

# Hitting the "Wall": The Role of Leadership and Organizational Process in the Successful Growth of SMEs

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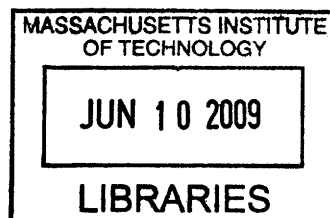
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**Abstract**

Rapidly growing companies often start out well, but hit a "wall" as they continue to expand. This wall is partly due to a lack of structure within the organization, but is also due to a lack of leadership and training to build new initiatives or to implement change. This thesis examines two components of the company: the organizational behavior at the company level and the leadership development at the level of individual stakeholders within the company. By examining the organizational structures and leadership teams of successful and failed rapidly-growing companies, this thesis proposes a new organizational developmental model to better understand and predict what makes a growing company successful in getting over the "wall" and to its next phase of development.

The first part of the study examines the leadership and organizational needs of small- and mid-sized enterprises (SMEs) at early and midlife stages of development. This thesis then examines leadership and organizational process theory before drawing on developmental psychology to propose a new model to address the stages of growth through which a company passes. Using the proposed developmental model as an analytic framework, two case studies are examined. The model provides insights into the kinds of leadership and organizational structure that are predictive of successful – or unsuccessful – growth in the SME. Lessons for SMEs are suggested, including what a company can do early in its life cycle to prevent it from hitting the wall.

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## **Introduction**

The needs of companies differ considerably in each stage of a company's life cycle. The needs of early stage start-up ventures vary significantly from those of already-established companies. For instance, a start-up's workforce may consist of only a few founders of the company, and these founders may have overlapping skill sets. The founders may not have any management experience, or they may all come from managing larger organizations. They may work together collaboratively to make all strategic decisions involving the company. Although not all early-stage companies share these characteristics, one can argue that at the early stages of a company's developmental cycle, the organization's management is often characterized by fluid and dynamic roles of the executive team and little process or structure within the organization. Team members are often generalists who are able to transition from one role to another and back again, and this need often arises at this stage.

Organizational structure is markedly different in a company with over 1000 employees that has developed formalized decision-making processes. This large organization may have an executive team, headed by a CEO or president, which is responsible for all of the important decisions related to the strategy of the company. There are usually experienced managers across all of the departments to manage the daily operations, and employee job functions are highly specialized.

The question is, then, how does a company progress from the highly dynamic, fluid venture of a start-up company to a process-driven, hierarchical organization? What steps does it need to take to move from a start-up, close-knit environment to a rules-based, large-scale operation? Small- and mid-sized enterprises (SMEs) are a unique subset of businesses that are

transitioning and growing, sometimes shrinking, but ultimately all struggling with the question of how they balance start-up ideals with increasing formalization to become a large company, capable of managing hundreds of employees in an efficient manner.

This thesis seeks to take a closer look at these SMEs, which represent about 99.7% of the estimated 27 million businesses in the United States and employ 50% of all private sector employees (U.S. Small Business Administration, 2008), to determine what steps SMEs need to undertake to sustain growth and move into the next stages of development. One must recognize that a number of factors exist that directly impact the growth of a company. While recognizing that many of these factors may be working in unison and may be difficult to parse, this paper cannot adequately address every factor. Instead, this thesis will focus on two areas in which entrepreneurial companies generally encounter substantial difficulty: developing leadership within the company and creating an organizational design to implement processes and create reporting structures as the company grows. It is also important to note that the following research is focusing on inexperienced entrepreneurs, not serial entrepreneurs, who are facing these challenges without the help of venture capital groups or other mentoring agencies, who may be involved in the leadership decisions.

Leadership and organizational theories have historically found difficulty in combining the traditionally “individualist” leadership frameworks with the organizational frameworks, which focus primarily on group dynamics. Drawing on a holistic picture of growth, based on human developmental theory, this thesis seeks to develop an integrated organizational development model that helps to integrate leadership and organizational components of rapidly-growing SMEs.

## Section One – The Unique Needs of Entrepreneurial Ventures

### *The Life Cycle of a Company*

The definition of company growth is not limited purely to number of employees or dollar figure of sales revenue. Although the U.S. Business Administration defines small business as those businesses with fewer than 500 employees, *growth* is not only related to size, and may instead mean an improvement in a quality or process resulting from a favorable environment (Penrose, 1959). It is the argument of this thesis that companies rapidly undergoing change may transition faster than they can sustain and may, therefore, hit a “wall” in growth. This is similar to an athlete who, lacking nutrition or exhausted from over-exhaustion, may “hit the wall” in a race, reaching a point of stagnation. The growth of the company may mirror the figure below before it hits the “wall”.

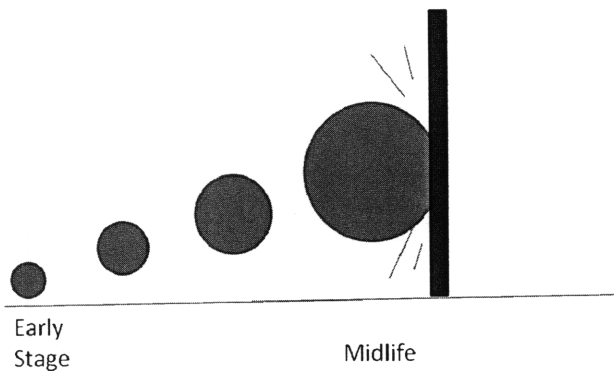


Figure 1. Hitting the Wall  
Source: Author

As one can see from the above figure, there exists a point at which the company in its development hits a figurative “wall”. Something must change within the organization before it can get over this wall and continue its progression. It is only if it steps back to assess the situation, change its course and alter the way that it is handling problems that the company can hope to overcome its challenges and make it over this wall.

When a company hits a wall, it can be due to a number of factors, which may include anything from leadership challenges (lack of development), succession planning, organizational design, IT/IS infrastructure, operations challenges (capacity building) to a lack of human resources (no good talent in the hiring pool) and financial constraints (funding needs, costs of growth). Research performed to explain different reasons for the abrupt halt of growth has focused on the restructuring of an organization in order to get over the wall. Zook (2007) looked at large companies overextended in services and products, and argued that to get over the wall, the company needs to redefine and reemphasize its core competencies. In a growing company that is just defining its core competencies, however, the challenges to growth are different.

As noted above, a number of different factors could impede company growth. However, one reason small enterprises fail to reach the next stage of development is that they fail to recognize that they require a change of leadership or a leader able to adapt his or her skills to more effectively mirror the company's needs. This failure to self-diagnose and adapt to changes within the company could ultimately lead to the company's downfall.

One example of this occurs when the leader is the entrepreneur who developed the idea or product around which the business was built. The company was conceived through the founder's passion, so the founder may be reticent to hand over leadership to someone else because he believes it to be "his" company, even if he does not have the skills required to lead the company as it enters its next phase of growth. This reticence to transfer leadership stems from the founder's huge investment of time and energy into building the company, and now the founder has difficulty stepping back and letting someone else take control.

In addition to leadership challenges, a company faces a new obstacle to growth if it has not carefully considered how to structure the company. In some early-stage ventures, the founders came together because they had a shared group of skills that may or may not be sufficient to lead the company as the organization evolves. Take, for instance, the case where a software company is formed by a group of three founders, all of whom have strong computer science skills, but may not have organizational expertise and so have neglected to create formal communication channels. As the company grows larger, the founders should hire to complement their skills and to fulfill the company's shifting needs. Without clear processes and communication, as the company develops, reporting structures become blurred and job descriptions and requirements become muddled. This results in employees having no clear idea of who is in charge of what, and to whom they should turn for resources. Clear knowledge of roles and reporting structure is incredibly important in growing companies, so that the company can begin to build processes, measure successes, and hire and train for needed skill sets.

This section of the thesis examines the needs of SMEs at different points in their development: the "Early Years", in which the companies are focused internally while building core competencies and managing growth, and "Midlife", in which companies have begun to face outward while building networks and restructuring to meet competition. The information within this section is based on conversations with leaders of rapidly-growing SMEs, secondary research and personal experiences of the author in working with entrepreneurs. The information here is meant to be a simplification of the very broad topics of leadership and development of growth-phase companies, and may not be indicative of all companies in these phases.

## **The Early Years**

### **Leadership Needs for Early-Stage Companies**

#### *Leader as Culture-Setter*

A company's "culture" is a system of shared beliefs and norms that develops within an organization. It binds people together around a central philosophy. As Schein (2004) states, "Culture is the glue in the early stages of a company." Culture is a necessary component of a start-up, a necessary precursor for innovation. When the culture of a company accepts uncertainty and is open to change, while remaining tolerant of failure, creativity is stimulated and innovation can occur. In addition, a culture that is non-bureaucratic, or informal and fluid, while remaining progressive and non-conformist, also encourages innovation (Gibson, 1988). Culture is a key contributor to the early development of an organization.

In start-up environments, the leader, often the founder, of the company and his or her co-founders serve to set the culture of the company. Because the organization has so few employees at the time, the organizational structure of the company is "flat", or non-hierarchical, so authority and responsibility are shared among the founders and perhaps a few key employees. As such, the leader has little authority on his or her own, and usually decisions are made by consensus. Thus, a leader must be able to persuade members of the team without any direct authority. This lack of authority usually helps to set the culture of the company as an informal organization. In the companies interviewed for this thesis, almost all of them said their company culture today stemmed from the original founders' efforts at the inception of the organization.

*“In the early stages, the founder creates the mission/vision that, when tied into values, sets the culture of a company.”* – CEO, data aggregation company for U.S. educational systems.

An organization’s culture is integral, as it often encompasses the many varied motivations of the employees. The values shared by employees in the company determine how productive employees are willing to be when the boss’s back is turned. If the culture is one of hard-working, enterprising people, then the likelihood of someone shirking work is much lower than if the corporate culture is decidedly less engaged in the success of the firm (Schein, 2004). Founders of companies, who may not have a clear understanding of what motivates their employees, may be surprised by how important it can be to nurture and promote a certain culture within the company.

*“We were unaware of the ‘notion’ of culture, what it meant and how we changed. If we could do it again, we would have worked on building a culture at the beginning.”* – Co-Founder & CTO, hardware technology company.

The leader of a start-up company has the often challenging task of building a culture from the ground up. Although much of the culture may be determined by his or her personality and behavior, it is also incumbent on the leader to understand the real desires and motivations of the employees as they are added to the company. As the numbers grow, the leader can expect adjustments to the company culture, and should be careful to maintain what is important to him or her.

### *Leader as Visionary*

Within a start-up company, it is essential that the leader, or one of the co-founders of the

company, is a visionary. A *vision* is that person's ability to see the future of the company and sell that image to the world. At the time of its founding, a company has no product to sell, no financial backing and few resources available to it or its founders. Therefore, the founder must be able to create a vision that appeals to a variety of audiences, including venture capitalists and angel investors, to procure funding for future employees needed to build the company. At the time of the company's inception, a vision is all the leader has to sell.

*"You can bring someone in to drive accountability, but only the leader can visualize the value within the company."* – CEO, data aggregation company for U.S. educational systems.

### *Leader as Salesman/Marketer*

The leader, or someone in the founding group, needs to have strong sales and marketing skills. As noted above, that person must be able to sell a concept, and not only sell it to one audience, but to a variety of audiences. To start, he or she must be able to talk to the angel groups or venture capitalists and sell the concept without a prototype or with only an alpha product, held together with tape and glue. The leader must sell his or her ideas to the other founders and keep them involved and interested in the product to ensure their commitment to the start-up. The leader must also be able to convince other talented individuals to join the group, usually at a point where salaries and funding promises are limited. Promises of future shares in the company are only valuable if the hires believe in the leader and think the company is going somewhere. Last, the leader must be able to sell the concept to potential clients and customers, again often without an actual product. In addition, he or she must remain in close contact with the customers as the product development cycle continues, always maintaining their interest and whetting their appetite for the finished product. In fact, Barrier (1995) argues that these early-

stage leaders are most often motivated by the close relationships they have with their customers and employees.

### *Leader to Get Buy-In*

The leader must be able to get buy-in from his or her co-founders and other hires. He or she must be able to lead without “leading”, per se. Since the culture of a start-up is often egalitarian, he or she cannot rule with an iron fist. Instead, he or she must be adept at persuasion, careful to listen to everyone’s ideas and to effect change through influence. In addition, the leader must seek to get buy-in from the hires he or she makes because getting the start-up off the ground requires an immense amount of energy and dedication by all of the employees involved. This point also refers to vision, in that if the employees are motivated by a compelling vision, then the leader may have an easier time getting them to follow his or her lead.

### *Leader as Risk Assessor*

The start-up phase is a particularly risky time for the company, as funding is irregular and dependent on outside sources, technological progress may be slow or hampered, and the founding team is just “learning the ropes” in building the company and learning to work together effectively. The leader has a unique responsibility in terms of calculating the risk of that next step for the organization.

*“The role of the leader is to calculate risk and what needs to be done to mitigate that risk or build redundancy around that risk.”* – CEO, data aggregation company for U.S. education systems.

This risk mitigation can often be handled by bringing in people who have dealt with these types of problems before or who know more about the industry and the types of challenges the

company will face. The leader must be the one to identify what risks the company should be willing to make and to trust others to help him or her to make them.

## **Organizational Needs for Early-Stage Companies**

### *Founders with Autonomous Skill Sets*

In a start-up environment, it is important for the founders to be able to work autonomously, with little or no supervision, and have a flexible skill set that may overlap with others on the team. Since there is no one to look over their shoulders, the team needs to be self-motivated to get the work done, and needs to feel invested and committed to the company's vision. In the initial team, the founders should have complementary tasks, with each individual taking over one function of the organization. For instance, a person taking on the "President" role may handle day-to-day operations, whereas another individual, as the "Chief Technology Officer", may handle the technical side of the company. A third person may handle the "Sales & Marketing" component of the company, by identifying new clients and working on developing business opportunities. In this example, each person has a complementary job function, but these may overlap from time to time. For instance, although the Sales person is presenting company information to new clients, the President may assume the presentations for the VCs or funding sources.

The hiring of people with flexible skill sets, who can handle a variety of job functions, is extremely important at this stage in the company. One reason it can be important is to protect the company in the event one of the founders "walks" away from the company. Is there another person among the founders who can take over that role, or is the company in a position to attract new talent at the time? Human resource searches can be time consuming, so it may mean another

founder has to temporarily step into that role. Finding initial founders with varied skill sets and the flexibility and adaptability to learn and step into other roles is key.

#### *Collaborative Focus Among Founders' Team*

It is important that the founders' management team maintain a collaborative focus. By this, "collaborative" means willing to share successes and failures, to consider all ideas even if decisions are not made by consensus, and to be willing to step up and help others on the team, should the need arise. The start-up company may or may not have initially hired employees with collaboration in mind. However, as new hires are made, care should be taken to ensure that people who are being brought into the company are able to work well with others. People who are collaborative, have flexible skill sets, and are willing and able to help others will ensure that the company achieves its goals.

#### *Inward-Facing Founders' Team to Build Internal Team*

The founders' team must be able to build consensus within the company. Therefore, some members of the team should be focused "inward" to determine what needs exist within the company. They should also focus on whether or not those needs are being met by skills of those on the management team, as well as which needs are not being met. This could mean hiring new employees or adapting the training of existing employees to meet the needs of the company (Ancona & Bresman, 2007). It may also mean adapting the business model to better address those issues.

The founders' team should focus on building relationships within the management team and working together. This may mean basic team-building so the founders adequately provide one another with feedback, create common goals, and work as an effective team. The team

members will need to be honest with one another and trust that each team member is doing the job that she or he was hired to do. Without trust and respect, successful implementation of founders' ideas will be hindered and the processes of change and growth can stall.

*“The role of the Founders’ group is to enable their managers, and later, when necessary, to help those same managers enable their subordinates.”* – CEO, online financial account services company.

### *Outward-Facing to Build Client Networks/ Supplier Networks*

Certain members of the founding team should be focusing on issues outside the company. They should look to prospective clients and suppliers to determine what potential demands may arise, and what the company should do to meet these demands. These same founding members should also build bridges to founding teams at other small enterprises and start-up companies, so they can compare best practices and have a network in place as they continue to grow (Ancona & Bresman, 2007). This will also serve as a prospective hiring pool for the company.

In addition, team members should be outward facing to find mentors who can help them address challenges that arise (Ancona & Bresman, 2007). For instance, VCs and larger companies in the industry may be able to provide sound advice if they have encountered similar challenges before. Therefore, it is in the founding team's best interest to look for mentors who are willing and able to help it think of creative solutions to challenges that arise.

### **The Midlife Crisis**

The “midlife” stage of the company, as defined by Schein, is the stage at which a company that has undergone a period of rapid growth is at a transition point and needs to start implementing policies and procedures to take the place of the initial reliance on the start-up

company's culture (Schein, 2004). Whether a company has reached this stage or not is subjective at best, and is often only recognizable in hindsight. In addition, what a "midlife" may mean for a company, either in size or revenue, greatly varies across industries.

For the purposes of this thesis, the definition of a midlife company is one in which the company has moved away from its start-up model to create processes and procedures for hiring and training, and has moved into the growth and acceleration phase with a hierarchical reporting structure consistently found at larger companies. For instance, the hypothetical start-up product company discussed in the "Early Years" has a management team consisting of a President, CTO and VP of Marketing or Sales. Although there are some differences in title, in general each of these individuals has a significant say in strategic development and each works independently to handle the different areas of the business.

As the company reaches its midlife stage, it is rapidly adding new technology, sales and marketing employees, and the total count of employees may balloon from around five people to more than thirty. Each of the founders still participates in the day-to-day functions of his or her area, but now oversees several employees as well. In fact, as the company continues to expand, the founding team may realize one of them needs to move into a CEO or COO position, and questions may arise regarding whether a member of the founding team has the requisite skills to move into one of those roles. The organizational and leadership needs of a midlife company and how they differ from its needs at the start-up phase are discussed below.

### **Leadership Needs for Growth Phase Companies**

The early start-ups may have a need for "leaders", but they do not have much need for managers. Good managers often have very different skill sets from those of good "leaders". They

can motivate people to work, but are also organized in terms of daily responsibilities. They are perhaps detail-focused, instead of visionary or strategic. As such, the demands of leadership within the company change significantly as more people are added to the personnel roster. The founders, who may have skill sets commensurate with raising funds and bringing good people on board, should re-assess their abilities and decide whether or not they are adept at managing people and focusing on day-to-day operations. If they do not possess these strengths, they should consider hiring someone else to handle these functions.

#### *Leader Who Understands the Culture of the Company*

As the company moves from start-up to midlife stage, the company and its management must begin putting formal policies and procedures into place. Managing large groups of people without formal processes in place is almost impossible, so it is necessary for the company to begin a period of adaptation. However, from an employee's perspective, especially one who has been with the company since its early stages, formalizing the company is a change from the cultural norm.

In the start-up phase, the company probably only formalized policies on an *ad hoc*, or as needed, basis. Individuals joining the company during this stage of development may believe such non-formal procedures are an important part of the work environment. Therefore, any deviation from the norm may be seen by an employee as the company trying to "change the culture". This can mean a decrease in employee morale or a backlash from employees in terms of changes they are willing to support or endure (Heifetz, 2001). Keeping a close eye on employee morale is especially important when the company is considering bringing in a new CEO or president. These are positions from which new executives can institute change, and employees are often afraid changes will be made that violate the company's culture.

In general, people are resistant to change. Culture is something built from the ground up, and especially if the employee has been at the company for a long time, he or she may have helped build and develop that culture. Beliefs and norms, integral parts of “culture”, are closely held by everyone. Violations of these beliefs result in unease and anger (Schein, 2004). Therefore, it is incredibly important that a company recognize that it has a culture already in place, and that its employees fear a cultural change that comes with a new leader. The company must find a leader who understands the culture of the company as it already exists and makes changes consistent with the culture. If the culture cannot be maintained, the leader must acknowledge that the cultural shift will be difficult and will take time. A leader must make it known that he or she is sensitive to the fears of the employees (Schein, 2004).

#### *Team Builder: Leader Who Can Create Collaboration During Change*

As discussed above, it is important to find a leader who is particularly adept at understanding employees’ fears and helping them to understand the need for change. However, it is also important for this leader to help the employees understand their roles as the company changes, and how they can add value to the company.

Assuming that new leadership was brought in to help the company at its transition point, the management team will need to procure the help of the rest of the company employees to really effect change. Therefore, the new leader will need to build consensus (Gibson, 1988), or at least find a way to motivate the employees to follow his or her lead. Obtaining buy-in from the rest of the organization will allow the company to move toward its goals and transition to a new stage.

In addition, social psychological research has consistently shown that people are much more willing to change their behavior when they are involved in the change process. Giving employees a very clear picture of what their behavior should be and why it is important to change can help them understand where they fit into the larger picture of the company and how their behavior directly impacts the organization. For this reason, the leader must focus on making as many people a part of the change process as possible, at all levels within the organization.

#### *Succession Planning/Independent Culture from Founder Personality*

In some instances, the founder of the company is a particularly charismatic individual who helps set the culture of the original company. In this situation, the company will need to make sure the employees of the company recognize that the culture of the company is independent from the personality of the founder (Schein, 2004). Then, if a change must happen at the leadership level, the employees will not necessarily assume the entire organization is changing. If successful, the company will not meet as much resistance from its employees when hiring a new leader, especially when the company intends to continue to promote its culture.

One example of this concept is an outdoor retail company with a particularly charismatic founder and CEO, who has worked very effectively to create a culture which focuses on community, employee happiness and dedication, flexibility and sustainability. The CEO's own personality is laid back and approachable – he still picks up his own phone and is reachable by any of the company employees. Many fear that, should he retire or quit as the CEO, the entire culture of the company would change, causing the company to become more “corporate”, a fate worse than death in the outdoor retail industry. This fear may be unfounded, but it can certainly serve as an example in which the personality of the founder has a perceived impact on the culture of the company (personal communication, 2009).

It is also possible for the next leader to make the company stronger, so the company must pay particular attention as it creates its succession plan or hires its next CEO. If culture is a concern, the company needs to find a leader who can work within the boundaries of the culture or who can encourage others to change by showing them why it is important and how he or she can help.

### **Organizational Needs for Growth Phase Companies**

As the company goes through its growth phase, the organizational structure of the company may not be sufficient to allow for the rapid change and implementation of formal processes necessary to make that growth sustainable in the long term. Therefore, it may become necessary for the company to reconsider its organizational design at its midlife stage of development.

Changes are being made to the leadership team, which means reporting structures may need to change. New departments may be created to meet the needs of clients or customers. Expansion may mean opening new offices. Therefore, it will become necessary for the company to reassess its current organizational design and determine what, not whether, changes need to be made.

*From Individual Roles (VP of Marketing) to Function-Driven Teams (Chief Marketing Officer, Analyst, Specialist, Assistant)*

In the early stages of the company, the founding members and key leaders held positions in which they were able to individually function to handle all of the needs of that business unit. For instance, the VP of Marketing may have acted alone to find new business opportunities, or he or she may have managed one or two other people. However, as the company grows and more

people are added to a department, the work being done becomes more and more specialized. Therefore, it becomes necessary for the company to build teams within a particular department in order to make sure all functions within that department are being handled by one position or another. In these teams, a person's role becomes more specific. For example, a marketing professional, after the hiring of several other individuals in the department, may take on less of a generalist role and specialize in one particular job function, such as marketing communications. In a department that once consisted of only the CMO, a revision of the department during the midlife stage may result in the following:

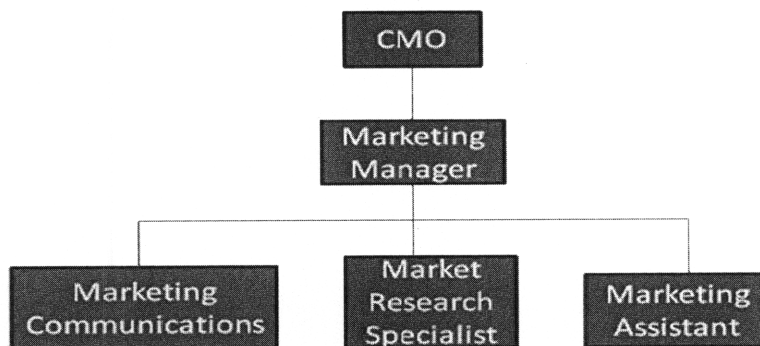


Figure 2: Hypothetical Organizational Chart  
Source: Author

This organizational change allows for the department to become more efficient, especially as business needs increase. Also, as people rotate through the company, a more specialized skill set might be easier for the company in terms of recruiting and finding replacements for employees who leave.

*From “Cross-functional” Individuals to Isolation of Inward-Looking Teams*

When there are few employees, as in a start-up company, these individuals must take on projects with other “departments” in order to get things done. For instance, in the early stages,

bringing in a new client may take the effort of all of the members of the founding team, each of whom has a designated function such as “Chief Marketing Officer” or “President”.

Consequently, cross-departmental collaboration is incredibly high early in a company’s life cycle. However, as the company grows, the emphasis once given to these cross-functional projects shifts to building teams within departments who can handle their department-appropriate projects. Marketing handles researching new client prospects. Sales representatives make phone calls to the prospects. The President is uninvolved in acquiring new clients, except in a remote supervisory capacity. These teams of people become relatively isolated within their own departments.

To counter this movement, teams should strive to look outside of their own departments to other areas within the company. The organization should focus on creating cross-departmental teams that can work collaboratively. This will ensure that information and communication flow happens across the entire company in an efficient manner. Also, by working with other departments, the teams will be able to service clients more effectively. Working cross-functionally will allow each department to discuss best practices with other groups and will help them learn from others’ mistakes and their own (Ancona & Bresman, 2007).

#### *Communication Processes – Top-Down and Bottom-Up*

In the early stages of a company, because there are few employees, communication flows freely between members of the founders’ team as they work collaboratively to build the company. Thoughts and ideas are shared between different “departments” with ease. However, as the company grows, individuals become more isolated in their departments as their tasks become more specialized. This isolation creates a barrier between inter-team and intra-company

communication. In addition, the company becomes too large to allow for face-to-face communication.

It becomes incumbent on the management team to build communication processes into all levels of the organization. Communication needs to happen between departments, information needs to be disseminated by management down to the rest of the organization, and feedback from the employees needs to find its way back to management. In order to make sure good communication can occur, formalized processes need to be created by which information can be sent out in a timely and efficient manner, so all people within the organization understand what is happening and what they need to be doing. In addition, the sharing of ideas and best practices is integral in saving time and resources, and as such, a formal process of information-sharing may help the company save money and time in the long run.

## **Conclusions**

In Section One, this paper examined the needs of entrepreneurial organizations at two stages of their growth – the early and midlife stages - and determined how the needs of these companies change as they transition from one developmental phase to the next. In Section Two, this thesis will look at the evolution of leadership theories over time and will discuss how models of leadership in literature may meet the needs of companies.

## **Section Two - Theories of Leadership**

*“A leader is best when people barely know he exists, when his work is done, his aim fulfilled, they will say: we did it ourselves.”—Lao Tzu*

Section One discussed the leadership needs of growing organizations, at both the start-up phase and at the midlife phase of the company. A significant change in leadership occurs during this period of transition, as the company shifts from start-up to midlife. By examining leadership models and understanding the development of leadership theory, one can better understand the unique role of the leader and how it relates to the organization he or she is to lead.

This section, therefore, will look at the evolution of leadership theory to understand what it is that allows for effective leadership of SMEs. Is successful company leadership purely due to the personality traits of the founder, or is it a more complex theory involving culture and others within the company? Does one type of leadership model work better at the early stage of the company and does another model work better later in the company’s lifecycle? How does the role of leader change as the leader transitions from being part of a founding team to overseeing and managing others in a traditional CEO role? These are important questions to keep in mind as we consider the evolution of leadership theory and discuss the importance of different models for SMEs.

### **Evolution of Leadership Theory**

How can individuals influence others when there is no apparent exertion of power? Understanding these individuals, whom we call leaders, has been a purpose of social scientists throughout the years. These researchers strove to understand what makes leaders influential and

to determine how one can learn or teach these skills. Theories of leadership have changed significantly throughout the years, from a rigid grounding in personality psychology, which focused on the leader's character alone, to a model that considers a fluid, dynamic individual who leads through his or her subordinates, rather than in isolation.

### **Personality Theories**

The earliest leadership theories centered on identifying personality traits characteristic of leaders in large organizations. Social scientists at the time studied individuals to determine what in their personality enabled them to lead effectively and what in their personality made people want to follow them. Often, these theories focused on examining attributes subordinates, co-workers or other executives used to describe the leader. These attributes could include aspects of physical, emotional or intellectual traits by which his colleagues described this individual. A leader might be defined by his or her subordinates as “charismatic”, “inspirational”, “self-confident” or “assertive” (McCall & Lombardo, 1983). Other attributes centered on a leader's perceived cooperation, adaptability, dependability and persistence. In general, these attributes were highly subjective, were based on reports by co-workers and subordinates, and could not easily be measured or validated. In a quest for validation, Stogdill (1974) tried to link trait theories with external measures like IQ. He found that individuals recognized as leaders tended to have high IQs, were alert and original, and showed personal integrity, self-confidence and individuality.

However, trait theories of leadership have a number of weaknesses, including the fact that many traits may work together in concert, and the leadership quality may be a result of this interaction and not attributable to any one trait (Gibson, 1988). Furthermore, the quality of leadership can be situation-specific. That is, attributes allowing a person to lead in one situation

may not be as effective in another situation. A leader known for being reflective and methodical may not be as effective in a situation in which he or she is required to make off-the-cuff decisions with little or no information. In addition to difficulties inherent in evaluating situation-dependent attributes, scientists over the years have added more and more “traits” to the list, to the extent that the number of traits may be too overwhelming to be useful and the definition of “trait” may be overly broad.

So, is there a place for considering personality when discussing leadership? Researchers have argued that personality is essential in leadership because personality underlies all aspects of an individual, including learning, motivation, perception and attitude (Gibson, 1988). Therefore, one cannot discount its importance, especially if the personality trait impels that individual to engage in a behavior consistent with the attribute.

### **Behavioral Theories of Leadership**

The behavioral theory of leadership argues that perceived traits are less important than actions when considering the characteristics of leaders. Of course, parsing the two is a challenge, but behaviorists argue it is a leader’s actions that encourage the commitment of his or her followers, not merely the attribution of an amiable trait.

#### *The University Studies in Behavior*

Rensis Likert (1947) conducted a series of experiments at the University of Michigan in which he measured performance-related tasks (*e.g.*, productivity, follower satisfaction, turnover, motivation) to determine leadership skill. These studies led him to argue there are two kinds of leaders. The first is the Job-Centered leader who closely supervises his followers, employing a “hands-on” style that directly rewards and coerces desired behaviors. The second leader is the

Employee-Centered leader, who focuses on creating a collaborative, supportive work environment in which decision-making is shared and the focus is on employees' personal growth and achievement. Although the study focused on actions of a leader that elicit follower behavior, the Likert study did not determine whether these leadership styles were useful in all contexts or whether one was superior in one situation over the other.

E.A. Fleishman developed a two-factor theory of leadership at Ohio State University. Fleishman theorized that a leader must show both "initiating structure and consideration" (Fleishman, 1973). That is, a leader organizes and defines relationships within a group. Also, a leader clearly states his or her goals and creates a clear process in order to achieve those goals. The leader must offer friendship and mutual trust or rapport with his followers. Fleishman validated his findings with a Leader Behavior Description questionnaire and conversations with followers. However, because his theory relies on questionnaires for validation, it cannot be generalized to a larger population.

### *Theory of Charismatic Leadership*

House (1976) developed the Theory of Charismatic Leadership, which focused on the shared values of both the leader and the followers. He argued that a leader needed to exhibit four characteristics, which included dominance, self-confidence, need for influence and conviction of "moral righteousness". It is this conviction that sets it apart from traditional trait theories that dominated leadership theory at that time. Understanding and believing in one's own message, and acting commensurate with that belief, is integral to gaining followers' acceptance. House's theory laid the groundwork for Bass's Transformational Leader, which was developed almost a decade later.

## *Transactional and Transformational Leaders*

Bass (1985) relied on personality theory to create his framework of Transactional and Transformational leaders, which bridges traditional trait and behavioral theories. Based on his belief that a leader who is “charismatic” encourages others to follow him or her through influence, Bass identified two different types of leaders whom he believed could effect change. Both of these types focus on the interaction between leaders and followers and ensuing motivating behaviors.

In the first type, Transactional, the leader has control over or possesses something the follower wants, which the leader is willing to provide in exchange for a service. The most relevant comparison is that of a contractor relationship, in which the contractor supplies a service to an organization in exchange for money. Within the Transactional framework, followers are motivated to act for a reward, but do not undergo any belief or value change as a result of the leader’s actions. Within the Transactional Leader category, there are a number of different “sub-types”. In one sub-type, a leader encourages followers by offering a reward contingent on behavior. Another sub-type of Transactional Leader manages “by exception” – that is, either by actively monitoring errors to curb behavior before problems occur or to act on errors when they occur, on an “as needed” basis.

In comparison to the Transactional Leader, the Transformational Leader effects change through appealing to the values of the followers, thereby motivating them to follow him. The “charisma” personality trait coupled with the actions of the leader in sharing his vision, an attribute and a behavior, both allow him to effectively inspire followers to action. As Gibson (1988) states, it is the Transformational leader who must “inspire or influence followers to

transcend self-interests for the good of the organization”. Therefore, it is not enough for the leader to espouse change; he or she must encourage buy-in from followers by getting them to think beyond their own needs and even sometimes to act in a way inconsistent with their own needs or ideals for the good of the whole organization. Again, though, these frameworks are validated only by the reports of the followers.

### **Situational Theories of Leadership**

Around this same time, social scientists began to believe that leadership can be situation-specific and that no one leadership approach is appropriate for every situation (Vroom and Yetton, 1973). Whereas personality and behavior may change leadership style, so might it vary because of task or group of subordinates. Consequently, leadership models began to seek ways to account for situational differences in leadership style.

#### *Early Situational Models: Contingency Leadership Model and Path-Goal*

One of the more influential models from this time is *Fiedler's Contingency Leadership Model* (1967), which argued that leadership style alone does not predict the performance of a group; instead, one must also consider the “favorableness of the situational factors” (Gibson 1988). These situational factors are three-fold. The first is the power the leader holds within the organization in a particular situation. The second factor is the trust and respect the leader has gained from his followers. The third is how well-equipped the leader and his followers are to handle the job required. Ultimately, if the leader is moderately-liked and has moderate power within the organization, the leader should adopt what Fiedler refers to as a “relationship-driven” approach, in which the leader focuses on relationships with colleagues and subordinates. If the

leader is either liked a lot with high power or incredibly disliked with no power, then the leader should adopt a “task-motivated” approach and lead focused exclusively on the task at hand.

The *Path-Goal Model* is based on House’s Theory of Charismatic Leadership, with an added assumption that the leader can change leadership styles in differing situations, which is distinctive from either House’s theory or Fiedler’s situational theory discussed above. In the Path-Goal model, the leader may adopt one of several leadership styles: the “directive leader” approach in which he or she directs the subordinates by communicating what is expected of them, the “supportive leader” approach in which he or she treats the subordinates as equals, the “participative leader” approach in which the leader consults with the subordinates and uses their ideas to make decisions, or the “achievement-oriented leader” approach in which the leader sets high goals and expects only the highest achievement levels from everyone.

All of these models are notable in that they are looking at leadership from the lens of a situation and a company’s employees, but they only deal with leader-follower relationships and ignore the broader organization and its role in leadership. The following models take into account the organization as a whole.

### **The Role of the Organization in Leadership**

One challenge in leadership theory literature is that the role of the organization and its effects on leadership is often overlooked. Leadership is considered to be an individual matter, when in fact the actions taken by the leader and the environment in which the leader is acting serve to predict the effectiveness of the individual. Indeed, compartmentalizing leadership as an individual matter becomes less compelling once we accept – as situational leadership theorists have - the important role that external variables play in defining effective leadership. Therefore,

this paper will focus on the three following theories of leadership – Schein’s Model of Organizational Culture and Leadership, the Distributed Leadership Model and the Adaptive Leadership Model - that include the organization as a whole in evaluating effective leadership.

### *Schein’s Model of Organizational Culture and Leadership*

An important aspect of Schein’s Model of Organizational Culture and Leadership is that it incorporates the role of the organization in leadership. This sets it apart from previous leadership models that looked at the role of the leader in isolation. According to Schein’s Model, the leader sets the culture for the entire organization and assumes a role in which he or she is a perpetual learner. As a perpetual learner, the leader is responsible for a number of things, including the development of new insights and motivating the rest of the organization to act on these new insights.

The leader plays a crucial role in the evolution and creation of a company culture. In a start-up company, the leader sets the culture. His or her role is to set this culture through actions, whether that means promoting individuals who share the same values or beliefs as the leader or by “deselecting” employees who do not conform to the culture the leader is creating (Schein, 2004). In addition, the leader can create reward systems to reinforce certain types of behavior that are part of the company culture. He or she can also set up certain employees as “model” employees or can coach others in certain areas of focus he or she finds important.

As the culture evolves from a start-up company into a midlife company, differentiation among the different departments and teams occurs within the organization, with each department or team creating its own unique subculture that may differ slightly from the culture of the broader organization. These subcultures are often defined by shared tasks among team members,

from which evolves or springs a shared point of view or even a common language or vocabulary. These adaptations might then be assimilated into the larger organization, where they share an overarching belief while retaining some distinctive characteristics.

When companies transition into midlife, however, subcultures that develop can be a barrier to creating a new company culture or changing the existing one. Because these cultures are rooted in the beliefs and values of the employees who adhere to them, a complete cognitive restructuring is necessary in order to promote change. As Schein discusses, this process first means that the leader needs to “unfreeze” the existing mindset. By creating a situation that is anxiety-provoking, the leader can shake up adherence to the standard culture and through cognitive restructuring and rewarding of new behaviors, change the culture of the company. This is particularly relevant when transitioning leadership away from a founder of the company. Often, employees confuse the culture of the company with the founder’s personality, which leads to problems when the founder steps down from his or her leadership position.

### *Distributed Leadership Model*

One advantage of the Distributed Leadership Model (DLM) over Schein’s model is that the DLM assumes an imperfect leader, or that no one person can be an expert at every leadership need. Organizational leadership responsibility is thus spread out over a number of individuals within the company, depending upon each person’s strengths. As such, leadership stems from within the organization, at different levels in the hierarchy, and across teams (Ancona, Malone, Orlikowski & Senge, 2007).

In DLM, a leader is assessed in four different areas of capability to determine his or her strengths and weaknesses. The first of these capabilities is called “sensemaking” and has to do

with the leader's ability to "make sense" of the company's position in light of its environmental context and any industry changes that might be taking place. It also involves the leader's ability to understand the direction in which the company needs to go and to map this direction for others within the organization.

The second area of capability assessment is called "relating", which has to do with how well the leader interacts with others within the organization by "inquiring, advocating and connecting" (Ancona, Malone, Orlikowski & Senge, 2007). In essence, good leaders actively listen, can argue their points of view without marginalizing others and can relate to people who do not necessarily share the same points of view. This skill is particularly important in early-stage companies, when the founder must be able to create a network of individuals who share his or her vision and can get things done.

This "vision" is the third capability in the DLM model. A leader must be able to portray his or her vision of the company's future and share it with the rest of the employees to create "buy-in" and to garner support. As discussed above, a visionary founder is key to creating a network of individuals who will rally around an ideal and move a company forward. This vision is fluid and involves everyone in the organization.

The last capability for assessment is called "inventing", and relates to developing new structures and processes within the organization for achieving the company vision. It is assumed that no one leader exhibits all four of these criteria perfectly. As such, it is important for a leader to recognize in which criteria the leader is particularly strong or weak so that he or she can bring in other people to help compensate for weaknesses within the leadership team.

### *Adaptive Leadership Model*

The Adaptive Leadership framework is important because it has a different perspective on a leader's responsibility for adapting the environment within the company. Heifetz (1994) developed the Adaptive Leadership framework which he claims mirrors the biological evolutionary process. In Heifetz's opinion, the environment of a company is like the DNA of an organism, which remains much the same with the exception of spontaneous mutations from time to time. In his theory, a company, in order to address a problem, may have to stretch outside of its traditional problem-solving repertoire. A new solution must then be created, drawing on the core competencies of the company.

The Adaptive Leadership Model is based on the premise that leaders should not focus on protecting their employees and assume the role of problem-solver, but should instead challenge employees to change their behaviors and come up with new solutions when the company faces new challenges. Heifetz argues that adaptive work only results when employees' beliefs are challenged, either because these beliefs are less relevant than they were in the past or because new perspectives appear, which often is a result of a merger or restructuring of the company.

In order for a leader to promote adaptive work, he or she must interrupt patterns of employee behavior and build new responses. According to Heifetz, this means the leader must be able to accomplish six principles: maintain an objective view to understand behavior patterns and resistance to change ("getting on the balcony"); diagnose the problems of employees and executives by regarding conflicts as clues (identifying adaptive challenge); maintain poise while applying an appropriate level of pressure to change and manage conflict while shaping norms (regulating distress); see diversity as a tool for innovation and conflict as creativity (maintaining

disciplined attention); decentralize authority and listen to voices on the periphery (giving work back to the people); and encourage dissent (protecting voices of leadership from below) (Heifetz, 2001).

Heifetz argues that the leader's role in this process is not a complete transformation, as suggested by Bass, but instead an adaptation that is rooted in the standard problem-solving base of an organization. Instead of what Heifetz refers to as "technical problems", which a leader already knows how to fix, these problems within the company do not have existing remedies and instead rely on new ideas to stimulate change (Heifetz, 1994).

As such, the role of the leader is distinctly different from other leadership frameworks because the leader is there only to facilitate identifying the problem. In this framework, a gap exists between the goal and the reality, and the leader should serve to understand the market and encourage innovation. Working at the margins of the company, the leader should be comfortable delegating or distributing responsibility to others within the company, because innovation can happen at all personnel levels.

## **Leadership for SMEs**

### **The Early Years**

Given the number of theories of leadership, it is sometimes difficult to determine which leadership model is most appropriate at certain stages of a company. Perhaps, too, the model that is most appropriate changes over time.

In the early stages of a company's life cycle, there are few employees, so the focus is really on the leader or the founding team. The leader's role is extremely important in setting the vision, the mission and the culture of the organization. In that case, it may be easiest for

companies to search for CEOs with certain character traits, or to take a *personality-based approach*. A charismatic CEO may work best for the company when it is seeking funding from venture capitalists and talking to prospective clients. Persons exhibiting charisma, who are capable sales people and who are confident in themselves and the company, may be able to garner the most trust from people outside the organization. In addition, that same confidence and charisma can serve to motivate the employees to work hard for the success of the company.

That said, *Schein's Theory of Culture* is also integral to this phase of the company, and the leader must be able to build a solid organizational culture around the ideals of the founding team and the employees of the company. Like the Transformational Leader, the small business leader must be able to motivate his or her employees to change their beliefs and values, which are intrinsically linked to the organizational culture. Consequently, emphasis is really on the leader-follower dynamics at this stage.

## **Growth Phase**

The growth and acceleration phase for SMEs, however, is a time of change within a company, and the role of the organization in leadership can no longer be ignored during this phase. In that respect, because of the rapid change occurring in the company, it is particularly important that the leadership within the company is fluid and dynamic, and is able to respond quickly to changes in the industry and within the organization. At this point in the company's life cycle, the company should be transitioning to a distributed leadership model, one in which leadership is shared among people at different levels of the organization. Particularly since change is so rapid and information is scattered throughout the organization, the company management cannot be called upon to understand every aspect of a decision making process, so

leaders must be developed at different levels in the company to handle different types of decision making.

## **Conclusions**

In Section Two, we looked at the evolution of leadership theory, from personality- and behavior-based theories to frameworks that included the environment and the organization as a whole. Looking at these models, several might be useful at different stages in the life cycle of an SME. However, certain models that are useful in early stages in the growth of an organization may not be as useful at later stages of growth.

However, this thesis has only addressed one component in determining growth – the leadership models that could directly impact growth. These leadership models are difficult to parse from the organizational design of the company. Section Three will examine organizational structures and organizational design theories that have been addressed in the literature, so we may better examine whether certain organizational designs would be appropriate for SMEs in various growth phases.

### **Section Three – Theories of Organizational Structure/Design**

*If you do not change direction, you may end up where you are heading. – Lao Tzu*

The organizational structure of a company is based on its division of labor. The definitions and delegation of job functions can directly affect whether the company is authoritative, the spans of control of its managers, and whether it is bureaucratic or “flat”. In essence, the division of responsibility arguably has one of the greatest effects on company culture, affecting how the company self-defines, how it positions itself in the market and whether it encourages creativity and innovation.

Further, the organization of the company impacts not only the management of its structure and processes but also the individual jobs within the company. The organizational structure allows for building networks and linking departments within the organization. When building an organization’s structure, there are a number of factors to consider, including the division of labor (whether there is high or low specialization within roles), authority (do managers delegate or hold central authority?), departmentalization (is it homogenous or cross-functional?), and span of control (does management oversee many employees or few?). These considerations all make up the design of an organization.

As discussed in Section One, a start-up company’s organizational structure is almost completely flat with little to no hierarchy. As the company grows and new people are hired on, it becomes incumbent on the company to establish some kind of structure, whether that means segmenting people according to job, geography, or client. This next section will look at the evolution of Organizational Design theory to better understand the options available to an SME as it begins to re-design its organization.

## **Evolution of Organizational Design**

Organizational Design theory has changed significantly over the years. The literature first favored a structured, formal, hierarchical organization like those designs used by General Motors or other large companies with thousands of employees. But, as time passed, new models developed that encouraged adaptable, informal structures. This section will walk through the evolution of organizational design theory, focusing on organizational structure, followed by organizational design in terms of team building and the creation of reporting structures. These last two topics are incredibly important to SMEs that are in the process of creating and implementing formal processes and reporting structures. Thus, these last topics will receive the most emphasis.

### *The Mechanistic Model (High Specialization, High Centralization, High Formalization)*

Weber's Mechanistic Model of a bureaucratic organization created an organizational model built on collective activities, or job function (Weber, 1947). Much as the name implies, this mechanistic type of organization is similar to a machine, focused on increasing speed and efficiency within each role in the company. Weber's model creates hierarchies within a functional job concentration, thus eliminating unnecessary training or responsibilities outside the requirements of this one job. Often used in companies where there exists some form of sequential development, this model is especially helpful at minimizing training time while maximizing efficiency.

The model draws upon four principles set forth by Henri Fayol in the early 1900s: specialization, unity of direction, authority and responsibility, and the scalar chain principle. The first principle, specialization, focuses on increasing productivity through emphasis on the

“technical” part of work, achieving efficiency through segmenting a complete job into discrete tasks managed by individuals who only focus on that one component. The second principle, unity of direction, is the principle by which people with similar jobs should be grouped together in a concentrated area like a department or company unit. The principle of authority and responsibility states that managers should have authority to make decisions and carry them out (centralized authority). The last principle, the scalar chain principle, suggests that communication must follow up the chain of command, from lowest-level managers to the highest-authority managers, and vice versa.

#### *The Organic Model (High Adaptability, Low Centralization, Informal, Low Specialization)*

Fundamentally different than the Mechanistic Model, the Organic Model focuses on individual growth and development within a company. As such, the model encourages managers and employees to take responsibilities outside of their areas. The emphasis is on promoting the individual’s self-worth through broader job function and responsibility. The advantage to this approach is that more people are able to handle functions outside of their own areas, leaving the company prepared to grow and the positions within it to change. Instead of focusing on creating departments around tasks, the Organic Model focuses on building departments around customers, services or products. This also allows communication to be more cross-company than vertical, as it is in the mechanistic model. Instead of communication flowing up and down the command chain, the communication moves across departments and individuals.

#### *Contingency Design Theory*

One argument against both the Mechanistic and Organic models is that they are not situation-specific. For instance, in one corporate environment, a highly specialized model may

work best, whereas in another, corporate organization should be flat to encourage knowledge transfer across departments to spur innovation. Some companies have adopted what is called a Contingency Design approach, which takes into account a company's environment, its goals, and its technology. In both of the models outlined above, the company's position in its environment is largely ignored, and as discussed below, its environment can be one of the most important factors in its growth. Failure to recognize this can lead to missed opportunity or obsolescence in technology or research, and missed competitive advantage within its market.

### *Environment and its Effects on Organizational Design*

A number of factors directly impact an organization's design, and environment is the umbrella overarching those factors. The term "environment" can mean a variety of things, including the company's position in its market or industry, given its competitors and any recent changes to the industry climate. Another factor to consider is technology. One might ask whether the company is up-to-date on changes in technology, whether this relates to creating a new IT infrastructure or to purchasing machines to use for new product development for increased efficiency or expediency. Last, the environment might include research and development (R&D), which relates especially to whether new research has been conducted in the area or if science has progressed in such a way that it might directly affect the technology of the firm.

Any changes in these environmental factors may lead to uncertainty within the company, which uncertainty would be based on a lack of communication and adequate information flow. Whereas stockpiling resources can deter slack in terms of availability of product, a lack of information and communication can be more difficult to predict and guard against. This process requires a restructuring of the company to allow information to flow more freely to the

appropriate areas. One way the company may remedy this lack of information flow is to differentiate its core processes and create sub-units around clients or geography. This reorganization would allow for better knowledge access where it is needed. Another option is to increase its capacity to process information, whether that means increasing the information system infrastructure or by creating roles for people who can work across various departments or teams to help disseminate information (Gibson, 1988). Hence, the organizational model should begin to shift to a paradigm that is more complex and can be more adaptive as the company continues going through its period of change.

#### *Integrative Frameworks: The Matrix*

The matrix is a very common organizational structure today. Its purpose is to provide some differentiation while still integrating across different units. The actual matrix organization can be grouped in a variety of ways, including by activity or function, type of output, client, or any blend of these (Gibson, 1988). The level of differentiation and integration between units differs across different types of matrices.

#### *Functional Matrix*

The functional matrix is similar to the mechanistic model described above, in that it differentiates according to each distinct job task. Therefore, employees are divided according to functional departments, such as Marketing, IT, or Finance. A Functional Manager oversees everyday tasks in each of the departments. One Project Manager serves as the coordinator or integrator across all of the different units. This Project Manager has very limited authority, which mainly involves disseminating information and coordinating efforts between units. This works very well when there is a product development company organized around a particular client.

Whereas in this model a Controller would retain control of the Accounting unit, the Project Manager would be responsible for the client and making sure production gets its costs to Accounting in time for the next billing cycle.

### *Balanced Matrix*

The balanced matrix is for companies that split their employees' time on various projects. For instance, a team member may only spend about 50% of his or her time on a particular project and work the rest of the time on departmental tasks. In this case, the team member may report to two different managers, one of whom is the Functional Manager of his or her business unit, while the other is the Project Manager for the client team. In this matrix structure, the Functional Manager retains control of the technical details, whereas the Project Manager retains control of the day-to-day management of the team member. The advantage of this matrix organization is that there is greater integration, but at the cost of two reporting relationships for each of the team members.

### *Project Management*

In the project team matrix, the Project Manager holds significant authority and may borrow team members as needed to complete a project. In this case, the project team integration is enhanced because problem solving becomes more collaborative, rather than distributive.

### *Project Teams*

Within a project team, the structure is almost completely horizontal. That is, the Project Manager holds no formal authority within the process and must be able to influence his or her

team members to effect change. The problem solving is much more rapid, because the team members may have overlapping responsibilities.

The project team structure is widely regarded to be the best structure for innovation and adaptability (Gibdi and Larson, 1986). Cobbenhagen (2000) argued companies that take a “project-oriented approach towards innovation are more likely to be successful innovators than function-oriented” companies.

### **Decision Making Structures**

As an organization changes its structure, significant changes may occur in terms of the reporting process and who the decision makers are in the company. In an organization with few leaders, the reporting structure may be completely informal and the decision making may be shared across several individuals. If one person has more experience in a relevant area, then this individual may assume responsibility for making the decisions in that area. As more people are hired into the corporation, a new reporting structure will be created as the job functions become more specialized. This means more managers assume roles in which decision making is a component, which results in a distribution of leadership responsibilities across the company.

#### *The Early Stages*

In the early stages of a company, decision making may be split among the founders of the company. The process may even be somewhat hierarchical, with equity founders carrying the most weight in decision making. At other times, decision makers may all carry equal weight and consensus decision making may be employed.

As the company grows and begins to segment into specialized departments or job functions, the leadership dynamics change. The leader still may maintain control over the departments within the company. One of the decision making structures used by earlier stage companies is that of “hub and wheel” management.

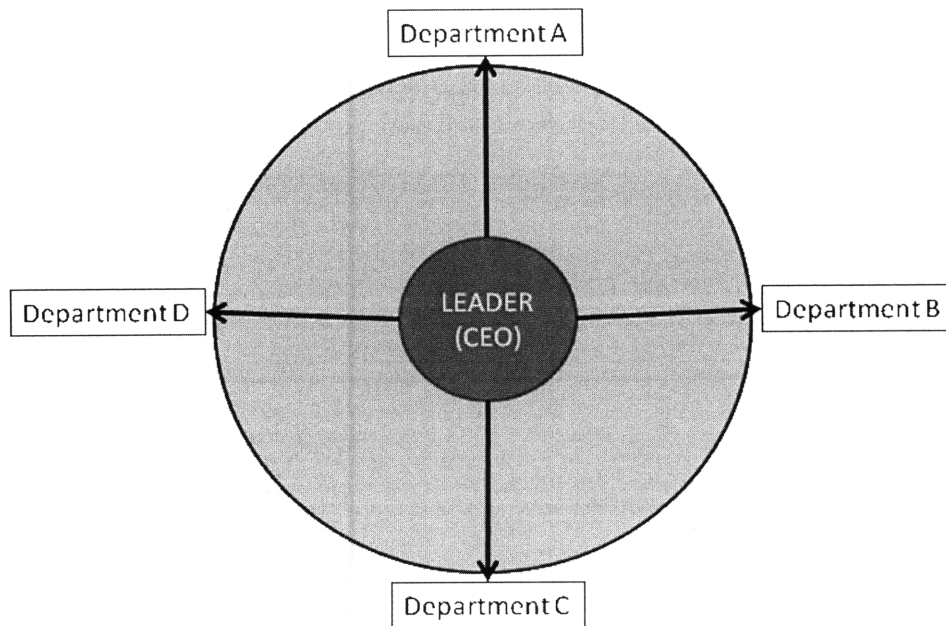


Figure 3: Hub and Wheel Management  
Source: Bavelas, 1951

In this structure, the leader, or leadership team, is at the center of the company and directly in touch with each departmental group. Job functions have been compartmentalized into various departments. These departments may have some hierarchy, but the core leadership team still makes decisions.

One benefit from this structure is that the leadership team can maintain “hands-on” control over the decisions influencing the company. Because the leader directly interacts with every department, the leadership team has a very clear picture of exactly where the company is and what types of projects are being done at all times within the company.

The major challenge with the hub and wheel management system is that the structure does not encourage interactions between departments. Because the leadership team is the center of all communication in the company, it may also act as a bottleneck of information. In addition, individual departments may have a very accurate idea of what is going on within their own departments, but may not have clear information regarding the standing of the company as a whole.

### *Midlife*

In the later stages of the company, as the organization transitions to more of a matrix structure, the leadership becomes more distributed. The few individuals in the leadership team can no longer be involved in all levels of decision making within the company. Due to time constraints and a lack of general day-to-day operational knowledge, a leader or leadership team will have to revoke control over smaller decisions within the company.

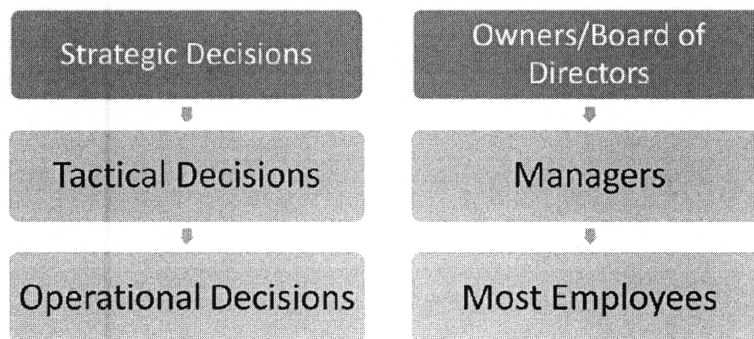


Figure 4: Example of a Linear Decision Making Framework  
Source: Author

A linear decision making framework assumes a company has transitioned to more of a matrix organization, in which departments are hierarchical and supervision has shifted to key

individuals within those departments. Within a linear framework, the strategic direction of the company is retained by the leadership team, which may include the owners or the board of directors. Day-to-day decision making is made at the level of departmental managers and individual employees.

At this point, decision making capabilities become aligned at different levels depending upon individuals' job responsibilities. This allows for a separation between big picture and operational decision making, so individuals within the company can focus on those decisions that are relevant to their own jobs. The leadership team, however the company defines it, retains control over the company's direction, and the "30,000 feet above" decisions, which allows them to think about the big picture and the company's strategy. The managers control tactical decisions within their own departments. Because they are closest to these areas, they know the most about what is going on and how things "ought" to be. Last, some operational decisions are made at the employee level, which empowers employees to assume responsibility over their own roles and to make changes as needed.

Communication, however, can be a problem, and it is easy to see where communication bottlenecks can occur. Employees report to managers, and managers report to the leadership team, but cross-departmental interactions and exchanges of information may be limited and need to be encouraged. As such, it becomes incredibly important for the company to encourage these inter-departmental exchanges at either the employee or management level. The leaders still retain much of the information as in the wheel and spoke system, but do not have the time to make decisions at all levels within the company.

## **Building Teams within an Organization**

Once the shift begins to a department-based organizational structure, it is important to look at the make up of the teams. Cross-functional teams are widely regarded as the best (Cobbenhagen, 2000). By having individuals with different strengths and weaknesses, the company can ensure that the team is maximally able to handle the challenges it faces.

### *Inward versus Outward-Facing Teams: X-Teams*

As a company develops, the focus shifts from looking inward to beginning to look outward, whether to the market, to the industry or to clients. If the company continued to simply perfect its product without any external interaction with prospective clients or investors, it would soon destroy itself. The inward focus would lead to missed opportunities for funding or customers. The same idea is true for teams that exist within a company.

Research on these teams suggests that because of the fast pace today of scientific and technological advances, teams within a company need to be able to pull together a complete picture of the market and opportunities, customers and competitors (Ancona & Bresman, 2007). This requires pulling information from various sources within the company, often from different departments. If no one within the organization is talking to anyone else, opportunities may be missed. By comparing notes and talking to one another within the company, people within the organization can be kept abreast of recent developments and are then able to nimbly change strategies or direction.

This does not mean that all members within the team should be outward-facing. In fact, a group of core members should focus on maintaining the efficacy of the team. These members should promote a safe psychological environment for everyone in which people can frankly

express their views without fear of retribution or fear of being wrong (Ancona & Bresman, 2007). By knowing and understanding the other group members' skills, this group of core members is then able to reflect on the strategy and actions of the group as a whole and can determine whether objectives are being met.

Only some of the members should be focused on the team. The rest of the individuals should be engaged in a variety of outward-facing activities, which are outlined below:

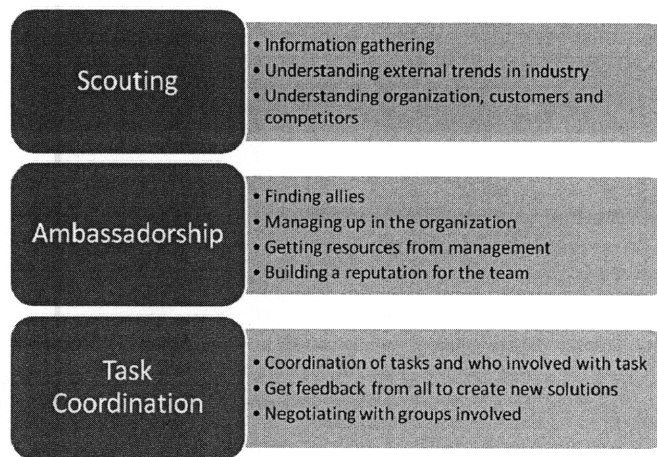


Figure 5: Outward-Facing Activities of X-Team Members  
Source: Ancona & Bresman, 2007

Within the team, activities are broken into several roles, including those of Scouts, Ambassadors and Task Coordinators, according to Ancona and Bresman (2007). The Scout gathers information about the organization and its place in the industry and builds bridges with individuals who can provide that information, whether they are within or outside of the company, including: contributors to industry publications, members of industry groups and individuals at competitor institutions.

The Ambassador is focused outside of the team, but within the company. This role promotes the team to the company, to keep upper management aware of what the team is doing

and to lobby for resources within the organization. This can only be done by building direct ties to management and involving them in the team's activities so they may advocate support.

The Task Coordinator is responsible for managing all aspects of tasks across departmental groups or even with external stakeholders, to maintain an accurate picture of where things are and what needs to happen to successfully complete tasks. In addition, this person seeks feedback from external stakeholders to present to the team to help it learn, adapt and propose new solutions as it moves forward.

Consequently, building inter-departmental or outward-facing teams is extremely important for getting an accurate view of what is going on within the company and how the team can effectively use its skills to further the goals of the company. As such, creating these outward-facing teams makes teams more nimble in responding to what is going on in the industry.

## **Conclusions**

Companies should be careful when creating organizational structures to make sure the structures they put in place make sense at the stage of development the company is in. In the early stages, the company may be able to sustain a very organic growth model, one that allows it to respond quickly to abrupt changes, but later on, this type of fluid, amorphous structure may actually inhibit the company by bottlenecking information. Therefore, the company may need to shift to a matrix design. If this shift is done in conjunction with building inter-departmental or cross-functional teams that engage in outward-facing activities, it may not limit the flexibility of the company the way a traditional matrix structure might.

## **Section Four – A Developmental Model for Leadership and Organizational Needs**

### **Development of a Company**

It can be argued that companies go through a “life cycle” similar to the development of a human being. In its early stages, an organization begins by focusing on idea generation and production, this phase is followed by a period of growth and expansion, and the final phase is an eventual productivity decline and exit. The company, itself, is an entity that is learning, adjusting and changing.

However, this image of the corporation as a living, breathing entity is only part of the picture. Much as a wayward child requires adequate parenting to guide it on the right track, so, too, does a corporation require a leader who can mold the company into a “being” with a moral right and wrong, and a strong sense of purpose and autonomy in moving forward.

One of the challenges in combining leadership theory with organizational theory is that leadership theory is almost always individualistic, whereas organizational theory is focused either on group dynamics or the organizational structure and rewards within a company. Often, the challenges the company faces in organizational processes are heavily influenced by challenges in leadership, and vice versa. Reconciling these theories, then, would be valuable in an integrated framework.

Although other writers have suggested that the development of a business is similar to human development, those efforts have stopped at this simple comparison and have not attempted to develop a comprehensive model connecting an organization’s developmental needs to its leadership needs, with few exceptions. In the 1970s, Larry Greiner developed an

organizational developmental model describing a company's growth as a period of "evolution" followed by "revolution" at each of five phases of development.

Greiner's model evaluates company growth according to five factors, including: age, size of company, evolution, revolution and industry growth rate. The phases of growth, or evolutions, are followed by revolutions, which Greiner describes as periods of crises in leadership, autonomy, control, bureaucracy, and what he terms the "?" crisis, which focuses on the psychological saturation of employees. As such, his model is an attempt to explain some of the challenges companies face during periods of growth. However, his model does not explore the intersection of leadership and organizational constraints.

This thesis seeks to propose a new organizational development model for use in examining leadership and organizational challenges in rapidly-growing organizations, as well as to provide a framework that could serve to predict whether a company will successfully overcome its challenges and move forward in the growth process.

### **Human Developmental Theory**

Developmental theory began with Freud and the Id, Ego and Superego. Freud took the first real look at how individuals change from children ruled solely by needs or wants (Id), to a development of self-control and an understanding of reality (Ego), to the recognition of morality and social norms (Superego).

This was followed by Piaget's effort to create a step-wise understanding of the cognitive development of children and adolescents. His model focused on how the human brain develops and how a child's capacity for understanding differs from that of an adult's. In Piaget's stages of intellectual development, children first develop in the Sensory Motor Period, during which

repeated reflexive behaviors evolve and the child begins to “control” these behaviors and interact with its environment. The second stage is the Preoperational Period, during which the child begins to speak, but everything is egocentric and morals are in the beginning stages. In Concrete Operations, logical thought has begun and concrete-problem solving occurs. Everything is logic-based. Last, in Formal Operations, the thinking becomes abstract.

Although Piaget’s research was meant to explain human development, many of these themes or motifs can be applied to the development phases of a company. A company begins by learning about its product, how to create it, and how to manipulate it. It then focuses on building the company from within, before understanding its surroundings and thinking abstractedly about its relationship to them.

This trajectory of company growth bears striking resemblance to the cognitive developmental approach of Erik Erikson, whose philosophy of development centers around the idea that people are born with certain traits, and that culture is the predominant driver of behavior and subsequent development. His approach toward human development focused on the interaction of three prongs: culture and external influences, the human mind or psychological nerve, and the body or biological programming of an individual.

This three-pronged approach can also be used when considering the life cycle of an organization, by focusing on the interaction of its culture, the mind (leadership and other key stakeholders) and the body (broader organizational structure, made up of processes and employees).

If one assumes, as I have discussed earlier in this thesis, that culture overlies all aspects of a company – stemming from leadership and directly influencing the actions of stakeholders,

employees and the entity as a whole – then that only leaves two central tenets around which to examine the changes facing the company, and these are leadership and organizational processes, or the “mind” and “body”. However, as mentioned before, these two areas are often examined individually, rather than in an integrated way. By examining Erikson’s developmental stages, we may be able to create a parallel framework for the corporation that can encompass both “mind” and “body”, pairing leadership, a traditionally individualistic theory, with organizational theory, which encompasses the entire company.

### **Erikson’s Stages of Human Development**

According to Erikson, a human being passes through eight phases in its development. Below is a graphic showing the direction of these phases and a brief description of the cognitive development of an individual at each phase.

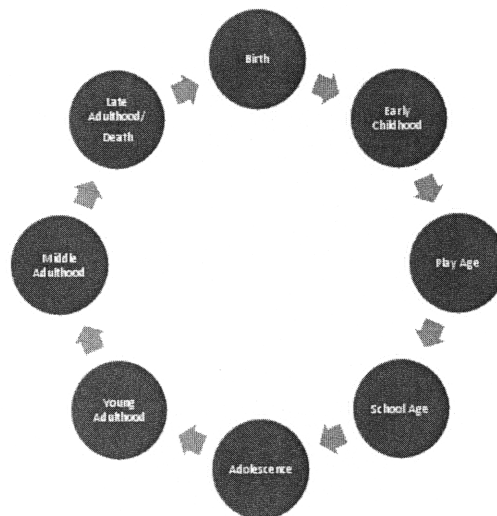


Figure 6: Erikson’s Stages of Development  
Source: Erikson, 1959

#### *Infancy/Birth:*

Starting at the top of the diagram, in the infant/birth stage, the focus is on caregiving by

the parent. This stage is marked by frustration by the child because its needs are not being met and it has not yet learned to trust the greater world.

### *Early Childhood:*

In early childhood, the focus is on the child learning and mastering basic skills for itself, including walking, talking, and eating. It is just learning to manipulate its environment, and doubt exists as to its own capabilities.

### *Play Age:*

In this phase, a child begins to take initiative by creating play situations and exploring his or her environment. At this phase, a child begins to identify with a social role in the family and begins to find purpose outside of itself.

### *School Age*

When the child enters school, the focus is on acquiring new skills and knowledge. It is at this time that the child begins to compare him or herself to peers, and outside relationships are formed at school and within the neighborhood.

### *Adolescence:*

In adolescence, an individual begins to create his or her own identity, and to separate him or herself from peers – setting oneself apart as an individual from those in wider society.

### *Young Adulthood*

It is in young adulthood that the individual begins to form long-term attachments, seeking out friendships and partners.

### *Middle Adulthood*

During middle adulthood, the focus returns to the individual, as he or she creates a stable environment for family and performs meaningful work. Bettering society and being active is important during this phase of life.

### *Late Adulthood:*

Integrity and reflection on experiences, including the despair of failures and death, are found in this phase.

What is significant about Erikson's stages is that, although these stages are meant to represent the development of an individual, they can very easily explain the "cognitive" development of a company, as it learns, grows and adapts to its environment. In much the same way an individual changes, a company must develop through certain phases along its path in order for it to mature to the next phase.

The traditional company life cycle model discusses phases of a company in relation to its financial needs at various points in time. For instance, in the "seed" phase, a company is looking for early capital, bootstrapping and relying on funds from family and friends. Later, it moves to "early-stage", where it is seeking funding from venture capitalists, and so on.

Certainly, financing is essential to company growth, but the development of a company does not relate solely to its funding. The company must move through different phases in its leadership and organizational structure so it can progress. Companies that cannot adequately adapt to change cannot move onto the next phase, and so, remain in stasis.

## A New Developmental Model of Organizational Change

Given that today's company life cycle models do not integrate the organizational and leadership needs, which often are related or even overlap, this thesis seeks to provide another model, one that takes into account these two crucial elements of organizational development. The proposed framework looks at the stages of a company in terms of both the leadership and organizational needs of the company at the key points of transition within a company's development.

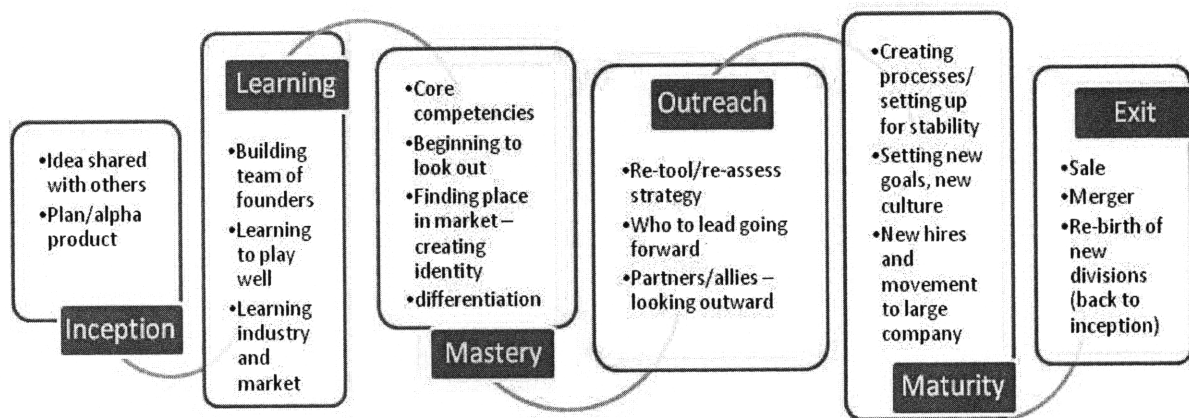


Figure 7: Organizational Development Model of Growth  
Source: Author

### An Explanation of the Phases

#### *Inception*

The inception phase parallels Erikson's Birth/Infancy phase because at this phase the founder most clearly adopts the role of caregiver. In this phase, the founder develops the idea, brings it to fruition, and begins selling it to VCs and like-minded entrepreneurial spirits who may be enticed to join in the creation of the company. As such, the founder holds all of the

responsibility for the company and handles all roles, from leading and envisioning to selling and hiring.

### *Leadership*

This framework for a leader is most consistent with the personality trait theories of leadership, in which it is most important for the company to find someone who exhibits certain characteristics. This phase is easiest when the founder is a leader who is charismatic, driven and persistent, someone who will not take “no” for an answer. Most important is this leader’s ability to sell his or her vision to future employees, founders and investors.

Another set of traits the leader requires is the patience and drive to develop the product idea. This is similar to Erikson’s idea of nurturing and incubating a child. As the product is developed, this process will require immense patience and creativity when encountering setbacks or challenges.

### *Organization*

Two founders may be needed, one who can manage the technical know-how and the other to develop excitement for the product. Organizationally, this stage of the company is individualistic, and there is no real need yet for any formal structure. If the founder is both technical and sales savvy, there may only need to be one leader. However, if the founder lacks one or the other of these skill sets, the founder should consider bringing on someone else who exhibits the skills he or she lacks.

Because there are no other employees to manage, the organizational structure is incredibly fluid and most closely resembles the organic model, if indeed, any framework exists

during this phase. If there are multiple founders, these founders are usually equal partners, so no reporting structures exist. In addition, skill sets are chosen to complement and overlap at this point.

### *Learning*

The learning phase of the company parallels Erikson's Play Age and School Age, in which children learn to master certain skills for themselves, such as walking, talking, and eating. While learning these activities, the child is plagued by doubt and is continually assessing whether the risk to benefit ratio of engaging in these activities is favorable.

In a small company, this is when the organization is creating a sample product and real doubt begins to emerge as to whether the company can become successful. The company is learning to self-express and create new thought processes within the founder group, creating a shared purpose among the founders. In addition, the company is learning about product development, is working with sources of external funding, and is learning to market its products and manage its resources.

### *Leadership*

At this phase, the role of the leader changes slightly and is more operations-focused. The leader must understand the technical know-how of the product and must exhibit patience with the team or engineers. The visionary leader is still important, but may step into more of a business development-focused role, with an outward-facing purpose of building prospective client and funding opportunities.

## *Organization*

The company begins to take on people to help develop the product, most often focusing on hiring technicians, scientists, and engineers. The team that is developing is focused almost solely on research and development of the new product. In general, this dynamic most resembles the Organic model, in which people may assume responsibility outside their areas, and allows people to focus more on what needs to be done, rather than on who is responsible for each function. Reporting structures are still rather flat, with equality among the employees. If employees report to anyone, it would be to the founding team at this point.

## *Mastery*

Mastery parallels Erikson's Adolescence, in which the individual has engaged in learning and is now acquiring new skills and accomplishing new goals. At this point, the teenager compares him or herself to peers, and begins to understand his or her own individual strengths. In addition, the adolescent begins to look outside of friends and family to build other relationships, such as in the school or neighborhood. As the teenager continues to grow, he or she develops his or her own personality, separate from people in wider society.

In the company context, Mastery is when the organization really finds its stride in the marketplace. Beyond the development of one product, it is focused on building its core competencies. In addition, it is beginning to understand and predict market trends and its own role within the industry. As such, the company is also beginning to differentiate itself from its competitors and to understand its unique position in the market.

## *Leadership*

At this phase, it is incredibly important for the company to bring in a CEO who is can lead the company to the next level. The leadership team must not only be operations focused, but must also definitely be forward-thinking in terms of what the next steps are, not only for the company, but also for the industry. At this point, the company should have a management team in place which has people in it with strengths in a variety of areas, including operations, sales, marketing and HR. Hiring will take place at this time as the company begins to attract more customers. As such, the CEO will need to build buy-in not only in the management team, but also in the new employees. This is the time when Schein's Theory of Culture is particularly important, because creating a culture for the company will help to solidify the different parts that are being acquired to create a whole.

## *Organization*

During this phase, the organization needs to develop teams so information can be adequately shared among everyone in the organization. Hiring usually begins at the management level, and for particular skill sets. Reporting structures begin to be acknowledged, with new hires reporting to the management team. Comparison metrics are needed, so processes should be created to analyze the efficiency and effectiveness of the organization.

In short, a hierarchy begins to form, with a type of reporting structure. In many cases, the reporting structure focuses on the Founders as ultimate decision makers, but this is when the company should trust the new CEO to make decisions about the general well-being of the company. The reporting structure may become something like a spoke and wheel management structure.

## *Outreach*

The Outreach period of the model most closely parallel's Erikson's Young Adulthood, in which the individual begins to form long term attachments, seeking out friendships and partners. During this phase of development, the focus is no longer on learning and what is done to the individual, but the individual begins to focus outside of him or herself. This means the person is confident enough in his or her own identity that he or she does not fear being "absorbed" by another person's identity when creating attachments.

An organization that has reached this phase has already determined its core competencies and is now reassessing or re-tooling as it creates new growth strategies. This may mean it will create new products, or even new partnerships or alliances with other companies to continue to develop and create a stronger "whole". The company is also looking to build long-term relationships with customers, suppliers and contractors.

## *Leadership*

At this phase, leadership becomes more distributed. As the company structure changes, key managers will assume more leadership within the company. The CEO will need to clearly see the next steps for the company and to motivate people to continue working on behalf of the organization. The actual role of the leader shifts from a more "transformational" leader, as defined by Bass, into a more "transactional" leader, one who can motivate because the employees expect something in return, whether it is recognition or pay.

## *Organization*

The structure at this time becomes more hierarchical for the company, as it begins to sort itself into a matrix. Reporting structures become more clearly defined within the hierarchy of this matrix, and the leader is no longer the center of all decision making for the company. An executive team takes assumes responsibility for company decision making, and leadership becomes distributed among a number of people within the company, each with varying skill sets. Departmental teams are developed, and it is at this phase of the organization's development that the company needs to be particularly careful to develop communication processes to ensure that teams are not isolated. It should build cross-functional teams within the company that integrate skills and facilitate the flow of communication.

## *Maturity*

The phase of maturity most closely parallels Erikson's Middle Adulthood, in which the focus of the individual is on creating a stable environment for family and engaging in meaningful work. At this time in one's life, the individual is seeking ways to better society, and being active is also important during this phase of life.

For a company, this stage means it is focused on creating a stable environment for itself and its employees. It may also mean that the company has begun to think about ways it can give back to its community.

## *Leadership*

Leadership functions within the company are highly specialized by this phase, and as such, leadership is distributed at various levels within the organization, with different levels of

authority and responsibility built into the company. This resembles the Linear Decision Making structure discussed in Section Three.

### *Organization*

At this phase in the company's development, the company has created a true matrix, with departments and reporting structures commensurate with the organization's needs. In addition, subsidiaries and other corporate structures may exist and require attention. Job roles are highly specialized and communication across different departments is incredibly challenging. Project teams built on X-Team frameworks would be highly effective ways to share communication across the different departments.

### *Exit*

In the Exit phase, similar to Erikson's Death phase, integrity and personal reflection are extremely important, as well as despair of failures. For a company, this is a reflection perhaps on the shortcomings of the company, detrimental changes to the industry, or even loss of key management people. It is important for the company to understand what has happened and why so it can begin to prepare itself for the next steps, whether that is to sell the company, to divide it into parts, or to take one of the products and begin anew (rebirth). This Exit phase, then, is a reflection of the past, with an eye toward continuation or change.

### *Leadership*

In the Exit phase, the leader, or CEO, plays a significant role in preparing the company employees either for a new cycle or rebirth, or in preparation for an acquisition. At this time of

uncertainty and doubt, the CEO must play a role in which he or she can reassure people about the future, whereas the functional managers are still leading the daily operations of the company.

### *Organization*

Because this is a time of change, the company may completely change its structure, shifting from a highly specialized matrix organization into a more hybrid company. This may be because funds are not sufficient to keep on as many employees, in which case the roles become less specialized, and the reporting structures may blur. At this phase, the company may move to a more Organic model to become more nimble for the next steps, whether they involve starting anew or finding a means of exit.

### **Take-Aways from the New Organizational Model and Erikson**

The most important point in both the proposed Organizational Model and in Erikson's Developmental Stages is that there exists a point at which the focus that has been on nurturing, teaching and acting upon the entity shifts to the entity learning, beginning to make its own decisions and forming its own relationships. In these models, the time allocation spent in each type of phase is roughly described in Figure 8. As a company develops, the emphasis changes from the company being acted upon by the founder to it beginning to act for itself.

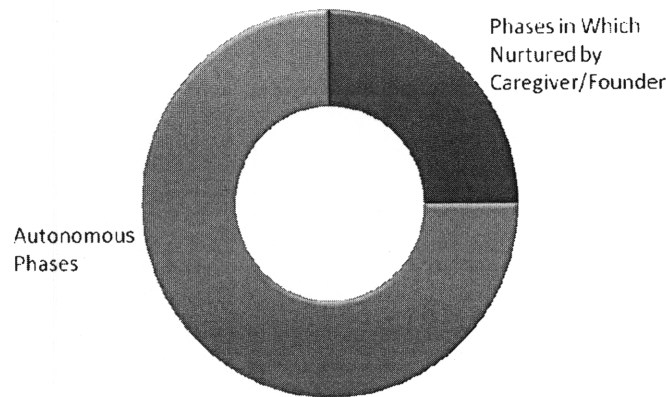


Figure 8: Time Allocation of Being Acted On Versus Acting  
 Source: Author

In the Autonomous Phases, the organization becomes a learning organization, within which learning and development occur at all levels. This may mean the establishment of multiple leaders within the company, more autonomy for these leaders, and influences from various directions within the company, all converging to help the company move to its next phase of development.

The following chart seeks to parallel more directly the distinctions between Erikson's and this model's development, and to show its leadership and organizational needs at each phase.

Model Phase	Distinctions	Leadership Need	Org Need	Erikson Phase
Inception	<ul style="list-style-type: none"> <li>•Coming up with idea</li> <li>•Inventing</li> <li>•Plan/Product concept</li> </ul>	<ul style="list-style-type: none"> <li>•Visionary Founder</li> <li>•Sales experience helpful</li> </ul>	<ul style="list-style-type: none"> <li>•Job flexibility that encompasses many functions</li> </ul>	Birth/Infancy Early Childhood
Learning	<ul style="list-style-type: none"> <li>•Building founders team</li> <li>•Learning how to interact with each other</li> <li>•Learning industry and market</li> </ul>	<ul style="list-style-type: none"> <li>•Operations focus</li> </ul>	<ul style="list-style-type: none"> <li>•Fluid teams</li> <li>•Organic model</li> </ul>	Play Age / School Age
Mastery	<ul style="list-style-type: none"> <li>•Create core competencies</li> <li>•Creating identity in market/ differentiation</li> </ul>	<ul style="list-style-type: none"> <li>•Visionary leader</li> <li>•Management team / some supervision</li> </ul>	<ul style="list-style-type: none"> <li>•Teams structure</li> <li>•Organic model</li> <li>•New processes</li> <li>•Spoke &amp; wheel reporting</li> </ul>	Adolescence
Outreach	<ul style="list-style-type: none"> <li>•Re-assess/re-tooling</li> <li>•Focus on looking outside company for allies</li> </ul>	<ul style="list-style-type: none"> <li>•Distributed leadership (DLM)</li> </ul>	<ul style="list-style-type: none"> <li>•Matrix</li> <li>•Processes</li> </ul>	Young Adulthood
Maturity	<ul style="list-style-type: none"> <li>•Setting new strategies</li> <li>•New goals</li> <li>•Stable company</li> </ul>	<ul style="list-style-type: none"> <li>•DLM</li> <li>• Highly specialized leadership roles</li> </ul>	<ul style="list-style-type: none"> <li>•Matrix structure</li> <li>•X-Teams (collaborative team building)</li> </ul>	Middle Adulthood
Exit	<ul style="list-style-type: none"> <li>•Reflection on past</li> <li>•Continuation/ change</li> </ul>	<ul style="list-style-type: none"> <li>•Return of transformational leader</li> </ul>	<ul style="list-style-type: none"> <li>•Organic structure to be nimble to change</li> </ul>	Late Adulthood/ Death

Figure 9: Chart of Leadership and Organizational Needs at Each Phase

Source: Author

## **Section Five – Case Studies of Company A and Z**

This section will examine the cases of two companies, both of which grew very quickly and both of which eventually were inhibited in their growth by organizational and leadership challenges. Although the two companies faced unique challenges, they shared some of the underlying causes. An analysis of these challenges will be introduced in Section Six, using the new organizational development model proposed in Section Four.

### **Company A**

Company A is a medical services firm that grew rapidly from 1997 until 2008. Although it was established in the mid-1960s, at that time the company consisted of no more than seven doctors working out of a small house. With advances in technology and an increased demand for their services, the company grew quickly in the last decade to over 40 doctors and 100 employees.

The company's focus was pathology. In the past, the doctors were generalists who conducted diagnoses on a number of different types of cell samples. As the company grew, it began to group the doctors by type of cell sample they could diagnose, building specialties around the particular part of the body from which the cells were taken (*e.g.*, lung, breast, brain, etc.). Over the last ten years, the company also began hiring people to perform non-medical job functions, such as sales and business development, accounting and administrators to liaise between laboratory staff and doctors.

Until 1997, the company had three leaders, two of whom were equity partners, and a third who was a founder with no equity in the company. These three leaders handled all decision making within the company; however, the two equity partners held the most sway within the

organization. As Company A grew to over 100 employees, few changes were made to this leadership structure. The company hired managers with previous experience in consulting and industry companies, but these managers were given no decision making authority, even over their own business units. The same three founders, all of whom were doctors, continued making all of the decisions, including those at the departmental, or non-medical, level.

The company created teams within the company to specialize on diagnoses in one body area and to act as autonomous units, with their own research, sales and financial accountability. In addition, Company A tried to shift to a hierarchical organizational structure, but failed to change its leadership model. The three founders still retained control over all decisions in the company, and the company failed to introduce management training for departmental managers. After trying its new organizational structure for one month, Company A quickly shifted back to its previous structure. Further growth within the company has been limited.

Company A is not “self-aware” and is unable to determine why the new organizational model failed. Furthermore, morale among doctors and managers remains low, as the company struggles to transition to a more efficient and effective management structure.

## **Company Z**

Company Z owned three small combined retail/restaurant locations and planned to open over twenty more locations in under one year. Company Z began as a part-retail/part-restaurant enterprise by three founders, who had a shared passion but very little experience running a company.

The founders sought out and hired an eighty-year-old, very experienced CEO named “Steve”, who had built one of the largest restaurant franchises in the area. In addition, they hired

on a fourth “founder” who had been a restaurant area manager to scale their business. They then brought on two more executives, one an MBA with experience in raising capital, who was installed as co-CEO with Steve, and another with knowledge of marketing, who became the CMO. The organization chart looked like this after just a few months:

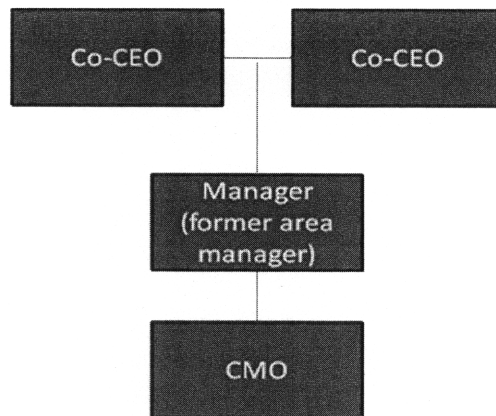


Figure 10: Organizational Chart of Company Z at Founding  
Source: Author

By this time, the founders were no longer involved in the day-to-day operations of the company. Company Z was approached by someone outside the company who wanted to open a franchise location. This individual had no prior experience running a business, but Company Z agreed and opened a franchise location. Company Z provided little to no oversight of the franchise store.

As the company grew, the Co-CEOs hired people for various functions: IT, franchising, training and corporate store operations, and an area manager. Over the next few months, the organization changed quickly to a hierarchical organizational structure, even though Company Z still had only three store locations and one franchised location. The resulting organizational chart looked something like this:

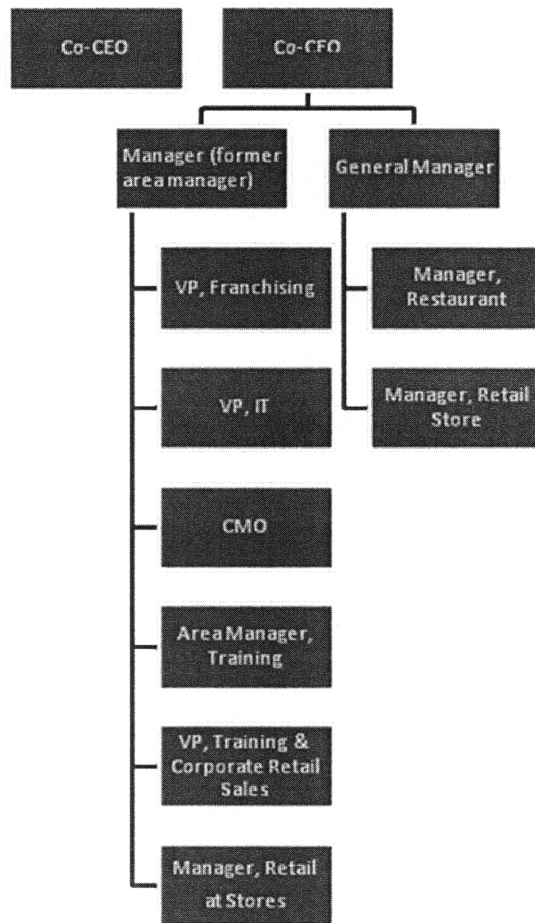


Figure 11: Organizational Chart of Company Z Several Months after Founding  
 Source: Author

This organization chart is an example of the corporate structure at this time. Note the overlap occurring within the individual roles. In total, Company Z had fourteen people working in its corporate office for four locations. At each individual location, the store hired over thirty individuals to handle both the restaurant and the retail sides. People with retail experience did not understand restaurant management, and people from restaurants knew nothing about retail.

Company Z then launched a rapid growth campaign. New franchises opened throughout the state, followed closely by five store openings around the country, from the west coast to the northern U.S. states. Overlap of job roles became extremely problematic. For instance, one person handled the retail *sales* information for corporate, whereas another managed the retail

*stores* for corporate. In addition, each location had a retail manager and sales associates to address the location's retail needs. The same overlap existed on the restaurant side for each location as well.

### *Leadership*

As the company grew, the leadership dynamic changed considerably. The MBA co-CEO left. Steve, the other co-CEO, became the sole decision maker in the company, and all of the employees tried to please him. Steve hired one of his close friends out of retirement to assume the role of COO for Company Z. This new COO was a former military guy who had been out of the workforce for several years, and whose leadership style was characterized by fear, which contrasted sharply with the culture of Company Z. All employees reported to this new COO.

### *Organizational Process*

Company Z retained the same organizational structure during its growth phase that it developed during its early stages (see Figure 10). Few new people were added, and the only real change was the addition of the COO. The number of employees at the corporate level remained the same, rather than starting small and growing with the company.

Unlike Company A, Company Z established a clear organizational hierarchy early on in its life, but it, too, was unable to sustain growth. The next section, Section Six, will look at the challenges these two companies faced, and, using the organizational development model from Section Four, will try to determine what aspects of leadership and structure hindered the growth in these examples.

## **Section Six – Analysis of Cases Using New Organizational Development Model**

The purpose of this section of the thesis is to use the organizational development model described in Section Four to understand the challenges of the companies outlined in Section Five. By understanding which phase of the model applies to each of the companies and what should happen at these phases before a company can move to the next phase, we can analyze what inhibited the growth of these companies. Using the lens of the model, we can assess the leadership and organizational capabilities of the companies and use this information to determine what must happen so they can move to the next developmental phase.

### **An Analysis of Company A**

#### *Determining the Company's Phase of the Model*

In Company A, the medical services firm, the company is limited by both its leadership and organizational processes. First, we should determine which phase best represents the company's current state. Based on the model in Section Four, Company A has completed the Mastery phase and is in the early stages of the Outreach phase. Company A has built its core competencies around pathology and has found a place for itself within the market. At this phase, it is re-assessing its leadership and organizational processes. However, Company A cannot move on to the next phase of growth, the Outreach phase, until it successfully develops a leadership team sufficient to sustain the next phase. An early attempt at moving to the next phase through an organizational redesign resulted in the company quickly falling back to re-assess its strategies.

#### *Leadership*

During the Mastery phase, leaders must be able to inspire and build teams of employees, creating a culture for the company. Company A has only successfully met some of these

requirements prior to trying to move into the Outreach phase. The founders built departmental teams, but did not empower the managers to make decisions before shifting back to its original hierarchy.

In the Outreach phase, the leadership should move to a more transactional, or operational, role, and Company A's leadership team does not meet this criteria. When the founders assessed their situation, they brought in an Executive Director to help manage operational needs, but did not give the Executive Director much authority. As the company became more specialized, leadership within the company should have become more distributed at different levels, which did not happen. This resulted in the company being stymied by the leadership structure within the organization, as decision making capacity was limited to the availability of the executive team to make all of the decisions in the organization.

### *Organization*

Company A compartmentalized its services and began creating specialty teams. Unfortunately, the company did not shift into any type of matrix hierarchy that would allow for more specialized job functions within the organization as described in the Mastery phase of the model. In addition, the reporting structure for everyone, including employees and doctors, was a hub and spoke design, with the founders at the center. Because the company did not transition into a more specialized organizational design with distributed leadership, the newly-created specialty teams were not viable. Therefore, the company was unable to successfully move into the Outreach phase.

## *Conclusions*

Using the organizational development model as an objective assessment tool may help the company understand how it successfully reached its current phase of development and may help it determine what it must do organizationally to reach the next phase of development. In the case of Company A, the inability of the founders to share leadership with others in the organization greatly influenced the organizational design of the company, preventing it from moving into a more hierarchical organization with leadership distributed among managers and specialty team leaders. Given this inability to remit control, the company could not sustain the specialty team model and moved back to its original hub and spoke reporting structure.

## **An Analysis of Company Z**

One of the most interesting aspects of Company Z, the retail/restaurant chain, is that it faced both leadership and organizational challenges within its short lifespan. The company scaled very quickly, but not successfully, often closing down stores before it could open more locations. Its leadership and management team have remained unaltered for most of its life, and the hierarchy in place did not change, whether the company owned only a few stores or controlled fifteen local stores and twelve franchised locations. In the case of Company Z, the organization did not effectively go through its natural development cycle and instead skipped over crucial growth phases.

### *Determining the Company's Phase of the Model*

Using the model, one can see that Company Z jumped from Inception to Learning phase very quickly, before leaping over Mastery directly to Outreach phase. This last leap drove the company backwards, because it did not allow for a natural progression to its next phase. Since it skipped over Mastery, Company Z had not adequately developed its core competencies, split as they were between retail and food service, and had not yet successfully positioned itself in the market. The company, while still early in the Learning phase, began looking outside of itself for franchise opportunities, which is a characteristic of a company in the Outreach phase. Beginning this outward focus without clear insight into the company's core strengths was detrimental to the company.

### *Leadership*

The original CEOs of the company focused on looking outward, rather than building up the internal management team. Steve, the CEO with large franchise experience, envisioned the company as the next national franchise success. However, neither of the two CEOs connected with the employees in any real fashion, so they were unable to manage the daily operations of the company.

The addition of a COO was another challenge for the company. The COO was brought in from a different business era. His management style was unfamiliar to the rest of the employees, and his approach was not consistent with the culture of the company. As such, the COO was unable to garner "buy-in" from key employees within the company.

If the company had not rushed through its growth phases, it might have been able to diagnose its leadership challenges and hire people able to lead small enterprises. The leadership

needs at earlier stages in the company differ significantly from those of a company in later stages. Company Z would have benefited from hiring someone who could lead a small start-up restaurant business of up to 15 locations or so, then hiring someone who could take the chain to 50 locations, before bringing in the current CEO, who knew about managing 1000+ franchise locations.

### *Organization*

The company staffed itself in its Learning stage the same way it staffed itself after it jumped to the Outreach phase, with the exception of local hires for new stores/locations. The corporate structure remained the same. Almost all of the corporate employees reported to the same person – the CEO – and no clear hierarchy existed among the departmental employees. Furthermore, jobs overlapped and no clear job distinctions existed.

One expects a company to grow, developing new “layers” of leadership and corporate structure, but Company Z did not grow in this manner. As mentioned above, Company Z hired people early on who knew how to manage many locations at once, but did not hire people who knew how to create a few locations first. The company began with people who knew how to manage 1000 locations, with the expectation that the company would “grow into” that number eventually. However, Company Z did not reach that level of growth, and as such, had management who did not know how to manage the smaller number or how to get to the next phase.

### *Conclusions*

Using the organizational development model allows us to see what happened in the development of the company that kept it from advancing as quickly as it otherwise might have.

By looking at the stages of growth, one can see that the company faced so many challenges because it had effectively leaped over stages of development. By skipping phases, the company handicapped itself and ultimately got stuck in its current phase, unable to move forward without first moving backward and re-grouping.

## **Section Seven – Conclusions and Call for Research**

Companies undergoing rapid change face a variety of challenges, which can include difficulties related to leadership and organizational processes. The purpose of this thesis was to explore leadership and organizational theory to determine how those theories might be useful in explaining the needs of companies at discrete periods of their growth. The new organizational development model proposed in Section Four may provide a useful framework to help companies diagnose difficulties related to growth. The framework should generate objective ways to approach these topics within the company and to help bridge two functions, leadership and organizational processes, that often directly impact one another.

Further research in this area should examine companies that meet the criteria at all phases of the organizational development model, to test the validity of the model at each stage. By examining SMEs that are encountering challenges, one might be able to develop a predictive assessment tool, based on the model stages.

In addition, research on SMEs should continue to address the challenges unique to this subset of companies and should look at a broader spectrum of challenges they face than those discussed here.

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