Managing complexity

Apple is a company that manages the complexities of today's business environment to great benefit

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Companies should start a simplicity revolution in the face of an ever-more complicated world

TODAY'S GLOBAL ECONOMY is an increasingly complex environment in which to do business. Executives have to face complexity on all fronts of their operations, as they adapt to globalisation, demographic shifts, climate change, emerging economies, social and economic change, and the sheer pace of innovation. But just what is it that leads previously successful multinational corporations – one-time darlings of their industries such as Nokia or the Royal Bank of Scotland – to struggle when their outwardly similar competitors continue to perform consistently, even in difficult financial environments?

Whether by accident or design, the more usual reaction of businesses facing increased complexity has been to increase their internal complexity through increased size, greater diversity of functions or more levels of hierarchy. But a study by the Advanced Institute of Management (AIM) Research finds that this is not necessarily the best response.

The research, led by Professor Simon Collinson, Lead Ghoshal Fellow at AIM, and Melvin Jay, one of the founders of a management consultancy firm called Simplicity, sets out to map not only how different businesses respond to complexity but also how their responses have affected their performance. What they find is a definite pattern of both 'good' and 'bad' complexity: the challenge for businesses is to identify which organisational complexity adds value and contributes to performance, and which adds costs and damages performance. Nearly two thirds of the managers interviewed for the research report that complexity is responsible for over five per cent of productivity loss, and as many as one in ten reported a 30 per cent loss of productivity.

Professor Collinson and Mr Jay have created the Global Simplicity Index, which takes the largest 200 firms in the Fortune Global 500 and ranks them according to their complexity and performance, to help them further understand the relationship. They identify four types of firms and their particular challenges:

SIMPLIFIERS: low-performing organisations with low levels of complexity, which have failed to capitalise on value-creating forms of complexity
PERFORMERS: high-performing organisations with low levels of complexity, which have managed to perform without over-complicating their business

Who you know

The role of social ties in corporate board appointments

MEMBERSHIP OF ELITE private clubs continues to influence boardroom appointments, according to research by Edward Cowley and Dr Helen Simpson of the ESRC Centre for Market and Public Organisation (CMPO) at the University of Bristol. But social connections made at school or university seem to play less of a role in board appointments and the careers of company executives.

In 2011, Lord Davies' Review of Women on Boards reported that: "The informal networks' influence in board appointments, the lack of transparency around selection criteria and the way in which executive search firms operate, were together considered to make up a significant barrier to women reaching boards."

The CMPO researchers have gathered a wealth of information to examine the impact of these informal networks. They analyse data on the educational and employment backgrounds of board executives, their positions on boards of trustees, and affiliations to private members' clubs and golf clubs. The research asks whether the likelihood of gaining further board appointments is related to these social connections. More precisely, it examines whether an individual is more likely to be appointed if he has a link with someone already on the board – for example, through membership of the same golf club, such as Wentworth or Sunningdale, or the same private members' club, such as the Reform Club or White's.

The findings suggest that social connections through these clubs, as well as networks of contacts established through existing boardroom positions, play an important role in shaping who gains a seat on a board. Educational connections established through attending an elite school, such as Eton, or the same Oxford or Cambridge college, play a lesser role, although they may well have a prior influence on social club memberships.

The data encompass individuals who had already gained their first boardroom position. For

COMPLICATORS: high-performing organisations with high levels of complexity, which generally manage to couple high complexity with performance, but are still losing profits because of value-destroying complexity
STRUGGLERS: low-performing organisations with high levels of complexity, who are finding it difficult to manage the high levels of complexity that damage their performance

THE SIMPLICITY REVOLUTION

By interviewing managers in these firms, the researchers identify six main drivers of complexity: the external environment; strategic choices; the company's product and service portfolio; organisational structure; management processes and procedures; and the behaviour of people. These are big, intimidating challenges for managers to deal with – encompassing everything from the global financial crisis to the inherent, intrinsic complexity that develops in a rapidly-growing firm in a new industry – and as a result many companies place tackling this complexity on a list of problems 'too difficult to deal with'.

But the researchers argue that there are ways companies can start a simplicity revolution. They suggest a programme of diagnosing the sources of complexity, prioritising the changes that need to be made and focusing on how to solve the major problems. Change must begin at the top for it to be effective across the organisation, and all employees must be engaged in the process.

There is undoubtedly a cost involved in reducing complexity in an organisation, but 'Performer' companies such as Apple, Microsoft and GlaxoSmithKline are testament to the value that can be gained. For those companies who manage to solve the complexity conundrum, there is competitive advantage to be had. ■

www.simplicitypartnership.com
www.aimresearch.org

this group with existing board experience, women actually appear more likely to gain additional board positions than men. But if social connections are also important for a *first* executive appointment, then the role of networks formed through mainly or exclusively male social clubs is likely to prove a barrier to increasing female representation on boards.

In relation to this, one recommendation from Lord Davies' Review is that firms should make more information available about their appointments process and the work of their nomination committees. This is probably the best way to improve transparency in recruitment and subsequent board diversity. ■

www.bis.gov.uk/assets/biscore/business-law/docs/w/11-745-women-on-boards.pdf
www.bristol.ac.uk/cmpo

Finding 'big, fixable problems'

The key to building enterprises and creating jobs in Africa

LARGE-SCALE, LONG-TERM job creation is essential for Africa's future. But while diagnosing the continent's wide range of economic ills is easy, what is really challenging is implementing solutions. In pioneering work for the International Growth Centre (IGC), Professor John Sutton of the London School of Economics emphasises the need to find and fix a small number of 'big, fixable problems'.

The best way to do that, he says, is to construct 'enterprise maps' of national economies – complete descriptions of their industrial structure and the existing capabilities of major firms. These can provide the low-level background knowledge for governments, local companies and overseas companies looking at opportunities for foreign direct investment (FDI). Having worked on enterprise maps for a number of sub-Saharan African countries, Professor Sutton points to a number of big, fixable problems, including difficulties with transferring land rights; illegal exporting to get round protection of infant industries; and an absence of mid-level finance for mid-sized companies.

Careful monitoring and development of FDI ventures should be a key focus of policy concern

Professor Sutton mentions industries that are seen almost everywhere in Africa – beer, cement, sugar – and the capabilities that they require – selling to a 'safe' local market, high transport costs and the absence of an international supply chain with other firms whose quality standards domestic firms must meet. He also describes the most notable scarcity in African countries – not entrepreneurship, which is abundant, but a cadre of middle managers with the market intelligence and ability to run mid-sized companies effectively. Mid-sized diversified companies – capable of spotting domestic market opportunities, often through 'import substitution' – are the ones most likely to generate much-needed jobs.

THE ETHIOPIAN STORY

The IGC has published the first of Professor Sutton's studies as *An Enterprise Map of Ethiopia*. The book describes the history and current capabilities of the country's leading industrial companies (agribusiness, manufacturing and construction), focusing on 50 key large- and mid-sized firms. The motivation is to help with the expansion of economic capabilities in Ethiopia by first understanding where the capabilities of the existing successful companies came from. The 50 firms represent almost all the largest firms in their respective sectors.

One of the book's most important observations is the fact that around half the leading firms in Ethiopia have emerged from the import/export (trading) sector. This is where the deepest and most acute knowledge of local and international market conditions is already at hand. A common and unfortunate tendency among many observers of developing economies is to see the trading sector as separate from and irrelevant to the growth of manufacturing industry. But these firms have a vital role in seeding successful manufacturing firms.

THE ROUTE TO FUTURE GROWTH

A second important observation is that among the 50 leading firms, only two can trace their origins back to a small domestic firm. The second private sector source of Ethiopia's leading industrial companies is foreign companies. This is likely to be an increasingly important route to future industrial growth – and the inflow of FDI in the past decade has been increasing significantly from a very low base. Four countries are leading this phenomenon: China, India, Saudi Arabia and Italy. Their FDI projects span every sector of Ethiopian industry. The book concludes that careful monitoring and development of FDI ventures should be a key focus of policy concern over the next decade.

Another crucial issue of economic policy the book identifies is import substitution – developing local industry to provide substitutes for expensive imports – and the need to nurture this on a level playing field with export projects, which tend to be given preferential treatment. Finally, the book addresses issues of access to medium-term finance for growth, and the availability of land for industrial use. ■

www.theigc.org/sites/default/files/sutton_pdf.pdf