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On the Road to Disaster: Strategic Misalignments and Corporate Failure



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Prior research has identified the link between strategic misalignment and corporate failure, but little empirical research to date has examined the process leading to misalignment and eventual corporate failure over time. To explore this crucial link, we conducted in-depth case studies of two American conglomerates: WorldCom and Nortel Networks. We find patterns in terms of factors through which misalignments develop, ultimately leading to bankruptcy. The process begins with dysfunctional leadership and ineffective corporate governance, moving to unduly risky strategic actions, which are then followed by lax execution. Gradually spreading organizational misalignments develop, which ultimately foster a large gap between the demands of the competitive environment and the organization's strategy and competencies, leading to failure. An unforgiving external environment exacerbates the effects of misalignments. With this study, we also expand the ESCO strategic alignment model (Environment, Strategy, Core Competencies, and Organization), by adding leadership as the actor guiding alignment, and sustainable advantage as an outcome.

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Introduction

Corporate bankruptcy rates have soared. Between 2007 and 2010, total bankruptcy rates rose by 87.2% (Flynn and Kearns, 2011). Among the bankrupt organizations in recent years were numerous multinationals, once healthy and leading corporations such as General Motors, Delphi, Tribune Group, Consec and Chrysler. Why do so many previously highly successful firms fail? Organizational failure can be brought about by strategic misalignments; e.g., an inappropriate strategy for the external environment, or a poor operationalization of the strategy. Strategic alignment is the consistency and synergy among the external environment, the strategy, core competencies, and organizational elements such as culture, organization design, processes and people (Heracleous et al., 2009). Conversely, strategic misalignment is inconsistency or tension among these elements.

Whereas the link between strategic alignment and competitive advantage (and conversely misalignment and failure) has been recognized (Beer et al., 2005; Miles and Snow, 1984a; Powell, 1992) the processes of how strategic misalignments can develop over time and lead to corporate failure have not yet been explored. Despite their valuable contributions, most studies on corporate failure have adopted a fairly static orientation, rather than a time-sensitive, processual perspective of how a corporation can move towards failure (Zajac et al., 2000). In light of environmental dynamism, and the insights that can be afforded by a longer-term examination, scholars have called for research that examines fit and alignment "within a longitudinal perspective" (Venkatraman, 1989, 441). In our research, we take such a perspective and examine how misalignments can develop over time, ultimately leading to corporate failure.

Are there typical patterns of strategic misalignments? What are the processes that can lead to failure if left unchecked, and can we identify factors leading towards failure? We explore these questions by applying a strategic alignment perspective that examines the interrelated levels of environment, strategy, competencies and organization (Heracleous et al., 2009). We begin with a discussion of the literature relating to strategic alignment and corporate failure. We then outline our research methodology and provide a brief background of the case studies, followed by the case analysis and findings. The analysis involves individual as well as cross-case analysis, upon which we develop a model of decline and failure. We then conclude with a discussion and contributions.

We identified six interrelated factors of strategic misalignment, whereby, the first three mark the most significant antecedents leading to corporate failure. Once strategic misalignments are established at one organizational level, further misalignments expand from this level to various other areas inside the organization. In the latter stages, significant gaps are created between the strategy and competencies of the firm, and between strategy and the demands of the competitive environment, which leads to corporate failure.

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Strategic alignment and performance

It has been recognized that several factors can influence a firm's performance. These include external factors such as changes in the industry and environmental uncertainty, as well as internal factors such as coordination and control, age, size, corporate culture and leadership (Anderson and Tushman, 2001; Fredrickson, 1986; Freeman et al., 1983). An alignment perspective attempts to interrelate such factors both internally within an organization, and between an organization and its environment. The logic is that internal organizational alignment or fit, as well as alignment with the external environment, are necessary requirements for any firm to ensure survival and success in the long run (Beer et al., 2005; Miles and Snow, 1984a; Porter, 1996). A distinction between descriptive and normative fit has been made, where the former is mostly concerned with description of the existing situation without explicit reference to performance, and the latter explicitly focuses on the alignment-performance relationship (Venkatraman, 1989).

Within strategic management, the alignment approach grounded in industrial economics or contingency theory is referred to as an "outside-in approach" (Voelpel et al., 2006). Strategy and structure are viewed here as being a response to external factors, which act as key determinants of the firm's performance (Ginsberg and Venkatraman, 1985; Porter, 1980; Venkatraman and Camillus, 1984). In contrast, the resource-based view, referred to as an "inside-out approach" (Voelpel et al., 2006), emphasizes internal elements such as resources and capabilities as routes to competitive advantage (Barney, 1991; Grant, 1991; Wernerfelt, 1984). Despite contrasting perspectives on directionality, both schools of thought concur that strategic alignment can lead to sustainable competitive advantage and, conversely, misalignment can lead to failure (Chabrak and Daidj, 2007; Miller, 1996; Porter, 1996; Powell, 1992). Holistic models of strategic alignment have endeavored to incorporate several interrelated factors. Such frameworks include the classic McKinsey 7-S model (Waterman et al., 1980), as well as the more recent ESCO model (Heracleous et al., 2009).

We discuss domains of alignment along the lines of the ESCO model (Environment, Strategy, Core Competencies and Organization) (Heracleous et al., 2009). This model suggests that a company's strategy has to be aligned with its competitive environment. It also has to be supported by appropriate core competencies, which can be delivered through suitable organizational configurations (including culture, structure, processes and people). Figure 1 below shows the ESCO model.

Four domains of (Mis)alignment: environment, strategy, core competencies and organization

With regard to environmental change, firms are faced with discontinuity and rapid changes caused by technological development, disruptive innovations, intense global competition, alterations in governmental regulations, and shifts in industry structures (Beer et al., 2005; Crossan et al., 2008). Many market environments have reached unprecedented levels of complexity, uncertainty and dynamism (Ireland and Hitt, 2005). While in the past, due to comparatively stable market conditions, alignment among a firm's strategy and external environment was easier to achieve, the dynamics have become significantly more challenging. A firm's insufficient realignment to drastic environmental changes represents one of the most common and dangerous sources of misalignment in organizations (Heracleous et al., 2009).

The second alignment element, strategy, includes the classic classifications proposed by Porter (1985), Hannan and Freeman (1986) and Miles et al. (1978), who emphasize the need for clear strategic choices. Dynamic views of strategy recognize that competitive advantage is fleeting, constant realignment between strategy and environment is needed (Ghemawat, 1991;

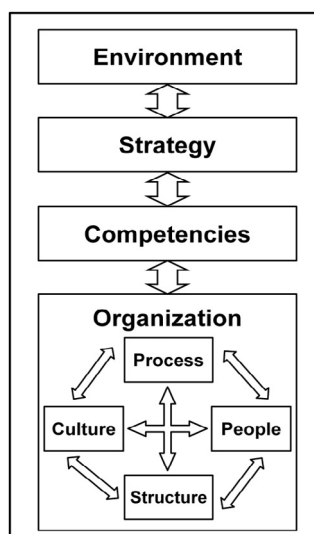


Figure 1. The ESCO model

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