchy of authority and decision rights; standardized rules and procedures; and the vertical separation of planning and execution so that plans are made in the upper ranks of an organization and executed in the lower ranks.

Scientific management
A focus on how jobs, work, and incentive schemes could be designed to improve productivity using industrial engineering methods.

rules and procedures; the vertical separation of planning and execution so that plans are made in the upper ranks of an organization and executed in the lower; and the use of technical criteria for recruitment and promotion.[19] Most modern organizations have explicitly or implicitly based their structures on the basic principles of this bureaucratic form.[20] The classic example of the bureaucratic organization is the military. According to Weber, the bureaucratic form's greatest contribution was its ability to make organizations more rational and efficient.[21]

Following Weber's work, many social scientists began exploring how organizations could be set up around a set of scientific principles to make them orderly and efficient. Some of this work, pioneered by Frederick Taylor in the 1910s, came to be known as **scientific management**. Scientific management focused on how jobs, work, and incentive schemes could be designed to improve productivity using industrial engineering methods such as time and motion studies. The results of these studies formed the basis of Taylor's principles of effective supervision within the firm.[22] Through this approach, the organization was likened to a well-oiled machine and the manager was seen as a machine operator. The manager prescribed certain actions based on scientific study that were expected to produce definitive outcomes. Taylor believed that employees were economically driven and rational in their motives.

Bettmann/CORBIS

In the 1930s, theories of management shifted away from the view of the organization as a machine. During this period, the **human relations movement**[23] emerged, which emphasized the importance of informal social relations at work. As opposed to scientific management's view of the firm as a machine, human relations scientists believed that organizations must be understood as a system of interdependent human beings who share a common interest in the survival and effective functioning of the firm. Through the human relations movement, emphasis shifted from the output of the firm to the informal and social side of the firm. From this standpoint, organizations served as a means for people to interact and learn as well as turn a profit.

Human relations movement
The belief that organizations must be understood as systems of interdependent human beings who share a common interest in the survival and effective functioning of the firm.

By the 1950s, theories of management had shifted yet again to examine the differences across organizations in the way they structured themselves. A debate raged on about how a firm should be organized. Some theorists believed that there was one optimal form of organizing all organizations. Others believed that the optimal form depended on the nature of the context in which the organization competed. This second group believed that organizational form depends on social, psychological, technical, and economic conditions.[24]

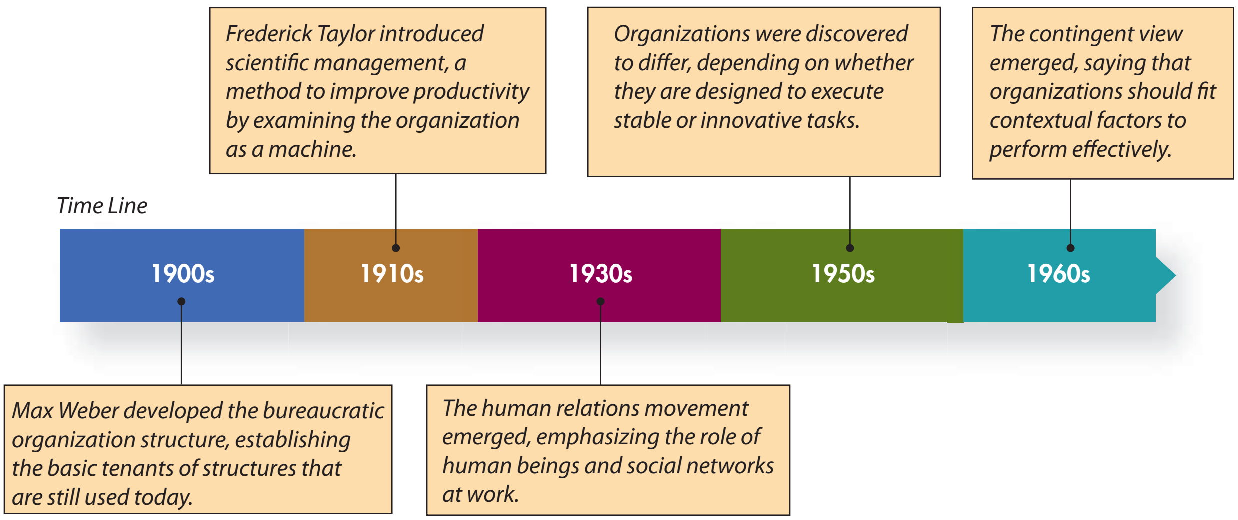

Figure 1.6 〉 Major Historical Events in the Study of Organizations

One of the most profound insights about organizational structure that came out of this period was the fact that organizations often differ based on whether they were designed to execute certain stable tasks or uncertain innovative tasks. Many researchers during the period believed that the nature of the environment and the tasks the firm had to accomplish should drive how organizations were structured and managed. According to this argument, firms that emphasized efficiency should maintain stable, mechanistic organizational structures. In contrast, firms that emphasized innovation should maintain flexible and organic organizational structures.[25]

In the 1960s, popular thought evolved and made a complete break from the notion that all firms should have a certain organizational structure. Ultimately a shared view emerged that there may not be one optimal form for all organizations and that the ideal form depends on its context. During this period, a **contingent view** of the firm emerged where effective organizational structure was based on fit or alignment between the organization and its environment.[26] This approach affirmed that the social, political, and business environments play a large role in shaping the way effective organizations are structured. According to this contingent view, the organization's structure should fit the firm's environment (see Figure 1.6).

Current research on the role of organizations has tended to be an extension of many of the previous theories. In general, there is no "one-size-fits-all" approach to organizational design. In making organizational design decisions, managers must evaluate their strategic objectives in relation to the contextual environment and their internal resource capabilities. That is why an understanding of the context is so important.

Contingent view
A view of the firm where effective organizational structure is based on fit or alignment between the organization and various aspects in its environment.

Business environment
The combination of all contextual forces and elements in the external and internal environments of a firm.

CHANGING PERSPECTIVES ON THE PURPOSE OF BUSINESS

Today's **business environment**, which includes all of the contextual forces and elements that shape or impact the internal and external environments of a firm, is infinitely more complex than it was just a few years ago. Over the years, the view of how to approach the business environment and drive performance has changed (see Figure 1.7).

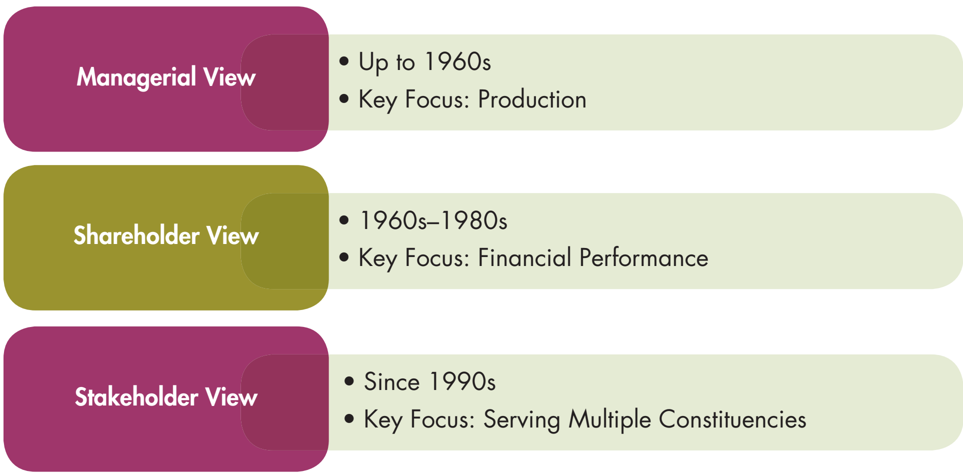

Figure 1.7 〉 Changing Perceptions of the Business Environment

Library of Congress Prints and Photographs Division [LC-DIG-highsm-15747]

For a good part of the twentieth century, many managers subscribed to the **managerial view** of the firm, which saw the firm as a mechanism for converting raw materials into products to sell to customers. In this framework, managers focused on relationships between the firm and its suppliers, customers, owners, and employees. During this period, management often did not focus on the broader set of parties that Walmart was forced to contend with in Inglewood. In fact, many firms did not consider outside parties such as local governments or nongovernmental organizations (NGOs) as anything more than annoyances. In this context, managers were the boss, and in many cases, there were limited checks and balances on their power.

Up until the 1960s, shareholders did not have the power they do today. Mutual funds had not been developed, and corporate takeovers had yet to be popularized. As a result, managers did not face many threats from shareholders to improve performance or seek business in other industries.

However, in the late 1960s, many managers began to view the firm through a more shareholder-focused lens. During the 1970s, American corporations were under siege from two forces: (1) the combination of slow economic growth and high inflation and (2) increased penetration of foreign competition in the U.S. market.[27] Many firms stopped growing, and their profits began to stagnate.[28] The owners of the company who were technically the shareholders felt they had lost a voice in how the company was run and that their interests were no longer being served by managers. At the same time, shareholders were no longer individuals but rather institutions who had more collective clout and voice. As a result, managerial focus shifted to the interests of shareholders as the primary stakeholder for whom they worked.

Managerial view
A business framework where the firm is seen as a mechanism for converting raw materials into products to sell to customers.

Shareholder view
A business framework where the job of top managers is to produce the highest possible stock market valuation of the firm's assets.

According to the **shareholder view** of the firm, the job of top managers was to produce the highest possible stock market valuation of the firm's assets.[29] A series of factors during this period combined to promote this view. In the early 1980s, antitrust restrictions on mergers and acquisitions (M&A) were relaxed, prompting many firms to seek new growth opportunities by acquiring companies.[30] This period saw a huge increase in both M&A activity and corporate takeovers as managers attempted to seek growth in any way possible. Overall, no firm was immune to the pressures of the market and the threat of takeover.

Ford Motor Company took advantage of these relaxed rules. In an effort to provide more value to their shareholders and grow their business, Ford acquired British carmakers Jaguar and Aston Martin in the late 1980s. Both companies represented a market that Ford had failed to break into—Jaguar with luxury cars and Aston Martin with high-end sports cars.[31] By securing Jaguar, Ford also discovered a way to increase its presence in Western Europe.[32]

Rob Kinmonth/Getty Images

In a similar way, Frank Lorenzo capitalized on the new regulatory climate in the airline industry when he used his small Texas International Airline to undertake a hostile takeover of the much larger Continental Airlines in the early 1980s. Through some clever financial maneuvering, Lorenzo pushed his newly acquired firm into bankruptcy to break the power of the union and hence reduce the airline's cost structure. It worked. Profits soared. When the firm emerged from bankruptcy, Lorenzo went on a buying spree, acquiring Eastern Airlines, New York Air, and People Express in less than two years to make Continental one of the largest airlines in the United States. Lorenzo ran the airline as a financial model, focusing on profitability and shareholder value, and completely ignoring the impact of these financial decisions on employees and customers.[33]

Many managers, like Lorenzo, came to believe that the organization owed allegiance only to shareholders—that employees, communities, and customers were secondary. The results of an overemphasis on shareholder value emerged in the late 1980s as many U.S. companies started to lose ground to foreign competition. For some firms, this singular focus on shareholder value resulted in a short-term orientation, leading to a lack of investment in new products and erosion in quality standards. These firms were caught off guard as more nimble companies stole market share with new products, a greater focus on consumer needs, and a stronger commitment to quality. Lorenzo's success at Continental was short-lived. The lack of investment in the company, the inattention to customer needs, and the erosion of trust between management and employees resulted in Lorenzo's early departure from the company.

About the same time the shareholder view of the firm was reaching its zenith, both the internal and external environments of many firms began to increase in complexity. The external environment of the typical U.S. firm began experiencing turbulence through foreign competition. Many U.S. firms, such as the Big Three U.S. carmakers (General Motors, Ford, and Chrysler), had faced little foreign competition up until the 1980s because of protectionist measures that had insulated the industry. The Big Three also faced lower competitive pressures because of the infancy of many car firms in emerging economies. As Japanese carmakers made inroads into the U.S. market beginning in the 1970s, the Big Three had a new element of complexity to deal with in their environments.

But firms' environments were not increasing in complexity just because of foreign competition. Rather, firms during the 1980s began to face mounting pressure from a series of external groups, including environmental activists, animal rights groups, and local community governments. Many environmental groups emerged during this period (see Figure 1.8).

While it has become popular recently for corporations to focus on their environmental footprint or carbon emissions, this wasn't always the case. Many firms simply ignored environmental concerns for much of the twentieth century. High-impact industries such as mining, oil, and gas exploration as well as waste management rarely allocated any attention to environmental concerns. However, all of this changed in the 1980s as the public became aware of some of the by-products of these firms' activities. As acid rain and smog entered the average citizen's vocabulary, many firms were forced to address environmental concerns.

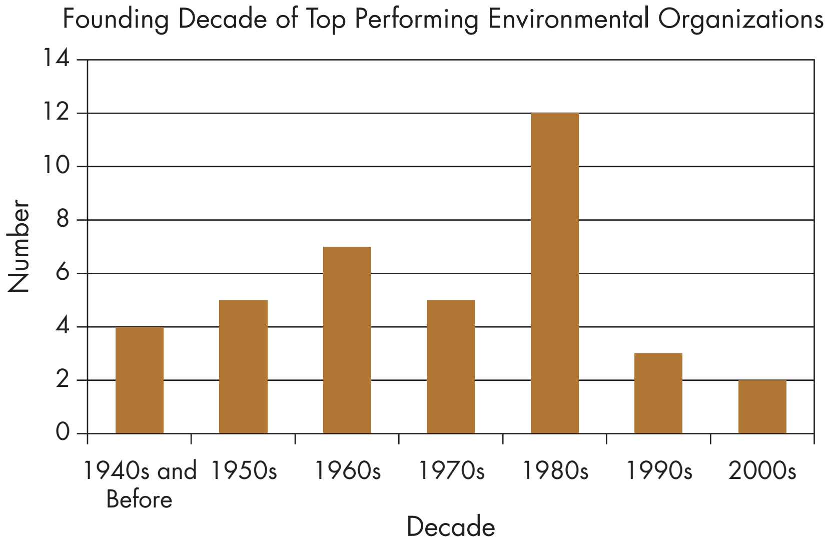

Figure 1.8 〉 Founding Decade of Top Performing Environmental Organizations

Source: American Institute of Philanthropy, http://www.charitywatch.org/toprated.html#enviro, January 15, 2015.

At the same time, the firm's external environment was increasing in complexity; many firms had to deal with new pressures in their internal environments such as employee activism. As the shareholder view of the firm progressed, shareholders continued to push managers to achieve specific quarterly targets. The manager's focus was stretched between dealing with new sources of external and internal complexity and dealing with pressure from shareholders to produce results. The combination of these forces led to the development of a new paradigm from which to view the firm.

The **stakeholder view** of the firm emerged among this increasing complexity and turbulence in the economic environment. Made popular through E. Edward Freeman's 1984 book *Strategic Management: A Stakeholder Approach*, the stakeholder view of the firm identifies and analyzes multiple groups that interact with the firm and attempts to align organizational practices to satisfy the needs of these various groups (see Figure 1.9).[34] A typical firm may have relationships or duties to governments, local community organizations, owners, advocacy groups, customers, competitors, media, employees, environmentalists, and suppliers. While this list is not exhaustive, it demonstrates the various parties and groups with which a firm has relationships. The stakeholder view of the firm helps managers better understand the complex internal and external environment of the firm in today's marketplace. After Lorenzo's departure from Continental Airlines, the airline floundered with a series of unsuccessful CEOs until Gordon Bethune took the helm. Instead of running the airline as a financial entity focused exclusively on maximizing short-term performance, Bethune developed a comprehensive change plan to address the needs of customers, employees, investors, and suppliers. This holistic approach to running the airline fostered a sense of collaboration that had not previously

Stakeholder view
A business framework that identifies and analyzes multiple groups that interact with the firm and attempts to align organizational practices to satisfy the needs of these various groups.

Figure 1.9 〉 Various Stakeholders of a Firm

existed. In one year, the airline went from posting the worst reliability and performance metrics in the industry to the best. While Bethune employed a series of specific tactical actions to turnaround the airline, the key to the ultimate success was a broad stakeholder view.[35]

Each firm has a different set of stakeholders that affect its performance in the marketplace. The importance of various stakeholders also changes at different points in an organization's lifecycle.[36] For instance, the local community may be an influential stakeholder when a firm establishes a presence in a new location. After a period of successful operation in a local community, this stakeholder's level of influence may dissipate. In upcoming chapters, we'll define some of these stakeholders when we discuss the firm's external and internal environments in detail. For now, let's take a look at how managers can use the stakeholder approach to manage the firm more effectively and improve firm performance.

STAKEHOLDER APPROACH

According to the stakeholder theory, "a stakeholder is any group or individual who can affect or is affected by the achievement of an organization's purpose."[37] At its core, stakeholder theory is concerned with who can influence a firm's decisions and who benefits from those decisions.[38] The first step in organizing for stakeholder management is to identify all of the important stakeholders of the firm. While Figure 1.9 advances a certain group of stakeholders, this is by no means representative of every organization. The second component of stakeholder management involves designing formal processes and systems to deal with the firm's various stakeholders.

Stakeholder Mapping

The first step of stakeholder management is to map all of the stakeholder relationships relevant to the firm (see Figure 1.10). The manager must ultimately decide which groups or individuals can affect or are affected by the firm.[39] The manager can initiate this process by using the template from Figure 1.9 and adding or subtracting the firm's various stakeholders. As mentioned, each firm will have a specific group of relevant stakeholders. Some stakeholders will be more important than others. For instance, stakeholders that control vital resources are particularly important to consider.[40] Once the initial stakeholder map is constructed, the manager should identify specific subgroups within each stakeholder. For example, it is not sufficient to identify just the "government" as an important stakeholder on the map. Instead, the manager should seek to expand this group to a greater level of detail by mapping out the specific governmental agencies that affect or are affected by the firm.

The next step in the mapping process is to define the stakes that each group or subgroup seeks through its involvement with the firm. For example, one might have listed the government on his or her stakeholder map and the Environmental

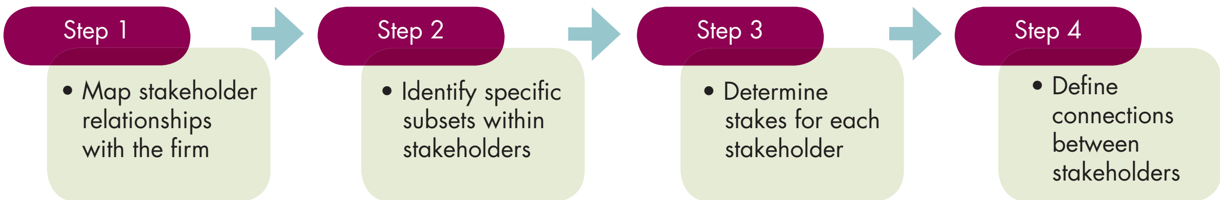

Figure 1.10 〉 Stakeholder Mapping Process

A DIFFERENT View

Profit, planet, and people. First introduced in the mid-1990s, "the triple bottom line," or the three Ps, measures the financial (profit), environmental (planet), and social (people) performance of a corporation over a period of time. Sustainable corporations that emphasize social and environmental responsibility, regardless of their motives, are increasing their profits and often outperforming their more traditional competitors.

Timberland is one company that is focused on reducing its carbon footprint, boosting renewable energy use, and increasing the integration of recycled, organic, or renewable materials for its apparel lines while maintaining its profitability. Identify another sustainable corporation that focuses on the triple bottom line.

- How successful are they at each of the three Ps?
- How do they quantify "planet" and "people?"
- Is this practice always ethical and why?

Identify a more traditional corporation that focuses only on profit.

- Would a focus on the three Ps benefit them?
- What are ways that they could implement the three Ps?

Protection Agency (EPA) as a subgroup within this category. The EPA's relationship with the firm might be aimed at reducing the carbon emissions from production processes. By mapping out this relationship, one can start to better understand why the EPA has an interest in the organization and how one can start to address this interest.

In general, some important lessons may emerge from the mapping process. First, a firm's stakeholders and their interests are not static. Just because the EPA is concerned with carbon emissions does not mean it will not raise issues with waste disposal policies in the future. Second, many of the stakeholders on the map have the potential to become interconnected on a specific issue. As we saw in the Walmart case, the firm encountered powerful resistance because the city council and the local unions banded together. In this instance, two groups that typically did not work with each other joined forces to help block Walmart from entering the Inglewood market. As a manager, you must recognize the potential for these types of linkages to occur. In recent years, Walmart has tried to improve its reputation by investing more in employee health benefits (a key concern of unions) and by launching efforts to reduce the environmental impact of its operations (a key concern of environmentalists and community organizers).[41]

Stakeholder Management Processes

Once the stakeholder mapping process is completed, the manager should move on to develop mechanisms in the firm that can better identify and respond to new stakeholders and the complexity in the environment. This is by no means an easy task. Managers can develop these stakeholder mechanisms in several ways, including through strategic review processes and environmental scanning.

In a **strategic review process**, senior leaders of a corporation meet with business unit managers in a formal review session.[42] During these meetings, business unit managers review the performance of their unit or division and present their perspective on the future prospects of the unit. The strategic review process generally includes information on financial performance and targets, new business prospects, research and development updates, manufacturing capacity, talent management, and competitive threats. While the primary goal of the strategic review process is strategy formulation and target setting, the leader can use this forum to merge the firm's stakeholder map with new strategic projects. For example, when Walmart decided to expand the Supercenter format into California, managers might have initiated a strategic review process to discuss the operational, financial, and organizational strategies that would accompany this major initiative. At the same meetings, management also could have discussed the various stakeholders that would affect or be affected by this new strategic move. Based on these discussions, Walmart might have developed various strategies to deal with the possibility of resistance from the city council. In a sense, the merging of stakeholder analysis into the strategic review process is an attempt to ensure that new proposals are adequately understood and evaluated. Through this process, leaders can take preemptive action to address potential concerns of various stakeholders.

Strategic review process
The process by which senior leaders of a corporation meet with business unit managers to review progress toward specific goals.

Environmental scanning
A tool that managers use to scan the business horizon for key events and trends that will affect the business in the future.

The second stakeholder process that can be used to identify and understand stakeholder response and activity is **environmental scanning**.[43] With environmental scanning, managers scour the business horizon for key events and trends that will affect the business in the future.[44] Managers who engage in environmental scanning tend to produce stronger financial results for their organization than those who refuse to pay attention to the contextual landscape. This is especially true for entrepreneurs who often capitalize on emerging trends.[45]

Managers can pursue environmental scanning through various avenues, including scenario building and trend analysis. In **scenario building**, a manager seeks to forecast the likely result that might occur when several events and stakeholders are linked together. For example, a Walmart manager may have used scenario building to determine that Supercenter expansion would push grocery prices lower, forcing other grocery chains to lower their cost structures to compete. This cost reduction effort could lead to other grocery chains lowering wages and health benefits, leading to protests from food worker's unions and ultimately to the unions pressuring the Inglewood city council to block Walmart from building in their town. This analysis is obviously variable, but it is extremely useful for identifying a potential scenario that might hurt or help a firm.

Having identified various potential scenarios, the manager can then turn his or her attention to **contingency planning** to prepare the firm for a reasonable range of alternative futures.[46] In contingency planning, the manager typically assigns probabilities to these alternative futures and begins to map out a series of preemptive action steps to prepare the firm.

Another technique used to predict stakeholder response and activity is **trend analysis**. In trend analysis, key variables are monitored and modeled to help predict a change that might occur in the environment. While trend analysis is an inexact science, it can be a useful tool for helping a manager better understand how certain environmental variables will affect the firm and its stakeholders. The success of environmental scanning and trend analysis is heavily dependent on the manager's ability to accurately assess the risks and opportunities that are confronting the firm.[47]

Knowing when and how to make strategic changes is not always easy. Managers must look beyond the boundaries of their internal operations to prepare for emerging competitive threats or capitalize on new potential opportunities.[48] In a sense, managers need to have peripheral vision—the ability to see beyond the boundaries of managing their day-to-day operations. Managers who excel at these boundary scanning activities possess **contextual intelligence**; they understand the impact of environmental factors on their business operations, and they understand how they can influence or react to those same factors.[49]

Managers can enhance their contextual intelligence by understanding historical precedents and how they have impacted an industry. An appreciation for historical trends and events in an industry can help managers be more attuned to the potential impact of similar occurrences in the future. Managers can enhance their environmental scanning skills by seizing opportunities to experience new situations that could impact their business (see Figure 1.11).[50] For instance, if a company is hoping to secure new suppliers in China or India, company executives need to visit these locations to better understand the opportunities that are available as well as the cultural implications of working in global locations.

Scenario building
Forecasting the likely result that might occur when several events and stakeholders are linked together.

Contingency planning
The systematic assessment of the external environment to prepare for a possible range of alternative futures for the organization.

Trend analysis
A tool where key variables are monitored and modeled to help predict a change that might occur in the environment.

Contextual intelligence
The ability to understand the impact of environmental factors on a firm and the ability to understand how to influence those same factors.

Figure 1.11 〉 Building Contextual Intelligence

Managing Uncertainty

Many aspects of the business environment are difficult to interpret. It is especially difficult to predict the impact of contextual forces on how an industry will evolve or a business will operate in the future. Engaging in processes to build contextual intelligence like environmental scanning helps to mitigate some of this inherent uncertainty and risk.[51]

Despite a manager's best efforts, there will always be some level of uncertainty about the direction of the business environment.[52] It is important that managers appropriately estimate this level of uncertainty. If managers underestimate the nature of uncertainty in their industry, they will fail to prepare for competitive threats or to capitalize on potential opportunities. If managers overestimate the level of uncertainty, they may become paralyzed and fail to act, assuming that there is nothing that they can do to influence their business environment. Managers generally face greater uncertainty when many contextual forces impact an industry and when these same forces are constantly changing (see Figure 1.12).[53] The rate of change in the context will dictate the extent to which managers should engage in environmental scanning activities and the degree to which companies will need to adapt their operations.[54]

Now that we have discussed the stakeholder approach and how it can be applied, let's take a look at a firm that has a very diverse set of stakeholders to see how the firm dealt with their constituents in a very complex environment.

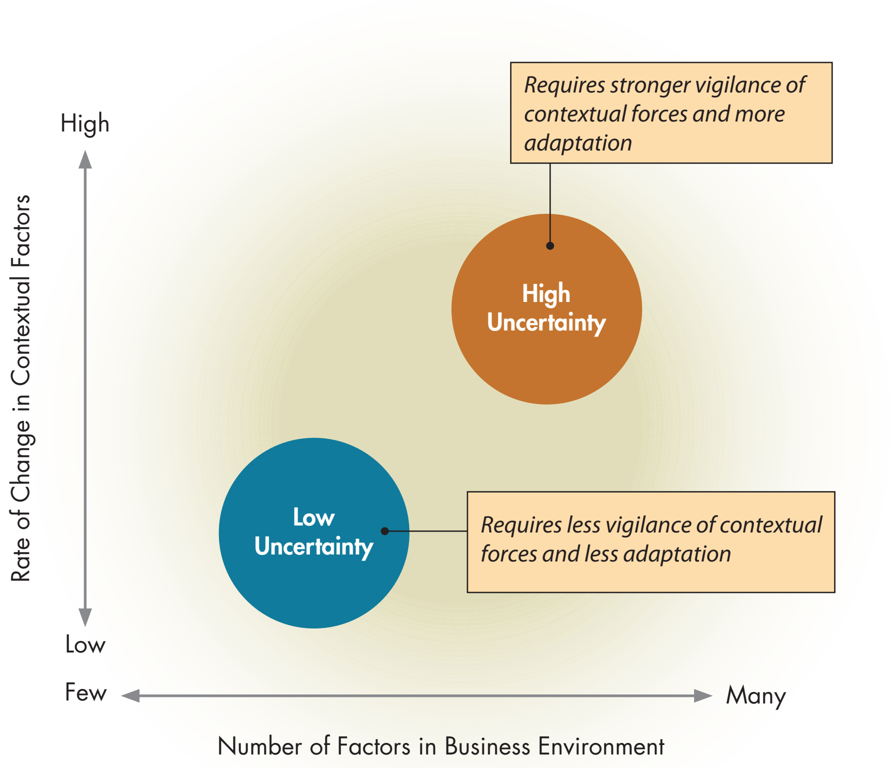

Figure 1.12 〉 How Contextual Forces Impact Uncertainty

BHP's Tintaya Copper Mine

While you may not have heard of BHP Billiton, you most likely own a product or live in a dwelling that uses its materials. In recent years, this metal mining company has grown in power and stature as the demand for base metals has increased in concert with the growth of economies in China and India. BHP is a global mining giant that maintains business in aluminum, iron ore, coal, lead, copper, and zinc extraction in 130 locations in 21 countries across the globe. In 2014, the company had revenues of $67 billion and net income of $14 billion.[55]

As part of its global expansion efforts, the company acquired the Tintaya Copper Mine, which was located in the Andean region of Peru known as Espinar province. While copper mining had contributed to greater prosperity for the Peruvian government, most of the local inhabitants of Espinar province did not see any benefits. In fact, the Tintaya mine had long been a source of contention between the locals and the mine's various operators. Established in 1985 as a state-owned enterprise, the mine originally stood on 2,368 hectares of land expropriated from 125 families in Tintaya Marquiri, an indigenous farming community.[56] In return for the land, the Peruvian government reportedly offered farmers as little as 10 soles per hectare (about $3 for 2.45 acres) and the promise of mining-related jobs.[57] The jobs, however, were few in number, and the loss of land pushed many local families into poverty.[58]

As metal prices continued to soar in the early twenty-first century, Peru's fortunes climbed in concert (see Figure 1.13). The rising profile of Peru's mining industry also attracted the attention of various NGOs and subsequently led to widespread unrest among some of the lower classes of society. Protests against large-scale mining and its environmental and social impacts became more frequent throughout the country.[59] BHP thought it had supported the local community by creating jobs for over 600 locals and voluntarily contributing close to $2 million for a local development fund. However, many locals in the Espinar province had grown tired of the company because it continued to acquire land cheaply in the areas surrounding the Tintaya mine. As concerns about BHP's land purchases mounted, community members also began to speak up about the perceived environmental degradation the company had caused. Residents living near the company's operations claimed that wastewater from the company's processing plant had contaminated pasture lands and rendered the water unfit for consumption.[60]

In the spring of 2003, nearly 1,000 people stormed the Tintaya mine and took the general manager hostage. This group consisted of people from the Ccañipia river basin, who claimed that the company's tailings reservoir had polluted water sources used in the local dairy farming industry.[61] BHP negotiated with this group and agreed to set up a development fund that contributed a certain percentage of the mine's annual profits to the fund. At the same time, other groups in the mining community became angry that the company had negotiated a settlement with the Ccañipia group that had stormed the mine.[62] On May 23, 2005, 500 members of left-wing political parties and student groups from the provincial capital gathered outside the mine's gates to protest the terms of the agreement with the community. The decision was made to shut down the mine and evacuate all personnel.[63]

BHP failed to recognize the importance of its various stakeholders throughout the entire process. When the company obtained the mine from the Peruvian government in the 1990s, it was apparent that BHP did not have a stakeholder strategy in place. And despite subsequent attempts to develop one in the early 2000s, the company's inattention ultimately led to a crisis situation. Though the mine eventually reopened, BHP decided to sell it in 2006.

Ric Francis/ZUMAPRESS.com/Newscom

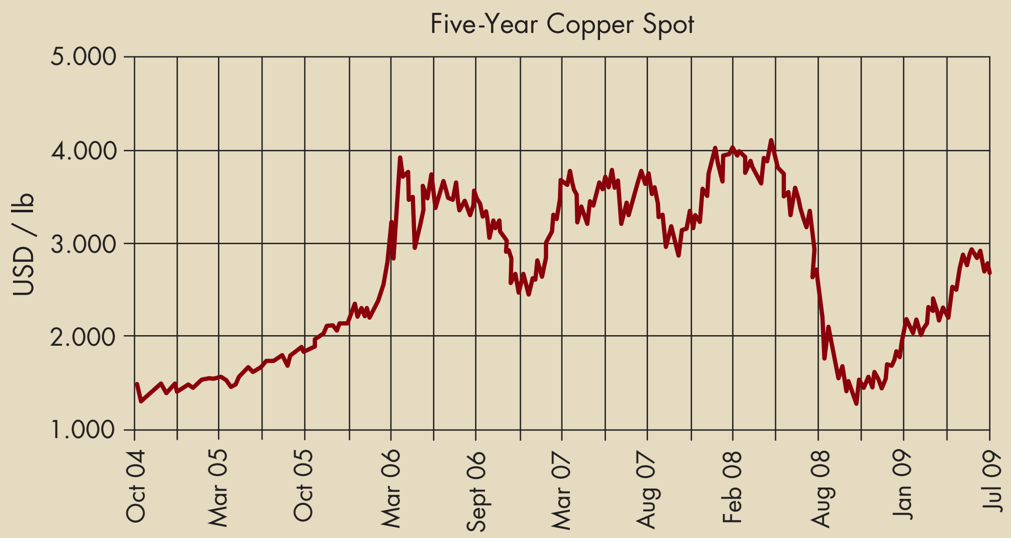

Figure 1.13 〉 Five-Year Copper Spot Price

Source: Kitco—Spot copper historical charts and graphs, kitcometals.com, www.kitcometals.com/charts/copper_historical_large.html, accessed October 7, 2009. Used by permission.

Case in Point

BHP's Tintaya Copper Mine

1. Often managers react to a crisis situation. An alternative strategy is to try to proactively prevent crises. What are some actions that BHP's managers could have done differently to prevent the crisis?
2. Contextual intelligence is an essential managerial skill. How could managers of BHP's Tintaya Copper Mine have analyzed the environment or its business operations to influence or react to the crisis?
3. For the executives of BHP's Tintaya Copper Mine, why was managing uncertainty a difficult task? How can scenario planning help you to manage uncertainty?
4. A stakeholder view of the firm takes into account how multiple groups interact with the firm. Who are the key stakeholders in the BHP's Tintaya Copper Mine case? Which stakeholders would you have collaborated with to prevent the crisis?
5. What are the important lessons learned from the BHP's Tintaya Copper Mine case? How can you apply these lessons to the management practices of other firms?

SUMMARY

LO1 There are three important pillars of managing organizations: strategic positioning, organizational design, and individual leadership. Success in business requires the ability to devise and nurture a defensible strategic position. The execution of this strategy, in turn, is dependent on a variety of organizational design decisions, including the allocation of resources, the structure of the organization, and the incorporation of key performance metrics. Ultimately, strategy and organizational design are the result of individual leadership actions. As such, it is critically important to understand how leaders identify and develop relevant skills.

LO2 Success in the global business environment requires effective management and leadership. Management is the act of working with and through others to accomplish a desired objective, and leadership is the ability to drive change and innovation through inspiration and motivation. Management and leadership skills are complementary.

Effective leaders develop and deploy technical, interpersonal, and conceptual skills. The relative importance of each of these skills is based on an individual's level in the firm. At the entry level, technical skills are vitally important. These technical skills often open the door for new employees. Interpersonal skills are also important for new employees as they join working teams, but new employees must rely on their technical skills to demonstrate competence in the organization.

At the managerial level, the technical skills are still important but are less relevant than interpersonal and cognitive skills. The work of managers involves many aspects of team management, which require strong interpersonal skills. Managers also provide support for innovative efforts and engage in scenario planning, both of which rely on conceptual abilities. At the senior level in a firm, leaders must focus on cognitive abilities to create the strategic positioning that will enable the firm to effectively compete in the marketplace. They do not do so in a vacuum. They must work with others and motivate the organization through effective communication, which is a central element of strong interpersonal skills.

LO3 The view of effective management has evolved over the last 100 years from a focus on the bureaucratic organization structure to scientific management to human relations to alignment or contingency theories. The contingent view of management states that there should be a fit or an alignment between an organization's structure, the business environment, and the leadership of the firm.

LO4 The business environment has grown more complex and the perspective on the purpose of business has changed in tandem. BHP and Walmart illustrate some of the immense challenges that managers may face. A manager can no longer evaluate his or her firm or its industry through a narrow managerial or shareholder viewpoint.

LO5 Rather, the manager must consider the numerous stakeholders with which the firm interacts and how those stakeholders impact or are impacted by the actions of the firm. In addition, the manager must be aware of all of the different dimensions in the company's external and internal environments.

Mapping out all of these stakeholders and environments is the first step in the stakeholder approach. Managers also use various stakeholder management processes such as strategic reviews, environmental scanning, and scenario planning to ensure that they are satisfying the important stakeholders of the firm. These processes help managers prepare for uncertainty and risk and help to ensure that the firm sustains its long-term relevance in the marketplace.

KEY TERMS

Bureaucratic organization structure
Business environment
Contextual intelligence
Contingency planning
Contingent view
Environmental scanning
Human relations movement
Leadership
Management
Managerial view
Scenario building
Scientific management
Shareholder view
Stakeholder view
Strategic review process
Trend analysis
VUCA

ASSIGNMENTS

Discussion Topics

1. Describe how the three pillars of management interact with each other. How can a firm's strategy influence the design of the organization? In what ways can a manager influence the strategy of an organization?
2. How do various contextual factors influence the business landscape? What levers can a manager use to influence the context?
3. What is the most important contextual factor impacting business today? How could a manager or firm influence this factor?
4. Combine the differences between managers and leaders with the various skills that are important to success in business (technical, interpersonal, and conceptual). What skills are more important to managers? Why? Do the same for leaders.
5. What are the advantages and disadvantages of the shareholder and stakeholder views of the firm? If you were a stockholder in a firm, what perspective would you want the management team to follow? Why? If you were an employee, would your perspective change?

6. What role do nonprofits and advocacy groups play in shaping the business context?

7. Review Figure 1.12. If you were starting a business, would you rather be in an industry with high or low uncertainty? What are the advantages and disadvantages of each environment? What skills would you need to be successful in each environment?

Management Research

1. Use resources in your library to identify examples of the different perspectives of management:
   - Bureaucratic Organization Structure
   - Scientific Management
   - Human Relations
   - Contingent View

2. How have management perspectives changed over time? How would you describe current management practices? What changes in management practices do you anticipate in the next five to ten years? How should individuals prepare for these changes?

3. Select a firm and draw a stakeholder map for it. What potential changes should the firm anticipate in its internal and external environments? How should the firm prepare for these changes?

In the Field

1. Spend some time with an experienced manager to learn how the individual "changed" while progressing through positions of greater career responsibility. Similar to Figure 1.4 in this chapter, create a map that identifies the importance of technical, interpersonal, and conceptual skills in that individual's career.
2. Visit a local business and collect the following information to enhance your contextual intelligence:
   - Identify historical events that have impacted its industry.
   - Scan its internal and external environments to identify current trends that affect the business.
   - Identify another industry or firm that the local business can learn from given its current environment.
   - Develop two future scenarios for the local business you visited. Given these scenarios, what type of contingency planning would you recommend?

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CHAPTER

2

The Global Business Environment

Chapter Outline

Introduction

Globalization

- Global Trade Agreements
- World Trade and Free-Trade Associations

External Environment

- General Environment
- Task Environment

Internal Environment

- Owners
- Board of Directors
- Employees
- Culture

Summary

Key Terms

Assignments

Endnotes

Learning Objectives

After reading this chapter, you should be able to:

LO1 Describe how changing contextual forces in the global business environment impact the competitive position of a firm.

LO2 Understand the role that globalization, including trade agreements and trade associations, has played in shaping the business landscape.

LO3 Define the primary dimensions of the external environment of a firm, including the components of the general and task environments.

LO4 Differentiate between the four components of the internal environment of a firm, including owners, boards of directors, employees, and culture.

SELF-REFLECTION

You and Your Business Environment

The ability to scan, acquire, and learn from your business environment is an important management skill. Please respond True or False to the following statements to assess your competency in this area.

1. I read articles from the business press and surf the Web to stay up-to-date on current events.
2. I understand how the development and usage of technology influences the external environment.
3. I track economic data to assess the global business environment.
4. I can identify sociocultural trends that influence the competitive environment.
5. I comprehend how demographic data can be used to make business decisions.
6. I realize that companies operate in a global environment, and because of this pay attention to events that happen in different parts of the world.
7. When analyzing a firm, I identify its competitors and their impact on the firm's environment.
8. I understand the critical role that customers and suppliers play in shaping a firm's operations.
9. I understand the different ownership structures of a firm and the governance role of a firm's board of directors.
10. I realize that a company's employees and its culture are important components to its success.

If you answered True to the majority of these statements, you are aware of your business environment.

INTRODUCTION

Businesses and their leaders do not operate in isolation. They are part of a much larger ecosystem that is constantly evolving. As we discussed in Chapter 1, today's business context is often referred to as VUCA—volatile, uncertain, complex, and ambiguous. Successful business leaders not only respond to a VUCA context in the global business environment but also try to influence it. Some leaders focus their efforts on lobbying to influence the government's role in business. Other leaders identify growing market niches or target consumer segments and develop products or services to fill specific needs. Still other leaders invest in research and development to commercialize technological innovations. In these ways, business leaders take a proactive stance in managing their environment and adapting their strategies accordingly.[1]

The context of the last decade provides ample evidence of how the business landscape can change so quickly. These changes have required managers to be even more nimble in their adaptability. Managers in all types of businesses faced the aftereffects of a credit crunch, largely fueled by banks and other institutions lending money for homes to subprime customers. This practice went unnoticed as home prices in the United States experienced a meteoric rise through most of the first decade of the twenty-first century. The rise in home ownership fueled a host of other businesses, including automobiles, home improvement, appliances, and landscaping. However, by late 2007, many consumers could no longer afford the payments on their adjustable rate mortgages, and their inability to repay their loans contributed to an unprecedented financial collapse. By the end of 2008, financial giants Lehman Brothers, American International Group, and Merrill Lynch had imploded. In addition, venerable companies such as the 86-year-old KB Toys, 60-year-old Circuit City, and 34-year-old Linens 'n Things collapsed. Within a few short years, the entire business landscape had changed and managers had to scramble to define a new way of operating in an environment in which consumers were skeptical, financing was tight, and employees were on edge. Unemployment in the United States increased from 4.6% in 2007 to a peak of 9.6% in 2010.[2] While the unemployment rate has been steadily declining since its peak in 2010, many individuals, including recent college graduates, have struggled to find employment that is commensurate with their skills, education, and experience.

The aftereffects of the post-2008 recession have not been isolated to the United States. The financial crisis has been global with many countries in Europe, especially Greece and Spain, experiencing crippling debt and very high levels of unemployment. The struggles in Europe and other parts of the world, in turn, impact the success of many U.S. businesses demonstrating the interconnectedness of the global economy. As we will see throughout this chapter, managers can no longer only pay attention to the U.S. economy; they have to develop a better understanding of the global economy.

While many of the events of the last decade seem tumultuous, they represent the constant changing nature of global business. These events represent both challenges and opportunities for managers. A review of the companies that comprised the Dow Jones Industrial Average over the last 100 years provides a quick glimpse into how dramatic these changes can be and how they impact the rise and fall of businesses (see Table 2.1).

Only 7 of 30 companies that appeared on the Dow Jones Industrial Average (DJIA) in 1956 were still on the list in 2015, and two of them (Chevron and AT&T) were removed from the list at one or more points during the past 59 years. In 2013, Alcoa, which had been on the DJIA for 54 years, was replaced by Nike. The current list also includes several companies that represent the new titans of industry including Cisco, Home Depot, Microsoft, and Walmart. While these companies have ascended to the list in the last few decades, there is one company that has stood the test of time.

General Electric Company (GE) is the only firm that has been included on the Dow Jones Industrial Average since 1896. GE has sustained its relevance by constantly adapting and refining its strategy and business processes. For instance, if you reviewed GE's business portfolio in the early 1980s, you would discover that 75% of its business was based in manufacturing and 25% was based in services. At the turn of the twenty-first century, those numbers were reversed: 75% of GE's business was based in services, and only 25% was derived from manufacturing.[3]

Throughout its history, GE has been able to reinvent itself. For instance, its first Chief Executive Officer (CEO), Charles Coffin, created a centrally controlled function-based organizational structure, which was dismantled by a successor CEO Charles Wilson, who favored a decentralized structure. In the late 1950s and early 1960s, another CEO, Ralph Cordiner, invested in computers. His successor Frederick Borch bailed out of computers. In the late 1970s, CEO Reginald Jones established a layer of senior executives and invested in a coal mine. A few years later, CEO Jack Welch abandoned the sector approach and sold the mine.

May 26, 1896	July 3, 1956	January 31, 2015
American Cotton Oil	Allied Chemical	3M Company
American Sugar	American Can	American Express
American Tobacco	American Smelting	AT&T
Chicago Gas	AT&T	Boeing
Distilling & Cattle Feeding	American Tobacco	Caterpillar
General Electric	Bethlehem Steel	Chevron
Laclede Gas	Chrysler	Cisco Systems
National Lead	Corn Products Refining	Coca-Cola
North American	DuPont	DuPont
Tennessee Coal & Iron	Eastman Kodak	Exxon Mobil
U.S. Leather	***General Electric***	***General Electric***
U.S. Rubber	General Foods	Goldman Sachs
	General Motors	Home Depot
	Goodyear	Intel
	International Harvester	International Business Machines
	International Nickel	JPMorgan Chase
	International Paper	Johnson & Johnson
	Johns-Manville	McDonald's
	National Distillers	Merck
	National Steel	Microsoft
	Procter & Gamble	NIKE
	Sears Roebuck	Pfizer
	Standard Oil of CA (Chevron)	Procter & Gamble
	Standard Oil of NJ (Exxon Mobil)	Travelers
	Texas Company	United Technologies
	Union Carbide	UnitedHealth Group
	United Aircraft (United Technologies)	Verizon
	U.S. Steel	VISA
	Westinghouse Electric	Walmart Stores
	Woolworth	Walt Disney

Table 2.1 〉 Composition of Dow Jones Industrial Average, 1896, 1956, 2015

Source: "Dow Jones Industrial Average: Components," available at Dow Jones website at http://www.djaverages.com/, accessed January 31, 2015

This reinvention of the company has continued. While Welch invested in insurance and many financial businesses, his successor Jeffrey Immelt has offloaded many of these business lines (see Figure 2.1). The capacity of the company to sustain its relevance over such a long period of time is a testament to the ability of

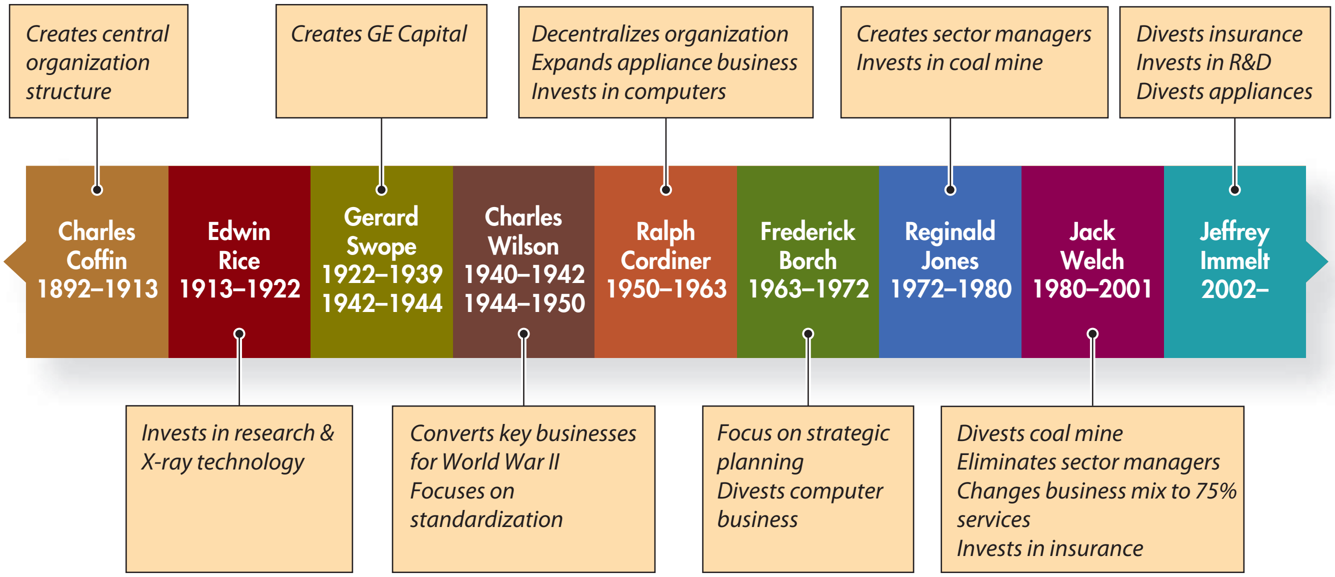

Figure 2.1 〉 General Electric's CEOs, 1892–Present

Source: Anthony J. Mayo

successive CEOs to accurately read and/or influence the global environment. This is one major way GE has been able to retain its place on the DJIA.

The increasing globalization of markets has hastened the pace and intensity of change. To remain competitive, companies can no longer sell exclusively in their domestic markets. Firms such as McDonald's, Starbucks, Apple, and Facebook have experienced slowing growth at home. In response to this trend, all of these firms (McDonald's in 1967, Apple in 1980, Starbucks in 1996, and Facebook in 2006) have ventured abroad for new sources of growth. By 2014, each of these firms obtained a significant portion of their revenues from international markets (McDonald's 67%, Apple 62%, Starbucks 31%, and Facebook 54%).[4] In emerging economies such as China and India, the opportunities are immense. In 2012, the Chinese middle class reached 300 million people, almost equivalent to the total population of the United States.[5] By 2020, China's middle class is expected to surge to over 500 million, and the Asia-Pacific region, as a whole, is expected to comprise 54% of the world's middle class (see Figure 2.2).[6] This growth provides many new opportunities for companies who can lead effectively across vastly different geographies.

Globalization has also presented challenges, including the emergence of new, powerful competitors in many industries. In computers, Dell and Apple must contend with the Chinese firm Lenovo, which purchased IBM's personal computer (PC) business. In automobiles, global producers such as GM must contend with Chery Automotive and Geely Automotive from China. The home appliance and electronics sector has also seen a number of formidable new competitors including Haier from China and Samsung and LG from South Korea.

Understanding the global business environment is vital to sustaining success. Many firms have failed in their attempts to expand globally. One company that has been able to build a consistently successful global presence in a constantly changing business environment is Coca-Cola.

In this chapter, we will explore the forces of globalization and the various internal and external entities that comprise a firm's business environment. Understanding the competitive landscape and knowing how and when to react to threats and opportunities are vitally important to a firm's long-term sustainability.

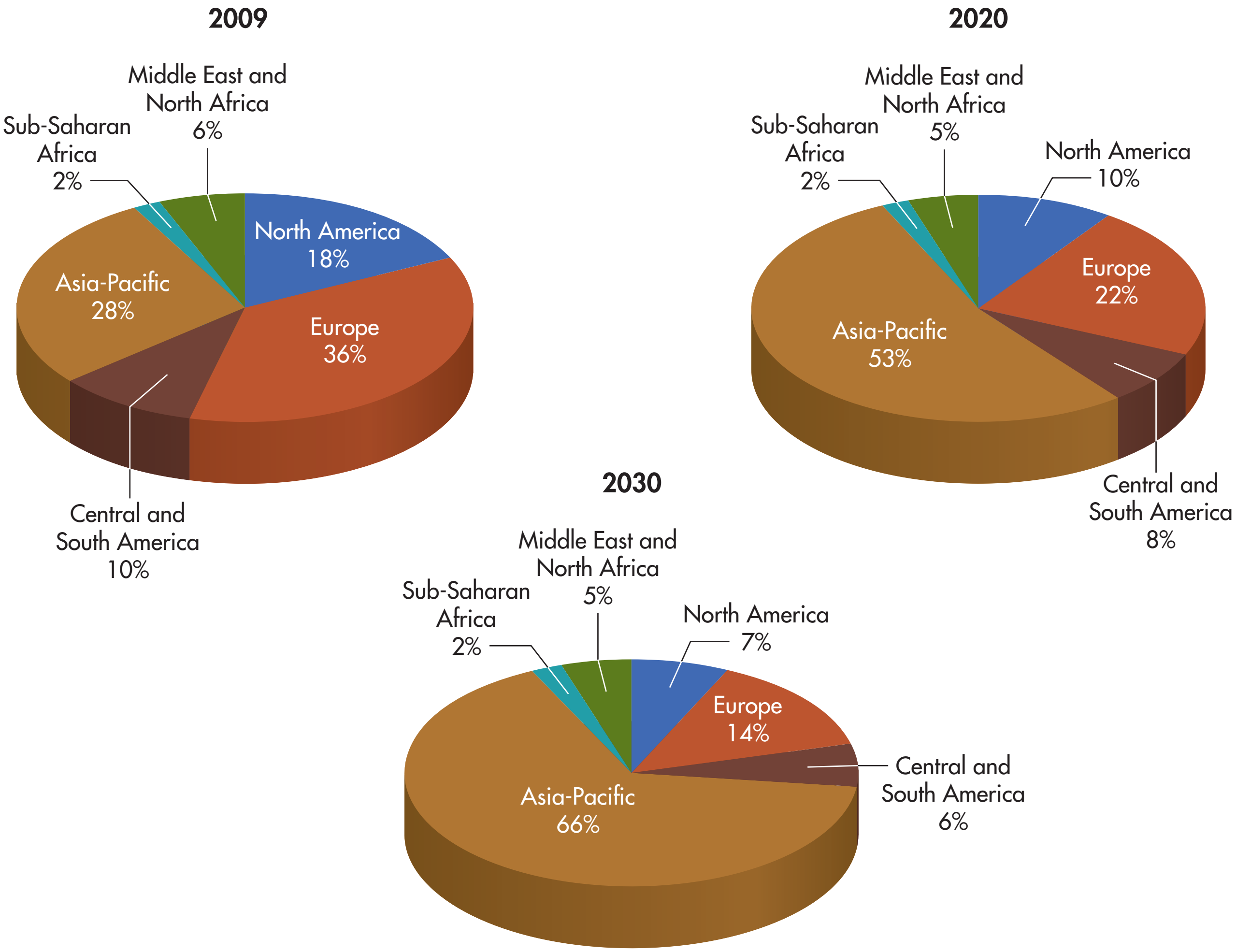

Figure 2.2 〉 Composition of the World's Middle Class, 2009, 2020, 2030

Source: "Hitting the Sweet Spot: The Growth of the Middle Class in Emerging Markets," Ernst & Young, 2013, available at http://www.ey.com/GL/en/Issues/Driving-growth/Middle-class-growth-in-emerging-markets–China-and-India-tomorrow-s-middle-classes

Coca-Cola Company

In 2014, Coca-Cola celebrated its 128th anniversary and was ranked as the third best brand in the world, after having held the top spot from 2000 to 2012.[7] Like GE, Coca-Cola has been able to sustain its relevance and market viability for more than a century. Unlike GE, Coca-Cola has concentrated on the proliferation and expansion of a core product line for most of its history. The basis of that core product line is the secret cola formula that was stored in a vault at the SunTrust Bank in Atlanta from 1925 to 2011. As part of the brand's 125th anniversary, the secret formula was relocated to a special enclosure at the new interactive World of Coca-Cola Exhibit at company headquarters.

John S. Pemberton, a pharmacist in Atlanta, Georgia, founded the company in 1886 when he combined a unique syrup with carbonated water to sell at the soda fountain at Jacobs' Pharmacy. One of the customers at the soda fountain was Asa Candler, whose colleague recommended the drink as a treatment for Candler's persistent upset stomach and headaches. The combination of caffeine and carbonation seemed to relieve Candler's pains, and he soon became enamored with the product. Five years after that fateful first drink, Candler bought the concoction's recipe and formula from Pemberton and began an aggressive campaign to expand fountain sales of Coca-Cola. By 1895, Coca-Cola was sold and drunk in every state and territory of the United States.

Candler's first expansion outside the United States came in 1906 when bottling operations were opened in Canada, Cuba, and Panama. That was also the year that Candler signed D'Arcy Advertising Company as Coke's agency of record. This relationship would last 50 years and result in the creation of many memorable advertising and promotional campaigns including the indelible image of Santa Claus with a Coke. Tapping into the social consciousness of the country was vital to the sale of Coke and its ascendance into an iconic American and global brand. A quick survey of Coca-Cola's trademark slogans throughout its history highlights the way in which the company was able to build a connection with the American populace (see Table 2.2).

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While Candler initiated the first globalization campaign for Coca-Cola, it was Robert Woodruff who was most responsible for making Coke a truly global brand. Woodruff became president of the company in 1923 and served in this capacity for more than six decades. He invested heavily in advertising and established the Coca-Cola Foreign Department in 1926 to service bottlers throughout the world. By this time, Coke had bottling operations in Belgium, China, Columbia, Germany, Mexico, and Spain, among others.

Coke's big push on the world stage came during World War II when Woodruff announced that Coke would be available to any soldier serving overseas for just five cents. Through this seemingly generous proposition, Woodruff was able to secure access to sugar, which was severely rationed during the war. The rationing could be lifted if a company demonstrated that their product fulfilled a vital military function. Though one would be hard-pressed to conceive of Coke as a military necessity, the product did provide a morale boost for the troops, and Woodruff used this connection between the soldier and the slice of Americana to advance his cause. The strategy worked so well that the company received government subsidies to build 64 bottling plants throughout the world, which resulted in the consumption of over 5 billion bottles of Coca-Cola. American soldiers drinking Coke unwittingly became global marketing ambassadors for the firm.[8] When the war ended, the company had a ready-made global infrastructure and a giant head start on its global positioning. By the end of the 1950s, foreign sales accounted for approximately one-third of company revenues.

During the first half of its history, the company sold and marketed only one product—Coca-Cola. That began to change in 1955 when Fanta Orange was introduced by the company in Naples, Italy. Once the product was successful in Italy, it was brought to the United States. From this point, a series of new products were launched including Sprite in 1961, TAB in 1963, Fresca in 1966, Mr. PIBB in 1972, Mello Yello in 1979, and Diet Coke in 1982.

Coke's efforts to expand globally were not always smooth. For instance, though the company had established operations in China in the 1920s, they were forced to leave the country in 1949 when the Communist Party came to power. Over the next 30 years, Coke was only available on the black market in China. That changed in 1979 when Coke became the first U.S. company to return to China. By the end of the twentieth century, the company had 28 bottling plants in China, and by 2008, when China hosted the Summer Olympics, Coke had partnered with a number of local establishments to create and distribute products that were aligned with the Chinese consumer market, including Heaven & Earth (noncarbonated fruit juice, tea, and water) and Lanfeng (honey green tea).[9]

The company's biggest success on the global stage has been in Mexico where per capita consumption of soft drinks is one of the highest in the world. Though Coca-Cola operated in Mexico for a number of decades, its major growth came in the 1990s when the Mexican government lifted regulations on the sale, packaging, and distribution of soda. The new laws enabled Coke to expand and leverage its distribution network in the country. Distribution was essential in Mexico as most soda in the country was consumed not in the home but on the spot. Consumers then immediately returned the bottles for refunds. Having a strong distribution network was critical for Coca-Cola to regularly and systematically replenish supplies at small, local retail shops. The company also increased its presence in Mexico through the acquisition of a major juice producer.[10] The company's efforts have resulted in a significant increase in the per capita consumption of Coca-Cola products, rising from 290 eight fluid ounces per capita in 1991 to 745 by 2012.[11]

By 2014, Coca-Cola had expanded to over 600 brands, seven of which generate more than $1 billion in revenues each, with consumers in more than 200 countries.[12] Of the $46.9 billion in revenue that the company generated in 2013, approximately 45% was derived from sales outside North America. While per capita consumption of the company's beverages had stabilized in the United States at roughly 400 eight fluid ounces, there was tremendous opportunity in Russia, China, and India where the per capita consumption was 79, 39, and 14 eight fluid ounces, respectively. Though these consumption numbers were small in comparison to the United States and Mexico, they represented significant increases. In 1992, per capital consumption in Russia and China was 2 and 1 eight fluid ounces, respectively, and consumption in India was virtually zero.[13]

The company has also invested in a number of efforts to jump-start sales in the United States. One campaign that has shown promise is "share a Coke." During the summer of 2014, Coca-Cola put the 250 most popular names of teens and millennials on 20-ounce Coke bottles. The campaign also included personalized cans available at roving kiosks and "virtual" personalized Coke bottles that could be shared in personal media. The result was a 2% increase in domestic consumption, the first such rise in a number of years.[14] Moving forward, the company seeks to increase consumption across all its markets through a combination of promoting its core cola products as well as by adapting to local customs and tastes.

Year	Slogan	Historical Context
1900	For Headache and Exhaustion, Drink Coca-Cola	Positioned as a medicinal product; offered initially in pharmacies
1906	The Great National Temperance Beverage	Positioned as an alternative to alcohol as part of the Prohibition movement in the United States
1929	The Pause that Refreshes	Marketed as an opportunity to relax during the "go-go" 1920s
1937	So Easy to Serve, and So Inexpensive	During the height of the Great Depression, Coke is marketed as a value-priced, convenient product
1949	Along the Highway to Anywhere	Coke expands with the growing suburbanization of the country
1960	Relax with a Coke	Coke's marketing is attuned to the easygoing vibe of the 1960s
1971	I'd Like to Buy the World a Coke	Coke is aligned with the free spirit of the times to promote world peace during the Cold War
1990	Can't Beat the Real Thing	Part of an effort to stave off competition from Pepsi and other cola products
2005	Make it Real	Coke's continued effort to position its brand as the first, and original cola product

Table 2.2 〉 Selected Coca-Cola Slogans

Source: Coca-Cola Company, "Coke Lore: Slogans for Coca-Cola," available at http://www.thecoca-colacompany.com/heritage/cokelore.html, accessed July 18, 2012.