

15.903: Strategy and Organization

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9 units, Spring 2003

TuTh 8:30-10:00 (E51-345) and 1:00-2:30 (E25-111)

Version 2/3/03

Overview

Organizational capability is increasingly believed to be a critical—perhaps the critical—source of competitive advantage. On one hand, firms everywhere are advised to use aggressive incentives, to be fast, to be flexible, and to be networked. On the other hand, we are in the midst of the largest merger wave in history: the large firms are getting larger.

What is going on? When should organizations outsource and when should they produce internally? When should firms diversify or merge? Can one maintain the creativity and enthusiasm characteristic of a small firm inside a large one? When should one even try? How do the answers to these questions change as one manages across boundaries, across industries, and over time?

Broadly speaking, these are the questions of corporate strategy: when and how should a firm operate in multiple markets (whether different industries, different stages of a value chain, different geographic regions, or different customer segments). This course provides some of the tools necessary to answer such questions. In particular, the course begins by discussing six basic concepts: incentives, control rights, relational contracts, structure, culture, and networks.

These discussions utilize, deepen, and integrate three courses from the first-year fall core: microeconomics (15.010), organizational processes (15.311), and strategy (15.900). For example, from microeconomics we take the ideas of incentives and game theory, from OP organizational structure and culture, and from strategy industry structure and core capability. These discussions also prepare the way for successor courses, such as technology strategy (15.912).

After discussing these six basic concepts, we turn to corporate strategy more explicitly. Much of our discussion will explore the important two-way street between a firm's "external strategy" in its product market and its "internal strategy" regarding organizational issues. One direction on this street is widely appreciated: an optimal external-strategy decision frequently requires complementary internal-strategy implementation. We will frequently emphasize the opposite direction: some external-strategy decisions are driven by internal-strategy considerations. The course is therefore appropriate for those considering management consulting, as well as for general managers who seek to understand and influence the design and performance of their organizations.

Administration

Required Purchase

The course packet is available from Graphic Arts. (Please check to make sure that all the cases and readings are included.) Some material will be distributed on-line through SloanSpace, including several lecture notes that cover core concepts (designated as “Notes” in the syllabus below).

Grading

The grading is split between in-class activities and team papers, as follows:

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|---|-----|
| ▪ Class participation and attendance | 15% |
| ▪ Four two-page papers on concepts | 50% |
| ▪ Final paper applying concepts to a firm | 35% |

Study Guide and Discussion Questions

The syllabus contains preparation questions for each session. These questions highlight key issues and should guide you in studying the case(s) and/or reading(s), as well as in preparing for the class discussion. We may not address all of these questions directly, but they will help in motivating our discussion.

Class Participation

Please be prepared for every class. If for some reason you are not prepared, please let me know before the start of class. This saves us both the embarrassment of having me call on you.

I may open the class by asking someone to summarize the readings or cases briefly, or to answer a short question. With a reading, you should be able to outline the problem that the article addresses, describe the core points of the reading, and, most importantly, offer your analysis of the strengths and weaknesses of the reading’s central argument. With a case, you should be able to identify the key issues, problems, and opportunities facing the central protagonists, articulate and evaluate alternative approaches to the problems, and your recommended course of action and the reasons for your recommendation.

I may end the class by asking someone to summarize the key lessons of the day’s discussion and to relate these lessons to the ongoing themes of the course. Part of a good closing is much like a good opening (*e.g.*, for a case, briefly summarize alternative courses of action and give reasons for your recommendation), but a good closing also looks backwards (to cases, readings, and concepts from earlier in the course) and, if possible, forwards (to topics yet to come).

Finally, we are all co-producers of the entire class discussion. It is therefore important that we all listen carefully to one another and attempt to build on or constructively

critique prior comments. Please resist the temptation to jump to topics that are not specifically open for discussion. Other issues related to effective participation include:

- Is the participant a good listener?
- Are the participant's points linked to the comments of others and to the themes that the class is exploring together?
- Do the comments add to our understanding of the situation? Are they incisive? Do they cut to the core of the problem?
- Is there a willingness to challenge the ideas that are being expressed?
- Is there a willingness to test new ideas (or are the comments "safe," such as repetition of case facts without analysis or conclusions, or repetition of a previous comment)?
- Does the participant integrate material from past classes or readings where appropriate, or does the participant merely consider each case in isolation?

Written assignments on course concepts

During the first part of the course, we will be developing six basic concepts that are useful in understanding the interplay between organization and strategy. To reinforce this learning, I will ask you to write 4 two-page papers on these concepts. (If you write 5 or 6 papers, I will take the 4 highest grades.) The paper topics are given in the syllabus below. The due dates for the assignments are

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|-----------------------------------|---------|
| ▪ Paper 1 (Incentives): | Feb. 13 |
| ▪ Paper 2 (Control Rights): | Feb. 20 |
| ▪ Paper 3 (Relational Contracts): | Mar. 4 |
| ▪ Paper 4 (Structure): | Mar. 6 |
| ▪ Paper 5 (Culture): | Mar. 18 |
| ▪ Paper 6 (Networks): | Apr. 3 |

These papers may be written by a team of up to four people. *If you choose to write the two-page papers in a team, you must maintain the same team composition for all of these assignments.*

Final paper

The final paper should pick one company and analyze the interplay between organization and corporate strategy in that firm. This paper will be due in class on May 15th. This paper may be written by a team of up to four members. (This team need not be identical to the team that wrote the two-page papers.)

The paper should provide a concise analysis of the strategic issues faced by the firm, in addition to a careful analysis of how organizational and managerial factors affect the ability of the firm to achieve its strategic goals. In particular, the paper should assess whether (and if so, how) the course's six concepts affected the firm's corporate strategy (where, as above, corporate strategy means a firm's decision to operate in multiple markets –different industries, stages of a value chain, regions, or customer segments).

You should write the project to take best advantage of the information at your disposal, and may therefore choose to emphasize some parts more than others. While you must master the facts of the case, the goal of the project is demonstrate your ability to understand and use the lessons from the course. A thoughtful analysis is essential; projects that are simple statements of facts and events will receive a low grade. You may use both primary and secondary data as you see fit.

You may study any case that interests you and your fellow group members. However, a project will not be considered successful unless it contains a thorough and thoughtful consideration of structural changes within the firm. Therefore, choose the firm carefully, with an eye toward being able to gather useful information on the internal workings of the firm. I highly recommend choosing a firm about which one or more group members has personal knowledge: your current or former employer, a competitor, a supplier or customer, or the like. It may be possible to write about the company you studied for the team project in the fall core, but this must be arranged with me beforehand.

Professional Conduct

Professional conduct is built upon the idea of mutual respect. Such conduct entails (but is not necessarily limited to):

Attending the class. Each class session benefits from the attendance and participation of all students. Your grade for participation will be affected by absences.

Arriving on time. Late arrivals are disruptive to both lectures and class discussion, and show disrespect to those who are on time. Class starts 5 minutes after the hour or half-hour.

Minimizing disruptions. All cell phones and pagers should be turned off during class. Please do not leave and re-enter the class. You should avoid engaging in side conversations after class has begun.

Focusing on the class. While you may take notes on laptops with the instructor's permission, do not use laptop computers or hand-held devices for other tasks while in class. Activities such as net surfing and emailing are impolite and disruptive both to neighbors and the class.

Respect. Please act respectfully toward all class participants.

Overview

Class 1 (2/4) *Introduction*

READING: “Mergers: Why Most Big Deals Don’t Pay Off.” D. Henry, *Business Week*, October 14, 2002, pp. 60-70.

Why does Sloan offer a course on “Strategy and Organization?” To what question(s) is this course the answer?

Class 2 (2/6): *Corporate Strategy*

CASE: PepsiCo’s Restaurants (HBS 794-078)

READING: “From competitive advantage to corporate strategy,” M. Porter, *Harvard Business Review*, May-June 1987.

Provide a strategic rationale for or against the acquisition of Carts of Colorado and/or California Pizza Kitchen. How will Pepsi benefit from these acquisitions? Will Pepsi add value to either of the two acquisition targets? Where in the organizational chart of PepsiCo should CoC or CPK be placed (choose one)? What kinds of organizational issues are raised in trying to integrate these units?

Building Blocks

Class 3 (2/11): *Incentives I: You Get What You Pay For*

READING: “On the Folly of Rewarding A, While Hoping for B,” S. Kerr, *Academy of Management Journal*, December 1975.

NOTE 1: Agency Theory

From your own experience, what are examples where firms “got what they paid for”? What were the consequences, and what might have been done instead? In what ways (if any) does the multi-task agency model help you understand “get what you pay for” experiences? Which important issues in these experiences are omitted by the model? What are the managerial lessons from this model, if any?

Class 4 (2/13): *Incentives II: Compensation, Organization, and Strategy*

CASE: Brainard, Bennis & Farrell (HBS 9-485-037)

PAPER 1: What pay plan would you implement at BB&F and why?

2/18 NO CLASS

Class 5 (2/20): *Control Rights I: Hold-Up and Vertical Integration*

NOTE 2: Hold-Up (May Be Your Friend)

PAPER 2: What other founding agreements could HGA have signed if they had anticipated the possibility of Alexander's hold-up? What are the pros and cons of these different founding agreements? What founding agreement would you have suggested?

Class 6 (2/25): *Control Rights II: Horizontal Integration*

CASE: Rudi Gassner and the Executive Committee of BMG International (A) (HBS 9-494-055)

By 1993, BMGI owned many operating companies around the world. What control rights did Gassner hold? What control rights did the operating companies hold? Which important control rights would have been held by a different party if the operating companies were independent firms, rather than operating companies owned by BMGI? What problems has this horizontal integration allowed BMGI to solve? What problems has horizontal integration created for BMGI?

Class 7 (2/27): *Relational Contracts I: Within Firms*

READING: "Taking the Dare," The New Yorker, July 26, 1993.

"Lincoln Electric's Harsh Lessons from International Expansion," D. Hastings, *Harvard Business Review*, May-June 1999.

NOTE 3: Relational Contracts

What should CSFB do now (i.e., at the end of the article)? What should they have done before and during the period of the article? What is CSFB's strategy, and how does their strategy fit with their organization? In what ways (if any) does the relational-contracts model help you understand the experiences at CSFB and at Lincoln? Which important issues at CSFB or Lincoln are omitted by the model? What are the managerial lessons from this model, if any?

Class 8 (3/4): *Relational Contracts II: Between Firms*

READING: "How Chrysler Created an American Keiretsu," J. Dyer, *Harvard Business Review*, July-August 1996.

NOTE 4: Make, Buy, or Cooperate?

- REVIEW: Crown Equipment (not Crown Cork & Seal!) from 15.900
- PAPER 3: What is the relational contract between Crown and Richardson Smith? Why is this relational contract self-enforcing for several decades? What potential changes (including but not limited to those that actually occurred) could cause this relational contract to stop being self-enforcing?
- Class 9 (3/6): *Structure I: Formal Structure*
- CASE: Jacobs Suchard: Reorganizing for 1992 (9-489-106)
- READING: “On Structure and Structuring.” R. Eccles and N. Nohria, in R. Eccles, N. Nohria and J. Berkley (eds.), *Beyond the Hype: Rediscovering the Essence of Management*, HBS Press, 1992.
- PAPER 4: What structure would you have proposed for Jacobs Suchards’ chocolate businesses in 1989, and why? What pros and cons do you see in the structures proposed in Exhibits 4 and 5?
- Class 10 (3/11): *Structure II: Informal Structure (Knowledge & Networks)*
- GUEST SPEAKER: Laurence Prusak, Former Executive Director, IBM Institute for Knowledge Management
- CASE: “Internal Disaggregation in Oticon: Interpreting and Learning from the Rise and Decline of the Spaghetti Organization,” N. Foss, 2000 (pp. 1-20).
- Class 11 (3/13): *Culture I: Culture and the Environment*
- CASE: Guaranty Trust Bank PLC, Nigeria (HBS 9-897-118)
- NOTE 5: Institutionalizing Corporate Culture
- What is GTB’s culture? What is its strategy? What role does the culture play in GTB’s strategy? What should have been done during the period of the case? What should be done going forward?
- Class 12 (3/18): *Culture II: Culture and Strategy*
- CASE: Sun Hydraulics Corporation (A and B) and (C) (HBS 9-491-119 and -125)
- PAPER 5: What is Sun’s culture? What is their strategy? How do the two relate? What potential threats do their culture and strategy face?

SPRING BREAK

Class 13 (4/1): *Networks I:*

RECALL: John A. Clendenin (HBS 490-028)
 Managing Xerox's Multinational Development Center (HBS 490-029)

READING: Ronald S. Burt, "Structural Holes versus Network Closure as Social Capital" pp. 31-56 in Nan Lin, Karen Cook, and Ronald S. Burt, eds., *Social Capital: Theory and Research* (Aldine de Gruyter, 2001).

(i) What was the attraction of the MDC to Clendenin? Why did he feel that the existing structure needed to be changed? What were the key moves that Clendenin made to make the MDC a successful operation? (ii) To what extent do you think that Burt's notion of structural holes applies to Clendenin? What limitations do you see with this perspective? (iii) To what extent does Clendenin make his subordinates more effective? Does he manage down in the same fashion as he manages up and across? Why or why not? What ethical issues do you see Clendenin's behavior raising? How do you reconcile his effectiveness at managing relationships with these ethical issues?

Class 14 (4/3): *Networks II:*

READING: "Chapter X: Confrontation" in John Brooks, *The Go-Go Years*, New York: Weybright and Talley.

PAPER 6: What was it about Chemical and Steinberg that provoked such fierce resistance and so made a takeover of Chemical by Leasco unlikely? What assumptions was Saul Steinberg making in launching the Chemical bid? What was wrong with these assumptions?

Corporate Strategy

Class 15 (4/8): *Basic Principles*

CASE: Beatrice Companies, 1985 (HBS 391-191)

(i) In what ways (if any) did Beatrice's corporate strategy in the Karnes era create value? What were the merits and drawbacks of this strategy? Given the sources of value creation in Beatrice's strategy under Karnes, was the company organized appropriately? Why or why not? (ii) Upon taking control, Dutt decides that Beatrice is in need of a strategic reorientation. Do you agree with this assessment? Explain how Dutt's strategy will or will not create value. Given Beatrice's

resources and capabilities, do you think Dutt's 1983 strategic redirection will improve Beatrice's long-term prospects? Should Dutt be fired in August 1985?

Class 16 (4/10): *Joint Ventures and Alliances*

GUEST SPEAKER: Judy Lewent, CFO and EVP, Merck

Class 17 (4/15): *Alliances (cont.)*

CASE: Honda-Rover (A): Crafting an Alliance (HBS N9-899-223)
 Honda-Rover (B): Honda Draws the Line (HBS N9-899-224)
 Honda-Rover (C): "The Sting" (HBS N9-899-225)
 Honda-Rover (D): The Changing Tide of the BMW-Rover Alliance (HBS N9-899-226)

(i) Evaluate the rationale for the initial and early stages of the Honda-Rover alliance. (ii) With respect to the Honda and Rover alliance, how would you characterize the relational contract (as opposed to the formal contract)? What steps did each side take to build it? What, if anything, could have been done more effectively on either side? (iii) In specific terms, assess BAe's negotiating moves (with respect to the possible sale of Rover) leading up through Simpson's January 27 trip to Tokyo. Do you think the extreme confidentiality was a good or a bad idea? What was the effect of the Honda-Rover relational contract on this process? (iv) Evaluate BMW's negotiating strategy. If successful, what should BMW do to build a new relational contract with Rover and, possibly, Honda?

Class 18 (4/17): *Intrapreneurship*

CASE: Xerox Technology Ventures: March 1995 (HBS 9-295-127)

At XTV, what are the important relational contracts, what would constitute renegeing, and what are the available punishments? What was done to manage these relational contracts? Could Xerox have done a better job of organizing XTV to realize its overall strategic goals? What could Xerox do in the future to address the problems XTV was intended to solve?

4/22 NO CLASS

Class 19 (4/24): *Matrix Management*

CASE: ABB's Relay Business: Building and Managing a Global Matrix (HBS 9-394-016)

Why does Percy Barnevik want ABB to be a matrix organization? What are the key structures, processes, and managerial activities in a matrix organization? What are the major costs and benefits of such an organization? In what settings are the benefits likely to outweigh the costs?

Class 20 (4/29): *Language in Organizations*

GUEST SPEAKER: John Reed, Former Chairman and Co-CEO, Citigroup

Class 21 (5/1): *Decentralization*

CASE: Johnson & Johnson: Hospital Services (HBS 392-050)

NOTE 6: Informal Authority

(i) What is J&J's culture? What is its strategy? What is its structure? What are the pros and cons of the credo, during the period of the case and afterwards? (ii) What obstacles does Pete Ventrella face as president of the new Hospital Services Company? How should he resolve these problems? How does J&J's culture affect its strategic options?

Class 22 (5/6): *Related Diversification*

CASE: The Walt Disney Company: The Entertainment King (HBS 388-147)

(i) What do you think were the key success factors for Disney during the Walt Disney years? Evaluate Disney's corporate strategy. What role did Disney's array of businesses play in its success? (ii) Assess Disney's corporate strategy under Eisner. How has the underlying logic changed since the days of Walt Disney? Do you think Disney's corporate strategy has become more or less compelling?

Class 24 (5/8): *Industry Dynamics*

CASE: Birds Eye and the U.K. Frozen Food Industry (A) and (B) (HBS 9-792-074 and -078)

Why did Birds Eye develop as a vertically integrated producer? Why did specialized intermediaries emerge? Could Birds Eye have prevented this occurring? Does a vertically integrated producer have a competitive advantage in the early 1980s? What should Birds Eye do in 1979?

Class 24 (5/13): *Student Project Presentations*

Class 25 (5/15): *Conclusion*