How CEO's Think

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John Roberts is a professor of Economics, Strategic Management and International Business at the Graduate School of Business at Stanford University. In 2004, he published a book, *The Modern Firm: Organizational Design for Performance and Growth* (Oxford University Press). *The Economist* promptly declared the book the best business book of the year. This is the kind of book that a smart CEO would read and I decided to read it just to remain informed on what *The Economist* and smart CEOs considered sage business advice. I was especially drawn to it by the subtitle, suggesting the book would provide insight into organizational design for performance and growth.

Roberts opens his book with the line - "The most fundamental responsibilities of general managers are setting strategy and designing the organization to implement it." That sentence resonated with me, since I strongly agree. Roberts went on to say that - 1) he was going to talk about the value of economics related to the study of strategy, and 2) this was not a "how to" book, but a book offering "ways to think about the problems of designing organizations for performance and growth." The author continued to lay his groundwork by mentioning that there are two bases for the book - first, "the proposition that general managers must be organizational designers" and second, "the idea that economics has much to say about the problem of organization." He goes on to say that the latter owes much to Michael Porter. Since I consider Michael Porter to be the father of modern Business Process Management theory, I settled in for an interesting read.

Roberts' book is well-written and it flows smoothly. No one interested in management could fail to learn from it. In the tradition of management books, it cites lots of examples of firms that have done things that worked, with occasional asides on inspiring leaders and interesting research.

Overall, however, I was disappointed. A quick check of the index shows that processes are only mentioned once. Activities are mentioned in the text, but not in the index. There are no references to today's process technologies like Lean, Six Sigma, or SCOR. It turns out that "organizational design," for Roberts, refers to arranging functional units. This is so important to Roberts that he includes a chapter on motivation that focuses on setting incentives for the people heading the functional units. A typical example is: "Organizational architecture can also be used to affect motivation. For example, creating small business units can have strong effects via a number of different mechanisms. First, it facilitates measuring performance more precisely and so supports giving stronger incentives."

When I first read this book, I decided not to review it. It simply doesn't talk about the issues that business process people are interested in. On reflection, I decided I should write about my response to the book, not to criticize it, but to remind everyone in the world of process just how far we have to go to have any significant impact on the way most firms are managed. This is a prize winning book, by a well-respected business management theorist, that was well received in the market place. This is the kind of book that the CEO of your company might very well read and it will reinforce how your CEO probably already thinks about the terms "organizational design," and "performance."

Those of us working in process management have our work cut out for us. We need to affect nothing less than a revolution in the thinking of senior managers. We have to convince them to reread Porter and understand his thinking at a deeper level. In *Competitive Advantage*, published in 1985, and in subsequent articles, including his wonderful HBR article on "What is Strategy?" published in Nov-Dec of

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1996, Porter argues for the key importance of the value chain and the integration of activities into a value chain. Specifically, he says:

- "Competitive advantage grows out of the entire system of activities. The fit among activities substantially reduces cost or increases differentiation."
- "Achieving fit is difficult because it requires the integration of decisions and actions across many independent subunits."
- "Positions built on systems of activities are far more sustainable than those built on individual activities."

The spirit behind Porter's approach, and the ideas advocated by Roberts, are as different as night and day. Porter argues that executives need to understand their value chains and work to assure that all of the activities in the value chain are integrated around a strategy designed to achieve performance that will assure sustained market leadership. Roberts, on the other hand, thinks something similar can be achieved by organizing the functional units and motivating the heads of the functional units. At one point, he admits that the incentives will make each functional manager try to maximize the success of his or her unit's performance, but he fails to follow up by considering what such silo-thinking might do to the overall performance of the organization.

The past two years have provided a number of examples of executives who focused on managing by structuring the organizational chart and motivating department heads. If costs aren't down and profits up in six months, the CEO shuffles the department heads and plays with the incentives. If things aren't improved in another 3-6 months the organization is subjected to another "reorganization." And, of course, each time the CEO rearranges the department heads, those people, in turn, rearrange their reports, guaranteeing that most managers spend the next 3-6 months settling into their new jobs and figuring out their new responsibilities. I assume that if the CEO is eventually fired, he or she will think that the failure resulted from not finding the right people, or from not structuring the business units in the right way, or from not finding the right motivational levers. It, presumably, will not occur to him or her that the company's core processes weren't properly organized, weren't integrated across functional units and weren't responsive to customers. In other words, it won't occur to him or her that simply changing the functional department structure and shuffling department heads will never change the underlying problems with the value chain.

My assumption, and the assumption of Michael Porter, and, I think, pretty much everyone else who is really process-oriented, is that you only optimize organizational performance when you focus on the value chain (or processes) and concentrate on how work gets done in the organization. If strategy doesn't ultimately result in "systems of activities" that are better integrated and more efficient than your competition, you won't achieve sustainable results.

This isn't being taught in most management schools – or, if it is being taught, it is only a minor part of the curriculum. Most senior executives seem to prefer to focus on creating organizational charts to describe how managerial authority is to be delegated – and on motivating their business unit and department heads. I honestly don't know how they decide what goals to set for their department heads.

Figure 1 suggests two ways of organizing strategic goals. On the left, we have Strategic Themes, which Porter recommends as a way of communicating what activities should be accomplished to implement a given strategy. He suggests, for example, that if the executive team decides they want their firm to be the "best possible company at doing X," they should go ahead and define the core activities required of a company that is the "best possible X company." Porter calls this set of activities a strategic theme and argues that senior executives should develop a Strategic Theme to assure that everyone in the organization knows how to implement the corporate strategy. On the right side, we break productivity strategy and growth strategy into the traditional financial measures that the various Balanced Scorecard programs usually recommend.

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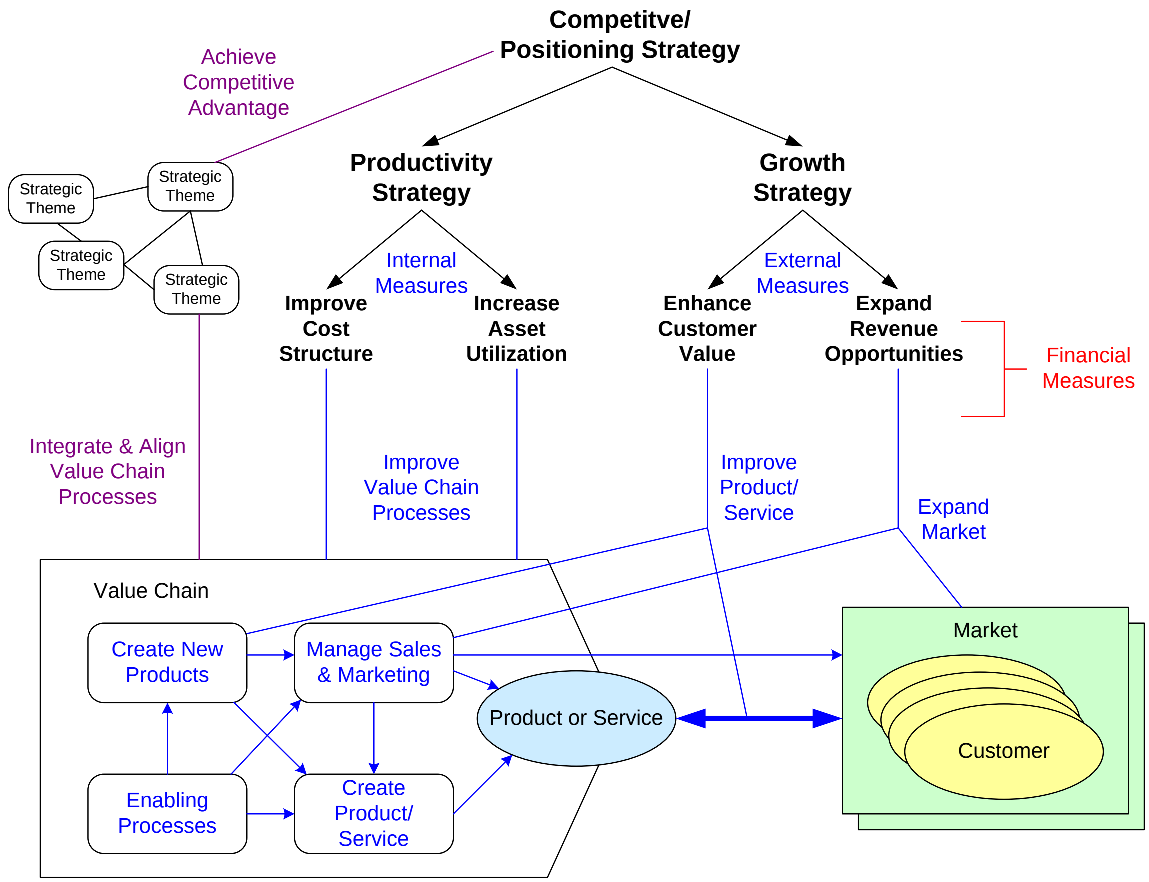

Figure 1. Implementing a Corporate Strategy.

It's relatively easy to see how the high level themes and the financial measures are tied to specific customer and process-level activities. Indeed, one can use the precise supply chain measures, recommended by the Supply Chain Council's SCOR methodology, to link each of the specific financial measures to specific processes in the supply chain. In other words, if I measure organizational performance by successful process performance, I know exactly how to relate specific actions of employees to successful organizational performance. Conversely, if there is a failure in organizational performance, I can trace back from the result to the process or activity that caused the failure.

If, on the other hand, I impose a functional structure and ignore the underlying value chain, I have to decide which department head is responsible for Customer Value or Cost Structure. What I end up doing is relying on the historical functional measures – units sold per quarter, or units manufactured per month - which may or may not add up to the corporate performance I'm after. It's hard to define these responsibilities precisely and its one of the reasons why there are turf wars among senior executives, and why, when something goes wrong, it is difficult to identify who or what is responsible. Each department head swears he or she did the job he or she was responsible for, but somehow the various departmental activities just didn't add up to a process that produced results that pleased the customers.

Most leading companies, today, have some kind of matrix organization. They have their traditional functional organization and, at the same time, they have some kind of process management structure. Many organizational problems result from trying to balance what is, in essence, a matrix management problem. Unfortunately, Roberts doesn't touch on matrix management.

As long as books like Robert's *The Modern Firm* remain the popular reading among smart executives, those of us who advocate a process-oriented approach to modern management are going to continue to struggle to sell these concepts to an audience that doesn't quite understand the value or the importance of these concepts. We have to work to initiate a revolution in how our CEO's think about organizational management. And, struggling to overcome the conventional wisdom is hard work.

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ABOUT PAUL HARMON

Paul is a Co-Founder, Executive Editor and Market Analyst at BPTrends, (Business Process Trends), the most trusted source of information and analysis on trends, directions and best practices in business process management, (www.bptrends.com). He is also a Co-Founder, Chief Methodologist and Principal Consultant of BPTrends Associates, a professional services company providing executive education, training and consulting services for organizations interested in understanding and implementing business process management. He has worked on major process improvement programs at Bank of America, Wells Fargo, Prudential and Citibank, to name a few.

Paul is the Co-Author and Editor of the *BPTrends Product Reports*, the most widely read reports available on BPM software products and the author of the best selling book, *Business Process Change*: *A Manager's Guide to Improving, Redesigning and Automating Processes.* He is an acknowledged BPM thought leader and noted consultant, educator, author and market analyst concerned with applying new technologies and methodologies to real-world business problems. He is a widely respected keynote speaker and has developed and delivered executive seminars, workshops, briefings and keynote addresses on all aspects of BPM to conferences and major organizations throughout the world. BPTrends Associates is partnered with Boston University to develop and deliver the BUCEC BPM Curriculum and Certification Program.

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