

MGMT 452: STRATEGY AND ORGANIZATION

Winter 2012

Sections 61

Jin Li

Course Description

This course focuses on the link between organizational structure and strategy. The core question the course addresses is how firms should be organized to achieve their performance objectives. To do so, the course makes heavy use of the microeconomic tools taught in MECN-430. The first part of the course takes the firm's activities as given and studies the problem of organizational design; topics include incentive pay, decentralization, transfer pricing, and complementarities. The second part examines the determinants of a firm's boundaries and covers such topics as horizontal and vertical mergers, outsourcing, and diversification. The course consists of both lectures and case discussions. Prerequisites: MGMT-431, MECN-430.

Office Hours

I have an open door policy and I encourage you to stop by whenever you want to talk. **If you want to make sure that I'm around you should come by during my official office hour which is Tuesdays 3.30 – 4.30pm.** My office number is 630 and it is located on the 6th floor of Jacobs. To get to there you want to take the elevators in Leverone Hall. You can also call (847 – 467 0306) or email me (jin-li@kellogg.northwestern.edu).

Laptop Policy

I have a no laptop policy that also covers all other electronic devices such as smartphones and the like. There are, however, two exceptions. First, the mid-term and final exams. Second, classes during which we need the laptop for teaching purposes. Such classes are indicated in the weekly overview below.

Grading

Your final grade will be based on the following four components:

- Team Performance (20% of final grade): Your grade on team performance will be based on two components:
 - **Team assignments:** There are **two written team assignments**, the first one is due on Jan 29 and the second on Mar 11. You should submit your answers via Blackboard. Teams must have between four and six members. You can form your own team. If you have trouble finding a team, let me know and I will help you.
 - **Peer review:** At the end of the quarter I will ask your team members to assess your performance in helping to prepare the answers to the written team assignments. Of course I will also ask you to assess their performances.
- Individual Class Performance (20% of final grade): Your grade on individual class performance will be based on three components:
 - **Participation in class discussions.**
 - **Individual assignments:** There are **two written individual assignments**, the first one is due on Feb 5 and the second on Mar 4. You should submit your answers via Blackboard.
 - **Case discussion questions:** You are required to submit **brief answers to the case discussion questions** for all cases, except the first one. Bullet point format is fine. The questions are listed in the weekly overview below. You should submit your answers via Blackboard before class.
- Midterm exam (20% of final grade): There will be a **midterm exam on Monday, Feb 13.**
- Final exam (40% of final grade): There will be a **final exam during finals week.** The final will cover the material from the entire course (not just the second half).

Reading Material

The **only required reading are the cases** and they are all **included in the casepack**. The casepack also includes some background material which you may find useful but which you are not required to read. I will post additional material on Blackboard.

Week 1

Strategy & Organization

- **Wednesday, Jan 4 (Makeup for Jan 2 class):** Case Discussion
 - **Required reading:** “*Keller Williams Realty.*”
 - **Assignments due:** None
 - **Discussion questions:** None

- **Thursday, Jan 5:** Lecture
 - **Required reading:** None
 - **Background reading:** Chapter 10, Rewarding Performance, in *Personnel Economics in Practice*, by Lazear, Edward P; Gibbs, Michael.
 - **Assignments due:** None

Week 2

The Economics of Motivation: Paying for Performance

- Monday, Jan 9: Lecture
 - **Required reading:** None
 - **Background reading:** Same as for the previous lecture.
 - **Assignments due:** None

- Thursday, Jan 12: Case Discussion
 - **Required reading:** “*The Lincoln Electric Company.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Other:** Watch the video about Lincoln Electric on Blackboard.
 - **Discussion questions:**
 1. Which ten features of Lincoln Electric’s human resources and compensation policy do you find most noteworthy?
 2. What are the advantages and disadvantages of Lincoln Electric’s piece rate system and the way it is implemented?
 3. What are the advantages and disadvantages of Lincoln Electric’s guaranteed employment policy?

Week 3

Motivating Teams: Initiative versus Cooperation

- **Wednesday, Jan 18 (Makeup for Martin Luther King Day Class):** Lecture
 - **Required reading:** None
 - **Assignments due:** None

- Thursday, Jan 19: Case Discussion
 - **Required reading:** “*Family Feud (A): Andersen versus Andersen.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Discussion questions:**
 1. Why did Arthur Andersen originally enter into consulting? Are auditing and consulting complementary activities?
 2. Consider the structure of Andersen Worldwide after the Florida Accord. Identify two ways in which the 15% transfer destroyed value in the organization?
 3. Can you propose a system that performs better than the 15% transfer rule?
 4. Do you think that the total joint value of Andersen Consulting and Arthur Andersen is highest if they stay together under Anderson Worldwide or if Andersen Consulting is spun off as a separate company?

Week 4

Decentralization I: Managing Externalities

- Monday, Jan 23: Case Discussion
 - **Required reading:** “*Transfer Pricing at Timken.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Other:** Download the Timken spreadsheet from Blackboard and bring your laptop to class.
 - **Discussion questions:**
 1. The Automotive Division of Timken expressed concern that the transfer pricing policy for steel transfers did not allow the automotive division to exercise its considerable market power as a purchaser of bearings quality steel. Do you think their concerns were valid?
 2. Did market-based transfer pricing rules for steel products provide divisional managers at the steel and automotive division with the right information and incentives?
 3. What are the advantages and disadvantages of cost-based transfer prices compared to market-based prices?

- Thursday, Jan 26: Lecture
 - **Required reading:** None
 - **Background reading:** Chapter 17: Divisional Performance Evaluation." In *Managerial Economics and Organizational Architecture*, 4th, by Brickley, James A; Smith, Clifford W; Zimmerman, Jerold L. 4th. pp. 477-508.
 - **Assignments due:** None

- Sunday, Jan 29: Assignment Due Date
 - **Assignments due:**
 - Team Assignment 1 is due by 12.00am (midnight).
 - Submit assignment via Blackboard.

Week 5

Decentralization II: Coordination

- Monday, Jan 30: The Corporate Turnaround Game
 - **Required reading:** None
 - **Assignments due:** None
 - **Other:** In this class we will play a computer game. It is crucial that you bring your laptop. If you don't bring your laptop you will not be able to participate.

- Thursday, Feb 2: Case-Based Lecture
 - **Required reading:** “*Continental Airlines: The Go Forward Plan.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Discussion questions:**
 1. If you were an hourly employee at Continental, how would you respond to the on-time bonus the company is offering? How would you expect your fellow hourly employees to respond?
 2. If you were a Continental shareholder, would you think that the bonus is a good use of your money? Why or why not?

- Sunday, Feb 5: Assignment Due Date
 - **Assignments due:**
 - Individual Assignment 1 is due by 12.00am (midnight).
 - Submit assignment via Blackboard.

Week 6

Prediction Markets

- Monday, Feb 6: Lecture
 - **Required reading:** None
 - **Background reading:** “*Prediction Markets at Google.*” I will distribute this case after class.
 - **Assignments due:** None
 - **Other:** Download the Google spreadsheet from Blackboard and bring your laptop to class.

- Thursday, Feb 9: Case Discussion and Midterm Review
 - **Required reading:** “*Examining Trader Behavior in Idea Markets: An Implementation of GE’s Imagination Markets.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Discussion questions:**
 1. How does GE’s idea market differ from a prediction market? How can it be turned into a prediction market?
 2. How would you address the problem of market manipulation by the idea founders?
 3. What distortions do you expect to result from the winner-takes-all system used to reward traders? Can you think of a simple modification that would solve the problem?

Week 7

Mid-Term Exam

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The Strategic Effects of Organizational Changes

- Monday, Feb 13: Mid-Term Exam

- Thursday, Feb 16: Lecture
 - **Required reading:** None
 - **Assignments due:** None

Week 8

Horizontal Mergers

- Monday, Feb 20: Lecture
 - **Required reading:** None
 - **Assignments due:** None

- Thursday, Feb 23: Case Discussion
 - **Required reading:** “*Whole Foods Market and Wild Oats Merger.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Discussion questions:**
 1. What are the main strategic challenges that Whole Foods faced before the merger with Wild Oats?
 2. How does the merger help Whole Foods meet these challenges?
 3. In your view, is the merger primarily a market power merger or an efficiency merger? Was the Federal Trade Commission right to challenge the merger?

Week 9

Vertical Integration I: Market Power

- Monday, Feb 27: Lecture
 - **Required reading:** None
 - **Background reading:** “Vertical Restrictions.” In *Modern Industrial Organization, 3ed*, by Carlton, Dennis W; Perloff, Jeffrey M. 3rd. pp. 522-538.
 - **Assignments due:** None

- Thursday, Mar 1: Case Discussion
 - **Required reading:** “*Pharmaceutical Industry in the 1990s.*”
 - **Assignments due:** Submit brief answers to the case discussion questions via Blackboard. The deadline is 1.30pm. The questions are listed below.
 - **Discussion questions:**
 1. How is the structure of the pharmaceutical industry changing in the 1980s and 1990s?
 2. Why do you think the pharmaceutical companies are merging with prescription-benefits-management companies (PBMs)?
 3. Will these vertical mergers reduce or intensify competition in the pharmaceutical industry and why?

- Sunday, Mar 4: Assignment Due Date
 - **Assignments due:**
 - Individual Assignment 2 is due by 12.00am (midnight).
 - Submit assignment via Blackboard.

Week 10

Vertical Integration II: Market Foreclosure

- Monday, Mar 5: Lecture
 - **Required reading:** None
 - **Background reading:** “Vertical Restrictions.” In *Modern Industrial Organization, 3ed*, by Carlton, Dennis W; Perloff, Jeffrey M. 3rd. pp. 522-538.
 - **Assignments due:** None

- Thursday, March 8: Lecture & Case Discussion
 - **Required reading:** “GE/Honeywell Merger.”
 - **Background reading:** “Vertical Restrictions.” In *Modern Industrial Organization, 3ed*, by Carlton, Dennis W; Perloff, Jeffrey M. 3rd. pp. 522-538.
 - **Assignments due:** None.

- Sunday, March 11: Assignment Due Date
 - **Assignments due:**
 - Team Assignment 2 is due by 12.00am (midnight).
 - Submit assignment via Blackboard.