Section 3.6 Managing change

22 Causes and effects of change

Definition

Change is a constant feature of business activity. The key issues are whether it has been foreseen by the company – and therefore planned for – and whether it is within the company's control.

Linked to: Impact of external influences, Ch 5; Growth, Ch 7; Mergers and takeovers, Ch 9; Reasons for staying small, Ch 10; Key factors in change, Ch 23; Scenario planning, Ch 24

22.1 The value of change

No one should doubt that most businesses, like most people, hate change. Just try persuading football supporters that it's time for a new home ground, or children that it's time to try a new type of food. So most business leaders drool over:

- Coca-Cola, born 125 years' ago, but still with 2015 retail sales of £1,154 million in the UK alone
- Cadbury's Dairy Milk, more than 100 years' old and with 2015 sales of £486 million in the UK.

Businesspeople value lack of change, because it makes it easier to hang on to strong profits. For the consumer, though, change has potentially huge benefits. Although we may want Cadbury's Dairy Milk unchanged, we benefit hugely when online retailers force shops to push prices down, or when Netflix starts paying for its own, high-quality programming – to draw in more subscribers.

And when change comes, managements have to rethink their whole operation, to figure out how to be more efficient while simultaneously offering exciting new products or services to customers. It's at that point that change can be of value to many stakeholders: customers, shareholders, managers and perhaps the environment as well.

22.2 Internal and external causes of change

Change arises as a result of various internal and external causes. The internal ones (such as a change in objectives) should at least be planned for. External causes may be unexpected, which makes them far harder to manage. Table 22.1 sets out some possible internal and external causes of change.

Internal causes	External causes
• Changes in organisational size • Poor business performance • New ownership • Transformational leadership	• Changes in the market • Political • Economic • Social • Technological • Legal • Environmental

Table 22.1 Examples of internal and external causes of change

22.3 Internal causes of change

Changes in organisational size

Whether a business expands or contracts, there will be pressures for change to the organisational structure and to the balance between spending for growth (R&D, new technology, new capacity) and spending for survival (labour-saving capital spending, redundancy payments). In either case, the impact on the business is short-term disruption that, if mishandled, can damage long-term relationships within the business – especially those between management and staff.

Whenever management hierarchies are reorganised, there are winners and losers. At a time of growth, creating new horizontal management layers will be necessary to prevent spans of control getting too wide. But with every promotion opportunity there will be staff members who get passed over – and feel unfairly treated. Some will then harbour suspicions of discrimination or favouritism – and of course they may be right. If **downsizing** is needed, the implications are still worse, with people actually being selected for redundancy (an embittering process) and others left behind, wondering whether they may be next to go.

Handling this process well is a huge test of leadership skill. At the time of writing, new Morrisons boss David Potts seems to have been able to make redundancies to senior and middle management in ways that have impressed shop floor staff. Very clever.

Poor business performance

In most modern boardrooms, the chief executive is judged by whether agreed objectives have been achieved. In early 2014, the boss of Whitbread plc announced that his Costa Coffee division would be expanding its number of coffee bars in China from 300 to 700 by 2017. If, by late 2016, it becomes clear that this objective will not be achieved, the directors will ask serious questions. From this may come a demand for change. Either that change will be at the top, or the chief executive must be able to explain why the disappointment happened and what will be done to prevent a recurrence. Ultimately, the job of the directors is to make sure that poor performance is never tolerated.

New ownership

Business is unpredictable because different people make different decisions based on the same evidence. So if ownership changes, policies can change – even if things were going well before. This is especially likely when the reason behind a takeover was strategic. In July 2015, German rivals BMW, Mercedes and Audi (VW) together paid £2 billion for Nokia's digital mapping business (called 'Here'). They did it to seize control of car navigation software that had been included in 80 per cent of new cars sold in Europe. In effect, it was an attempt to prevent newcomers such as Apple and Google from easily being able to develop their new driverless cars. Needless to say, the new ownership is likely to cause significant change to the internal operations of the business. Here employs 6,000 staff – they will doubtless find a huge amount of change as their new owners refocus the business on the development needs of the German luxury car market

Transformational leadership

A transformational leader can achieve change in a situation that others might find too difficult. After its 2015 election defeat, the Labour Party collapsed into squabbling. It needed a new vision, new policies and a clear focus on a defined but large section of the population. It desperately needed a transformational leader. As of August 2015, there was no sign!

When Indian-born Rajeev Suri became chief executive (CEO) at Nokia in 2014, he was taking over a business that had been humiliated in the smartphone market by Apple and Samsung. It had just given up on a market for which it was once the global number one. Since then Suri has transformed the Finnish company, but without needing large redundancy programmes.

A new approach by a transformational leader might require flattening a hierarchy to create more empowerment and generate more creative thinking – or it might be focused on finding new efficiencies to cut costs and improve competitiveness. Either way, there will be significant human and structural change.

22.4 External causes of change

Changes in the market

Market change can come about from a combination of business, economic and social factors. In the UK grocery market, a remarkable market share boom pushed discounters Aldi and Lidl to the forefront, creating a panicky price-cutting reaction from the other grocers. In Figure 22.1, contrast Morrisons' position in 2012 compared with Aldi and Lidl, then do the same for 2015. The impact of Aldi and Lidl on Morrisons was dramatic. Asda/Wal-mart might also be needing an urgent change in management strategy.

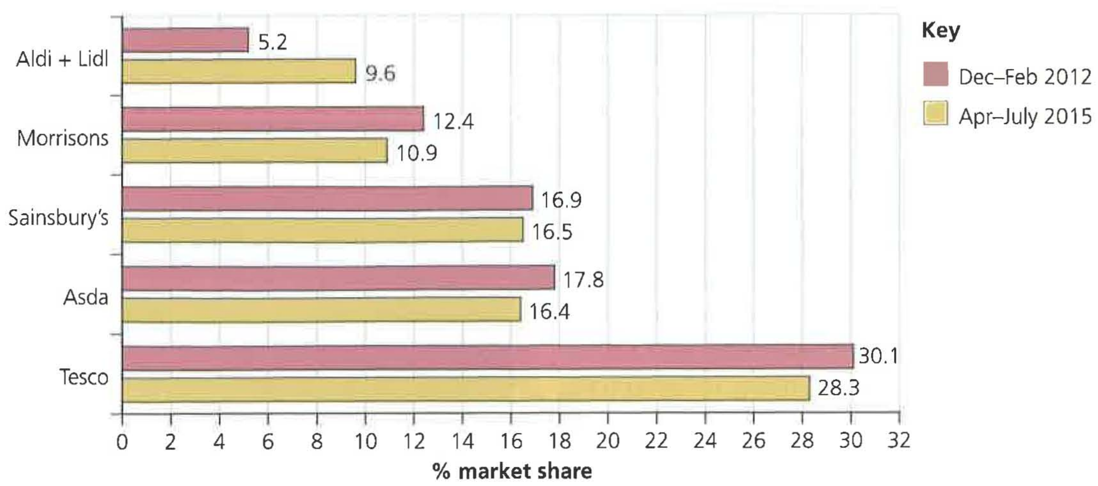


Figure 22.1 Grocery market transformation: booming Aldi and Lidl (source: Kantar Worldpanel)

'All great change in business has come from outside the firm, not from inside.'

Peter Drucker, business guru (1909–2005)

'Change is inevitable; except from vending machines'.

Anonymous

'When you play it too safe you're taking the biggest risk of your life.'

Barbara Sher, author

'It isn't the changes that do you in, it's the transition.'

Daniel Webster, US politician (1782–1852)

Political change

The Edexcel specification picks out the term **PESTLE** (covered more fully in Chapter 5) to indicate the value of seeing external influences from a broad perspective. Political change may impact mainly on business and market confidence. Although the Labour Party's election manifesto in 2015 was rather bland, businesspeople queued up to emphasise the threat they perceived from a potential Labour government. Some threatened to up and leave the country.

What is not in doubt is that business leaders care hugely about political outcomes. Businesses such as Virgin rely far more on the public sector than their publicity might suggest. Virgin Rail and Virgin Care are effectively outsourced government spending – and the Virgin Group's ability to use offshore tax minimisation techniques is a function of government policy towards business taxation.

Economic change

In 2015, with the economy growing at 2.5 per cent, companies and consumers felt quite confident about their future. Accordingly consumers spent 7.5 per cent more on their credit cards than in 2014. In the short term, businesses love to see consumers feeling flush; in the long run this has to be self-correcting. If people's spending outstrips their income (helped by debt), there has to be a cutback in future. This creates the familiar British cycle of confidence + debt = upturn, then faltering confidence + consumer spending cutbacks = downturn.

As economic growth varies through its cycle, businesspeople should be able to anticipate what might happen next, but the evidence is that they do not. When upturn becomes downturn there are always a number of companies caught out badly. Economic change is easily to rationalise with hindsight, but very difficult to anticipate.

Social change

Despite sustained media focus on diet and body shape, the biggest trend by far in consumer lifestyles is the desire for greater convenience. We want to spend less time cooking and less time eating. So breakfast cereals are in decline because we'd rather eat a snack bar, and retail bread sales are down because we'd rather buy a sandwich. That's good for Greggs and Prêt à Manger, but bad for Hovis and Kelloggs.

The key management skill, therefore, is to understand the consumers' reasoning and then refocus the business on the new social impetus. Apple understands the mobile phone user; Marks & Spencer understands food shoppers; underperforming businesses such as French Connection, Tesco and Nestlé UK need to retune to modern social wavelengths.

Technological change

It is easy to think of the modern era as the most significant ever in terms of technological change and its impact on society and businesses. In fact, a strong case could be made for steam/the railways, oil/the car and the arrival of electricity. The key is to appreciate that technological change may come in waves, but it's always there, creating havoc for businesses that get complacent. In recent years a series of companies have been caught out by online selling, including Game, HMV, Marks & Spencer and Morrisons. Today, virtually every business talks about a multi-channel strategy – in other words making sure that they are as equipped for e-commerce and social media as they are for traditional distribution and traditional media.

Legal change

When parliament passes new laws, the impact on business can be immediate, such as the boom in crash helmet sales when motorbike riders were forced to wear one at all times. At other times, the warning period for a legal change is sufficient to allow extensive planning. Within the European Union, all car manufacturers had to ensure that their 'fleet average' yielded a maximum CO_2 level of 130 grams per kilometre by 2015. By 2021 the figure comes down to 95 grams. So producers have made CO_2 reduction a priority for their Research and Development teams.

Environmental change

As with technological change, historical perspective is crucial here. For the UK, the environmental change between the mid-nineteenth century and the mid-twentieth century far outweighs anything that hits headlines today. In 1851, male life expectancy was about 40; by 1951 it was 67. Life had largely moved on from constant pollution (in urban areas, anyway) to a much better-ordered life. Today there are real problems with diesel-based pollution in cities, but it's as nothing compared with years ago.

Companies often marvel at the irrational approach consumers take to environmental factors. Ultimately, though, companies can do no more than to reflect their customers' concerns. Sadly, these tend to be short-lived. One year 'food miles' is all-important; the next it's sustainability – then natural ingredients.

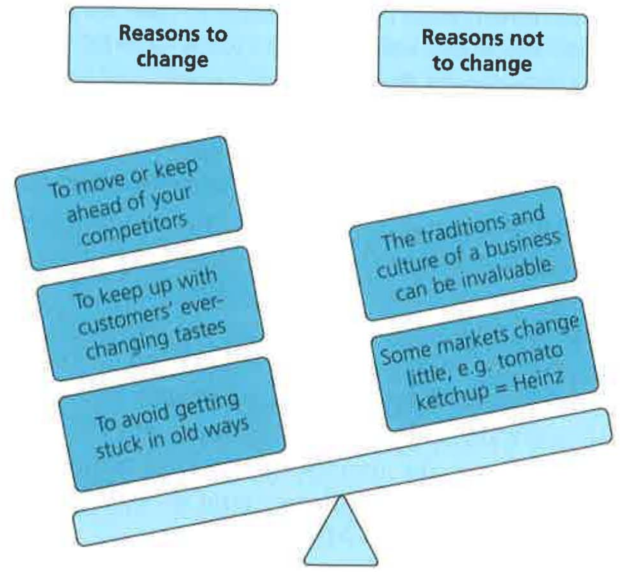


Figure 22.2 Reasons to change (or not to)

22.5 Possible effects of change

Effect of change on competitiveness

It would be very rare to have a business where competitiveness can survive unless changes are made. Let us take the example of Morgan Cars, where traditional British sports car motoring is the key source of differentiation and value added. Customers want a retro product, such as the Morgan Plus 4, which was introduced in 1950. Nevertheless modern customers don't complain if there's a heater in the car, or if the company has introduced new production techniques. Today Morgan produces 20 cars per week at its Worcestershire factory. Customers get a tailor-made car and are encouraged to come and see it being made. Even at Morgan, though, some change is needed.

Figure 22.3 Manufacturing at Morgan

For some businesses, radical change is the only way to catch up with competitors. Rolls-Royce Aero Engines is a world leader, but is unable to achieve the profitability of its key US competitor General Electric. Although the design of the Rolls-Royce engines is super high-tech, the production process remains labour-intensive – effectively job production. The company needs to change its working practices to become competitive with General Electric. Just such a change is slow coming, however. In Spring 2015, chief executive John Rishton was replaced, with the new boss recruited from ARM – a hugely successful British software business. Perhaps new boss Warren East will achieve the desired change and restore the competitiveness of Rolls-Royce (and secure the jobs of many staff in the East Midlands).

Competitiveness can be achieved in one of two ways:

- cost minimisation, i.e. changing the ways of working to squeeze all surplus costs out of the business and thereby become a Ryanair, a Primark or an Aldi
- high differentiation, i.e. mark yourself out as distinctly different from your rivals, in a way that adds value, such as BMW, Apple, Singapore Airlines and Galaxy chocolate.

Change must therefore be focused clearly on one (not both) of these positions in the market.

Effect of change on productivity

If you produce a middle-market car such as the Ford Focus with a labour productivity score of 24 cars per worker per year while your competitors achieve 36, you have a real problem. OK, if you produce those cars in Romania with wages of £60 a week, the low productivity matters less. But assuming that you produce them in Western Europe with wages of £400 a week, you need to make a change.

It may be that productivity can be improved by investing in automated systems, but it's important to remember that only 10 per cent of the British economy is based on manufacturing. So most firms are in the service sector. To boost productivity in services can be difficult, as indicated by Figure 22.4. It shows the extraordinarily flat productivity path for UK services between 2010 and 2015.

Realistically, boosting productivity in the service sector is likely to require a huge upheaval in workplace attitudes. Manufacturing companies learned from the Japanese that 'kaizen' (continuous improvement) requires the full commitment of staff to making things steadily more efficient. This change is required in service sector organisations in the public and private sectors if overall UK productivity is to rise significantly.

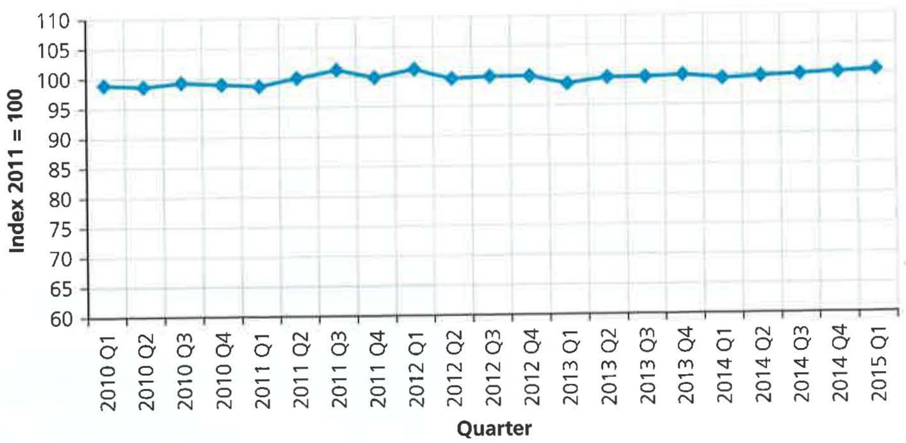


Figure 22.4 UK service sector productivity (source: ONS)

Effect of change on financial performance

Achieving major change can mean short-term pain for long-term gain. This is likely to be reflected in financial performance. In 2014 and 2015, Morrisons tried to reconfigure itself, with strategic moves into urban convenience stores and also online shopping, plus the removal of a layer of management in-store. In addition, when new boss David Potts arrived in 2015, the business hacked into its senior management ranks, cutting 700 head office jobs – and also initiated some serious price cuts. The full effects of the decisions made by David Potts won't be seen until the 2015/2016 figures, but already Table 22.2 is able to reflect the dramatic short-term pain felt by the supermarket chain. It has two problems: the decline in the underlying profitability of the business (that's what David Potts is really trying to tackle) and the short-term financial difficulty caused by huge one-off (exceptional) items. These are the effects of closing down under-performing stores, and cancelling contracts on new stores that are no longer going ahead.

As can be seen, change management can have a severe impact on short-term financial performance. But as long as the long-term problems are solved, no one will mind.

	2012/2013	2013/2014	2014/2015
Turnover	£18,116m	£17,680m	£16,816m
Gross profit	£1,206m	£1,074m	£761m
Underlying pre-tax profit	£880m	£719m	£345m
Exceptional items	***(£1m)***	***(£895m)***	***(£1137m)***
Effective pre-tax profit	£879m	***(£176m)***	***(£792m)***

Table 22.2 Morrisons revenues and profit at a time of change, 2013–2015 (source: Data from Morrisons accounts)

Effect of change on stakeholders

In the case of Morrisons, not only were the shareholders hit by the collapse into a lossmaking position in 2014 and 2015, employees also suffered as staff numbers fell by 9,000 between 2013 and 2015. Much of this reduction in staffing would have been achieved by non-replacement of staff (rather than actual redundancies) but there can still be negative impacts if staff find themselves over-stretched once a colleague has left.

Change can also have a devastating effect on suppliers. Tesco, as part of its turnaround strategy, chose to cut back on the number of suppliers. This is to ensure buying in greater bulk from fewer suppliers, thereby getting purchasing costs down (to compete more effectively with Aldi and Lidl). Horribly caught out by this in 2015 was the huge bakery Kingsmill, which was dumped by Tesco in favour of Hovis and Warburtons. Kingsmill stood to lose about £100 million of annual sales.

Another key stakeholder is the customer, and here change can also be significant. Spare a thought for elderly residents in care homes closed down as part of a structural reorganisation in a private care home business or as part of a local authority's response to cutbacks in central government funding.

'Change is hard because people overestimate the value of what they have – and underestimate the value of what they may gain by giving that up.'

James Belasco and Ralph Stayer, authors

'Change is the law of life and those who look only to the past or present are certain to miss the future.'

John F. Kennedy, former US President

'If past history was all there was to the game, the richest people would be librarians.'

Warren Buffett, investor extraordinaire

'The entrepreneur always searches for change, responds to it, and exploits it as an opportunity.'

Peter Drucker, management academic and author

Five whys and a how

Questions	Answers
Why do plc bosses tend to blame poor results on external causes, but good results on internal causes?	Because external factors are outside the firm's control, whereas internal causes are down to the management.
Why is social change happening faster now than ever before?	Much of the answer to this is technology – a cynic might say we waste more time online and therefore demand more convenience; others see social media and online shopping as ways to give consumers more power.
Why is social change hard to predict?	Although experts try to read early signs of changes in social behaviour or lifestyle, it is impossible to accurately forecast the future.
Why do some businesses seem to be in a permanent process of change?	They may keep failing to get a satisfactory answer to their underlying problems, and therefore keep trying; many companies seek quick-fix solutions (such as new financial incentive programmes) and then find that little has changed.
Why may change hit shareholders less than other stakeholders?	Shareholders own the business and therefore have huge sway over management; so when change happens, it tends to be more focused on the long-term needs of shareholders (i.e. profit) than on staff, customers or suppliers.
How might a small business effect major internal change among staff?	The key will be whether the business leaders have discussed its problems well enough to convince all important staff members to get involved.

22.6 Causes and effects of change – an evaluation

Seasonal, competitive, economic and other causes of fluctuation make change a regular part of business planning and management. Some change factors are so predictable (the lead-up to Christmas for a supermarket) that they can be handled by middle or junior management. Others are more fundamental and game-changing, and therefore need a higher-level strategic plan, such as whether or not to build a third runway at Heathrow airport. Many successful businesses do not have a formal strategic planning process. This does not mean that the issues raised here are not relevant to these organisations. The same problems must be dealt with when strategy emerges over time as when it is planned more systematically. The advantage of explicitly setting aside time for strategic planning is that managers' minds are concentrated on the key questions facing the firm in the future. Then the actions decided upon can be more closely integrated.

Key terms

Downsizing: rethinking staffing numbers and the organisational structure needed given that sales revenue has fallen; often used as a euphemism for redundancies.

PESTLE: key external factors that impact on business objectives and achievements: Political, Economic, Social, Technological, Legal and Environmental.

22.7 Workbook

Revision questions

(30 marks; 30 minutes)

1 Distinguish between internal and external causes of growth, using examples. (5)

2 Explain how social change has affected businesses operating in the following markets in the UK over the last 20 years:
a) grocery retailing
b) restaurants
c) consumer electronics retailing. (12)

3 Outline one example of how a social change might:
a) create a brand new market
b) destroy an entire market. (4)

4 Explain why it may be hard for young, inexperienced managers of a successful business start-up to cope effectively with an unexpected, dramatic change. (5)

5 Explain one reason why change may be of value to an established grocery business. (4)

Revision exercises

Data response

You've had your chips: award-winning chippy closes doors

In 2011, Ian Shaw ditched his day job and set up his own fish and chip shop. Using £15,000 of his own money, Shaw rented a bakery in Rochdale, converted it and, in early 2012, The Best Cod in Town opened its doors for the first time. The chippy proved to be a hit with customers. Shaw's business model was based on selling a top-quality product at low prices. This meant buying in the best fish and changing the oil used for frying more often than usual.

Like many other entrepreneurs just starting out, Ian worked very long hours, which helped to boost sales and keep staff costs down. Most of Shaw's customers who tried his fish and chips liked them, and came back for more, becoming regulars. Thanks to its popularity, the chippy generated good revenues. At the end of its first year, The Best Cod in Town was ranked in first place by Trip Advisor as Rochdale's best takeaway. Despite its substantial turnover, the business struggled to make a profit. This was because fixed costs were too high, which created a high break-even point. The biggest fixed cost that he had to pay was business rates. Every month The Best Cod in Town had to pay Rochdale council £1,872. This was even higher than the £1,200 he paid per month in rent to lease the premises. When the council increased his rates again, and said it would do so in the following years, Shaw decided that there was no other option; the writing was on the wall: 'We had a break clause in our lease after 18 months and I've decided it's best to get out sooner rather than later.' The Best Cod in Town closed its doors for the final time in September 2013. At the time Shaw said:

'The town centre is dying. Unless you want a payday loan, a television on hire purchase or to go to a charity shop, there just isn't a reason for people to come into Rochdale. With the changes that are coming in to the benefits system later this year, people will have even less money to spend. We're the fourth business that is closing at this end of the high street and I can't see things getting any better.'

MP Simon Danczuk, Rochdale's MP, was critical of the government, arguing:

'This government does not care about people like Ian, they are only interested in big business. Small businesses like Ian's are the lifeblood of the economy and if we're going to have a proper recovery, then they need to be given a fighting chance of survival. Big business seems to get all the support and subsidies from the government and are being allowed to exploit tax loop holes. At the same time, smaller firms are getting bigger and bigger business rate bills.'

The biggest employer in the town is Rochdale Council. Due to government spending cuts, unemployment has soared and spending is sharply down. In December 2014, nearly a quarter of Rochdale's shops were vacant. The council reacted by offering new businesses that were prepared to move into an empty shop an 80 per cent discount on their business rates in the first year, and a 50 per cent cut in the second year.

Questions (50 marks; 60 minutes)

1 Assess two factors that would have affected the break-even output level of The Best Cod in Town. (8)

2 Assess how private businesses like The Best Cod in Town might benefit from government spending. (10)

3 When The Best Cod in Town made losses, Ian Shaw responded by closing down the business. Were there any other options? Assess Ian Shaw's decision to shut down his business. (12)

4 The Best Cod in Town's competitive advantage was based around selling a high-quality product at a low price. Evaluate whether this business model can deliver long-run, sustainable success. (20)

Extended writing

1 The soft drinks' company Fever-Tree has grown at a rate of 50 per cent per year for nearly a decade. Evaluate whether it's inevitable that this pressure for change will cause setbacks for the business. (20)

2 Evaluate the extent to which UK net migration represents an opportunity for UK supermarkets. (20)

Section 3.6 Managing change

23 Key factors in change

Definition

Change is a constant feature of business activity. The key issues are whether it has been foreseen by the company – and therefore planned for – and whether it is within the company's control.

Linked to: Impact of external influences, Ch 5; Growth, Ch 7; Corporate culture, Ch 16; Causes and effects of change, Ch 22; Scenario planning, Ch 24

23.1 Successful change

There's a tendency on the part of senior managers to see change as a good thing. It can be their way of stamping their authority on the organisation. It's important to bear in mind, therefore, that as many as 70 per cent of change management initiatives prove to be a flop. Big management reorganisations, or quality initiatives, or customer service response programmes – all are more likely to fade away than to achieve anything. Therefore it's terribly important to make sure of the following:

- All staff understand the need for change.
- All staff understand what the new, changed world is going to look like.
- All staff understand the plan for getting from A to B.

Academics Carolyn Aiken and Scott Keller say that fundamental human issues get in the way of successful change:

- What motivates leaders doesn't motivate most of their employees.
- Leaders believe mistakenly that they already are the change.
- Money is the most expensive way to motivate people.
- The process and the outcome have got to be fair.

This highlights that successful change management is about people – not technology or software systems. Therefore a business is much more likely to beat the 70 per cent flop figure if it has an underlying position of trust between bosses and staff.

Among the key factors in successful change are:

- organisational culture
- the size of the organisation
- the timing/speed of change
- managing resistance to change.

23.2 Organisational culture

When David Moyes succeeded Sir Alex Ferguson as boss of Manchester United, he brought in new players such as the giant Belgian Marouane Fellaini. Brought up on the talents of Ryan Giggs and Paul Scholes, the home crowd struggled to take to the Belgian's muscular style. The expectations and conventions within the Manchester United crowd represented their culture – and the crowd would feel (just as company staff do) that they represent the 'real' Manchester United/company. Managers (and players) come and go; the fans are the constant. And the culture within the fans has been built up over years, perhaps generations. Newcastle fans expect excitement and goals; Chelsea fans expect home wins and trophies; Manchester United fans expect all of those things. Clever managers of companies and football clubs try to work with the grain of the organisational culture – not against it.

Figure 23.1 Football clubs have their own culture

Real business

In January 2013, Barclays Bank's new boss Anthony Jenkins told staff to 'sign up to ethics or leave'. After at least a decade in which success at Barclays meant creating more profit (and bonus) than the next guy, suddenly the bank was to become ethically pure. Fast-forward to July 2015 and it was Anthony Jenkins leaving. The chairman sacked him in favour of a man with a more ruthless, profit-focused streak. Anthony Jenkins was working against the culture of the business – and failed to make it change. (Don't weep for Mr Jenkins; he is expected to clear £28 million as a leaving present.)

To achieve successful change in a business with a strong organisational culture:

- Make sure you really understand that culture (it may seem jokey and carefree, with a focus on Friday nights, but underneath be seriously committed to the success of the business).
- Work with it not against it.
- Use consultation to make sure that key figures from every part of the organisation are with you because they understand and trust you.
- But don't waver; people want a very clear lead; as the saying goes: 'indecision is final'.

23.3 Size of the organisation

Logically it should be much harder to change a big organisation than a small one. Oddly there's no evidence for this. Businesses (or organisations such as schools) employing perhaps 50–100 staff also find it's hugely difficult to achieve change. Ultimately, though, change is achieved successfully when the boss changes the hearts and minds of staff; and organisational size must matter.

In a large organisation, it'll be necessary to do the following:

- Rely on upward information from middle managers, as the boss will never be able to get a real feel for the views of 200,000 staff (Unilever) or 500,000 staff (Tesco).
- Find a compromise between the different views and needs of different parts of the business; a change to temporary or outsourced staff may be right in one division, but not in another.
- Rely on cascading, with senior managers explaining the changes to middle managers who, in turn, brief the next layer down; this will be time-consuming and expensive, but more important is that it is likely to be ineffective. A passionate chief executive explains the new vision and changes to senior managers, whose explanations to their juniors are slightly less powerful and accurate – and so on.
- And with every aspect of the change programme, there's a chance that the different business functions will fail to work together effectively.

For small organisations, change may also be challenging because of the following:

- The business may lack the financial resources to both finance the change and to withstand any short-term problems caused by the change.
- Small businesses are usually dominated by one person (or family). There may be too few independent voices to persuade the boss to change.
- Large firms have staff with a wide range of skills, making it easier to cope with new ways of working. Small business may lack that flexibility.

'Plus ça change, plus c'est la même chose.'

Jean-Baptiste Karr, French journalist (1849)

'Give employees the information they need to understand the reasons for change.'

Carla O'Dell, businesswoman

'I always loved change, something new. Change is a challenge, an excitement.'

Dawn Sibley, Executive Vice President

23.4 Time and speed of change

Most businesses can cope reasonably well when the pace of change is relatively slow. A slow pace of change is referred to as **incremental change**. From as early as 2005, John Lewis appreciated that its world was changing. From a purely physical ('bricks') high-street retailer it saw that more and more people wanted to purchase online. Perhaps they might want to go to a store to choose which sofa or which TV to buy, but they would find it easier to make the transaction via a 'click' at home. To the operation's great credit, it worked hard to create an easy-to-use e-commerce site and encouraged sales staff to see it as a complement, not a competitor to the stores. By 2015, with Marks & Spencer floundering in its wake, John Lewis was getting close to 30 per cent of all sales arising online, but with a clear strategy to open new stores within Britain to act as a shop window for the website.

This incremental change (steady and quite predictable) towards online shopping was intelligently managed by John Lewis, but botched by Marks & Spencer (and

Morrisons). Quite simply, with years to look ahead and plan for this incremental change, there can be no excuses for the management failures of those who woke up to find they had missed the boat.

By contrast, **disruptive change** typically occurs within a timescale that makes planning almost impossible. In 2009, two years after the launch of the iPhone, Nokia held a 38.9 per cent share of the global market for smartphones. Two years later, its share was 8.2 per cent and dropping like a stone. Looking back, one could point to the mistakes Nokia made; but it simply didn't have enough time to rethink the new world created by Apple (and Samsung). In the same timescale as Nokia's collapse, Samsung's global market share went from 3 per cent to 30 per cent.

The unusual aspect of Nokia's collapse was that the disruptive change came from Apple's marketing and design brilliance. Usually the causes of disruptive change are either technology or legislation, i.e. external to the business. Banning smoking in public places meant that pubs had to adapt quickly – or die. Many died. And the onset of online retailing finished off HMV, Blockbuster and Game retail chains.

The problem for businesses faced with dramatic change is that managers don't yet know the timescale and therefore do not know how disruptive a given change will be. When General Motors launched its 'Volt' electric car in 2010, it forecast sales of 60,000 cars by 2012. In fact sales struggled to reach 24,000 units. The company had thought electric cars were the disruptive technology that would sweep petrol-based cars aside. Not yet. Now, as it plans its 2016 Volt, General Motors is trying hard to dampen down sales expectations.

23.5 Managing resistance to change

Academics Kotter and Schlesinger have identified a series of methods for dealing with resistance to change. Generally a mixture of methods should be used. They should be selected by carefully considering the methods that are most appropriate given the nature of the workforce and the nature and speed of the change. They are explained below:

Education and communication

A highly effective method for breaking down resistance to change is to successfully explain the need for change before it is implemented. This is especially effective where resistance is the result of misunderstanding or a different assessment of the firm's position before the change. However, this method relies on a level of trust between management and staff if the communication is to be believed by the staff whose resistance is to be overcome. Large-scale presentations, or even corporate films, can be used to try to provide the information and education needed for staff. Exactly these methods were used by British Airways in its difficult struggle to change working practices at the airline.

Participation and involvement

Involving unofficial staff leaders in designing the how and why of the change can be an excellent method of breaking down resistance before it becomes entrenched. The change managers must listen carefully to the views of staff and try where possible to take these views into account. Kotter and Schlesinger report that some managers believe participation of staff is vital, whilst others feel that it is highly dangerous. If staff feel that change is based on their ideas, they are far more likely to commit to the change. It is worth pointing out that this method is likely to take time due to the amount of consultation needed, and therefore be unsuitable as a way of overcoming resistance when change is needed fast.

Negotiation and agreement

This involves offering some kind of incentive to resistors if they accept the change. Often used where resistance is led by a trade union, staff may be offered a pay rise

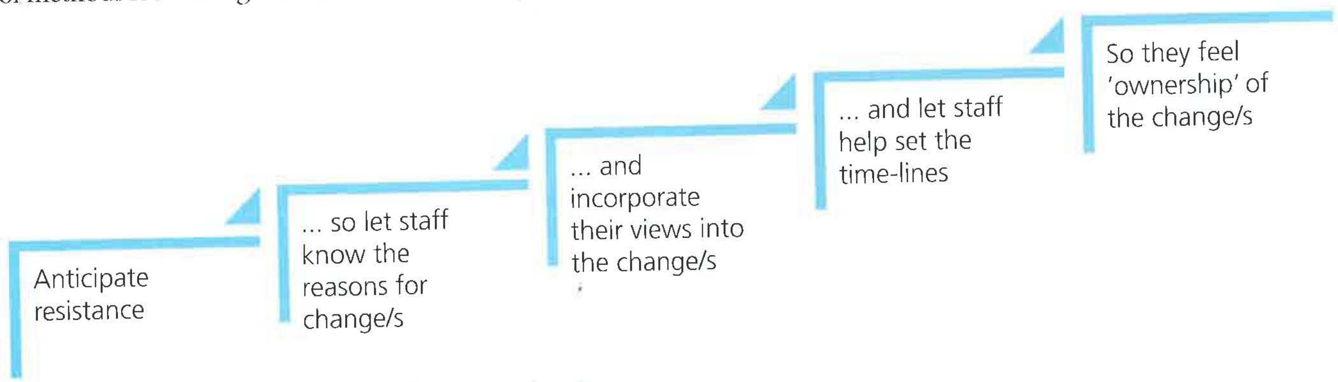


Figure 23.2 Logic chain: overcoming resistance to change

Five whys and a how

Questions	Answers
Why do people resist change?	Because change introduces uncertainty and therefore insecurity. They also frequently doubt that the goals of the people at the top fit the needs of the people further down the hierarchy.
Why do organisations need to change?	Changes in the markets in which firms operate force businesses to change in order to remain competitive.
Why is it important to manage change?	Changes must be planned and then managed to ensure that staff implement those changes in the way that was planned.
Why is change so hard when a business is growing rapidly?	All the inherent problems of change are multiplied by the pressure of rapid change; staff may fail to see the emerging problems because they can't keep up with the implications of rapid growth.
Why is commitment a key to successful change management?	Staff who feel that the changes are for the best will work harder to make new methods work – meaning the new methods are more likely to work as planned.
How should managers choose the best method to overcome resistance to change?	Managers must assess the changes planned, the extent to which they have all information needed to make the changes, the speed with which change must take place, the importance of managing costs during the change and the main causes of resistance to the particular changes planned.

for accepting changed working conditions, or perhaps offered the chance of early retirement. This method works particularly well when resistors are resisting due to parochial self-interest – since it is designed to reduce the extent to which the change will make them worse off. However, if this method is used, there is the danger that staff will feel that resisting future changes will always lead to compromise from managers. This would push up the costs of the next change programme (remembering that change is a constant in many firms).

'Everyone thinks of changing the world but no one thinks of changing himself.'

Leo Tolstoy, novelist

23.6 Key factors in change – evaluation

Change is normal, not abnormal. Therefore firms need to be alert to causes of change and quick to devise a strategic plan for coping. It is also hugely important that those at the top should be self-critical about their motives and their chance of success. Staff hate to see what they believe to be a self-serving, 'I'm the new boss and I'm going to show everyone what I'm about' change-for-change's-sake approach. New football managers often sell and buy players with little net difference to the team – apparently just to prove themselves (and create '*my* team'). That can be contrasted with the situation of David Potts (Morrisons) and Dave Lewis (Tesco), both of whom were appointed in 2014/2015 at a time of serious crisis for the businesses. Few staff would have doubted the need for radical change.

In the long run, the business that will cope best with change is the one that has a good, trusting relationship between management and staff, strong enough finances to afford the 'right' change rather than the most affordable, and a leader with the skills to be able to paint a clear picture of how the future is to look.

Key terms

Disruptive change: this kind of change happens suddenly, unpredictably and with a substantial impact that shakes up the whole market.

Incremental change: this kind of change occurs in small, gentle steps, allowing a business to adapt gently.

23.7 Workbook

Revision questions

(30 marks; 30 minutes)

1 Examine the key factors that might make it difficult to change the age range of a school from 11–16 to 11–18. (5)

2 Identify three problems for a fast-growing firm caused by changes in the management structure. (3)

3 Explain one way in which your school/college could be affected by:

a) incremental change (4)

b) disruptive change. (4)

4 Explain why misunderstanding is more likely to cause resistance to change in branches of an international retailer. (3)

5 Explain two issues that a change management team should consider when deciding which approach to take to overcoming resistance to change. (6)

6 Explain why it may be hard for young, inexperienced managers of a successful business start-up to cope effectively with an unexpected, dramatic change. (5)

Revision activities

Data response

Hemmings and Bennett Ltd is a medium-sized engineering firm that specialises in manufacturing cutting-edge propulsion systems used in rockets. The firm has been established for over 25 years and has a loyal and exceptionally highly skilled workforce. Over recent years it has found it increasingly hard to generate the profit levels expected by shareholders as it has struggled to compete with emerging rivals from Europe and China. Chief executive Andy Bennett has been convinced by his finance director that the firm needs to reduce costs in order to maintain competitiveness. In order for this to happen, they have identified a number of steps that can be taken without damaging the quality of output produced:

- 30 per cent of the workforce to be made redundant.
- Staff holiday entitlement to be cut by 25 per cent.
- Several simple processes to be outsourced to a company in the Czech Republic.
- A 50 per cent cut in the training budget.

The shareholders agreed these proposals and gave Andy twelve months to make the changes. He and his directors held a series of planning meetings in order to decide how to proceed.

	Hemmings and Bennett Ltd before the changes	Industry average
Capacity utilisation	70%	85%
Average age of staff	46	32
Index of unit cost	124	100
Labour costs as a % of total costs	52%	38%
% of workforce who belong to a trade union	17%	12%
Net profit margin	8%	15%
ROCE	6%	16%

Table 23.1 Hemmings and Bennett Ltd – selected data before the change programme

Questions (40 marks; 45 minutes)

1 Using the information from the case study and Table 23.1, assess why change is needed at Hemmings and Bennett Ltd. (10)

2 Assess possible causes of resistance to the changes proposed at Hemmings and Bennett Ltd. (10)

3 Evaluate the best method(s) for Andy to use to overcome any resistance to change from staff. (20)

Extended writing

1 'Managing change is easier within a successful business than one that is struggling.' Evaluate this statement. (20)

2 Evaluate the difficulties a new boss would face in changing Marks & Spencer into a dynamic, young, fashion-conscious organisation. (20)

24 Scenario planning

Definition

Scenario planning means visualising possible futures for a business, then planning how to get the best out of the opportunities and how to deal with the threats.

Linked to: Corporate objectives, Ch 1; SWOT analysis, Ch 4; Growth, Ch 7, Causes and effects of change, Ch 22; Key factors in change, Ch 23

24.1 Introduction to scenario planning

Since its birth in 2005, soft drinks maker Fever-Tree has grown at a ferocious pace of around 50 per cent a year. By the first half of 2015, its sales had risen to an annualised £48 million. So what might the position of the business be in, say, five years' time? Three scenarios come to mind:

- It might carry on growing at 50 per cent a year; this compound growth would mean a £365 million revenue business by 2020 – a business the size of SuperGroup plc, and therefore needing strong, experienced financial management.
- Growth might slow to 20 per cent a year; that would mean a £120 million business by 2020 – probably not requiring any fundamental change from the current board of directors.
- Growth might tail away, leaving a business of £50 million by 2020, and probably facing tough competition from others catching Fever-Tree up; the current management set-up might need to be slimmed down to reflect the lack of growth.

The point is simple: look ahead and think about what might happen – and start planning for what you might do if a particular scenario happens. For big companies with big brands, years can go by with relatively little happening – then suddenly a decision is needed – and that decision must be right. In June 2015, a government department in India announced that Nestlé's Maggi noodles contained unacceptably high levels of lead. For several days Nestlé argued that the tests were wrong and that the products were fine. Ten days later the government banned further production or importing of the brand and Nestlé was forced to strip the product from Indian shop shelves. Maggi noodles had annual sales of more than £400 million in India; it remains to be seen whether they can recover to that level. Surely Nestlé should have withdrawn the product first – and argued second; that would have preserved the brand and company image. Such a misjudged response may point to poor scenario planning.

24.2 Identifying key risks through risk assessment

Risk assessment comes in three parts:

1 Identify the possible risks faced by the business.

2 Quantify their possible cost to the business.

3 Attempt to quantify the probability that each risk might occur.

If that sounds rather like drawing up a decision tree, that's good. It is.

In truth, you're unlikely to be able to quantify stages 2 and 3 with anything like accuracy. But that's not a problem. The key is to have gone through the thought process and therefore start a planning process – and perhaps even put one or two things into practice.

Among the key risks a business might consider are:

- natural disasters
- IT systems failure
- loss of key staff.

Natural disasters

Manufacturing businesses have some obvious vulnerabilities: to their sources of supply (earthquake in Turkey, where Ferrero gets its hazelnuts to make Nutella); to their own factory (local flooding makes roads impassable); and to the warehouses here or abroad where finished goods stocks are held. In the computing and consumer electronics business, a surprising number of companies and factories are based in earthquake zones: in California, in Japan and in China.

Real business

In March 2011, a massive undersea earthquake off the east coast of Japan sent massive waves that went deep inland, killing around 18,000 people. The flooding and the direct impact of the earthquake were compounded by a catastrophic failure at a flooded nuclear power plant. A senior manager of US Cisco Systems said that the scale was unprecedented:

'In the past we had incidents where five suppliers or a single contract manufacturer were shut down. But we had nothing like this before where we had we had 60 to 70 suppliers impacted in some form or fashion. In addition, the supplies affected included a wide range of production materials, including semiconductors, passives, wafers and chemicals.'

Car manufacturers were hit round the world, leading them to the view that in future they must make sure to get supplies from more than one region.

In the UK, serious natural disasters are rare, with the exception of localised flooding. It wouldn't be hard for a large business to plan for this eventuality, but there may be local service businesses that have no opportunity to diversify. For them, the key would be to try to build up cash reserves for that rainy day. There is always sense in **contingency planning**.

Figure 24.1 Outbreak of the Great East Japan earthquake and tsunami

'Individuals should think about the worst-case scenarios and plan for them. The world will be crazier than you think.'

Nicolas Taleb, author of The Black Swan

IT systems failure

On 8 August 2015, Carphone Warehouse warned that its website had been hacked three days before, risking the credit card security details of 90,000 of its customers. The company's security systems had failed, but the shock to customers was that the business had taken three days to own up to the problem. Proper scenario planning would have identified that the proper response was to inform customers immediately.

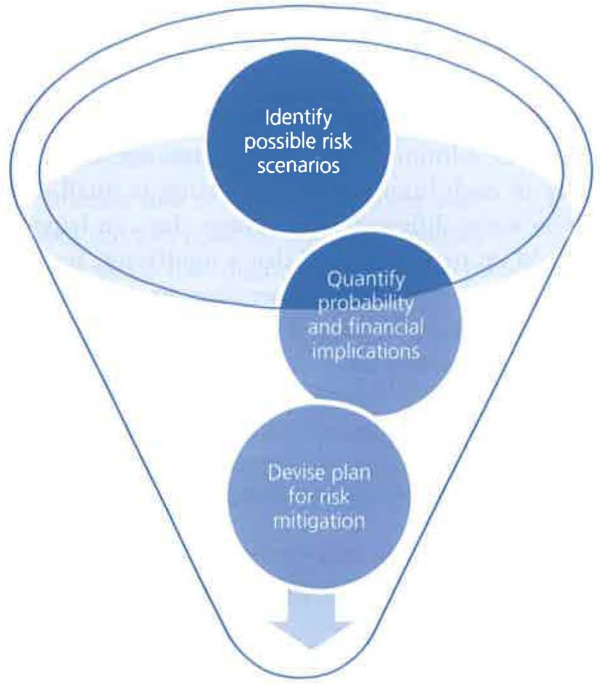
The Carphone Warehouse fiasco came just two months after a more widespread IT systems failure at RBS/NatWest Bank. RBS had tweeted: 'Some customer payments are missing this morning – we are investigating this issue as a matter of urgency'. In fact 600,000 customers were affected by a systems failure that meant deposits to their bank accounts failed to register. This would mean that thousands would be unable to withdraw cash as needed. Only seven months before, the bank had been fined £50 million for a previous systems meltdown that left 6.5 million customers locked out of their bank accounts for days. Both episodes had newspapers asking whether RBS is Britain's worst bank.

For any business today, scenario planning must include careful thought about the vulnerability of the firm's reputation to IT systems failure. Back-up systems may be expensive to install – but are surely an essential cost in doing business.

Loss of key staff

In most large companies, although the boss may be paid huge sums, the business is bigger than any individual. If the chief executive leaves, another can slot in without too much disruption. Businesses such as Mars, Next, Primark and Halfords would fall into that category. There are important exceptions, however. Ted Baker plc was started by Ray Kelvin, who still runs the business. Ray *is* Ted Baker; what would happen if Ray retired? And for many years shareholders in News International/Sky worried what would happen when Rupert Murdoch had to stand down (he's over 80).

No less important are key technical experts within a workforce. At Apple, Jonathan Ive is the design guru and for Nintendo, Shigeru Miyamoto (designer of Donkey Kong, SuperMario and the Wii system) has long been the star. Quite clearly if either of these experts left the business, the implications would be significant. This scenario can be anticipated and planned for.



Effective scenario planning

Figure 24.2 Logic chain: effective scenario planning

24.3 Planning for risk mitigation

Mitigating risk means taking actions that will reduce, even minimise it. No one can prevent natural disasters, but you can make sure that your supplies come from different companies in different regions, to minimise the possibility of disruption due to 'acts of god'. You can also make sure that your sales revenue isn't overly dependent on one product line. In the first half of 2015, Apple was 69 per cent dependent on the iPhone for its income. No wonder the company launched the Apple Watch and also started work on an Apple self-drive car.

Business continuity

Business continuity means planning how to restore things to normal after a setback or disaster has struck. This will have several aspects:

- There must be a strong enough financial position to be able to withstand short-term shock and finance any capital requirements to get the business straight again. For example, the cost to Nestlé of withdrawing all Maggi noodle products from shop shelves in India was about £50 million.
- The British government has a committee called COBRA that meets when security or other physical disasters occur. In a similar way, a company might set up a business continuity committee, including marketing and public relations staff as well as resource and personnel managers.
- There must be clear lines of authority showing who is responsible for making the key decisions at a time of crisis. This shouldn't be the chief executive, who should be more focused upon long-term strategy.

Succession planning

Succession planning means thinking hard and planning ahead for when a leader leaves and must be replaced. *Forbes* magazine has published research showing that 55 per cent of large companies recruit a new chief executive from outside the business. So only 45 per cent of appointees are the product of succession planning. Presumably the internal candidates were too weak to be worth appointing – which indicates poor planning. A successful succession plan would have identified the right person to be groomed for the role – and set up a suitable training plan.

The value of effective succession planning is that the new person understands fully the thinking behind current strategies and given insights into policies that have been trialled but failed. For middle managers, nothing is more frustrating than a new boss who seems determined to make the same mistakes as the previous one.

Eventually, every boss will go and so will every one of the business's most valuable specialist staff – so planning their replacement makes a huge amount of sense. Unfortunately what makes sense for the company doesn't necessarily suit the staff. Some may feel that 'succession planning' threatens their job security, as shown in the following case.

Real business

Dominic is a software expert working for a major oil company. He is employed on a consultancy contract which gives him a regular four days a week (at a huge daily rate). A new divisional boss employs two IT graduates and asks Dominic to train them up. Not unreasonably, Dominic suspects that he is being asked to plan his own succession, with his own job being scrapped as soon as the younger, cheaper staff can do the work. He doesn't hurry; nor does he explain things well enough for the younger staff to feel comfortable that they can take over.

Is there a solution to this problem? Probably not. Succession planning can only work effectively when the boss is a willing participant, perhaps because he or she wants to retire or to move on.

'Succession planning should be gradual and thoughtful, with lots of sharing of information and knowledge and perspective, so that it's almost a non-event when it happens.'

Anne Mulcahy, former CEO, Xerox Corp

'Good fortune is what happens when opportunity meets with planning.'

Thomas Edison, inventor

24.4 Scenario planning – evaluation

The logic behind scenario planning is not that you'll be able to predict what will happen. It's simply that if you've thought about what might happen, and how you might respond, you should be in a better position to cope. Nicolas Taleb, in his book *The Black Swan*, warns that totally unexpected things happen more often than we imagine, from planes falling out of the sky to companies suddenly collapsing into administration. He points out that the probability of each bizarre event occurring is small, but there are so many different weird things that can happen that they add up to a likelihood that a significant, strange event will happen quite often. Therefore, he says, always keep a strong enough balance sheet to cope with tough times. This is very sound advice.

Key term

Contingency planning: thinking through a Plan B in case Plan A goes wrong.

Five whys and a how

Questions	Answers
Why is scenario planning needed?	Because it's hard to cope with a sudden problem if you haven't thought it through beforehand.
Why do some companies focus on downside rather than upside risks?	Downside risks may threaten business survival; upside risks can just be seen as good news.
Why might scenario planning prove a mistake?	It might take up more time than makes sense, especially if there are so many different possibilities that none can be tackled in sufficient depth.
Why might scenario planning prove useful for a business such as British Airways?	It can plan for the downside implications of a price war or of even higher passenger taxes, and the upside risks of a major rival going into receivership or of new routes opening up to Africa.
Why might a company use risk mitigation methods?	To turn its scenario planning process into a way to smooth out potential future problems.
How might a small construction company use scenario planning?	It can think about what might go wrong, cost it out and then build those potential costs into its pricing method for quoting for jobs.

24.5 Workbook

Revision questions

(25 marks; 25 minutes)

1 Choose **one** of these companies and set out two positive and two negative scenarios that might impact on the business.
   a) Heinz, in its management of its Tomato Ketchup brand
   b) Sony, in its management of its PS4 console. (8)

2 Unusually high rainfall causes flooding throughout the Midlands, cutting off the Mini engine factory at Hams Hall. Explain two possible effects if the business had failed to carry out scenario planning. (8)

3 Explain why scenario planning might be of particular value to **one** of these businesses:
   a) Primark
   b) Jaguar Land Rover
   c) Instagram. (4)

4 Explain why the leader of a business such as Marks & Spencer might be reluctant to carry through a full succession plan. (5)

Revision activities

Data Response

JCB: one of the UK's most successful manufacturers

In 2015, JCB hopes to break the £3 billion turnover mark for the first time in its history. One of the country's biggest and most important engineering companies, JCB's yellow and black construction vehicles are among the top three bestsellers globally. In its UK heartland of Staffordshire and Derbyshire, JCB employs over 5,000 people in highly skilled, secure jobs.

One of JCB's secrets has been its willingness to invest. Its 1979 decision to start up in India has led to the achievement of a 50 per cent market share in this huge, fast-developing country. India's new government is embarking on a huge programme of investment in roads and other infrastructure which should be great for JCB. Just in 2014, the company announced:

- a £25 million programme to double production in Germany
- a £45 million investment in a six-cylinder engine to slot into its fuel-efficient Dieselmax range
- a £150 million plan to expand production in the UK, with the expectation of creating 2,500 more jobs by 2018.

As Figure 24.3 shows, not long ago – in the 2009 recession – the company's plans were thrown into turmoil by a collapse in sales. That year the company was saved by sales growth in India and China. Even so, with an estimated total capacity of 72,000 units in 2009, the rate of utilisation was very poor.

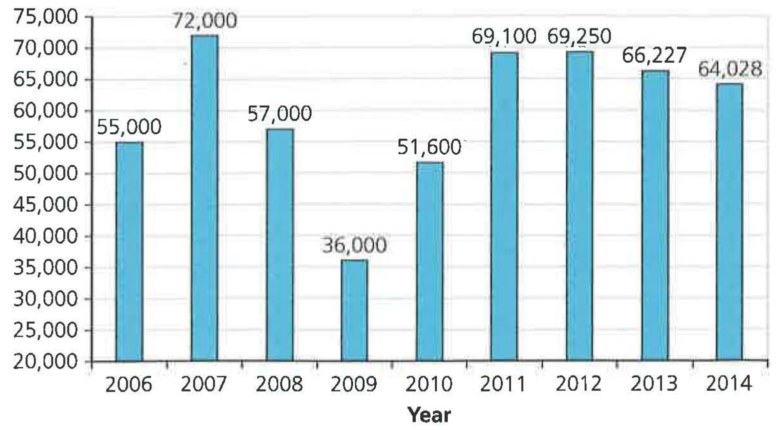


Figure 24.3 JCB annual global sales (in units) (source: JCB press reports)

To their credit, senior managers kept their heads and kept investing in the firm's future. From a struggle to break even in 2009, the company bounced back to make £365 million profit in 2012.

In 2014, JCB has been holding to its long-term plan for significant increases in its global capacity. Its factories in India and Brazil are getting greater investment and new factories are being built in Uttoxeter and Cheadle in Britain. JCB believes that developing countries will continue to plough funds into construction investment, and that JCB should be at the heart of this business. It shows no fear of its two huge global rivals: Caterpillar of America and Komatsu of Japan.

Another plan for the future is to improve the productivity of the JCB factories worldwide. In 2014, the 12,000-strong workforce produced 64,000 units. By 2018, the hope is to get annual productivity up to eight units per worker.

Questions (40 marks; 45 minutes)

1 a) Calculate JCB's capacity utilisation in 2009. (3)

b) Explain how JCB might have set about rebuilding this figure. (4)

2 Assess the problems JCB might face in implementing a new strategy that matches output to demand. (10)

3 a) Calculate JCB's labour productivity in 2014. (3)

b) JCB's directors have asked managers to devise a new strategy to meet a productivity objective of eight units per worker by 2018. Evaluate how detailed scenario planning might help the business achieve this objective. (20)

Extended writing

1 Coca-Cola UK is having to face the possibility that its future will be much harder than its past. It believes there is a 40 per cent chance that a soft drinks' sugar tax will be brought in. Evaluate how scenario planning might help Coca-Cola UK face this prospect. (20)

2 Richard Branson has run the Virgin Group since he founded it in the 1960s. Evaluate whether it's inevitable that the Virgin Group will decline once Sir Richard retires. (20)

Theme 4

Global business