

Crisis and Renewal: Ethical Anarchy in Mature Organizations

JUST AS A MATURE FOREST NEEDS TO BURN TO RENEW ITSELF, A MATURE ORGANIZATION

NEEDS TO DESTROY ITSELF – CREATIVELY – IF IT WANTS TO CONTINUE TO SUCCEED

IN EARLY SUMMER 1995, huge forest fires raged through Northern Ontario and Western Canada. Our television screens were dominated by images of smoke and flame. The news reports focused on the heroic efforts of hundreds of firefighters to save the forests and on the massive destruction and loss. Unusually dry conditions, high winds and lightning were cited as the causes of these disastrous infernos. Relatively little attention was paid to the systemic causes, especially the forest management practices of both the government and the timber industry, which have usually tried to minimize the role of fire in the ecology of forests. Such efforts often have perverse consequences. In the United States, for example, from the 1880s to the 1970s, the U.S. National Park Service pursued a policy of putting out all fires in America's parks. The objectives were to stabilize the complex ecosystems in the parks and to conserve the flora and fauna in a pristine condition for the enjoyment of visitors to the parks.

At first the policy worked well. But as time went by it became increasingly difficult to implement. Small fires were easy to control, but gradually they became larger and more difficult to handle. Mature trees, receiving the most sun and water, began to dominate the forests, choking the growth of other organisms. As these trees dropped their leaves and branches, vast amounts of fuel

accumulated on the ground. Once fires were started they could grow out of control rapidly and become catastrophic. In the process of trying to keep complex systems stable, the forest managers had actually reduced the flexibility, variety and resilience in these systems, making them dangerously unstable. Preserving the forest's complex system cannot be done by "stopping the clock." The only way such systems can survive is through constant renewal. Mature forests have to burn to be renewed.

Organizations are like ecosystems; crisis is an essential part of this renewal process. As complex systems, forests and mature human organizations share the systemic property of having constraints. When human organizations are young, these constraints are introduced for the very best of reasons – to preserve a tested recipe for success. But over time, as conditions change, they become a hindrance; strengths eventually become weaknesses. When such conditions arise, managers are so constrained by the success of the system they have developed that they can no longer innovate within it. Their only way out of this impasse is to destroy the system – creatively – in an act of what I call "ethical anarchy." Unless they do so, they risk being overtaken by far larger "natural" disasters. In mature organizations, it is inevitable that the seeds of failure are contained in the fruits of success.



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Such advice may be rejected by many managers educated in the 50 years that have followed the Second World War. During this period, management teachings have been much more concerned with rationality in management and stability in organizations. Indeed, far from “burning” their organizations, managers have usually been preoccupied with making them “fireproof.” To this day, crises and surprises have usually been regarded as dysfunctional.

ORGANIZATIONS AS ECOSYSTEMS

An important benefit of looking at human organizations as ecosystems is that it allows us to integrate, both in theory and in practice, several perspectives on management action that have usually been regarded as mutually exclusive. Three of the best known of these perspectives are:

1. *Rational Action:* Action has a purpose and is rational. It is directed toward the achievement of goals by managers who make clear choices before they act. This assumption is buried deeply in modern western, culture. It is the only perspective on action that most of us have grown up with.

2. *Constrained Action:* Action is externally constrained and situationally determined. While individual actors may believe that they are acting with purpose, their actions are in fact constrained by the circumstances in which they find themselves. This has been an unpopular view among managers, except when the organization's results are poor. Then the constrained actor model is often used to explain the “circumstances beyond our control” that led to the disaster.

3. *Emergent Action:* Action emerges from a process that is almost random in nature. It unfolds over time and the logic emerges retrospectively from the process. In this perspective, managers are free to act but do not know what to do. Their problems are unanalyzable.

FROM LIFE CYCLE TO ECOCYCLE

Ecosystems, such as forests, are dynamically stable entities whose survival depends upon the effective interaction of many organisms and processes. Ecosystems maintain their stability by going through a continual process of creation, growth, destruction and renewal. The organization survives while its elements change. Even if ecosystems do not live forever, they endure for very long periods, and the totality of the change they undergo should

be thought of as an “ecocycle” rather than as a life cycle. Of course, humans are self-conscious actors capable of rational action. Hence, a human organization’s ecocycle needs to have the capacity for conscious, rational action added to the emergent and constrained behaviors that characterize ecosystems such as forests.

KEY FEATURES OF THE ORGANIZATIONAL ECOCYCLE

By following the diagram, “The Organizational Ecocycle,” one can see that the ecocycle splits the processes that sustain an ecosystem into two “loops.” As the ecosystem moves through the different phases of the ecocycle, different contexts are created in which different kinds of management action are possible.

The front loop is the familiar, conventional life cycle. It tracks the system from birth to decline and crisis. The back loop is a less familiar, renewal cycle of “death” and “reconception.” It begins in confusion in the aftermath of crisis, which has shattered the constraints that bind the ecosystem and fragmented the large hierarchical structures.

Several key features of the ecocycle need to be emphasized:

- *Change is continuous.* Sometimes it is smooth and almost linear; at other times it is rapid and nonlinear.

- *Renewal requires destruction.* The only way to open up space in the forest is to creatively destroy the large-scale structures that monopolize its resources.

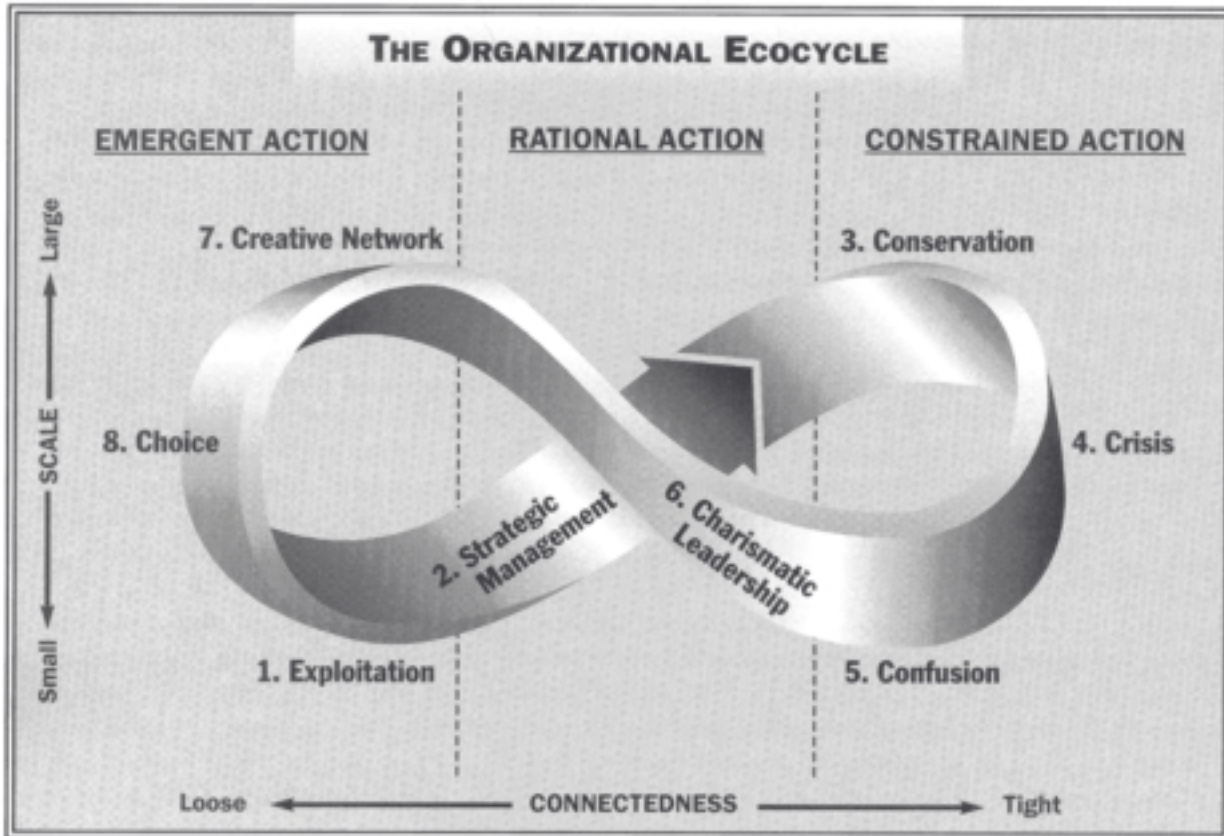
- *There are two types of rational action,* each conforming to the half-loops that traverse contexts in which rational action is possible. Each form of rationality takes the organization in a different direction. Strategic management is characterized by an instrumental, means-to-an-end rationality. Charismatic leadership, on the other hand, is a values-based rationality — action is taken for its intrinsic worth in demonstrating deeply-held beliefs about human relationships.

TRAVERSING THE ECOCYCLE

Eight phases make-up the ecocycle:

Phase 1. Exploitation

This phase of the ecocycle is characterized by several processes that lead to the rapid colonization of any available space. In an open patch of space, resources are easily



available and require little investment to be harvested. Thus a forest clearing will be colonized initially by a large variety of plants and other life. These organisms are the “pioneers,” the opportunists that take quick advantage of the open space that has appeared. Similarly, in human organizations entrepreneurs are usually opportunists. They rarely have a very clear idea of what products or services they should sell, let alone what business they are in. For example, when Bill Hewlett and Dave Packard founded their company in the late 1930s, they had no idea what products the company should make. They played around with a variety of technical challenges that ranged from the control of telescope motors to a foul-line roll indicator for a local bowling alley. It took about a year for their first practical product to emerge from the laboratory at Stanford University. That product, an audio oscillator, supplied the logic that created the context for the ecocycle’s next phase.

Phase 2. *Instrumental Rational Action*

Strategic Management

Instrumental rationality first becomes possible in young organizations when managers learn cause-and-effect relationships. As was the case in Hewlett Packard, this learning is often a result of a series of trial-and-error experiments made in an earlier, emergent phase of the organization’s existence. Of course this does not preclude many organizations from imitating the apparently successful recipes of others and short-circuiting the trial-and-error process. Indeed, much activity and change in organizations is driven by imitation.

The Case of Compaq Computers

Although the transition from growth to efficiency occurs in the rational action phase of the ecocycle, this does not mean that it is an easy passage. This is illustrated by the recent, well-publicized jolting transitions at Compaq.

The company was founded in early 1982 by three former Texas Instruments employees. Compaq’s emphasis was on introducing personal computers with leading edge technology soon as it became available. The manufacturing emphasis was on quality, flexibility in shifting products and speed in bringing new products to market. Cost considerations were “way down the list.”

Compaq reached the *Fortune* 500 after only four years of operation - the shortest time on record. Sales reached over \$1 billion by 1987 and nearly \$3 billion by 1989. All this was accomplished in a culture that emphasized wide-open communication, teamwork, extensive consultation and fact gathering, and decision-making by consensus. These are exactly the kinds of social dynamics one would expect to find in a young, emergent organization.

By 1990, however, Compaq’s growth rate had slowed dramatically to less than 4% in the United States. Competitors were undercutting its prices by as much as 35% on machines with comparable features. In 1991 sales fell for the first time - by 9% - and Compaq had its first-ever losses and layoffs.

There were two competing rationales for the situation. The first was CEO Rod Canion’s belief that the worldwide recession was largely to blame, implying that no strategy change was necessary. The second argument was based on chief operating officer Eckhard Pfeiffer’s conviction that the market had changed and that Compaq would have to change its strategy. When he was a marketing executive in TI, Pfeiffer had seen a similar downward price spiral in the consumer electronics market. Where Canion saw a temporary interruption in Compaq’s growth, Pfeiffer saw a more sinister pattern. He realized that what was once a product configuration unique to Compaq, was now the dominant design offered by many competitors. In his view the firm now needed to focus on the efficient production of this established design.

The business world was shocked when the Compaq’s board accepted Pfeiffer’s view and fired Canion. The company was then split into two divisions; one to take on the lower-cost clones and the other to sell the more complex systems, where a feature-based strategy would still be viable. At the same time, Pfeiffer launched a series of wide-ranging cost-cutting initiatives, still with the objective of building high-quality computers, but at radically lower costs. In the first phase the workforce was cut by 25% to 9,000 people. Cost reductions and efficiency were now at the top of the list.

In its pure form, however, this phase is characterized by the reduction of what was once a successful experiment to a repeatable formula. This formula is then extended into multiple open “patches.” The story of Nike’s growth during the 1970s is a classic example of this. Having established the company in high-performance track and field shoes, Nike managers developed products for a succession of other sports. Their progression was a combination of planning and opportunism in an unexploited field using a formula that became steadily more rational. The unstructured environment was such that the results of actions were almost immediately apparent. Activities that paid off were extended; those that did not were stopped. During this phase, strategies often emerge as a retrospective rationalization of what worked.

A critical period during this phase occurs when the organization changes from a growth strategy to one emphasizing efficiency. A new, open patch in a market favors organizations that can grow fast but, as the market matures, the fast growers risk being selected out if they cannot hold their own in an increasingly competitive field. From a product and technological perspective, the transition is marked by the emergence of a “dominant design.” This design embodies all the features that customers now regard as basic requirements. As such, its emergence often signals the end of radical product innovation in an industry (or organization) and a move toward improvement in the production process.

Phase 3. Conservation

Once the transition to an efficiency-driven strategy has been made, the competitive premise becomes one of “more of the same.” When an organization becomes successful, managers naturally will tend to restrict activities to those that have been proven to work. Successful strategies will be elaborated upon and expanded. Considerable effort and capital will be invested in describing these activities and embedding them in technology and formal organizational procedures to perpetuate their performance. Often this is accompanied by an increase in the scale of operations. The organization will specialize, “stick to its knitting” and emphasize efficiency. This will make **it** even more successful than it might otherwise have been.

Immediately after the Second World War, the North

THE SAD STORY OF “BIG STEEL”

A particularly poignant instance of the vulnerability to catastrophe of large successful businesses occurred in the U.S integrated steel industry. The preservation of its production facilities from attack during the Second World War gave the industry a tremendous advantage afterwards, and in 1946 the U.S. industry accounted for 54.1% of the world’s raw steel production. However, that success was accompanied by a failure to innovate, and the industry stuck with the massive technology of the open hearth furnace long after it was obsolete. Its market share fell to 20.1% by 1970 and to 11.8% by 1984. It is now under ferocious attack from a new smaller-scale, more-flexible technology: the scrap-fed, electric furnace mini-mill.

American economy favored growth strategies in many industries. From the late 1940s to the early ‘60s there was a pent-up demand for consumer goods and a need to rebuild war-shattered Europe and Japan. By the late ‘60s and early ‘70s, growth began to slow. Major markets began to saturate as demand for steel, autos and housing peaked and then started to fall. By the ‘80s, the majority of the *Fortune* 1000 companies were conservative structures pursuing strategies that emphasized efficiency in their domestic markets. In the process of institutionalizing their successes and pursuing efficiency, however, conservative organizations sacrifice resilience and flexibility and become more vulnerable to catastrophe.

Phase 4. Crisis – Creative Destruction

The description of the effects of a forest fire resonates with the carnage these days among what were once thought to be large, invulnerable organizations. The forest fire reduces the forest to a smoking ruin, but it creates the preconditions necessary for new elements to enter the situation, for new connections to be made, for new processes to operate and for new systems to emerge. Crisis seems to play the same role in human organizations.

Wang Laboratories’ performance peaked in 1989 with more than \$3 billion in revenues and a ranking of 146th in the *Fortune* 500. Wang had been a dominant player in dedicated word processors and their VS range

of minicomputers. Three years later it filed for bankruptcy, with its common shareholders' equity all but wiped out. Wang's hierarchical structure, under which the activities of 31,500 people had once been coordinated world-wide, was destroyed as the business dwindled and divisions were closed or sold. Capital of all kinds, from asset values to employee morale to the goodwill of customers and suppliers, evaporated. Customers turned to other suppliers. Wang employees left to join other companies, form their own ventures or retire. In these new roles many of them made a significant contribution to society. Like the nutrients and seeds that were once bound up in a large tree, with its destruction and fall they are returned to the soil to benefit the forest as a whole.

Wang's story is a familiar one in the business world. A once-successful enterprise experiences a series of setbacks, and change is precipitated by some kind of crisis. A hectic period of "rationalization" follows, during which many parts of the business are shrunk, sold or closed. After a while a smaller version of the enterprise emerges. Often this organization is focused on the core businesses that led to the enterprise's original success.

Such turnarounds are often necessary in organizations that have become inefficient, usually during extended periods of prosperity. But the top-down, directive management style that accompanies such activities often ensures that the business is reduced rather than renewed. There is destruction, but it may not be creative. To revert to the forest analogy, the forest has been logged but may not have been replanted — new organisms may not have been allowed to enter the ecospace.

Whereas the conventional organizational life cycle is the story of technical system's evolution, the renewal cycle is about the evolution of social systems. It is this emphasis on people and their interactions in the aftermath of crisis that allows one to explore the roots of innovation and the organizational contexts that nurture it.

Phase 5. Confusion and

Phase 6. Charismatic Leadership

Renewal begins in the confused aftermath of crisis,

which shatters the previous forms of hierarchical control. Out of the confusion there must emerge one or more charismatic leaders — individuals who act in ways that express their values and their beliefs about how people ought to relate to each other. Their actions are rational, not in a means-to-an-end, instrumental sense, but in the sense that their behavior consistently expresses a coherent belief system.

One of the best documented examples of charismatic leadership as part of a planned effort to renew a major organization is that of Jack Welch's efforts to transform General Electric. GE was not in any apparent trouble at the time, so Welch created a pre-emptive crisis. Shortly after he was appointed CEO in 1981, he announced that each GE business had to be either first or second in its market or it would risk disposal. This statement was widely criticized as being strategically naive. But it was not a rational statement of strategy; it was an emotional "call to arms," directed at getting the complete attention of the senior management group. Welch reinforced this message with action, delayering the management hierarchy, reducing corporate staff and slashing 100,000 employees to focus on what he believed to be the core elements of the business.

It is the confused aftermath of this "shake up," this creative destruction, that sets the stage for the values-based behavior called charismatic leadership. Now, managers have to live the values they espouse — "walk the talk" in current management jargon. Their action is rational, not because it is a means to an end, but because it is intrinsically valuable. Managers in this phase are models of the behavior they expect from others. They create the crisis, but then they have to join their followers in living out the consequences. It is anarchy, but it is ethical anarchy.

This values-based, rational action seems to be essential to attracting creative people and creating contexts that nurture innovation and entrepreneurship. It attracts to the charismatic leaders followers who are self-selected and who themselves can learn to lead. This allows a network of relationships to form, which is held together by shared values and an emerging vision of common purposes. With the emphasis on learning and the options it generates, the ability to choose is now restored to the renewed organization.



"RENEWAL BEGINS IN THE CONFUSED AFTERMATH OF CRISIS ..."

Phase 7. The Creative Network and Phase 8. Choice

The jury is still out on GE's transformation process. It is difficult to track it further along the ecocycle's back loop. The logic of the renewal cycle suggests that, if it is to be successful, groups of individuals will begin to gel around a variety of opportunities and projects and start to take entrepreneurial action. The individuals will have interacted with each other on the "boundaryless" networks developed in the contexts created by Jack Welch and his senior managers. In keeping with the emergent quality of activities in these phases of the ecocycle, the formation of small work groups and the projects themselves will appear to be spontaneous and lucky, rather than planned.

The cycle should progress in much the same way as it did at Blue Ribbon Sports (BRS) when Phil Knight and Bill Bowerman went through the creative process for the first time on their way to inventing Nike. At this time the organization had no permanent employees. A loosely connected network of athletes and suppliers was forming, anchored and sustained by the visions and passions of Knight and Bowerman. They were the nucleus of a new social system that would invent a new technical system.

To an outside observer at that time, the organization would have been invisible or, at the very least, diaphanous. One would have looked right through it and seen only a social network. Yet this was when BRS was the most acutely sensitive to its environment, and when small, insignificant events had significant consequences. That is why, in retrospect, the "founding" of the business often appears to consist of a series of unpredictable events and chance encounters with helpful people.

In the case of Nike, over time, the loosely connected network began to pulse in a pattern. If one had attended the track meetings where the athletes gathered to compete (and talk about their equipment), one might have observed how, after a brief bonding period, the patterns in the loosely connected network began to change. Using new distribution channels and some of the contacts they had made, Knight and Bowerman began to sell their shoes to a wider market. A more regular pattern of interactions began to

emerge as the contacts and events became linked into coherent flows and better articulated routines.

Soon a small, simple, but permanent structure formed and moved into the next phase of the ecocycle. At about this time, although insignificant in size, it became clearly visible to outside observers and was ready to be named. Nike was on its way.

CRISIS AND CREATION

It has been more than 50 years since Harvard economist Joseph Schumpeter described capitalism as a process of "creative destruction," yet managers may still find the organizational corollary of this — that organizational renewal requires crisis — to be a disturbing thought. They are not alone; the view that technological change and innovation in business is an instrumentally rational affair is a popular one.


Despite conventional wisdom, however, the evidence that crisis plays an important role in organizational innovation and technology is considerable.

At one level, the phenomenon is so familiar that we scarcely give it a second thought:

safety legislation is introduced in the aftermath of serious accidents, building codes are strengthened after earthquakes, shakeups of the armed forces follow military defeats, and economic and social reforms are enacted in the wake of depressions.

We usually think of such actions as being consciously introduced by rational reformers; but there is much evidence that innovation in the aftermath of crisis takes place on a far broader scale than just these direct actions. In the early 17th century, the English Civil War created

the context needed for the emergence of dissenting religious groups such as the Quakers, who were to play a central, entrepreneurial role in the English Industrial Revolution. The American Revolution created significant trading opportunities between America and Europe, resulting in the emergence of many new entrepreneurs and contributing to the formation of a new aristocracy of wealth and power. Also, it is thought to have encouraged the development and spread of the joint stock company and the rise in prominence of lawyers and law firms in American society. The American Civil War seems to have stimulated the



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transformation of the U.S. banking system and to have led to a good deal of innovation in the formation of federal government agencies.

Perhaps our failure to recognize the crucial role of crisis in organizational change is not so much an intellectual problem as it is a human problem. In human organizations, destruction is likely to seem creative only to those who are either at one level above the system being destroyed or who are outside of the situation altogether. Observers can agree that trees must burn to renew the forest and that organizations must fail if an industry is to remain competitive. But it is the people inside the system who are the subjects of change, and the resulting feelings of fear and uncertainty contrast unfavorably with the feelings of control and even omnipotence that characterized the previous phase of the organizational ecocycle.

It is no wonder that managers usually talk about making their businesses “fireproof,” a metaphor that conjures up notions of the protection and insulation of valuable assets — and themselves — from external events. But while things that are insulated from the environment may be preserved, they are also unable to develop and hence unable to be renewed.

The approach used by 3M yields a different perspective. This company appears to have institutionalized the systematic “burning” of its mature businesses using internal methods. They insist that all of their 50 or so divisions generate at least 30% of their sales from products introduced within the past four years. At the same time, the organization’s culture clearly encourages extra-curricular activities — for example, they allow employees to spend up to 15% of their working time on personal projects. The well-known story of the evolution of the **Post-it**TM note and its initial rejection by senior management suggests even more subtle cultural aspects of 3M that facilitate the mobilization of their people’s talents. Far from making their businesses fire-resistant, 3M’s reliance on crisis

seems to make them fire-dependent. Exposure of the businesses to the environment allows them to be renewed.

In its use of such a process, 3M bears a striking resemblance to the behavior in nature of the community of shrub-land plants known in the American Southwest as chaparral. Chaparral is fire-dependent for its growth: as they age, plants within the community secrete volatile oils and esters that are highly flammable. When ignited by lightning or other sources, the plants burn fiercely. Fire destroys decadent growth and accumulated litter, recycles nutrients and promotes vigorous growth in seeds and shoots, which are themselves protected from fire. Just as is the case in 3M, it is the fire-dependence of the chaparral that promotes growth and allows it to survive.

But what are the equivalents of “seeds” and “shoots” in human organizations? What is the “it” that survives during renewal and allows us to say that such-and-such an organization has been renewed? “It” is not the people or their possessions, the customers or the suppliers. “It” is not the physical or legal structures, products or technologies. All these can and will change. “It” can only be non-physical “things” — shared beliefs, stories, memories, visions and values. Only they have the capacity to create meaning and inspire people — to regenerate and renew an organization.

This is true of people who once worked for any organization to which they felt an emotional attachment. When everything else is gone, they will still remember the visions, values and social contexts that once inspired the commitment of thousands to work together. Wherever they are, these contexts may be recreated and knowledge of them passed on to the next generation. Thus “the company” remains as patterns of interaction in an immense network, vast beyond our comprehension. But through this network, the patterns have the potential to be reincarnated in new, formal organizations at any time. Perhaps, in the long run, this is the only sense in which any human organization survives. **BQ**