CHAPTER FOUR

**External and Internal Organization Environments and**

**Corporate Culture**

* 1. **Define the external environment of organizations**

Organizations must react and adapt to many forces in their internal and external environments. This process of adaptation leads to competitive advantage, a topic we discussed in the introduction to Chapter 3 (see Michael Porter).

The **external environment**, involves all outside factors and influences that impact the operation of a business that an organization must respond or react to in order to maintain its flow of operations.

* This relates closely to a PESTEL analysis, which stands for Political Economic Sociocultural Technological Environmental and Legal See Exhibit 4.16 for a simplified model. We will learn more about the PESTEL Analysis in Chapter 8.

**Globalization**: The development of an integrated global economy and characterized by free trade, capital flows, communications, and cheaper foreign labor markets, the processes of globalization underlie the forces in the general international economic environment.

* **Business is increasingly global. How well (or poorly) do the concepts we are learning translate outside of your country?**
* **What approach would you use to expand your company abroad?**

**Economic Forces:** Economic environmental forces generally include such elements in the economy as exchange rates and wages, employment statistics, and related factors such as inflation, recessions, and other shocks—negative and positive. Hiring and unemployment, employee benefits, factors affecting organizational operating costs, revenues, and profits are affected by global, national, regional, and local economies.

* **Technological forces** impact all aspects of business, from production to communication to the types of businesses themselves.
* **Government and political forces** also affect industries and organizations. Major political events such as Britain’s exit from the European Union, military conflicts, trade wars, the COVID-19 Pandemic, and rising nationalistic policies will all have an impact that is difficult to predict.

**Sociocultural Forces:** Sociocultural forces include demographic trends, lifestyle changes, gender issues, and ethics.

* **Why do demographic shifts and technological developments create both challenges and new opportunities for business?**

**Natural Disasters and Human Related Problems:** Natural disaster and environmental problems are events such as high-impact hurricanes, extreme temperatures, water and food crises, as well as human-induced environmental disasters such as coastal degradation, uncontrollable forest fires, water pollution, and biodiversity loss.

* **As we continue to learn about a corporation and manager's role in society, ask yourself: "What is a corporation or manger's responsibility outside of generating profits for shareholders?"**
* **While there are diverse opinions on the solutions to many problems of this type, there is no debate that they will continue and will cause even more disruption. How should managers of global firms plan for and react to approaching changes such as mass relocation/migration of people?**

Organizational characteristics such as size and geographic location impact how environmental forces affect each organization differently. An understanding of the forces and they currently affecting organizations and pressuring structural change is crucial.

* 1. **Identify contemporary external forces pressuring organizations**

**NOTE**: This module is written in a somewhat circular manner – first presenting the different organizational contexts and then talking about how they might be used. *It’s always recommended that students read and re-read each passage of textbook to be certain they fully understand it; this section presents the perfect case for that approach.*

To be successful, organizations must fit their environment, and adapt as needed. Certain industries, as a whole, bring specific factors and forces to the companies within them.

The two distinguishing factors are:

1. **Simplicity vs. complexity,** determined by the number and similarity/dissimilarity of external forces.
   1. A simple environment has a low number of similar external forces.
   2. A complex environment has a high number of dissimilar external forces.
2. **Stability vs. instability,** determined by the rate and “size” of change of those forces.
   1. A stable environment stays the same or changes slowly.
   2. An unstable environment changes frequently and unpredictably.

*Misconception alert:* While it may seem “easier” to work in any environment that is both simple and stable (a simple-stable environment), note that all of your competitors would exist in that same environment. As a result, the lack of change might limit competitive advantage. *Every environment has its plusses and minuses.* With that said, your *personal* fit and purpose might make one environment appeal to you more than others.

The four combinations are:

* **simple-stable environment:** a small number of external elements, and element
* **complex-stable environment:** a large number of external elements, elements are dissimilar, and elements remain the same or change slowly.
* **simple-unstable environment:** a small number of external elements, but the elements change quickly or are unpredictable.
* **complex-unstable** **environment:** a large number of external elements which change quickly or are unpredictable.

**Name one industry or company that fits each of the four categories above.** (Note, a test on this section would likely include such a question.)

* **Simple-stable:** \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_
* **Complex-stable**: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_
* **Simple-unstable:** \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_
* **Complex-unstable**: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

**Organizational Complexity:**

* ***External complexity*** is defined as the amount of complexity derived from the environment where the organization operates; such as the country, the markets, suppliers, customers and stakeholders
* **Internal complexity** is the amount of complexity that is internal to the organization itself, i.e. products, technologies, human resources, processes and organizational structure.

**Be able to answer the key question from this section: "How does a manager deal with organizational complexity?" Keep it in mind as you move forward.**

* 1. Identify different types of organizational structures, and their strengths and weaknesses

An understanding of Mechanistic vs Organic Structures and Systems and how they differ and how these major concepts help classify different organizational structures is crucial to recognizing organizational structures. Finally, the issue of organizational complexity and its impact on organizational structure needs to be understood.

You should be able to discuss the evolution of different types of Organizational Structures. You should understand and identify the six types of organizational structures, and the advantages and disadvantages of each: Functional, Divisional, Matrix, Geographic, Networked Team, and Virtual.

**Mechanistic organizational structures** are best suited for environments that range from stable and simple to low-moderate uncertainty

* They are characterized by top-down hierarchies of control that are rule-based.
* The chain of command is highly centralized and uses formal authority
* Tasks are clearly defined and differentiated to be executed by specific specialized experts.

**Organic organizational structures** work best in unstable, complex, changing environments.

* Their structures are flatter, with participatory communication and decision-making flowing in different directions.
* While there is more fluidity and less-rigid ways of performing tasks, there may also be fewer rules.

**Think about a current or past organization you’ve been a part of. Which of these two structures did it have?**

**The six structures:**

* **Functional**. This structure is organized by departments and expertise areas, such as R&D (research & development), production, accounting, and human resources. Functional organizations are referred to as pyramid structures since they are governed as a hierarchical, top-down control system.
* **Divisional**. This structure has many functional departments grouped under a division head. Each functional group in a division has its own marketing, sales, accounting, manufacturing, and production team.
* **Geographic**. This structure is organized by locations of customers that a company serves. This structure evolved as companies became more national, international, and global. Geographic structures resemble and are extensions of the divisional structure.
* **Matrix**. Matrix structures use teams to combine vertical with horizontal structures. The traditional functional or vertical structure and chain of command maintains control over employees who work on teams that cut across functional areas, creating horizontal coordination that focuses projects that have deadlines and goals to meet within and often times in addition to those of departments.
* **Networked Team**. Network structures are horizontal which move beyond matrix and are more informal and flexible. There is not one classical depiction of this structure, since different companies initially design teams to solve problems, find opportunities, and discover resources to do so.
* **Virtual**. This structure moves beyond network team structures in that the headquarters or home base may be the only or part of part of a stable organizational base. Otherwise, this is a ‘boundaryless organization.”

**Of the structures listed below, functional is probably the most popular. Why do you think that is the case?**

**Why does the matrix structure have a dual chain of command?**

**How does a matrix structure increase power struggles or reduce accountability?**

**What are the advantages of committees?**

Each of these structures has advantages and disadvantages. As companies evolve, new structures are often put in place to better fit the environment.

* 1. **Explain how organizations organize to meet external market threats and opportunities.**

Organizations are considered as either **Open or Closed systems**. depending on the organization’s sensitivity to the environment. Closed systems are less sensitive to environmental resources and possibilities, and open systems are more responsive and adaptive to environmental changes.

* At the **input** phase, open systems take in resources, raw materials, information, talented people, users, clients, items needing improvement, and other entities.
* At the **throughput** (or through-put) phase, the entities are transformed, processed, improved, or served by the organization. (For example, grain is processed into bread; actors are recorded and edited to create episodes; data is analyzed.)
* At the **output** phase, the results of the throughput phase are transmitted, shared, sold, or certified. (For example, the bread is sold; the episode is streamed; the data analysis results are published.)

**While you likely don’t think about it this way, entered your institution (your school) as an “input.” What occurs at the institution’s throughput and output stages related to you?**

**What are the inputs, throughputs, and outputs of an automotive repair shop?**

**What are the inputs, throughputs, and outputs of a social media platform?**

**Domain:** An organization defines itself and its niche in an environment by the choice of its domain. In other words, what sector or field of the environment it will use its technology, products, and services to compete in and serve.

**Internal organizational dimensions:** These dimensions and systems include leadership, strategy, culture, management, goals, marketing, operations, and structure. Relationships, norms, and politics are also included in the informal organization.

***Example: The McKinsey 7-S model***: shown in [**Exhibit 4.17**](https://openstax.org/books/principles-management/pages/4-4-the-internal-organization-and-external-environments#ch04fig17). Similarly, strategy, structure, systems, skills, staff, and *style* all revolve around and are interconnected with shared values (or culture) in an organization.

* You may be responsible to explain this model. Learn more about it here: <https://www.investopedia.com/terms/m/mckinsey-7s-model.asp>

**Analysis and Change:** Organizational leaders perform different types of analysis, including SWOT (strengths, resources, opportunities, threats), and continue to refine the organizational goals, mission, and model. From there, the organization can be structured or restructured based on internal and external forces.

* **What part of the SWOT analysis is most important for creating company strategy?**

**No company structure is permanent:** This is why it is so common to see businesses restructure, especially with the on-boarding of a new CEO or after a major shift in the market. Companies and organizations change leadership and strategies and make structural and systems changes to meet changing competition, market forces, and customers and end users’ needs and demands.

**4.5 Identify the fit between organizational cultures and the external environment**

You should be able to identify and differentiate between the four types of organizational cultures and the fit of each with the external environment and describe the CVF framework. Finally, you can identify the internal dimensions of organizations, the interconnection among the dimensions, and how these affect the ‘fit’ with external environments.

Organizational culture is considered one of the most important **internal dimensions of an organization**’s effectiveness criteria.

* **Based on what you know so far in this course, why do you think organizational culture is so important for success?**

The **Competing Values Framework** (CVF) is one of the most cited and tested models for diagnosing an organization’s cultural effectiveness and examining its fit with its environment.

* The two axes in the framework, external focus versus internal focus, indicate whether or not the organization’s culture is externally or internally oriented.
* The other two axes, flexibility versus stability and control, determine whether a culture functions better in a stable, controlled environment or a flexible, fast-paced environment. Combining the axes offers four cultural types:
  1. **Adhocracy Culture**—an external focus with a flexibility orientation
  2. **Clan Culture**—an internal focus with a flexibility orientation
  3. **Hierarchy Culture**—an internal focus with a stability/control orientation; and (4) the results-oriented, competitive
  4. **Market Culture**—an external focus with a stability/control orientation.
* **Based on the descriptions above, what is the value of each culture category in the Competing Values Framework (CVF)?**
* **Can an over-reliance on one culture lead to negative outcomes?**
* **How can employee diversity give a company a competitive advantage?**
* **Explain the concept of hiring for fit as it relates to corporate culture.**
  1. **Identify environmental trends, demands, and opportunities facing organizations.**

The Global Risks Perception Survey predicts these trends in the external environment:

* persistent inequality and unfairness
* domestic and international political tensions
* environmental dangers
* cyber vulnerabilities

**How would you recommend businesses address these challenges?**

**How can you prepare now to address these challenges as a future manager?**

**Resilience:** To address negative external changes like those listed above, organizations began to focus on resilience, or the ability to manage or reduce the impact.

* “Structural resilience” considers the systemic dynamics within the organization itself.
* “Integrative resilience” underlines complex interconnections with the external context.
* “Transformative resilience” responds to the fact that mitigating some risks requires transformation.

**Why is resiliency so important in business?**

**How can managers (and workers) contribute to resilience?**

**Social impact:** Another trend is that organizations will no longer solely be judged only for their financial performance, or even the quality of their products or services. Rather, they will be evaluated on the basis of their *impact on society at large—*transforming them from business enterprises into social enterprises.

* (If you have ever seen a company sponsor a community event, you know what the authors are talking about here. Many companies desire to be involved in their communities.)
* **What is social capital? Why is it phrased this way? (Hint: What is capital in relation to business?)**

**Note**: As you move into the next chapter on ethics and responsibility, consider the above.

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