

## The past and future of global organizations

Wouter Aghina, Aaron De Smet, and Suzanne Heywood

After more than 50 years of trying, the search for an ideal model of the global organization remains elusive. But intriguing new experiments are under way.

**Consider if you will the following quotations**, each from executives at Philips, the global technology company—one in the late 1970s and one quite recently:

1. “We typically lose out when a market commoditizes and we no longer differentiate, further aggravated by us being too slow or expensive.”<sup>1</sup>
2. “The matrix is too slow—we are in a very turbulent market with great potential, and we have far too many low-cost competitors. We need very short communication lines, quick decisions, alertness—we’ve got to be able to adapt fast.”<sup>2</sup>

The first statement, from current chairman and CEO Frans van Houten, is the new one; it appeared in a 2013 working paper from the MIT Center for Information Systems Research. The second, older statement, from a Philips product manager, initially appeared in a 1978 *Management Today* article and was quoted by Tom Peters in his first *McKinsey Quarterly* piece, “Beyond the matrix organization.”

<sup>1</sup> Martin Mocker, Jeanne W. Ross, and Eric van Heck, “Transforming Royal Philips: Seeking local relevance while leveraging global scale,” MIT Center for Information Systems Research, MIT Sloan School of Management, Working Paper 394, February 27, 2014.

<sup>2</sup> Tom Peters, “Beyond the matrix organization,” *McKinsey Quarterly*, 1979 Number 3, mckinsey.com.

The similarity of these statements, from thoughtful leaders at a well-run company, speaks to the difficulty of the global corporation's perennial challenge: how to capture scale across borders while differentiating products and services to suit the needs of local customers—all without letting complexity get in the way of speed and agility.

Aspects of this persistent challenge have played out over the years in recurring fashion in major corporations, in the marketplace for management ideas, and in the *Quarterly*. Surveying the range of heroic efforts by great practitioners and thinkers to solve these challenges once and for all, you come away convinced that there is no silver bullet to the global company's challenge. Indeed, faith in one-dimensional solutions—redrawing organizational boundaries, constructing matrices, winning the war for local talent, reengineering business processes, moving the global headquarters—is arguably dangerous. The fact is that solutions need to combine changes across organizational structures, people, and processes.

We recognize that the absence of a simple solution may not be entirely satisfying and defies the impulse to fix everything at once through a single “big bang” change to one of these elements. But we think that's more realistic, too. We also believe that, within this mix, a focus on processes is taking on greater importance—not in place of people and structure but as a means of influencing them. Thanks to digital technologies, the growing connectivity between knowledge workers, and the more collaborative organizational behavior this connectivity supports, ours is a time of significant process innovation both inside and across corporate boundaries. These process innovations may provide new ways forward in dealing with the persistent difficulties of managing complex global organizations and meeting the urgent need for greater efficiency in the face of rising global competition.

## **The evolving organizational challenge: A brief tour**

In 1959, five years before the birth of *McKinsey Quarterly*, an ambitiously titled article appeared in the *Harvard Business Review*:

“Creating a *world* enterprise.” Written by McKinsey’s Gilbert H. Clee and Alfred di Scipio, it made the radical proposal (radical, at least, for its day) that expansionist American corporations, instead of treating international activities as subdivisions of their domestic businesses, should turn the US organization into a subdivision of the wider global one.

The Clee and di Scipio article, calling as it did for “major revisions in business thinking,” was pertinent as well as provocative. In the late 1950s, after all—with the reconstruction of Europe well under way after World War II and new industrial forces stirring in Asia—growing numbers of North American executives were eyeing overseas pastures for the first time. Faced with economic pressures and foreign competition at home, and lured by bright prospects abroad, a majority of representative executives questioned in a McKinsey survey of the time (and cited by Clee and di Scipio) reported that these companies were actively stepping up the ratio of their foreign-to-domestic investments.

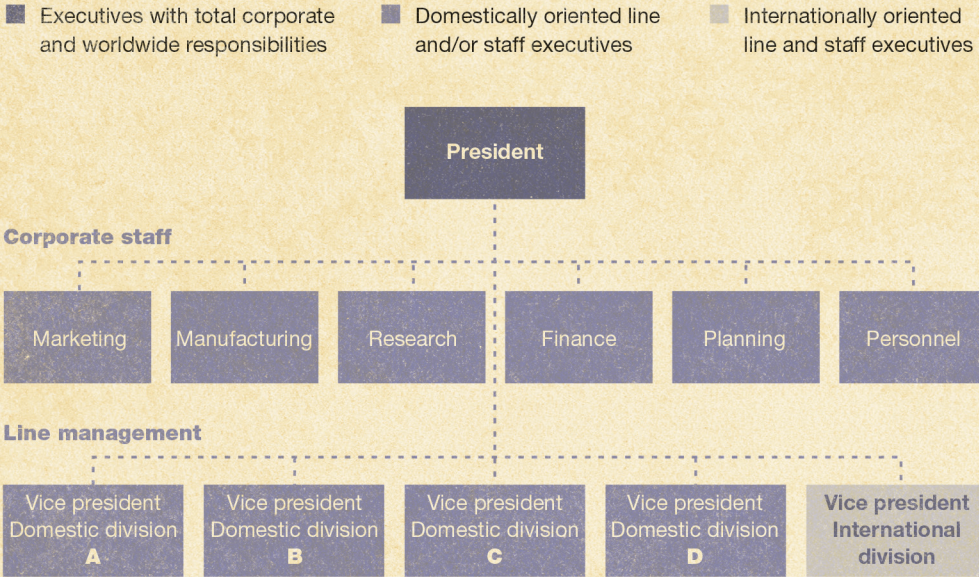
Opening such profit opportunities beyond their borders, though, created new planning, resource-allocation, and management-control issues, as well as unprecedented organizational strains. Old structures and relationships that had worked smoothly for an export-oriented domestic company were no longer appropriate as global engagement increased.

In many ways, that organizational response is the story of multinational enterprises over the past 50 and more years. In a 1965 article<sup>3</sup> featured in the *Quarterly*’s third-ever issue, Clee and McKinsey consultant Wilbur Sachtjen set out some evolving organizational patterns for global companies. There were several such models. The traditional international-division structure and its variants (Exhibit 1) all involved a shift in responsibility for policy and worldwide strategic planning to the corporate center. Then the international division was replaced by subsidiaries in assigned geographic areas, run by locally based senior line managers bearing full operating responsibility, notably in production and sales. Next, product-based and business-based structures replaced the international division with units run by senior line managers bearing worldwide responsibility for the P&L of their divisions.

<sup>3</sup> Gilbert H. Clee and Wilbur Sachtjen, “Organizing a worldwide business,” *McKinsey Quarterly*, 1965 Number 3.

## Exhibit 1

**In 1965, this exhibit from a *McKinsey Quarterly* article showed how international operations were often treated as an afterthought.**



Source: Gilbert H. Clee and Wilbur Sachtjen, "Organizing a worldwide business," *McKinsey Quarterly*, 1965 Number 3

Some of these approaches, particularly the last one, contained the seeds of the matrix organization, which gained favor in the 1970s as a solution for large organizations struggling to coordinate decision making and activities that cut across functional and business-unit lines. The theory was strong, but when Tom Peters appraised the scene, in the late 1970s, "the matrix 'solution' had brought with it problems at least as knotty as those it was supposed to cure."<sup>4</sup>

The quest for an alternative led Peters, Julien Phillips, and Bob Waterman to assert that "Structure is not organization" (as another of their *Quarterly* articles in that period was titled) and McKinsey to develop the 7-S framework of organizational effectiveness and change. Interestingly, four of the seven (skills, staff, style, and shared values) pertain to people, one (systems) to processes, and one to

<sup>4</sup> Tom Peters, "Beyond the matrix organization," *McKinsey Quarterly*, 1979 Number 3, [mckinsey.com](http://mckinsey.com).

structure. The seventh, strategy, spoke to the important and still-relevant idea, first articulated by Alfred Chandler in his 1962 book, *Strategy and Structure*, that the structure of an organization can be designed only after it has formed its strategy. The underlying focus of the 7-S framework on structure, people, and processes still represents a useful summary of the challenges in global organizational design today. In our experience, corporate leaders devote most attention to the first two and probably not enough to the third—even though processes can greatly influence both structure and talent.

Processes admittedly came to the fore during the business-process reengineering movement of the 1990s, which involved “rethinking and, if necessary, fundamentally reengineering how a company delivers value to its customers.” Such a rethinking, according to a 1993 *Quarterly* article, “inevitably runs up against the company’s entrenched business system and organizational structure,” requiring process redesign to “help managers break through these barriers.”<sup>5</sup> For large, complex organizations, taking a clean-sheet approach to processes rather than automating existing ones as information technology advanced was a sensible step. But it was far from sufficient to ensure a smoothly humming, healthy organization.

Continued advances in technology and connectivity have allowed companies to push well past process reengineering to new forms of engagement within and across organizational boundaries. Social networks are an obvious element of this development. But even before the full flowering of Facebook (and its equivalents behind corporate firewalls), McKinsey’s Lowell Bryan, in a 2007 *Quarterly* article, asserted that “in the digital age, there is no better use of a CEO’s time and energy than making organizations work better.” In his view, that involved “remaking the organization to mobilize the mind power of the workforce and tap into its underutilized talents, knowledge, relationships, and skills.”<sup>6</sup> Companies have begun realizing this vision by crowdsourcing ideas and holding “values jams,” as IBM famously did. They have even been throwing open the strategy

<sup>5</sup> See John Browning, “The power of process redesign,” *McKinsey Quarterly*, 1993 Number 1.

<sup>6</sup> See Lowell Bryan and Claudia Joyce, “Better strategy through organizational design,” *McKinsey Quarterly*, 2007 Number 2.

process “to enhance the quality of dialogue, improve decision making, and boost organizational alignment,” as Arne Gast and Michele Zanini wrote in a 2012 *Quarterly* article.<sup>7</sup>

## **As the world turns**

We survey this scene with respect both for the continually shifting nature of organizational opportunities and challenges and for the relentless efforts of leading companies and management minds to respond to them. Large global companies are often beset by complex structures and country-specific processes that proliferated over years of geographic expansion, not to mention cultural differences that can undermine smooth operations. By necessity, these companies have been at the forefront of formulating those responses, even if, at times, only by assimilating the innovations of smaller, more swiftly moving companies. Despite these efforts, high-performing global companies consistently score lower than more locally focused ones on several critical dimensions of organizational health, according to a decade-long study—of hundreds of businesses—that we highlighted in a 2011 *Quarterly* article.<sup>8</sup> These critical dimensions include direction setting, coordination and control, innovation, and external orientation.

Our research and experience suggest that the existence and persistence of a “globalization penalty” isn’t just a function of today’s context, typified by rapid growth in emerging markets and technological change. It also reflects the continuation of a journey that global organizations have been on for many years. Continually remaking the organization to embrace change is a messy endeavor—and one that’s likely, at any given time, to be accompanied by growing pains.

If that’s true, there’s no substitute for fairly regular soul searching to adapt structures, people, and processes to create the most effective organizational designs (Exhibit 2). Experimentation continues along

<sup>7</sup> See Arne Gast and Michele Zanini, “The social side of strategy,” *McKinsey Quarterly*, May 2012, mckinsey.com.

<sup>8</sup> See Martin Dewhurst, Jonathan Harris, and Suzanne Heywood, “Understanding your ‘globalization penalty,’” *McKinsey Quarterly*, July 2011, mckinsey.com.

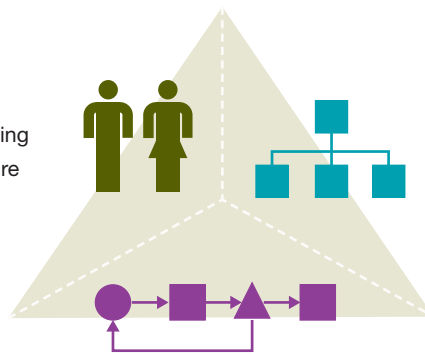
each of these dimensions. L'Oréal has emphasized its people credentials by establishing itself as the top employer for female sales and marketing talent in South Korea through a conscious emphasis on empowerment, communication style, and manageable working hours. Philips has recently identified three core processes—idea to market, market to order, and order to cash—it uses to create standard models for the products, services, software, and systems that flow through most of its global operations. Although standardization has

Exhibit 2

**There's no substitute for regularly revisiting how to adapt structures, people, and processes to create the most effective organizational design.**

### People

- Leadership
- Skills
- Workforce planning
- Values and culture



### Structure

- Reporting lines
- Roles and accountabilities
- Governance structures
- Geographic footprint
- Partnerships

### Processes

- Decision making
- End-to-end business processes
- Cross-functional linkages
- Performance and knowledge-management systems

### Ask yourself ...

Does the composition of our leadership group—and our talent proposition—adequately reflect our aspirations in high-growth markets?

Are we doing enough to help our people build skills to differentiate themselves from increasingly intelligent machines?

How can we use social networks to speed up cross-border and cross-functional processes?

Which processes do we want to standardize (using, say, industry standards) and which do we want to differentiate?

How much of our structure can be virtual?

How can technology help relocate key functions to optimize our talent, engagement with customers, and cost advantages in emerging markets?

been imposed on these core processes, exceptions are permitted, and the idea is to drive greater speed and flexibility, more localization, and higher efficiency simultaneously.<sup>9</sup>

Experiments like Philips's point toward more process-oriented structures, which are likely to become increasingly useful given the power of technology and connectivity to transcend traditional boundaries both within and across companies. Process improvements today can go beyond the cost-oriented "denominator" of corporate productivity to embrace the "numerator" of learning-based performance-enhancement networks and spaces where innovation and growth occur.

The possibilities are particularly alluring for large global organizations, where these process-oriented structures can help harness the specialized capabilities of a distributed network of business partners. In the apparel industry, for instance, Li & Fung has organized and coordinated a fully fledged supply network of more than 10,000 business partners.<sup>10</sup> The flexible scalability of this network, which uses processes to address the structural aspects of organizational design, speaks to the global corporation's long-standing difficulty in coordinating complex and far-flung production operations.

These distributed process structures are proving powerful *inside* companies, as well—for instance, by bringing diverse participants into the strategy-creation process. For example, in 2009, 3M reinvigorated its Markets of the Future process, which provides critical input to its strategic planning. The company's crowdsourcing of the strategy process to more than 1,200 employees in 40 countries helped energize creative talent—the people side of the organizational-design conundrum—while identifying nine new future markets with an aggregate revenue potential in the tens of billions of dollars.

Similarly, learning environments where teams of participants interact with other teams around sets of processes designed to enhance performance not only help solve difficult operational challenges but also enable employees to continue the learning and

<sup>9</sup> See Mocker, Ross, and van Heck, "Transforming Royal Philips: Seeking local relevance while leveraging global scale," 2014.

<sup>10</sup> F. Warren McFarlan, Michael Shih-ta Chen, and Keith Chi-ho Wong, "Li & Fung 2012," Harvard Business School Case 312-102, January 2012.

development that create meaning in their professional lives. Consider, for example, how the software company SAP drew together participants from a wide range of otherwise unrelated companies, in 2003, to help speed the adoption of its new NetWeaver technology architecture. The processes in this network structure supported peer-to-peer collaboration and learning among customers, systems integrators, and independent service vendors, while helping SAP to achieve its own strategic objectives. These newfangled process-oriented solutions to the structure and people part of the perennial organizational challenges contrast—and yet coexist—nicely with the more traditionally standardized routines, which remain suitable for wringing scale-based cost efficiencies from less varying (and often industrial) processes. The trick is to recognize which process-based structure is best for which objective and then to proceed accordingly.

We're starting to see glimmers of global organizational redesign reflecting these new realities. One international engineering company, for example, has restructured to put its commercial-project process (including decisions about whether to bid on a contract and then the preparation of the offer) at the heart of the organizational structure. This model enables more effective team-based problem solving that transcends organizational silos and geographic boundaries, in part through the use of collaborative technologies.

It's still too early to paint a definitive picture of what the global organization of the future will look like as efforts like these become more commonplace. What we're confident about is that "process-centric" thinking will be a more prominent feature of organization design than it has been in the past, even if the peculiarities of culture suggest that each process-based structure is likely to be a custom fit. Leaders should bear in mind these principles as they pursue their own solutions:

- Tomorrow's answer will be different from today's. As markets, competitors, and strategies evolve, so will the structural, people, and process elements of a coherent design system.
- The specification of globally consistent roles and processes should be kept to a minimum. The most effective companies allow business units to tailor their organizations to local conditions so as to better achieve their wider commercial goals.

- Technology has made location less important than it used to be— but it still matters. While videoconferencing and social media keep far-flung executives connected, co-location brings additional benefits. Companies should always seek ways to bring people physically together.

If the last 50 years are any guide, the most important organizational structure, process, and people issues will continue to ebb and flow as the environment evolves and organizations respond. But new opportunities for organizational innovation will present themselves, and those companies able to recognize and willing to embrace them will gain huge competitive advantage by doing so. ◉

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**Wouter Aghina** is a principal in McKinsey's Amsterdam office, **Aaron De Smet** is a principal in the Houston office, and **Suzanne Heywood** is a director in the London office.