case sixteen
General Electric: Life after Jack

Teaching Note

Synopsis

The case looks at GE at a time of management change and considerable uncertainty. Jack Welch, Chairman and CEO of GE for 20 years and widely regarded as one of the greatest business leaders of the past 100 years, has retired. Jeff Immelt has the daunting task of following Welch at a time when GE is facing a combination of challenges: sharply reduced demand in several key businesses (notably turbines and jet engines), its financial reporting is subject to increasing scrutiny, and the financial strength and stability of GE Capital is being questioned.

The case offers an opportunity to review the state of GE and assess its strategy, structure, and management systems, as well as address the thorny question being asked by an army of financial journalists and stock-watchers: where does GE go next?

GE is not just one of the world's great corporations; it is also an anomaly. In an era when most conglomerates have been breaking up their diversified structures and releasing shareholder value by spinning off their separate businesses, General Electric, one of the world's biggest, oldest, and most diversified corporations, has maintained a vast array of businesses that stretch from TV broadcasting to jet engines. Under its remarkable CEO, Jack Welch, to whom much of the credit is due, the company went from strength to strength. GE's spectacular performance in terms of growth, profitability, and shareholder return have been attributed to the two decades of continuous strategic and organizational change, behind which Welch was the driving force.

The bulk of the case is concerned with the strategic and organizational innovations implemented by Welch from 1981 to 2001. Welch's tendency to communicate

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these initiatives through slogans ("Being #1 or #2 in your sector," "Speed, simplicity, self-confidence," "the boundaryless corporation," "The GE growth engine," "Workout") makes them seem simplistic. Yet, taken together, Welch created a new system of management at GE that reflects penetrating insights into the nature of strategy and management in the mature corporation and a novel approach to coordination and control in the multibusiness enterprise.

The case offers the opportunity for a retrospective view of Welch's career as chairman of GE and to reflect on how the diversified firm can create value for its constituent businesses through the management systems and processes that it creates. It provides the opportunity to assess the extent to which such systems and processes need to be associated with a charismatic leader, and whether a new CEO, with a different personality and facing different external challenges, must inevitably redefine the strategy and systems of the corporation.

Teaching Objectives

The case asks how and under what circumstances a diversified corporation creates value for its constituent businesses. This raises some fundamental issues concerning the relative roles of firms and markets in coordinating different business activities. The prevailing wisdom has been that, in an era of turbulent economic conditions and efficient markets, the diversified firm is at a disadvantage to specialized firms that transact through markets for their inputs and are free of the costs and inertia of the corporate infrastructure of the diversified firm. GE's success forces students to reevaluate this conventional wisdom and to consider more circumspectly the potential for corporate management systems to contribute to business-level performance.

The case also introduces issues of leadership. How important can a single individual be in determining the performance of a corporation employing 300,000 people? To what extent can a corporation's strategy, structure, and systems be viewed as an extension of the vision and personality of its CEO? Such issues are critical for the management of executive succession and central to comprehending the challenge facing the new CEO.

Position in the Course

The GE case fits into the corporate strategy section of a strategic management course.

Assignment Questions

1. What were the principal strategic and organizational changes introduced by Welch at GE and inherited by Immelt?

2. Why have the strategy, structure, and systems created by Welch at GE been so successful, not just in delivering shareholder value during the 1980s and

1990s, but also in making GE seemingly invulnerable to the calls for breakup that have overwhelmed most other conglomerates?

3. Can you detect a theory of management or set of general principles that link together Welch's various initiatives?
4. To what extent should other large, diversified corporations imitate the management systems and leadership style developed by Welch at GE?
5. What changes in strategy, organizational structure, and management systems and style should Jeff Immelt be implementing in order to sustain and revive GE's track record of superior performance? In particular, should GE consider breakup (like so many other highly diversified companies)?

Reading

R. M. Grant, *Contemporary Strategy Analysis* (5th edn), Blackwell Publishing, 2005, chapter 16.

Analysis

1. *What were the principal strategic and organizational changes introduced by Welch at GE?*
   I begin by building a list of the principal initiatives pushed by Welch during his tenure as chairman. I organize these into three main categories as follows (the table is just a partial list):

STRATEGIC CHANGES	STRUCTURAL CHANGES	CHANGES IN MGMT SYSTEMS
Being no. 1 or no. 2 in each global market	De-layering (including removing the sector level)	Bigger performance incentives
The "3-circle" conceptualization	Widening spans of control	Stretch financial targets
Divesting mining, housewares, etc.	Shrinking headquarters departments	Reorganization of strategic planning
Growing in services – especially financial services	Workout – initiating organization change from below	Shifting basis of control from approvals (inputs) to performance (outputs)
Cost cutting		The boundaryless company
Globalization		The six-sigma quality program

2. *Why have GE's strategy, structure, and systems been so successful in creating value?*
   To address this issue, I ask why it is that most other highly diversified companies (ITT, ABB, Vivendi, Hanson, Grand Metropolitan, General Foods)

experienced so much difficulty during the 1980s and 1990s and, for the most part, were forced to refocus or break up entirely. Several factors should emerge from this discussion:

- Lack of shareholder focus. Much of the diversification of this (and earlier periods) was driven by corporate empire building rather than a quest for shareholder value.
- The increasingly volatile business environment of the 1980s and 1990s put huge pressure on the organizational structures and management systems of these companies. The need for rapid decision-making and fast-response capability meant that smaller, more focused companies were able to respond more quickly and purposefully than the giant, multi-divisional corporations with more hierarchical levels, and more complex decision-making procedures.
- The increased efficiency of capital markets and markets for technology and labor meant that the internal markets for capital, labor, and technology of the diversified corporation became less efficient as compared to more specialized companies that accessed factor markets directly.

So, what is different about GE? Several factors appear to be important here:

- Under Welch, GE was resolutely focused on shareholder value creation and these goals were enforced by a culture and performance management system that made GE's individual businesses strongly oriented towards the goals of profit maximization and value creation. The financial controls of GE and its system of linking divisional CEOs' remuneration very closely to value creation resulted in GE's internal system providing incentives to business-level managers that were highly effective in driving value creation.
- GE avoided the problems of bureaucracy and unresponsiveness to market requirements that are characteristic of large, multibusiness corporations. Under Welch, GE de-layered, resulting in faster decision making and greater responsiveness both to the external environment and to the performance demands of the corporate HQ. The simplification of strategic planning systems and increased accountability of business-level managers reinforced speed and responsiveness.
- GE was able to combine a strong performance orientation of its individual businesses with considerable gains from sharing resources between businesses. Welch's initiatives such as "boundarylessness," "six-sigma quality," and globalization resulted in highly effective technology transfer, sharing of best practices, and collaboration in new market development.
- GE's human resources practices sustained not just strong performance incentives among employees at all levels, but also considerable investment in skills and expertise. This was especially evident among GE's managers. GE's ability to attract highly capable MBAs and young managers, and its system for developing these managers – especially through career paths that allowed considerable internal mobility between businesses – provided GE with the deepest and most accomplished cadre of business managers of any corporation.

- GE's business portfolio, although exceptionally broad, was also carefully constrained to include only the types of business where GE's resources and capabilities had the potential to add value. GE's business portfolio seems impossibly broad – yet most of these businesses were mature, capital intensive, and global in scope. All represented potentially good fits with the financial control, strategic management, and human resource systems of the corporation.

3. *Can you detect a theory of management or set of general principles that link together Welch's various initiatives?*

   I try to bring out the following points:

   - Many of these initiatives are deceptively simplistic. I ask the students to consider the "#1 or #2 position in your global market" dictum. This is far less sophisticated than the GE portfolio-planning matrix deployed during the 1970s (see Grant, pp. 477–84). Early in their strategy course, students learn that competitive advantage and superior performance cannot be equated with market share. So what is the thinking behind Welch's "#1 or #2 or else . . ." threat? First, it is simple, which means it is easy to communicate and can provide an initial screen. Second, it carries a powerful motivational incentive to divisional managers – we had better move to a leadership position in our market quickly. Third, it focuses divisional managers on the world market. Finally, it links with GE's core competencies – unlike Virgin, GE is not good at new business startups; where it can add value is in squeezing costs and driving growth in big, powerful businesses.
   - Welch's strategy involves a continued commitment to diversification, but in a more focused way. GE's business portfolio is designed around the principles of (1) focusing on attractive industries (hence, exit from mining and small household appliances), (2) focusing on businesses where GE's corporate-level capabilities of strategic planning, managing globalization, financial control, and the development of general managers can be effectively deployed, and (3) building interlinked sets of businesses (the 3-circle views of GE).
   - Welch's organizational transformation of GE is built upon the view that a large diversified corporation can outperform a set of independent specialized companies. The critical task is to build a corporate-level system that can enhance the performance of the individual businesses. The key to Welch's model of the multibusiness corporation is reconciling the advantages of size and diversity with the flexibility and responsiveness of the small, specialized company. The changes in incentives, de-layering, and control systems may be viewed as creating conditions for fostering entrepreneurial flexibility in the business. Control becomes performance based (i.e., *ex post*) rather than based upon decision approvals (*ex ante*). Coordination and control are also shifted towards influencing behavior and culture. Welch's exhortations for "simplicity, speed, self-confidence" and "boundarylessness" are attempts to boost performance through

influencing behavior and values. Finally, Welch recognizes that a critical feature of GE's corporate system is its management development process. Throughout all of Welch's leadership we can see the priority he gives to developing general management capabilities throughout the company. If GE is to survive and prosper for another century, it will be its ability to continually develop high-caliber executives that will be the key.

- Welch embraces management as a dynamic process. Unlike his predecessor Jones, Welch is not attempting to build an optimal system. Welch recognizes that a performance-driven organization must be in constant change. A key feature of Welch's leadership has been the introduction of a succession of initiatives. As soon as one is established, another is introduced to drive some other area of company performance.
- Welch embodies a particular approach to leadership. His role has been less of a decision-maker or corporate statesman and much more a catalyst for organizational change. It is a tribute to Welch's remarkable stamina and commitment that he has spent 18 years continually battling with his own company in continually pushing change and fresh thinking.

4. *To what extent should other large, diversified corporations imitate the management systems and leadership style developed by Welch at GE?*
As one of the world's most observed, written-about, and admired chief executives, it is inevitable that Welch's style and actions have been widely imitated. Indeed, we must not go overboard in attributing all Welch's activities to his own initiative. From organizational de-layering to six-sigma, Welch has adopted concepts and techniques from other companies and from prevailing management practice. Probably the most important learning from the Welch/GE case is that, even under conditions of turbulence with the availability of highly efficient markets for capital and most other inputs, it is possible for the diversified corporation to outperform specialized enterprises. The critical issue is to establish corporate systems of coordination and control and a corporate culture that foster motivation, entrepreneurship, cooperation, best-practice sharing, and human resource development. The specific initiatives and approaches introduced by Welch at GE can be and have been adapted to the requirements of other companies.

5. *What changes in strategy, organizational structure, and management systems and style should Jeff Immelt be implementing in order to sustain and revive GE's track record of superior performance? In particular, should GE consider breakup?*
Identifying the challenges that GE faces and recommending changes to meet these challenges is a difficult task. The important issue here is to distinguish strategic and longer term issues from the short-term problems that GE is facing in 2002. These immediate issues concern the transparency of GE's public accounting, the stock-market slide of 2001–2, and the depressed conditions facing several of GE's major businesses (notably power systems and jet engines).

Among the strategic and organizational questions that Immelt needs to address are:

- What changes in GE's business portfolio are desirable?
- What changes in GE's structure can improve company performance? In particular, should the two main sides of the company – industrial businesses and financial services – be separated?
- What changes need to be made to GE's management systems and management style, and do these call for a change in the culture of GE?

At the root of these questions is the issue of GE's "corporate advantage." How is GE able to add value to its businesses? Given the sources of its corporate advantage, what are the kinds of businesses where this corporate advantage is likely to be especially effective in improving business-level performance?

GE's corporate advantage has its roots in GE's resources and capabilities. At the resource level we can readily identify GE's massive financial resources, its brand and corporate reputation, its managers, and its global presence. In terms of capabilities, GE is renowned for its mergers and acquisitions capability, its financial management, its strategic management, its management development, its international management, and its capability in sharing technologies and best practices between companies.

What does this mean for the portfolio? GE creates value in making big, capital-intensive businesses even bigger, extending their global reach, and improving their management. Are there businesses within GE where prospects for value creation still look good? During the past decade, financial services has been the main area for GE's growth. Opportunities for further growth (especially through acquisition) probably lie in insurance and maybe other financial sectors too. Are there sectors not already within the portfolio where GE should consider entry? Are there any businesses within GE where the prospects for adding additional value look poor, or where industry attractiveness is deteriorating?

In terms of GE's management systems and style, two factors are important:

- *Given the changes in the external environment, what changes in organization and management are needed for GE to continue to add value to its businesses?* The new decade is clearly a much more difficult time for business in general than the "roaring nineties." In 2002, much of the world is facing economic stagnation, international political and economic instability has increased, and the need for flexibility, responsiveness, technological progressiveness, and strategic innovation is greater than ever. At the same time, international opportunities – especially in China, India, and elsewhere in Asia – are substantial. (Growth prospects look worse in North America, Europe, and Japan.) Hence, continued international expansion looks sensible. Given the depressed state of world equity markets, GE faces interesting opportunities to make acquisitions at attractive valuations. In terms of management systems, Immelt needs to continue the work of Welch in fostering entrepreneurial vitality and market responsiveness among GE's businesses. This may require further de-layering (possibly breaking up some of GE's larger businesses), additional decentralization of decision making, and increased use of information and communication technology to permit self-organization and a lower level of corporate involvement in the individual businesses.

- *Does Immelt need to remake GE to conform to his own management style?* One interpretation of the Welch era at GE is that GE was remade in the image of Jack Welch. Thus, Welch's values of self-confidence, aggressiveness, self-reliance, and simplicity became the basis for GE's management style more generally and the principles for designing GE's management systems. Immelt's management style is different. His priorities are different (to begin with, he appears to give greater attention to marketing and customer satisfaction). What are the implications of this different orientation for GE's financial control systems, its strategic planning, its human resource management, and corporate initiatives?

Ultimately these questions require consideration of the GE business model. GE is a company where value has been created through portfolio management (the buying and selling of businesses) and through a corporate management system that enhances the competitive advantage of the individual businesses by transferring resources and capabilities and motivating and developing general managers. This system has adjusted to changing business circumstances. During the 1970s, GE created value through a highly sophisticated system of strategic and financial management. During the 1980s and 1990s, GE created value through a strategy that emphasized international expansion and a shift from manufacturing to services, the transfer of best practices, and a system of performance management that drove a sustained quest for increased profitability. In 2002, GE is facing new internal and external contexts. Externally, the values of shareholder wealth maximization are subject to increasing questioning. Internally, Immelt brings different skills, preferences, and style to the position of chief executive. GE needs to adjust its business model to both.

Updating the Case

For current information on GE, go to General Electric's web site: www.ge.com.