

Organizational Change at Procter & Gamble: *Organization 2005*

In 1996, Procter & Gamble's CEO committed the company to doubling its worldwide sales by the year 2006, to \$70 billion. Two years later, P&G had barely managed 3% annual growth and its share price was falling dramatically. The CEO, John Pepper, and the COO, Durk Jager, together embarked on a personal study mission to twelve top companies, including GE, H-P and 3M, to gain a broader perspective on how they might go about making P&G more innovative, faster to market, and more efficient. They concluded that P&G's problems were deeply embedded in its organization in a culture that was risk-averse and skeptical of innovation) and a political system that focused power on country general managers, each of whom had the right to decide which P&G products would be sold in that country and whether those products would be manufactured locally or sourced from other P&G units. Their solution was a change program called "Organization 2005" and the task of carrying it out passed to Jager, a lifelong P&G manager who became CEO in January 1999.

"Organization 2005" tackled the challenges of cultural and political change by redesigning the organizational structure. It replaced the long-standing geographic design with a product divisional structure) composed of seven global business units - GBUs! Each GBU had worldwide responsibility for the entire value chain of the products in the division, from new product development and production to marketing and distribution. Because it also had responsibility for support functions such as IT and personnel, most of P&G corporate functional staff moved into the GBUs, although a Global Business Services organization was set up to centralize the previously geographically distributed functions of accounting, payroll, and order management. This GBS Organization was to provide support not only for the GBUs but for another set of units: the Marketing Development Organizations (MDOs). These were eight regional market development organizations, whose mandate was to develop business strategies for their geographic regions and provide consumer and market information to the GBUs and to bring all regional markets up to the level of the best current performers. Product managers within the old country organizations would now report directly to a GBU; country managers would have a narrower range of responsibility and report to their MDO Vice President. Even for those within P&G who welcomed the new structure, the scale of the changes was formidable. The new head of worldwide marketing for the Food and Beverage GBU, for example, was the former head of the Latin American region. He took on the position of head of the new Latin American MDO as well as his new GBU position, and persuaded the company to base his new organization, which developed the worldwide marketing strategy for brands such as Jif peanut butter, Folges coffee, and Pringles potato chips in his home city of Caracas. P&G saw large numbers of its managers moving physically as well as organizationally, to fit into their new organizational roles. One account claimed that by June 2000, only 20% of P&G's top 200-300 managers were doing the same job they had 18 months earlier. According to another account, "P&G's staff lost their feel" for the company; so many found themselves in new roles that senior management admitted that they no longer had that crucial instinctive understanding of how the company was operating.

Initial press coverage was favorable, although there were many skeptics who cautioned that seeing clear results from the change processes would take time. Sales did not grow quickly, however, and profits actually fell. The few new products that emerged, although they were introduced with a speed that was impressive by traditional P&G standards were not seen as home runs (they included, for example, the Swiffer electrostatic broom). A couple of highly publicized attempts at acquisitions failed to materialize. Rumors began to emerge that there was strong internal resistance to the changes, and a number of managers nearly a quarter of P&G's brand managers, according to one report-quit the company. Complaints began to surface of a growing gap between Jager's optimism about the company's progress and the growing unhappiness and

confusion within P&G's ranks. All of this resulted in a fall in the share price that halved the value of the company between January and June 2001.

Jager resigned in June 2001, barely 18 months into his tenure. Analysis in the business press spanned a wide range of opinion. At one extreme was the judgment of the Lex columnist in the Financial Times, who commented that: "Things have come to a pretty pass when a company has to restructure its way out of its previous restructuring. Procter & Gamble's 1999 revamp—"Organization 2005" - is only 50% complete but already 100% a disaster. It has neither boosted innovation and sales growth nor reduced costs. Revenues in the fiscal year to June will be flat at best; operating profits have fallen for the past four quarters; and administrative costs, at 30% of sales, are 300 basis points higher now than in 1998". Other commentators blamed P&G's board for not giving Jager enough time to deliver on his program: "They hanged the wrong guy", says Burt Flickinger III of Reach Marketing. "He was just what was needed in a culture that had gotten far too complacent. Durk was a take-no-prisoners, win-dammit-win CEO", Flickinger points out that former P&G chief John Smale gave Jack Smith nearly a decade to reverse the decline of General Motors. "At P&G, the board did not give the CEO sufficient time to turn the company around". In their conversations with the business press, which was eagerly covering the P&G situation, the Board of Directors gave three reasons for moving to replace Jager so quickly. One was of course the fall in the share price. Underlying the fall, however, was the second factor: perceived failures in the reorganization effort, especially the changes in reporting responsibility and systems. As one source pointed out "P&G, a model of fiscal conservatism, overpromised on its numbers for the past two quarters because accurate numbers about profit and loss were not getting to headquarters in Cincinnati". Finally, the Chairman of the Board criticized Jager for a political failure: having moved "too far, too fast" and failing to carry the company with him. "Jager's inability to win over the majority of his key subordinates contributed to the board's loss of confidence in him". P&G's employees welcomed the announcement that Jager's successor as CEO would be Alan G. Lafley, a P&G senior manager known for his superb "people skills". The analysts and the business press were far more skeptical. In fact, the share price fell when his appointment was announced and Business Week carried a critical article entitled "Warm and Fuzzy won't save P&G". Lafley refocused P&G's strategy on its existing brands and tackled the cost increases that accompanied Organization 2005 by cutting 9,600 jobs and ending some of Jager's cherished product innovation projects. He did, however, keep the new Organization design of GBUs and MDOs and GBS, either because he thought it was an improvement on the old structures or because he believed that the company would not cope well with another radical restructuring, even one that returned it to its former design.

Just over two years later, Lafley was hailed by Fortune magazine for turning P&G around in 27 months and held up as an example of "the new breed of turnaround specialist" who leads by listening rather than by making speeches about vision and by a focus on building upon established strengths rather than on initiating aggressive change programs (Brooker, 2002).

Source: Ancona, D. et al. (2005). Managing for the future: Organizational behavior and processes.