Chapter 2

Organizational Environments and Cultures

LEARNING OBJECTIVES

After reading this chapter, you should be able to

1. discuss how changing environments affect organizations.
2. describe the four components of the general environment.
3. explain the five components of the specific environment.
4. describe the process that companies use to make sense of their changing environments.
5. explain how organizational cultures are created and how they can help companies be successful.

External Environments
Changing Environments
Environmental Change
Environmental Complexity and Munificence
Uncertainty

General Environment
Economy
Technological Component
Sociocultural Component
Political/Legal Component

Specific Environment
Customer Component
Competitor Component
Supplier Component
Industry Regulation Component
Advocacy Groups

Making Sense of Changing Environments

Internal Environments
Organizational Cultures: Creation, Success, and Change
Creation and Maintenance of Organizational Cultures
Successful Organizational Cultures
Changing Organizational Cultures

Environmental Scanning
Interpreting Environmental Factors
Acting on Threats and Opportunities
It’s the summer of 2000 and Tim Hortons seems to be on top of the world as it surveys its empire. A little donut shop set up 36 years earlier by a former hockey player and police officer, it is now one of the strongest franchises in Canada, with annual sales of $1.6 billion, 1700 outlets, and an aggressive expansion plan into the United States. In Canada, it is even predicted that in the next year or two that Tim Hortons will overtake McDonald’s in total annual sales. One in three cups of coffee sold in Canada comes from Tim Hortons, and Canada—a country with more donut shops per capita than any other country—seems to be a country in love with coffee and donuts. Canadian soldiers even take tins of Tim Hortons coffee with them on overseas deployment, and one of your competitors, Country Style Donuts, recognizes your dominance and sets its sights on becoming number two in the market—they are not even considering challenging your dominant position. Even the purchase of the company by U.S.-based Wendy’s International doesn’t seem to have slowed the company down or tainted its image as a Canadian icon. Even though you appear to be the undisputed coffee-and-donuts champion, and may even soon be the biggest fast-food franchise in Canada, you can see the storm clouds gathering on the horizon.1

Obesity levels are reaching unprecedented levels and the rates of diabetes are skyrocketing. Canadians, and North Americans in general, are becoming increasingly health conscious. Popular culture is even reflecting the changing landscape of the fast-food industry. In Super Size Me, filmmaker Morgan Spurlock decided to only eat McDonald’s food for a month, during which time he ate every item on the menu at least once and only super-sized items when asked. The results? Eating 5000 calories per day, Spurlock gained 25 pounds, increased his cholesterol from a healthy 160 to an unhealthy 230, and developed liver problems that later subsided after he lost weight.

With almost a quarter of Canadians obese, obesity is—no pun intended—at epic proportions, and that could affect Tim Hortons in terms of lawsuits, regulation, and complaints from public interest groups. For example, a group of obese U.S. teenagers sued McDonald’s, claiming its food had made them fat. While a judge threw the case out, any fast-food restaurant could be a target and the cost of defending the company could easily exceed several million dollars per case, and that’s only if you win. Other competitors have responded to the growing public health concerns. At Subway, a 6-inch roast beef sandwich with lettuce, tomatoes, onions, green peppers, pickles, olives, and fat-free honey mustard sauce is just 320 calories and 5 grams of fat. Also, Subway’s spokesperson, Jared Fogle, is famous for having lost 250 pounds (about 114 kg) by eating at Subway twice a day.

If the general interest in health-consciousness isn’t enough, along comes the Atkins diet. It’s so popular that food manufacturers are attempting to have their products “Atkins certified” in order to take advantage of the growing interest in the diet. A central feature of the Atkins diet is to significantly reduce a person’s intake of carbohydrates—and some fast-food restaurants have been experimenting with low-carbohydrate foods in response to the craze. The concern about fat and carbohydrates pretty much focuses on what a donut is—fat and carbohydrates. You know it’s only a matter of time before more of your competitors will respond to these trends, just as Subway has.

If the growing interest in eating health food wasn’t worrying enough, an aggressive new U.S. competitor is entering your market—Krispy Kreme. Although Krispy Kreme has only about a third of the sales (all U.S.) of Tim Hortons, its growth rate has been phenomenal. It has doubled its sales and stores over the last five years, including an incredible 40 percent increase in sales in the last year alone. Even Hollywood has jumped on the Krispy Kreme bandwagon, with Nicole Kidman declaring them “God’s gift to donut lovers,” and the product has been seen on over 80 TV shows. It now has plans to aggressively enter the Canadian market and take Tim Hortons head on. In the meantime, Tim Hortons’s U.S. expansion plans haven’t gone well, with the company losing millions of dollars. And now even McDonald’s seems to be entering the fray with a plan to open ten McCafés in Ontario.

Should Tim Hortons pay attention to what its customers traditionally want—donuts and coffee—and not healthy food? After all, the list of “healthy” fast-food items that have not sold well is very long: McDonald’s Lite Mac, McLean Deluxe, and McSalad Shakers; Wendy’s Light Menu; Burger King’s low-sodium pickles and veggie burger; and Taco Bell’s Border Lights. If you focus on your traditional line of food, how do you respond to the threat of Krispy Kreme?

If you were in charge of Tim Hortons, what would you do?
Even when you are a successful company, remaining successful is a very difficult task. Wherever you look, you see changes and forces beyond your control that threaten your ability to make your new business a success. This chapter examines the internal and external forces that affect companies.

External Environments

External environments are all the events outside a company that have the potential to influence or affect it. For example, Canada exported more than $10 billion worth of lumber to the United States in 2000. In mid-2002, after many years of threatening to place tariffs on Canadian exports, the United States imposed a 27 percent tariff on softwood lumber. This significantly affected producers in British Columbia, Quebec, Ontario, and Alberta, with exports from Quebec and Ontario falling by more than half. Canadian trade officials and industry groups appealed to the World Trade Organization (WTO) and under the North American Free Trade Agreement (NAFTA). In August 2005 Canada won a major NAFTA judgment, but the U.S. government ignored the ruling and appealed an unfavourable WTO ruling. In the meantime, the effect on some companies and communities has been devastating. Thousands of jobs have been lost, mills have closed, and the economies of entire towns have been ruined. In mid-2006, it appeared that the U.S. and Canadian governments had come to a resolution, but until the final agreement is signed, the industry will continue to struggle.

After reading the next four sections, you should be able to
1. discuss how changing environments affect organizations.
2. describe the four components of the general environment.
3. explain the five components of the specific environment.
4. describe the process that companies use to make sense of their changing environments.

CHANGING ENVIRONMENTS

Let’s examine the three basic characteristics of changing external environments: environmental change, environmental complexity and munificence, and uncertainty.

Environmental Change

Environmental change is the rate at which a company’s general and specific environments change. In stable environments, the rate of environmental change is slow. In dynamic environments, the rate of environmental change is fast. While it would seem that companies would either be in stable external environments or dynamic external environments, recent research suggests that companies often experience both stable and dynamic external environments. According to punctuated equilibrium theory, companies go through long, simple periods of stability (equilibrium), followed by short, complex periods of dynamic, fundamental change (revolutionary periods), finishing with a return to stability (new equilibrium).

One example of punctuated equilibrium theory is the Canadian airline industry. Twice in the last 30 years, the Canadian airline industry has experienced revolutionary periods. The first occurred with the advent of airline deregulation that began in 1978 in response to U.S. deregulation. Prior to deregulation, the industry was dominated by the “friendly duopoly” of CP Air and Air Canada that shared over 95 percent of the market, but the federal government controlled where airlines could fly, when they could fly, prices they could charge, and the number of flights they could have on a particular route. Although full deregulation was not seen in Canada until 1988, airlines had more choices to make and many competitors such as Wardair, which was primarily a charter airline,
and Pacific Western Airlines, a regional carrier, expanded and new air carriers were started. Competition among the airlines was fierce, and Pacific Western Airlines purchased several smaller airlines, including Wardair. In 1987 it purchased the much larger CP Air to form Canadian Airlines. Canadian Airlines was a truly national carrier, and although somewhat smaller than Air Canada, it was in a position to compete with Air Canada on an even basis. After experiencing substantially increased levels of competition, two companies again dominated the skies, Canadian Airlines and Air Canada, and a period of relative stability was seen. The dominance of these two carriers was first seriously challenged in 1996 with the emergence of WestJet Airlines, which started as a western-based airline. Canadian, too, was a western-based airline. Competition once again increased and a faltering Canadian Airlines was purchased by Air Canada in 2000, leaving only two national carriers, Air Canada and WestJet. Several smaller carriers tried to take advantage of the failure of Canadian Airlines, some of which have since gone bankrupt. Now Air Canada and WestJet dominate the Canadian skies and there appears to be no serious challengers on the horizon. These two periods of stability followed by revolution and regained stability illustrate punctuated equilibrium theory well.5

### Environmental Complexity and Munificence

**Environmental complexity** is the number of external factors in the environment that affect organizations. **Simple environments** have few environmental factors, whereas **complex environments** have many environmental factors. For example, the baking industry exists within a relatively simple external environment. Except for more efficient ovens (i.e., technology), bread is baked, wrapped, and delivered fresh to stores each day much as it always has been. Baking bread is a highly competitive, but simple business environment that has experienced few changes.

By contrast, in recent years, cereal companies such as Kellogg’s, maker of Kellogg’s Corn Flakes, Frosted Flakes, Sugar Pops, and other popular cereals, find themselves in a more complex environment in which three significant changes have occurred. The first significant change has been more competition. Twenty-five years ago, Kellogg’s competed against just a few cereal companies, such as General Mills and Post. Today, Kellogg’s competes against those companies, as well as private-label store brands (IGA, President’s Choice, Safeway, etc.).
The second important change in the cereal industry has been significant price cuts. For years, Kellogg’s made gross profits of 50 percent on a box of cereal. Yet, with profits that high, private-label store brands could still make a profit of $1 per box by slashing the price that consumers paid.

The third significant change has been the entrance of Wal-Mart into the grocery business. Wal-Mart often relies on cheaper private-label store brands, such as its own soft drinks, produced by Canada’s Cott Corporation, and Old Roy dog food. Consumers like these products because they cost substantially less than brand-name products. However, Wal-Mart prefers private-label store brands because, even with their lower prices, the store makes a higher profit on these brands. So when Wal-Mart aggressively expanded into the grocery business in the last few years, Kellogg’s saw its market share drop even more as Wal-Mart pushed cheaper private-label cereals. Together, these three changes have made Kellogg’s external environment much more complex than it used to be.6

**Environmental munificence** is the degree to which an organization’s external environment has an abundance or scarcity of critical organizational resources. For example, the primary reason that flat-screen, LCD (liquid crystal display) TVs with lifelike pictures are six times more expensive per inch than regular TVs, two times more expensive than rear projection TVs, and 25 percent more expensive than plasma TVs is that there aren’t enough LCD screen factories to meet demand. At $2 billion to $3 billion each, LCD factories are the scarce resource in this industry. Without more of them, LCD TV prices will remain high. LCD factories are complex and difficult to build because, like computer chips, LCD flat screens must be made in expensive, super-clean environments. Furthermore, the manufacturing process is complex and difficult to manage because the liquid crystal, which can be ruined by just one speck of dust, must be poured onto glass in a layer thinner than a piece of paper. Finally, even in current LCD factories, production is further restricted because most produce LCD glass panels that are only 43 inches by 49 inches (109 cm by 125 cm). These can be cut into one dozen 17-inch (43 cm) LCD screens for computer monitors, but just two 30-inch (76 cm) LCD screens for TVs. By contrast, only Sharp has a factory that can produce LCD glass panels that are 59 inches by 71 inches (150 cm by 180 cm). In comparison, these larger panels can be cut into as many as eight 32-inch (81 cm) LCD screens for TVs or six 37-inch (94 cm) screens for TVs.7 To address these shortages, LCD manufacturers plan to build 12 new factories in the next few years at a total cost of between $15 billion and $20 billion.

### Uncertainty

Exhibit 2.1 shows that environmental change, complexity, and resources (i.e., munificence) affect environmental uncertainty, which is how well managers can understand or predict the external changes and trends affecting their businesses. Starting at the left side of the figure, environmental uncertainty is lowest when there is little complexity and change, and resources are plentiful. In these environments, managers feel confident that they can understand and predict the external forces that affect their business. By contrast, the right side of the figure indicates that environmental uncertainty is highest when there is much complexity and change, and resources are scarce. In these environments, managers may not be at all confident that they can understand and predict the external forces affecting their businesses.

### Review 1: Changing Environments

Environmental change, complexity, and munificence are the basic components of external environments. Environmental change is the rate at which conditions or events affecting a business change. Environmental complexity is the number of external factors in an external environment. Environmental munificence is the scarcity or abundance of resources available in the external environment. The greater the rate of environmental change and environmental complexity and the lower the environmental munificence, the less confident managers are that they can understand and predict the trends affecting
their businesses. According to punctuated equilibrium theory, companies experience periods of stability followed by short periods of dynamic, fundamental change, followed by a return to periods of stability.

2 GENERAL ENVIRONMENT

Exhibit 2.2 shows the two kinds of external environments that influence organizations: the general environment and the specific environment. The **general environment** consists of the economy and the technological, sociocultural, and political/legal trends that indirectly affect all organizations. Changes in any sector of the general environment eventually affect most organizations. By contrast, each organization has a **specific environment** that is unique to that firm’s industry and directly affects the way it conducts day-to-day business. The specific environment, which will be discussed in detail in the next section of this chapter, includes customers, competitors, suppliers, industry regulation, and advocacy groups.

Let’s take a closer look at the four components of the general environment that indirectly affect all organizations: economy, technological component, sociocultural component, and political/legal component.

**Economy**

The current state of a country’s economy affects most organizations operating in it. A growing economy means that, in general, more people are working and therefore have relatively more money to spend. More products are being bought and sold than in a static or shrinking economy. While a growing economy doesn’t mean that sales of an individual firm are necessarily growing, it does provide an environment favourable to business growth.

For example, in 2005 Canada was in its 14th straight year of economic expansion. So, according to economic statistics, Canadian businesses exist in a relatively healthy, growing economy. In contrast, Japan, after having suffered from a decade of recession, could be finally turning an economic corner. Japanese companies such as Mazda Motors had been reporting regular, if not record, losses. Unemployment, while still low by Canadian standards, had been growing. Now there are signs of an economic turnaround.
but economists are still unsure as to whether the upturn is sustainable, especially given that the Japanese economy contracted in the last quarter of 2004.\(^9\)

Of course, by the time you read this, the Japanese economy could be enjoying healthy growth rather than struggling to recover, and the Canadian economy could be shrinking as the U.S. economy slows in the wake of Hurricane Katrina and takes its toll on the Canadian economy. Because the economy influences basic business decisions, such as whether to hire more employees, expand production, or take out loans to purchase equipment, managers scan their economic environments for signs of change. Unfortunately, the economic statistics that managers rely on when making these decisions are notoriously poor predictors of future economic activity. A manager who decides to hire ten more employees because economic data suggest future growth could very well have to lay those newly hired workers off when the economic growth does not occur. In fact, a famous economic study found that at the beginning of a business quarter (a period of only three months), even the most accurate economic forecasters could not accurately predict whether economic activity would grow or shrink in that same quarter!\(^{10}\)

Because economic statistics are such poor predictors, some managers try to predict future economic activity by keeping track of business and consumer confidence. Business confidence indices show how confident managers are about future business growth. For example, the Conference Board of Canada (www.conferenceboard.ca) quarterly asks CEOs of approximately 1000 Canadian businesses to express their optimism (or pessimism) about future business sales and prospects. They also survey Canadian consumers about their optimism about the Canadian economy. Managers often prefer business and consumer confidence indices to economic statistics, because they know that the level of confidence reported by real managers and consumers affects their purchasing decisions. In other words, it’s reasonable to expect managers and consumers to make...
decisions today that are in line with their expectations concerning the economy’s future. So if the Conference Board of Canada’s Index of Business Confidence or Index of Consumer Confidence suddenly drops, managers would think hard about hiring new employees or might stop plans to increase production for fear of being stuck with unsold inventory should the economy slow dramatically in the future.

**Technological Component**

**Technology** is the knowledge, tools, and techniques used to transform inputs (raw materials, information, etc.) into outputs (products and services). For example, the knowledge of authors, editors, and artists (technology) and the use of equipment such as computers and printing presses (also technology) transformed paper, ink, and glue (raw material inputs) into this book (the finished product).

Changes in technology can help companies provide better products or produce their products more efficiently. For example, advances in surgical techniques and imaging equipment have made open-heart surgery much faster and safer in recent years. While technological changes can benefit a business, they can also threaten it. For example, over the last few years, with sales of blank CDs up 40 percent, and more than 400 million songs downloaded for free at Kazaa.com alone (the largest music file swapping Web site), it’s no surprise that sales of music CDs have dropped 26 percent between 1999 and 2002. British college student Dave Watson says, “You’d be hard-pressed to find a group of students who’ve never downloaded music. You can’t stop them, as long as it’s free.” How extensive is this technological threat to the music industry? When a *Wired* magazine reporter logged on to Kazaa on a quiet Monday morning, he found at least a hundred copies of each song on the Billboard 100 and 13 of the 15 songs on Mariah Carey’s new CD, which hadn’t even been released to the public. Companies must embrace new technology and find effective ways to use it to improve products and services or decrease costs. If they don’t, they will lose out to those that do. Chapter 10, “Innovation and Change,” provides a more in-depth discussion of how technology affects a company’s competitive advantage.

**Sociocultural Component**

The sociocultural component of the general environment refers to the demographic characteristics and general behaviour, attitudes, and beliefs of people in a particular society. Sociocultural changes and trends influence organizations in two important ways.

First, changing demographic characteristics, such as the number of people with particular skills, or the growth or decline in particular population segments (single or married; old or young; men or women; or visible minorities, Aboriginals, or the disabled, etc.) affect how companies run their businesses. For example, women with children are much more likely to work outside the home today than 30 years ago. In 1976, only 39 percent of women with children under 16 years old and 28 percent of women with children under three years old worked outside the home. In 2003, those percentages had risen to 72 percent and 63 percent, respectively. Because of these changes, many more companies now offer...
child-care as a benefit to attract and retain scarce, talented workers of both genders. One example is Hydro One, formerly known as Ontario Hydro, which provides space and pays the occupancy costs for Hydro Kids, its on-site daycare.¹⁵

Second, sociocultural changes in behaviour, attitudes, and beliefs also affect the demand for a business's products and services. Today's harried worker/parent can hire baby-proofing agencies (to baby-proof their homes), emergency babysitting services, bill payers, birthday party planners, kiddie taxi services, personal assistants, and personal chefs.¹⁶ All of these services are a direct result of the need for free time, which is a result of the sociocultural changes associated with a much higher percentage of women in the workplace.

**Political/Legal Component**

The political/legal component of the general environment includes the legislation, regulation, and court decisions that govern and regulate business behaviour. Throughout the last decade, new legislation and regulations have placed additional responsibilities on companies. Unfortunately, many managers are unaware of these new responsibilities. For example, the Canadian Human Rights Act prohibits discrimination against those who are infected with HIV/AIDS. Discrimination against anyone with HIV/AIDS could result in the company having to pay damages and back pay.

Many managers are also unaware of the potential legal risks associated with traditional managerial decisions such as recruiting, hiring, and firing employees. Indeed, it is increasingly common for businesses and managers to be sued for negligent hiring and supervision, defamation, invasion of privacy, emotional distress, fraud, and misrepresentation during employee recruitment.¹⁷ Likewise, there were few wrongful dismissal cases (i.e., unfairly firing employees) in the past but, for example, it is estimated that about 10 percent of all trials scheduled in Calgary's Court of Queen's Bench involve allegations of wrongful dismissal, and court awards can exceed $100,000 and are increasing in size.¹⁸

Not everyone agrees that companies face severe legal risks. Indeed, many believe that government should do more to regulate and restrict business behaviour, and that it should be easier for average citizens to sue dishonest or negligent corporations. From a managerial perspective, the best medicine against legal risk is prevention. As a manager, it is your responsibility to educate yourself about the laws and regulations and potential lawsuits that could affect your business. Failure to do so may put you and your company at risk of sizable penalties, fines, or legal charges.

**Review 2: General Environment**

The general environment consists of economic, technological, sociocultural, and political/legal events and trends that affect all organizations. Because the economy influences basic business decisions, managers often use economic statistics and business confidence indices to predict future economic activity. Changes in technology, which is used to transform inputs into outputs, can be a benefit or a threat to a business. Sociocultural trends, such as changing demographic characteristics, affect how companies run their businesses. Similarly, sociocultural changes in behaviour, attitudes, and beliefs affect the demand for a business's products and services. Court decisions and revised federal and provincial laws have placed much larger political/legal responsibilities on companies. The best way to manage legal responsibilities is to educate managers and employees about laws and regulations and potential lawsuits that could affect a business.

**SPECIFIC ENVIRONMENT**

In contrast to general environments that indirectly influence organizations, changes in an organization's specific environment directly affect the way a company conducts its business. If customers decide to use another product, or a competitor cuts prices 10 percent, or a supplier can't deliver raw materials, or federal regulators specify that industry pollutants must be reduced, or environmental groups accuse your company of selling unsafe products, the impact on your business is immediate.
Let's examine how the different aspects of the specific environment affect businesses. These can be broken down into the customer component, competitor component, supplier component, industry regulation component, and advocacy groups.

**Customer Component**

Customers purchase products and services. Companies cannot exist without customer support. Therefore, monitoring customers’ changing wants and needs is critical to business success.

There are two basic strategies for monitoring customers: reactive and proactive. *Reactive customer monitoring* is identifying and addressing customer trends and problems after they occur. One reactive strategy is to identify customer concerns by listening closely to customer complaints. Not only does listening to complaints help identify problems, but the way in which companies respond to complaints indicates how closely they are attending to customer concerns. For example, companies that respond quickly to customers’ letters of complaint are viewed much more favourably than companies that are slow to respond or never respond. In particular, studies have shown that when a company’s follow-up letter thanks customers for writing, offers a sincere, specific response to the customer’s complaint (i.e., not a form letter, but an explanation of how the problem will be handled), and contains a small gift, coupons, or a refund to make up for the problem, customers will be much more likely to purchase products or services again from that company. For example, when Tim Hortons head office receives a customer complaint, a district manager immediately visits the franchise in question in order to respond to the customer by the end of the day. By contrast, companies that don’t respond promptly to customer complaints are likely to find customer rants and tirades posted publicly on places like www.planetfeedback.com (a Google search will reveal many more of these types of sites, some specifically targeting a single company). Customers hope that posting complaints on these sites will force someone to address their problems. It worked for Lena West. The day after she posted a complaint against Budget Rent-a-Car, she received an e-mail containing an apology and a promise to solve her problem.

*Proactive monitoring* of customers means trying to sense events, trends, and problems before they occur (or before customers complain). For example, over the next few years, more stores that sell toys will offer electronic gift cards—not gift certificates, but gift cards—that are preprogrammed with a dollar amount and are “swiped” like credit cards. With kids’ bedrooms stuffed full of every toy you can think of, savvy retailers have already noticed that parents and grandparents would rather give gift cards because they don’t have to worry about getting the wrong toy or a toy that the kids already have. Likewise, an example of proactive monitoring in the fast-food industry is multi-branding, where two or more food chains share space under the same roof. Multi-branding brings in more customers by giving them more choice. For example, Wendy’s and Tim Hortons are often located together in order to increase sales.

**Competitor Component**

*Competitors* are companies in the same industry that sell similar products or services to customers. GM, Ford, and DaimlerChrysler all compete for automobile customers. CBC, CTV, and Global compete for TV viewers’ attention. And Tim Hortons, Subway, and McDonald’s compete for fast-food customers’ dollars. Often, the difference between business success and failure comes down to whether your company is doing a better job of satisfying customer wants and needs than your competitors. Consequently, companies need to keep close track of what their competitors are doing. To do this, managers perform what’s called a *competitive analysis*, which is deciding who your competitors are, anticipating competitors’ moves, and determining competitors’ strengths and weaknesses. Surprisingly, because they tend to focus on only two or three well-known competitors with similar goals and resources, managers often do a poor job of identifying potential competitors.
The second mistake managers make when analyzing the competition is to underestimate potential competitors’ capabilities. When this happens, managers don’t take the steps they should to continue to improve their products or services. The result can be significant decreases in both market share and profits.

For nearly a decade, traditional phone companies have ignored the threat to their business from VOIP (voice over Internet protocol)—that is, the ability to make telephone calls over the Internet. Early on, software products made it possible to make inexpensive long-distance phone calls on the Internet. All you needed was an Internet service provider; a computer with a sound card, speakers, and a microphone; and Internet phone software. The sound quality was only as good as AM radio, but since the calls were so much cheaper and people were used to poor-quality sound on their cell phones, it didn’t matter.24

Today, though, because phone companies were slow to adopt VOIP capabilities themselves, they’re facing a rash of new, unexpected VOIP competitors, all of whom plan to slash prices and take their market share using the high-speed Internet services connect to peoples’ homes. Vonage (www.vonage.ca), an Internet phone company, charges just $19.99 per month (maybe less by the time you read this) for unlimited calling in Canada, the United States, and Puerto Rico. Its international long-distance charges are generally cheaper than your local long-distance provider. How much of a threat is Internet phone service to traditional phone companies today? Jeff Pulver, CEO of Pulver.com, which owns Free World Dialup, an Internet phone company, said that within the next few years, “it’s quite possible that 50% or more of voice traffic will take place off the traditional public telephone network and run on the Internet wireless or other systems.”25

**Supplier Component**

**Suppliers** are companies that provide material, human, financial, and informational resources to other companies. Stelco, Canada’s largest steel producer, buys iron ore from suppliers to make steel products. When IBM sells a mainframe computer, it also provides support staff, engineers, and other technical consultants to the company that bought the computer. If you’re shopping for desks, chairs, and office supplies, chances are Office Depot will be glad to help your business open a revolving charge account to pay for your purchases.

A key factor influencing the relationship between companies and their suppliers is how dependent they are on each other.27 **Supplier dependence** is the degree to which a company relies on a supplier because of the importance of the supplier’s product to the company and the difficulty of finding other sources of that product.

---

**THE TEN COMMANDMENTS FOR ETHICAL COMPETITIVE ANALYSIS**

Sometimes, in their zeal to dig up information about competitors, managers and employees commit unethical or illegal acts such as digging through trash dumpsters on a competitor’s property or paying a competitor’s employees for information about secret designs or components. Fuld & Company, a major consulting firm in competitive intelligence, offers these “ten commandments” for ethical competitive analysis:

- Thou shalt not lie when representing thyself.
- Thou shalt observe thy company’s legal guidelines as set forth by the legal department.
- Thou shalt not tape-record a conversation.
- Thou shalt not bribe.
- Thou shalt not plant eavesdropping devices.
- Thou shalt not deliberately mislead anyone in an interview.
- Thou shalt neither obtain from nor give price information to thy competitor.
- Thou shalt not swap misinformation.
- Thou shalt not steal a trade secret (or steal employees away in hopes of learning a trade secret).
- Thou shalt not knowingly press someone for information if it may jeopardize that person’s job or reputation.26
**Buyer dependence** is the degree to which a supplier relies on a buyer because of the importance of that buyer to the supplier and the difficulty of selling its products to other buyers. For example, because it believed that the clothes sold in its stores were too expensive, Wal-Mart’s Canadian division sent letters to its clothing suppliers, demanding a “retroactive, nonnegotiable price rollback of between 4 and 10 percent.” So if Wal-Mart had purchased $100,000 of goods from a supplier in the last six months, it expected to receive a refund from the supplier totalling between $4,000 and $10,000. The suppliers were furious, but had little choice since Wal-Mart was one of their largest customers.29

As Wal-Mart’s demand indicates, greater buyer or seller dependence can lead to **opportunistic behaviour**, in which one party benefits at the expense of the other. Opportunistic behaviour between buyers and suppliers will never be completely eliminated. However, many companies believe that both buyers and suppliers can benefit by improving the buyer–supplier relationship. General Motors, for example, which has a long history of adversarial relationships with its suppliers, has an “Ambassador Program.” The Ambassador Program is designed to improve communication between GM and its suppliers by assigning a GM executive (but not the GM executive who makes purchases from the company) to meet regularly with the supplier to discuss problems or new ideas. In contrast to opportunistic behaviour, buyer–supplier transactions such as GM’s Ambassador Program emphasize **relationship behaviour**, which focuses on establishing a mutually beneficial, long-term relationship between buyers and suppliers. Like General Motors, the trend in the last decade is for companies to reduce the number of suppliers they deal with and to improve the relationships they have with remaining suppliers.30

**Industry Regulation Component**

In contrast to the political/legal component of the general environment that affects all businesses, the **industry regulation** component consists of regulations and rules that govern the business practices and procedures of specific industries, businesses, and professions. Regulatory agencies and government departments affect businesses by creating and enforcing rules and regulations to protect consumers, workers, or society as a whole. For example, after many years of debate, the federal government passed the Employment Equity Act, which is enforced by the Canadian Human Rights Commission (www.chrc-ccdpe.ca). This act places a responsibility on federally regulated employers to increase the representation of four historically disadvantaged groups (women, Aboriginals, visible minorities, and persons with disabilities). In addition, it also enforces the Canadian Human Rights Act, which places further responsibilities on federally regulated employers. Failure to comply with the Employment Equity Act or the Human Rights Act can lead to fines of as much as $50,000. Not only must one be aware of the acts themselves, employers must constantly monitor regulations under the act and new policies developed by the Canadian Human Rights Commission.

There are almost 100 federal government agencies, departments, and regulatory commissions that can affect nearly any kind of business (see http://canada.gc.ca/depts/major/depind_e.html). Exhibit 2.3 lists some of the most influential federal agencies and commissions.

However, businesses are not just subject to federal regulations. They must also meet provincial, county, and city regulations, too. Surveys indicate that managers rank keeping up to date with and implementing government regulations as one of the most demanding and frustrating parts of their jobs.

---

**DEALING WITH GIFTS AND SUPPLIERS**

In hopes of getting a buyer’s business or getting more business, suppliers sometimes offer buyers trips to exotic locations, dinners at expensive restaurants, or expensive gifts. Excessive gift giving and receiving creates a conflict of interest between what’s best for the company (purchasing items of the best quality and cost) and what’s personally best for the buyer who receives the gifts. Follow these general guidelines to avoid conflicts of interest:

- **Remember that there is no such thing as a free lunch.**
- **Make sure that business meals and entertainment (parties, outings, sporting events) have a valid business purpose and that the buyer and the supplier take turns paying for or hosting them.**
- **Don’t accept gifts worth more than $25 in value. If an offered gift is worth $25, report it to your manager who can decide whether it is appropriate to keep the gift.**
- **Never accept cash or cash equivalents, such as gift certificates.**
- **Don’t accept discounts on goods and services, unless they are generally available to others.**
- **Don’t accept offers to own stock in suppliers’ companies.**
- **Don’t allow personal friendships with suppliers to influence buying decisions.**31
Advocacy Groups

**Advocacy groups** are groups of concerned citizens who band together to try to influence the business practices of specific industries, businesses, and professions. The members of a group generally share the same point of view on a particular issue. For example, environmental advocacy groups might try to get manufacturers to reduce smokestack pollution emissions. Unlike the industry regulation component of the specific environment, advocacy groups cannot force organizations to change their practices. However, they can use a number of techniques to try to influence companies: public communications, media advocacy, and product boycotts.

The **public communications** approach relies on voluntary participation by the news media and the advertising industry to get an advocacy group's message out. For example, the Canadian Cancer Society (www.cancer.ca) undertakes public information campaigns on a variety of issues, including tobacco use and diets, that aims to reduce the rate of cancer in Canada by reducing smoking rates and improving people’s eating habits. To accomplish its goals, the Canadian Cancer Society makes heavy use of public service announcements on TV and radio (as part of their community service, TV and radio stations donate this time). It also maintains an extensive Web site, provides a toll-free number to disseminate cancer information, provides a community services directory, issues news releases, and works in conjunction with other groups to make Canadians more aware of cancer-related issues.

In contrast to the public communications approach, media advocacy is a much more aggressive form of advocacy. A **media advocacy** approach typically involves framing issues as public issues (i.e., affecting everyone); exposing questionable, exploitative, or unethical practices; and forcing media coverage by buying media time or creating controversy that is likely to receive extensive news coverage. People for the Ethical Treatment of Animals (PETA), which has offices around the world, uses controversial publicity stunts and advertisements to try to change the behaviour of large organizations, fashion designers, medical researchers, and anyone else it believes is hurting or mistreating animals. PETA’s co-founder and president Ingrid Newkirk says, “People now know that if they do something ghastly to an animal, they can’t necessarily get away with it. When we

---

### Exhibit 2.3
Federal Regulatory Agencies and Commissions

<table>
<thead>
<tr>
<th>Federal Agency</th>
<th>Regulatory Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental Assessment Agency <a href="http://www.cea-ace.gc.ca">www.cea-ace.gc.ca</a></td>
<td>Reduces and controls pollution through research, monitoring, standard setting, and enforcement activities</td>
</tr>
<tr>
<td>Canadian Radio-television and Telecommunications Commission (CRTC) <a href="http://www.crtc.gc.ca">www.crtc.gc.ca</a></td>
<td>Regulates communications by radio, television, wire, satellite, and cable</td>
</tr>
<tr>
<td>Bank of Canada <a href="http://www.bank-banque-canada.ca">www.bank-banque-canada.ca</a></td>
<td>As the nation’s central bank, controls interest rates and money supply, and monitors the Canadian banking system to produce a growing economy with stable prices</td>
</tr>
<tr>
<td>Competition Tribunal <a href="http://www.ct-tc.gc.ca">www.ct-tc.gc.ca</a></td>
<td>Restricts unfair methods of business competition and misleading advertising</td>
</tr>
<tr>
<td>Health Canada <a href="http://www.hc-sc.gc.ca">www.hc-sc.gc.ca</a></td>
<td>Protects nation’s health by making sure food, drugs, and cosmetics are safe</td>
</tr>
<tr>
<td>Canadian Industrial Relations Board <a href="http://www.cirb-ccri.gc.ca">www.cirb-ccri.gc.ca</a></td>
<td>Monitors union elections and stops companies from engaging in unfair labour practices</td>
</tr>
<tr>
<td>Canadian Centre for Occupational Health and Safety <a href="http://www.ccohs.ca">www.ccohs.ca</a></td>
<td>Saves lives, prevents injuries, and protects the health of workers</td>
</tr>
</tbody>
</table>
started, nobody knew what animal rights meant.... Now, it’s an issue.” PETA protesters have skated in only bikini briefs on the Rideau Canal in Ottawa in –25ºC weather while wearing banners saying, “We’d Rather Bare Skin Than Wear Skin.” From PETA’s perspective, any animal-based product is bad. One of PETA’s latest protests is the distribution of 2000 blood-covered, knife-holding, “evil Colonel Sanders” bobble-head dolls to news organizations and KFC restaurants. PETA spokesman Joe Hinkle said, “We’d like them to stop breeding and drugging chickens so that they grow so big that they actually cripple under their own bulk.” KFC issued this response, saying, “PETA has disparaged our brand and misrepresented the truth about our responsible industry-leading animal welfare standards. KFC is committed to the humane treatment of chickens.”

A **product boycott** is a tactic in which an advocacy group actively tries to convince consumers to not purchase a company’s product or service. For example, Pamela Anderson narrated a five-minute video that called for a boycott of KFC because she felt that chickens used for their products were being mistreated. It was produced by PETA and distributed on the organization’s Web site.

**Review 3: Specific Environment**

The specific environment is made up of five components: customers, competitors, suppliers, industry regulators, and advocacy groups. Companies can monitor customers’ needs by identifying customer problems after they occur or by anticipating problems before they occur. However, because they tend to focus on well-known competitors, managers often underestimate their competition or do a poor job of identifying future competitors. Since suppliers and buyers are very dependent on each other, that dependence sometimes leads to opportunistic behaviour, in which one benefits at the expense of the other. Regulatory agencies affect businesses by creating rules and then enforcing them, and the number of rules and regulations continues to increase. Advocacy groups cannot regulate organization practices. However, through public communications, media advocacy, and product boycotts, they try to convince companies to change their practices.

**MAKING SENSE OF CHANGING ENVIRONMENTS**

In Chapter 1, you learned that managers are responsible for making sense of their business environments. However, our just-completed discussions of the general and specific environments indicate that making sense of business environments is not an easy task. Because external environments can be dynamic, confusing, and complex, managers use a three-step process to make sense of the changes in their external environments. The steps are environmental scanning, interpreting environmental factors, and acting on threats and opportunities.

**Environmental Scanning**

**Environmental scanning** is searching the environment for important events or issues that might affect an organization. Managers scan the environment to stay up to date on important factors in their industry. Managers also scan their environments to reduce uncertainty. For example, with one out of every four new car buyers purchasing highly profitable sports utility vehicles (SUVs), auto executives haven’t paid much attention to environmental groups’ complaints about SUVs’ extremely poor gas mileage. Now, however, with market research showing that current SUV owners are unhappy with their vehicles’ poor gas mileage and that potential car buyers in their teens and 20s are beginning to express strong disapproval of SUVs as well, auto executives are beginning to pay attention—because their sales and profits could be affected. James Schroer, DaimlerChrysler’s executive vice president for sales and marketing, says that the increasingly negative view of SUVs is “a big deal, and it’s real.”

Organizational strategies also affect environmental scanning. In other words, managers pay close attention to trends and events that are directly related to their companies’ abilities to compete in the marketplace. A major trend that is affecting television advertising...
is the increasing use of digital video recorders (DVRs). DVRs allow people to record TV shows and watch them at a later time. Of course, this allows people to easily skip the commercials, a trend that affects both TV stations, who derive revenue from the ads, and the companies who advertise on TV. In response to this matter, Montreal-based etc.tv Inc. has launched a pilot program that offers viewers interactive ads. An icon appearing in the corner of the TV during ads allows viewers to access video on demand. These videos will be ads that run from 2 to 20 minutes. Many hope that this flexibility in advertising will create new advertising strategies that will allow companies to reach their target market. Large organizations such as Procter & Gamble and the National Bank of Canada have already signed up for the service. This practice may be an interesting strategy to deal with environmental changes.36

Environmental scanning is important because it contributes to organizational performance. Environmental scanning helps managers detect environmental changes and problems before they become organizational crises.37 Furthermore, companies whose CEOs do more environmental scanning have higher profits.38 CEOs in better-performing firms scan their firms’ environments more frequently and scan more key factors in their environments in more depth and detail than do CEOs in poorer-performing firms.39

Interpreting Environmental Factors

After scanning, managers determine what environmental events and issues mean to the organization. Typically, managers view environmental events and issues as either threats or opportunities. When managers interpret environmental events as threats, they take steps to protect the company from further harm. For example, in France, the neighborhood boulangerie, boucherie, fromagerie, patisserie, and poissonnerie (bakery, butcher, cheese, pastry, and fish shops) have begun to go out of business in large numbers. Their existence is now threatened by the Carrefour, huge hypermarkets that are sometimes as large as three football fields. French shoppers load up on cartloads of groceries once a week at the Carrefour to save scarce time and money. One of the best buys is France’s traditional loaf of bread, the baguette, which sells for about $1.50 at small bakeries but goes for 60 cents at the hypermarket. So with their businesses in decline, the
neighbourhood boulangerie, boucherie, fromagerie, patisserie, and poissonnerie have turned to the French government for help, asking it to enact laws limiting construction of new hypermarkets. They’re also asking the French government to prevent hypermarkets from selling products below cost, a practice that hypermarkets say they don’t use.40

By contrast, when managers interpret environmental events as opportunities, they will consider strategic alternatives for taking advantage of the event to improve company performance. In the snack business, Hostess Frito-Lay saw opportunities in the increasing demand for healthier snacks. By being quick to market with Baked Frito-Lay Potato Crisps, Baked Tostitos, and Rold Gold Fat Free Pretzels, Hostess Frito-Lay captured a large share of the Canadian low-fat snack market.41

**Acting on Threats and Opportunities**

After scanning for information on environmental events and issues, and interpreting them as threats or opportunities, managers have to decide how to respond to these environmental factors. However, deciding what to do under conditions of uncertainty is difficult. Managers are never completely confident that they have all the information they need, or that they correctly understand the information they have.

Because it is impossible to comprehend all the factors and changes, managers rely on simplified models of external environments called cognitive maps. **Cognitive maps** summarize the perceived relationships between environmental factors and possible organizational actions. For example, the cognitive map shown in Exhibit 2.4 represents a small clothing store owner’s interpretation of her business environment. The map shows three kinds of variables. The first, shown as rectangles, are environmental factors such as Wal-Mart or a large mall 20 minutes away. The second, shown in ovals, are potential actions that the store owner might take, such as a low-cost strategy; a good value, good service strategy; or a large selection of the latest fashions strategy. The third, shown as trapezoids, are company strengths, such as low employee turnover, and weaknesses, such as small size.
The arrows on the map indicate whether the manager believes there is a positive or negative relationship between variables. For example, the manager believes that a low-cost strategy wouldn’t work, because Wal-Mart and Zellers are nearby. Offering a large selection of the latest fashions would not work either—not with the small size of the store and that large nearby mall. However, this manager believes that a good value, good service strategy would lead to success and profits, because of low employee turnover, knowing customers well, a reasonable selection of clothes at reasonable prices, and a good location.

In the end, managers must complete all three steps—environmental scanning, interpreting environmental factors, and acting on threats and opportunities—to make sense of changing external environments. Environmental scanning helps managers more accurately interpret their environments and take actions that improve company performance. Through scanning, managers keep tabs on what competitors are doing, identify market trends, and stay alert to current events that affect their companies’ operations. Armed with the environmental information they have gathered, managers can then take action to minimize the impact of threats and turn opportunities into increased profits.

**Review 4: Making Sense of Changing Environments**

Managers use a three-step process to make sense of external environments: environmental scanning, interpreting information, and action. Managers scan their environments based on their organizational strategies, their need for up-to-date information, and their need to reduce uncertainty. When managers identify environmental events as threats, they take steps to protect the company from harm. When managers identify environmental events as opportunities, they formulate alternatives for taking advantage of them to improve company performance. Using cognitive maps can help managers visually summarize the relationships between environmental factors and the actions they might take to deal with them.

**Internal Environments**

External environments are external trends and events that have the potential to affect companies. The **internal environment** consists of the trends and events within an organization that affect the management, employees, and organizational culture.

For example, consider the internal environment at SAS, the leading provider of statistical software. Unlike most software companies that expect employees to work 12- to 14-hour days, SAS offices close at 6 P.M. every evening. Employees also receive unlimited sick days each year. And to encourage employees to spend time with their families, there’s an on-site daycare facility, the company cafeteria has plenty of highchairs and baby seats, and the company even has a seven-hour workday. Plus, every Wednesday, the company passes out M&M chocolate candies, plain and peanut, to all employees—a total of more than 200 tonnes of M&Ms per year. SAS senior vice president Jim Davis says, “We are firm believers that happy employees equal happy customers.”

Internal environments are important because they affect what people think, feel, and do at work. Given SAS’s internal environment, it shouldn’t surprise you to know that almost no one quits. In a typical software company, 25 percent of the workforce quits each year to take another job. At SAS, only 4 percent leave. Jeff Chambers, SAS’s vice president of human resources, says “We have always had a commitment to investing in and cultivating meaningful, long-term relationships with our employees and clients. This has led to unusually low turnover in both populations and is at the core of our 28 years of sustained profitability and success.”

Comments such as these reflect the key component in internal environments—organizational culture. **Organizational culture** is the set of key values, beliefs, and attitudes shared by organizational members. Clearly, one of SAS’s key values is its commitment to its employees.
After reading the next section, you should be able to explain how organizational cultures are created and how they can help companies be successful.

ORGANIZATIONAL CULTURES: CREATION, SUCCESS, AND CHANGE

Let’s take a closer look at the creation and maintenance of organizational cultures, successful organizational cultures, and changing organizational cultures.

Creation and Maintenance of Organizational Cultures

Organizational culture, often referred to as corporate culture, can be strong and enduring. Shared values, beliefs, attitudes, and assumptions drive organizational culture. Organizations also have subcultures, or cultures within cultures. For example, different divisions within an organization that are located in different parts of the country or the world will often share some similar elements of culture, but there may also be things that make them a little different. Within the same company, managers in Toronto and Hawaii may have different beliefs about how managers should dress or communicate with each other.

Visible elements of corporate culture are called *visible artifacts*. The way people dress, company rituals and ceremonies, and corporate offices are all visible artifacts. IBM was once referred to as “the men in the blue suits” because most of their employees dressed in dark blue suits and employees’ dress reflected the uniformity and strength of IBM’s organizational culture. In addition to dress, language and forms of communication can indicate the level of formality expected within a workplace. The way language is used in the workplace can also tell you a lot about an organization. How do co-workers address each other? How do you address your boss? Is it by first name or is it Ms. Smith? Is communication formal and usually written or is it informal and usually in person? What sort of job titles are used? The answers to these questions can speak loudly about organizational culture. For example, Wal-Mart calls employees “associates” to indicate their importance in the success of the organization, while at AdFarm, a small Calgary advertising firm that was named one of Canada’s best employers, there are no job titles, increasing the feeling of belonging. Each of these patterns of behaviour forms part of the corporate culture and tells us something about the organization.

A primary source of organizational culture is the company founder. Founders such as Thomas J. Watson (IBM), Frank Stronach (Magna), Bill Gates (Microsoft), or John Forzani (Forzani) create organizations in their own images that they imprint with their beliefs, attitudes, and values. Microsoft employees share founder Bill Gates’s intensity for staying ahead of software competitors. Says a Microsoft vice president, “No matter how good your product, you are only 18 months away from failure.”

While company founders are instrumental in the creation of organizational cultures, founders retire, die, or choose to leave their companies. For example, neither Michael Cowpland, founder of Corel Corporation, nor Mitch Kapor, founder of Lotus software, which created Lotus 1-2-3, one of the first and most successful spreadsheet programs, is still with the company he created. Yet they both still work in the computer industry. So when the founders are gone, how are the founders’ values, attitudes, and beliefs sustained in the organizational culture? Answer: stories and heroes.

Organizational members tell *stories* to make sense of organizational events and changes, and to emphasize culturally consistent assumptions, decisions, and actions. At Wal-Mart, stories abound about founder Sam Walton’s thriftiness as he strove to make Wal-Mart the low-cost retailer that it is today:

In those days, we would go on buying trips with Sam, and we’d all stay, as much as we could, in one room or two. I remember one time in Chicago when we stayed eight of us to a room. And the room...
wasn’t very big to begin with. You might say we were on a pretty restricted budget. (Gary Reinboth, one of Wal-Mart’s first store managers)\textsuperscript{48}

Today, Sam Walton’s thriftiness still permeates Wal-Mart. Everyone, including top executives and the CEO, flies coach rather than business or first class. When travelling on business, it’s still the norm to share rooms (though two to a room, not eight!) at inexpensive hotels like Motel 6 and Super 8 instead of more expensive Holiday Inns. Likewise, on business travel, Wal-Mart will reimburse only up to US$15 per meal, which is half to one-third the reimbursement rate at similar-sized companies (remember, Wal-Mart is the largest company in the world). And, at one of its annual meetings, CEO Lee Scott reinforced Sam Walton’s beliefs by exhorting Wal-Mart employees to bring back and use the free pencils and pens from their travels. Most people in the audience didn’t think he was kidding.\textsuperscript{49}

A second way in which organizational culture is sustained is by creating and celebrating heroes. By definition, \textit{organizational heroes} are organizational people admired for their qualities and achievements within the organization. Consider the case of Bowa Builders, a full-service construction company. When it was renovating a large auto dealership, its carpet subcontractor mistakenly ordered the new carpet to be delivered two weeks \textit{after} it was scheduled to be installed. Rather than allow construction to be delayed, a Bowa employee kept the project on schedule by immediately reordering the carpet, flying to the carpet manufacturer’s factory, renting a truck, and then driving the carpet back to the auto dealership, all within 48 hours of learning about the problem. CEO and company co-founder Larry Weinberg says this story is told and retold within Bowa Builders as an example of heroic customer service. Moreover, the car dealership was so delighted with this extraordinary service it has referred $12 million to $15 million in new business to Bowa Builders.\textsuperscript{50}

A third way in which organizational culture is sustained is through \textit{rituals}, \textit{ceremonies}, and symbols. Wal-Mart is famous for having all its employees gather before the store opens and sing the national anthem and perform the company cheer.\textsuperscript{51} Annual employee awards ceremonies can reinforce company values, and company picnics are examples of \textit{organizational ceremonies} that provide opportunities for organizations to transmit and maintain its culture. One can consider physical artifacts such as buildings, logos, stories, slogans, rituals, and ceremonies to be organizational symbols that represent organizational values.\textsuperscript{52}

\section*{Successful Organizational Cultures}

Preliminary research shows that organizational culture is related to organizational success. As shown in Exhibit 2.5, cultures based on adaptability, involvement, a clear mission, and consistency can help companies achieve higher sales growth, return on assets, profits, quality, and employee satisfaction.\textsuperscript{53} Weak corporate cultures can leave companies without vision leading to unfocused strategies and unmotivated employees. On the other hand, a strong corporate culture can stifle change or create conflict when organizations merge.

Adaptability is the ability to notice and respond to changes in the organization’s environment. Previously, we discussed the difficulty that CEO Louis Gerstner was having trying to turn around IBM. Frustrated with his inability to change IBM culture, Gerstner eventually decreed that the core IBM beliefs set forth by founder Thomas J. Watson, Sr. (excellence, customer satisfaction, and respect for the individual) were to be replaced with the eight new goals shown in Exhibit 2.6. Instead of responding to his attempts to improve the company, many IBMers were shocked because Thomas J. Watson, Jr., who succeeded his father as IBM’s CEO, once stated that IBM’s success was dependent on its ability to change everything “except those basic beliefs.”\textsuperscript{54}

In cultures that promote higher levels of employee involvement in decision-making, employees feel a greater sense of ownership and responsibility. For example, at Hewlett-Packard, each “business,” such as laser printers, calculators, or personal computers, makes its own decisions. So when the video products division was deciding which computer

---

\textit{organizational heroes} people celebrated for their qualities and achievements within an organization

\textit{organizational rituals} routine activities that emphasize the organization’s culture

\textit{organizational ceremonies} planned activities or events that emphasize culturally consistent assumptions, decisions, and actions

\textit{organizational symbols} something that represents another thing
chips to use in its products, it chose not to use H-P’s own computer chips because they were too expensive. Instead, they purchased integrated circuits for half the price from one of the H-P computer chip division’s competitors. Because involvement and participation are so central to H-P’s culture, no one (even in the H-P computer chip division) questioned this decision.55

A company’s vision is its purpose or reason for existing. In organizational cultures in which there is a clear organizational vision, the organization’s strategic purpose and direction are apparent to everyone in the company. And, when managers are uncertain about their business environments, the vision helps guide the discussions, decisions, and behavior of the people in the company. At F.H. Faulding & Company, an Australian-based provider of health-care products and services that does business in 70 countries, the vision is “delivering innovative and valued solutions in healthcare.”56 This vision lets employees know why the company is in business (to deliver health-care solutions) and

| 1. The marketplace is the driving force behind everything we do. |
| 3. Our primary measures of success are customer satisfaction and shareholder value. |
| 5. We never lose sight of our strategic vision. |
| 6. We think and act with a sense of urgency. |
| 7. Outstanding, dedicated people make it all happen, particularly when they work together as a team. |
| 8. We are sensitive to the needs of all employees and to the communities in which we operate. |

the values that really matter (innovative and valued solutions). To give its employees even more guidance, Faulding has clearly defined each of the key words in the vision statement. For example, “delivering” is defined to mean targeting quality drugs, products, and services to the right place at the right time while concentrating on a global perspective. Likewise, “solutions” means being focused, timely, and profitable by making quality products and services that satisfy customers’ and partners’ needs.

Finally, in consistent organizational cultures, the company actively defines and teaches organizational values, beliefs, and attitudes. Consistent organizational cultures are also called strong cultures, because the core beliefs are widely shared and strongly held.

Changing Organizational Cultures

As shown in Exhibit 2.7, organizational cultures exist on three levels. First, on the surface level, are the reflections of an organization’s culture that can be seen, heard, or observed, such as symbolic artifacts (e.g., dress codes and office layouts, and workers’ and managers’ behaviours). Next, just below the surface, are the values and beliefs expressed by people in the company. You can’t see these, but by listening carefully to what people say and how decisions are made or explained, those values and beliefs become clear. Finally, unconsciously held assumptions and beliefs are buried deep below the surface. These are the unwritten views and rules that are so strongly held and so widely shared that they are rarely discussed or even thought about unless someone attempts to change them or unknowingly violates them. When it comes to changing cultures, it can be very difficult to change unconscious assumptions and beliefs held deep below the surface. Instead, managers should focus on the parts of the organizational culture they can control; these include observable surface-level items, such as workers’ behaviours and symbolic artifacts, and expressed values and beliefs, which can be influenced through employee selection. Let’s see how these can be used to change organizational cultures.

One way of changing a corporate culture is to use behavioural addition or behavioural substitution to establish new patterns of behaviour among managers and employees. Behavioural addition is the process of having managers and employees perform new behaviours that are central to and symbolic of the new organizational culture that a company wants to create. Behavioural substitution is the process of having managers and employees perform new behaviours central to the “new” organizational culture in place of behaviours that were central to the “old” organizational culture.

Sometimes organizations change their name and/or logo to help reinforce cultural change. The second way in which managers can begin to change corporate culture is to change visible artifacts of their old culture, such as the office design and layout, company dress codes, and who benefits (or doesn’t) from company benefits and perks such as stock options, personal parking spaces, or the private company dining room. At Petro-Canada, once a Crown corporation, corporate jets were eliminated and senior executives had to purchase their own golf-club memberships. Even their Calgary headquarters, dubbed “Red Square” and a symbol of federal government intrusion in the private sector, was sold and only half of it was leased back. Change was in the air, and the company eventually sold its large Canadian art collection, gave up its most expensive office space, and closed the executive dining room.

Corporate cultures are very difficult to change. Consequently, there is no guarantee that behavioural substitution, behavioural addition, or changing visible cultural artifacts
will change a company’s organizational culture. However, these methods are some of the best tools that managers have for changing culture, because they send the clear message to managers and employees that “the accepted way of doing things” has changed.

**Review 5: Organizational Cultures: Creation, Success, and Change**

Organizational culture is the set of key values, beliefs, and attitudes shared by organizational members. Organizational cultures are often created by company founders and then sustained through the telling of organizational stories and the celebration of organizational heroes. Adaptable cultures that promote employee involvement, that make clear the organization’s strategic purpose and direction, and that actively define and teach organizational values and beliefs can help companies achieve higher sales growth, return on assets, profits, quality, and employee satisfaction. Behavioural substitution, behavioural addition, and changing visible artifacts are ways in which managers can begin to change their organizational cultures.

**EXHIBIT 2.7 Three Levels of Organizational Culture**

<table>
<thead>
<tr>
<th>Level</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Surface Level</strong></td>
<td>Seen and observed (what people say, how decisions are made and explained)</td>
</tr>
<tr>
<td><strong>Expressed Values</strong></td>
<td>Heard but not seen (widely shared assumptions and beliefs)</td>
</tr>
<tr>
<td><strong>Unconsciously Held</strong></td>
<td>Unwritten and rarely discussed (buried deep below surface)</td>
</tr>
</tbody>
</table>

**What Really Happened?**

Managers use a three-step process to make sense of external environments. First, they scan their environments based on their organizational strategies, their need for up-to-date information, or their need to reduce uncertainty. Second, when they identify environmental events such as threats, they take steps to protect their companies from harm. And third, when they identify environmental events as opportunities, they formulate strategies to improve company performance. As mentioned earlier in the chapter, managers need to pay close attention to trends and events that are directly related to their companies’ abilities to compete in the marketplace. Environmental scanning is important because it contributes to organizational performance. Companies can succeed by scanning their business environments for events and trends, interpreting what those changes mean, and then acting to adapt to those changes.

So the question is “Are the threats serious, and if so how will you respond?”

Just because you are a Canadian icon and dominate your market niche does not mean that you can survive anything. Many great companies have gone out of business because they were unable to adapt to changing times. Many managers become complacent. Because a company is on top it can become beholden to the formula that brought it such great success. While having a successful strategy is clearly important, you can’t answer this question without taking a look at external environments, meaning the forces and events outside a company that have the potential to influence or affect it. Organizations are influenced by two kinds of external environments: the general environment, which consists of economic, technological, sociocultural, and political/legal events and trends, and the specific environment, which consists of customers, competitors, suppliers, industry regulators, and advocacy groups. There are two basic strategies for monitoring customers: reactive and proactive. Reactive customer monitoring is identifying and addressing customer trends and problems after they occur. Proactive monitoring of customers means trying to sense events, trends, and problems before they occur (or before customers complain).

Even though Tim Hortons is on top, it must be aware of any developments in its highly competitive environment. Tim Hortons has been very successful in evolving with a changing environment. The changes have come over a long period of time. Some of the changes have been symbolic (a change in organizational symbols) but reflective of a changing marketplace. In 1988 the process of reshaping the company’s image began when it began phasing out the word “Donuts” in all of its signage. Tim Hortons attempted to broaden its menu’s appeal in the early 1990s with sandwiches; however, it didn’t market the new products much, and the new menu items didn’t catch on with customers.

Given that you recognize that the marketplace is changing, competition is increasing, and you failed with the first
major change in your menu, what do you do? Do you change your menu so that it has a broader appeal or do you retrench and rely on your tried-and-true formula: coffee and donuts?

After managers scan their environments and identify environmental events as threats, they take steps to protect their companies from harm by formulating strategies to deal with the impending problems. The top management at Tim Hortons was very proactive in scanning the environment and making changes to its menu. As mentioned, the company was already slowly downplaying the importance of donuts in its menu and had removed the word “Donuts” from its restaurant signs. It then did extensive market research and testing to see what customers would like and began changing the menu. It started to add drive-through windows to all its locations to tap into a market populated by people wanting to run and go, rather than stop and linger, to enjoy a cup of coffee and a donut.

The changes in the menu and a slick marketing campaign have paid off. Tim Hortons started by adding bagels to its menu in 1996 and now has items such as iced cappuccino, soup, sandwiches, and chili on the menu. The Atkins diet appears to have been a fad that is slowly fizzling out. Tim Hortons essentially ignored the threat without any detrimental effect. Nonetheless, customer interest in healthier choices has increased, and Tim Hortons has successfully responded. In 2002, the company’s sales in Canada exceeded that of McDonald’s, and Krispy Kreme appears to be in full retreat. Krispy Kreme had planned to open 32 stores in Canada, but before it had done so, it was already closing stores for lack of business. It had hung on to its coffee and donuts product line with little product diversification or innovation, unlike Tim Hortons. On the other hand, Tim Hortons plans on doubling the number of U.S. locations to 500 by 2007, and as of 2006 has over 2400 locations in Canada. Clearly, the research and development the company undertook, coupled with the environmental scanning, has paid off. Wendy’s has now spun Tim Hortons off from the parent chain, offering shares to the public, and Tim’s remains the king of the fast food industry in Canada, even though donuts now account for a small portion of total sales.

Key Terms

advocacy groups (42)  
behavioural addition (50)  
behavioural substitution (50)  
business confidence indices (36)  
buyers’ dependence (41)  
cognitive maps (45)  
company vision (49)  
competitive analysis (39)  
competitors (39)  
complex environment (33)  
dynamic environment (32)  
environmental change (32)  
environmental complexity (33)  
environmental munificence (34)  
environmental scanning (43)  
external environments (32)  
genre environment (35)  
industry regulation (41)  
internal environment (46)  
media advocacy (42)  
opportunistic behaviour (41)  
organizational ceremonies (48)  
organizational culture (46)  
organizational heroes (48)  
organizational rituals (48)  
organizational stories (47)  
organizational symbols (48)  
product boycott (43)  
public communications (42)  
punctuated equilibrium theory (32)  
relationship behaviour (41)  
simple environment (33)  
specific environment (35)  
stable environment (32)  
supplier dependence (40)  
suppliers (40)  
technology (37)  
uncertainty (34)  
visible artifacts (47)
Self-Assessment

CHECK YOUR TOLERANCE FOR AMBIGUITY
Think of the difference between playing chess (where you can see all the pieces and anticipate attacks and plan counterattacks) and playing poker (where no one knows anyone else’s hand, and you have to make guesses based on your interpretation of opponents’ betting patterns). In chess, there is little ambiguity, whereas in poker there is tremendous ambiguity. Although many people liken business to a game of chess, probably because of the strategic aspects of the game, business is actually more like poker. The business environment is complex and uncertain, and managers never really know all the cards the opposition is holding. Managers must learn to adapt to environmental shifts and new developments—sometimes on a daily basis. For some managers, however, this can be a challenging task because everyone has a different comfort level when it comes to ambiguity. For some, not knowing all the details can be a source of significant stress, whereas for others uncertainty can be energizing.

As a manager, you will need to develop an appropriate tolerance for ambiguity. For example, being stressed out every time interest rates change can be counterproductive, but completely ignoring the economic environment can be detrimental to your company’s performance. On page 511 of the Assessment Appendix, you will find a 22-question survey designed to help you get a sense of your tolerance for ambiguity.

Management Decisions

CULTURE SHOCK
As a vice president of a medium-sized software technology company located in Ottawa, you have been involved in several acquisitions of smaller firms over the last few years, each having resulted in increased growth and profitability for your firm. Recently, your company has been discussing plans to acquire a small, relatively new, computer-networking services company located in California’s Silicon Valley. Your firm is interested in this acquisition because it has the skills, equipment, and knowledge desperately needed but currently lacking in your firm. Additionally, some of your current clients are located in and around Silicon Valley.

The firm being considered has a solid reputation and a growing number of customers located in Canada. If this acquisition occurs, it will serve to broaden the services currently provided by your firm, increase your firm’s presence nationwide, and strengthen your firm’s core competencies by alleviating the need to outsource certain activities. Investment capital has already been garnered to facilitate the acquisition.

Tomorrow morning, you and several other top executives will decide whether to go ahead with the proposed acquisition. Unfortunately, one item makes you uncomfortable with this plan. In comparing the two companies, you have found that your firm’s corporate culture differs dramatically from that of the firm being considered. Although some of your colleagues denounce this as being an insignificant problem and one that can be easily solved, you consider it to be one of high importance.

Your firm is larger and more bureaucratic, is formal in structure, and utilizes centralized decision-making techniques. Typically before key decisions are made, an extensive amount of time is spent involving group discussions and developing consensus before any action is taken. Additionally, there is a clear chain of command within your firm, and individuals have distinct job descriptions and duties. On the other hand, the proposed company’s structure and culture appear to be very informal. The organizational hierarchy is relatively flat, with key decisions being made at all levels. Employees have no clear responsibilities or duties and are empowered to “take the ball and run with it.” The firm’s founder claims that it is their unique culture that has resulted in the firm’s rapid growth in market share, profitability, and innovativeness.

Your main fear regarding the proposed acquisition is that the new company’s culture will be too different to effectively mesh the two companies together. Further, it is your belief that the employees of the new company will feel trapped and constrained by your firm’s formalized structure. As you look over the acquisition proposal, the projections and possibilities are certainly appealing. If the acquisition becomes a success, your firm could stand to become the largest, most powerful communications firm in the industry. Tomorrow morning, you and four others will vote to move ahead or abandon the proposed acquisition.

Questions
1. How will you vote and why?
2. If you vote to pursue the acquisition, what changes might you recommend to ensure that the acquisition and subsequent transition succeed?
3. If you vote to abandon the acquisition, what changes might you propose that (if accepted by the group) would change your mind regarding pursuing the acquisition?
Management Decisions

CULTURAL CHANGE: EVOLUTION OR REVOLUTION?
Tandem Computer makes “fault tolerant” computers guaranteed to keep working during power outages, natural disasters, and catastrophic computer glitches that would easily shut down standard computers. Since 1974, Tandem has sold its computers at high prices and high profit margins to stock exchanges, phone companies, banks, airlines, and other companies whose businesses are dependent on uninterrupted computer service. Tandem computers are used in 75 percent of all ATM transactions, 66 percent of all credit card transactions, and 70 percent of electronic interchange networks (data sharing between companies).

Jimmy Treybig, Tandem’s CEO, founded the company with $1.5 million in venture capital money from Thomas Perkins, who chairs Tandem’s board of directors. That $1.5 million investment grew into a company with $3.1 billion in annual revenues. During its 20-year run of success, Treybig developed a patriarchal culture at Tandem. Once a week, at every Tandem facility, there was a “beer bust.” Attendance wasn’t mandatory, but most people wanted to attend. The point: not to promote drinking, but to get to know each other better and encourage informal communication, which is often lacking in corporate environments. Treybig’s stated management philosophy was that
(1) all people are good;
(2) workers, management, and company are all the same thing;
(3) every single person in the company must understand the essence of the business;
(4) every employee must benefit from the company’s success;
(5) you must create an environment where all the above can happen. (Ward, 1995)

One symbol of this philosophy was that Tandem’s sales representatives had one of the most generous compensation plans in the industry, earning $150,000 to $600,000 a year. In all, CEO Treybig was well liked and ran the company like an extended family.

Unfortunately, the party ended a few years ago. Customers began refusing to pay premium prices for Tandem’s computers, especially since they used Tandem’s proprietary software, Guardian, which was not compatible with other kinds of computers. In just three years, profits, which had been running between $150 million and $300 million annually, dropped to a loss of more than $750 million. Customers wanted Tandem to produce computers that run UNIX, an “open” operating system that runs on different kinds of computers, unlike Guardian, which runs only on Tandem computers.

The company’s struggles have not only affected profits, but have also begun to affect Tandem’s organizational culture. Said CEO Treybig, “Nothing is as fun as it used to be. My wife says I never use the word ‘fun’ anymore. In the 1980s you could just do a good job and make money. But nowadays, you have to be the best. I mean, every day you have to really worry about being successful. The bar for success is higher. It takes fun out of it” (Ward, 1995).

Questions
1. At critical times like this, CEOs have two basic choices: evolutionary change or revolutionary change. Explain which would be the best choice for returning Tandem to profitability. Why?
2. Either approach will affect Tandem’s family-like culture. Depending on which you chose, explain three ways in which a company like Tandem could incrementally change its culture or change its culture in a revolutionary way.

DEALING WITH THE PRESS
In this age of 24-hour cable news channels, tabloid news shows, and aggressive local and national news reporters intent on exposing corporate wrong-doing, one of the most important skills for a manager to learn is how to deal effectively with the press. Test your ability to deal effectively with the press by putting yourself in the following situation. To make the situation more realistic, read each scenario and then give yourself two minutes to write a response to each question.

Fatty Restaurant Food Contributes to Heart Attacks
Today, in the nation’s capital, a public-interest group held a press conference to release the results of a study that found that the food sold in most Chinese restaurants is high in fat. The group claims that the most popular Chinese dishes, such as orange chicken, pork fried rice, and Hunan beef, contain nearly as much fat as the food you get from fast-food chains such as McDonald’s, Wendy’s, and Burger King. (Much of it is fried or is covered with heavy sauces.) Furthermore, the group says that customers who hope to keep their cholesterol and blood pressure low by eating Chinese food are just fooling themselves.

A TV reporter from Channel 5 called your Szechuan-style Chinese restaurant, Szechuan, to get your response to this study. When she and the camera crew arrived, she asked you the following questions. (To simulate these conditions, give yourself only two minutes to write a response to each question.)
1. “A new study released today claims that food sold in Chinese restaurants is on average nearly as fattening as that sold at fast-food restaurants. How healthy is the food that you serve at Szechuan’s?”

2. “Get the camera in close here [camera closes in to get the shot] because I want the audience at home to see that you don’t provide any information on your menu about calories, calories from fat, or cholesterol. Without this information [camera pulls back to get a picture of you and the reporter], how can your customers know that the food that you serve is healthy for them?”

3. “These new studies were based on lunches and dinners sampled from Chinese restaurants across the country. A local company, Huntington Labs, has agreed to test foods from local restaurants so that we can provide accurate information to our viewers. Would you agree to let us sample the main dishes in your restaurant to test the level of calories, calories from fat, and cholesterol? Furthermore, can we take the cameras into your restaurant, so that we can get your customers’ reactions to these studies?”

Discussion Questions

1. Universities and colleges have elements of culture that are shared and some elements that are unique to each university or college. Thinking of your university or college, what elements of its culture are shared with other universities or colleges and which are unique?

2. Punctuated equilibrium theory states that industries go through alternating periods of stability and change. Identify an industry that has been relatively stable which is now being transformed by a change in the external environment. What caused the change and what are the likely consequences of the change?

3. Uncertainty refers to how well managers can understand or predict the external changes and trends affecting their businesses. Name an organization that faces a low level of uncertainty and explain why it has a low level of uncertainty. Name an organization that faces a high level of uncertainty and explain why it has a high level of uncertainty. What could it do to reduce the level of uncertainty it faces?

4. Advocacy groups are groups of concerned citizens who band together to try to influence the business practices of specific industries, businesses, and professions. Identify an advocacy group and provide examples of activities they undertake to communicate their position. Do you think their activities are effective? Why or why not?

5. Give an example of an attempted product boycott. Which group(s) initiated the boycott and why? Was the boycott effective? Why or why not? How did the company that was boycotted respond and was the response effective?
Biz Flix
Brazil

Set somewhere in the twentieth century, the retro-futuristic world of Brazil is a gritty, urban cesspool patched over with cosmetic surgery and “designer ducts for your discriminating taste.” Automation pervades every facet of life from the toaster and coffee machine to doorways, but paperwork, inefficiency, and mechanical failures are the rule. Brazil stars Jonathan Pryce in the role of Sam, a low-level bureaucrat whose primary interests in life are his vivid dream fantasies to the tune of “Brazil,” a 1940s big-band hit. In this scene, Sam is starting a new job and is being assigned an office and employee identification number.

What to Watch for and Ask Yourself
1. Describe the culture at Sam's new employer.
2. How easy would it be to change the culture at Sam's new company?
3. In which kind of business environment do you think the culture at Sam's employer is able to operate most successfully?

Management Workplace
Boston Duck Tours

After a bus tour of the United States that passed through Memphis, Andy Wilson was inspired to create a unique tourism company in Boston. Even though he had a great idea, enlisted the aid of a consultant to prepare a solid business plan, and cultivated a source for the technology he needed, Andy still faced challenges in the external environment. Nonetheless, he preserved and created Boston Duck Tours, the number one tourist attraction in the state of Massachusetts.

What to Watch for and Ask Yourself
1. What components of the external business environment does Andy Wilson mention in the video?
2. How would you characterize Andy's relationship with Bob McDowell?
3. Outline the external environment of Boston Duck Tours.
4. How would you describe the culture of Boston Duck Tours?