Organization Theory/Structure and Design
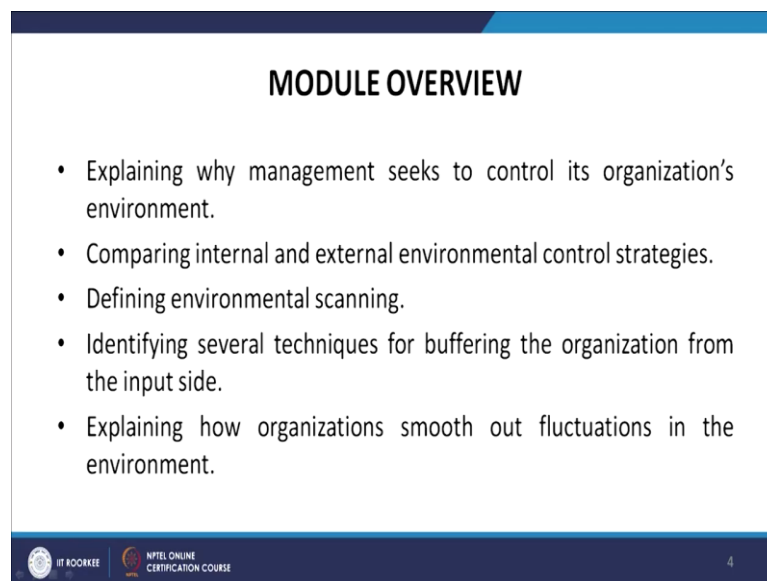**Prof. Zillur Rahman**
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Lecture - 31
Managing the Environment - I

Welcome to module 31 of this course Organization Theory Structure and Design. Now, as you can see in this slide that now, we are starting with the last part of this course that is part 4 in which we will be discussing about the contemporary issues in organization theory.

So, module 31 to module 40 covers the contemporary issues in organization theory and module 31 and 32 will be talking about how to go about managing the environment. So, now let us see what are the things, that we will cover in this module 31.
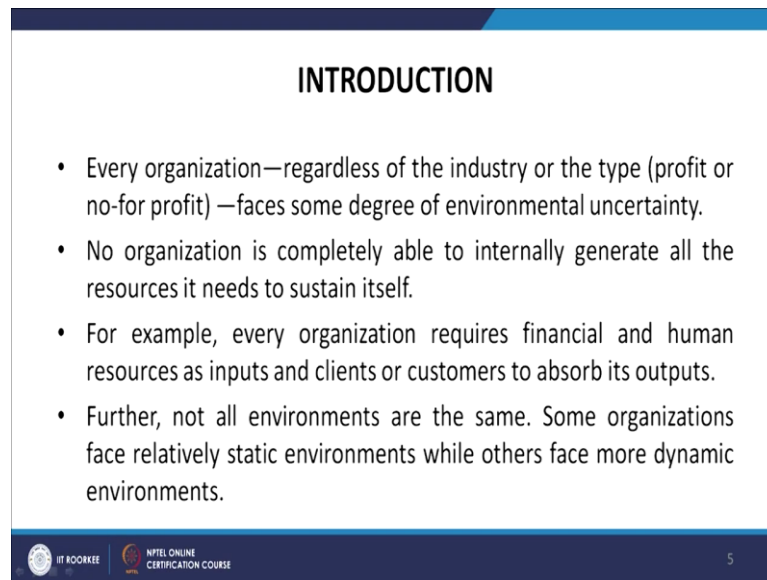
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So, we will start with explaining why management seeks to control its organization's environment. Comparing internal and external environmental control strategies. Defining environmental scanning. Identifying several techniques for buffering the organization from the input side and explaining how organizations smooth out fluctuations in the environment.
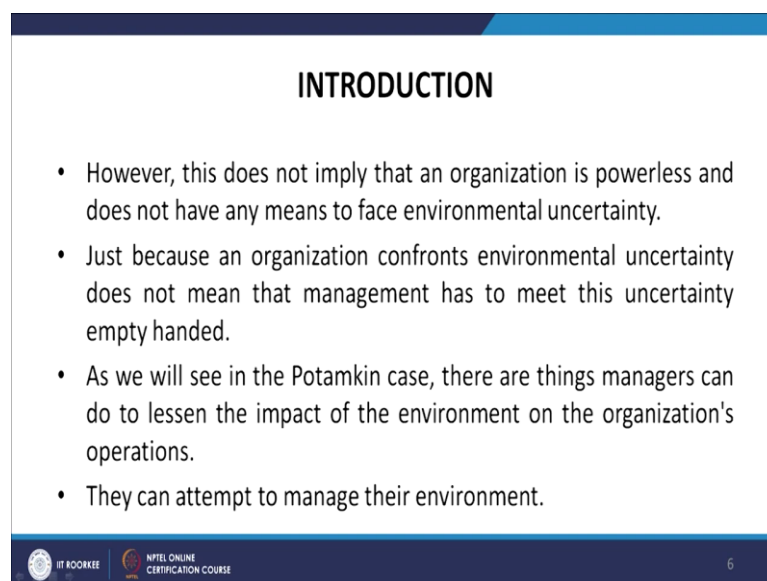
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So, to start with, every organization - regardless of the industry or the type - profit or not for profit - faces some degree of environmental uncertainty. No organization is completely able to internally generate all the resources it needs to sustain itself. For example, every organization requires financial and human resources as inputs and clients or customers to absorb its outputs. Further, not all environments are the same. Some organizations face relatively static environment while others face more dynamic environments.
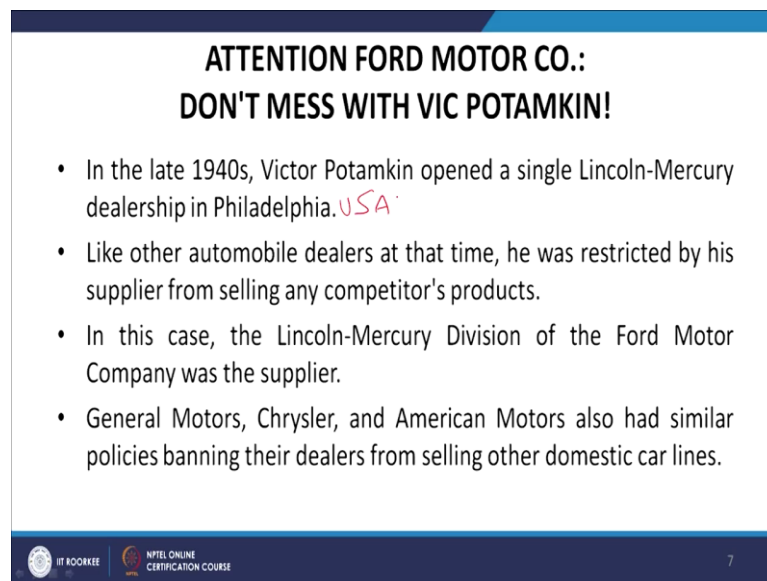
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However, this does not imply that an organization is powerless and does not have any means to face environmental uncertainty. Just because an organization confronts environmental uncertainty does not mean that management has to meet this uncertainty empty handed. As we will see in the Potamkin case, there are things managers can do to reduce the impact of the environment on the organization's operations. They can attempt to manage their environment.

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So, now let us give our attention to the Ford Motor company: Do not mess with Vic Potamkin. In the late 1940's, Potamkin opened a single Lincoln-Mercury dealership in Philadelphia that is in the US. Like other automobile dealers at that time, he was restricted by his suppliers from selling any competitor's products. In this case, the Lincoln-Mercury division of the Ford Motor company was the supplier.

General Motors, Chrysler and American Motors also had similar policies banning their dealers from selling other domestic car lines.

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This practice made dealer like Potamkin, totally dependent on their suppliers. For example, if you were a Chevrolet dealer and in any given year Chevrolet were poorly made, too expensive, or had an outdated design, there was nothing you could do about it. Moreover, the domestic manufacturers made dealers like Potamkin sign long-term contracts that governed the interaction and relationship between the manufacturer and the dealer.
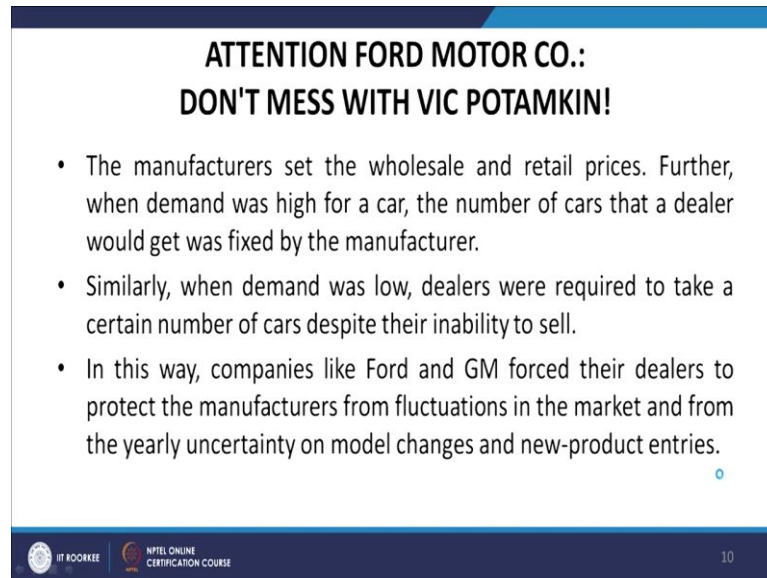
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These contracts were quite regressive and controlled pretty much every major decision of the dealer such as; 1st, the number and type of cars they were allowed to receive, the 2nd is the cars they had to receive, 3rd how much of the cost of failure they had to absorb under the warranty and how much they could charge for repairs and how much advertising they had to do. So, all these points were covered in the contract.

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The manufacturers set the wholesale and retail prices. Further, when demand was high for a car, the number of cars that a dealer would get was fixed by the manufacturer. Similarly, when demand was low, dealers were required to take a certain number of cars despite their inability to sell those cars. In this way, companies like Ford and GM forced their dealers to protect the manufacturers from fluctuations in the market and from the yearly uncertainty on model changes and new product entries.

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Things started to change in 1979. Auto sales in the United States started decreasing rapidly. Consequently, U.S. manufacturers were forced in the early 80's to ease their restrictions on dealers selling domestic competitors. At about the same time, consumers were discovering the higher quality in imported cars. To protect their sales volumes, many dealers of domestic brands added import franchises. Potamkin was one of these.
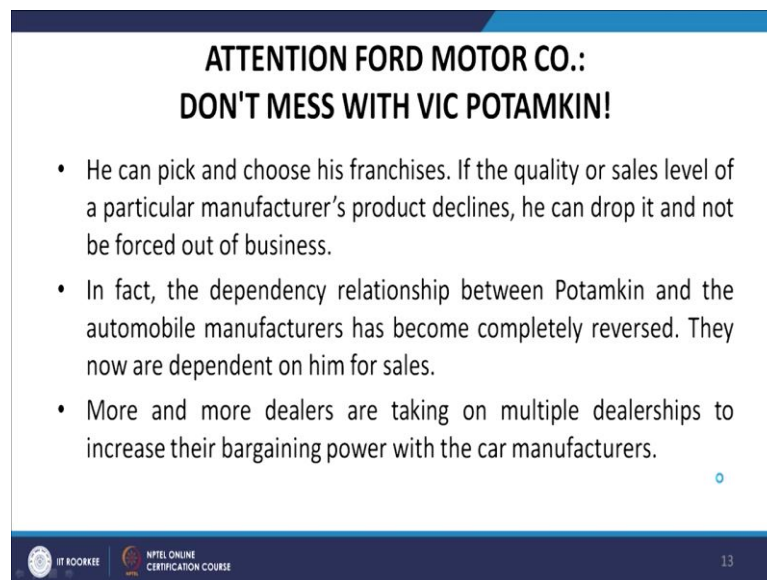
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He and his sons run a chain of auto dealerships that include all models made by Ford and Chrysler plus Cadillac, Chevrolet, Isuzu, Hyundai, Subaru, Toyota, Mitsubishi and

Volkswagen. Potamkin has become the largest automobile dealer in the United States, selling near 40,000 new cars and trucks every year and 26,000 used vehicles. One of the more interesting outcomes of Potamkins having become a super-dealer is that he is no longer beholden to a single automobile manufacturer.
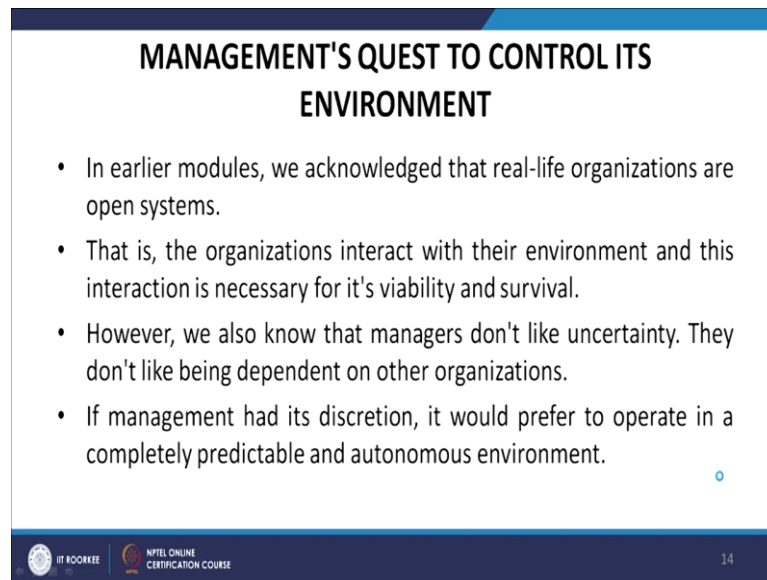
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He can pick and choose his franchises. If the quality or sales level of a particular manufacturer's product declines, he can drop it and not be forced out of business. In fact, the dependence relationship between Potamkin and the automobile manufacturer has become completely reversed. They now are dependent on him for sales. More and more dealers are taking on multiple dealerships to increase their bargaining power with the car manufacturers.

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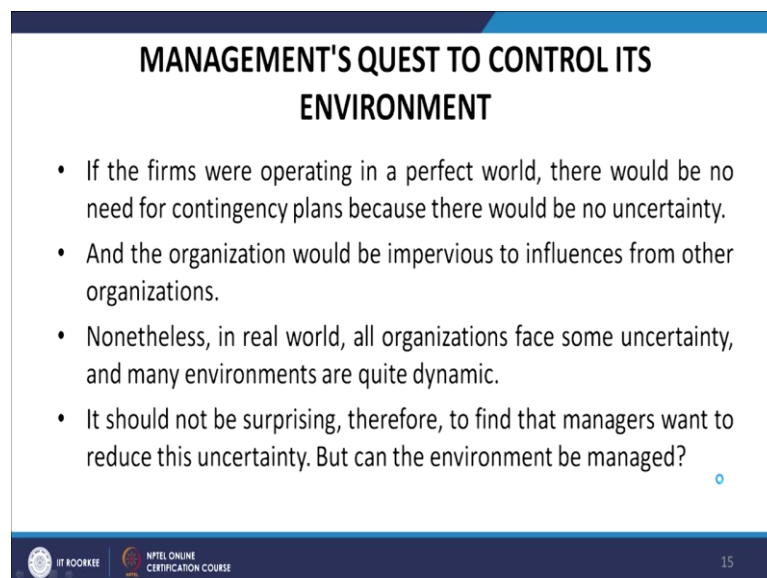Now, let us look at management's quest to control its environment. In earlier modules, we acknowledged that real-life organizations are open systems. That is, the organizations interact with their environment and this interaction is necessary for its viability and survival. However, we also know that managers do not like uncertainty.

They do not like being dependent on other organizations. If management had it is discretion, it would prefer to operate in a completely predictable and autonomous environment.
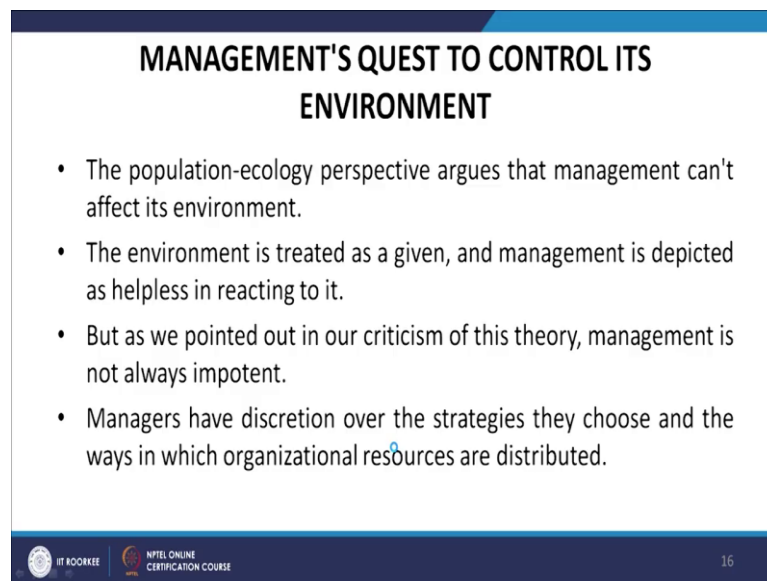
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If the firms were operating in a perfect world, there would be no need for contingency plans because there would be no uncertainty, and the organization would be impervious to influences from other organizations. Nevertheless, in real world, all organizations face some uncertainty, and many environments are quite dynamic. It should not be surprising, therefore, to find that managers want to reduce their uncertainty. But can the environment be managed? So, that is a big question.
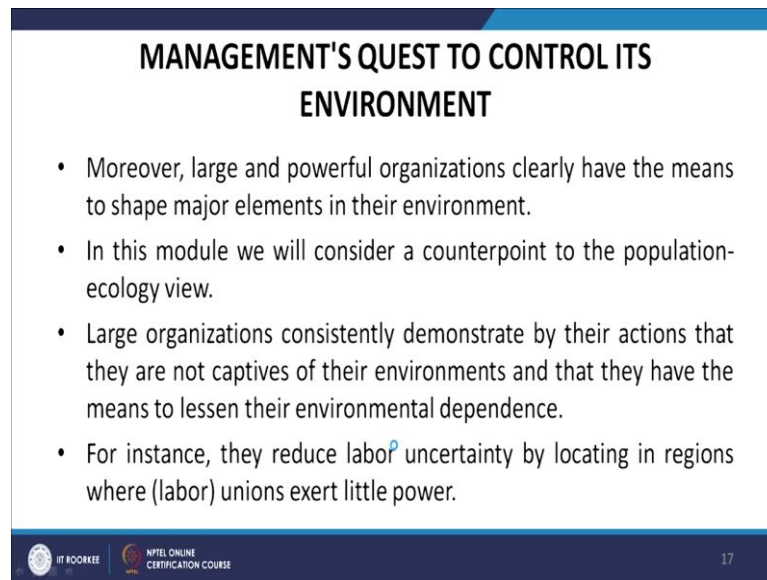
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The population-ecology perspective argues that management cannot affect its environment. The environment is treated as a given and management is depicted as helpless in reacting to it. But as we pointed out in our criticism of this theory, management is not always impotent. So, managers have discretion over the strategies they choose and the ways in which organizational resources are distributed.
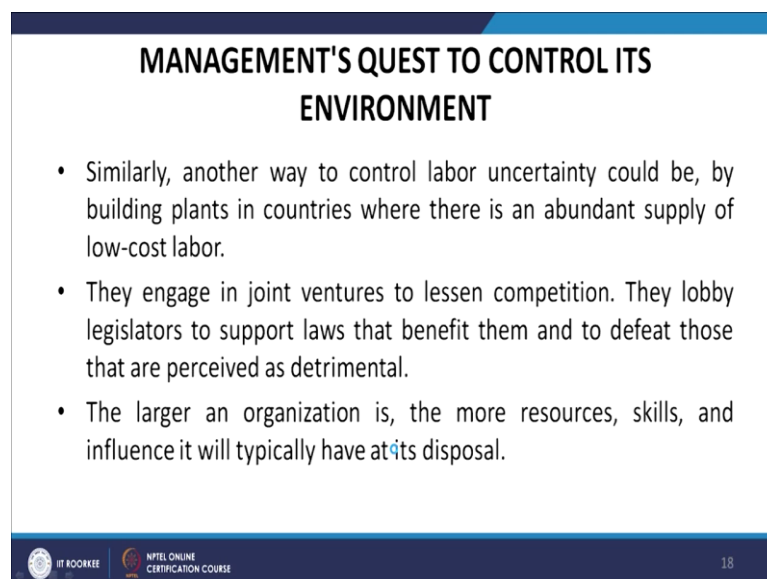
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Moreover, large and powerful organizations clearly have the means to shape major elements in their environment. In this module, we will consider a counterpoint to the population ecology view. Large organizations consistently demonstrate by their actions that they are not captives of their environments and that they have the means to lessen their environmental dependence. For instance, they reduce labor uncertainty by locating in regions where labor unions exert little power.
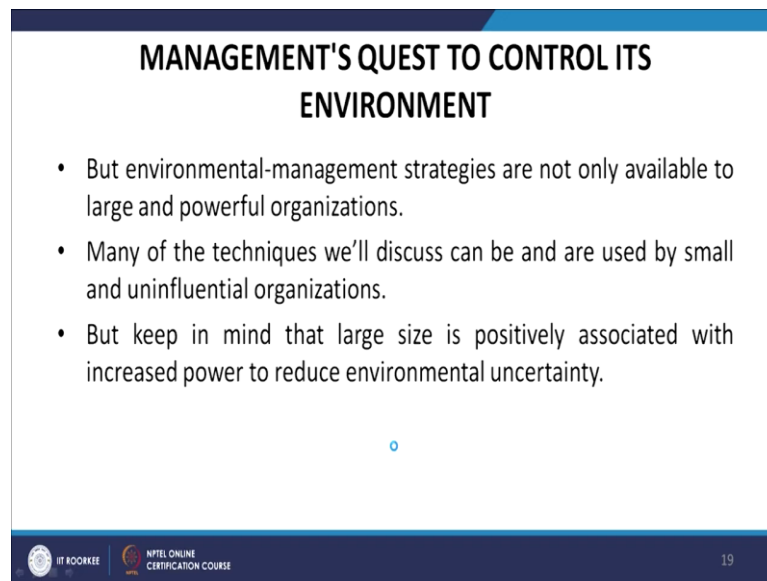
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Similarly, another way to control labor uncertainty could be, by building plants in countries where there is an abundant supply of low-cost labor. They engage in joint ventures to lessen competition. They lobby legislators to support laws that benefit them and to defeat those that are perceived as detrimental. The larger an organization is, the more resources, skills and influence, it will typically have at its disposal.
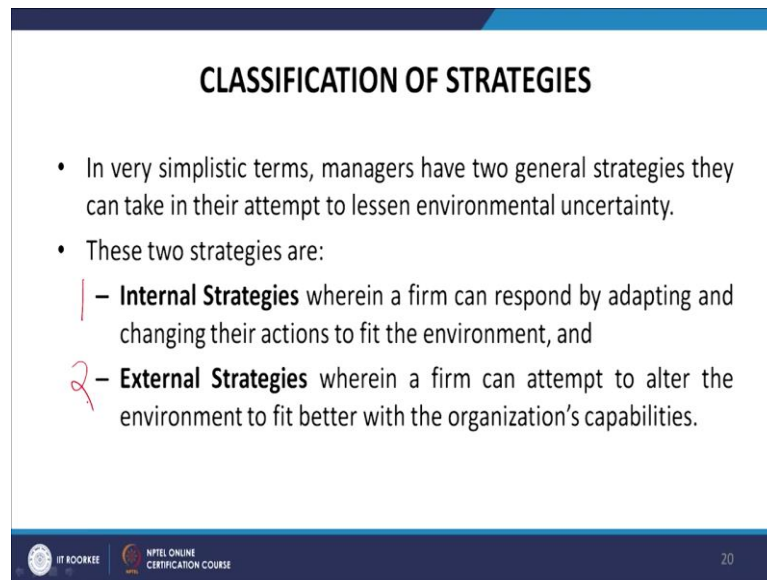
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But, environmental-management strategies are not only available to large and powerful organizations. Many of these techniques we will discuss, can be and are used by small and un-influential organizations. But keep in mind that large size is positively associated with increased power to reduce environmental uncertainty.
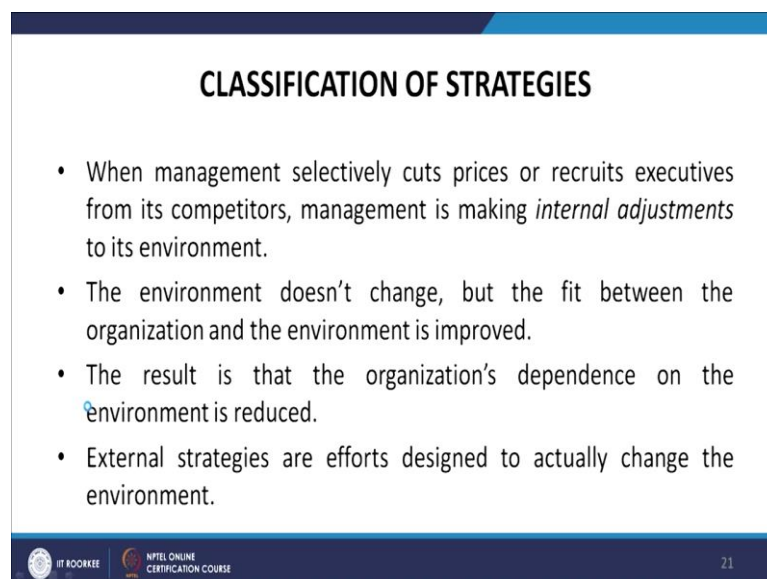
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Now, let us start with the classification of strategies. In very simplistic terms, managers have two general strategies they can take in their attempt to lessen environmental uncertainty and these two strategies are: 1st internal strategies wherein a firm can respond by adapting and changing their actions to fit the environment, and external strategies wherein a firm can attempt to alter the environment to fit better with the organization's capabilities.
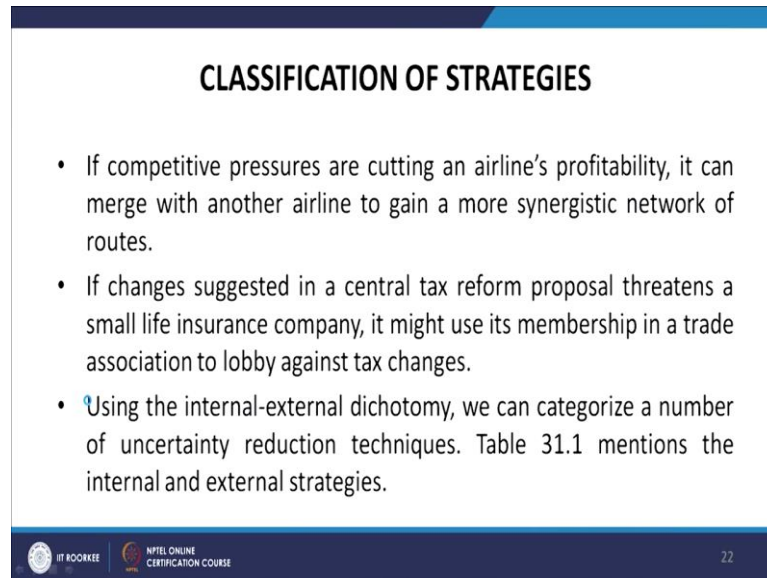
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When management selectively cuts prices or recruits executives from its competitors, management is making internal adjustments to its environment. The environment does not change, but the fit between the organization and the environment is improved. The result is that the organization's dependence on the environment is reduced. External strategies are efforts designed to actually change the environment.

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If competitive pressures are cutting an airline's profitability, it can merge with another airline to gain a more synergistic network of routes. If changes suggested in the central tax reform proposal threatens a small life insurance company, it might use its membership in a trade association to lobby against tax changes. Using the internal-external dichotomy, we can categorize a number of uncertainty reduction techniques. This table 31.1 mentions the internal and external strategies.

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So, this is table 31.1 that classifies the internal and external strategies. So, on the left-hand side, we have internal strategies and on the right-hand side, we have external strategies. So, internal strategies cover domain choice, recruitment, environmental scanning, buffering, smoothing, rationing and geographic dispersion. While external strategies include advertising, contracting, co-opting, coalescing and lobbying.
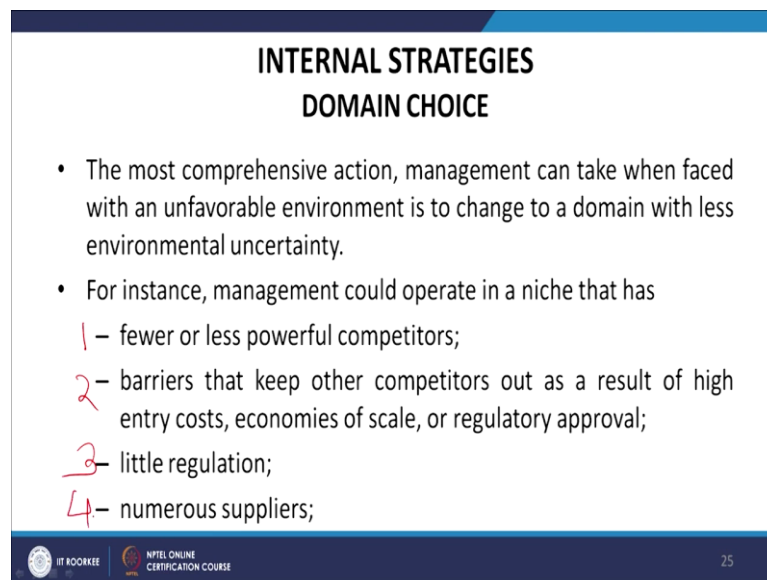
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So, we will look at each one of those strategies. Management does not actually have to change the environment in order to lessen the organization's dependence on it. The

following internal strategies demonstrate that there are actions that almost any organization, a small as well as large can take. These strategies help organizations to match better with its environment and in so doing, lessen the impact of the environment on the organization's operations.

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So, the first of those internal strategies is, domain choice. The most comprehensive action management can take when faced with an unfavorable environment is to change a domain with less environmental uncertainty. For instance, management could operate in a niche that has fewer or less powerful competitors, barriers that keep other competitors out as a result of high entry cost, economies of scale or regulatory approval, little regulation and numerous suppliers,

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no unions, less powerful public pressure groups and the like. Unfortunately, because there are not many opportunities for organizations to become unregulated monopolies, most domain choice decisions substitute one set of environmental uncertainties for another. If management cannot change to a more favorable domain, it might choose to broaden its strategy to take a generalist format.

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The more general an organization's objectives, structure and activities, the more is the availability of slack resources and the greater flexibility in responding to environmental

changes. Generalists, in contrast to specialists can exploit a number of segments of the environment. They do a lot of different things and employ individuals with greater versatility. This flexibility, of course, has some inherent costs. Generalists tend to be less efficient than specialists and if the environment is stable, the advantage goes to the specialists.

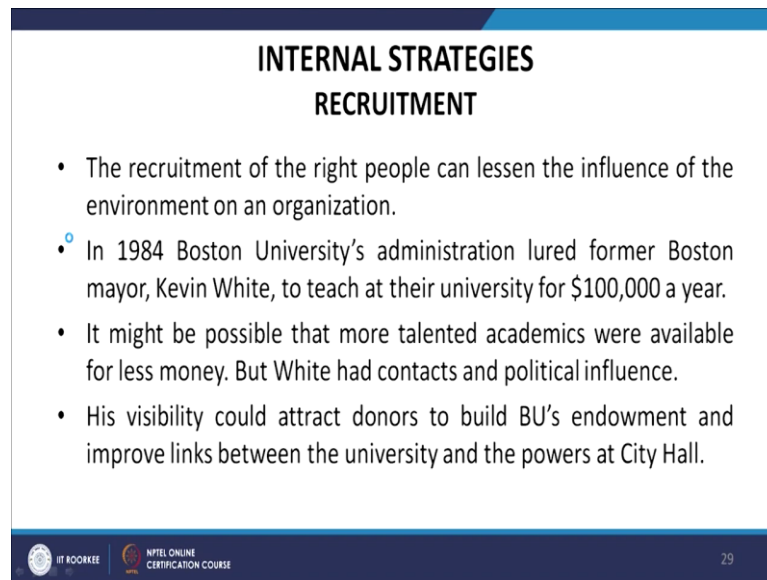(Refer Slide Time: 15:39)

Specialists have a minimal amount of slack resources, rely on more standardized technologies and achieve economies through high formalization. But when the environment is dynamic, the generalist's flexibility allows management to internally redirect resources to take advantage of opportunities in the environment.

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Another internal strategy is, recruitment. The recruitment of the right people can lessen the influence of the environment on an organization. In 1984, Boston University's administration lured former Boston mayor, Kevin White to teach at their university for dollar 100,000 a year.

It might be possible that more talented academicians were available for less money, but White had contacts and political influence. His visibility could attract donors to build Boston University's endowment and improve links between the university and the powers at the City Hall.

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The practice of selective hiring to reduce environmental uncertainty is widespread. Corporations hire executives from competing firms to acquire information about their competitor's future plans. High-tech firms entice scientists from competitive firms with large salary increases and stock options to gain the technical expertise held by their competitors. However, the greatest media attention is received by private organizations that recruit former government officials.
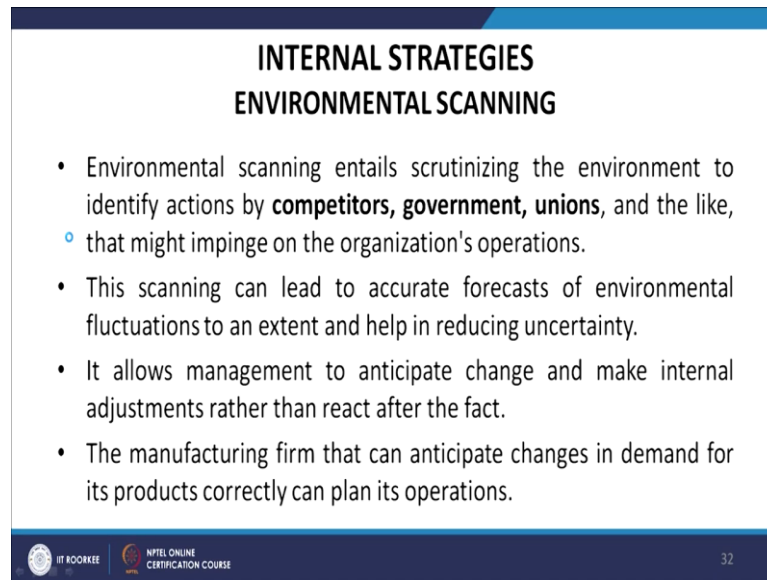
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Business and legal firms regularly hire such government officials, often offering exorbitant salaries. This is done with the intention to acquire their favorable ties with influential decision makers and knowledge of government operations.

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The third type of internal strategy is, environmental scanning. Environmental scanning entails scrutinizing the environment to identify actions by competitors, government and unions, and the like, that might impinge on the organization's operations. This scanning can lead to accurate forecasts of environmental fluctuations to an extent and help in reducing uncertainty.

It allows management to anticipate change and make internal adjustments rather than react after the fact. The manufacturing firms that can anticipate changes in demand for its product correctly can plan its operations.

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This help in scheduling operations of its technical core ahead of time and thereby minimize the impact of these changes. Similarly, the consulting firm that can forecast accurately which contracts it will win during the next six months is better prepared. It can plan for having the right numbers and mix of consultants available to handle these projects.

Environmental scanning is often done by boundary spanners. Boundary spanners function, in effect, as exchange agents between the organization and the environment.
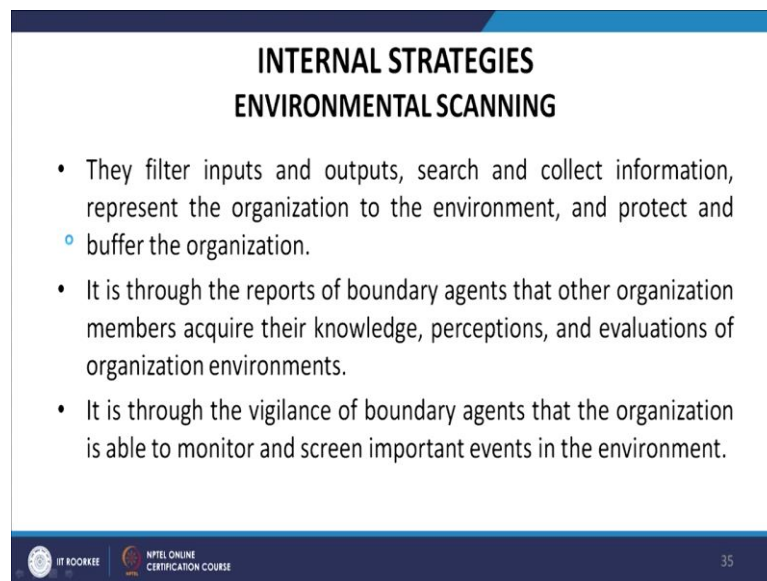
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Boundary spanners are persons who operate at the periphery or boundary of the organization, performing organizational relevant task and relating the organization to elements outside it. Example of typical boundary spanning jobs include, sales representatives, marketing researchers, purchasing agents, lobbyists, public relation specialists and personal recruiters. Boundary spanners perform a broad range of actions such as handling input acquisitions and disposal of output transactions.
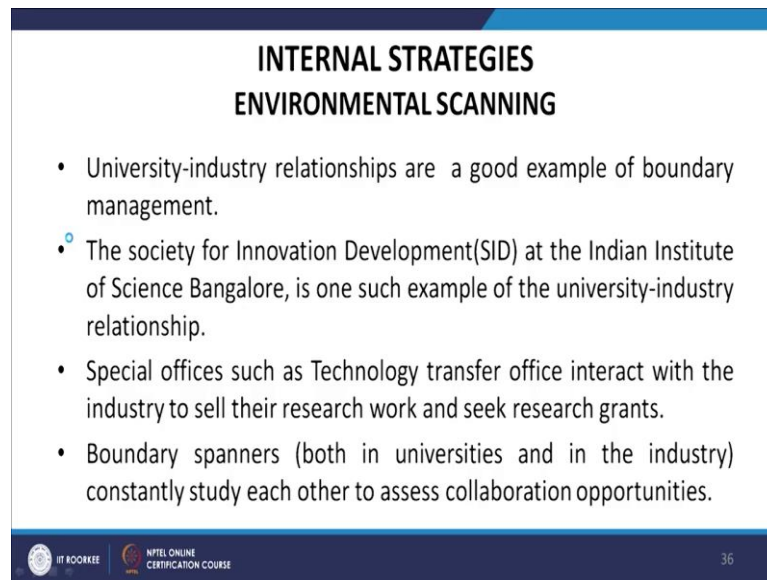
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They filter inputs and outputs, search and collect information, represent the organization to the environment and protect and buffer the organization. It is through the reports of boundary agents that other organization members acquire their knowledge, perceptions and evaluations of organization environments. It is through the vigilance of boundary agents that the organization is able to monitor and screen important events in the environment.

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University-industry relationships are good example of boundary management. The Society for Innovation Development at the Indian Institute of Science Bangalore is one such example of the university-industry relationship. Special offices such as technology transfer office interact with the industry to sell their research work and seek research grants. Boundary spanners, both in the universities and in the industry, constantly study each other to assess collaboration opportunities.

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Now, let us look at how Ballard's sales people effectively scan the environment. Ballard Medical Products is a small firm that makes products for the hospital-supply industry. Because the company has to compete against giants like American Hospital Supply and Johnson and Johnson, Ballard has developed a strategy to find and dominate small niches in its market. This requires identifying customer's needs, that others do not see and the ability to quickly turn customer needs into new-product innovations.

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Ballard has made its strategy work by using its sales representatives as boundary spanners. Ballard's sales representative's job, in addition to selling the company's current product line is to listen to customers and watch them at work. Ballard's representatives do not gather the information by written surveys or asking direct questions. Rather, they actually observe doctors, nurses and medical personnel using the company's products.

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They personally get to know their users, build friendships with them and then look and listen as they put the product to daily use.

Ballard has turned their sales representatives into effective boundary spanners and the company's principal intelligence-gathering mechanism. They go beyond merely meeting with hospital purchasing employees and go inside their customer's organizations. This information is then passed to company's headquarters where it is used to develop and modify its product line.
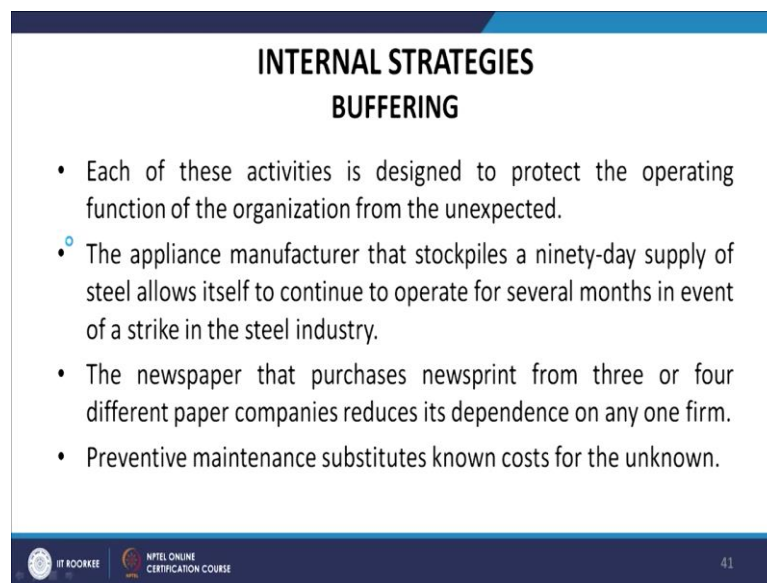
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The next, internal strategy is, buffering. Buffering reduces the possibility that the organization's operations will be disturbed by insuring supplies and or absorption of outputs. Management allows the organization to operate as if it were a closed system by buffering its operating core from environmental influences at the input or output side. On the input side, buffering is evident when organizations stockpile material and supplies, use multiple suppliers, engage in preventive maintenance and recruit and train new employees.
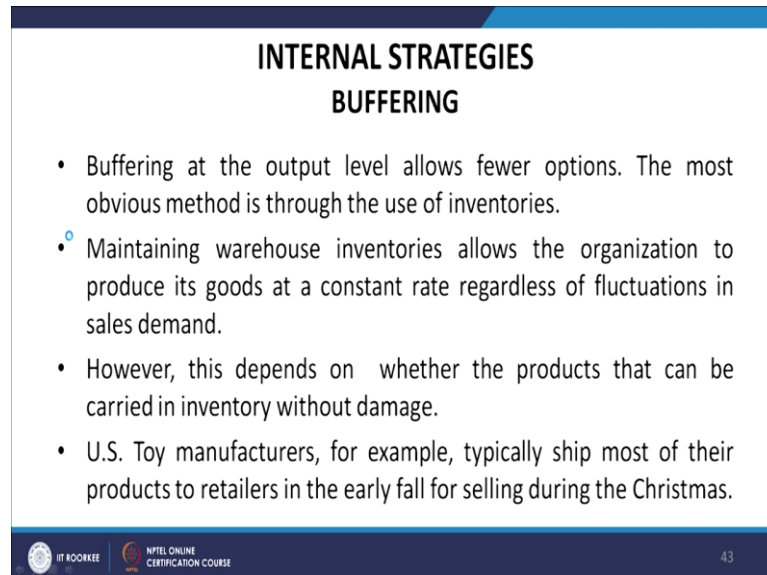
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Each of these activities is designed to protect the operating functions of the organization from the unexpected. The appliance manufacturer that stockpiles a ninety-day supply of a steel allows itself to continue to operate for several months in event of a strike in the steel industry.

The newspaper that purchases newsprint from three or four different paper companies reduces its dependence on any one firm. Preventive maintenance substitutes known costs for the unknown. Buffering in some sense is analogical to taking your car in every few months for a checkup and precautionary service to avoid the expenses of an unexpected breakdown.

In case of an organization, buffering can also be done with human resources. Since, the organizations require trained personnel, their unavailability or lack of appropriate skills

can mean a loss in productive efficiency. Management can meet this uncertainty through recruitment and training.

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Buffering at the output level allows fewer options. The most obvious method is through the use of inventories. Maintaining warehouse inventories allows the organization to produce its goods at a constant rate regardless of fluctuations in sales demand. However, this depends on whether the products that can be carried in inventory without damage. U.S. Toy manufacturers for example, typically ship most of their products to retailers in the early fall for selling during the Christmas.

These manufacturers of course, produce their toys year-round and merely stockpile them for shipping later in the year. Buffering provides benefits by reducing environmental uncertainties. We could predict management's propensity to buffer to be related directly to the degree of routinization in the organization's technology. However, the benefits must be appraised against the cost such as increased carrying expense of buffering activities and the risk of obsolescence inherent in stockpiling.

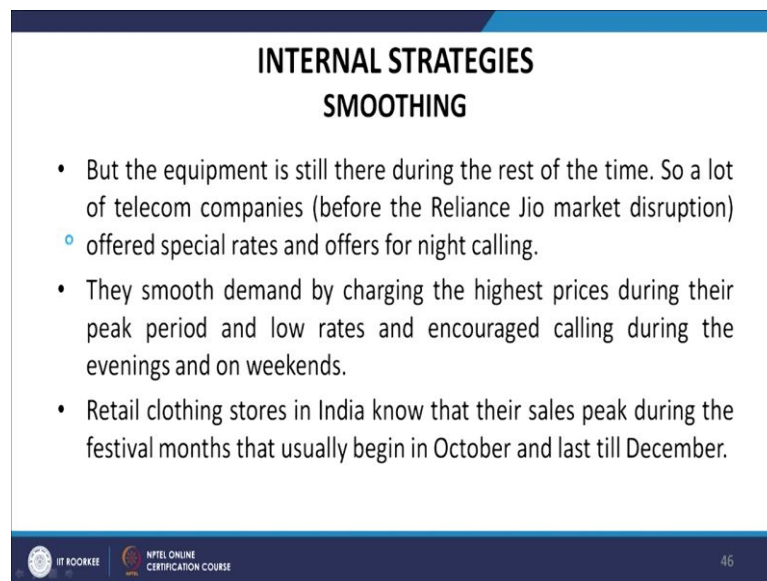Another internal strategy is, smoothing. Smoothing seeks to level out the impact of fluctuations in the environment. Organizations that use this technique operate in a wide range of industries and diverse categories such as telephone companies, retail stores, car rental agencies, magazines and sports teams. The heaviest demand for telecom company services is by business between the weekday working hours, that is, 9 to 5. Telephone companies have to have enough equipment to meet peak demand during this period
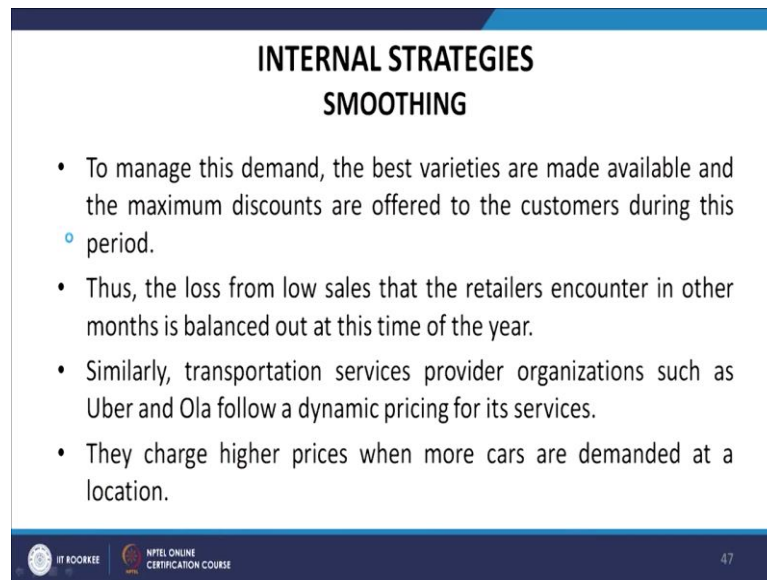
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But the equipment is still there during the rest of the time. So, a lot of telecom companies before, the Reliance Jio market disruption, offered special rates and offers for night calling. They smooth demand by charging the highest price during their peak periods and low rates and encouraged calling during the evenings and on the weekends. Retail clothing stores in India know that their sales peak during the festive months that usually begin in October and last till December.
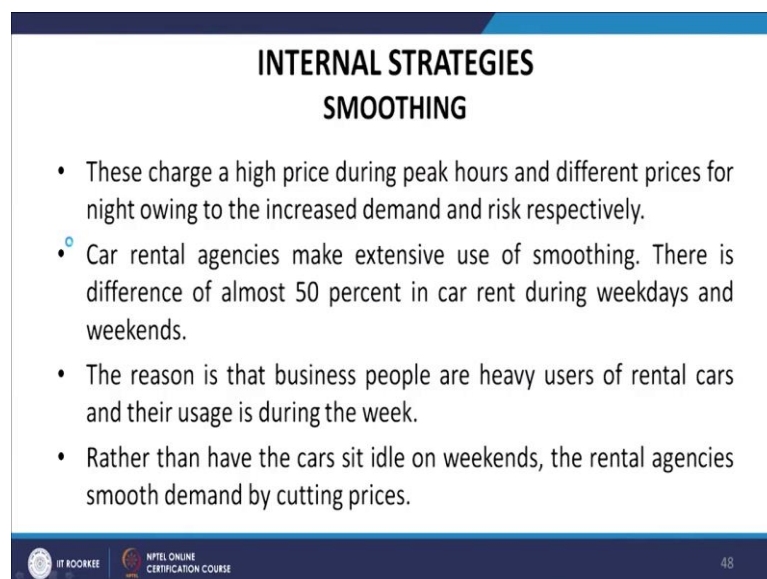
To manage this demand, the best varieties are made available, and the maximum discounts are offered to the customer during this period. Thus, the loss from low sales that the retailers encounter in other months is balanced out at this time of the year. Similarly, transportation services provider organizations such as Uber and Ola follow a dynamic pricing strategy for its services. They charge higher prices when more cars are demanded at a location.
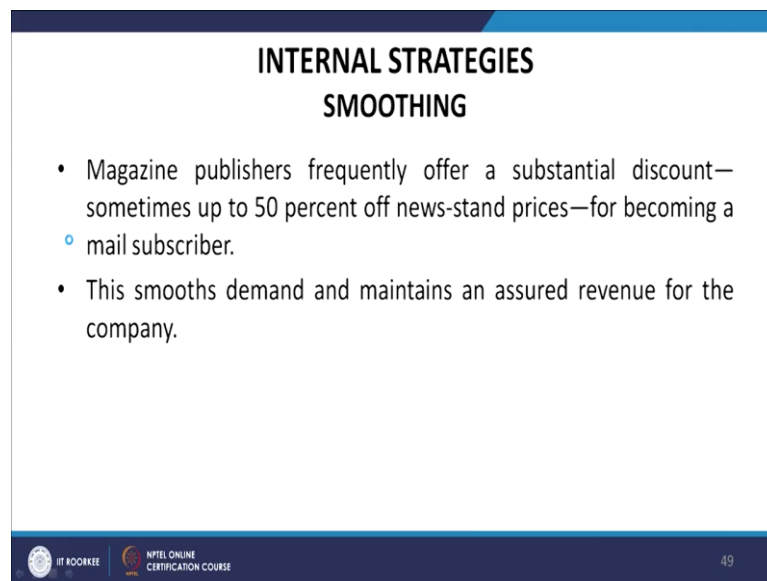
These charge a high price during peak hours and different prices for night owing to increased demand and risk respectively. Car rental agencies make extensive use of smoothing. There is a difference of almost 50 percent in car rent during weekdays and weekends. The reason is that business people are heavy users of rental cars and their usage is during the week. Rather than have the cars set idle on weekends, the rental agencies smooth demand by cutting prices.
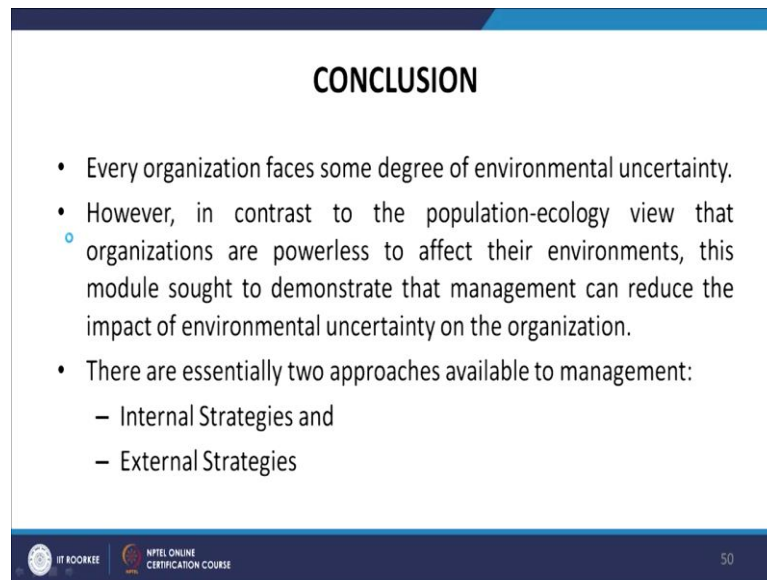
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Magazine publishers frequently offer a substantial discount sometimes up to 50 percent off news-stand prices - for becoming a mail subscriber. This smooths demand and maintains an assured revenue for the company.
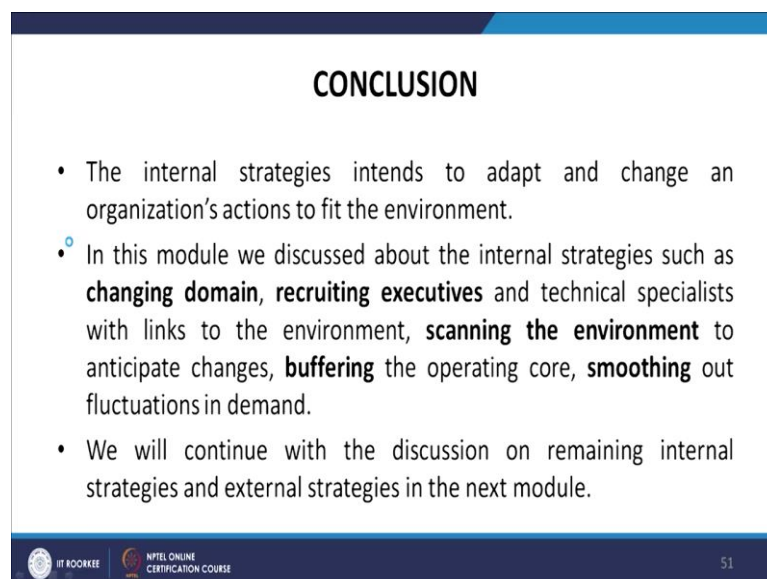
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So, to conclude this module, every organization faces some degree of environmental uncertainty. However, in contrast to the population-ecology view that organizations are powerless to affect their environments, this module sought to demonstrate that management can reduce the impact of environmental uncertainty on the organization. And there are essentially two approaches available to management: internal strategies and external strategies.

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The internal strategies intend to adapt and change an organization's action to fit the environment. In this module, we discussed about the internal strategies such as changing domain, recruiting executives and technical specialist with links to the environment, scanning the environment to anticipate change, buffering the operating core, smoothing out fluctuations in demand. We will continue with the discussion on remaining internal strategies and external strategies in the next module.

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These are the four books from which the material for this module was used.

Thank you.