Redefining the Corporation

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In recent years, a great many corporations have been reshaping – or at least attempting to reshape – themselves, with varying degrees of success. In North America, at least, the 1980s could easily end up being called the Decade of Downsizing. Reasons for this trend include deregulation, volatile OPEC prices, and intensifying international competition. In addition, the emergence of junk bonds fueled a wave of mergers and acquisitions. Each industry had its own challenges to face.

Downsizing has not been limited to North America. Not long ago, Siemens announced that 9,000 jobs were going to be restructured or changed. In November 1989, a major British regional bank announced a 5,000-job cutback. Two weeks later, major banks in Denmark combined. Nor are Japanese firms immune to this phenomenon. It turns out that the much-vaunted guarantee of lifetime employment does not apply to a number of Japanese workers.

In this article we take a close look at the often unforeseen costs of downsizing and suggest a radically different approach.

The Costs of Downsizing

The main objective in most of the cutbacks of the 1980s was to reduce costs by lowering the number of employees. This very narrow focus had significant unintended consequences, including very high human costs. In North America, about 2.5 million white collar and managerial positions have been eliminated in the wave of cutbacks since 1979. Most of these professionals were good, loyal employees. There just wasn't work for them anymore. Furthermore, additional costs have been borne not by the people who lost their jobs, but by the survivors. More than one person has complained that the lucky ones were the ones who had an opportunity to leave – because downsizing took away half the people and left all the work in place. The consequent overloading of remaining staff certainly weakens morale.

Another problem has been loss of critical talent. Some early-retirement programs have been so generous as to be nearly irresistible. More than one company has had to go back to people who accepted its retirement offer and say, „What would it take to get you back on the job?“ For example, a European maker of high-quality consumer goods attempted to cut costs and prune a bloated payroll by offering an early-retirement window. As often happens, it was quickly oversubscribed – by the company's most senior craftsmen. The company was left with mid-level and junior people who were so unproductive relative to those who left that the company's net earnings were wiped out for the entire next year.

Disabled innovativeness is another cost. Often, cutbacks have been handled in a way that leaves the organization with a cadre of managers worrying about when the next shoe will drop. People who are fearful tend to hunker down and focus narrowly on their own jobs. Under these circumstances, employees hesitate to take risks or try new ideas. This mindset has crippled more than one large company's competitiveness. Furthermore, there is always the danger that you will cut muscle rather than fat, especially when you focus only on cost minimization through head-count reduction. This is really the most significant issue for businesses. Many companies have made very deep cuts, feeling that they were going to send a signal to Wall Street that their problems were behind them and they could move on. In a number of cases, however, their problems were not so much bloated head-counts as poor products, outdated technologies, or lack of responsiveness to competitors. For some chief executives, cutting costs and head-counts essentially gave them just enough rope to hang themselves.

Reshaping the Organization

The alternative to simply resizing is reshaping. Although most cutback efforts in the '80s were primarily the former, we are now seeing more and more clients focusing not so much on reducing head-counts as on streamlining their organizations. And that means starting not with the number of people, and not with the cost structure, but with the work. It means looking at what is important and what isn't. Where are things done? How are redundancies handled? What is the basis of organization, and how well does it fit management's strategies?

Companies that are reshaping need to focus considerable attention on the number of levels of management between the first-line supervisor and the head of the company. As Peter Drucker has said very well, each additional management layer cuts in half the possibility that information is correctly transmitted, and doubles the noise. Many of us have focused on reducing numbers of managers. The real organizational issue is how many layers of managers there are and how those layers distort information as it travels both up and down a hierarchy.

The objectives of reshaping efforts are broader than just resizing. Exhibit 1 represents a balance sheet of selected targets for this more planned approach to organizational change. For such efforts to prove successful, they need to work both on the efficiency side and on the effectiveness side. Certainly management must eliminate redundancies, but it must also make sure that the company has gone through a process that focuses the bulk of its payroll on its most strategically significant activities. And that means that the company has to take a careful look at the way its work is arrayed. Management has to make some priority decisions about that before making decisions about staffing levels.

Management needs to focus not just on cutting overhead, but on getting the most value from it. On the efficiency side, many jobs can be better leveraged – which means making sure that senior staff members are not spending too much of their time doing the work of junior staff members. But it is also important to look at job design, to make sure that people's responsibilities are broad enough to be motivating.

Exhibit 1

Results of Reshaping

More efficient

Eliminate redundancies

Cut overhead

Reduce fragmentation of effort

Create better-leveraged jobs

Lower cost of managing each dollar of payroll

More effective

Focus payroll on most critical activities

Focus overhead Pinpoint responsibilities

Spur motivation through broadened jobs

Minimize management layers

It is also useful to home in on certain key numbers – such as the cost of managing each dollar of work or payroll – and use those as targets to be reduced, along with layers of management. This latter idea – of flattening the management pyramid – has become very popular. Companies that do it end up with fewer managers, each of whom has a broader span of control – i.e., more „direct reports" and wider management responsibility.

The Role of the Middle Manager

Span of control tends not to be a problem at the bottom of organizations, where, in general, the amount of supervision needed is well matched to the workload. At the top, too, the span of control is often reasonably appropriate. But in the middles of many companies it's a terrible problem. In the middle, we see one-on-one management and even two- to three-on-one. However, flattening the pyramid needs to be more than a pencil-eraser exercise on a chart. You need to change the distribution of a manager's activities. You really need to rethink what the role of a middle manager is.

Exhibit 2 summarizes the actual allocation of time for many middle managers. Notably, such managers spend only 15 to 3 5 percent of their time on management activities. That may well explain why middle managers in large companies often have only one or a few subordinates. They're too busy doing the work of individual contributors or just passively relaying information. In effect, the company is composed of part-time managers and full-time workers. That pattern can lead to over-supervision, because too many managers are too close to the work of their subordinates. It can also – dangerously – mean that judgments on technology issues are made by people who simply cannot keep up with them. And it can certainly de-motivate the workers underneath. All these issues are in addition to the cost problems.

Therefore, if you want to make some changes in the number of management levels, you must really change the distribution of work. You have to analyze typical middle-management activities and find different homes for them in the organization. You may need to reexamine basic assumptions about the structure of the work done in the middle of companies. One pattern that is beginning to emerge effectively splits the typical middle manager's tasks into two jobs, each with one key function (Exhibit 3). One job might well be that of a full-time manager who has seven, eight, or as many as 20 people reporting to him or her. Managers of this kind are essential if you want to run an operation with relatively few levels of management.

Exhibit 2

Many Middle Managers Manage Only Part-time

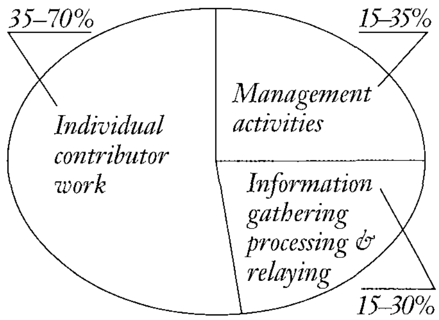
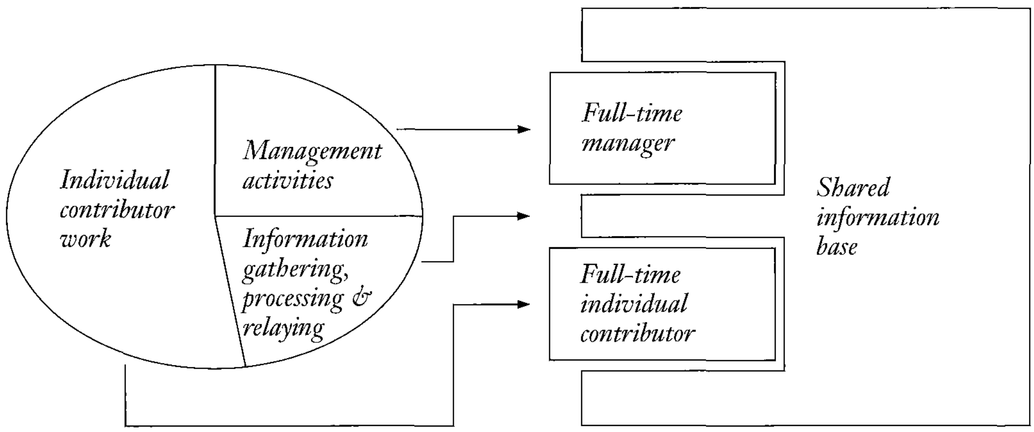


Exhibit 3

Design Jobs so That Managers Manage and Task Workers Add Value



However, the „individual contributor" portion of the work will not go away. As managers devote more time to managing, we need to find another place for it, in the role of full-time individual contributors. We are now just beginning to see companies creating some dual hierarchies that offer individual contributors a professional career track, so that they can rise in responsibility, pay, title, power, and influence without taking on management responsibilities.

This idea has functioned successfully for many years in R&D facilities. But it's too good an idea to be limited to the scientists and the engineers. We need to extend it into the rest of the organization.

Keeping Businesses Directed

The key to pulling together these very broad strands of control is replacing some of the hierarchy with systems that gather, process, and relay information. By using the information systems we have – but in a different fashion – we are able to imbed our management structure in what is now popularly known as an information-based organization. We will return to this theme later.

One common pitfall of reshaping the corporation is that, like dieting, it can produce only transitory improvements. In 1984, a company in the information services business was extremely proud that it had cut its headquarters staff from several thousand to 99 people. It was so proud of its „lean-and-mean" headquarters, in fact, that it bought two-page color ads in *Business Week* to pat itself on the back. Four years later, that headquarters staff numbered 500 and was still growing.

What happened? The question is worth looking into, because, unfortunately, we are seeing this pattern again and again in companies that have made very deep cutbacks. The issue was that the company had made the head-count change without really redefining the mission and the job of headquarters. In particular, management hadn't really examined what it needed to do to keep the company directed and under control.

Traditional tactics for keeping businesses directed include close supervision, which is no longer available in a flattened pyramid. Another traditional tactic is rule books, but who has time in this lean-and-mean era to read them, let alone write them? A third traditional approach has been to deploy small armies of staff policemen and auditors, but many of these positions have now been eliminated. For many companies, the net result of restructuring has been a vacuum – and in organizations, just as in the physical world, vacuums don't persist. Companies suffering from vacuums have two options: either they go back to some of the old ways of doing things, or they begin to adopt some new approaches to fulfilling the direction-and-control function.

One new approach involves rethinking the role of training and development programs. Management development programs are now being used in a much more focused way to address specific in-house needs. For example, when General Electric cut back many millions of dollars of corporate overhead, it increased its management development and training budget by a significant amount, realizing that it had to replace explicit controls with implicit ones.

Changes in pay systems are another tactic. Some companies are broadening eligibility for stock options and offering more focused bonus plans, not just for middle and upper management, but for all workers. We are seeing these changes adopted across many industries.

Perhaps most interesting are some approaches being taken to information systems technology. The impact of much information technology on organizations and on management work has been mixed. Companies have invested tremendous amounts in hardware and software. They have hired many analysts to look at the way things are done, capture these processes in computer code, and then entomb them in their large capital investment. This approach actually makes it harder, rather than simpler, to change business processes and improve them.

The result has been an effort to routinize work and to operate with a de-skilled work force. The management philosophy underlying this approach requires that employees follow a straight and narrow path. The essential attitude needed is one of compliance.

Other ways of using the same information technology are more effective in terms of exploiting its real potential. In these approaches, the objective is not merely to flatten the pyramid. For example, Peter Drucker is predicting that by the mid-1990s the typical large business will have half the levels of management of its counterpart today. Furthermore, it will be a knowledge-based organization composed of specialists who direct and discipline their own performance by means of organized feedback, delivered through information systems, from customers, colleagues, and superiors. This is what he defines as the information-based organization.

Life in the Information-Based Organization

An area of keen interest to Arthur D. Little is the actual implementation of such an organization. What would its organization chart look like? How would management work be re-thought and transformed? To answer these questions, it is helpful to take apart the organization chart (Exhibit 4). Groups of workers are going to be going off in different directions.

Redefining Workers and Managers. At the worker level, we expect to see fewer but more knowledgeable workers, with broader responsibility for monitoring the quality of their own performance. They will probably be paid on a different basis. There will be much more emphasis on flexibility and on trying to measure individual value added.

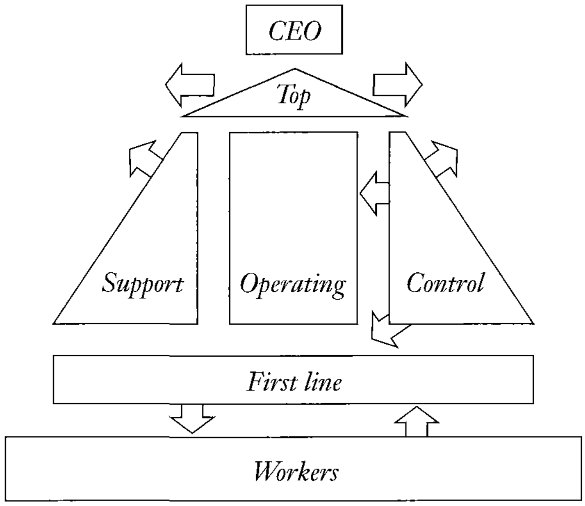
Because of these changes, the distinction between workers and managers is going to blur. Workers – assisted by technology – will assume much of the monitoring-and-measuring work that formerly belonged to middle managers, while many middle managers will move into essentially mid- or high-level positions as individual contributors. These people will all need to be wired together through systems that move information horizontally, not just up and down the hierarchy.

The role of the first-line manager – the traditional factory-floor work boss – is already disappearing in favor of other arrangements. Often, in companies that broaden their spans of control, the second line becomes the first. Other firms are paying a lot more attention to team management and giving team leaders narrowly defined responsibilities in terms of both coordination and work-flow management. In all these arrangements, information technology will tell workers what to be doing when. It will also replace much traditional order-giving and work-monitoring.

Union Carbide has had considerable success in these areas. Proctor & Gamble, too, is going to great lengths, whenever it can, to turn factory workers into salaried technicians and to minimize the amount of management above them.

Exhibit 4

Reshaping the Pyramid



Coordinating the Operating Core. But it is work that is done higher up in the pyramid – at the operating core of management – that has been the main target of much downsizing. This is where we are beginning to see some missing levels on organization charts, as companies broaden their spans of control. Here is the area of greatest need for horizontal infomation systems that will help managers coordinate their work areas with other divisions and functions.

Companies are now spending a lot of time creating interlocking teams and task forces in order to achieve coordination horizontally, rather than impose it from above. Managers of streamlined organizations no longer have the luxury of imposing coordination from above. These fundamental shifts in the organization raise a number of questions. Who should the middle managers of the future be? Should they be simply the survivors of all the downsizing and the early-retirement plans? In my view, they should go through a new selection – or reselection – process to make sure that their skills match their new and expanded responsibilities. Companies are already beginning to look hard at what it will take to be a middle manager in the redefined corporation.

Staff positions are likely to migrate in two directions, depending on whether the kind of staff work involved is control or support work. Control staff primarily keep the company moving along prescribed paths. They include strategy planners, quality engineers, environmental auditors, and financial controllers. Forward-looking companies are now moving many of these responsibilities up to a streamlined middle management core or down to workers. In addition, as companies recognize the principle that the person who sets the rules doesn't have to be the one who's constantly there to monitor them, a number of these activities are opening up to outside vendors.

Concentrating – or Offloading – Services. Support staff are primarily internal service providers – in effect, miniature businesses within companies. While they don't directly add a great deal of value to the end product or service, they tend to fulfill functions that are necessary. We are beginning to see a number of patterns in this area. One pattern is to pull these pieces of overhead out of the operating units and put them into one central operation, which is then managed like a business to make it much more customer-accountable. Many companies, through quality-assurance programs, are now moving in that direction.

An alternative approach, as exemplified in Europe by Unilever, is to sell off certain staff functions. Unilever needed distribution for its products, but distribution is not the basis of the firm's business. So Unilever sold its distribution function to the managers and then contracted it back from them.

Many other activities can be similarly offloaded. Bankers Trust decided that a number of support functions, such as telephone-answering, mail-handling, and employee orientation, might be done better by outsiders than by themselves. So the company contracted with Xerox Corporation to provide these services by hiring the employees in charge of them. Overnight, the Bankers Trust employees who had been doing these activities became (on a voluntary basis) Xerox employees. For Xerox, the arrangement provided a way to grow the company's business into some service areas, rather than primarily making hardware. Bankers Trust, although it didn't actually save money, enabled its middle management to concentrate on activities that directly served the company's customers.

That pattern is being repeated again and again. IBM employees run Kodak's Data Processing Center in Rochester, New York, and Digital Equipment employees operate parts of the telephone-switching operation. At IBM headquarters, Pitney Bowes employees deliver the mail. In a sense, everyone is getting into everyone else's pockets as companies home in on those areas where they can add the most value.

In some cases, a firm first concentrates its internal support activities, then gradually spins them off. They begin orienting these activities toward the marketplace by taking their budgets away and making them charge back for every single thing they do. The next step, after the activities have learned pricing and marketing, is to sell their services to outside customers. The final step is to spin them off and contract back their services. Bell Atlantic is proceeding along these lines.

Forging New Patterns at the Top. For the senior management team – with emphasis on the word „team" – the main change will be a much stronger sense of partnership. Senior management will do a lot more sharing of responsibilities, a lot more pulling together the functional parts of the company below the chief executive's office.

At the same time, new senior roles are being created – such as that of chief technologist – without direct operating responsibilities. These functions can represent the other peak of the dual-ladder system, for senior individual contributors.

Tearing Down Walls

The result of all these changes is a lowering of walls. One key wall that will come down is the one between line functions and staff functions. This may be done by moving some functions out; by rotating people across that wall, as Heineken has done over the years; or by doubling up these responsibilities.

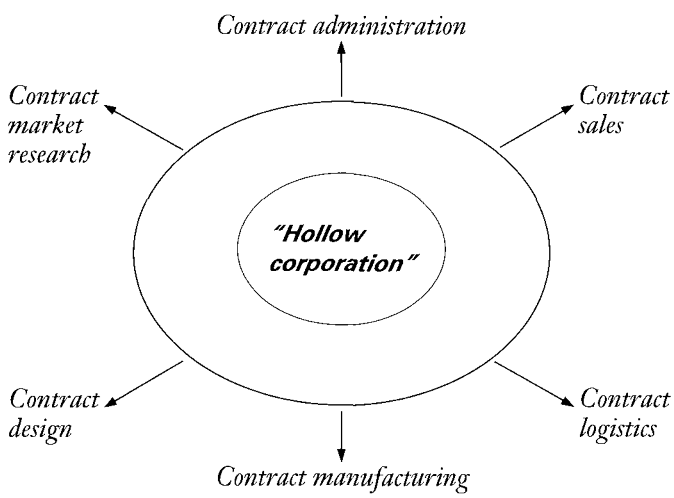
More significantly, walls will come down among divisions. Back in the early 1980s, everyone got excited about autonomous, self-sufficient strategic business units (SBUs). However, that system leads to tremendous duplication and redundancy. Today, we see the logic of doing much more sharing of resources across divisions. Negotiating is becoming a key skill for operating middle management.

Important though these changes are, the most significant wall that will come down is the one between the company and the outside. Firms will find themselves in all kinds of novel partnerships – with suppliers, with customers, and even with competitors (for a discussion of this theme, see Third Quarter 1990 *Prism).*

Where can these changes lead? One possible outcome – though we don't recommend it for most companies – is the organization chart in Exhibit 5. It's that of a toy manufacturer. Because this is a business in which sales can escalate very quickly and drop almost as fast, firms don't want to be committed to many fixed assets. Basically, this company found that it could contract out many of the functions that most companies take for granted. Market research? Buy it from Arthur D. Little. Contract toy design? The best toy designers seldom work for large corporations anyway. Manufacturing? That's done off-shore. Logistics? No one wants to own their own planes and ships. A sales force? Management found a number of good, effective manufacturers' reps. And many traditional administrative functions were contracted out as well.

Exhibit 5

Build Networks, Not Conglomerates



What is left is a small group of managers who function effectively as „switchboard managers.“ While they have a great deal of management responsibility, they have to learn to exercise control in very different ways. Again, I don’t offer this as a model for most companies, but it’s a useful way to stimulate people into seriously rethinking what they need internally and what they don’t.

Caveats for Management

Finally, a few words of caution for those who want to begin a process of redefining the basics of their organizations. One thing to avoid is quick fixes. Another is the feeling that if you have only resized, your problems are behind you. You should also avoid a very narrow focus on cost-cutting. That’s one objective, but it’s not the only one – and for long-term competitive advantage, it’s not necessarily the most important one. If you’re going to eliminate anything, eliminate work before eliminating people.

Avoid doing any of this in ways that destroy loyalty or morale. Pay a lot of attention to the ways that you can retrain and redeploy employees. And be sure to over-communicate what’s going on. Don’t just make a single announcement and then leave a long information vacuum.

Above all, avoid one-shot solutions. The changes outlined in this article are profound and far-reaching. Their implementation needs to advance on multiple fronts simultaneously: technology, compensation, careers, and the way management work is set up. Also, avoid back-sliding. It is essential to rethink – really from scratch – such basic questions as what do we expect of staff work? What do we expect of line work? And how do we really get the most positive advantage for our companies from information technology?

Robert M. Tomasko is a Washington, D.C. – based consultant to Arthur D. Little, who specializes in helping companies adapt organization structures and management practices to business strategies. He is the author of the book Downsizing *(AMACOM Books, 1987) and is writing a follow-up book about how the management job needs to change in streamlined companies.*