Hayekian insights into intra-firm coordination:

Exploring the rule following perspective.

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Thesis Abstract: The purpose of this thesis is to examine intra-firm coordination by individuals following common rules of behaviour. Individuals within a firm have to coordinate their activities where each has knowledge that others in the firm do not have; there is a division of knowledge just as there is a division of labour. Rule following may be a solution to that problem. Rule following behaviour may be consistent with much of the internal organisation of firms that is currently explained by ‘command’; for example hierarchy and the giving of ‘orders’. The thesis attempts to make three contributions: Firstly, the case for coordination by rule following within the firm is a minor tradition within organisational analysis theory and practice. The first contribution is to highlight and explore this literature. Secondly, the thesis describes two small-scale exploratory studies to test the propositions that rule following might be a coordination mechanism within two examined firms and then to explore processes of change through the rule following perspective ‘lens’. Finally, the thesis uses the first two contributions to tentatively conjecture the case for an invisible hand (or Mengerian) explanation for the emergence of the modern business firm. Some implications of this perspective and some opportunities for further research are also outlined.

'… seeing that you, sir, do not yourself desire to command the Macedonians tyrannically, but expressly state that you will lead them only by gaining their approval, and failing this you will not compel them…' Alexander's men to Alexander. (Quoted in Keegan, 1987, 45)

Chapter 1: Introduction:

The purpose of this thesis is to examine intra-firm coordination by individuals following rules of behaviour. The thesis attempts to make three contributions:

1. The case for coordination within the firm by rule following is a minor tradition within organisational studies theory. The first contribution is to try to highlight and explore this literature.
2. The thesis then proceeds to carry out two small-scale exploratory studies to test the propositions that rule following might be an important coordination mechanism within the two examined firms and then to explore processes of change, in those firms, through the rule following 'lens'.
3. Finally, the thesis uses the first two contributions to tentatively conjecture the case for an invisible hand (or Mengerian) explanation for the emergence of the modern business firm.

The researcher is a partner in a global accountancy firm. He was motivated to undertake this research by a perceived lack of realism in the management literature. In the management literature, managers seem to function in a realm about which they have considerable knowledge, over which they seem to have some control and in which wide-ranging opportunities are open to them. In the researcher's experience things are more uncertain. In addition, nothing in the management literature seemed to adequately describe the experience of being an employee – especially the lengthy and often difficult mental process of becoming an effective employee. It seemed to the researcher that there was more to being an employee than following the instructions of a superior; that employees are never 'docile' (Hamel, 2007, 130) and that their most useful traits are not being 'tractable, manageable and, above all, teachable.' (Simon, 1991)

This research project gave the researcher an opportunity to explore this inconsistency between the researcher's experience and the management literature in a more formal, rigorous and structured way. It was an opportunity for the researcher to change, refine and explore his ideas and to test them against the literature, the opinions of the executives in the case study firms and his research colleagues and supervisors.

The initial insights for this thesis came from the writings of the Austrian economist FA Hayek. These writings, at least after 1948, were focused on individuals acting in an uncertain dynamic environment about which they know very little. These writings did not seem to feature to any great extent in the management literature but, to the researcher, they seemed a like a useful starting point. In circumstances of uncertainty and ignorance, Hayek showed, individuals participating in the market order, each with his or her own unique but limited knowledge, solve problems and coordinate their behaviour by following rules. It seemed to the researcher, and to others (Sautet, 2000, Ioannides, 2003a and b), that this knowledge problem (the, so-called, Hayekian knowledge problem) also existed within the firm. However, the conventional view is that, within the firm, this knowledge problem is solved by a completely different coordination mechanism than rule following – command. It seemed to the researcher from his own experiences that perhaps command is over-privileged, by Hayek and others, as a coordination mechanism within the firm. On re-examination of the management literature the researcher has found that rule following as a coordination mechanism within the firm is a minor, thin, but constant stream through the literature, at least since the 1930s and the writings of Mary Parker Follett (1940).

If rule following was an important coordination mechanism within the firm, the researcher thought through when such a mechanism might be more clearly visible. Like Horwitz (2008), the researcher thought that rule following may present a problem for any change process within a firm. Therefore, one of the central features of this thesis is to try to test the rule following perspective in situations where some form of change would be hard to avoid. The situations chosen were, firstly, where CRH makes an acquisition and the post-acquisition integration process there and, secondly, where local food brands were sold by global food companies to a new small Irish food company, Jacob Fruitfield. The times around acquisitions and disposals may be associated with change in the firms involved. (Roberts, 2004, 252; Kotter, 1996, 18; Pautler 2003; Harrison, 2007)

The structure of the thesis.

Chapter 1 introduces the subject matter and purpose of this thesis. This chapter also contains a discussion on two preliminary matters that are important for the rest of this thesis. Firstly, there is an attempt to explain more fully what is meant by a 'rule' and the difference between a 'rule' and 'command'. Secondly, command seems to be taken for granted as a coordination mechanism within the firm with a corresponding neglect of rule following. Therefore, as a preliminary point to exploring rule following in Chapter 2, the researcher outlines some problems with command as a coordination mechanism.

Chapter 2 builds on Hayek's conjecture that rule following behaviour is the solution, to a greater or lesser degree, to the dispersal of knowledge among individuals – as rule following behaviour allows individuals to predict the actions of others and thus extends the range of knowledge available to each individual. Reviewing the management and economic literature shows a small but persistent stream of writings on the usefulness of rule following within the firm. Using the writings of Mary Parker Follett as a base, the chapter attempts to recover this literature and attempts to show that certain features within firms can be explained by rule following behaviour. The point is then made that rule following behaviour, while it may not necessarily result in rigidity, may present difficulties for change within a business firm.

Chapter 3 outlines the research methods for the case studies to follow. It explores whether narrative examples, stories, are useful in making sense of decisions in the complex environment in which all managers function. This point is then used as the main methodological support for the two case studies to follow, both of which are explored in narrative form. These cases were small, limited, studies designed to test some basic propositions resulting from the rule following perspective. Some particular problems with investigating rule following are explored.

The case studies are designed to test the conjecture that there may be more visible evidence to support the rule following perspective if change were a difficult, voluntary, complex activity within the business firm. Therefore, the case studies are focused on situations where some form of change seems inevitable. In first part of Chapter 4 the post-acquisition integration strategy in CRH plc is documented. In this case study we see a post-acquisition integration strategy that allows for integration to stretch out for decades and, as such, is out of tune with the conventional wisdom. Also documented in Chapter 4 is the story behind Jacob Fruitfield; the acquisition of local food-brands from two large multi-nationals by a small Irish management team. Here the Irish brands struggled when owned by two global food brand powerhouses but have prospered under the ownership of the Irish management group. The two cases were chosen as they allow for an exploration of different sides of the consequences of acquisition and divestment decisions within firms - occasions where some form of change is almost inevitable. In Chapter 5, these two case studies are analysed in terms of the rule following perspective. The rule following perspective is used to try to explain the decisions that were made and not made in the organisations. The two case studies are compared and contrasted both with each other and with Warren Buffett's Berkshire Hathaway and a number of other entities.

Chapter 6, as a conclusion and offering areas for further research, conjectures, as an implication of the rule following perspective, a Mengerian, or invisible-hand, theory of the business firm. It discusses the implications of the fact that within the extended market order, individuals will, by definition, have to follow similar rules. Thus problems will, as individuals use rules to solve problems, tend to be solved in similar ways. The business firm emerges as a way of solving problems in different ways – every business firm has its own unique body of rules and so its own unique problem-solving abilities; within the market order the ability to solve problems in a large number of different ways is enabled by the business firm.

The difference between a rule and a command.

There is one, somewhat complex, point that has to be confronted at an early stage. This is the difference between a 'rule' and a 'command'. Making this distinction is harder than it appears because, upon examination, the distinction is only rarely, if ever, made in our day to day lives. Therefore, it may be useful to attempt, however vainly, to be clear on this point as early as possible.

Any reader may immediately think that the essence of coordination within a firm is an individual telling other individuals what to do, where to do it, how to do it and when to do it (see Coase, 1988, 35). However, these instructions may not be commands. The Shorter Oxford English Dictionary defines ‘command’, inter alia, as ‘…The act of commanding; an authoritative statement that a person must do something; an order, bidding…’ An ‘order’ is defined as, including, ‘… bid, command, direct...’ A command is given by one individual to another. A command must, by definition, be aimed at a particular foreseen result: ‘do this’, ‘perform that task’. According to Hayek a command ‘aims at a particular result or particular foreseen results, and together with the particular circumstances known to him who issues or receives the command will determine a particular action.’ (Hayek, 1976, 14; see also Hayek, 1976, 128 and 129) A command must not be in accordance with the rules; otherwise the ‘command’ is merely rule articulation.

Hayek contrasts a command with a rule: ‘a rule refers to an unknown number of persons, and merely states certain attributes which any such action ought to possess.’ (Hayek, 1976, 14) ‘Rule’ is defined in the Shorter Oxford English Dictionary as, including, ‘… A principle regulating practice or procedure; a dominant custom or habit. Also accepted or prescribed principles, method, practice custom etc.; *rare* rigid system or routine.’ As Becker (2004) points out: ‘If {condition A}, then {do B}’ is a rule and not a command. The fact that the first part of this statement is often not articulated but is merely tacitly understood can lead an observer astray:

- Simon called the following instructions 'commands' (Simon, 1991): 'repair this hinge…all purchases must be made through the purchasing department…manufacture as cheaply as possible consistent with quality… Always decide in such a way as to maximize company profit!' These are not, it is submitted, commands but rules: rules aimed at known and unknown individuals solving as yet not fully known problems.

- Even the first of Simon's rules: 'repair this hinge' is not a command despite its close resemblance to a command. It is merely information and not a command (as repairing faulty hinges is a rule known to all; 'repair this hinge' is merely an alternate way of saying 'I have noticed this hinge is broken and I think the rule is that this hinge should be repaired'). A command would only come into play if the rule was not to repair broken hinges and someone in authority decided that a particular hinge should be repaired by a particular person.

What is often considered a command may just be the transmission of information. For example, Mary Parker Follett wrote: 'The head of the sales department does not give orders to the head of the production department, or vice versa. Each studies the market and the final decision is made as the market demands. This is, ideally, what should take place between foremen and rank and file, between any head and his subordinates.' (Follett, 1940, 58, 59) As Schlicht points out: 'If the sales department provides notification that more production is needed, this is not a command in the usual sense of the word: what it is is a piece of information that serves to coordinate various economic activities in accordance with a shared understanding of roles and responsibilities.' (Schlicht, 1998, 222, 223) Obviously, this shows Coase's example of a command, an employee being moved from one department to another, (1988, 35) in a different light.

In every case an instruction to a machine, including a computer, is a command. It is given by the commander to the machine and aims at a particular foreseen result. A command is always outside the rules, arbitrary and ad hoc, it never creates a precedent or an expectation. Knowing the purpose of a command is irrelevant to the person commanded. When we think of a command in that way, we can see how it differs from any instruction we give to another human being. (Schlicht, 1998, 232 and Schlicht, 2008) Rule following necessarily requires an individual to search for the appropriate rule to follow. The actual expression may be a fumbling phrase that sounds like a command but it is, nevertheless, rule articulation and not a 'command' or an 'order'.

Mary Parker Follett's understanding of the correct nature of intra-firm coordination, and the limited circumstances when a command is actually given, allowed her to redefine the word 'order' as merely 'a symbol' (Follett, 1940, 65). She wrote: 'I may say to an employee, "Do so and so," but I should say it only because we have both agreed, openly or tacitly, that that which I am ordering done is the best thing to be done. The order is then a symbol.' (Follett, 1940, 65) 'The best leader has not followers, but men and women working with him.’ (Follett, 1940, 262) The leader ‘knows how to encourage initiative, how to draw out from all what each has to give.’ (Follett, 1940, 247).

Finally, the body of rules is often described using the words ‘custom’, ‘routine’ and ‘standard operating procedure’. There will be recourse to these terms in this thesis but their use often causes people to mistake rule following for rigidity of behaviour. Rule following can result in inflexibility but this is not necessarily so. We will return to this important point in Chapter 2. In the meantime, as it is a central discussion in this thesis, we will note that rule following does result in certain difficulties for change (Schlicht, 2008; Horwitz, 2008) and, therefore, focusing on change would seem like fruitful ground for any exploration of rule following. This we will do in the case studies later in this thesis.

Some problems with command as a coordination mechanism.

The benefits of coordination by rule following may not be as obvious as they should be; this is partly because the problems with command as a coordination mechanism are often not considered. For example, that command is the main coordination mechanism within the firm is, if it is considered at all, taken almost as a given in the economic literature on the firm (Coase, 1988, 35; Williamson, 1994; Simon, 1991; Hayek, 1973; Sautet, 2000; Groenewegen, 2002; Foss and Foss, 2002). This is puzzling because command may be a cumbersome coordination mechanism with a large number of practical problems.

Michael Polanyi (1951) explored command in his essay *The Span of Central Direction*. Polanyi noted that he 'may be labouring the obvious. But obvious though my result may seem, I can find it stated nowhere, while a great deal has been written which contradicts it in detail.' (Polanyi, 1951, 136) In this essay, Polanyi took the example of a corporate body coordinated by command from the top. 'Since the chief can give orders only directly to no more than three to five subordinates, any larger body must be coordinated through devolution to successive tiers of subordinate officials… which is also the organ for reporting upwards the events which occur among the workers (or soldiers, etc.) at the base… A corporation thus elaborates the ideas of the chief executive and his advisers into a wealth of detail…' (139) Polanyi then explored the logic of this structure. 'A corporate system … can be extended to any considerable extent only by increasing the height of the pyramid through the addition of new tiers…' Polanyi then worked though the ability of a number of individuals to coordinate their activity where there was a mutual self-adjustment and where there was command. Even with an organisation of five people, self-adjustment rapidly showed itself to be superior to command.

But this is not the only problem. Other problems include:

- If an individual in the firm is commanded or ordered to do something the individual may, mistakenly, ascribe to that instruction the status of a rule.

(Schlicht, 2008) The individual then may, in similar circumstances, follow that rule as he or she understands it. However, if the instruction was a command, and necessarily not in conformity with the rules of the firm, the individual is now constructing a set of rules that is in conflict with the other rules of the firm; the order within the firm starts to break-down.

- Foss and Foss in their paper *Authority in the Context of Distributed Knowledge* (2002) argue that in certain circumstances authority can be 'an efficient mechanism for performing the coordination task under distributed knowledge.' They argue that in certain circumstances that the loss of knowledge in giving a command is overcome by the advantages of command. They give a series of examples of such circumstances: an urgent decision required or the coordination of decomposed tasks. However, these explanations may not be complete as, for example, one of the pieces of knowledge missing to a commander may be to make what was thought was urgent into not urgent at all or what was thought to be a task that could be decomposed was actually subject to hidden interdependencies.

- There can be no learning where people act on command; the person giving the command is 'the only one who would be allowed to profit from experience' (Hayek, 1978, 141). For example, if an individual comes across a situation similar to one he or she has been in before, there is no option but not to act and wait for a command, with command previous experience can be no guide to future actions; a command contains no information about future action.

- In a hierarchy, there is an opportunity for a large number of persons to give commands. However, any particular command, given the unique knowledge of the person giving the command, may appear almost random to others, who do not know the crucial piece of information upon which the decision was made, and thus place an intolerable burden on intra-firm coordination. On the other hand, allowing individuals to act based on their own unique knowledge but within common rules, may provide others with a more accurate picture of what is going on – knowledge of this fact is useful in itself. Hayek pointed out: '[T]he captain of a battleship may sometimes recognize the nature of an observed object less from his direct perception of it than from the response of his ship…' (Hayek, 1952, 91) If any part of the organisation can supersede this with a command, this ability is destroyed completely. (See also, Polanyi, 1951, 141, 142)

- Some argue that simple tasks can be coordinated by command (Hayek, 1973, 49; Sautet, 2000, 98; Ioannides, 2003a). One such simple task was FW Taylor's central experiment in *The Principles of Scientific Management* (1911), the loading of pigs of iron onto a railcar; a task so simple it could be undertaken by a trained 'intelligent gorilla' (Taylor, 1911, 18). Taylor's clerks gave what they thought were complete instructions to the workman undertaking the task: Henry Noll. Taylor wrote of these experiments:

> '[E]ach man receives in most cases complete written instructions, describing in detail the task he is to accomplish, as well as the means to be used in doing the work… This task specifies not only what is to be done but how it is to be done and the exact time allowed for doing it.' (Taylor, 1911, 16 and 17)

However thorough their planning, there must have been an immense amount of information that Taylor's clerks did not know, even if it is only Noll's knowledge of himself or his particular knowledge of time and place. In the end, Taylor must, at some level, have realised this because he paid Noll not for following these complete instructions but only if he made his target of loading 47 tons of pig iron in a shift. In other words, Noll's internal commitment to the rules of this little order and his commitment to overcome the gaps in Taylor's clerks' knowledge was an essential requirement for completing the task. Taylor recognised this and paid for the completion of the task and not the mere following of the 'commands'.

There is one further problem with command as a coordination mechanism within the firm: a command, as defined by Hayek (see above) necessarily aims at a particular foreseen result. However, all business, all firms, function in a dynamic environment. Very often in business the solution to a problem cannot be foreseen; the goal is ill-defined (Klein, 1998, 146). Witt points out:

> '[The entrepreneur has no] formal blueprint for financing, investing, hiring, assigning tasks, producing, purchasing and marketing as it is in business

> strategies and formal planning discussed in the management literature….[A]llowing for, and relying on, decentralized problem-solving capabilities of the firm members in a potentially growing firm organization, a business conception must be sufficiently general and unspecific… It must be able to codevelop with the unfolding business venture in order to cope with its uncertainties and the initial lack of experience. The outcome of learning and the discovery of unforeseen problems and their solutions can, and often do, mean rearrangement or even entire reconceptualization of the underlying notions…' (Witt, 2000, 740)

Members of the firm will proceed towards the solution to a problem by a process of clarifying the goal as they try to achieve it. A command may not be useful in such circumstances as a command given in the past may not be congruent with the goal as perceived now. As Mary Parker Follett wrote: 'If the situation is never stationary, then the order should never be stationary… How is the order to keep up with the situation? External orders never can, only those drawn freshly from the situation.' (Follett, 1940, 65)

Given these problems, there is some evidence for the contention that command is a cumbersome coordination mechanism. This view could be taken further and it may be possible to suggest that management within a firm may *actively seek to avoid* using command as a coordination mechanism; 'mixing very different coordination mechanisms may lead to efficiency losses' (Foss, 2002). Rule following behaviour is a useful coordination mechanism, particularly in a dynamic (changing) environment, but rule following behaviour is disrupted by command. For example, an employee may mistake a command for a rule and inappropriately repeat the command in, what the employee thinks is, similar circumstances in the future. (Schlicht, 2008) Or the reverse may happen, for example, in a dynamic environment a rule may be mistaken for a command and an employee may continue towards a particular concrete result that is no longer appropriate. Therefore, even if the power of command does exist within the firm, over time, the practice may have arisen that this power is suppressed and managers within a firm would avoid command as a coordination mechanism. (Follett, 1940, 52) There is a clue, which we will return to later, in the fact that in business firms the distinction between a rule and a command, when giving an instruction, is *never explicitly made*. It is possible that this distinction is tacit but this seems unlikely as, again, interviews with executives and an examination of experience seems to show that managers do expect employees, when told to do something once, to do similar things in similar circumstances even if not told. (Schlicht, 2008; see also Brady and Walsh, 2008)

The above discussion is just a brief outline of some problems with command as a coordination mechanism. Rule following as a coordination mechanism is explored in the next chapter of this thesis.

Chapter 2

Rule following within the firm.

Key-words: Knowledge, order, ‘the law of the situation’, coordination, rule following.

Chapter Summary: The conventional argument is that firms are coordinated by command. This chapter examines whether what happens within a firm can be explained by rule following behaviour. The rule following perspective seems to have support in the writings of Mary Parker Follett and others. The chapter goes on to try to resolve a number of common misunderstandings about the nature of rule following behaviour within the firm. For example, it is speculated that rule following may be consistent with coordinated behaviour in a dynamic environment and with hierarchy. The chapter concludes with an introduction to the problems that will be investigated in the case studies.

'1. Ages 18 to 35, middle-school education
2. Good health, good quality
3. Attentive to hygiene, willing to eat bitterness and work hard.'

'Willing to eat bitterness and work hard, 25 to 45 yuan a day, male, middle school.'

Job advertisements: Wenzhou, China. (Hessler, 2007)

Chapter 2: Rule Following within the firm.

We saw in the previous chapter that there are difficulties with coordination within the firm by command. In this chapter coordination by rule following behaviour is examined. This is made somewhat more difficult as the role of rule following generally in human behaviour is not widely recognised. Therefore, this chapter opens with a brief general look at rule following before returning to the firm.

Rule following is pervasive in human action.

The focus in decision-making analysis has been on what Klein (1998) calls rational choice strategies: when making a decision people are supposed to identify options, identify ways of evaluating those options, evaluate each option, rank them and pick the option with the highest score (see for example, Simon, 1965). It is now becoming clear that these strategies are not generally used: Zhou argues: 'our attention should be less on complicated models of decision making and more on subtle models of rule following…' (Zhou, 1997, 278). March writes: 'Actual decisions … seem often to involve finding appropriate rules to follow…. Rather than evaluating alternatives in terms of the values of their consequences it matches situations and identities.' (March, 1997, 17) Individuals follow rules in every aspect of their behaviour, often without realizing it: as one modern anthropologist writes, 'The rules may vary from culture to culture, but there are always rules.' (Fox, 2004, 13) It is not going too far to repeat Peters's assertion: '*Man is a rule following animal.*' (Peters, 1958, 5 – italics in original.)

Unfortunately, an early focus on rule following, the literature on 'heuristics and biases', focused on situations where rule following seemed to lead individuals to behave in ways that were not optimal (Kahneman et al, 1982). More recent research has left few in doubt as to the power of rule following (Klein, 1998; Dane and Pratt, 2007). The literature shows the usefulness of rule following in making decisions in the following circumstances:

- It seems to underpin individuals' ability to make decisions where there is uncertainty (Heiner, 1983). Heiner argued that 'uncertainty requires behaviour to be governed by mechanisms that restrict the flexibility to choose potential actions, or which produce a selective alertness to information that might prompt particular actions to be chosen.' (Heiner, 1983; see also Witt, 1998, 1999) In other words rule following economises on brain-power; in Loasby's (2007) phrase, it is a source of 'cognitive economy'. As Witt has pointed out, and this is a crucial point for decision-making in the firm, in a culture individuals tend to economise cognitive resources in the same ways: 'intense communication tends to induce similarities in which alternatives of action the agents involved selectively perceive as being feasible and in what they disregard.' (Witt, 1999; see also Witt, 2000 and Nooteboom, 2006)

- Rule following also economises on the amount of time it takes to make a decision. Klein (1998) studied the decisions made by experienced firefighters, medical personnel and soldiers. For these individuals, decisions are often made under considerable pressure: injury or death can follow from a slow or wrong decision, there is often inadequate information, the goals can be unclear, tasks are decomposed and there are usually poorly defined procedures as to what to do. Despite the intense pressure to make the right decision, experienced firefighters generated comparison rarely. One firefighter told Klein: 'I don't make decisions… I don't remember when I've ever made a decision.' (Klein, 1998, 11) Their actions were guided by the application of complex, usually tacit rules, to the unique facts of any given situation. No time was spent considering different options; although further situation analysis could follow the initial decision.

- But there is a further benefit to rule following that is crucial to this thesis. An individual knowing and following the rules, however unconsciously and tacitly, can, despite the subjectivity and uniqueness of each individual's experiences (Hayek, 1952; Rizzello, 2004) and knowledge (Hayek, 1948), predict the behaviour of others following the same rules and his or her behaviour can also be predicted by others. (Heiner, 1983) We can walk

> down a crowded street without physically touching another person because we and all the other individuals on the street will follow rules of behaviour that will guide us to move to the left or the right, to move first or second, to move faster or slower and so on as we approach every other individual. This rule following behaviour also extends the range of our knowledge because we can predict the behaviour of others. We can drive down a crowded motorway at 130km per hour. Our knowledge of the rules and our knowledge that other road users will follow those rules, allows us to *see* a clear path in time and space down that crowded motorway.

Economising on cognitive resources and making faster decisions are useful but this thesis will focus on that other benefit of rule following – the ability to predict the behaviour of others. Hayek (1948) argued that knowledge is dispersed between every participant in the larger market order; any one individual or smaller group of people will be ignorant of much of the knowledge of every other market participant. This has been called the Hayekian knowledge problem. (Sautet, 2000, 13) There is a division of knowledge just as there is a division of labour (Hayek, 1960, 157). However, the Hayekian knowledge problem raised a problem. Given this division of knowledge and the ignorance of each individual market participant, how is the market economy ordered, how is there any coordination? Especially as much of that unique knowledge is the fleeting knowledge of time and place or, incommunicable, tacit knowledge. How are all the activities of each individual market participant coordinated given how little each individual market participant knows? Hayek formulated the problem by pointing out: ‘We need decentralization because only thus can we insure that the knowledge of particular circumstances of time and place will be promptly used. But the man “on the spot” cannot decide solely on the basis of his limited but intimate knowledge of the facts of his immediate surroundings. There still remains the problem communicating to him such further information as he needs to fit his decisions into the whole pattern of changes in the larger economic system.’(Hayek, 1948, 84) Having identified this problem, Hayek offered a solution.

The market is ordered because each individual in the market follows rules; the market is a rule-bound order – a spontaneous order created by rule following behaviour (Hayek, 1973). This rule following behaviour mitigates the effects of the division of knowledge: ‘Rules are a device for coping with our constitutional ignorance.’ (Hayek, 1976; 8) Rule following behaviour allows individuals to predict the actions of others and thus extend the range of our knowledge; the rules tell a person, wrote Hayek, ‘the facts he may count on and thereby extends the range within which he can predict the consequences of his actions’ (Hayek, 1960, 156). Thus rule following is the basis on which the market order is created; the market order is a spontaneous order created, unintentionally, by the rule following behaviour of individuals.

The Hayekian knowledge problem and rule following within the firm.

A recent stream of literature has pointed out that, given the division of labour and knowledge among employees, there must also be Hayekian knowledge problem within the firm. (Sautet, 2000; Ioannides, 2003a, 2003b; Foss 2002) Some writers contend that this knowledge problem within organisations is mitigated, to a more or less satisfactory degree, by commands. (Sautet, 2000, 99; Hayek, 1973, 49) However, it has recently been suggested that it must also be mitigated, to a greater or lesser degree, by a reliance on rule following behaviour (Ioannides 2003a, 2003b; see also Schlicht, 1998).

Given that rule following is pervasive in the daily lives of individuals, it would be surprising that individuals did not follow rules within the firm. There is evidence to support this view; as Becker (2004) notes: 'members [of organisations] are rarely surprised at each other's behaviour.' This predictability may be a consequence of rule following.

Ioannides (2003a, 2003b) suggested that rule following is an essential feature of coordination within the firm: 'We … introduce rules as an essential element for the running of business firms' (Ioannides, 2003b). This 'blurs the distinction between spontaneous order and organization as proposed by Hayek.' (Ioannides, 2003b) He argued that within the business firm rule following behaviour helps solve the Hayekian knowledge problem: 'rules in organizations promote the effective use of knowledge' (2003b). It also increases 'the quantity of knowledge available to the firm' (Ioannides, 2003a) including the utilisation of the unique knowledge of individuals within the firm, knowledge that might otherwise go to waste.

Further, as did Follett (1940), Ioannides argued because the firm functions in a dynamic environment ever stepping into the unknown, rules must be the most useful coordination mechanism: 'In this view, the promotion of the entrepreneur's business conception requires the information absorption capacity, the creativity and the problem solving capability of firm members. All these capabilities presuppose that the individual member acts within a framework of sufficiently abstract rules … In other words, the firm *cannot* but, at the same time, *must not* operate on the basis of commands. Therefore, we must think of the exercise of entrepreneurship as consisting primarily in the execution of a plan that unfolds in an uncertain future, thus making necessary the constant absorption of new knowledge by all team members, its interpretation, and the implementation of the necessary adjustments to the firm's operations.' (Ioannides, 2003a [emphasis in original])

But these more modern writers are not the only ones to argue that there is a role for rule following as a coordination mechanism within the firm. In fact, on re-examination, a number of earlier writers have focused on rule following and sought to privilege it above command as a coordination mechanism within the firm. Kline and Martin (1958) argued that: 'the chief characteristic of the command hierarchy, or any group in our society, is not knowledge but ignorance. Consider that one person can only know a fraction of what is going on around him… we may really be institutionalizing ignorance. While making better use of what the few know, we are making sure that that the great majority are prevented from exploring the dark areas around our knowledge.' They proposed instead that within firms rules 'provide a nonpersonal and objective method of supervision and coordination… They are *rules of reason*. The implication is that any rational person would come up with the same course of action as set forth in the rule. The administration of freedom requires the existence of a comprehensive system of rules in order to insure a maximum of "elbowroom" for each individual and at the same time a maximum of coordination and efficient action.' (Kline and Martin, 1958 – italics in original)

Simon, while wedded to command as a coordination mechanism, also argued the superiority of rule following in using the knowledge of individuals: 'If authority is used to transmit premises for making decisions rather than commands for specific behaviours, then many different experts can contribute their knowledge to a single decision. Information and policy rules can flow through the organization along many channels, serving as inputs – decision premises - for many organizational behaviors.' (Simon, 1991)

Jensen and Meckling (1995) come to the same conclusion by a somewhat interesting route. They start by citing Hayek (Hayek, 1948) and the 'distribution' (Jensen and Meckling's word and not Hayek's) of knowledge among market participants. They note Hayek's conclusion that this knowledge problem, including tacit knowledge, can only be solved by allowing the person on the spot to make decisions. But they seem unaware of Hayek's later writings, saying: 'Hayek assumes that markets automatically move decision rights to the agents with the relevant knowledge, and that those agents will use the decision rights properly. Unfortunately, he never discusses how this occurs.' They then analyse the problem themselves and come to the conclusion that '[b]ecause agency costs inevitably result from the delegation of decision rights, the CEO must devise a control system (a set of rules) that fosters desirable behaviour…' This rule following aspect is further articulated when they refer later to the 'common law' traditions in firms and say that 'our empirical observations indicate that knowledge of these "rules of the game" enables one to make good predictions about an organizations behaviour and effectiveness.'

The clearest articulation of rule following as a coordination mechanism within the firm was in the writings of Mary Parker Follett. In her collected papers, *Dynamic Administration* (1940), Ms Follett explored power and authority from a number of different angles. Her theory, as articulated through the essays, seems to be that there is, or should be, no authority or power in an organisation; that power and authority are merely a convenient explanation of a phenomenon that she considered not the following of commands or orders but obeying 'the law of the situation'. 'One person should not give orders to another person, but both should agree to take their orders from the situation. If orders are simply part of the situation, the question of someone giving and someone receiving does not come up. Both accept the orders given by the situation. Employers accept the orders given by the situation;

employees accept the orders given by the situation.' (Follett, 1940, 59) There is no authority, no 'orders', in a firm; instead there is a search for information, for 'facts' (105), 'to unite all concerned in a study of the situation, to discover the law of the situation and obey that…The head of the sales department does not give orders to the head of the production department, or vice versa. Each studies the market and the final decision is made as the market demands. This is, ideally, what should take place between foremen and rank and file, between any head and his subordinates.' (58, 59)

Follett is clear that if individuals in a firm are guided by rules then this causes a severe difficulty for command; if she was right this may result in at least one reason why management in a firm would, actively if - possibly - tacitly, avoid command as a co-ordination mechanism. Follett writes that 'people can obey an order only if previous habit-patterns are appealed to or new ones are created' (52). In other words, there is, at the very least, what Schlicht calls 'consistency in organization'. If a manager gives an arbitrary command, outside of the rules, then there is a danger that a subordinate may take this as a 'rule' and not a 'command' and apply the same 'rule' in similar situations; the arbitrary 'order' is taken as the fumbling articulation of a rule. 'If the workman is told to stay in department Y in the afternoon, he will interpret this as meaning that he is expected to stay in department Y in the near future, even if not explicitly ordered to do so.' (Schlicht, 2008) The end result of a 'command' could only be chaos as individuals, each following his or her own misunderstanding of the rules, are now unable to predict the behaviour of others; a prerequisite, we have argued, of coordinated behaviour within the division of knowledge within any firm.

Rule following and rigidity.

A reason why rule following behaviour may be relatively neglected as a coordination mechanism in intra-firm behaviour, as we saw in Chapter 1, may be because rule following may be, erroneously, associated with rigidity, with routines and with articulated standard operating procedures. Certain aspects of this rule system can also be called ‘routines’ or ‘habit’ or ‘custom’ (Schlicht, 1998, 87; Langlois, 1995). ‘[R]ules serve because they have become adopted to the solution of recurring problem situations…as a propensity to act in certain types of situations in a certain manner…’ (Hayek, 1976; 21) This ‘releases time and energy for more complex problems.’ (Loasby, 1998) Having said that, the rules also can guide us in completely new situations; perhaps by some sort of mental system of analogy with similar, more familiar, situations; as Schlicht points out ‘new routines are developed as variations of the old in order to cope with changing conditions, or to introduce improvements.’ (Schlicht, 2008; see also Klein, 1998)

The ability of rules to guide us in new situations is not widely appreciated. Almost everyone agrees that certain visible rules (the routines, the standard operating procedures, the defined processes) in an organisation can be a co-ordination mechanism but that following those rules implies rigidity (Langlois, 2007, 1119);

but this is incomplete - rule following behaviour is not just appropriate where there is ‘stability and repetitiveness of conditions.’ (Grandori, 2002). The ability of the rules to ‘govern’ (Hayek, 1967, 45) our behaviour in novel, or what appear to be novel situations, is clear. Some commentators assert that rules imply rigidity but then allow that societal norms guide behaviour in problem solving, which by definition involves the rules guiding behaviour in a novel situation (see Trompenaars and Hampden-Turner, 1997, 27 but then 31; Casson, 1995). Instead, rules-following helps us to solve completely new problems – even if, as Heiner (1983) points out, it is by selective attention to certain things or the closing off of available options (see also Nooteboom, 2006, where he argues the usefulness of ‘cognitive myopia’).

The fact that humans can make such rule-guided decisions in novel situations, apparently effortlessly, caused Cyert and March some difficulty in their *A Behavioural Theory of the Firm*. They deal with ‘task performance rules’ and argue that rules are only useful for routine tasks. They write: ‘... in most organizations pricing, output, inventory, and sales strategy decisions are made within heavily circumscribed rules. In most of the firms we have studied, price and output decisions were almost as routinized as production line decisions. Although the procedures changed over time and the rules were frequently contingent on external feedback, price and output were fixed by recourse to a number of simple operating rules. What was apparently a complex decision problem involving considerable uncertainty was reduced to a rather simple problem with a minimum of uncertainty.' (Cyert and March, 1963, 104ff). There is a problem with this explanation: in fact, *every* pricing decision is a step into the unknown in the discovery process that is competition in the market; it can never be a routine decision but is always a novel problem where the individual is guided to a solution by the rules. (Later March was more explicit about the importance of rule following in novel situations: 'The use of rules and standard operating procedures in routine situations is well-known, but their importance is not limited to routine worlds.' (March, 1997, 17)) The fact that an individual, as Klein (1998) demonstrated, familiar with the rules and often having solved similar problems, solves the problem in an instant blinded Cyert and March, initially, to the non-routine nature of the problem being solved. The fact that the individuals themselves also do not appreciate their feat was noted by Klein (1998).

As March pointed out (March, 1997, 17) a further mistake to be avoided is to see the 'rules' as only embodying the articulated rules of a procedure or a formal process. Most rules of behaviour are tacit and complement or even contradict the formal articulated rules. Eisenhardt and Sull (2001) make the point that rules are an appropriate coordination mechanism in 'rapidly changing, ambiguous markets' where strategies are 'constantly evolving.' While this article, *Strategy as Simple Rules*, does usefully point that complex strategies can flow from individuals following simple rules, the article does only focus on the top layer of clearly articulated rules. It would be a similar error to see the formal 'rules of the road' or road traffic legislation as the rules for driving a motor vehicle and not the tacit (and often quite local rules) that govern the behaviour of drivers. (See Fox, 2004 and Hayek, 1979, 159ff)

Command and hierarchy.

One obvious reason why most people do not question command as a coordination mechanism with the firm is because firms are, ubiquitously, hierarchical; a superior gives articulated 'commands', 'orders', to a subordinate. It has already been suggested that perhaps these articulated 'commands' may be rule articulation. However, hierarchy presents a further difficulty for any rule following perspective. As Alchian and Demsetz (1972) and Williamson (1994) have pointed out, hierarchy is not a, visible, feature of other orders created by rule following behaviour, such as the market. Hierarchy would seem to be entirely consistent with command and inconsistent with rule following. The argument is made that authority/command and hierarchy go together (see for example, Foss, 2002). Accordingly, given the Hayekian knowledge problem within firms, some have argued that the inevitable lesson from the rule following perspective is that hierarchy should be allowed to wither away within the firm; by definition, they say, the Hayekian knowledge problem in companies is inconsistent with hierarchy (see, for example, Pongracic, year unknown). Grandori writes that this problem of knowledge not being available to the person giving the command 'causes authority (as a centralized decision-making system) to fail in all its forms.' (Grandori, 2002) In other words, the knowledge using firm is a non-hierarchical firm.

However, this is not necessarily the case, the solution to the Hayekian knowledge problem, rule following behaviour, can be consistent with hierarchy. Given the number and complexity of the rules within a firm perhaps there may be a division of knowledge of the rules. The youngest trainee's entire knowledge of the rules within the firm may be of a series of routines that guide his or her daily actions. In turn he or she will be taught the rules by a supervisor who will both know, to some degree, these rules and the other rules of the firm that allow him or her to instruct others in the rules and to deal with unforeseen or non-routine events. In turn, the supervisor may be instructed in the rules by a manager who may not know many of the rules of the routine of the factory floor that other members of the firm know but may have a greater knowledge of the rules of the firm outside that particular location and of the rules in the larger market order. These rules of the larger market order may appear too abstract (Langlois, 1995) and, thus, unintelligible to the young trainee or even the supervisor. This division of knowledge of the rules may be one reason why hierarchy exists within the firm. (This point is also made by Langlois in the context of the M-form firm (Langlois, 1995)). This is borne out by experience; for example this writer works in the international tax planning department of a large accountancy firm; a more knowledge-based activity could not be found – but at the same time the department has a steep, multi-layered hierarchy.

It may be helpful, when looking at this 'hierarchy' of rule knowledge, to compare the common law judge (a central institution within a spontaneous order created by rule following behaviour) with the executive in the firm; both appear to be people who make decisions based on particular circumstances and issue, consequent, orders or decisions. In fact, like judges, managers are often concerned about 'precedent' and creating ‘expectations’ when they make a decision; ‘Every order and each decision creates a precedent… Within a firm every command creates the expectation that similar future situations will be handled in a similar manner…’ (Schlicht, 2008) Hayek (1973, 99) has shown how the common-law judge is, in fact, merely articulating a rule or an order of rules that was not apparent before a particular set of facts resulted in a dispute about which rule to follow. Both Chester Barnard (1938, 279) and Edith Penrose (1959, 16) have compared executives in a firm to judges:

> ‘There is no escape from the judicial process in the exercise of executive functions. Conflicts in the codes in organizations are inevitable… The judicial process, from the executive point of view, is one of morally justifying a change or definition or new particularizing of purpose so that the sense of conformation to moral codes is secured. One final effect is the elaboration and refinement of morals – of codes of conduct.’ (Barnard, 1938, 280)

But in every situation ‘authority’ and ‘hierarchy’ follows him or her that knows the rules: Follett turned hierarchy on its head, ‘The dispatch clerk can give “orders” even to the superintendent.’ (Follett, 1940, 277) It is never just a matter of giving a ‘command’. The fact that those in ‘command’ of an organization are often ‘disobeyed’ and thwarted is commonplace. As Barnard noted: ‘It is surprising how much that in theory is authoritative, in the best of organizations lacks authority – or, in plain language, how generally orders are disobeyed.’ (Barnard, 1938, 161, 162 see also Schein, 1992, 217, 226, 235) In Intel at a crisis point in its history between 1982 and 1985, Andy Grove (Grove, 1997; Burgelman and Grove, 2007) noted that employees were already, spontaneously, exiting from the memory chip business while senior management was committed to staying in the business; the eventual strategic decision to exit was facilitated by the activities of these more junior employees.

Finally, this understanding of hierarchy as a division of knowledge of the rules of the firm may allows us to add a layer of understanding to the findings of Carlson (1951), Mintzberg (1973) and Stewart (1967). They found that much of management time is taken up with subordinates having a problem about which they do not know what to do or are not sure and asking their superior for a solution. The problem is articulated and the solution is instantly given. Hence, typically, the large number of brief interactions of subordinates with superiors in a working day. Interestingly, when Tengblad (2002) reinvestigated Swedish CEOs in the 1990s as a comparison to Carlson's 1940s studies, he found that the CEOs suffered fewer interruptions but spent a lot more time travelling. On the one hand Tengblad found '[d]elegation and decentralisation … help explain why the CEOs in the new study work in a less fragmented way in terms of time.' On the other hand 'communication of norms, values and expectations, have become more important. The CEO who saw his main mission as "telling the history of the company" is a good example of this.' In either case, the role of the CEO is, directly or indirectly, about rule articulation.

Learning the rules and the problem for change:

If firms are orders created by rule following behaviour and every firm has a different set of rules then one of the most difficult tasks facing a new employee in joining a firm is learning those rules. In becoming an employee of the firm a person makes a commitment to learn and follow those rules. As Barnard points out how successful a person is depends on their own commitment and their abilities. Individuals may fail on both counts:

> 'Perhaps often and certainly occasionally men cannot be promoted or selected, or even must be relieved, because they cannot function, because they 'do not fit', where there is no question of formal competence.' (Barnard, 1938, 224)
>
> '[T]he requisite ability without … a high sense of responsibility leads to the hopeless confusion of inconsistent expediencies so often described as 'incompetence'.' (Barnard, 1938, 276)

The process of learning the rules can be difficult for even the most able executives. Andy Grove, the former CEO of Intel, describes one such situation:

> 'Some time ago we hired a very competent senior manager from outside Intel as part of the process of bringing computer experts into our management ranks. He seemed to land on his feet, seemed to enjoy the give-and-take characteristics of our environment and diligently tried to follow the workings of the company as he understood them. Yet he missed the essence of what really made it work. At one point he organized a committee and charged it to

> investigate an issue and come up with a recommendation. It turned out all along that this manager knew all along what he wanted to do, but instead of giving that direction to the committee, which he could have, he was hoping to engineer a bottom-up decision to the same effect. When the committee came up with the opposite recommendation, he felt cornered. At this late stage, he tried to dictate his solution to people who by now had spent months struggling with an issue and had firmed up their minds. It just couldn't be done. Coming at this late stage, his dictate seemed utterly arbitrary. The workings of our corporate culture rejected it, and the man had a very hard time understanding where he went wrong.' (Grove, 1997, 163)

This rule learning experience is tremendously difficult and leaves a person, for at least some years, if not always, in a position where they are part of a rule-based order they do not fully understand and where they are in the uncomfortable position of frequently breaking the rules. This is the burden of becoming an employee, and for most people one of its principal disutilities. 'The force of habit, the awe of traditional command… the desire to satisfy public opinion – all combine to make custom to be obeyed … In this the 'savages' do not differ from the members of any self-contained community with a limited horizon, whether this be an Eastern Europe ghetto, an Oxford college, or a Fundamentalist Middle West community… [I]n the main these rules are followed because their practical utility is recognized by reason and testified by experience. Again, other injunctions of how to behave in associating with your friends, relatives, superiors, equals and so on, are obeyed because any deviation makes a man feel and look, in the eyes of others, ridiculous, clumsy, socially uncouth.' (Malinowski, 1926, 52) The avoidance of embarrassment becomes both an internal motivator and a key signal of success in following the rules of the order (Warren and Smith-Crowe, 2008).

Any employee in a firm and especially a new employee must be willing bear the uncomfortable burden of joining an order where the person knows that they do not know the rules and can only learn them through bitter trial and error experiences. (This insight also clarifies a puzzle for many economists (Foss, 1999): why are visible incentives within firms often so simple, low-powered or fixed (even where measures of performance are available) as compared to the more complex, high-powered incentives that theory would require? In this argument, individuals will conform to the rules through an, invisible high-powered, *internal* incentive, as pointed out by Malinowski (see also Warren and Smith-Crowe, 2008).)

But this insight then causes a real problem for change in any organisation. Individuals within a firm will resist change because a change in the rules will affect their ability to predict the behaviour of others and appearing to not know the rules may cause them to appear ridiculous to their colleagues. Will others follow the same new rule or will they follow the old rule? Uncertainty about the rules reduces the amount of knowledge that can be used by that individual and that is available to the firm. It is this uncertainty and embarrassment avoidance, together or as individual preferences, that may be why, as we have seen, rule following is often associated with rigidity.

However, as we know, firms do change. But this process of change is complicated. Solving it is never just a matter of giving orders: One prominent CEO said: ‘Whenever I had an idea or a message I wanted to drive into the organization, I could never say it enough, I repeated it over and over and over, at every meeting and review, for years, until I could almost gag on the words.’ (Welch, 2001, 393) Nearly 80 years before another prominent CEO complained: ‘There are so many people involved and it requires such a tremendous effort to put something new into effect, that a new idea is likely to be considered insignificant in comparison with the effort that it takes to put it across.’ (Alfred Sloan in a speech to the General Motor’s sales committee 29 July 1925, quoted in Stewart, 1963, 165) The purpose of the next few chapters in this thesis is to examine in more detail the process of change in a rule-bound order.

Conclusion.

Rule following behaviour, it is submitted, offers a solution to the Hayekian knowledge problem within firms, in a way that is consistent with hierarchy and the giving of ‘orders’ and ‘commands’. However, the rule following perspective does result in a particular problem for change within firms. Each individual within the firm will have a natural incentive to avoid any change in the rules. A rule-change will impede the ability to predict the behaviour of others. Acting on the basis of new rules may appear inconsistent to others and may mark an individual as someone who does not actually know the rules. Change becomes a process of great complexity.

In much of management theory, managers can make any decision that is appropriate for the problem they are seeking to solve. However, if there is any merit in the rule following perspective, options that may be open to managers may in fact be closed off. Following the rules will guide decisions, but those rules may not be suitable for the problem in hand. Acting outside the rules, as has been pointed out above, may not be as open as might be thought. But changing the rules, to new rules suitable for the problem in hand, requires each individual involved to understand and commit to that change. It is never just a matter of a manager deciding on the change.

The case studies, described in Chapter 4, are designed as limited tests of rule following within the two firms examined. Like Horwitz (2008), the researcher thought that rule following would be especially visible during a period of change within a firm. Therefore, one of the central features of this thesis is to test the rule following perspective in situations where some form of change would be hard to avoid. The situations chosen were, firstly, where CRH makes an acquisition and the post-acquisition integration process there and, secondly, where Irish specific food brands were sold by global food companies to a new small Irish food company, Jacob Fruitfield. It seems clear, the times around acquisitions and disposals are almost inevitably associated with change in the firms involved. (Roberts, 2004, 252; Kotter, 1996, 18; Pautler 2003; Harrison, 2007)

Chapter 3.

Research method.

Keywords: Complex, simple, principles, change, managers, management.

Chapter Summary: It is difficult to find a consistent theme in the management literature; there are many inconsistencies and contradictions. This chapter argues that this apparent difficulty falls away once we understand that managers function in a complex environment where there are no hard and fast rules but only 'general principles'. This argument is then applied to the research methods for the current thesis. The method chosen is deliberately anecdotal, based on semi-structured interviews. Efforts are made to counter possible weaknesses in this approach.

‘[I]t would be more helpful if they [case study researchers] were more explicit about what their epistemological beliefs are and how these beliefs affect their understanding of appropriate quality criteria.’ (Langley and Royer, 2006)

Chapter 3: Research Method.

One of the most influential management writers of the late 20th century was the Austro-American writer, Peter Drucker. His books, starting with *The Concept of the Corporation* in 1946 were widely read (including Alfred Sloan who wrote one of the best books on being a manager, *My Years with General Motors* (1963), largely because he thought *The Concept of the Corporation* was ‘pernicious’: according to Drucker himself in his introduction to 1990 edition of Sloan’s book). Drucker’s *The Practice of Management* is ‘often hailed as the best introduction to management ever written’ (Magretta, 2002, 8).

If we focus on Drucker’s influence on Jack Welch we may see a problem with the management literature. In *Jack*, Welch, the former CEO of GE, wrote of an early central initiative as CEO:

> ‘The central idea came from earlier experiences with good and bad businesses and was supported by the thinking of Peter Drucker. I began reading Peter’s work in the late 1970s … If there was ever a genuine management sage, it is Peter. He always dropped a few unique pearls into his many management books. The clarity of [the policy of only being in a business where GE was

> ‘number 1 or number 2’] No. 1 or No. 2 came from a pair of tough business questions Drucker posed: “If you weren’t already in the business would you enter it today?” And if the answer is no, “What are you going to do about it?”’ (Welch, 2001, 108).

But while the No. 1 or No. 2 policy did, according to Welch, serve GE well, it was later dropped. ‘[O]our strategy of being No. 1 or No. 2 in the marketplace might be holding us back and stifling growth opportunities… For nearly 15 years, I had been hammering away at the need to be No. 1 or No. 2 in every market. Now this class [of GE executives] was telling me that one of my most fundamental ideas was holding us back. I told them, “I love your idea!” Frankly, I also loved the self-confidence they showed in shoving it in my face…. Perhaps our stress on No. 1 and No. 2 or “fix, sell, or close” now limits our thinking and hurts our growth mind-set.’ (Welch, 2001, 201, 202)

How could Welch praise Drucker’s advice on one page and then, less than 100 pages later, agree that the advice ‘limits our growth’ and starts to do the exact opposite?

The contradictions become even clearer when we look at some of the most commonly repeated views in the management literature. For example, in *In Search of Excellence* the authors told managers to ‘stick to the knitting’: ‘organizations that do branch out but stick very close to their knitting outperform the others.’ (Peters and Waterman, 1982, 293) Much of this section of their book is taken with pointing out the unfortunate consequences of 'diversify[ing] into a wide variety of fields.' (294) But then clarifies this by saying it is only a 'general rule.' (293) Indeed one company has thrived by *literally* not taking this advice; Toyota went from being a manufacturer of looms to making cars in the 1930s (Ohno, 1988, 88; Womack et al, 1990, 49). And even Peters and Waterman's main point about diversification or Drucker's comment that 'a business becomes unmanageable when it is spread out into so many [different] businesses' (Drucker, 1954, 234) is contradicted by Warren Buffett's Berkshire Hathaway (Lowenstein, 1996). Famously a large number of the companies extolled in *In Search of Excellence* subsequently ran into trouble.

What is the point of the management literature if any particular statement can be contradicted by any number of examples from real-life? To understand why the management literature is still useful we need to take a step back to more fundamental issues. When FW Taylor sought to put management on a 'scientific' foundation there can be little doubt that he had in mind emulating the tremendous prestige in the early 20th century of the physical sciences; particularly physics. He thought, according to his biographer, the laws of management once discovered would be as fixed as the laws of Newtonian physics. (Kanigal, 1997, 13, 278) Unfortunately, for managers things turned out to be more complex than that. Indeed when it comes to studying the organisations that managers run the main lesson we seem to have learnt is that, far from there being 'one best way', theory seems to show 'nearly anything can happen … a laundry list of a vast number of possibilities that rules out little.' (Fisher, 1991) And it is this complexity that lies at the heart of a problem with the management literature. Managers are functioning in a complex environment: there are no simple cause and effect rules at play.

In his essay, *Degrees of Explanation* (1967, 3), Hayek made the distinction between relatively simple and complex sciences (Caldwell, 2004, 301; see also Hayek, 1973, 16). In the 'simple' sciences, rules and laws allow the scientist to make predictions. In the complex sciences this is not possible; the best that can be hoped for is an 'explanation of principle' or an 'orientation' (or a 'general principle' – meaning one that is subject to exceptions rather than one that is to be applied generally). The reason why this is the case is important for managers:

> 'Where we have to deal with a complex situation in which observation discloses only very limited regularities, be it in the "applied" branches of physics or in biology or in the social sciences, we usually ask to what extent our existing knowledge of the forces at work, or of the properties of some of the elements of the complex, may account for what we observe. We endeavour to find out whether this may be derived by deduction from what we know about the behaviour under simpler conditions of some of the factors involved. Or course we can never be certain that what we know about the action of those forces under simpler conditions will apply in more complex situations, and we will have no direct way of testing this assumption, since our difficulty is precisely that we are unable to ascertain by observation the presence and specific arrangement of the multiplicity of factors which form the

> starting point of our deductive reasoning… But though our observation of such complex situations cannot decide whether our condition ("if then") statement is true, it will help us to decide whether to accept it as an explanation of the facts which we observe.' (Hayek, 1967, 10)

The same applies to managers: they also function in a complex human environment. And so, for example, the increased productivity of the division of labour is as clear to all managers as it was to Adam Smith when he described in such loving detail the making of a pin in a pin factory (Smith, 1776, 109). But at the same time no manager is surprised that Michael Hammer can give an example in Aetna Life and Casualty of a situation where the division of a task between too many people resulted in a task that took only 26 minutes of actual work taking 28 days to complete and where the solution was to combine tasks formerly performed by different individuals so that they were performed by a single customer account manager. (Hammer, 1996, 28) The principle of the division of labour only results in an 'orientation', a 'general principle' subject to exceptions in any particular factual situation which means that in every situation a manager merely uses the principle as an 'aid to judgment'.

In his apparently iconoclastic book, *The Halo Effect* (2007), Phil Rosenzweig tried to show that the management literature is full of 'delusions' that 'distort our understanding of company performance, that make it difficult to know why one company succeeds and another fails. These errors of thinking pervade much of what we read about business, whether in leading magazines or scholarly journals or management bestsellers.' (Rosensweig, 2007, xv) These delusions included the halo effect, confusing correlation and causation, 'connecting the winning dots' and so on. Rosenzweig could show plenty of these examples in the management literature but then made an unwarranted assumption – he assumed that managers actually also suffered from these delusions. In fact any manager that reads more than one management book, and often only one, has to absorb, sift and discern between contradictory advice and lessons.

In fact it is Rosenzweig, along with many management writers, who, from a Hayekian point of view, are possibly inappropriately using the putative methods of the 'simple sciences'. For example, Rosenzweig criticises Tom Peters (one of the authors of *In Search of Excellence*) who 'admitted' (Rosensweig, 2007, 87) in 2001 that 'we faked the data' in that they did their 'quantitative data analysis … after they reached their findings.' Peters is quoted as saying: 'Because McKinsey is McKinsey, we felt we had to come up with some quantitative measure of performance.' He also criticises Jim Collins's *Good to Great* for being mere stories designed merely to 'inspire and comfort' as opposed to 'good social research' with its 'adherence to rigorous standards of scholarship.' (Rosensweig, 2007, 134, 135) However, there is a different view:

- No scientist, no matter how simple the science, does other than what Peters did (see for example: Popper, 1963 and 1972; Polanyi, 1958, 123; Hayek, 1978, 23 ff) even if some also search for facts that would falsify their theories (see for example: Popper, 1972, 81, 186, 259) – it is over 60 years since Popper showed that 'scientists did not really do what most of them not only told us they did but also urged the representatives of other disciplines to imitate.' (Hayek, 1967, viii)

- In addition, in a complex realm like management, storytelling may often be the *only* appropriate tool and one that all participants in complex realms *naturally* use (see Klein, 1998, 177 to 213; Popper, 1972, 185 ff) 'our understandings of complex systems and their properties will always be grounded on the narratives we construct about them.' (Tsoukas and Hatch, 2001); certainly any manager would struggle to find anything useful in the conclusion that 'specific management practices were indeed associated with differences in performance and explained about 10 percent of the total variance in firm performance…' (Rosenzweig, 2007, 134). It is for this reason that a 'renowned CEO doubtless speaks for many when he labels academic publishing a "vast wasteland" from the point of view of business practitioners.' (Bennis and O'Toole, 2005) In other words, applying the methods of the simple sciences to a complex activity like management may not only be inappropriate, but also, perhaps unsurprisingly, may not often yield useful insights for practitioners.

One of the exceptions to this limited usefulness but an example of the frustrations inherent in trying to emulate the inappropriate methods of the 'simple sciences' is one of the pioneering studies of managers – *Executive Behaviour* by Sune Carlson.

Carlson (Carlson, 1951) investigated the activities of a number of Swedish managing directors between 1947 and 1949. Carlson studied what the CEOs were doing 'hour by hour, where they were located, who they met, what they were reading and how all this together influences their way of leading the company.' (Carlson quoted in Tengblad, 2003). But Carlson was dissatisfied with his achievement. Tengblad explained that one of the reasons Carlson abandoned his efforts was epistemological: 'It was for him [Carlson] problematic that the study had to rely partly on the CEO's opinion of his own behaviour, and that he was not able to develop new administrative concepts which corresponded to clearly defined sets of operations … If Carlson had adopted a "weaker" epistemology he would have been able to see his study in a more positive light. It may still represent the most extensive and best empirically grounded study of top managers at work ever made, and it was a major loss that Carlson did not subsequently publish more material about the study.' (Tengblad, 2003)

Implications for the Case Study method in this thesis:

The conclusions from the above can be summarised as follows:

- It may be inappropriate to apply the methods of the simple sciences to more complex areas.
- Management is a complex activity functioning in a complex environment.
- Theory is an essential guide to interpreting management decisions but theory

can only be a general guide; a statement of general principle.

- But examples from real life can tell us what is possible, what is difficult in practice and can help us falsify a theory; as an 'explanation', 'to show the application of an idea' or to 'prove the possibility of an idea'.
- In a complex realm like management, storytelling is an appropriate tool for understanding an organisation. As Leavy (1994) has pointed out 'some of the most influential research in the business studies area … has been … case based…'

Therefore, in this thesis, the research proceeded by way of face-to-face interviews with a number of current or former executives in the firms studied. The interviews were semi-structured, 'loosely structured, seeking to evoke stories' (Yiannis and Griffiths, 2004, 118); the fixed questions asked are set out in tables 3.3 and 3.4, below. This approach was deliberately anecdotal. This interview, anecdotal, approach, as we have seen, may appear 'soft' but '[s]tories of success and failure are also specifically important sources of empirical information for organizational scholars…' (Vaara, 2002) As Mintzberg has pointed out: 'Theory building seems to require rich description, the richness that comes from anecdote. We uncover all kinds of relationships in our hard data, but it is only through the use of this soft data that we are able to explain them.' (Mintzberg, 1979)

Having said all this, the limitations of the narrative approach and the semi-structured interview are numerous. The most important limitation, and particularly relevant here, is unintended bias on the part of the researcher. Bell argues that interviews are 'a highly subjective technique' (Bell, 2005, 157) where bias is going to be one of the major problems. This is especially true where the interviews are to result in a narrative description of events. In constructing any story to make sense of events individuals, including researchers, will not only overweight facts that confirm their hypothesis but, as is well-known at this stage, can ignore or dismiss disconfirming facts (Bell, 2005, 166, Klein, 1998, 273, see also Popper, 1962, 1972 and, especially, 1959, 248 ff) This problem has to be guarded against. In this thesis, this was partly done by interviewing more than one participant in each company and, to mitigate bias on the part of the researcher, by sending drafts of the relevant chapters to participants in the studies; their feedback was reflected, it is hoped accurately, in the final version. This checking back process was designed to 'force investigators to go beyond initial impressions' (Eisenhardt, 1989) and to reflect on the feedback the researcher received to his initial impression on the cases.

In addition to Carlson (above), Klein (1998) has also pointed out the further problems with investigating this type of rule following: researchers in this area, noted Klein, 'rely on introspection….We ask people to describe what they are thinking, and we analyze their responses. We do not know if the things they are telling us are true, or maybe just some ideas they are making up.' (Klein, 1998, 290) Klein (and Carlson) underestimated the problems here; there is also the problem of the individual being unable to articulate (Polanyi, 1958, 1966) why he or she did certain things and not others, even if they are consciously aware that they applied some mental process. The problem with this thesis is that in looking at rule following behaviour it is enquiring into decisions made by individuals based on following rules that are, at best, tacit and, at worst (for the purposes of the thesis), unconsciously being followed by the individual. (See also Ioannides, 2003a, 167, where he notes that it is 'much more difficult to discern empirically' the role of rule following within the firm.) Further, the interviews were also held retrospectively. This raises the problem of 'retrospective reconstruction' (Vaara, 2001); interviewees were telling the researcher later why they did things at the time.

Two preliminary propositions.

Therefore, some thought was put into what questions could be asked of individuals in the studies where the answers should be easier to articulate but would, to some degree, deal with the subject matter of this thesis. Three preliminary questions were settled on, which turned around the articulation problem – imposing the articulation problem on the question rather than the answer. In other words, asking the participants if they and their subordinates followed complex, tacit rules of behaviour that guided their actions within the firm was unlikely to be a question that could readily be comprehended but asking questions on the effects of rule following might be somewhat more fruitful. Each participant was asked:

1. 'What is the purpose or goal of your company?'

2. ‘If you told someone to do something once would you expect them in similar situations to do the same thing again, even if they were not told?’

3. ‘Is the distinction between a rule and a command made in your organisation?’ (If the individual was unsure what the question being asked meant an explanation was given: ‘A command is ‘Do A’; a rule is ‘In situation A do B. A command is once off but a rule applies in similar instances in the future.’)

These questions gave rise to two preliminary propositions that were explored before the main issue was discussed. Basically, the purpose of these three questions was to test whether rule following could be an important coordination mechanism within the firms being examined before proceeding to the examination of the main issue. It was felt important to try to test these preliminary propositions before proceeding.

First preliminary proposition: Individuals would not be able to articulate a concrete goal for their firm but instead a somewhat fuzzy goal would be articulated.

Hayek argued that command was possible in organisations; this was so because an organisation had ‘concrete’ goals. This argument, at least in relation to the business firm, was tested by the first question. If the answer is vague and not concrete that could create a problem for command as a coordination mechanism. In particular a goal or a purpose expressed in terms of profit, sales, turnover or growth must, by definition, mean that the goal is not concrete as all of these terms measure performance in the dynamic discovery process that is market competition and, accordingly, cannot be fixed but must be constantly evolving.

Second Preliminary Proposition: That when a superior gives an instruction to a subordinate, this is the articulation not of a command but of a rule, where the subordinate and superior would expect that the subordinate would do similar things in similar circumstances in the future even if not specifically told.

In conventional theories of the firm, behaviour is coordinated by command and rule following behaviour, as we have seen. If that is the case, individuals should be clear which was which; this would seem like a crucial distinction - as rules will apply in future instances and commands will not. This is especially so because rule following behaviour, it is submitted, does not just apply to routine procedures and the rules are not all written down in a standard operating procedure; there is no clear realm where rules apply and another different realm where command applies. If individuals confirmed that when they asked someone to do something and they expected that individual to do similar things in similar circumstances in the future then it should be clear at this stage that that is a rule and not a command. The second and third questions, above, *together*, if the former is answered in the positive and the latter in the negative, would present support for the proposition that command is over-privileged as a coordination mechanism and would support the view that rule following, within the firm examined, may be pervasive.

Before the main case studies commenced, these questions were piloted in an exercise involving a law firm. It was thought that if lawyers, being well-educated and generally articulate, struggled with these questions that they might be unworkable. In fact the pilot was quite successful. The results of that pilot were published (in Brady and Walsh, 2008).

Getting the participants to tell stories.

Next, the case studies proceeded to elucidate stories. These stories would then lead to the main point of exploration of this thesis**.** The case studies would become a small and limited testing ground to explore, in the stories, whether, for example, what might appear to be open options were in fact closed off to managers and change was a more complex process than the conventional wisdom might allow. As was explained in the Introduction, if rule following was an important coordination mechanism within the firm, the researcher thought through when such a mechanism might be more clearly visible. Like Horwitz (2008), the researcher thought that rule following would present a particular problem with any change process within a firm. Therefore, the thesis focused on stories where some form of change would be hard to avoid. The situations chosen were where CRH makes an acquisition and the post-acquisition integration process there and where Irish specific food brands were sold by global food companies to a new small Irish food company, Jacob Fruitfield. It seems clear, the times around acquisitions and disposals are almost inevitably associated with change in the firms involved. (Roberts, 2004, 252; Kotter, 1996; Pautler 2003; Harrison, 2007)

Further factors.

The main limiting resource in the case studies was time; the researcher is a partner with a Big 4 accountancy firm and this thesis was undertaken on a part-time basis. The time available to undertake an interview based case study was limited; therefore, some thought was put into maximizing the return from the interviews actually undertaken by substantial preparation work and a focused conversation. On the one hand the researcher's position facilitated access to the higher levels of the firms involved, with access to somewhat sensitive information and an awareness that time was precious on both sides. There was also a focus on the 'rules of work'; the case study was not expanded to explore wider cultural or emotional aspects for the interviewer and interviewees (see for example, Down et al, 2006). On the other hand, the number of interviews was small.

It is submitted that the fact that all the interviewees were Irish and working in Irish owned firms was not a limiting factor in relation to the propositions above. All of the employees had functioned in a multi-national environment. There was no indication that the situations they found themselves in would be different in a non-Irish firm or in non-Irish subsidiaries in the groups in which they worked. In any event, extrapolating from a single cultural perspective to others is not illegitimate. (Evers and Wu, 2006; Langley and Royer, 2006) As Vaara argues: 'by examining of a carefully selected case from a theoretically grounded perspective … can then lead to analytical generalizations, that is to say, to findings which upon due reflection can be generalized beyond the particular case. In this light, the selection of a particularly revealing case makes sense.' (Vaara, 2001) Further, using examples from other organisations (for example, Ford and Berkshire Hathaway) has been a feature of this thesis; although the research is relatively shallow for these other organisations, these examples are also case studies and provide for useful comparisons. (Langley and Royer, 2006)

Access to the two groups studied was through direct and indirect relationships of the researcher. In relation to CRH, access was through his father, an ex-CRH executive, and through a mutual business contact to Jacob Fruitfield. In addition, the pilot study firm was accessed through a direct business contact of the researcher. On the one hand this relationship and personal basis for access might be considered a limiting factor and leave the researcher in a difficult situation if the case studies had thrown up stories critical of individuals. However, within Irish business culture, business tends to be more relational than transactional and so access based on relationships was not considered inappropriate. Given the researcher's limited academic credentials and senior position within a global firm, access on a basis other than relational was considered less likely to be successful, likely to take more time, and likely to result in more limited access.

The interviews proceeded on the basis that the interviewees would not be identified (except for Michael Carey, the chairman and former CEO of Jacob Fruitfield). This is a common agreement with interviewees and their employers. (Bell, 2005, 51). However, it was agreed that the firms involved would be identified; all of the participants were aware that this meant that, in the event that any of the interviews entered the public arena, their identities could be discovered by those knowledgeable about the firms involved; while the cultures seemed open it cannot be ruled out that this knowledge may have had a bearing on some issues discussed.

A semi-structured interview process was designed. The key questions are set out in tables 3.3 (CRH) and 3.4 (Jacob Fruitfield), below. The questions asked were designed to be a mix of open-ended and closed-ended questions. Each participant was asked all the key questions but in each case a fluid dialogue ensued and other issues were discussed and other questions asked; the interviewees are all well-educated and articulate. Each interview was expected to take a half hour; in fact all lasted between one and two hours. The interviews were not recorded but a note was taken of the interview by the interviewer. (The researcher is an experienced professional and it was thought that note-taking would not interfere with the interview process to a material degree.) This note was then typed up within a day of the interview process. A draft of the case study was then circulated back to participants for comment, clarification and correction. Two participants replied in writing and there were subsequent follow-up interviews.

Specific Research Method points in relation to the Individual Case Studies:

The CRH Case Study. Interview Design:

CRH was chosen for the case study of post acquisition integration activity as it is now a by-word for successful acquisitive behavior. The acquisition focused on was John A Wood Limited because it was one of the first acquisitions by the group and the integration model followed for that firm has become, in some ways, the CRH model since. An initial informal approach was made through the researcher's father who was a retired executive in John A Wood (and was one of the interviewees below, although not quoted).

The case was designed to be a study of CRH's post-acquisition integration process focusing on John A Woods for the 40 years after it was first acquired by CRH (or Roadstone, as it was at the time). Five executives were interviewed; their careers in CRH are summarised at Table 3.1; all of the interviews took place in 2007. All, except one, of the interviewees were long-term employees of John A Wood over that period and all retired as senior executives; two of the interviewees went on to senior management positions in CRH. Two of the interviewees were university graduates and they started out in the company as engineers. Two started out as junior 'office clerks'. The fifth was an engineer and started out with Roadstone in Dublin as a business 'development manager'. Overall the five interviewees averaged over 35 years experience each with the group. All are now retired. They were chosen as they could give a longer term perspective on the post-acquisition strategies of CRH and, at the same time, not disclose confidential information about CRH's current activities.

Interviewee A	Interviewee B	Interviewee C	Interviewee D	Interviewee E
Joined John A Wood 1965. Retired 2003.	Joined John A Wood in 1961. Retired 2001 as company secretary	Joined in 1966. Retired 2004.	Joined John A Wood early 1960s. Retired as a senior executive in CRH plc.	Joined Roadstone in the early 1960s as a development manager. Retired as senior executive in CRH.
Started as a junior office clerk. Retired as head of concrete division in JAW.	Started as a junior office clerk. Retired as company secretary.	Joined as an engineer. Worked for a period with Roadstone in Dublin. Retired as a director; head of pipeworks and quarries.	Joined JAW as an engineer. Initially was head of pipeworks. Also worked on earth moving project. Later md of John A Wood and then moved to Roadstone in Dublin. Pioneered group's international acquisition program.	Pioneered the group's acquisition program in the US. Headed up the US operations and then returned to Ireland to fill a senior role.

Table 3. 1

A large volume of background information on the group was gathered from the media, annual reports and so on. Unexpectedly, despite its success, there is very little published academic research on CRH plc (other than a teaching case, referred to in the next chapter).

The interviews took place in a variety of locations. Three participants were interviewed in their homes and two in a coffee shop near their homes. Unless otherwise cited, all of the quotes below are from this interview process (with the letter at table 3.1 identifying the person quoted). There were two repeat interviews and two of the executives followed up with a correspondence and annotations to a draft of this piece.

The Jacob Fruitfield Case Study. Interview Design:

Jacob Fruitfield was chosen because it owns a number of exceptionally well-known food brands in Ireland and the reason why two global food companies would wish to dispose of these brands to a small Irish management group was not immediately obvious. An initial informal approach was made through a mutual business acquaintance of the researcher and Michael Carey, the current chairman and former managing director of the group. The case was designed to be a study of Jacobs for the seven years after the initial acquisition of Fruitfield Foods from Danone. All of the interviewees were long-term employees over that period. Their experience and positions is summarised in Table 3.2; all of the interviews took place in 2008.

Michael Carey	Interviewee B	Interviewee C
BComm and MBS from UCD. Moved into marketing jobs – food and drinks. Worked for the UK company Northern Foods, in Dublin and then in the UK. Came back to Dublin and worked for C&C as marketing director. Then worked with Jacob Biscuits (which was a recent purchase by Danone). Danone were upgrading the marketing function and he was brought in as part of that process. Danone asked him to move to the UK – to be the md for Evian and Volvic in the UK and Ireland. This was his first general management role. Then back to Northern Foods to be the m.d. of Fox's biscuits. Took the position of m.d. of Kelloggs for UK and Ireland. This was November 2001.	Joined Nestlé as sales rep/sales manager in 1989/1990. In 1997, he was 26/27, doing MBA. Asked to go on a 'special project' in Nestlé which he could use for his MBA: was told 'You will fall out with all of your colleagues in Ireland as you will end up closing the manufacturing in Ireland.' Worked on an 'as is' and 'to be' project. The culmination of this project was the sale of the business to Cleary. Left Nestlé. Rejoined Fruitfield after it was acquired by Carey.	Trained with a small firm in Dublin and then moved to Trebor in 1986. They were bought by Cadbury. He then moved to Rowntree Mackintosh which was in 1998 acquired by Nestlé. Worked in the finance department and then IT in Nestlé. Stayed on, for a trial period, after Management Buy In by Carey. Moved back into the finance dept.
Left Kelloggs and returned to Ireland and established a small company. Nestlé were selling Fruitfield and Carey decided to bid for it with private equity backing. Since that acquisition, 2002, he has been managing director/chairman of Fruitfield and later of Jacob Fruitfield.	Now head of sales and member of board.	Now head of finance and on the board.

Table 3. 2

All of the executives were carefully chosen, 'central actors' (Vaara, 2002), as each could give a before, during and after perspective; only a small number of executives in the company could give this. The case study approach proceeded with semi-structured interviews with the three employees of the firm. Some background information on the group was gathered from media sources. The company is private so only limited financial information is available; some financial information about the group was given at the interviews but for commercial confidentiality reasons is not repeated below. The researcher was not aware of any previous academic research on the group.

The interviews took place in a variety of locations. Two participants were interviewed in hotels and one in his office. Unless otherwise cited, all of the quotes used are from this interview process (with the letter at table 3.2 identifying the person quoted).

Conclusions:

Gary Klein in investigating the decision-making processes of fire-fighters, medical personnel and soldiers in naturalistic settings was confronted with a problem. He wrote: 'one weakness in our work is that the studies relied on interviews rather than formal experiments… This book has presented many arguments. But arguments can be refuted.' (Klein, 1998, 291) Despite these weaknesses, Klein felt that what he was doing was 'science' (290).

The purpose of this section of the thesis has been to argue that, despite the limitations in the research methods used, these methods are appropriate and can lead to useful results. A number of precise questions are asked to try to test two preliminary propositions; these questions may provide some support that rule following is a tacit coordination mechanism within the case study firms. The case studies then, under this rule following lens, proceed to tell, firstly, the story of CRH's acquisition strategy and the post-merger integration of a firm in Cork, John A Wood Limited, and then, secondly, the story of the disposal of a number of Irish food brands by two multinational groups and their acquisition by a relatively small Irish owned and managed food company. Integration and divestment are typically times of change in business firms (see Kotter, 1996, 18) and change presents a particular problem for coordination by rule following (Horwitz, 2008). Therefore, it is hoped that the stories from CRH and Jacob Fruitfield will make more visible some consequences of rule following, if it is a coordination mechanism in those firms.

Table 3.3: CRH questions:

1. Can you describe your career, within CRH/JAW and in other employments?

2. When did you join the group and at what level?

3. What was your position when you retired?

4. Was there ever a situation when someone in CRH but not employed in JAW told you to perform your tasks in a different way?

5. Was there ever a situation where you performed tasks differently because of what you saw or heard about elsewhere in the CRH group?

6. Did you feel that even at the end of your career there were material differences between the way things were done in JAW and CRH?

7. You have been asked to do something once by a more experienced colleague. If you were faced with similar circumstances again would you do the same thing even if not asked?

   If so, would you do this always, usually, or sometimes?

8. If you told a subordinate to do something once, would you expect them, in similar circumstances to do the same thing even if not told?

9. Has anyone in CRH (or in a previous employment) ever made the distinction between a 'command' ('do task X') and a 'rule' ('in circumstance Y do task X')?

   Is this a familiar distinction to you?

10. Have you puzzled or reflected, outside of office hours, about the professional behaviours/actions of others in CRH/JAW?

    If so, could you give an example?

11. What is the purpose or goal of CRH/JAW?

Table 3.4 Jacob Fruitfield questions:

1. Can you describe your career, within Jacob and in other employments?

2. When did you join the group and at what level? What is your current level?

3. Why do you think Nestlé and Danone sold their local Irish brands?

4. Can you give me examples of actions/inactions under Nestlé and Danone that you felt were not suitable for the local Irish brands.

5. Can you give examples of things that you do now that you think would not have been possible or very difficult under Nestlé and Danone.

6. You have been asked to do something once by a more experienced colleague. If you were faced with similar circumstances again would you do the same thing even if not asked?

   If so, would you do this always, usually, or sometimes?

7. If you told a subordinate to do something once, would you expect them, in similar circumstances to do the same thing even if not told?

8. Has anyone in Jacob (or in a previous employment) ever made the distinction between a 'command' ('do task X') and a 'rule' ('in circumstance Y do task X')?

   Is this a familiar distinction to you?

9. Have you puzzled or reflected, outside of office hours, about the professional behaviours/actions of others in Jacob?

   If so, could you give an example?

10. What is the purpose or goal of Jacob?

Chapter 4.

Post-Acquisition Integration Behaviour in CRH and Post-acquisition Decisions in Jacob Fruitfield.

Key words: Acquisition, disposal, integration, order, rule following, change.

Chapter Summary: The purpose of this chapter is to describe the CRH and Jacob Fruitfield cases. The post-acquisition integration strategy in CRH is described in general and more specifically based on a study of an acquisition made in the 1960s. The disposal of Irish brands by Danone and Nestlé and their acquisition by Jacob Fruitfield are described in the second case study. This second case study focuses on decisions made by management before and after those acquisitions by Jacob Fruitfield.

Hamlet: *"…Will you play upon this pipe?"*
Guildenstern: *"My lord I cannot … I know no touch of it…"*
Hamlet: *"Why look you now how unworthy a thing you make of me! You would play upon me, you would seem to know my stops you would pluck out the heart of my mystery. You would sound me from my lowest note to the top of my compass, and there is much music, excellent voice, in this little organ - yet cannot you make it speak. Sblood, do you think I am easier to be played on than a pipe? Call me what instrument you will, though you can fret me, yet you cannot play upon me."* Hamlet, Act III Scene 2

Chapter 4: Case Studies.

The first part of this chapter tells the story of CRH and its post-acquisition integration strategy and then moves on to the integration of an acquisition in Cork from the 1960s. The second part of this chapter tells the story of a number of Irish food related businesses before and after the divestment of these Irish businesses from larger multinational companies to a relatively small Irish-owned and managed food company.

The CRH post-acquisition integration process.

The purpose of this section of the thesis is to describe the post-acquisition integration process in CRH plc. CRH is generally regarded as having a successful acquisition strategy and considerable 'proven' (NCB, 2007) success with its acquisitions; 'most analysts and investors sing CRH's praises' (Hohler, 2003).

CRH plc background:

Cement Roadstone Holdings plc (now CRH plc) was founded in 1970 with the merger of two of Ireland's leading quoted companies, Cement Limited (established in 1936) and Roadstone Limited (1949). At that time the group had sales of c€26m, 95% of this in Ireland. (CRH website, 2007). By 2007 annual sales amounted to €21bn with profit, before tax, of more than €1.9bn and it had operations all over Europe and North America. The compound annual growth, in sales, between 1970 and 2006 is 'an impressive 19.4%.' (McGrath, 2007); in 2007 earnings per share had grown every year for 15 years.

A large part of this growth is driven by a long-standing policy of focused (and never hostile) acquisitions. This articulated policy dates back to the 1970s; two key pillars of the strategy from the start were sticking to core businesses in building materials and negotiating deals that meet sellers' and CRH's needs. (CRH, 2007) In many cases the previous 'owner-entrepreneurs and their teams' are retained in management positions. (Liam O'Mahony, the current CEO quoted in Business 2000 Case Studies: CRH.)

The number of acquisitions is enormous, and details of the number of more recent acquisitions is summarised in Table 4.1.

Year	Number of Acquisitions	Spend on acquisitions
2000	More than 60	€1.6bn
2001	More than 50	€1.08bn
2002	45	€1bn
2003	43	€1.6bn
2004	About 40	€922m
2005	64	€1.45bn
2006	69	€2.1bn
2007	78	€2.2bn

Table 4. 1

Source: CRH Annual Reports 2000, 2001, 2002, 2003, 2004, 2005, 2006, 2007.

The size-mix of acquisitions is great too. In 2006 one single acquisition was for €1bn, in 2003 one acquisition was for nearly €700m. Many other acquisitions are for small amounts and can include the acquisitions of individual plants, aggregate pits etc. It is true to say that since the larger merger of Roadstone and Cement in 1970 most acquisitions have been of operations that are, relative to CRH, small; there is a ‘preference for acquiring small and mid-sized, privately-owned, and usually family run and profitable businesses…’ (CRH company profile published at Answers.com)

When CRH first considered acquisitions in the US in the 1970s they engaged one of the foremost US management consultancy firms; who said ‘what can you bring? You have no advantages in experience, technical ability or finance – perhaps the reverse.’ (Interview by the researcher with interviewee D – see Table 3.1 for details of all the interviewees in CRH) The consultants were also quoted as saying: ‘We would love to support you but you have no transferable skills…’ (Interviewee E) When the researcher asked the senior executives why after the consultant’s report they still went abroad, one executive replied: ‘We didn’t believe them – they didn’t understand the business… What the CRH group had to bring was an experience of how such businesses should be run, demonstrated by the acquiring terms, and certainly influenced by the success of the John A Wood acquisition and the lessons jointly learned therefrom.’ (D) ‘They said we had no transferable skills. We had, but it was not obvious to the consulting firm – we had an understanding of how family firms operate. There was an affinity with the owners.’ (E) The conventional view of CRH is that they went abroad to diversify the business and not to be so exposed to the limited Irish economy. But there were also more tacit motives at play: ‘The management was young – in their late 30s – there was a great appetite. We had hammered the business [in Ireland] into shape, we could see that other markets were not as competitive as Ireland. There was surplus energy, surplus brainpower. We could recruit better people in Ireland [given the state of the Irish economy] – we had a cadre.’ (D) ‘We had confidence.’ (E)

The acquisition process is somewhat unusual. CRH does not generally use merchant banks to identify targets but has 19 acquisition teams roaming the globe not so much looking for immediate acquisitions but building relationships; ‘CRH took a patient approach to purchases, often spending years wooing owners of business it wished to acquire.’ (Answers.com) ‘It is important to emphasise that these [acquisition] teams are part of the regional/product based management system and have to deliver on the deals and manage the existing organisation as well.’ (Letter to the researcher from Interviewee D, 16 November 2007) CRH would wait for considerable lengths of time saying to the owner-entrepreneurs, ‘when the day comes and you want to sell we will be here.’ (D) Some of these relationships can take many years to bear fruit – even after 30 years the sons of owners first approached by CRH are still being courted. (E) The number of acquisition teams and the number of relationships is important to the acquisition strategy. Interviewee E said: ‘*Buying is like selling.* You have to have a pipeline, a multiplicity of transactions. Otherwise you get caught up in one deal and pay too much… The selling opportunity is outside your control. A divorce, a row with a son… You have to have the relationship and be there at that time.’

CRH’s post-acquisition integration process is clearly set out on its website:
‘CRH is divided into six regionally focused business segments, three in the Americas and three in Europe, supported by a lean Group centre. Within these segments:

- experienced operational management are given a high degree of individual responsibility

- local autonomy, within Group guidelines and controls, helps accommodate national and cultural needs and capitalizes on local market knowledge
- the Group's size and structure is leverage to drive margin improvement and earnings growth
- product-based best practice teams promote performance improvement through sharing of experience, technologies and ideas' (CRH website, 2007)

This 'high degree of individual responsibility and operational autonomy … is central to the culture of CRH.' (CRH, 2007).

When making an acquisition, it is clear that CRH is not just buying a physical location or plant but is also looking for something else. One former senior executive said that they would not buy companies that they considered 'dead losses'; that is CRH 'would not buy companies involving a lengthy, major and costly turnaround.' (Letter to researcher from D, 16 November 2007) In the 1970s and 1980s, this executive used to sit in his car outside potential acquisitions - plants, truckworks and builders providers; he would wander through builders providers and buy small amounts of product. What he was looking for was obviously largely tacit – 'the amount of traffic going in and out… the packaging… dust and dirt or the absence of it…' as well as what the CRH 'people on the ground' knew of the business. One example of the quite subtle nature of their approach was in the early 1990s: 'we went to Russia but did not like the look of it…' But later they did enter the Russian market but through their operations in Finland; they felt the Finns knew this market better.

There are two things that CRH do insist on immediately on acquisition; these two have not changed significantly since the 1970s. The first is that the acquired company has to install or have the ability to provide 'clear physical reporting' 'which tell the facts' to head office; usually that meant installing the CRH reporting and accounting system but not always – 'if the local system was as good as ours we would take that… we learned from their systems.' (D) The second was a certain ethical standard, 'honesty and disclosure… warranties and indemnities matter … we did call in indemnities (in a small number of cases)…' (D) For another executive: 'The relationship is the due diligence'. (E) 'The integration process in CRH could be considered over when the financial and reporting systems were fully integrated into CRH's systems and entity was slotted into the reporting hierarchy in people terms – probably not more than two years max.' (D) This integration, generally, did not cause any problems: 'The game plan was known before the deal was done. There was a convergence of ideas. You had a good and agreed program before you got the keys. In fact you never got the keys – the guy just kept driving!' (E)

On all other matters, great discretion is given to local management. Liam O'Mahony the current (2008) CEO said, 'You can't direct the price of ready-mix concrete in Omaha Nebraska from an office in Dublin. It is a dynamic model so you have to have local people who buy in to a sense of ownership of the business. You give them a lot of authority and responsibility and a lot of support and encouragement to go out and do the business and that's one of the secrets of success, the idea that we recognize we needed a lot of local management input into this rather than trying to direct everything here from the centre…We have come from humble roots here… We genuinely try to give everyone the opportunity to be the best they can be themselves, in keeping with their own abilities, desires and aptitudes.' (Liam O'Mahony quoted in Brennan, 2005) O'Mahony also said 'we try to make ourselves user friendly to crusty owner-entrepreneurs. We support the hidden talent in a family business where the rake of a son was about to take over.' (quoted in Answer.com). The 'user friendly' approach is based on a common understanding: 'CRH … at top-level always had people who had done 'the heavy lifting' and this was the attraction to many owners, to sell to people who understood and could judge the operational as well as the financial side of the business.' (Letter, D, 16 November 2007) This did sometimes mean that solutions were sub-optimal: '[We did not] force the owners. Want him to keep his stature. We might have to live with a few things but in the end it will come right. Persistence is important.' (D)

The degree to which the selling owner-entrepreneur can remain within the business is unusual. In a 1995 interview former CEO Don Godson said:

> 'We've purposely invested in development teams in the regions and even within the regions in the product groups. We see that as people who learn CRH value system, who can negotiate deals, integrate them and later on manage them, and these deals are often, oh, pursued over many years, and they offer us an opportunity to keep aboard the owner/entrepreneur and indeed in many cases his son. So it's a different type of strategy. What it

> does is it enables you to negotiate good value. It enables you to meet vendors' different needs, not just financial needs, but a need to have two sorts of bets, that he can still run his business having sold it or even consider his son to come on after him, sort of that comprises forbearance and flexibility and enough sense on professional managers to listen carefully to people who have had the skills to build these businesses and run them successfully, and it's a two-way process. We think we teach in systems and disciplines and planning. We think we learn an awful lot from the grass roots entrepreneurs in our industry and have been able to maintain them and motivate them in our business…We sort of grew up in that environment in Ireland, and we've been able to use it not just in the United States but also very successfully in Europe where the name above the door is often the name of the guy still running the plant after 5 or 10 or 15 years…' (Dow Jones Investor Network, 7 March 1995)

'The best calling card is the former owners and their sons. Many times the son ended up running a business ten times the size of the father. The former owners would say: they give me plenty of support but don't cramp my style. You get to go to Ireland to give your views. They want to learn from you.' (E)

Having said all of this, the process is not immutable and CRH will deal with situations that are not working; 'while CRH is a canny buyer, things can go wrong, you must have perseverance.' (D). Also, sometimes business reasons will require some changes to the more usual process; for example, some business have been renamed to avail of larger brand dynamics (for example, ‘Keyline’ in the UK; where the existing builders’ merchants were rebadged as Keyline in 1988 – this business was then sold in 1999). ‘There are no golden rules you can follow blindly. You have to know the idiosyncrasies that attach to any one situation.’ (D)

The above has focused largely on the US acquisition history of CRH but confirmation that the post-acquisition strategy is as described by management, above, can be obtained by investigating an acquisition in Cork, in the south of Ireland, in the 1960s.

John A Wood Limited.

In 1961, Roadstone acquired a building materials company based in Cork, John A Wood Limited. This company had been founded in the 1930s by Mr John Wood. Originally it was a supplier of aggregate from several pits just outside Cork city and gradually branched out into other activities. The acquisition gave Wood a substantial shareholding in CRH and a great deal of management autonomy in Cork.

There were always differences between the ways that Roadstone and Woods were run for a variety of reasons. One interviewee who worked in both wrote: ‘The management style and organisation in Woods and Roadstone reflected very much their origins and history. The former’s markets were intensely competitive and low-cost production was vital – as was extended credit [to customers] (up to 120 days on average in bad times). The latter [Roadstone] had achieved significant and dominant market shares – with consequent high-prices, margins and reasonable credit terms. The downside of this in Roadstone's case was the growth of strong and powerful unions which the centralized [management] structure favoured. High labour costs were exported to the rest of the country from the capital, Dublin – into country regions where labour was much cheaper and the company suffered in cost terms and fear of strikes (particularly as monopoly supplier in many of their markets). John A Wood Limited was not immune from labour problems either but a strategy of industry agreement (including competitors) and eventually taking a very firm and tough line on unofficial strikes was effective. At branch and shop steward level in Ireland in the 1960s and 1970s being "at the vanguard of the socialist revolution" appeared to be the dominant force – allied, of course, to the usual "human mischief". The differing approach was driven largely by the relative competitive situations.' (Letter, D, 16 November 2007)

One of the insights that CRH learned from its builder providers businesses was how local pricing is in the building materials business and how quite large price differences between the same product in quite close localities will stick despite the ease of price comparison. One cause of this is, with a low weight to value product, local geology will play a large part. If, for example, the local geology provides a source of clean, alluvial or glacial aggregrate, which can extracted and put immediately on a truck, pricing will be very different to an area where granite has to be crushed to provide aggregate. Even 20 miles apart pricing can be quite different and those differences will be stable over long periods of time. These geological differences and other (perhaps consequent) differences like local building practices, customer profiles, climate and so on, meant that no two CRH businesses functioned in the exact same market conditions.

Every individual business in the firm was run differently, inevitably for these reasons. For example, one of the interviewees, A, was in charge of John A Wood's ready-mix concrete business from the early 1970s until 2004 was aware that on the one hand he was running a unique business within CRH but at the same time was aware that there was a commonality of interest. For example, Roadstone always had a process of 'the cross-fertilization of ideas'. (D) Originally this process was informal; 'we always encouraged travel, to see how things were run elsewhere; this was always a Roadstone feature.' (D) This then developed into the 'Continuous Improvement Committee' in the 1970s, but for some reason this name was not popular and it became the 'Best Practice Committee'. There was a Committee for ready-mix concrete and the Cork executive was involved in setting this up and had a key role on it over a number of years.

The role of this Committee was quite particular. No-one in CRH, said A, was ever 'told what to do…but there was peer pressure. If underperforming the onus is on us to bring it up to the best level. You were just asked to look at people with good ideas – "Go and look at it and see if there is anything in it for us". We might or might not bring it into play.' (A) The key measures in ready-mix concrete were cost per cubic metre and cost of delivery per cubic metre. But other comparisons were also made, including what might seem like superficial features, like the physical appearance of trucks. This manager was quite clear why this voluntary approach was required. 'It is very hard to get to the bottom of comparisons … complex. We were always trying to figure out a better way… it was never simple.' (A) Local building practices, climate, customers and so on all played a part. Even the smallest difference had some effect, for example, one executive pointed to a cultural difference between Ireland and the US: 'The trucking industry in the US has a much higher level of pride – you can see that in the way they look after their trucks, they are always in better condition.' (D) There was no-one best way. There was something to be learnt from everyone, for example, for a large number of reasons, costs in the US for ready-mix were always higher than in Ireland but 'the Yanks were great'. (A)   'The openness culture in the whole group ensured that, on balance, best-practice adapted to the local situation invariably prevailed.' (D) The comparisons between different concrete plants, required managers to see through the differences in local geology, practices and customers to the areas where possible improvements could be brought home and that would actually result in cost-savings or other improvements. These practices would then have to be accepted by the employees or 'owner-drivers' and so an evaluation of whether an improvement was actually practical was also needed.

Making comparisons with other concrete plants must have required some insight into the fact that things that seemed to work well there might not work in Woods for no other reason than it would not appeal to the culture within Woods. But there must also have been an awareness that sometimes the rules would have to change or the priority of rules would have to change. This would be difficult for everyone. 'You would look for a reason why you were more expensive [which did not require a solution or could not be solved] but you were only fooling yourself. There was a resistance to change even within myself. I wanted to be left to look after my own patch.' (A)

In the next chapter we will analyse this case in more detail within the frame of the rule following perspective.

Post-Acquisition Decisions in Jacob Fruitfield.

There is no doubt that global brands enjoy many advantages - not only of scale and cost efficiencies but also in consumers' perceptions of value and quality. (Steenkamp et al, 2003) But there are many products that only have local appeal. They are reflections of very local cultural preferences as to taste, quality, service or marketing. Even within a homogenised culture like the US there are many products that are local; for example a recent article in the New York Times discussed the controversial decision of Kraft Foods to discontinue the production of The Crown Pilot chowder cracker which was popular only in the region around Portland, ME. (Zezima, 2008) Perhaps these local preferences will not last. (Levitt, 1983) But in the meantime, some of these local brands are successfully competing directly with the best-known global brands. (Boston Consulting Group, 2008) As Ghemawat (2007) has pointed out, we live in a world that is only semiglobalized and is likely to stay like that for some time to come. Ghemawat argues that 'borders still matter' and classifies the reasons why in 'terms of the cultural, administrative, geographic and economic distances between countries.' (Ghemawat, 2007, 8) For example, a 2006 report by ACNielsen on the top 100 brands in Ireland had Coca-Cola as number 1 but five Irish brands in the top 10, of which Jacob's biscuits was number 4. (The Grocer, 9 September 2006). This bears out Ghemawat's thesis that food products tend to be most sensitive to 'cultural distance.' (Ghemawat, 2007, 49)

The purpose of this section of the thesis is to explore why two global food companies struggled to combine global and local businesses in single operations in Ireland. The case study looks at the difference in decision making by managers (sometimes even the same managers) while part of the global firms and, then, part of a purely Irish firm.

Background to Jacob Fruitfield.

The brands owned by the Jacob Fruitfield mostly date back to the Victorian era. W&R Jacob was founded in Ireland in 1853 and launched Kimberly and Mikado biscuits in 1881 and the Cream Cracker in 1885. In 1914 the company opened a factory in Liverpool. In 1919 (or 1901 – different dates are given) the 'Club Milk' bar was introduced. After Irish independence, in the 1920s, the UK and Irish businesses were split. Ownership of both was combined in Groupe Danone, in 1990, management was not combined. Danone sold its Irish and UK biscuit businesses in August 2004. For 'competition issues' (The Grocer, 7 August 2004) United Biscuits did not buy the Irish businesses when it acquired the UK businesses. The Irish businesses were acquired by Fruitfield Foods, as it was at that time. Some confusion is caused by this split: United Biscuits produce 'Jacob's cream crackers' and so on in the UK and Jacob Fruitfield do so in Ireland; in 2004, when the two businesses were last under the same ownership, total combined sales in Ireland and the UK were GBP£183m – with about €70m in Ireland. (The Grocer, 31 July 2004, 7 August 2004; O'Mahony, 2005)

The confectionary brands have their roots in Williams and Woods which was founded in 1876 out of existing confectionary businesses. Silvermints was launched in 1880. The company floated in 1893. In 1967 the company was fully acquired by Nestlé. In addition, Rowntree and Mackintosh, UK company, established factories in Ireland in the 1920s, to avoid the protectionist policies of the new Irish state. Over time these companies merged and were taken over by Nestlé in 1998. Some of the confectionary brands now owned by Jacob Fruitfield came through this route. The jams and marmalade businesses date to 1917 when Lamb Brothers established an operation outside Dublin; Fruitfield jam, Little Chip and Old Time marmalades have their roots in this business. Crosse & Blackwell also established the Chef businesses in Ireland and then acquired the jam and marmalade businesses. In the 1960s Crosse & Blackwell was acquired by Nestlé. By 2002 Nestlé owned a diverse range of Irish brands (sweets, jams, marmalades, ketchup and vinegar) through these various acquisitions; indirectly through their acquisitions of UK companies and directly through the acquisition of Williams and Woods, over the previous 50 years. (Unless otherwise cited, this information is sourced from the Jacob Fruitfield website.)

Nestlé undertook a strategic review of its Irish businesses in the early 2000s. In Ireland, its operations included the distribution of its global brands and the manufacture and distribution of a large number of Irish brands. The international brands were very successful in Ireland. The Irish brands were not profitable. Ireland was booming but these brands seemed stuck in an earlier, poorer time; old fashioned packaging, no advertising, limited availability; ‘neglected’ was how one executive described them. As a consequence of this review, Nestlé decided to move the Irish distribution base of its international brands to a new location and announced, in January 2002, that it would sell off the Irish-only businesses in - what was called by the 120 staff remaining – ‘the sinking ship’.

Michael Carey had returned from the UK in 2001. He had financial backing from a private equity house, Lioncourt Capital, and bank debt. (O’Mahony, 2005; The Grocer, 24 February 2007) He decided to bid for these Irish businesses. Carey said: ‘I knew the brands, I knew the company… It was an obvious opportunity.’ (O’Mahony, 2005)

When Carey acquired the Nestlé Irish businesses, now renamed Fruitfield Foods, they were loss-making. Within 12 months of taking over, all this had changed. Costs had been slashed and, at the same time, sales increased. The company almost immediately went from negative EBITDA to positive EBITDA. ‘It took Carey just 12 months to turn Fruitfield to profit, something he achieved with most of the original 120 staff and many of the same products.’ (O’Mahony 2005)

In 2004 Danone announced that it was selling its Irish and UK biscuit businesses; Danone’s CEO Franck Riboud said, in that year’s annual report for the group, that the operations were sold as ‘our share of market was too small to hold much promise…’ The businesses were to be sold together. In late July, United Biscuits entered into an agreement to acquire the entire business, but a week later it was announced that the Irish businesses were to be sold to Fruitfield to avoid competition issues in Ireland for United Biscuits' already dominant biscuit operations in Ireland. The biscuit business in Ireland was profitable but nearly three-times the size of Fruitfield Foods. The merged company, Jacob Fruitfield, had, at that time, over 500 employees with a turnover of €110m. (O'Mahony, 2005)

Carey and the other interviewees confirmed that the market share of their brands has increased by over 10% and that EBIDTA is increased (although the bank debt may, obviously, mean lower absolute profit). Visibly, the brands have been 'refreshed' with new packaging and advertising campaigns; for example Chef in 2008 sponsored a TV series about a comedian learning Irish. In addition, the land and buildings that were acquired as part of the acquisitions have turned out to be hugely valuable, have been spun out into a separate entity, and, according to Carey, now amount to a separate business line within the group and will allow for substantial future profits. In a recent article in the Irish Times (Hancock, 2008) showed an increase in operating profit of 16% in 2007 with turnover flat at just over €90m.

Why did Nestlé and Danone struggle to maximise the return from these brands?

The ability of Jacob Fruifield to run the businesses more successfully than Nestlé and Danone would not be expected. On the one hand these groups have huge resources and on the other hand they were aware the importance of managing local brands properly.

On the financial side:

- In 2001 Nestlé had sales of CHF85bn (€57bn based on foreign exchange rate at 31 December 2001 between the Euro and the Swiss Franc of 1€:CHF1.48), net profits of CHF7bn (€4.7bn) and total assets of CHF94bn (€64bn) of which shareholders' funds amounted to CHF34bn (€23bn) and it had cash and equivalents of CHF15bn (10bn).

- In 2004 Danone had sales of €14bn and net income of €917m. It had a market capitalisation of €18bn, shareholders' funds were €5bn and the company generated free cash flow of €1.3bn.

In addition the two companies were conscious of the local cultural sensitivities of their business; this was not just a matter of two groups with a tin ear to Irish culture. There was something here that both Nestlé and Danone were aware of:

- In a 2008 speech to shareholders, Nestlé's CEO Peter Brabeck-Letmathe (10 April 2008) is on the one hand aware of the advantages of global consistency and on the other hand acutely conscious of local differences: 'Poorly understood in the beginning by many observers, the vast GLOBE (Global Business Excellence) project is a means for managing both the complexity resulting from the diversity of our consumers and the operational efficiency we strive to achieve. … The GLOBE project has also enabled us to transform the Nestlé supertanker into a flotilla of rapid and maneuverable vessels… We are, however, convinced that downstream – that is, in our interaction with the consumer – it is our obligation to maintain a high degree of decentralisation. We continue to believe that there is no such thing as a global consumer, and this is why we absolutely must take local preferences and habits into account. It is this respect of cultural and ethnic or religious differences that enables us to maintain the trust of consumers throughout the world. Our marketing and communication activities are carefully evaluated to ensure that they conform to the sensibilities of our local consumers. This, Ladies and Gentlemen, is the key to our success….'

- In an interview with the 2004 annual report, the CEO of Danone, Franck Riboud was asked: 'You often talk about the Group's culture and your special way of doing things. Doesn't geographical expansion threaten that?' Riboud replied: 'There was that risk. But we have taken steps to spread and share our culture across the Group in its expanded form, ensuring a degree of overall consistency. Our DANONE Way program makes an important contribution to that. But we have also learned to welcome the influence of the developing countries we work in, because it enables us to take a fresh look at our differences and develop innovation and exciting new ways to move ahead…. I very believe that our new frontiers are not just about new sources of growth. They also help us to ask new questions, look for new solutions, find new ways of working and new ways of thinking.'

As can be seen above, both companies on the one hand were seeking to create cultures within their organisations that would span the world but on the other hand they were seeking to serve and avail of cultural differences.

Carey had worked for nearly 20 years for global brands. He could see a problem with global brands. For example, he had spent a few years as managing director for the UK and Ireland for Danone's Evian and Volvic. The global marketing was focused on the purity of the water. In the UK, however, at the time, bottled water was a fashion item and its source was secondary. 'We couldn't stress this point in the UK [advertising]. We had to follow the global branding.' Carey said: 'I could see the frustrations for local management… Global branding must be consistent across the world. [There is] no such constraint in Jacobs. We tailor brands totally for the local market. So Chef is sponsoring [a tv programme on learning Irish]. If this was an international group you would have to convince head office and you would never be able to do that… This is not to say that global brands are wrong – they are right to have … global consistency.'

When Carey was doing the due diligence on Nestlé's Irish businesses he could see, on the one hand, the opportunity to grow the brands and, on the other, the cost savings that could be achieved. One the one hand: 'The scale of the offices! A marble atrium! They used commission research on the marmalade business every two months. Every two months it showed a 51% share of the market. It never changed but they kept commissioning the research.' Another executive said: 'It was very evident that money was being wasted… [Suppliers] saw the big multinational as a soft-touch… there were no controls [on spending].' (C)

On the other hand: 'There had been no activity on the brands for years, old packaging, no advertising and so on….' (Carey) If a mint was to be advertised it was 'obviously' (B) going to be the global mint and not the local brand. Worse, given the focus on global brands, the sales teams would readily agree to de-list Irish items from supermarket shelves if it freed up shelf-space for new global products; the Irish brands were 'sacrificial lambs'. (B) Over many years, one interviewee (C) could only recall one advertising campaign in Nestlé for a local Irish brand; usually ad campaigns were the international or UK ads for the global brands with an Irish voiceover. Another executive (B) said: 'The Irish brands were neglected… year on year the Irish brands were declining.'

For example, the Club Milk bar was an Irish institution; it is a small chocolate covered sandwich biscuit sold in single units with a distinctive yellow foil wrapper; it was ubiquitous being sold in every pub, shop and club. However, within Danone, its iconic status was not appreciated and, in order to enhance its unit profitability, the ingredients in the bar were gradually replaced with lower quality ingredients. The bar's popularity dramatically fell. One of Carey's early objectives was to return the level of quality.

A further example, in Nestlé, was the preference for a global financial reporting and management information system; Nestlé worldwide used a bespoke SAP system tailored for Nestlé– 'there were constant SAP projects'. (C) This preference for consistent, standardised reporting across the globe is understandable. However, in Ireland any new products had to be put up on the system in the UK, this was expensive and took time. A small extension of an existing Irish brand required similar IT support, time and expense to a completely new global product. The Irish product was often not worth this effort. In addition, the cost of the system was inappropriate for the size of the Irish products; IEP£1m (€1.3m) a year in IT support was allocated to Ireland. Once Carey took over, the accounting and reporting system was switched to SAGE. This is a product for SMEs, it is a standardised product that required minimal IT support within the company. Putting up new products on this system is cheap and quick. In addition, because of its simplicity, management could also make the systems more available, for example, all sales staff can access it which was not possible with the Nestlé SAP system.

Another example was a logistics decision; here the global consistency worked against Nestlé on two different fronts. Nestlé engaged one logistics firm to undertake deliveries of product in Ireland and the UK. However, this logistics company did not have an existing operation in Ireland so they set up a new operation. However, this operation struggled with the unique requirements of the Irish retail trade. For example, full pallets are the norm in the UK whereas 'broken' (that is, pallets with more than one product on them or pallets that are not full) pallets are the norm in Ireland; this is a result from the fact that Irish retail units (even of the big supermarket chains) tend to be smaller in Ireland than in the UK. The UK logistics company struggled with managing product on broken pallets and customer service suffered. After the take-over from Nestlé, deliveries were switched to an Irish logistics firm and customer service rapidly improved.

Appealing to the rules of the global organisation could mean that counter-productive decisions were made at a local level on the local brands. For example, to justify a production plant in Ireland in the global group, production had to be of a certain level. However, the natural market in Ireland did not support that level of production. As a result, while production levels were retained, sales volume was then supported by trade rebates and free promotional product. One executive said: 'The size of the rebates was frightening.' Interestingly, all of the interviewed executives noted the amount of time Irish management spent on the local brands before Carey took over.

The management team was, explictly, aware that global consistency was the problem for the global brands and the opportunity for him; one executive said that the problem was 'one size fits all' (B). For example, Carey worked briefly for Kellogg in the UK but the experience was not successful. Carey understood that this was a result of the global and consistent culture within Kellogg: '… it was a bad fit. A wrong fit. They have a very strong culture – [it is] amazingly successful. Neither side was right or wrong… I didn't operate in that culture… in the 'Kellogg way'.' In an interview in the Irish press, Carey was explicit about the consistency preference in global brands: 'The fact is that we're able to do things that are right for the Irish market – things that multinationals would never do, because it wouldn't be right for the British market.' (O'Mahony, 2005)

At the same time, Carey and his management team struggled with the different cultures within the Jacob's and Fruitfield companies; they called it 'de-Nestléing' and 'de-Danoneing'. It took time and effort to change this culture: 'Michael took the personal approach … there was a paradigm shift … he was the first in every morning and the last out every night.' To deal with the absentee rates in Fruitfield, Carey 'would sit down with you and say "why were you out yesterday?"' In particular, Carey found that the Jacob's culture was not as he would have expected or liked: 'The cultures were quite different. Fruitfield was by that time [2004] quite entrepreneurial; it operated at a fast pace, which was pretty typical for a local firm. Jacobs was part of a multinational group and had all the qualities that brings with it.' (O'Mahony, 2005) 'The atmosphere was terrible; there were corridors and corridors of offices.' For example, when one executive moved his office to Jacob's he found that he could not make himself a cup of tea but had to order it from the canteen; 'it took me two weeks to get the key to the kitchen.' (B) Most of the management team in Jacob's did not survive in the new culture. (C)

Again we will return to this case and explore it further in the next chapter.

Chapter 5.

Hayekian Insights into the Post-Acquisition Integration Strategy of CRH plc and Post-Acquisition Decision Making in Jacob Fruitfield.

Key words: Integration, acquisition, disposal, order, rule following, change.

Chapter Summary: The purpose of this chapter is, initially, to test the preliminary propositions of this thesis, that rule following could be pervasive within a business firm. The chapter then proceeds to investigate whether rule following might play a part in the options that are open to managers, by analysing the post-acquisition integration strategies of the building materials firm CRH plc and the post-acquisition decisions in Jacob Fruitfield.

‘At any rate in order to grasp such tremendous changes, we must also remember the influence which, supported by custom and legend, priests and chiefs are able to exercise on both. Indeed their influence is chiefly directed toward preservation, but it also happens from time to time that it is directed toward change, especially if that serves their personal interests. Persuasion, and above all example, can do what the ruler, particularly the alien rule and conqueror, cannot accomplish by direct force.’ (Tönnies, 1961, 56ff)

Chapter 5: Hayekian Insights into the Post-Acquisition Integration Strategy of CRH plc and Post-Acquisition Decision Making in Jacob Fruitfield.

There seems to be a division of knowledge within CRH plc and within Danone and Nestlé. At the very least, certain employees have knowledge of local conditions that more senior employees do not have; as Liam O’Mahony of CRH said: ‘You can’t direct the price of ready-mix concrete in Omaha Nebraska from an office in Dublin.’ (Brennan, 2005) The question for this chapter of the thesis is whether the rule following perspective might allow for insights into the consequences of that Hayekian knowledge problem within the firms being studied.

The purpose of this chapter is to investigate whether, firstly, there is support for the two preliminary propositions, described in the previous chapter, in the answers given by the executives to the specific questions asked of them, and, secondly, if rule following is a coordination mechanism in those firms, whether the post-acquisition integration strategies in CRH plc and the disposal by multinational food companies of their Irish brands and their acquisition by Jacob Fruitfield could be considered supportive of the rule following perspective. It attempts to show that rule following, tacitly or otherwise, informed the decisions that managers in those firms made.

First preliminary proposition: Individuals would not be able to articulate a concrete goal for their firm but instead a somewhat fuzzy goal would be articulated.

When specifically asked what the purpose of CRH was, the answers were supportive of the first preliminary proposition:

- On its website the strategy confirms that while the overall business will remain focused on building materials: the 'focus is on **performance and growth**.' [bold in original]
- 'To make a good return for shareholders. It is bottom-line orientated, it is not a good business unless profitable. The whole business culture in CRH was: you only got on by growing the business successfully.' (D)
- 'To make sure that we got paid for what we did!' (B)

When specifically asked the purpose of Jacob Fruitfield interviewees were also not concrete despite the fact that the company's best known brands are products that are fixed in the public mind for over 100 years:

- The firm's website says: 'The Jacob Fruitfield Food Group is a progressive, leading Irish food company with a brand portfolio second to none that includes Jacob's Fig Rolls, Kimberley, Mikado, Coconut Creams and Elite; as well as Chef, Fruitfield, Tuc, Silvermints and many more. With full sales, marketing, distribution, manufacturing and product development capabilities; Jacob Fruitfield Food Group is committed to growth of its domestic, foodservice and export business.'

- Carey said that the purpose was: 'To be the leading local food company. We have the freedom to act locally, we understand the Irish consumer and we understand the local trade. We want to double EBITDA'
- Another executive said: 'To make money!' (B) He then clarified that to say: 'To create a sustainable long-term marketing and distribution business that commands high-levels of market share.'
- A third executive (C) said: 'To make profit. If you have profit you have options.' He clarified this by saying: 'The purpose of Jacobs is to be the largest and most successful privately owned-food company in Ireland by gross sales, market share and EBITDA in a way that enhances shareholder value.'

To articulate the purpose of CRH and Jacob Fruitfield in terms of profits, profitability, growth, EBITDA or market share is, essentially, to confirm that the goal is not concrete; as any sustained retention of growth, profits, market share must mean that the firm is engaged in a competitive discovery process where each competitive action is a step into the unknown. Therefore, there is support for the first preliminary proposition that in both CRH and Jacob Fruitfield the goal of the organisation is not concrete but is vague and yet to be fully discovered. As has been suggested in previous chapters this should place some stress on command as a coordination mechanism within the firm. It should imply, as Follett (1940) and others have submitted, that rule following may be a more useful coordination mechanism in these dynamic circumstances.

Second Preliminary Proposition: That when a superior gives an instruction to a subordinate, this is the articulation not of a command but of a rule, where the subordinate and superior would expect that the subordinate would do similar things in similar circumstances in the future even if not specifically told.

The distinction between a 'command' and a 'rule' was never made to any of the CRH interviewees in all their years in the company; which meant that every instruction was treated as a rule. All said that if they told someone to do something once they would expect that in similar circumstances that the person would do the same thing 'if the circumstances were really similar' (D) and that if they were told to do something once they would also do the same thing in similar circumstances even if not told. One interviewee said that he had one employee who had to be told each time to perform the same task that was regularly required to be undertaken; 'he broke my heart' (A) and eventually was let go. This approach did not apply to just the routine: two phrases that were repeatedly used were 'logic' and 'common-sense'; you did what was 'logically required', everyone was 'expected to use their common-sense' (A). 'Treat them like you would be treated yourself…. You asked them to do something and if they did not do it, you asked them why.' (A) 'People who did what needed to be done got on.' (both B and D used this phrase). 'There was always local discussion; let them be the committed agents of change, where change has to happen. The way to handle people is the secret. Everyone wants power over their own future. People want to do their own thing' (D) 'Part of management was to get the other guy to see it your way or if he had a strong reason maybe I could learn from that.' (E) Indeed one of the executives involved was renowned for his approach to requests for guidance: 'He would ask you what you thought you should do, and if he agreed with you he would say "do that", if he did not agree with you he would say "What else might you do".' (A) The researcher asked this executive why he took that approach; he said 'I made enough mistakes to know that you are not always right. The person asking advice always knew a bit more. I wanted to be participative and not dictatorial. But I did, I had to, make some decisions and make sure that people knew where they were going…. If I wanted a quarry to change I'd sit down with them and say: "aim at this – more crushers, less labour and so on." They would get all enthusiastic but I would have to deliver the cash to make the capital spend. They were on side and will deliver for you. A bargain must be good for both sides.' (D) Finally, a number of the interviewees (A, B and C) were explicit that once a decision was made once that it 'created a precedent' and that had to be borne in mind when making any decision. There is support here for Schlicht's 'consistency preference' (2003) and for Barnard's (1938, 279) and Penrose's (1959, 16) analogy between the business manager and the common law judge.

The distinction between a 'command' and a 'rule' was also not made to or by any of the interviewees in Jacobs; although one executive said that he was somewhat familiar with the difference. All said that if they told someone to do something once they would expect that in similar circumstances that the person would do the same thing and that if they were told to do something once they would also do the same thing in similar circumstances even if not told. It was clear that some emphasis was placed on rule articulation. One executive (C) said that 'the style of the company is much more: we should do this because….' Carey said: 'We spend a lot of time talking about the kind of culture that we want. There are rules for everything, discussion and debate. We all agree on something and then do it. Not hierarchical. We have people we can trust and we give them the freedom to do it their way.' Interestingly, one of the former senior executives in Nestlé Ireland was described as 'dictatorial'; working with him was described as stressful and unpredictable.

Therefore, there is support in both cases for the second preliminary proposition: that the distinction between a command and a rule is not, generally or even ever, made in the case study firms. When a person is told to do something once, that person is generally expected to do the same thing in similar circumstances in the future. Thus, the instruction should be seen as rule-articulation and not as a command, for the reasons outlined previously in this thesis.

The difference between a command and a rule is so important we would expect that making the distinction between a rule and a command would be a central feature of every instruction. Every time a subordinated was told to do something, it would seem vital that the subordinate was told whether this instruction was a rule, to be undertaken in all similar circumstances in the future, or a command, to be undertaken for this particular foreseeable result only. In fact this distinction was not made in the case study firms and this proposition was also supported by the pilot study undertaken in a professional services firm (See Brady and Walsh, 2008) and any examination of personal experience will not discover any situation where rules and commands are explicitly distinguished in instructions in a business firm. This is a severe challenge to the conventional wisdom that command is the main coordination mechanism within the firm and a problem with command within the firm that the researcher has not seen identified elsewhere.

We will return to CRH and Jacobs, where we will deal with some of the implications of our finding that rule following may be an important coordination mechanism within these firms.

The consequences of rule following in CRH and Jacob Fruitfield.

At this point it may be worthwhile to summarize the thesis to this stage. It has been submitted that rule following may be an important but underestimated coordination mechanism within the business firm. The researcher has suggested that a business firm is an order created by rule following behaviour; that command as a coordination mechanism appears to be over-privileged, at least within the firms examined. Individuals knowing and following the rules allows for predictable behaviour, the ability to predict the future and the consequent extension of knowledge of each individual within the order and of the order as a whole. But these strengths of rule following come at a price. Individuals, even if only unconsciously, will not wish to disrupt the coordination of knowledge within the firm by not following the rules. Rule following will also result in what some might call conservatism and aversion to change but what Schlicht (2003) calls, more accurately, a consistency preference: 'Similar cases must be treated similarly … otherwise entitlements and obligations will not be coordinated smoothly.' Schlicht noted the importance to individuals of appearing to be consistent: 'the consistency of behaviour is tied up with … perceived competence which is in turn an important element in eliciting authority…' Otherwise, there is the danger of appearing to be clumsy, uncouth, irresponsible or incompetent in terms articulated by Barnard: 'the hopeless confusion of inconsistent expediencies so often described as "incompetence".' (Barnard, 1938, 276) Any one individual within the firm will, generally, exhibit, or try to exhibit, this consistency preference. Finally, as we have seen, command may be avoided as a coordination mechanism so that the theoretical traditional tool of the manager to overpower the routine and the conventional may not be as available as has been thought.

In theory, managers exist in a world of open alternatives. As Magretta notes in her review of the management literature: 'The fundamental premise of doing better by being different is that you are playing in a world of alternatives. The strategic choices every enterprise makes, explicitly and implicitly, determined how it is positioned and configured in relation to those other alternatives. Broadly speaking, they are choices about which customers and markets to serve, what products and services to offer, and what kind of value to create. Made well, these strategic choices enable an enterprise to outperform its competitors.' (Magretta, 2002, 72) In the real world, however, options may be less available than it might seem. We have seen that there is a logical and understandable basis for employees resisting all forms of change within a firm; as any change to the rules disrupts the order, the predictability of behaviour and the extension of knowledge. We have seen that in rule following orders choices that may appear to be available are not available. Instead, choices and facts are ignored, and one course of action will appear, generally, to be the only course available. If the course does not prove to be effective, then taking another option may be more difficult than it seems and companies may have to solve the problem in ways that can appear to outsiders to be extreme, odd or even just 'whimsical'. (Sloan, 1963, 162 on Ford's decision to close 'the Rouge' to re-tool for the Model A)

In the preliminary propositions we outlined some support for the view that rule following is an important coordination mechanism in CRH and Jacob Fruitfield. If this is correct then we should see in Jacob Fruitfield and CRH that this consistency preference and the requirement that rule following requires internal commitment would place constraints on the ability of management to make decisions that might otherwise appear to be available. In the conventional management literature, 'fast-paced integration and early pursuit of available cost savings improves outcomes' (Pautler, 2003). The requirement for rapid integration has been refined down to the need for action within the first 100 days or the 'critical six to 12 months'. (Harrison, 2007; see also MC, 2000; Ashkenas and Francis, 2000; Ashkenas et al, 1998; Early, 2004; Walt, 2005). In addition, there is no real understanding as to why employees would seek to retain the 'old ways' and so Roberts writes that '[i]mposing the organization of one of the firms [on the other] has the great advantage of minimizing the confusion and disruption that that is involved in organizational change. It also contributes to rapid integration. There is a clear model, and the new people simply have to adapt.'(Roberts, 2004, 252)

In our argument the conventional advice may not be as achievable as is thought and, in fact, may not even be desirable. In CRH then, each acquisition is, we have argued, the acquisition of a complex rule-bound order with rules different, possibly quite different, to the rules in the any other entity within CRH. For example, the acquisition of John A Wood was the acquisition of rule-bound order that had quite different rules to the rules in Roadstone. These rules remained quite different over the following 40 years but, as we have seen, this was quite useful for CRH as each performed in quite different competitive settings and with quite different local geology, building cultures, competitive positions, management teams etc. Any attempt to reward or promote conformity might have integrated the two orders more closely but one or the other may now be less suited to its environment. And head office did not attempt this, instead in an important fetter on their own abilities to influence behaviour, the managers in Roadstone and then in CRH, left the members of Woods to themselves to improve their own processes and techniques through a voluntary commitment to advantageous change. As a clear signal of this forbearance, the name of the acquired company was not changed, there was no common branding. Later CRH reaped the benefits of having these different orders when the competitive situation for Roadstone in Dublin became more competitive in the 1970s and managers from Cork were transferred to Dublin to assist change there.

Senior managers in Roadstone fettered themselves but then reaped the rewards of changes that might have been slower and less complete than ideal but were also, in the long-run, suitable for their local environment both inside and outside the acquired firm. Each order within CRH retains its internal rules, its consistency, and the extension of knowledge that flows from this. Furthermore, within each acquired firm change now flowed from a member of this order who had seen some improvement or insight elsewhere and returned to his or her order with an internal commitment to change that, as a cultural leader within the organisation, they could transmit to others; change did not flow from a remote and ignorant source. But here we can see the struggle with change in each participant in the order. Within the individual, even one deeply committed to achieving best practice and who had clear measurable metrics of performance, any change was a struggle: 'You would look for a reason why you were more expensive but you were only fooling yourself. There was a resistance to change even within myself. I wanted to be left to look after my own patch.' (A) We can see this resistance not as mental laziness or conservatism but as an unwillingness to disrupt the existing complex order.

We can see the reluctance to embrace this loss of coordination and knowledge when we look at Nestlé and Danone. Global brands, almost by definition, require a level of global consistency. For example, Mercedes 'has a handbook that subsidiaries and sales agents must strictly follow while developing local advertising.' (Kotabe, 2003) The Coca-Cola brand would not last long if a single bottler in a single country did not follow the global rules on, for example, hygiene or product recipe. Even when Coca-Cola adapted a 'Think Local, Act Local' strategy in 2000 which was designed to devolve strategic decision-making to local country executives the degree of global consistency was stressed with Douglas Daft, Coke's CEO, saying: 'If our local colleagues develop an idea or strategy that is the right thing to do locally, and it fits within our fundamental values, policies, and standards of integrity and quality then they have the authority and responsibility to make it happen.' (quoted in Ghemewat, 2007, 21) But at the same time, given the differences in taste and culture across the world Ghemawat's logic is impeccable: '*it may not make sense to compete in the same way in all markets*' (Ghemawat, 2007, 23 [Emphasis in original]) but he does not make the point that it may also not be appropriate to compete in the same way, even in the same market. Ghemawat has also noted that 'Some degree of internal consistency is a basic requirement for a good strategy…' (Ghemawat, 2007, 195) but does not explain why it is a basic requirement.

The difficulty with not being consistent, it is suggested, is invisible without the rule following perspective. Managing global and local brands required managers to apply one set of rules when making decisions in relation to one set of brands and then applying different rules when making decisions in relation to another set of brands. Given the internal requirement for consistency, Ghemawat's advice that it may not be sensible to compete in the same way in all markets may be harder to achieve than might be thought.

We saw that the local brands, despite the inactivity on them, took up a disproportionate amount of time of the local management. We might be able to explain that again by recourse to rule following, we have seen that following rules allows for quick (and coordinated) decisions. The local management could have quickly applied the global rules to the local brands but that was clearly inappropriate. Without any clear rules to apply the management floundered, probably searching for rules that fitted within the global framework and failing to find them. While the individuals *knew* that they could, should, treat the local brands differently there was an important constraint stopping them. If they behaved one way with the global brands – applied one set of rules – and a different way with the local brands – applied another set of rules – other individuals in the firm would find it hard to predict their behaviour. This would have resulted in a loss of knowledge and the individuals would have felt internal pressure to conform. No individual wants others to think that he or she does not know or understand the rules – even if they feel they are doing the right thing. We can also see that coordination by command was an illusory option; managers could, in theory, have made arbitrary decisions on the local brands and commanded others to conform for that particular concrete purpose but, in reality, that option does not seem to have been available.

Once Carey had taken over the Irish brands, the setting for those individuals became different; the rules changed. Now every rule was consistently appropriate for local brands; on the one hand spending on offices and market research plummeted – in facts costs fell almost everywhere. One the other hand the local brands were refreshed, appropriately for the local market, and new localised advertising commenced. Now employees could be both consistent and appropriate for the local brands. This explains why Carey was able to achieve this transformation largely with the existing staff from Nestlé and why the change could be fast enough to turn the company from an EDITDA loss to a profit in less than a year. But at the same time, it showed why Carey struggled with the Jacobs culture. Jacobs in Ireland was somewhat profitable, managers felt no need to change and to adapt their behaviour. The voluntary commitment to change, and not mere obeying of commands, may explain why so few of those managers survived in the new setting: they did not wish to change and so leaving to find a more conducive setting was a superior alternative.

It is submitted that Danone and Nestlé made a mistake when they put the local brands in the same entity and same physical location as their global brands and under the same management; in other words, in the same 'setting'. Here, as we have outlined, the consistency preference required by rule following behaviour may have meant that the rules for managing a global brand were, almost inevitably, applied to the local brands if anything was done at all. This would also explain why, as Carey noted, Nestlé's remaining businesses, all global brands, in Ireland are also doing better now that the Irish brands are gone. The rule following environment is simpler and clearer. Thus we can reverse Ghemawat and argue that Nestlé and Danone's mistake was not to create enough (internal) 'distance' between the global and local brands; in fact, Ghemawat notes that Procter and Gamble may be doing just that (Ghemawat, 2007, 211) by using three separate units. But in the end both Danone and Nestlé did see this error and created that distance by selling off the Irish brands. It is interesting to note that when interviewee B was involved in reviewing Nestlé's operations in Ireland before the disposal of the Irish brands, it seemed obvious to that group to split the global brands into a separate entity and a completely separate location to the 'sinking ship' – the Irish brands.

The reverse, but similar trajectory, can be seen in the recent Coca-Cola story as told by Ghemawat. Here, as we have seen, Douglas Daft who had previously headed Coke's Middle and Far East operations (and we can suspect, like Carey, had often been frustrated with having to adhere to the global rules in these markets), in 2000, introduced a new 'Think Local, Act Local' strategy. For example, global advertising of Coke was ended. Instead all ads were to be created locally. However, here Coke made the opposite mistake to the mistake that Danone and Nestlé made in Ireland, with no global rules the decisions made locally were incoherent even where there were umbrella themes. Ghemawat describes the result as 'flailing around'

(Ghemawat, 2007, 22), sales sagged and by 2002 oversight over marketing was returning to Atlanta and by 2004 Daft was gone.

The disposals by Nestlé and Danone may not have appeared completely necessary, especially to an outsider, but both groups may have felt that they had nothing useful to bring pure Irish brands. In this they may have been objectively mistaken. Jacob Fruitfield is now applying some of the techniques that Carey saw in the global companies he worked for; particularly in relation to outsourcing production to achieve production scale-savings on smaller brands. One of the interviewees (C) was of the view that outsourcing production is the key to global firms being able to successfully manage local brands. His view, again explicitly framed in consistency terms, is that low-production costs can be achieved by producing local brands in small production runs in large centralised manufacturing plants. The local requirement is now only for distribution (packaging, advertising, deliveries) and it is much easier to tailor these to specific products, especially as the costs of packaging changes and producing advertisements is much reduced in recent years. (C) With Jacob Fruitfield, outsourcing production to larger global scale plants in now underway and production has largely or will largely cease in Ireland. (Hancock, 2008)

The solution to the problem of the Irish brands in Nestlé and Danone was Carey's opportunity. We can understand now why Carey saw both an opportunity and value in buying from these global groups despite their skills and resources. For both

Nestlé and Danone opportunities that were available to Carey were not available to them – with different rules the cognitive frame in each was different to Carey's. In value terms, the opportunity was probably less visible to them than it was to Carey. Thus Carey could both do things that were not open to Nestlé and Danone and, when selling the brands, Nestlé and Danone would be prepared to accept a lower price than objectively justified because the value proposition that was visible to Carey may have been available to Danone but may not have been visible to them.

The consistency preference that flows from rule following behaviour, also allows us to explain why companies establish 'skunkworks', new venture units, spin-offs and so on (Prahalad and Bettis (1986) make the same point). Ghoshal and Bartlett were critical of managers for establishing these units as it was merely bypassing the problem, 'rather than attempting to fix the bureaucratic structures and elaborate systems that have stifled entrepreneurial initiative.' (Ghoshal and Bartlett, 1997, 39) While on the one hand those authors are right in that this is a mere bypassing of the rules of the larger order, on the other hand managers are right too. The rules that may be useful in a skunkworks or in a new venture may be exceptionally useful in that order but may not be suitable or may be just plain disruptive in the larger order. If the rules in the new unit are useful for the larger order it is always open to management to reabsorb it rather than spin it out. These separate ventures seem like a sensible way to experiment at the fringes of the rules of the order within the firm (see Schlicht, 2008 and Popper, 1962, 158 on 'piecemeal social engineering') attacking, as Popper recommends, a particular problem in a complex order rather than seeking out optimal solutions for the order as a whole. It is to be expected, however, as Chesbrough and Rosenblool (2002) note in relation to spin-offs from Xerox, the spin-off cannot completely escape the rules of the order from which it came although it can be 'less constrained in the evaluation of alternative models.'

> Retaining local initiative, retaining 'distance', requires some thought and deliberate effort. One executive than may be deliberately trying to do this is Warren Buffett. This view of the firm as a complex order created by adherence to rich rules of conduct, may allow us to explain some of the actions of Buffett. In his *An Owner's Manual* given to all A and B shareholders, in June 1996, Buffett explained 'The Managing of Berkshire': 'Charlie [Munger] and I are the *managing* partners of Berkshire. But we subcontract all the heavy lifting in this business to the managers in our subsidiaries. In fact we delegate *almost* to the point of abdication: Though Berkshire has about 180,000 employees, only 17 are at headquarters. Charlie and I *mainly* attend to capital allocation and the care and feeding of our key managers. Most of these are happiest when they are left alone to run their businesses, and that is customarily how we leave them… Most of our managers are independently wealthy, and it's therefore up to us to create a climate that encourages them to choose working with Berkshire over golfing or fishing. This leaves us needing to treat them fairly and in the manner that we would wish to be treated if our positions were reversed… On my death … my job will be split into two parts, with one executive becoming responsible

for investments and another, who will be CEO, for *operations.'* [emphasis added]

In his 1982 Annual Letter to Shareholders, and repeated in subsequent years, Buffett gave details of the types of company that Berkshire Hathaway prefers to acquire. He promises that a commitment of possible interest can be given in as little as five minutes. The business should be 'simple businesses (if there's lots of technology we won't understand it) … demonstrates consistent earning power … management in place (we can't supply it)…' Therefore, in almost all cases where Berkshire makes an acquisition management are retained. For example, when Berkshire Hathaway acquired the Nebraska Furniture Mart, a furniture retailer, in 1983, the owner and, very hands-on, chief executive was Mrs Rose Blumkin, she stayed on as manager of the Mart even though she was 90. At 95 she fought with her grandsons, who had become managers of the business, left the company and set up in competition. At 99 she sold this new business to Berkshire Hathaway and continued to put in seven-day weeks at the store; she worked until she died at 103 (2003 Letter to Shareholders).

Buffett is not just a stock-picker or a passive investor. There are certain behaviors that Buffett insists on and is looking for in an acquisition; he is clear about that – for example, he said 'We misjudged the culture in Swiss Re [when it was acquired]… I doubt if standard due diligence would have discovered that.' (Robison, 2005) Just as CRH insists on a certain ethical element and clear reporting of the 'facts', Buffett insists on honesty from his managers. His biographer noted: 'As far as is known, Buffett had never fired a manager – rather remarkable given the breadth of his career. He was clearly displeased with George Aderton, the president of the tiny Buffett holding, Citizen State Bank of Mount Morris, Illinois, in the 1970s. (Buffett wrote to Aderton how "irritating" and "annoying" he found his allegedly inaccurate reports – for Buffett strong words.)' (Lowenstein, 1996, 290). Seeing this behavior seems to be a factor in at least some of Buffett's investments: ' "One thing has always bothered me," Chace [manager of the Berkshire's textile mills in New Bedford] admitted. "I never knew why he picked me. When I resigned, he said, 'I remember you were absolutely straight with me from the first day I walked through the plant', that was all he ever said to me."' (Lowenstein, 1996, 256) Getting accurate information from his managers and knowing that the information was accurate extends the range of Buffett's abilities to allocate capital within the group. Interestingly, he did not fire Aderton at the Citizen State Bank of Mount Morris but instead sold the entire company, one of his few decisions to sell. (Lowenstein, 1996, 290)

If we return to CRH and Jacobs, we noted earlier in this chapter that there did not seem to be much similarity between the CRH and Jacob Fruitfield. It is hoped that examining the acquisition strategies in both has allowed for some degree of common insight into the problems that rule following within firms creates and the opportunities that it affords. In CRH the goal is to retain the existing order, retain consistency, but to assist in self-improvement. In Jacobs, it is to allow for a consistent rule following order that is appropriate for the Irish market.

It could be argued that the conventional business axioms about the 'need for speed' in all cases of post-merger integration is merely a manifestation of US cultural preferences as to time (see Trompenaars and Hampden-Turner, 1997, 130) and the preference for global rules from the US preference for homogenisation and both are examples of where apparent 'general axioms of business administration turn out to be largely American cultural axioms.' (Trompenaars and Hampden-Turner, 1997, 182) However, the purpose of this chapter is to transcend that observation and to point out that both preferences flow from a misunderstanding of how business firms actually function and an almost complete underestimation of the complexities involved. This synoptic delusion also involves a view of employees and culture as being obstacles to desired end-states while not understanding what motivates employees to try to retain the existing rule-based order and not understanding the damage to the knowledge within a firm that can be done by *any* integration or globalization process.

Conclusion of Case Studies:

In conclusion, we can argue that the rule-based perspective has given us an insight into the behaviour of employees of and managers in CRH, John A Wood, Jacob Fruitfield, Danone and Nestlé. There has been some support for the proposition that rule following can be a pervasive coordination mechanism within firms. There is also support for the proposition that this rule following behaviour imposes an important constraint on the decisions that may appear open to managers and may, in fact, be open to managers in other organisations. It would seem to be difficult to understand these behaviours without the rule following perspective and the consistency preference required.

In the final chapter in this thesis we will draw some tentative conclusions from and conjecture some implications of the rule following perspective into intra-firm coordination.

Chapter 6

Conclusion, suggestions for further research and implications of this thesis.

Key words: Orders, spontaneous orders, invisible hand explanations, rules.

Chapter Summary: This chapter draws some conclusions from the application of the rule following perspective to intra-firm coordination; it focuses on the implication for merger and acquisition activity. It makes some tentative suggestions for further research. Finally, it attempts to conjecture a Mengerian, or invisible hand, explanation for the origins of the modern business firm. Theories of the firm tend to favour visible hand explanations, this chapter tries to formulate an invisible hand explanation for the creation of firms as an economic institution within the market order.

‘Anthropologists may travel from island to island and observe that each harbours people with a particular custom. It is not necessary to go that far away, however. In modern economics, each firm forms an island of custom in the ocean of the market.’ (Schlicht, 1998, 207)

Chapter 6: Conclusion, suggestions for further research and implications of this thesis.

There can be little doubt that Mary Parker Follett thought her insight into intra-firm coordination was innovative. When she wrote of coordination of activities by following the law of the situation within a firm she concluded: ‘This gives, does it not, a slightly different aspect to the whole of business administration through the entire plant?’ (Follett, 1940, 59). However, this rule following view of coordination within the firm is still a minor tradition, as we have seen. It may be expected then that the full implications of this tradition have not been fully explored.

Through Taylor (1911), Drucker (1946, 1954), Ansoff (1965) and Chandler (1977) a central theme in the management literature has been on the ability of the manager to make, and implement, *any decision* by decomposing tasks and performing context-free analysis (as pointed out in Leavy & Wilson, 1994, Klein, 1998, Mintzberg, 1994 and 2004, Langlois, 1995). This trend continues (Porter, 1980 and 1985, Magretta, 2002). The economics literature on the firm follows a similar theme. (Coase, 1988, 35; Williamson, 1994; Simon, 1991; Hayek, 1973; Sautet, 2000; Foss and Foss, 2002.)

The alternate stream in the literature, the soft-stream if you will, has lacked a solid core. Largely starting with the famous Hawthorne experiments in the 1920s, but continuing through the works of partly neglected writers like Follett, Mayo and Maslow there was an emphasis on the importance of motivation and 'human relations' (Gabor, 2000). This trend was exemplified by MacGregor's Theory Y: 'In engineering, control consists in adjustment to natural law. It does not mean making nature do our bidding. We do not, for example, dig channels in the expectation that water will flow uphill; we do not use kerosene to put out a fire… With respect to physical phenomena, control involves the selection of means which are appropriate to the nature of the phenomena with which we are concerned. In the human field the situation is the same, but we often dig channels to make water flow uphill … trying to make people behave as we wish without concern for natural law.' (MacGregor, 1960, 8 and 9). The rule following perspective may allow for a possible solid, knowledge-based, core to this stream of literature. The purpose of the emphasis on the rule following perspective has been to suggest that without understanding business firms as complex rule-bound orders managers may be trying to make water flow uphill more often than they think.

Opportunities for further research.

The rule-based perspective of the firm, it has been suggested throughout this thesis, is under-explored. The possibilities for further research may be substantial. Horwitz writes: 'If the Hayekian-cognitive perspective on organizational learning … is worth pursuing, the next task will be to apply it empirically. Perhaps the most obvious research agenda would be to explore in detail how firms react to change … Such studies could focus on how new routines are formed and/or how old routines get adapted to new circumstances, with particular attention paid to the speed at which such learning takes place.' (Horwitz, 2008) Individuals within a firm will resist change because a change in the rules will affect their ability to predict the behaviour of others. Will others follow the same new rule or will they follow the old rule? Uncertainty about the rules reduces the amount of knowledge that can be used by that individual and that is available to the firm.

However, as we know, firms do change. But this process of change is complicated. Firm-wide change is not like changing the behaviour in an individual; it is changing a network or structure of relationships. (Hayek, 1952, 71) These rules are polycentric (that is each rule interacts with all other rules to a greater or lesser degree); a change to one rule will, more or less, affect every other rule. (Polanyi, 1951, 210) This network or structure is too complicated for any one person to master; 'The number of separate variables which in any particular social phenomenon will determine the result of a given change will as a rule be far too large for any human mind to master and manipulate them successfully.' (Hayek, 1952, 42) Given this complexity, it is no wonder that Hayek was dubious about the ability of anyone to change the behaviour of a complex order in a particular desired way: 'the insights which we gain from the study of society more often have a dampening effect on our aspirations…' (Hayek, 1978; 30). Change is an enormous burden on participants in any order. It requires each employee in a firm to change their zone of commitment; to change the rules that they follow, to risk feeling and looking, in the eyes of others, ridiculous, clumsy, socially uncouth, incompetent and, at the same time, to risk losing their ability to foresee the actions of others, to risk the loss of knowledge.

The individual participants in some orders may voluntarily recognize that the rules in their order have to change rapidly after integration and act accordingly. But this may not be so clear to individuals in other orders. And so, predictably, we end up with a situation where some post-acquisition integration processes are quite fast and, looking from the outside, relatively painless but others appear much more difficult. We can also see why to an outsider to the orders involved or even to members of the absorbing order, without an understanding of the consistency preference in rule following behaviour, the problem can seem like perverse employee resistance. (Roberts, 2004; see also for examples Vaara, 2001, 2002) But the rule following perspective would allow for a more favourable, coordination and knowledge retention, interpretation of events. A useful piece of research would be to study the speed of post-merger integrations and see if employee acceptance that change had to happen was correlated to faster integration and vice versa; in other words that internal commitment to change was at the core of any change process. If employees did not see any need for change then they would not be committed to it and change would not happen or could be slower than was hoped for. Certainly, Vaara (2002) has found evidence that the financial success of a to-be-merged entity, which may have led employees to think that no change was needed, slowed integration. The Jacob Fruitfield case study, where existing management in Jacobs Biscuits, which was always profitable, would not commit to the new order after acquisition but the employees in Fruitfield which had been loss-making would so commit, also supports this view. Vaara (2002) concludes: 'It is interesting to note that this mechanism, whereby financial success impeded integration, has received virtually no attention in the literature in this field. Rather, the model according to which successful integration creates benefits that are then reflected in improved financial performance dominates the literature. This is a major issue calling for future research in the field.' If this supposition were correct, it would allow for a possible reconciliation between the conventional post-acquisition integration literature and the 'need for speed' (see: Pautler, 2003; Harrison, 2007 Ashkenas and Francis, 2000; Early, 2004; Walt, 2005) and the rule based perspective. Successful acquisition would flow from the inner commitment of the individuals involved to change; that process could happen quite quickly. Therefore, the possible mistake in the conventional literature is not to see the importance of the invisible inner commitment of the individuals involved to change but to focus on speed of change which may be merely a visible *consequence* of this commitment.

This thesis would also imply that some work needs to be done with conventional methods of evaluating the success or otherwise of mergers and acquisitions; Roberts writes that based on stock market returns 'little or none of [the value from a deal] accrues to the acquiring firm'. (Roberts, 2004, 247) But without a full understanding of all the rule-based orders involved and how the merger or acquisition had resulted in change, if any, to those orders there is no way of knowing if the original transaction was a success or not. It is quite possible that an operation could be purchased for 100 and sold six months later for 150 and for the transaction to be a disaster and it is quite possible for the purchase to be for 100 and the sale six months later for 80 and for the acquisition to have been a brilliant success; the success or failure of an acquisition must not only take into account the monetary factors but also take into account the effects of the acquisition on the rule following orders involved. This piece should be taken as further support for the non-financial perspective in judging success or failure in mergers and acquisitions (Vaara, 2002). For example, in Danone, the Irish biscuit brands were just about profitable on their own, what was completely invisible was the cost in lost focus to the global brands in Ireland; the cost of the acquisition of the Irish brands in purely financial terms could never have discovered that.

While there has already been much work on the more complex cultural reasons for the success of firm mergers and acquisitions (see for example Vaara, 2002), the rule-based perspective would imply that this stream of work may require integration with the more traditional, rational, finance-based appraisals of success in the area (see Roberts, 2004). While it is clear that investment appraisals based on common accountancy, for example NPV or CAPM models, are useful; it may also be useful to think through that these models might throw up very different answers in different 'cognitive frames' (Witt, 2000). For example, some firms may ignore certain risks, others may factor them into calculations and other firms again may recognise them but view them as incapable of qualitative analysis; so we should not be surprised that, as Ghemawat points out, Citi, an organisation where global leadership was always a priority, had operations and investments in over 100 countries before it started to take country-risk ‘seriously’ (Ghemawat, 2007, 80). This then would imply that industry-wide appraisals of the ‘success’ or ‘failure’ of acquisitions etc are only of limited utility. A useful research project would be to assess how different firms make investment decisions where they use common techniques and to see if they actually apply these techniques in different ways and judge success in different ways as well. In other words, within each rule-based order, what is taken into account and what is ignored would frame every decision, even decisions that seem purely objective. Therefore, one of the consequences of the rule-based perspective would be an expectation that when working within their individual cognitive frames that one rule-based order will use apparently objective models in a different way to another order; they would include and ignore different factors.

Studies of rule following within firms - firm culture studies (Schein, 1994), decision-making theories (Klein, 1998; Kahneman et al, 1982; Shapira, 1997), leadership and followership studies (Hamel, 2007), studies of the learning within organisations (Senge, 1990), change-management (Hammer 1996; Welch, 2001), complexity theories (Stacey, 1996), emergent strategy theories (Mintzberg, 1994) and the resource-based view (Foss, 1997) - are somewhat fragmented areas. A focus on rule following as being foundational to all these studies might allow researchers to create some commonalities, particularly around rule learning, feedback, change, and other features of management practice. This might allow us to recast the management literature in a different way. For example, in Prahalad and Bettis's article on *Dominant Logic* (Prahalad and Bettis 1986), the authors argued that top management in a firm were a collection of individuals making decisions in a complex information-rich environment. '[M]anagers must be able to scan environments selectively so that timely decisions can be made.' The dominant logic also guides decisions: 'A dominant general management logic is defined as they way in which managers conceptualize the business and make critical resource allocation decisions…It is expressed as a learned, problem-solving behaviour.' Referring to feedback, pattern-recognition, heuristics and problem solving – the article may be susceptible to being recast using Hayek's formulation of rule following. However, without Hayek's insights the article could be considered to neglect the importance of rule following in allowing individuals predict the behaviour of others and the knowledge benefits that flow; instead the authors treated dominant logic as a problem to be overcome. A similar review of other influential contributions to the management literature from a rule following perspective may be a useful exercise.

It is only recently that economists have sought to crack open the production black box that is the business firm and investigate its hidden interior. The modern peek inside the firm started, largely, with Edith Penrose's thesis (1959) that every firm is a unique bundle of non-divisible 'resources' that the firm has acquired over its existence. These resources are now thought to comprise the 'routines' (Nelson and

Winter, 1982; Smith, 1776, Vol II, 345) of the firm and its wider ‘capabilities’ (Richardson, 1972; Prahalad and Hamel, 1990). One of the resources in every firm is the expertise of its management group. The management in a firm are a team and a limitation to the growth of a firm is the ability of this team to absorb new members (Penrose, 1959, 77). This resource based view, runs parallel to the transaction cost (Coase, 1988; Williamson, 1985, 1994 and 1996) or contractual view of the firm (Alchian and Demsetz, 1972; Grossman and Hart, 1985: Casson, 1995) where firms exist because the information processing abilities of the market come at a price and intra-firm coordination by command and hierarchy can coordinate at a lower cost – firms are ‘islands of conscious power in the ocean of unconscious cooperation like lumps of butter coagulating in a pail of buttermilk’ (Coase, 1988, 35)

It may now be useful to use the rule following perspective to take a more critical look at contractual and transaction cost theories of the firm. It should be clear that, for example, knowledge transfer costs are different in the market than in the firm; every firm processes information in different ways and so the processing costs of that information will be different in every firm and from the market – but it may now be clear that this may be merely a side-effect of the rule following perspective. The foundation for the contractual basis of the firm, given the rule-based perspective, would seem to be on shakier ground. One example of this would be to try to use the rule-based perspective to explain the origins of the modern business firm, without any contractual element. This leads us to the final piece in this thesis and an articulation of an interesting possible implication of the rule-based perspective.

A Mengerian or invisible-hand explanation for the origins of the modern business-firm.

In his *Principles of Economics*, first published in 1871, Carl Menger (1840 - 1921), using Adam Smith's simile of the 'invisible hand', but understanding it more deeply and more fully aware of its power, showed how money came about.

Step 1: Exchange.

Individuals, at some distant stage in history, discover 'the economic gains that can be derived from exploitation of existing exchange opportunities' (Menger, 2007, 257). For example, A has a sword but this has a 'smaller use value' (258) to him than a plough. B has a plough, but this has a smaller use value to him than a sword. A and B exchange the sword for the plough.

Step 2: The problem.

There is a problem resulting from this exchange opportunity: 'How rarely does it happen that a good in the possession of one person has a smaller use value to him than another good owned by another person who values these goods in precisely the opposite way at the same time!' (258)

Step 3: The solution.

'This difficulty would have been insurmountable, and would have seriously impeded progress in the division of labour, and above all in the production of goods for future sale, if there had not been … a way out.' (258) This way out was to interpose an additional transaction or transactions in the exchange process. A smith in ancient Greece has made a suit of amour of copper. He wishes to exchange this for food and for raw materials for his trade. It is unlikely that he will meet a person who wants to exchange food and copper ingots for a suit of armour. Therefore, our smith solves this problem indirectly. He exchanges his suit of armour for cattle, even though he does not need the cattle. Cattle are the most marketable commodity in ancient Greece. He then exchanges these cattle for food and copper ingots. In other words, our smith exchanges goods of limited marketability for goods of more or general marketability; this happens 'naturally' and 'everywhere' (260) people were guided by their own self-interest to the same solution.

Step 4: A refinement of the solution.

Over time, 'under the powerful influence of custom', certain goods become 'acceptable to everyone in trade and thus capable of being given in exchange for every other commodity.' (260) This good may change over time: for example, as a people becomes more urbanised cattle may lose their marketability and be replaced by a metal like copper or tin or gold.

Step 5: The influence of the state.

There is one final step in the origin of modern money: 'Within the boundaries of a state, the legal order usually has an influence on the money character of commodities which, though small, cannot be denied.' (261) However, this does not mean that one can go too far in looking for a role of the state in the origin of money: 'Money is not an invention of the state. It is not the product of legislative act.' (262) But the state can have a role, when the money character of a good has emerged: 'Thus the sanction of the state gives a particular good the attribute of being a universal substitute in exchange, and although the state is not responsible for the existence of the money character of the good, it is responsible for a significant improvement of its money-character.' (262) So gold coins issued by the state become acceptable to everyone and tin plate loses any former money-character.

In conclusion, Menger wrote: 'Money is not the product of an agreement on the part of economizing men nor the product of legislative acts. No one invented it. As economizing individuals in social situations became increasingly aware of their economic interest, they everywhere attained the simple knowledge that surrendering less saleable commodities for others of greater saleability brings them substantially closer to the attainment of their specific economic purposes.' (262)

Application to the origins of the modern business firm.

This explanation of the origins of money is what the American philosopher Robert Nozick calls 'an invisible hand explanation'; 'An invisible hand explanation explains what looks to be the product of someone's intentional design, as not being brought about by anyone's intentions.' (Nozick, 1974, 19) Hayek expressed the same concept in slightly different terms. Money, he argued, is just one example of many features of human life that have arisen ‘spontaneously’; there are many more such examples – Adam Smith showed how the market order arose spontaneously as a result of unintended consequences of individuals looking after their own interests. Human language, private property (Menger, 2007, 97) are two further examples. How could an invisible hand explanation allow us to conjecture a theory of the origins of the business firm? Again, we should approach the problem step by step. However, the problem is more complex, and the solution less visible, than the bilateral problem solved by money.

Step 1. The market order.

We have seen above that a market order arises spontaneously. As we have also seen, it arises naturally, spontaneously, because individuals follow certain common rules of behaviour. The larger this market order becomes, the more people that it involves, generally, the greater prosperity involved. For example, the division of labour can be finer in a large town than in a small village. Therefore, there is always the general tendency for a market to grow in size until, as we have now, it largely encompasses all of humanity.

Step 2. The problem.

But there is a problem resulting from this extended market order. Hayek argued that in the extended market order that the common rules of behaviour must become ‘attenuated’, that is they must be thinned out as compared to the rules of a small tribe where, for example, everyone is known to everyone else and everyone owes intricate duties to everyone else:

> ‘This application of the same rules of just conduct to the relations to all other men is rightly regarded as one of the great achievements of a liberal society. What is usually not understood is that this extension of the same rules to the relations to all other men (beyond the most intimate group such as the family and personal friends) requires an attenuation of at least some of the rules which are enforced in the relations to other members of the smaller group. If the legal duties towards strangers or foreigners are to be the same as those towards the neighbours or inhabitants of the same village or town, the latter duties will have to be reduced to such as can also be applied to the stranger. No doubt men will always wish to belong also to smaller groups and be willing to assume greater obligations towards self-chosen friends or companions… A system of rules intended for an Open Society and, at least in principle, meant to be applicable to all others, must have a somewhat smaller content than one to be applied in a small group.’ (Hayek, 1976, 88ff)

These rules, thinner or not, are, to a greater or lesser degree, common to all. This alone creates a problem. Individuals solve problems by following the rules; they guide our behaviour even in the most novel of situations. Different cultures have different rules and so will be guided in different ways: As Casson noted: ‘Since different values legitimate different objectives, and different objectives generate different kinds of problem[s], societies with different cultures will tend to focus on distinctive types of problem solving. “Learning by doing” is an important aspect of problem solving and so learning effects will give each culture a distinctive type of problem-solving expertise.' (Casson, 1995, 89)

It is obvious that an extended market order then creates a problem. If everyone in a market order follows, however approximate, the same rules (even if those rules are 'fuzzy' (Schlicht, 1998) at the edges), then there can only be a limited number of ways that any problem can be solved.

Step 3A. The solution.

'This difficulty would have been insurmountable, and would have seriously impeded progress in the division of labour, and above all in the production of goods for future sale, if there had not been … a way out.' This way out was for an entrepreneur to see or realise, however tacitly, that a problem could be solved in a new way. However, the entrepreneur cannot solve this problem directly but must approach it indirectly because he or she needs the assistance of others to realise this goal.

If the entrepreneur is to realise his or her vision to solve a problem with other individuals in a new way, some form of coordination must occur; in other words some form of common rules (however, fuzzy) must be created. This order is not created or designed by the entrepreneur; it is strongly influenced by him or her, 'a natural leader of *men*', (Marshall quoted in Streissler, 1990, 58) like a general, a Wallenstein (Roscher quoted in Streissler, 1990, 58), 'a cognitive leader' (Witt, 2000, Ioannides, 2003a). No person, however, ever 'creates' the order within a firm and this is why employers and firm owners are sometimes, even commonly, surprised at the behaviour of their employees and vice versa.

(One point worth noting, some early firms, it is submitted, were created to solve the opposite problem – the problem of a large number of different rule-based orders existing across a single trading territory. Post-offices, canal companies, the early railways (see for example, Chandler, 1977, 98), the Hudson Bay Company, resulted in the creation a common set of rules over an extended area where there were limited common rules of behaviour. This may also be a feature of some global or regional companies today. This early reason for firms and the more general reason, above, may confirm Chandler's conjecture that it was the great size of the US market and then its early cultural homogenisation that resulted in the early development of larger firms there (Chandler, 1977, 498))

(It also explains why having internal markets as a solution to the Hayekian knowledge problem within firms (Cowen and Parker, 1997; Koch, 2007), may miss the point of having firms in the first place. If intra-firm behaviour can be coordinated by market rules, why create a firm at all?)

Step 3B: The solution.

Simultaneously with Step 3A, other individuals make choices and act; they have their goals but realise that they can, however tacitly, only achieve them indirectly. These individuals realise that, in the long or the short term, their self-interest is served best if they do not sell their services, directly, into the larger market order. Instead, he or she realises that if they participate, if they commit, to the sometimes new but always changing order, outside of the market, in a firm that they may obtain benefits that they might not obtain in the larger market order and bring themselves closer to their personal goals.

One reason an individual may wish to become an employee is that it allows that individual the opportunity to convert what might otherwise not be an economic good into an economic good. (The individual is, of course, unconscious of this directly but is conscious of the higher remuneration available in a firm particularly early in a career and the individual also, as Hayek pointed out, may have a preference for assuming greater obligations towards certain self-chosen companions.) That good, that might otherwise not be an economic good, is the ability of humans to follow complex and usually tacit rules and the ability to follow different rules in different 'settings'.

Step 4: A further refinement of the solution.

Over time, under the powerful influence of custom, establishing firms, becoming an employer or an employee become well-established and profitable behaviours. Firms become common in the economy. The habits, skills and practices that are required of employees in a firm become more common; for example, punctuality, reading and writing. Further, the skills to manage and control employees in firms become more widespread – skills like double-entry bookkeeping.

Step 5: The influence of the state.

There is one final step in the origin of the firm: within the boundaries of a state, the legal order usually has an influence on the character of the firm which, though small, cannot be denied. There is no doubt that the legislative acts of a state can improve the character of firms in many ways and can improve the chances that firms will be created and that the individuals in them will prosper. However, this does not mean that one can go too far in looking for a role of the state in the origin of the firm: firms are not an invention of the state. The firm as a market institution is not the product of legislative act. But the state can have a role, when the firm has emerged as an economic institution: for example, individuals may be more inclined to establish a firm when there is limited liability, individuals may be more inclined to become employees of a legal fiction than of a particular individual. The legal personality of the firm has somewhat blinded observers to this fact; Sautet is right and the 'firm can be seen as a pulling together of entrepreneurial activity by a central entrepreneur… the essence of the firm, in that context, is coordination rather than ownership.' (Sautet, 2000, 134)

A Mengerian, an invisible hand, explanation of the existence of the firm as an economic institution.

In conclusion, we can follow Menger: a firm is not the product of an agreement on the part of economizing individuals nor the product of legislative acts. No one invented it. As economizing individuals in social situations became increasingly aware of their economic interest, they everywhere attained the simple knowledge that participating in a rule-bound order to achieve some purpose, however vague, where the rules are different to those in the larger market order brings them substantially closer to the attainment of their own individual specific goals.

The firm, as a market institution, arises naturally, spontaneously, in the larger market order. However, each individual firm is not a spontaneous order; it does result from human action and not human design but, unlike a spontaneous order, a firm is deliberately created to fulfil some purpose, however vague. Any rule following perspective 'blurs the distinction between spontaneous order and organization as proposed by Hayek.' (Ioannides, 2003) But at the same time the firm having a purpose, fundamentally, retains the distinction between what Hayek called 'an organization' and a spontaneous order (Hayek, 1973, 49); although Hayek's broad distinction between the former being coordinated by commands and the latter by rules is somewhat flawed (as Hayek himself immediately granted (1973, 49)). Ioannides (2003) makes the same point. The firm does have many of the useful features of a spontaneous order and, in particular, its rule based coordination mechanism allows it to cope with a dynamic environment: Richard Langlois is almost exactly right, firms 'emulate in some degree a spontaneous order.' (Langlois, 1995) This may refine Coase's (1988) conclusion: the firm does not 'supersede' the market but arises naturally as part of the market order but the solution to a problem within a firm may supersede a solution to the same problem in the market.

Conceptual and Practical Implications.

In order to try to demonstrate some of the implications of the rule following perspective this thesis focused on the change process around corporate acquisitions and disposals. However, the rule following perspective has implications for many aspects of intra-firm coordination. One practical implication of the Mengerian origins of the business firm may be to business strategy: each firm is a different solution to a particular problem in the market order. One firm cannot be a superior solution to every problem. Seeing the firm in this light has an important insight for strategy formulation and execution within each business firm. This limits the range of strategic opportunities that are open to any firm. This, it is submitted, may not be fully recognised in the strategy literature (see for example, Porter, 2008; Teece, 2007; Brady and Walsh, 2008 give further examples from the student textbook literature; Prahalad and Hamel (1990) could be seen as an interesting exception). For a firm to consider that the rules of its order can be used to solve every potential business problem in a profitable way is, given the Mengerian perspective, to misunderstand the purpose of firms in the market order.

For example, for over 20 years Xerox has been heavily criticised for not exploiting all the opportunities that arose from its PARC research facility (for example, the graphic interface first used commercially by Apple and now used in all computers, Adobe and 3Com technologies and many others); one book by two McKinsey consultants decried Xerox's efforts as *Fumbling the Future*. (see Chesbrough, 2002)

However, if we see a firm as a complex rule-bound order created to solve problems in a particular way, we can see that Xerox executives were almost certainly quite wise to allow many PARC technologies to be exploited outside Xerox. Many technologies may only be successfully exploited if problems are solved in different ways to the Xerox way. It is quite reasonable to assume that Xerox executives, at a tacit level, saw that and were quite happy for those teams to leave PARC with their ideas – *even if* the Xerox executives could have known that the ideas would lead to substantial commercial success. On the other hand, Laser printers may have been more consistent with the Xerox way; the technology arose in PARC and was successfully exploited within Xerox. Chesbrough and Rosenbloom (2002) criticised management in Xerox for evaluating 'the technical potential of these spin-offs through its own business model', its own cognitive frame or 'dominant logic'. But the Mengerian perspective would allow us to see Xerox's managers' actions in a different light; we could surmise that the managers saw the rules followed in Xerox as being suitable to solve the business problem of profitably exploiting some technologies and not others. Thus, some technologies they exploited within Xerox and some they spun-off into new firms with different rules.

Strategy is about making choices and the rule following perspective shows that pursuing every profit making opportunity, no matter how lucrative, is not available to every firm. The rule following perspective shows why this is, what kinds of opportunities are available, why these opportunities are different for every firm and why figuring this out is a complex process that only a person who is familiar with the order involved will be able to perform. To do otherwise may be to sin against the market process: a 'Blue Ocean Strategy' (Chan and Mauborgne, 2004) may be profitable and offer fast growth but not every blue ocean is open to every firm.

It is each employee's role to commit to learn and to follow the unique and largely tacit rules of the firm. A personal achievement, if done well, that is analogous to and as complex as becoming fluent in a new language. It is the manager's role to supervise this unique rule-bound order – to teach the rules and to provide feedback when individuals break the rules. It is a social task that stretches the edges of human achievement. The role of the leader, who can be at any level in the organisation, on the other hand, is to change the rules – this requires that practically every individual in the firm has to understand the new rules the leader wants followed and then for each individual to commit to those new rules; as Mary Parker Follett wrote: 'The leader gets an order followed first, because men really want to do the right things and he can show them that way.' (1940, 246) The successful leader's achievement is probably beyond the powers of any human being to describe. (Hayek, 1952)

Rule following, as Mary Parker Follett pointed out (1940, 59), is a different way of looking at firms, at employees in firms and management in firms. The social side of the firm is now paramount. The visible features of a firm, its processes, physical infrastructure, divisions, business units and articulated and actual strategies are merely the outward signs of the rule following behaviour of the individual participants in the order.

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