GREGORY KESLER | AMY KATES

BRIDGING ORGANIZATION DESIGN AND PERFORMANCE

5 WAYS TO ACTIVATE A GLOBAL OPERATING MODEL

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This book is printed on acid-free paper. ♾

Published by John Wiley & Sons, Inc., Hoboken, New Jersey
Published simultaneously in Canada

Library of Congress Cataloging-in-Publication Data is Available:

ISBN 978-1-119-06-422-0 (hardback)
ISBN 978-1-119-06-449-7 (ePDF)
ISBN 978-1-119-06-432-9 (ePub)

Cover Design: Wiley
Cover Image: iStock.com/step2626

Printed in the United States of America
10 9 8 7 6 5 4 3 2 1

FOREWORD

Running a global business is hard. Technology and information management innovations have made us more productive, but have also increased the rate at which leaders must make decisions in order to meet rising customer expectations for quality, speed, and choice.

Business leaders and human resource professionals have a combined responsibility in any organization to create an environment in which talented, hard-working people at all levels can collaborate across boundaries to execute complex strategies. The core of this work is talent management and organization design and development.

CEOs and other top business leaders are becoming much more sophisticated about how to overcome the frustrations in making global-matrix organizations work effectively through management processes, collaborative governance, and selection and development of the right leadership talent. Getting these complex structures to work is a learning process for any large company managing multinational growth initiatives. CEOs and their top teams own this work in companies that are making the most progress. It is not delegated to staff managers or consultants.

The human resources function can provide business leaders with robust decision frameworks, performance analytics and insights, efficient and inclusive methodology, and ways to monitor and adjust plans as changes are implemented. Creating the right decision support for line managers is among the highest value activities for the HR function, just as it is for other functions. For example, a core premise of an effective decision science in areas such as finance, marketing, and operations is to provide frameworks that are consistent whether decisions are made at corporate, unit, or functional levels. Examples include "net present value," "customer segmentation," and "logistical optimization." Business units do not reinvent net present value or logistics optimization to suit their particular preferences. The HR function, however, has had few consistent and tested decision frameworks to offer managers in the realm of organization design.

In *Bridging Organization Design and Performance*, Greg Kesler and Amy Kates build off of the conceptual foundation laid by Jay Galbraith over the past 30 years to provide executives and HR professionals with exactly the decision tools needed to bring sophisticated global organizations to life. In this book, they introduce the concept of *activation*, which goes beyond implementation. Activation is the dynamic, multiyear journey of analysis, design, evaluation, and adjustment of the organizational "wiring" needed to make strategic intent a reality.

Kesler and Kates provide a rich narrative on the successes and the misses of many global companies to help readers create their own road map for activation. You will find that this book speaks to the questions that many CEOs and CHROs want answers to:

- How do I match my organization to our growth strategies without creating undue complexity?
- How do I harness the energy of global networks for innovation and speed while leveraging the diverse assets of the organization?
- How do I ensure the right planning, decision-making, and performance evaluation conversations are occurring across geographic, product, and functional boundaries and set them up for success?
- What type of talent thrives in complex, global environments, and how do I build a pipeline of leaders able and willing to work in a matrix?
- What is the practical plan for assessing and adjusting as we go?

With this book, Kesler and Kates make a significant contribution to the decision science behind organization design and development. Business leaders and HR professionals will find it a practical guide for gaining competitive advantage from their global organization.

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CHAPTER 1

The Global Operating Model

A FAILURE OF STRATEGY OR EXECUTION?

Companies that compete globally must have sophisticated playbooks for sustaining competitive advantage in the face of myriad new challengers, continued waves of technological change, and uncertain economic and regulatory environments. As a result, leaders of these companies must design organizations capable of immense creativity and agility to manage the tension that is inherent in complex, global strategies.

The economic recovery of 2010–2015 has triggered a number of high-profile mergers, but even more breakups and spinoffs among large global companies, particularly those based in the United States. Between 2012 and 2014 alone, Kraft, Royal Philips, Hewlett Packard, Ingersoll Rand, ConocoPhillips, Darden, and eBay agreed to split off substantial portions of their businesses in response to a groundswell of hostility toward underperforming diversified companies. The chief executives of iconic companies including DuPont, Amgen, and GE were under pressure from activist investors such as Bill Ackman, Nelson Peltz, Daniel Loeb, and Carl Icahn to do the same. Even Procter & Gamble announced its intention to shed more than 50 percent of its brands "in order to simplify the way we organize and manage the company" (Byron 2014).

As organization designers, this trend intrigues us. Have conglomerates and diversified companies underperformed because of failures in enterprise strategy? Or are these companies failing the acid test for organization effectiveness, stumbling on execution brought about by lumbering, layered, and siloed organizational models unsuited to delivering on diverse, global strategies? Hewlett Packard's CEO, Meg

Whitman, defended plans to break up the company into two parts. "Our markets are moving at lightning speed, both the enterprise market as well as the printing and PC market, and we need to be faster, we need to be more nimble, we need to have a cost structure that is appropriate for the competitors that we face in both those businesses," she told the business press in May 2015 (CNBC 2015). Cost increases of about $400 million are expected to be offset by other synergies in the two separate companies at the end of 2017.

THE GLOBAL OPERATING MODEL

The global operating model is the means to manage this complexity, this tension, this need for both leverage and agility. It is the artful combination of organizational structure, process, governance forums, metrics, and reward systems that tie together global business units and functions with far-flung geographic market units. The global operating model is intended to structure interactions at the strategic nodes that will build and execute needed capabilities. Global operating models are typically composed of three dimensions:

1. Geographic market units (regions, countries, or country clusters)
2. Global business units (products, brands, categories, or customer segments)
3. Global operating and support functions (R&D, supply chain, marketing, IT, HR, finance, etc.)

Figure 1.1 illustrates how Deere & Co. defines the relationship among its region–market units, global product platforms, and worldwide functions.

In addition to Deere, companies such as Nike, P&G, Medtronic, PepsiCo, Unilever, IBM, Levi Strauss, and Philips have created elegant organization models and consider their worldwide, matrix organizations to be sources of competitive advantage. Some leadership teams inhabit these models as though they are second nature. Others struggle mightily.

No companies have completely solved the challenges of bringing these complex organizational models to life, but many have made great

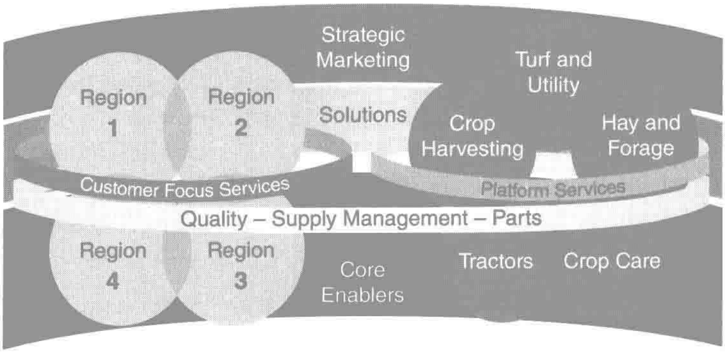

Figure 1.1 Deere's global operating model.

Source: Deere & Co.

progress. Studying these companies up close is productive. There are reasons some deliver superior results with these organizational arrangements while others seem to have real problems. This book will explore what factors yield success and provide a road map to effectiveness that any leadership team can follow.

> **GLOBAL OPERATING MODEL**
>
> An interdependent set of organization structures, processes, governance, metrics, and reward systems that tie together center-based business and functional teams and diverse geographic teams in order to execute complex strategies around the world.

WHY ORGANIZATION IS AS IMPORTANT AS STRATEGY

Profitable growth comes not from the articulated strategy, but a company's actual strategy, which is reflected in how the organization's resources are allocated. Outdated capabilities, structures, and decision-making processes get in the way of implementing good intentions and block attention for new sources of growth. In effect, the backward pull of structure, if left unattended, inhibits the very best laid strategic plans.

CEOs of large multinational companies can overcome the central challenge of designing for growth by building critical organizational capabilities that build the bridge from strategy to structure to performance. Such enterprisewide capabilities are difficult to build. They are cultivated by the intentional arrangement of structure, process, metrics, and talent. Organizational capabilities are a distinct source of competitive advantage that enable both the rapid execution of strategy and the envisioning of new strategic options.

Most of the truly critical capabilities that drive growth—innovation, brand building, digital marketing, and ecommerce—are formed at the intersections of business units, functions, and geographic markets as shown in Figure 1.2 below.

For example, after years of failed attempts to penetrate Asian and Latin American markets with its best-in-class agricultural equipment, Deere & Co. embraced the reality that retrofitting its American product lines (tractors, planters, harvesters, etc.) for emerging markets was not the solution for competing against tough local players that could bring low-cost equipment to farmers with good-enough levels of reliability. "Shifting the center of gravity" from Moline, Illinois to Pune, India helped bring a very different mindset to product development in emerging markets (Govindarajan and Trimble 2012). However, it would be years before Deere could overcome the immense regulatory barriers in China in order to provide cheap capital to small farmers who, instead, chose to buy low-cost Chinese tractors and planters. Meanwhile, Deere's investment in state-of-the-art paint

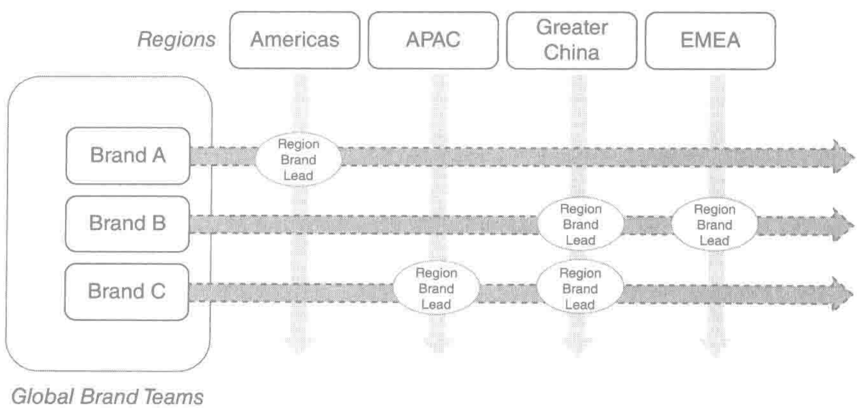

Figure 1.2 Growth comes at the intersection of global and local.

systems in China and its global rollout of sophisticated production process and engineering standards appeared to its critics as grossly overengineered for markets with price points that simply could not support those levels of process innovation. Deere's new global operating model, implemented in 2009, is intended to more nimbly manage the tensions among developed and developing markets across its five product platforms.

Or consider Nike, marketing a core brand across a number of consumer categories with hundreds of footwear and apparel products all over the world. The voice of the global soccer consumer has made its way into Nike's day-to-day decision making, and with record-setting results. But the seasonal marketing story line for the *swoosh* has to work for basketball, running, fitness, and other consumer categories too, so the global soccer team has to line up behind a bigger marketing idea. That's only the beginning of the creative conflict. South Africa might want to go one way on footwear design profiles and color palettes while the Netherlands, South Korea, and Brazil have other ideas. And apparel, footwear, and accessories have to fit together as an integrated collection for the footballer in all of those markets.

To ignore any of these competing voices diminishes the potential of Nike's powerful blend of brand, design, and market reach. It must be agile, but it must leverage its design prowess and its considerable cost structure. Nike executives cannot afford to keep things simple and make the wrong compromises. Nike's top team is very deliberate about how to work the complexity and the tension across the matrix in their organization to competitive advantage.

Both of these examples illustrate how sophisticated management of the connections and conversations across product lines, markets, and functions are needed to drive growth strategies.

AGILITY VERSUS LEVERAGE

The global operating model, with its multiple dimensions, embodies the promise of the matrix organization—that a company can have it all: robust global products and brands, local market responsiveness, and cost-effective functional processes and systems. The reality is that many senior executives in companies trying to execute global strategy are frustrated by the challenges of meeting *any* of these objectives.

Mike Canning, CEO of Duke Corporate Education, observes: "In the past, many organizations moved to a matrix to better position themselves for opportunities and customer solutions; decades later, they are still trying to figure out why it isn't working. CEOs discuss how their companies have 'perfected the art of working in silos.' Leaders point out that collaboration across business units remains challenging because people are not properly incentivized and no single business unit will bear the burden of investing in collaboration" (Canning 2015).

Efforts to get closer to the customer through stronger regionally based commercial organizations do not necessarily lead to greater customer focus. In fact, strong regional autonomy can slow the movement of brand-building ideas across regions and lead to duplication of programs, addition of redundant resources, and shadow functions springing up in distant corners of the business. Smaller, autonomous business units also slow the movement of talent and other resources to new growth targets, trapping resources in slower-growth priorities (Sull, Homkes, and Sull 2015). Then, when the central groups attempt to exert control, decision making often grinds to a crawl and leaders can feel they are living in a house of mirrors.

Underlying these difficulties are two opposing objectives continuously in play in the global operating model: agility and leverage. *Agility* delivers speed and flexibility—the ability to anticipate and respond to opportunities quickly. *Leverage* is the advantage conferred by size—influence with suppliers and distributors, the ability to invest in technology, systems, and talent with less overall cost than what the operating units could accomplish on their own. All too often the more a company tries to realize the benefits of leverage by imposing common ways of work from the center, the slower and less agile that decision making out in the markets tends to become. But it doesn't have to be this way.

Smart leaders move toward a balance in decision authority between the global and local elements of their organizations as shown in Figure 1.3. PepsiCo's CEO, Indra Nooyi, is skillfully realigning decision authority for brand building and product creation away from decades of local business management to more center-led, cross-regional, and cross-category decision making. In contrast, executives of companies that have long operated with heavyweight global business units, like Royal Philips, are rebuilding skills, capability,

Figure 1.3 Balancing power in the matrix is rarely a once-and-done task.

and governing authority back into regional markets, especially in developing countries. Strong market leader positions have been added to 11 of Philips' critical growth markets. The market leader roles work across the 20 or so business units, at the local level, to maximize the company's influence with regulatory agencies, suppliers, sources of talent, and distribution-channel partners. Instead of trying to sell globally standardized products around the world, Philips develops locally relevant offerings. As an example, shaving products are designed to fit the specific facial hair needs of different regions. "We are not shipping the same devices worldwide; our products reflect the specific needs of each market," says Jeroen Tas, top executive of Philips Healthcare Informatics Solutions and Services. But Philips CEO Frans van Houten makes the case for balancing this agility with leverage. "I cannot allow hundreds of product managers to go their own way. It is unrewarded complexity when everybody invents their own process, as it hampers cross-learning and efficiency" (Mocker et al. 2014).

Managers tend to associate agility with small, focused, and highly autonomous local units that can move quickly. This is certainly true from the local perspective. But, many local profit and loss (P&L) units

Table 1.1 Two different kinds of agility.

When Decentralized Business Units Add Agility	When Being More Center-Led Adds Agility (Enterprise)
• Local business units adapt the offering to local tastes and preferences • Product innovation can move quickly in focused business units • Business units know their competitors and can react quickly to challenges	• Top executives make hard, objective choices about getting in and out of businesses • Resources and talent can be shifted across business lines and initiatives quickly • Technologies and information can move across segments • Companywide view of innovation opportunities leads to bigger ideas

actually limit agility at the enterprise level. The company is less able to flexibly use resources and shift focus to new growth spaces (Sull 2009). Consider Apple's very large, functional organization model with its single P&L at the top. Apple has proven to be a far more agile organization than Microsoft, with its entrenched product division structure, in terms of ability to anticipate and respond to the arrival of cloud-based computing and smartphones as an Internet platform. Apple's organization also ensures that the consumer experience is the same across all products and applications. At the same time, Apple achieves remarkable degrees of leverage with its scale and the outsized popularity of its centrally led brand. Table 1.1 summarizes the different types of agility that can be achieved.

THE CHALLENGE OF ACTIVATION

There are only so many ways to design enterprise structure. The gravitational pull to greater complexity, and all the challenges that come with it, is powered by the need for new sources of growth in diverse geographic markets across multiproduct divisions with increasingly demanding customers and consumers with lots of technology at their fingertips (Galbraith 2009). After working closely with over 25 large

US and European-based global companies during the past seven years, we have concluded the problem is not in the fundamental design of these operating models. The challenge is ineffective and incomplete *activation*. Despite large-scale, well-funded change initiatives, sophisticated communication programs, and countless worldwide leadership summits, the hard work of bringing these complex organization designs to life often lacks focus or is not sustained over the three or more years that it typically takes to fully embed new ways of working.

As we look across the companies we have studied and worked with, we see a common set of symptoms that indicate incomplete activation:

- Excess layers and duplicated work make the organization slow and internally focused. Over time mid- to large-cap companies tend to build in layers of organization. Overreliance on structure and hierarchy to coordinate and control work not only adds cost, but also makes organizations slow and internally focused. Collaboration (both internal and external) is easier with fewer organizational levels, where each level plays a unique and value-adding role. While hierarchy is likely to continue to play a role in future organization models, it must be simplified, and more emphasis placed on horizontal connections.

- Global product teams and functions are overlaid onto the existing regional (commercial) organizations without adjustments in legacy P&L structures, creating unproductive friction. Companies do not become more global just because they have added worldwide product and brand teams, or global functions and councils, to manage centrally driven growth strategies and programs. Rather, companies become truly global when they have carefully orchestrated relationships among global, regional, and local teams with strong, interactive partnerships. The business targets and processes they comanage, and the nature of talent that staff these new roles, are all part of bringing global organization to life. Many companies eager to implement a new organizational structure simply do not have the wisdom, patience, and discipline to change the larger system. Too often, new initiatives and P&L structures are layered in without redesign of the larger whole.

- Power dynamics remain unresolved across global business units, regional teams, and functional units. Power for purpose should define how decisions will be made in the connections between global businesses, global functions, and regional or local businesses. The design of a global operating model is not complete until these decision-making ground rules and forums are defined, and too many executive teams leave this guidance to chance or to the political forces that unfold among strong personalities in the company. Having said that, some companies believe decision rights can be simply spelled out in detail with RACI (Responsibility, Accountability, Consult, Inform) charts and the like. This is also a fallacy.

- Global functions are designed to do yesterday's work, often independently from the needs of the business (and businesses have low expectations for functions). No one knows for sure where the future of management is headed, but it's clear that management teams must adapt to new ways of working, enabled by continuous waves of technology. The work of support and operating functions like finance, marketing, supply chain, and human resources must change to leverage these technologies, and do so in a way that serves enterprise objectives as well as the needs of individual businesses.

- Leaders do not know how and are not motivated to work in a matrix—metrics and reward systems continue to reinforce lack of enterprise thinking. Uncertainty is unnerving for most of us. Big organizations have been designed to eliminate uncertainty, and generations of leaders have been trained to allocate resources where assets are certain to produce the greatest return. "Silo thinking" is a rational response to the definition of success. But leaders who succeed in the global operating model demonstrate high degrees of learning agility, challenge existing business models, and colead growth strategies with partners in other parts of the world. They have grown up moving through jobs that take them across regions, cultures, functions, and business models. As importantly, the metrics and reward systems in the company make it clear that this kind of collaboration is expected.

- The corporate executive committee continues to act as a group of individual leaders, each focused entirely on their own business versus the needs of the enterprise. The top executive teams in successful global companies spend time together, sharing the enterprise leadership role. When the sole focus of top leaders is on their own business results, the message is clear to those who look up to them, and subtle or not-so-subtle forms of internal competition prevail. This is an often-ignored element in activating the new organization.

In short, it's one thing to design global business units, regional operating units, and worldwide functions; it's quite another to figure out how to get them to interact effectively to serve consumers and customers profitably.

If you are with a fast-growing, successful company and you have read this far, you may be feeling that this book doesn't apply to you. Or maybe you are wondering how these concepts apply to the technology industry. Haven't the likes of Google shown that culture trumps organization? How do these learnings from mature, and sometimes sclerotic, companies apply to the twenty-first century organization? Why are we talking about layers and processes and power dynamics—isn't hierarchy going to be replaced with holocracy? We would point out that nearly all companies have a phase where high growth, a strong founding culture, and robust revenues or profits make worrying about organization design a rather esoteric concern. This phase can last years or decades. However, leaders easily become imprisoned by their past successes (Govindarajan and Trimble 2012). The "dominant logic"—which forms the very culture that led to past success and which is deeply held and shared across the organization and implanted in the minds of leaders, their relationships, and the way they plan, organize work, make decisions, and evaluate and reward people—becomes a barrier. One only has to look at the airline, car, publishing, media, or telecommunications industries to find plenty of examples of previously successful companies caught flat-footed when disruptive competitors came on the scene with new business models.

This book is for leaders of companies that need to activate a new global operating model in response to external change as well as those who are looking for insight into how to design the global organization to create the most value and unlock growth and performance that will win in the marketplace. It is also for forward-looking leaders of companies that are on a high-growth trajectory, but want to avoid being surprised to find themselves one day unprepared when a new formula for success is required.

OUR RESEARCH

Throughout the book we will draw upon our organization design and activation work with 25 global, matrixed companies across industries as well as some nonprofits. The companies range in size from about \$3 billion to \$65 billion. We also tap into research on other companies, utilizing the work of other writers and public accounts in the media.