# A GROWTH ANALYSIS OF A SMALL WOOD PRODUCTS FIRM

A Thesis

Presented in Partial Fulfillment
for the Degree Master of Business Administration

by

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PREFACE

This study is an analysis of the organizational problems of the Hoge Lumber Company, New Knoxville, Ohio. The analysis is made primarily within the framework of current business growth theory.

Prior to entering The Ohio State University to complete my formal education, I was associated with this firm in various positions of production management. This experience provided me with an excellent background for my subsequent education in Business Administration. Throughout my formal studies, I have often related subject matter to problems and situations in this firm.

It is my belief that a major shortcoming of typical business analysis arises from the failure to correctly identify the firm within its growth cycle. In typical analyses the firm's condition is compared with the organizational variables which ideally exist in a mature organization. Such an analysis does not give proper recognition to the appropriateness of organizational characteristics in early stages of growth.

This thesis is an analysis which employs growth theory as its basic tool. The objective, as with all business analysis, is to identify problem areas, determine their causes, and develop recommendations for their solution.

The author's grateful appreciation is given to the owner-managers of the Hoge Lumber Company for their cooperation during the preparation of this thesis. I also wish to express my appreciation to Professor Irving Abramowitz who acted as adviser and to my wife, Marilyn, for her cheerful assistance in the preparation of the original draft and typing of the final manuscript.

Ned W. Hoge

Columbus, Ohio
June 4, 1965

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# LIST OF EXHIBITS

# INTRODUCTION

This thesis is a case study of a small wood products firm in Northwest Ohio. Primary emphasis is placed on the analysis of the firm within the framework of business growth theory.

## OBJECTIVES AND ORGANIZATION OF THE STUDY

### Objectives

The purpose of analyzing a firm is normally one of identifying the problems which the firm is experiencing in accomplishing its objectives and then making recommendations for their solution. The ultimate purpose is to develop conditions which will facilitate efficient and effective functioning of the firm. It is often recognized that when an analysis is completed, this ultimate objective is only half attained. The job of implementing the specific recommendations and initiating the changes called for is by far the most difficult portion of the entire undertaking.

It is my belief that a major shortcoming of typical business analysis arises from the failure to correctly identify the firm within its growth cycle. In typical analyses the firm's condition is compared with the organizational variables which ideally exist in a mature organization. Such an analysis does not give proper recognition to the appropriateness of organizational characteristics in early stages of growth. By failing to recognize this appropriateness, a "you're all wrong" connotation is unconsciously attached to subsequent recommendations. This implication then seriously hinders their acceptance and implementation.

The process of change is not easy, it involves both mental and physical considerations which are often deeply rooted in the organization. Changes are often resisted by the assertion that "our business is different". With respect to the firm's position in its growth cycle, this assertion may be justified. The characteristics of a small firm are and rightly should be different than those of a large mature firm. In an analysis which provides recommendations for change, these differences should be recognized.

Business growth theory provides a model which delineates three distinct stages of business growth. Key organizational variables are identified and their characteristics described for each of these stages. Between successive growth stages, periods of transition exist where important factors must be present. Growth theory identifies these factors and explains their role in transition.

This thesis is an analysis which employs growth theory as its basic tool. The objective, as with all business analysis, is to identify problem areas, determine their causes and develop recommendations for their solution.

There are several important advantages to this approach. Of primary importance is the perspective it lends to an evaluation of the firm's current situation. By comparing the existing conditions of key factors to those in each of the three stages of growth, the firm's position in its own growth cycle can be firmly established. Causes of problems become evident where the development of key factors are out of phase with one another. Recommendations can then be formulated for syncronizing these factors so that they will be in closer harmony. Finally, the use of this approach provides a better base of understanding for the recipients of the recommendations which should greatly ease the task of implementing them. This is of the utmost importance for only if the recommendations are accepted and implemented will progress toward the ultimate objectives of analysis be made.

Organization of the Study

This study is divided into six areas. In Chapter I, a chronological history of major events in the growth of the firm is developed. Changes in ownership and managerial personnel are traced throughout the life of the firm. Major changes in markets served are identified and the growth of the firm, as measured by annual net assets, net sales and total number of employees was determined.

Chapter II presents a concise picture of the current situation of the firm. The existing organizational structure and method of operation is described. Major divisions of activity are identified on a product basis and an estimate of the relative importance of these divisions is presented. An analysis of management personnel is developed which describes the background and current duties of each. Existing procedures and systems which link these personnel together are then described. The Chapter is concluded with an analysis of the firm's current financial condition.

At this point a concise picture of the firm has been developed. Chapter III and IV present a summary of the growth theory which is to provide the framework in which analysis is later accomplished. The growth model of Dr. Alan Case Filley is used in this thesis. Dr. Filley's model, which was developed as a doctoral dissertation at Ohio State University, describes three distinct stages of a firm's growth. A description of these stages and the transition periods between them is presented.

Chapter V develops a growth profile of the firm. Key business factors are examined to determine their present stage of development.

These are compared to establish the position of the firm in its growth cycle. This comparison identifies basic problem areas and prepares the way for the development of specific recommendations.

In the final chapter recommendations for basic changes are developed. These recommendations are based on guidelines set forth in the growth model. Detailed recommendations have not been presented and are beyond the scope of this thesis, however, recommendations for solving basic problem areas are outlined. In the closing section the timing and problems of implementing changes are discussed. This is an important part of any analysis because it addresses the question of when and how to implement the recommendations.

# CHAPTER I

# HISTORY OF THE FIRM

This chapter contains a brief history of the Hoge Lumber Company. The history was compiled by a thorough study of company records, trade journal and newspaper publications, and memoranda from the private files of owners. Personal interviews of the owner-managers were also conducted to fill in needed information. For purposes of discussion the history is broken down into six areas: (1) the founding of the firm, (2) relocation, (3) addition of owner-managers, (4) growth of assets, (5) growth of sales and (6) growth in number of employees.

## Founding of the Firm

The Hoge Lumber Company was founded in New Knoxville, Ohio, in 1904, by Herman H. Hoge. The founding resulted from Mr. Hoge's purchase of the entire stock of the New Knoxville Hoop Company, which was incorporated in 1900 to manufacture, sell, and deal in barrel hoops and barrel tubs. The short life of the Hoop Company was plagued by many difficulties. Before operations were well under way, the price of barrel hoops had dropped fifty per cent. Raw materials had to be hauled to the plant by horse drawn wagon and by 1903, suitable timber for hoop manufacture within hauling range, had been depleted. As a result, the stockholders decided to dissolve the corporation. Mr. Hoge was elected trustee to accomplish the liquidation and on May 28, 1904, the stock was offered on public sale where he purchased all outstanding shares.

The first few years of the Hoge Lumber Company were difficult. The market for elm hoops continued to decline. At the encouragement of local builders, Mr. Hoge started to stock pine lumber for siding and flooring. A supply of wood shingles was also inventoried. As the market for elm barrel hoops died out completely, the firm began manufacturing oak wagon wheel spokes and rims. These were supplied to a wheel manufacturer in a nearby community. Other products such as furniture dimension lumber and handle squares for wheelbarrows and earth scrapers were developed.

## Relocation

The mill was originally built on leased ground. The founder continued to lease the property for approximately four years. Then, feeling that the conditions of the lease were undesirable, he purchased a new location on the edge of the community and in 1908, moved the entire mill to that site. The new site was approximately two blocks from the original location and is the location which the plant occupies today. The move involved considerable expense and before operations could again be resumed, Mr. Hoge was $30,000 in debt.

## Addition of Owner-Managers

The firm continued to operate with Mr. Hoge as its only manager for the next eleven years. As his sons became old enough to work, they helped him in the summers and in the evenings after school. In 1919, the oldest son, Arthur Hoge, returned from service in the First World War and immediately went to work with his father full time. A short time later, the second oldest son, Gustave Hoge, also

EXHIBIT I

NEW KNOXVILLE HOOP FACTORY, 1902

joined the firm on a full time basis. The firm continued as a proprietorship until 1925 when it was incorporated. 300 shares were issued. 150 of these were issued to Herman Hoge, 75 to Arthur Hoge, and the remaining 75 to Gustave Hoge. Operation continued with three stockholders until 1935 when two additional sons, Joel Hoge and Oliver Hoge, obtained stock and began actively participating in the operation of the firm.

From this point on, the firm began to grow rapidly. The members of the firm felt it was undesirable to rely too heavily on wagonwheel parts as their only product and began actively to build houses, barns, and other farm buildings. Machinery was purchased for manufacturing residential and architectural millwork and the firm began supplying millwork for homes, schools, and other public buildings.

The founder of the firm, Mr. Herman Hoge, was active in the daily management until 1945 when he became semi-retired. He continued as President of the firm, however, until his death in 1962. As a result of the settlement of his estate in 1963, a portion of his stock was sold to a grandson, Mr. John Hoge, who has been active in a sales capacity since 1959. At present, ownership of the firm is distributed between the four sons and one grandson of the founder.

## Growth in Assets

The sawmill and other woodworking machines in the plant were originally powered by belts and line shafting from a steam engine. In 1932 an electric generator was connected to the engine and power transmission by line shafting and belts was replaced by electric motors. This first generator was soon proved unsatisfactory and in 1935 a larger steam engine-generator unit was installed. This unit is still in use today.

In 1938 the Hoge brothers began looking for an outlet for short pieces of lumber that were going to waste. The answer to this problem was found in the manufacture of brush backs for commercial type floor brushes and street cleaning brooms. In 1939, machinery was purchased for the manufacture of brushes and the Hoge Brush Company, a subsidiary, was started. Brush operations were begun in an old school building which was vacated the year before when a new community school was built.

The following year, 1940, the old boiler in the powerhouse was replaced by a new 210 horsepower watertube boiler. This boiler more nearly matched the requirements for the engine-generator unit which had been installed five years earlier. This boiler like the steam engine it serves is still in operation today.

In 1944, a cross-ventilation lumber dry kiln was installed. The kiln was the most modern type available at that time. To facilitate its use, a new storage yard for air drying of hardwood lumber was also built. As a part of this yard facility, a stacking pit was constructed and equipped with a twenty-ton hoist. Use of this hoist permits the lowering of lumber stacks so that stacking can be accomplished at a comfortable working height.

In 1946, a new showroom and office was built. The showroom provides space for complete display of the entire building products line including hardware and paint. Office space was provided for sales and accounting offices, and an office for trucking operations. The office building is equipped with a full heated basement for the storage of doors, plywood, paint, and other miscellaneous building supplies.

From 1948 to 1951 warehouse space was doubled by an addition to an existing storage shed and then redoubled by the construction of a ten thousand square foot, post free, warehouse.

In 1952 a second dry kiln was built, which increased drying capacity of native hardwood lumber by 130 per cent. As part of this same project a new roughmill building was constructed to provide enlarged space for processing lumber into rough blanks for subsequent machining operations.

In 1956 the firm faced the problem of equipping the entire plant with a sprinkler-type fire protection system. After considerable investigation and planning, it was decided that as an alternative to putting in this sprinkler equipment, a complete new fireproof manufacturing plant should be built. Construction was started in 1956 and completed in midyear 1957. Most of the manufacturing machinery was removed from the old plant, however, it is still used to house prefabricating departments for cabinets and building components. Upon completion of the new manufacturing building, a new, fire-proof powerhouse was built around existing power facilities and a large steel silo was added for fuel storage.

In 1960 the improvement of assets turned to the sawmill division, where the entire rear half was completely rebuilt with fireproof construction. This portion of the sawmill was enlarged in order to facilitate plans for completely conveyorizing the sawmill at a later date.

In the same year, a complete conveyorized layout was installed in the rough mill. Through the installation of this equipment, rough mill capacity was increased 300 per cent.[1] The following year, in order to supply sufficient materials to this new rough mill facility, the hardwood lumber storage yard was doubled, and the two dry kilns were placed on double shift operation.

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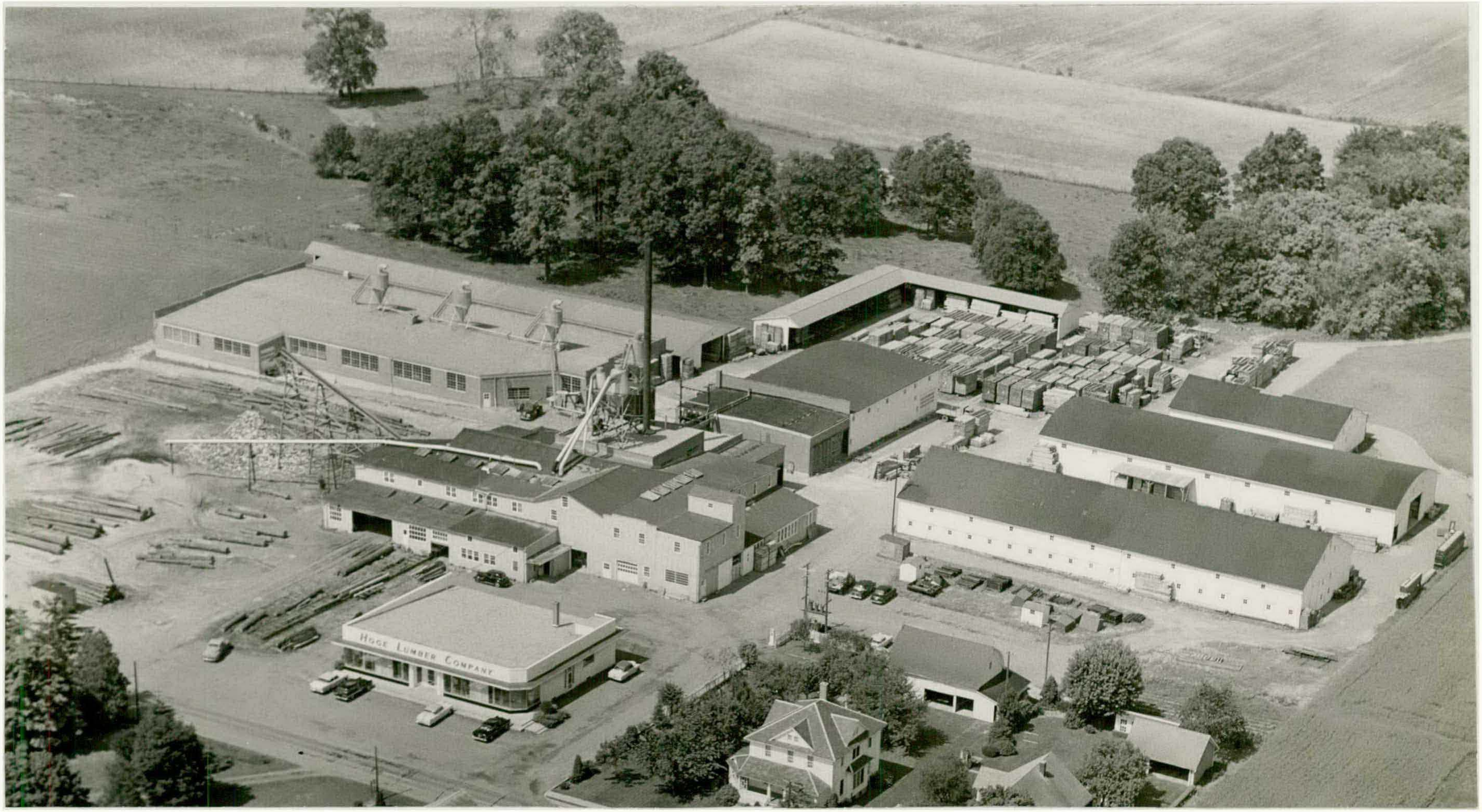
[1]Management estimate.

EXHIBIT II

HOGE LUMBER COMPANY, 1960



In 1962 with sales on the increase, a lumber predryer, for accelerated lumber curing, was built. This predryer extracts free water from green lumber and thereby cuts drying time, in the kilns, in half.

In 1963 attention again shifted to increasing efficiency in the sawmill. A new automatic riderless log carriage was purchased and a completely conveyorized layout was installed. A large fork-lift was purchased for delivering logs into the mill. Logs are now placed on loading chains which deliver them to the carriage and sawed lumber is moved by conveyors to all successive operations including the final sorting.

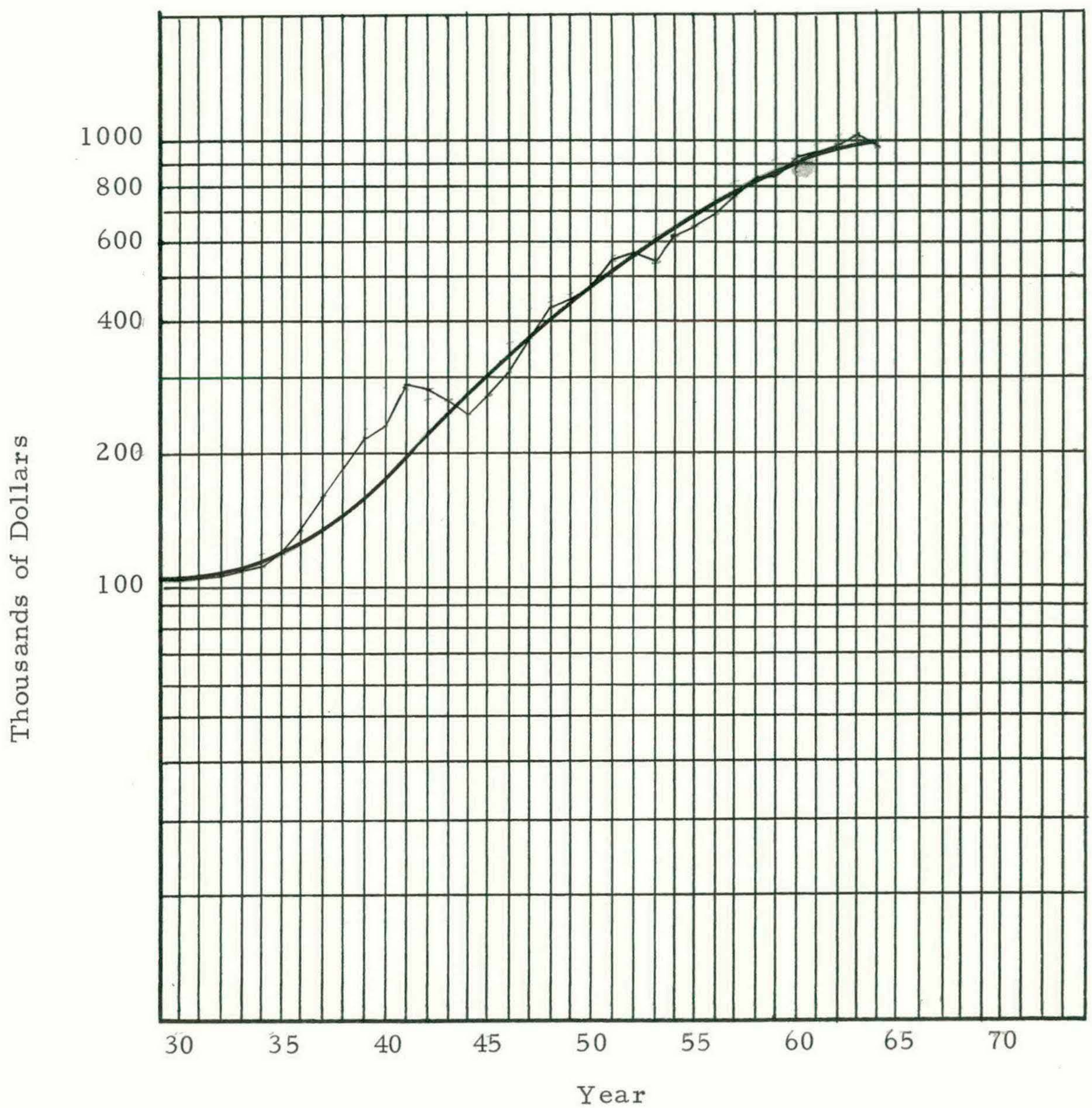
With the continuous addition of more modern equipment, the power output of the firm's generating plant became insufficient and additional electric power had to be purchased. Increased waste also became a problem. Faced with a large supply of waste for fuel but a lack of sufficient generating capacity, the owners decided to again increase the capacity of the power plant. In 1964 a 400 horse-power boiler and a 750 KVA turbine-generator were purchased and installation begun. This installation is currently reaching completion and plans are for it to be in operation by July of 1965.

In order to obtain a graphic picture of the rate of asset growth, company records were examined and net assets plotted from 1929 through 1964. Exhibit III indicates a relatively constant rate in net asset investment with some indication that the rate has been decreasing slightly in recent years.

The management team has tentative plans for additional expansion in the years ahead. Two proposed projects involve additional warehouse facilities. One of these would serve as a distribution point for laminated roof trusses. The company was recently selected by a large west coast manufacturer of these trusses to become a

EXHIBIT III

NET ASSET INVESTMENT, 1929-1964



distributor for its products in the central Ohio area. Sale of the trusses would be actively promoted by the manufacturer's representatives. It is generally felt that the new distributorship would be beneficial, due to the possibilities of stimulating sales of allied materials.

The second warehouse would serve the manufacturing division by providing storage space for dry hardwood lumber and work in process inventories between the rough mill and final machining operations.

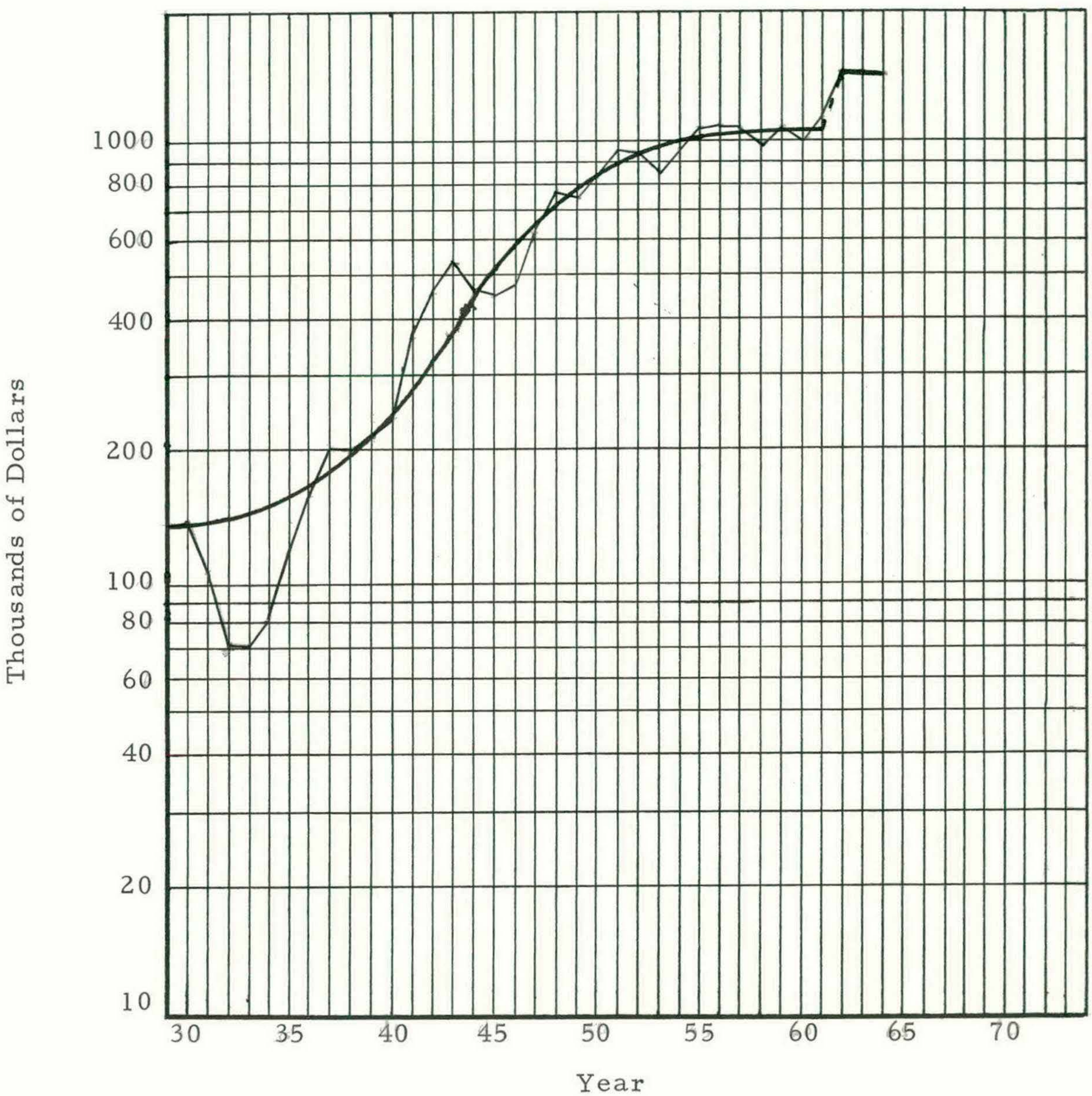
## Growth in Sales

Net sales of the firm have increased from $144,000 in 1929, to $1,650,000 in 1964. This is an average increase of $43,000 per year. Sales have grown in softwood lumber building materials and in products developed from native hardwoods. To obtain a graphic picture of the sales growth rate, annual net sales figures were obtained from company records and plotted for the years 1929-1964. Sales figures prior to 1929 were not available. As a result of the depression, ssles dipped considerably from 1930 to 1934. Since this dip was a function of over-all economic conditions and not a direct reflection of management decisions, it was ignored in fitting a growth curve. Exhibit IV indicates an increasing rate of sales growth until 1943. Since 1943, sales have been increasing but at a decreasing rate.

The reader will notice that the curve in Exhibit IV is fractured in the 1962 sales period. This was the result of the firm's entry into the bowling alley market. Bowling alley components were first developed in 1961. Initial reception of the firm's bowling line was very favorable and led to an intense effort to "cash in" on the 1962 season.

EXHIBIT IV

NET SALES, 1929-1964

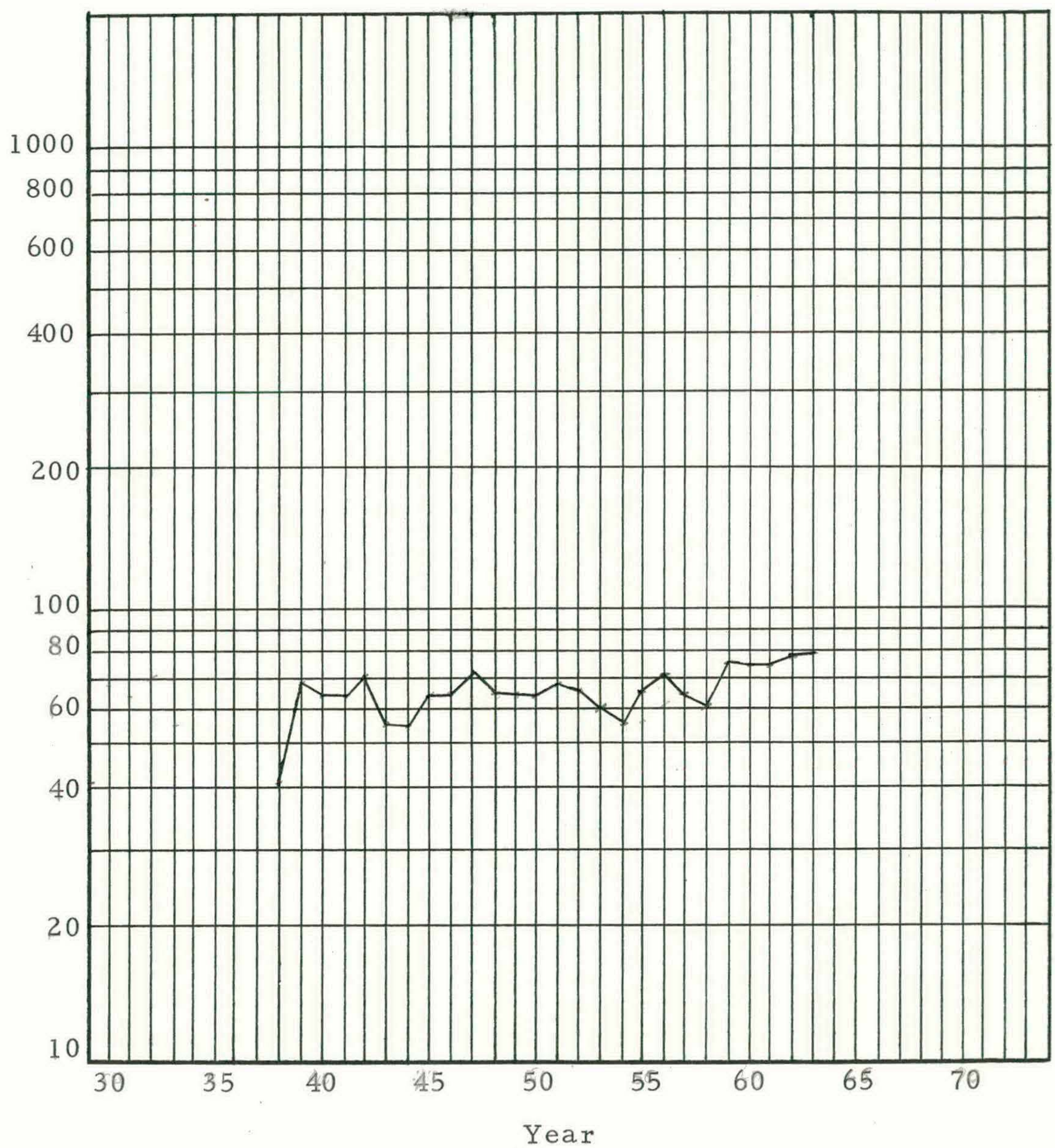


Employee Growth Rate

The total number of people employed by the firm for the years 1938 through 1964 were obtained from Social Security tax records. Total employees have never exceeded 80 persons. A substantial increase in employees in 1938 resulted from the starting of the Hoge Brush Company. Since that time, the number of employees has fluctuated around a mean of 65. Sales increases have been possible through increased productivity of labor-saving equipment. In the last five years, additional employees have been added so that the current total is 79. In talking with members of the management team, it was learned that employment may increase in the near future. In order to fully realize the sales potential of the firm, tentative plans are being made for the addition of a night shift in the manufacturing division. It is believed that this would be advisable because it would provide a broader base for the distribution of overhead costs and more fully utilize the capacity of present production facilities. There is some question, however, if a night shift could be managed successfully if present methods of supervision and production planning and scheduling are maintained.

EXHIBIT V

TOTAL EMPLOYEES, 1938-1964



# CHAPTER II

## THE CURRENT SITUATION

This chapter is an analysis of the current situation of the firm based upon actual observation of: (1) the existing organization, (2) its products, (3) its management personnel, (4) existing procedure and systems and (5) financial condition.

### Organization

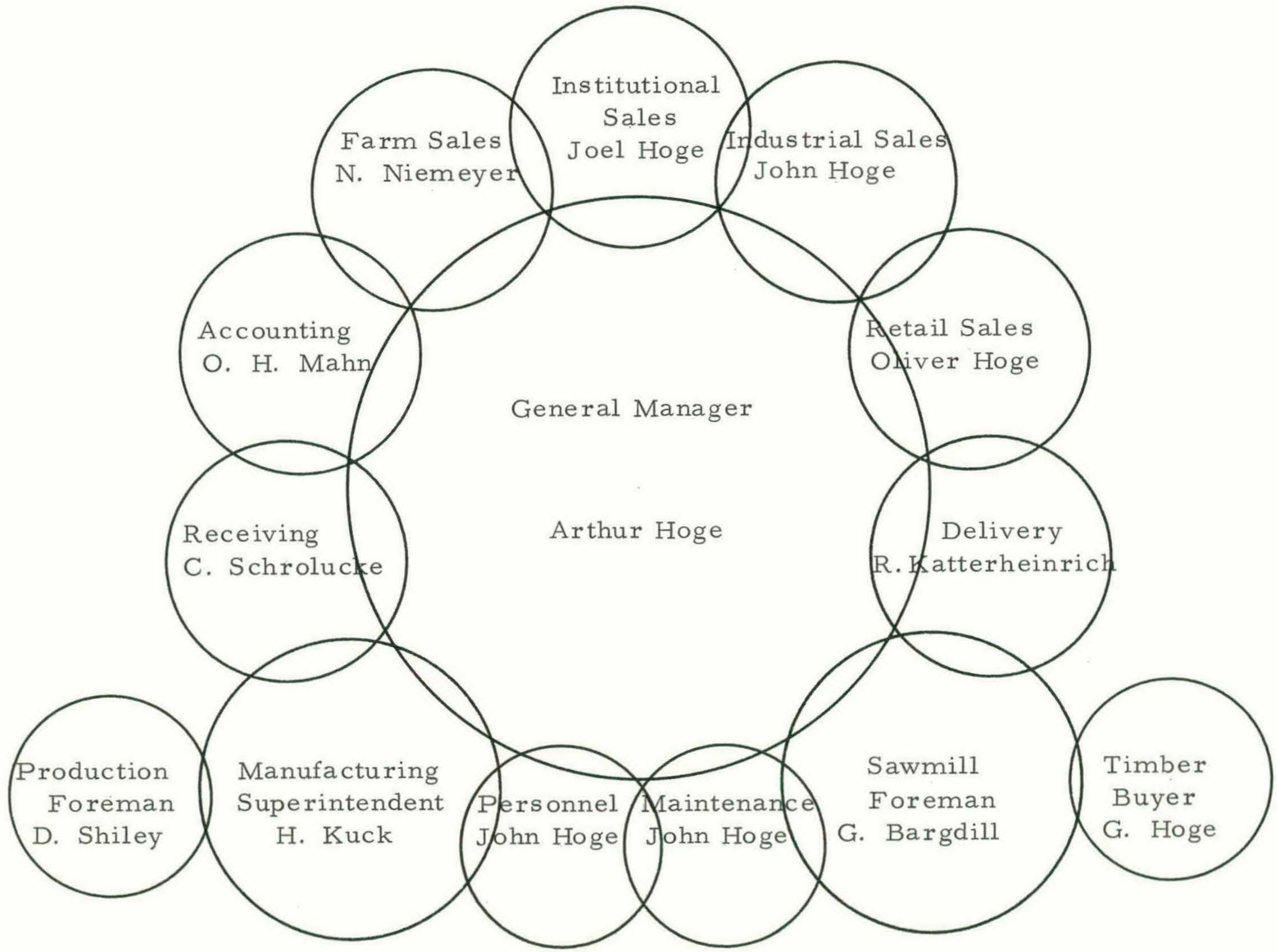
The firm is currently managed by five owner-managers. No organizational chart exists to define levels of authority and channels of responsibility and communication. Communication is informal with heavy reliance on face to face contact. The Board of Directors is made up of these same owner-managers who make all major corporate decisions. The Board meets once each month to discuss company plans and problems. Operating problems which are not resolved through daily informal contact are brought to these monthly meetings for consideration. Exhibit VI is an organizational chart of the firm. It was developed as a result of observations of the existing situation with respect to channels of authority responsibility and communications.

### Products

With the exception of the sales of the brush division, all records of the firm are kept in one consolidated set of accounts. Sales are not classified by either products or major divisions, but are tabulated each month on the basis of who wrote up the order. This basis is used

EXHIBIT VI

EXISTING ORGANIZATIONAL STRUCTURE



primarily because it is the only convenient way to break down the total sales figure. No use is made of this tabulation because management does not believe it accurately reflects sales effort.

Exhibit VII represents an analysis of sales by major divisions. This analysis is a management estimate based on the forgoing classification. The breakdown was possible because some sales personnel concentrate their activity in major areas. Where sales were made for more than one division, they were prorated on the basis of estimates made by the persons involved.

"Major divisions" for purposes of analysis were made to cover significant product areas and do not represent clear-cut divisions on either a market or managerial basis. Products noted are representative items and do not constitute a complete list.

## Managerial Personnel

Exhibit VIII is a summary of the management team, their position in the firm, age, and length of service.

## The Management Team's Responsibility and Functions

Following is a description of the management team's present responsibilities and the functions they perform. These descriptions are based on information obtained from questionnaires submitted to each member of the management team, from personal observations made during the study and from conversations held with each executive. No actual job description or organization chart exists to outline or describe these functions.

# EXHIBIT VII

## SALES ANALYSIS BY MAJOR DIVISIONS

| Major Division and Products | % 1964 Net Sales* |
|---|---|
| A. Manufacturing Division | 28.0 |
| Industrial and Commercial Products | |
| Truck Floor | |
| Wheelbarrow and Lawn Mower Handles | |
| Farm Machinery Parts | |
| Bowling Alley Components | |
| Brush Blocks | |
| Carpet Display Racks | |
| Institutional Millwork--Mouldings and Trim for | |
| Schools | |
| Churches | |
| Banks | |
| Residential Millwork--Mouldings and Trim | |
| B. Fabricated Millwork Department | 4.6 |
| Residential Cabinet Work | |
| Institutional Cabinets, Wardrobes | |
| C. Sawmill Division | 1.9 |
| Grade Lumber for Remanufacture | |
| Bending Oak | |
| Crating and Pallets | |
| D. Retail Lumber and Building Supplies Division | 34.0 |
| Residential Construction | |
| Farm Building Construction (Including Prefabricated Buildings) | |
| E. Hoge Brush Company (Subsidiary) | 31.5 |
| Floor Brushes | |
| Street Brooms | |

*Sales figures used to compute percentages do not include transfer prices between divisions. Divisional sales was estimated from a tabulation of sales on the basis of who wrote up the order.

EXHIBIT VIII

MANAGEMENT ANALYSIS

| Name | Position | Age | Length of Service |
|---|---|---|---|
| A. F. Hoge | General Manager | 69 | 46 |
| G. A. Hoge | Timber and Log Buyer | 66 | 46 |
| O. H. Mahn | Accountant and Office Manager | 58 | 37 |
| R. Katterheinrich | Delivery Foreman | 59 | 33 |
| H. Kuck | Manufacturing Plant Supt. | 56 | 32 |
| J. W. Hoge | Institutional Millwork Sales | 56 | 30 |
| O. H. Hoge | Retail Building Products Sales | 50 | 30 |
| C. Schrolucke | Receiving Foreman | 49 | 17 |
| N. Niemeyer | Farm Building Sales | 27 | 9 |
| J. H. Hoge | Industrial Sales | 33 | 6 |
| D. Shiley | Manufacturing Plant Foreman | 26 | 8 |
| G. Bargdill | Sawmill Foreman | 36 | 1 |

Mr. Arthur Hoge, General Manager

Arthur Hoge has been associated with the Company throughout his career. From the age of 16, he helped his father after school and on Saturdays at odd jobs around the sawmill. In 1919, upon returning from military service from the First World War, his father encouraged him to help with the operation of the firm. He has been actively engaged in managing the firm since that time. His primary background and interest has been in sales. However, as the firm has grown, he has become more involved in financial and general administrative areas. Since incorporation in 1925, he has served as Secretary-Treasurer of the firm.

Following is a list of activities he is currently involved in, the functions he actually performs and the subordinates he supervises:

1. General over-all management of the firm
2. Performs financial management and maintains creditor and banker relations
3. Coordinates salary and wage administration for management personnel
4. Determines selling and advertising policies for farm sales
5. Performs short-range sales planning
6. Sales of farm buildings
7. Sales to industrial accounts
8. Accepts telephone orders and maintains selling liaison with customers
9. Personally grants credit and supervises over-all credit and collections activities
10. Expedites his sales orders to delivery or production departments
11. Performs product development and improvements (currently promoting a new line of products for recreation and park facilities)
12. Makes spot checks for inventory purposes
13. Approves purchase requisitions from the plant
14. Interviews salesmen, negotiates contracts and maintains liaison with major suppliers

15. Issues purchase orders for the following materials:
    (a) all hardwood and softwood lumber
    (b) all large quantities of plywood hardboard and insulation board
    (c) all capital equipment purchases
16. Direct supervision of the following management personnel:
    (a) Oliver Mahn, Accountant and Office Manager
    (b) Ned Niemeyer, Farm Sales Manager
    (c) John Hoge, Industrial Sales Manager
    (d) Carl Schrolucke, Receiving Foreman
    (e) Ray Katterheinrich, Delivery Foreman
    (f) Gerald Bargdill, Sawmill Foreman

Mr. Gustave Hoge, Timber and Log Buyer

Mr. Gustave Hoge has also been associated with the Company throughout his career. He has been primarily involved in plant operations, serving first as a manufacturing division foreman. Upon the semi-retirement of Mr. Herman H. Hoge in 1945, he assumed the full management responsibility for sawmill operations. He held the position of sawmill manager until September of 1964 when he became semi-retired. Daily operation of the sawmill is now under the direction of a sawmill foreman who reports to Arthur Hoge. Gustave Hoge currently performs all timber and log buying and generally supervises land and woodlot holdings of the firm.

Following is a list of the activities he is currently involved in, the functions he actually performs, and the subordinates he supervises:

1. Estimating and bidding on timber purchases
2. Negotation of timber contracts with woodlot owners
3. Negotiation of purchase contracts with independent timber buyers
4. Maintains liaison with all timber and log suppliers
5. Scheduling of log hauling by independent loggers
6. Produces special order items in the shop
7. Operates production machines in the sawmill for short periods

8. Performs maintenance and odd jobs around the sawmill
9. Provides minor supervision of the sawmill foreman

Mr. Joel W. Hoge, Institutional Woodwork Sales Manager

Mr. Joel W. Hoge has been directly associated with the Company since 1930 when he obtained a B.S. degree in Architectural Engineering from The Ohio State University. His primary background and interest has been in sales and over the years he has been actively involved in sales of farm buildings, residential construction and institutional millwork.

Currently, his primary area of activity is in the sale of institutional millwork. In 1963 following the death of the founder of the Company, he was elected President of the firm.

Following is a list of the activities he is currently involved in, the functions he actually performs, and the subordinates he supervises:

1. Determines selling and advertising policies for the institutional millwork market
2. Performs all estimating and submits bids on institutional millwork contracts
3. Negotiates institutional millwork contracts
4. Accepts telephone orders for miscellaneous building materials
5. Processes all customer complaints pertaining to his own sales
6. Determines by-out items on package jobs and initiates purchase orders for special items
7. Makes spot checks for inventory purposes
8. Initiates purchase orders for the following materials:
   (a) structural iron and steel
   (b) builders' hardware
   (c) finish hardware
   (d) glass
   (e) insulation
   (f) mouldings
   (g) plywood
   (h) fiberglas
   (i) doors
   (j) windows

9. Performs all drafting work of shop drawings for institutional millwork orders
10. Answers technical questions by shop personnel relative to shop drawings and other fabrication problems.
11. Creates and initiates process and procedures improvement in the fabricated millwork department
12. Performs salary and wage administration for employees in the fabricated millwork department
13. Supervises three operative employees in the fabricated millwork department

Mr. Oliver H. Hoge, Retail Sales Manager

Mr. Oliver Hoge became a stockholder in 1935 and has been active in the operations of the firm since that time. He was initially involved in the supervision and expediting of residential construction and gradually worked into residential and remodeling sales work.

He is currently in charge of all residential construction and retail building product sales. Following is a list of the activities he is currently involved in, the functions he actually performs, and the subordinates he supervises:

1. Sales of custom built housing
2. Determines selling and advertising policy for the residential and building products market
3. Custom housing design
4. Design of residential custom cabinet work
5. Performs estimating and drafting work for residential construction
6. Accepts telephone orders for all building products
7. Perform counter sales of building products
8. Processes customer complaints pertaining to his own sales
9. Initiates purchase requisitions for building materials
10. Maintains liaison with fabricated millwork department, fabricated building department, and a manufacturing division with respect to his own sales orders
11. Direct supervision of:
    (a) Three operative employees in the fabricated building component department
    (b) two retail order processors
    (c) one building products counter salesman

Mr. John Hoge, Industrial Sales Manager

Mr. John Hoge is the son of Arthur Hoge, the General Manager of the firm. He has been associated with the firm since 1959 when he terminated a position as a research chemist with the Union Carbide Corporation of Charleston, West Virginia. John Hoge holds two B. S. degrees from The Ohio State University; one in Mechanical Engineering and the other in Chemical Engineering. Upon graduating from the University in 1955, he became associated with the Union Carbide Chemical Corporation in Charleston, West Virginia, where he served as a research textile engineer until 1956. He then became a research polymer chemist developing new testing methods for evaluation of polymers to determine their mechanical properties and possible use as a synthetic fibers. In 1957 he began research with primary emphasis on dyeable polyesters and high-tenacity copolymers. His initial duties when coming with the Lumber Company, were the assumption of the industrial sales responsibility. He currently performs the bulk of industrial sales and is involved in many other activities as listed below:

1. Sales to industrial accounts
2. Performs short-range sales and production planning
3. Processes quotations for industrial sales
4. Determines selling and advertising policy relating to industrial sales
5. Accepts telephone orders for building and industrial products
6. Personally grants credit and supervises the credit and collections function related to his sales
7. Expedites sales order to delivery and producing departments
8. Processes customer complaints pertaining to his own sales
9. Maintains creditor relations
10. Determines by-out items on package jobs and initiates requisitions for special items

11. Makes spot checks for inventory purposes
12. Interviews salesmen for shop tooling and maintenance supplies
13. Purchases shop supplies, new tooling and varnish for the manufacturing division
14. Performs product design
15. Performs special machine and tool design for the manufacturing division
16. Responsible for plant operations of the manufacturing division
17. Maintains liaison with the manufacturing division with respect to all industrial orders
18. Interviews prospective plant employees
19. Performs salary and wage administration for manufacturing and sawmill division employees
20. Supervises:
    (a) manufacturing division plant superintendent
    (b) sawmill foreman
    (c) maintenance crew on major maintenance projects and special machine building

Mr. Oliver Mahn, Accountant and Office Manager

Mr. Mahn first became associated with the firm on a part-time basis. He initially assumed the bookkeeping function but quickly became involved in retail sales work. He has been associated with the firm on a full-time basis since 1928. Prior to coming with the firm, he attended a business school, with emphasis on bookkeeping and accounting work.

Mr. Mahn is currently the accountant for the firm and generally supervises the performance of office work involved in billing and pricing of the firm's large variety of products. Following is a list of his activities and responsibilities:

1. Maintains a general accounting system of the firm
2. Maintains accounts payable file and issues checks in payment
3. Checks billing and pricing of sales invoices
4. Performs follow-up collections on slow accounts
5. Operates the firm's cost accounting system

6. Attempts to do office work that others neglect to keep things straightened out and running smoothly
7. Prepares all tax returns
8. Prepares annual financial statements
9. Direct supervision of one office clerk

Mr. Ned Niemeyer, Farm Sales Manager

Mr. Niemeyer has been associated with the firm since 1956. He was hired as an assistant to Mr. Arthur Hoge, and initially was involved in drafting, estimating, and minor sales work for the farm building market. He is currently the farm sales manager and is responsible for the bulk of the farm building sales volume.

The following is a list of the activities he is currently involved in, the functions he actually performs and the subordinates he supervises:

1. Farm building design
2. Estimating and selling to the farm market
3. Performs counter sales for building products
4. Accepts telephone orders for all building products
5. Dispatches sales order to delivery and production departments.
6. Processes customers complaints in the field with respect to construction and/or materials
7. Initiates purchase requisitions for needed building materials
8. Interviews supplier salesmen on items needed for the farm building market
9. Answers technical questions by shop personnel relative to shop drawings and other fabrication problems
10. Directly supervises:
    (a) lead man in the prefabricated building department
    (b) subcontractors

Mr. Howard Kuck, Plant Superintendent

Mr. Kuck came with the firm in 1933 when he terminated six years of employment as a masonry tender. His initial duties were in timber cutting and log hauling activities. As the firm expanded its millwork operations, he became a production machine operator and soon advanced to assistant foreman. In 1945 when Gustave Hoge assumed the full management of sawmill operations, Mr. Kuck succeeded him as superintendent of the millwork department. Since that time he has been the key figure in manufacturing operations. As the firm grew, the scope of his activities expanded accordingly. The activities he is currently engaged in and subordinates he supervises are as follows:

1. Prepares all production orders for the manufacturing division
2. Maintains scheduling list of all production orders in the plant
3. Prepares shop drawings when not supplied by customers
4. Prepares cutting schedules for the rough mill department
5. Prepares schedules for lumber drying
6. Performs short-range production planning
7. Creates and initiates process and procedures improvements
8. Performs product development and improvement
9. Dispatches production orders to machine operators
10. Answer technical questions by all shop personnel relative to shop drawings and other fabrication problems
11. Determines and administers quality standards
12. Interview prospective plant employees
13. Performs salary and wage administration for manufacturing division employees
14. Makes spot checks for inventory purposes
15. Interviews salesmen of mill supplies
16. Initiates purchase requisitions for
    (a) paint, varnish and other finishing materials
    (b) shop supplies, including hand tools and sandpaper
17. Designs and constructs production tooling
18. Performs tool maintenance
19. Performs machine setups

20. Produces special order items
21. Supervises minor maintenance jobs
22. Directly supervises:
    (a) rough mill lead man
    (b) manufacturing division foreman
    (c) receiving foreman in the performance of lumber drying responsibilities
    (d) 20 operative employees in the manufacturing division

Mr. David Shiley, Manufacturing Division Foreman

Mr. Shiley became associated with the firm in 1957, immediately after finishing his high school education. He was initially employed as a maintenance worker involved in new plant construction and rebuilding of the firm's powerhouse. In 1959 he was transferred to the manufacturing division as a machine operator. He quickly became skilled at operating a large variety of woodworking machinery, and in 1962, became an assistant to the plant superintendent.

Following is a list of the activities he is currently involved in, the functions he actually performs, and the subordinates he supervises:

1. Dispatches work orders to machine operators
2. Directly supervises machine operators
3. Expedites orders through the plant
4. Answers technical questions by shop personnel relative to shop drawings and other fabrication problems
5. Initiates production process and procedures improvements
6. Supervises minor maintenance jobs
7. Performs minor maintenance work
8. Performs machine setups
9. Initiates purchase requisitions for shop supplies
10. Supervises shipping
11. Bills out-materials shipped by commercial carrier
12. Operates production machinery for short periods
13. Produces special order items
14. Performs many minor duties as an assistant to the plant superintendent

Mr. Raymond Katterheinrich, Delivery Foreman

Mr. Katterheinrich began work with the company as a truck driver in 1932. He served in that capacity for several years until it became necessary to have a full-time delivery foreman. He has served in that capacity ever since. Mr. Katterheinrich's activities are as follows:

1. Schedules deliveries of all stock and manufactured items which are to be delivered by company trucks
2. Directly supervises three full-time truck drivers
3. Supervises the maintenance of the firm's trucks, semi-trailers and forklift trucks
4. Makes spot checks for inventory purposes on all softwood lumber items

Mr. Carl Schrolucke, Receiving Foreman

Mr. Schrolucke first came to work for Hoge Lumber Company in 1946 as a delivery truck driver. He worked in that capacity until 1951 when he left the firm to become a service station operator. In 1952 he returned and worked as a machine operator in the manufacturing division. In 1956 as the firm entered a major remodeling and expansion program of its physical facilities, Mr. Schrolucke became a maintenance crew leadman. He performed in that capacity until 1958 when he again became a machine operator. A year later, he was promoted to the position of lumber inspector and receiving foreman which is the position he currently holds. The activities he is engaged in and the subordinates he supervises are as follows:

1. Inspects and tallies all incoming lumber
2. Supervises the yard crew in lumber stacking and drying operations
3. Initiates hardwood inventory records
4. Controls dry kilns
5. Performs minor maintenance work

6. Initiates purchase requisitions for required supplies
7. Substitutes as delivery truck driver when inspection and yard work is slack
8. Substitutes as relief engineer in the powerhouse
9. Directly supervises two operative employees who do stacking and move lumber to and from the dry kilns

Mr. Gerald Bargdill, Sawmill Foreman

Mr. Bargdill is the newest member of the management team, being with the firm approximately one year. Prior to coming with the firm, he operated his own sawmill. He was hired to assume the day-to-day management responsibilities of the sawmill, upon the semi-retirement of Gustave Hoge. He reports directly to Mr. Arthur Hoge, although he receives some instruction from John Hoge and minor supervision from Gustave Hoge. The activities which he is engaged in are as follows:

1. Classifies and sorts all incoming logs on the yard
2. Scales and grades logs for cost purposes
3. Directly supervises five operative employees in the sawmill
4. Coordinates sawmill output with lumber yard foreman
5. Creates and initiates process and procedures improvements
6. Processes customer complaints relative to custom sawed logs and lumber
7. Operates a large forklift truck for handling logs
8. Operates machine for short periods
9. Makes spot checks for inventory purposes
10. Performs maintenance work

## EXISTING PROCEDURE AND SYSTEM

A procedure is the method or the manner in which the company, through its personnel, accomplishes the work necessary to manufacture and sell its products. The following is a brief outline of the general procedure of receiving, processing, and general flow of customer orders in the company. The various other existing systems or the lack of them will be presented in the chapter dealing with recommended solutions to the various problem areas.

## General Procedure

1. Sales Originate from:
   (a) phone orders
   (b) mail orders
   (c) sales calls

2. Sales Orders are Written by:
   (a) A. F. Hoge
   (b) J. W. Hoge
   (c) O. H. Hoge
   (d) John Hoge
   (e) Ned Niemeyer
   (f) Counter salesman
   (g) Receptionist
   (h) Truck Drivers

3. Sales Order Copies Dispatched to:
   (a) General files
   (b) Accounting Office
   (c) Delivery Foreman
   (d) Production Office or Sawmill Foreman

4. Stock Items are Shipped by Company Truck Within a Few Days

## Production Order Procedure

1. On items produced in the fabricated millwork department, the salesman taking the order prepares a production order and shop drawings and dispatches them to operatives in the fabrication and retail order shop.

2. On items to be produced in the manufacturing division, the salesman taking the order dispatches one copy of the sales order and any customer furnished blueprints to the production office.

3. The production superintendent prepares a production order for all items produced in the manufacturing division.

4. Copies of the production order are dispatched to:
   (a) Production office files
   (b) Accounting department for accumulation of cost data
   (c) A third copy serves a route sheet to follow the order in production

5. The production superintendent prepares cutting orders for the rough mill. Copies are dispatched to:
   (a) Production office files
   (b) Rough mill machine operatives
   (c) Rough mill tally man

6. Shop superintendent makes shop drawings for all nonstandard products. (Where required)

7. Shop superintendent estimates materials required on each job and instructs materials handlers to deliver them to production at the time they are required.

8. New production orders are dispatched by either the shop superintendent or the shop foreman to machine operators.

9. Machine operators return route sheet for all finished order to the production office.

10. The shop superintendent, shop foreman, or the shipping clerk, prepare and bill all orders to be shipped by commercial carrier.

11. Shop superintendent, or the shop foreman, notify the delivery foreman of all finished orders to be shipped by company truck.

12. Delivery truck drivers bill all items shipped by company trucks.

## FINANCIAL CONDITION

The Company is a privately-held corporation owned and controlled by five owner-managers. All owners are active in daily management of the firm.

The assets of the Company are financed by funds provided by trade creditors, spontaneous credit, common stock and retained earnings. This conservative financing is a result of a corporate policy which is opposed to long-term debt or outside equity financing.

The following is a percentage analysis of the liabilities and owners equity section of the balance sheet as of December 31, 1964:

| | |
|---|---|
| Taxes payable | 1.80% |
| Accrued Wages and Salaries | .62% |
| Accounts Payable | .54% |
| Notes Payable | 25.30% |
| Capital Stock | 3.04% |
| Paid in Surplus | 6.10% |
| Retained Earnings | 62.60% |
| Total Liabilities and Owners' Equity | 100.00% |

The Company's credit rating and bank relations are excellent and it is afforded liberal credit terms from its major suppliers. Notes payable are held by the owner-managers and their close relatives.

The Company has a current ratio of 2.5 to 1. Profits before taxes were only 2.6% of sales and 1.9% of sales after taxes. The return on equity was 4.5%. The profitability pictured by these ratios is somewhat misleading due to the salary structure of the firm with respect to officers' salaries. The firm's average collection period on accounts receivable is 43 days. Sales volume in 1961 was approximately 1.7 times total assets. The following is a percentage analysis of the assets of the firm:

| | |
|---|---|
| Cash on hand and in the bank | 6.06% |
| Accounts Receivable | 19.40% |
| Notes Receivable | .16% |
| Prepaid Items | .71% |
| Inventories | 44.25% |
| Fixed Assets | 25.00% |
| Real Estate | 4.00% |
| Investments | .42% |
| Total | 100.00% |

The asset position of the firm is unusual since a very high portion of total assets are in the form of inventories. A partial explanation of this is the high degree of vertical integration practiced by the firm. The inventory figure represents investments in standing timber, green hardwood lumber, manufactured working process, finished manufactured goods, a complete line of softwood lumber and miscellaneous building products. A breakdown of inventories was not available; however, Mr. Arthur Hoge stated that due to the length of the drying cycle for hardwood lumber, it was necessary to maintain large inventories in the drying yard.

# CHAPTER III

# A GROWTH MODEL

## The Purpose of the Chapter

The purpose of this and the following chapter is to present a growth model that will provide a framework for analysis of the problems of the firm. By comparing conditions within a firm to those in the growth model, it is possible to identify the source of many current problems and to anticipate additional problems the firm will face as it continues to grow.

The model used in this thesis was developed by Dr. Alan Case Filley in his doctoral dissertation on "A Theory of Small Business and Divisional Growth".[2] This chapter is a summary of his growth model. Chapter V provides a summary of the changes which key organizational factors undergo, as Dr. Filley has identified them, in each stage of a firm's growth.

## The Growth Model

This model presents an integrated and logically consistent pattern of growth for a firm with a single product base. Limiting the theory to firms with a single product base permits the use of

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[2] Alan Case Filley, "A Theory of Small Business and Divisional Growth" (unpublished doctoral dissertation, The Ohio State University, Columbus, Ohio, 1962).

measures such as total sales, assets, and employment as measures of growth within that base. A firm with several product bases, on the other hand, might well find itself with different bases in different stages of growth, thus compounding the difficulty of allocating costs or employment to particular product segments. Three stages of growth are indicated, with special attention to the points between each where the growth rate increases or declines. As each stage is discussed, attention is focused upon basic management factors, so that the change in each factor is noted as the business moves into a new stage of growth.

Stage I -- "Small Business" Stage

The first stage of growth may be classified as the "small business" stage. "Small business" is used here to describe the method of operation rather than the relative sales volume or number of employees. It probably includes a majority of the small retail, service, and jobbing establishments in the United States, as well as other types of enterprise in their first few years of existence.

The firm in the small business stage has one or two owner-managers with a few employees reporting to the owner or owners. The relationship between the owner and his subordinates is direct and personal, with no evidence of a formal organization. What exists is a simple line relationship in the first stage of line devolution. The group resembles a large family organization with each person acting in a traditional assigned role. There is closeness and frank communication between the members of the business "family" but an unwillingness to disclose business information to outsiders.

The typical small business has no idea of progress. Success is measured by comparing the present with the past. If the firm made more profit or had greater sales this year than last, then the operations are felt to be successful. The owner-manager is largely unaware of business methods used by other similar enterprises, unless provided with these methods by his trade association, wholesaler, or supplier. His attitude is one of long-run fatalism, feeling that things won't be much better in the future than they are now. Often he blames his lack of progress on some special group. For example, interviews with small businessmen who showed no apparent evidence of growth yielded the following statements about farmers ("they get rich for doing nothing"), unions ("you can't make a profit when the unions eat it up with wage demands"), and the government ("they spend their time catering to big business because it finances their campaigns").

A free market economy provides anyone the opportunity to risk his capital in a legal venture. One would normally expect that the small, inefficient nongrowth firm would be driven from the market by its larger counterpart. There are apparently three main conditions under which the small nongrowth firm may exist in the market: (a) the existence may be temporary; (b) the existence may be protected; (c) the firm may have a competitive "niche" in the marketplace. In the first place, the firm may be unable to survive and may simply exist temporarily until its eventual failure. For example, 60 per cent of all service establishments, typically small business, fail within two-and-a half years of business; 64 per cent of all retail establishments fail in the same period.[3] Secondly, the firm may be

[3] Department of Commerce figures in Statistical Abstract of the United States, 1959 (Washington: U.S. Government Printing Office).

permitted to exist by larger members of the industry through protection of umbrella-pricing or some other means. Such practices are sometimes stimulated by fear of the larger firms that reduced prices and number of suppliers would stimulate government antitrust action. Finally, the firm may have found a competitive "niche". Examples of this situation are a neighborhood grocery with a monopoly on a small neighborhood area, or a carpentry shop that specializes in heat-laminating Formica counter tops, or a plumber who specializes in installing gasburning lawn lamps. Such firms may be able to give faster, more specialized, or more convenient service desired by the consumer, even at a higher cost.

The competitive advantage may be explained further. The small firm is able to specialize in a minor service, doing a job well that might not otherwise be done. Its overhead costs are low because of size and because it does not have to share the overhead burden as it might if part of a larger organization. This is the case, for example, in a company which specializes in packing bulky items for shipment. The small firm is often exempt from wage or tax provisions that would fall on a larger counterpart, and is less in the public eye.

Whether or not the firm desires to grow, it can not grow until it overcomes certain traditional characteristics of the small business. These have to do with its management and organization. Traditionally, the small firm has no organization objectives that are apart from the objectives of the owner-manager. These are to "make a living" for its owner and to continue in business. Policies, too, depend upon the day-to-day whims of the chief executive and upon lessons that he had learned from his experience. Like policies, plans change from day to day with no long-run goal to give them meaning and direction. Policies and plans are not put in writing.

The few written records of the small business are largely financial. As one small business manager said, "The only reason that we keep records is because the government makes us do it for tax purposes." Yet the owner-manager has difficulty explaining what portion of his income was an imputed return on his investment, what portion was rent on his property, and what portion was wages paid to himself. If he were to do this, he might find that his income was below what could be earned if he invested his funds and worked for someone else. In any case, he need cope with no great risk or uncertainty, hence demands no great reward.

The leadership of the owner-manager is likely to be a routine, trial and error type. He tends to be an independent sort of person who enjoys having his own firm and being "on his own". He does not want to be told how to do his job. When asked if he would like to attend lectures on small business problems, he is likely to say that he is too busy, or that his is the kind of business that one has to "learn by experience." The owner-manager's main talent is likely to be on some functional area like selling, manufacturing, or purchasing. There is little evidence of the performance of management functions of planning, organizing and controlling.

The employees of the small firm look upon their jobs as rather routine. They may know and respect the owner-manager, but he does not instill any crusading desire in them to work hard and build the firm. They simply work their required job and meet the day-to-day problems that come along. Whenever there is more work to be done than can be handled by the present employees, the owner will add new people. He will not have any particular job or worker specifications in mind for employment guides; rather, he will hire just because he is too busy. One would expect to find, under these conditions, that the proportion of sales per employee would not change significantly, so long as the nature of the business did not change.

The organization structure of the small firm is defined informally or by custom. The jobs at the top are filled by the owner and his family and any supervisory positions that exist are likely to be filled by long-time lieutenants who have the title of supervisor but little authority. In a typical small firm all employees will report to the owner. With large firms in this stage, there may be levels of supervision, though supervisors are chosen more for personal than for rational business reasons. Such staff functions as are performed will usually be done as a part of a line employee's job. The only staff differentiation that will commonly appear will be in a secretary or part-time bookkeeper.

Morale is not likely to be a problem since employees will not expect anything better and will simply perform within their traditional roles. Employees know what is happening in the business and work closely with the owner, so that communication is good in all directions. Similarly, the lack of a hierarchy and the absence of close supervision by the owner will avoid serious morale problems.

Unless conditions change considerably, the small firm may continue to operate in the fashion just described until it dies through insolvency, sale, or termination by the owner's death or withdrawal. It may even grow through fortitudinous external circumstances or minor internal changes by the owner, but it will not enter what could be called a "take-off."

## Disequilibrium and Take-Off

For the firm to leave its traditional "small business" stage of growth it will have to establish certain basic conditions. These conditions introduce a disequilibrium into the otherwise equilibriated business. Where before the organization was a closely knit family of interests, now there will be strong personalities with diversified interests. Where before the rate of saving and investment roughly paralleled the rate of output, now the income and output will rise at a faster rate than an also increased rate of investment and saving. Where before it was felt that the business would continue in much the same way until its demise, now it is clear that revolutionary changes can be made to take place.

The basic preconditions that are necessary if the take-off is to take place appear to be the following:

1. An innovation
2. An entrepreneur
3. Capital
4. Risk and uncertainty
5. Reward for assuming uncertainty
6. The desire to change
7. Supporting economic services
8. Proper environment

1. An innovation. If rapid growth is to take place, there must be an innovation which can be exploited. This innovation may take the form of a new good, a new method of production, a new market, a new source of supply of raw materials, or a new market position.[4] A new method, for example, may be one which enables the production of a higher quality of goods at the same cost, or the same quality at a lower cost, or the same quality at the same cost but in greater quantity in the same or less time.

An innovation may be a kind of invention, but it might also be the recognition of a heretofore unexploited market opportunity.

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[4]These are patterned after Schumpeter's classification of innovations. Joseph Schumpeter, The Theory of Economic Development (Cambridge: Harvard University Press, 1934), p. 66.

This distinction between invention and innovation is stressed because the person who invents is not necessarily the same person who exploits or promotes the innovation. History is full of examples of promoters (entrepreneurs) who took inventions that had been ignored and exploited their real potential.

2. An entrepreneur. An entrepreneur is a dynamic, self-seeking, promoter type of person who thrives on activity, risk, competition, profit, and power. He may exploit an idea developed by an innovator, or he may simply recognize the opportunity in a new market or process. Examples of the latter would be the promotion and development of a market arising from population changes or resource discovery.

It is unlikely that the owner-manager of the first stage will be of the entrepreneurial type, so that an entrepreneur will have to be introduced into the organization if the take-off is to be realized. In some cases the organization is begun by the entrepreneur at the beginning of the second stage of growth, so that the first stage will not take place at all.

3. Capital. The take-off can not be financed from the retained earnings of the first stage of growth, although such earnings are an important source of funds once the growth is begun. The rate of net investment must increase to pay the cost of increased fixed and working capital needs. For this reason, the savers in the economy must be willing to provide money for investment. Equity capital or bank credit must be made available. It is expected that if the funds are available, they will be drawn easily to this form of investment because of the high marginal efficiency of capital arising from the unique profit opportunity. Profits will be high because costs will lag behind prices. The factors of production that are required will be priced at a rate corresponding to the price of those in the rest of the economy.

4. Risk and uncertainty. Rapid growth can not take place without the existence of risk or uncertainty. When uncertainty does not exist, there can be no great reward. And, in the absence of excessive profit reward, the entrepreneur does not appear. When risk and uncertainty are removed, rapid growth is absent.

5. Reward for assuming uncertainty. There must be a sufficient profit opportunity in the exploitation of an innovation to reward the entrepreneur for the assumption of the uncertainty involved. Where the reward for assuming uncertainty does not exist, then no entrepreneur will be interested in accepting it. Both the provision of capital and the reward for the assumption of uncertainty therefore indicate the need for some degree of unequal distribution of income. Without the risk or uncertainty or the opportunity for riches, there can be no investment capital nor reward for great deeds.

6. The desire to change. Obviously, if a take-off is to occur, the people involved in its accomplishment must believe that change is possible and desirable. This is no mean feat if the employees of the firm have been imbued with the long-run fatalism that is characteristic of the first stage of growth. Generally, the idea of and desire for change are instilled in the employees by the entrepreneur. They identify with him and believe that he will benefit them. They foresee business growth, better job opportunities, and greater reward for themselves.

7. Supporting economic services. The term "social overhead capital" has been used in studies of economic development to refer to basic social requirements that serve many businesses, not just one. Such would be transportation systems, power sources, communication media, schools, hospitals, roads. Just as these

become the underpinning of economic development as a whole, so they and other more specific conditions also become important to the single firm. For example, the opening of a seaway may provide access to new supplies of raw materials. Or, the exploitation of a new household device may require the advertising media to reach the consumer and the transportation facilities to get the device to the buyer.

8. Proper environment. Finally, there must be an environment in which the economic, political, and social conditions are favorable to growth. For example, the government can suppress certain forms of business ownership and operation. It can, within limits, control the flow of funds into certain sectors of the economy. The philosophy of the country will affect the willingness of its population to change and advance. A related situation is industry control by a few firms. If the take-off is to occur in an already existing industry, the degree of market control by competitors may affect the realization of the new growth. All of these conditions have some effect on the ability to achieve a take-off.

If all of these factors can properly jell, the firm will increase its rate of growth, entering the second stage of growth.

## Stage II -- Dynamic Stage

The second stage of growth may be called the dynamic stage. It is a period of rapid, sustained growth of assets, sales, and number of employees. The pessimism of the first stage gives way to a prevailing philosophy of optimism, engendered largely through the leadership of the entrepreneur. The group is heterogeneous, with employees of widely differing personality, training, and goals. All work together for business success.

The objective-setting pattern in the second stage is much different from that of the first. Instead of viewing success in terms of comparison with the past, the entrepreneur of the second stage will set optimistic goals for future growth or profit and then measure business success against progress toward these goals. The goals are still personal, however, measured in terms of "his" profit from "his" business. He generally wants his employees to share in the expected rewards also, since he feels that they are his "friends" and would like to see them benefited.

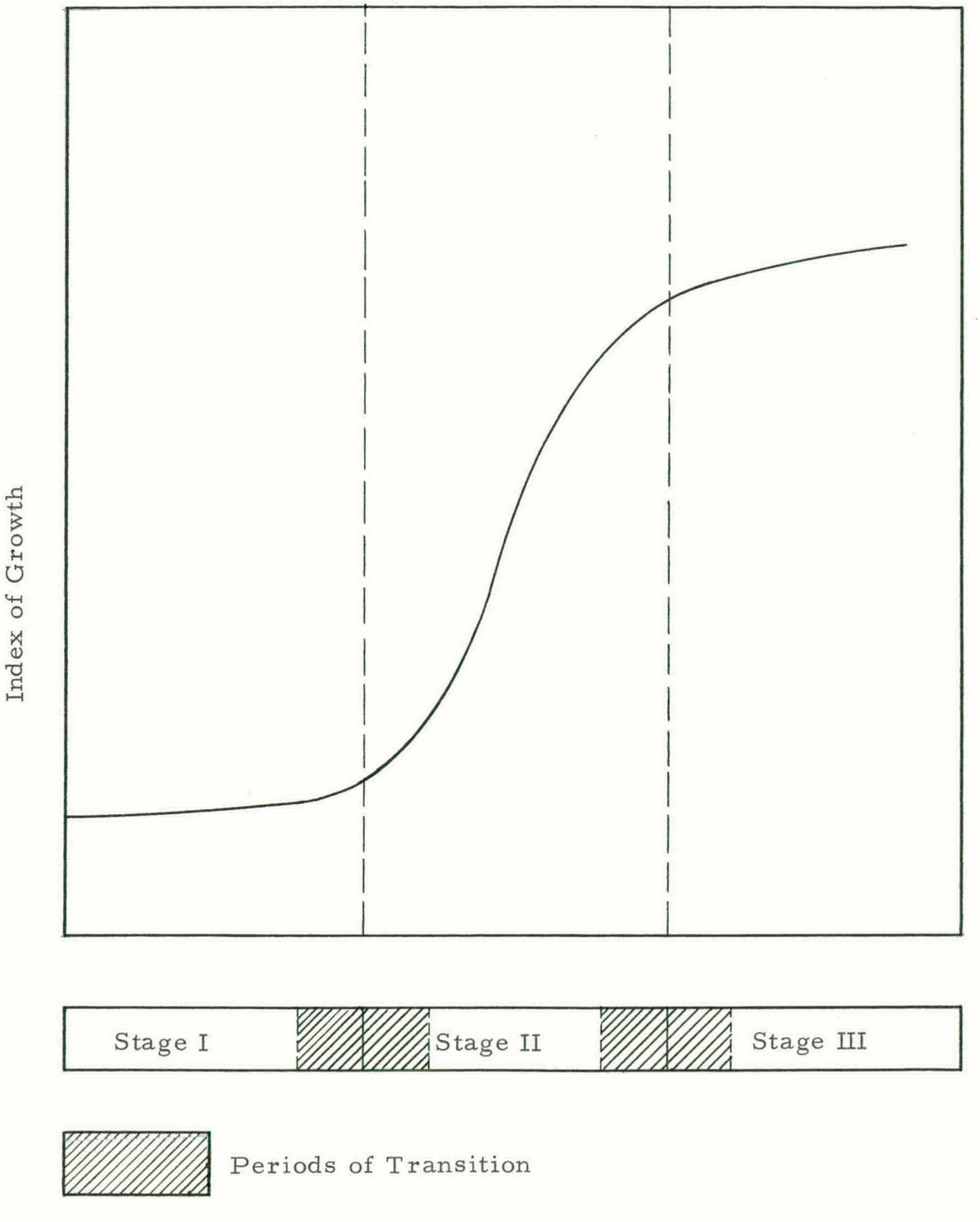
The firm pursues these objectives by exploiting the sales opportunities for its products. It often values immediate sales above a longer-run development of the market. An example of this would be the willingness to offer costly services or cut prices to get sales. In its haste to gather the fruits of its innovation there is little time for the subleties of planning, control, or the development of weaker functions. Policies are changed according to the whims of the entrepreneur. Written policies and procedures are absent. Few records are kept.

As the organization grows, the entrepreneur adds able lieutenants in various functional areas, who surround him like a field of force. As one entrepreneur put it, "After things got rolling, I just sat in the middle and pulled the strings." The emphasis by the entrepreneur on brining strong specialists into the firm pays off eventually, as the firm gains a reputation in the industry for superior knowledge and service.

The rate of investment, increased at the take-off, is expected to continue at the higher rate. Profit margins on sales are high during the dynamic stage since factor prices are at the market while the innovation yields a higher price from the high degree of product

EXHIBIT IX

STAGES OF GROWTH



differentiation. This margin will reach a peak sometime in the middle of the stage; then it will decline as other firms introduce close substitutes and force a lower price through competition. At such time the firm may resort to further product differentiation. Since sales will increase more rapidly than investment during this stage, the sales to asset ratio will increase. The high profits will be reinvested in the firm to finance further growth. Growth is costly in terms of its drain on working capital, so that even though the firm is constantly increasing its income, it will experience a shortage of working capital.

The entrepreneur is willing to subject himself to the risk and uncertainty of dynamic growth largely because he is unaware of what he is facing. Since he minimizes the difficulties that lie ahead, and enters the situation with optimism, he expects to become a "millionaire" in a few years and cheerfully hopes to similarly reward those loyal followers who aid him in his efforts. This stereotype of the entrepreneur frequently builds financial empires with a sort of "hip pocket" operation; records are written on the back of matchbook covers and stuffed in a pocket; the business may be run from a small, cluttered corner of a rented building.

The entrepreneur is quite unlike his predecessor, the owner-manager, in that he has no illusions about his "born right" of leadership or his intellectual superiority. He respects the ability of his technicians and generally rejects the adage that "experience is the best teacher." His employees are motivated to follow the leadership of this entrepreneur for many reasons. Some are poor and hope to raise their income; some are dissatisfied with themselves and choose to identify with the stronger personality; others are ambitious and recognize the opportunity provided by the situation. All tend to identify with the head man, however, rather than with the organization itself, and all bear the stamp of his personality. Even though there will be many strong, independent individuals in the organization, and even though conditions will be changing rapidly, morale will be high.

The total number of employees in the company will increase as sales and assets increase, though not as fast. Since the rate of output will surpass the rate of increased employment, one may expect to find an increasing ratio of sales per employee during this stage.

The nature of the innovation being exploited or the nature of the particular talent of the entrepreneur are such that the growth of the firm in the second stage is largely within one function. Quite often this function is sales. In some cases where a device is protected by patent, yet under strong demand, then the function may be production. As the stage progresses, the product base will broaden with other products added to the line, utilizing the technology developed initially in the product base. Also, as the stage progresses, the strength of other functions will be increased, so that by the time the firm reaches maturity, it will be strong in all of its major functions.

The organization structure of the second stage of growth is characteristically a flat one. This flat structure contains few levels and wide spans of control. Since the leadership talents of the entrepreneur are of a person-to-person rather than an executive type, the levels must not be so many that it is difficult for the entrepreneur to make contact with every member of the organization. Even though the organization chart shows three or four levels, it is expected that any of the employees have easy access to the entrepreneur.

The constantly widening span of the entrepreneur places such a demand on his time that he will extend his capacity by using general staff assistants. These staff assistants serve as extensions of his personality, acting in his name. The use of more specialized technical and coordinative staff will be held until the firm develops a rational organization structure.

The strong-willed entrepreneur will delegate responsibility to subordinates as the organization grows and develops. He tends to retain authority, however, until the firm begins to develop sound general administrative management. In sum, the growth in the second stage is largely the result of innovation and an entrepreneur, both of which contribute to the stage of disequilibrium and rapid progress.

## Equilibrium and Maturity

The point of maturity is much less easily defined than the point of "take-off." It is not the unique jelling of certain components, as was the take-off. Instead, it is the establishment of a new kind of equilibrium. This equilibrium may be established in several ways. It may occur in steps during the end of the second stage of growth, especially if the entrepreneur is also imbued with management talents. The equilibrium may be established rather suddenly at the end of the second stage. Or, it may be established during several crises after rapid growth is completed.

Nevertheless, there are several characteristics of maturity that help one to determine when it has been reached:

1. Stable rate of investment
2. Stable employment
3. Stable sales
4. Full functional development in a rational organization structure

5. Effective administrative and operative management
   (a) planning
   (b) organizing
   (c) controlling

1. Stable rate of investment. The rate of net investment is expected to decline to a minimum at the point of maturity, although gross investment may be high just to replace worn-out equipment. Productivity may increase somewhat from this new equipment, when it is more efficient than that which it is replacing.

2. Stable employment. Total employment will also stabilize at the point of maturity. After reaching that point, both line and staff employment will remain in the same proportions of total employment.

3. Stable sales. The rate of sales will level off at the point of maturity. Should the firm desire to increase sales further, it will have to do so by increasing its investment, and since sales will increase at only the same rate as investment, to do so will not normally be productive.

4. Full functional development in a rational organization structure. By the time that the firm reaches maturity it will have developed strength in all of its major business functions. It will be able to effectively create, distribute, and finance all of the products in its product base. Major staff functions like personnel and purchasing should also be performed well. A rational structure will provide the necessary support for successful maturity and future growth.

5. Effective administrative and operative management. The mature firm will have instituted the necessary requirements for sound administrative and operative management. First, it will have executive leadership at the top levels capable of planning, organizing,

and controlling the operation of the entire business or of major parts. Second, it will have at its middle and lower levels the necessary operative management to plan, organize, and control the operations of various lesser functions and organization units. Third, both of these groups of managers will utilize a sound company philosophy, including certain basic objectives, planned policies and procedures, a decentralized organization, and required controls. In short, the principles of sound management as they are known today will be applied.

## Stage III -- The Stage of Maturity

By the time that it enters the third stage of growth, the firm has become a large, complex organization. The dynamic period of growth which preceded it will be replaced by a period of stability, during which time the organization becomes institutionalized. The entrepreneur exercising face-to-face leadership will have been replaced by executive leaders who perform the management process of planning, organizing, and controlling. Attitudes will have become more conservative. Action will be undertaken only after rational consideration of its consequences.

In order to operate profitably in the third stage of growth, the firm must function as a well-constructed machine. It can not overcome the inefficiencies of growth with rapidly increasing sales. With sales stabilized, it must reap the profits of its growth efforts by reducing costs and introducing economies of operation. These savings are the result of attention to its organization and management.

In a few cases one finds a firm which was begun at the third stage of growth. One of the best examples is the U. S. Steel

Corporation, which was formed in 1901 through the consolidation of eight major steel companies. Presumably, each of the eight companies would have gone through at least one of the first three stages of growth before this move. The combined firm grew much more slowly than its competitors and was noted for its full publicity of affairs and its fair dealing with smaller competitors.

As the firm becomes institutionalized, it develops an organizational philosophy of management. As an important part of this philosophy it sets out certain organizational objectives, as opposed to the personal objectives of those connected with it. As a firm, it wants to provide the customer with sufficient value so that the public will allow it to grow and continue profitable operations. The provision of this salable value enables the persons participating in the firm to gain their own wages, dividends, salaries, or other rewards.

The mature firm will have written policies to guide the activities of various parts of the enterprise toward its objectives. The responsibility for the policy-making function will lie with the chief executive committee. Policy-making is much more likely to be a group process in the third stage, for the organization will have become so complex that it is difficult for one man to consider all its aspects.

The third stage is marked by the addition of specialized staff personnel who aid line management in planning, and control. Matters like production control, cost control, budgeting, or replacement analysis are seldom considered in depth when a company is devoting its efforts to meeting the demand for its products, but they are extremely important once the firm has exploited its market opportunity and must rely on efficiency and economy for increased profit. It is also characteristic of the third stage that all planning be done with greater futurity. The firm has to map its major strategy for future operations.

Having reached maturity the marginal efficiency of capital will be reduced unless the firm can add additional growth sectors or unless its market position is secure enough to warrant satisfactory margins. Its capital needs will have been reduced, particularly for working capital. The sales to assets ratio should be stable on the average.

By the time the third stage is reached the dynamic, obsessive entrepreneur either becomes or is replaced by a more deliberate professional manager. To the entrepreneur the firm was an organism to be kept alive and exploited, to the manager it becomes a well-planned and ordered mechanism to be kept in working order.[5] The professional manager is not likely to be a major owner in the company; instead, he runs the company for the benefit of the stockholder and other interested groups. Management is a group process in this stage. Management groups provide the necessary conservative and thorough consideration of important matters. They provide an important tool for communication at a time when face-to-face leadership is insufficient. Without them it would be difficult to keep the various parts of the firm moving in the same direction.

By the time the organization reaches maturity, clear-cut descriptions of responsibility and authority will have been developed

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[5]This is similar to a statement made by the following authors although they use different definitions for entrepreneur and manager, failing to see their true significance in growth stages. Alfred D. Chandler, Jr. and Fritz Redlick, "Recent Developments in American Business Administration and Their Conceptualization," Business History Review, Vol. XXXV, No. 1 (Spring, 1961), p. 4.

and employees will have been hired to meet these definite employment standards. One expects to find that employees are more skilled, technical, or professional than was true in the earlier stages. Although they fit into more definite job categories, the employees are more alike as a group; that is, they are better indoctrinated with a single philosophy and are held together by this kinship.

Employees in this stage identify with the company and the job rather than with the entrepreneur. They tend to view their jobs as contractual relationships in which they cooperate in an economic system in order to reach their own objectives. Thus morale in this stage is maintained by the similarity of interests rather than by the dynamic stress of the second stage. Once maturity has been reached, line and staff ratios remain the same and sales per employee are fairly stable. The scale of operations may vary somewhat but the proportions will remain fixed.

The organization structure of the third stage tends to be longer than it was in the second. Responsibility and authority are delegated, spans of control are reduced, and new levels of middle management are created. Then top management truly has the time to reflect upon the future, setting objectives and establishing basic policy. Middle management levels take over the job of coordinating the complex of functions, and supervisory management handles day-to-day affairs. The company must decentralize in this manner if it is to handle the new problems of maturity.

It is interesting to note that the process of organization and the introduction of sound management systems all serve to eliminate risk and to reduce uncertainty--the factors upon which the reward of the entrepreneur was based. Instead, the organization becomes better informed and less inclined to gamble on the future.

But what is the future of such an organization? Once it has achieved maturity and benefited by its efficiency, then several courses of action are open to the mature firm:

1. First, it may grow old gracefully, probably becoming something very close to the traditional "small business" type of firm. With designs and processes fixed and regularly declining demand for its products, the firm can operate with a minimum of staff or middle management until its eventual demise.

2. Second, the old product base may be purposefully liquidated over a period of time, and a new product base introduced to take its place. So long as the old base is able to break even it may be operated so that it can carry part of the overhead and continue to operate on depreciated equipment.

3. The old product base may continue to grow though not at its earlier rapid rate. The firm may continue to rely on internal growth through the addition of product improvements, the introduction of cost-saving machines or practices, or the extension of its market.

4. The firm may elect to expand the old product base as previously explained, and also add new product bases. Thus it may have different parts of the firm in different stages of growth.

5. The firm may choose to grow externally through acquisition or merger with other companies. This growth often permits economies of scale or creates a more preferred market position so that additional profits may be made.

6. The owners of the firm may sell it to another company, freeing the funds for new investment. Where the company is still in the hands of an entrepreneur, he may then embark upon another type of exploitation.

7. It will be recognized that there are many other combinations as well. The ones mentioned would appear to be the most common, however.

## Summary

The growth model sets forth what has been called a growth cycle. This cycle is in three stages: a stage of equilibrium in which the firm has the characteristics of traditional small business: a stage of disequilibrium during which the dominant characteristics are those of growth and change; and, finally, a third stage of equilibrium which occurs after the firm has worked itself out of its unbalance and into an efficient, scientifcally managed and organized institution.

The pattern of the growth cycle is common to many kinds of economic, political, social, and religious institutions. More specifically, the pattern is similar in nations, industries, and firms. Since this is true, and since the characteristics of growth in nations and industries are also similar, it is possible to extend the knowledge of growth patterns and parameters to include firms as well. Thus the theory has a built-in test of reliability, in addition to its support by empirical evidence.

The theory demonstrates two critical points in the cycle. The first is the take-off, when the conditions of the first stage are changed and disequilibrium is introduced into the firm. The necessary prerequisites for the take-off are: the innovation, the entrepreneur, investment capital, risk and uncertainty, reward for uncertainty, the desire to change, social overhead capital, and a suitable growth environment. The second critical point--the development prerequisites for maturity--is likely to cover a longer period of time than the take-off. It includes the achievement of stability in net investment, employment, and sales, a full functional development in a rational organization structure, and effective administrative and operative management. Thus, the first of these points introduces instability, while the second seeks to overcome that condition, creating a stable base from which a new growth cycle may be initiated.

CHAPTER IV

# A COMPARISON OF KEY ORGANIZATIONAL FACTORS IN SUCCESSIVE GROWTH STAGES

## The Purpose of the Chapter

This chapter examines the most important basic business factors as they pass through the stages of growth. The following are important growth factors:

1. Objectives. The objective of the leader in the first stage is survival of the firm and a satisfactory personal income. In the second stage the objective of the entrepreneur is personal gain like riches, power, or the creation of a successful institution. The goal is quite optimistic, with the entrepreneur unaware of many of the difficulties involved in attaining it. The firm in the third stage will have differentiated between the primary service objective which serves as an intermediate system for the institution, and collateral and secondary objectives. All of these third stage goals are rational and attainable.

2. Policy. Policy in the first stage is determined by precedent, with certain limited legitimate rights of the leadership to interpret precedent. It is centralized, restrictive, and unstable. Policy in the second stage if legitimized by the charisma (personal power) of the entrepreneur, who initiates centralized, personal policy to support his business tactics. In the third stage policy becomes the product of group administrative processes. Unlike the earlier kind, this policy is built upon scientific principles of action, is formal and recorded, and tends to promote greater freedom for individual action.

3. Leadership. At least four different types of leadership may be identified in the growth of a firm: the unimaginative small business leader, the innovator, the entrepreneur, and the executive leader.

(a) The unimaginative small business leader is bound by tradition. He feels that no one can tell him how to run his business, since things have to be learned by "experience". The firm functions like a family, rather than a rational organization, with the leader assigning roles by custom rather than by job performance. Change is unwelcome.

(b) The innovator is one who develops a new idea and adapts it to business use. He may also be the inventor of the idea or he may be the entrepreneur. He has the creative insight to recognize the need for a new good, method of production, market, source of supply, or organization of industry. In reality, the personification of the innovator is often a fiction, since several persons generally contribute to what might more accurately be called the "process of innovation."

(c) The entrepreneur is a promoter who exploits the advantage of an innovation which he has introduced himself or simply recognized as important. He is typically egocentric, ambitious, and against tradition. He introduces the disequilibrium into the organization from which the firm achieves its take-off. He typically represents a hero-figure to his subordinates. The stamp of his personality is upon them, and they tend to identify with him personally. To him uncertainty and risk add interest and zest to action. The entrepreneur is an artist, who, unaware of the difficulties involved in his action, leads loyal subordinates in the tactics of daily operation. As the organization matures, however, he must develop the skills of executive leadership or be replaced by such a person, lest the organization fail.

(d) The executive leader is distinguished by the fact that he performs the management process. That is, he is able to scientifically plan, organize and control the operations of the firm, besides performing a leadership role as well. By introducing sound management once the initial advantages of the growth stage are past, the firm can avoid a tendency to decreasing returns to scale. Unlike the entrepreneur, the executive leader typically deals with future strategy, relying on an impersonal, legal system of authority. He assigns subordinates to particular areas of responsibility and authority organized in a rational manner. He introduces the necessary coordination to insure continued efficient operation as the firm grows, and he sees that by the time the firm reaches maturity it has developed strength in all its functions and has developed written rules of action. He functions as a professional leader in a complex organization system, eliminating uncertainty through scientific business operation.

4. Work Group Bonds. Morale in the first stage reaches no particular extreme of good or bad, since the environment is structured by tradition and hence subject to little question. The prevailing attitude is one of fatalism. Morale in the second stage is high, with frequent interaction among the heterogeneous group, and stimulated by the conditions of dynamic change and an optimistic outlook of the future. Interpersonal relations tend to be quite informal. In the third stage of growth morale is also high, though for different reasons. Leaders achieve good morale quite differently in the second and third stages of growth. Research and authoritative opinion indicate that the dynamic, unstructured group achieves high morale through the close interaction of the group members as they seek to overcome the tension of the situation. This tension is introduced by the entrepreneur

as the desire for some optimistic future goals, or as a result of some external threat. The complex organization developed as the firm moves to maturity requires a different kind of morale maintenance, however. While the dynamic growth of the second stage allowed the union of a heterogeneous group, the achievement of morale in the complex organization requires some degree of conformity among the participants. This conformity is created by selecting individuals who meet the criteria of an organizational philosophy, and by indoctrinating the members of the firm with the same philosophy. In this manner the maturing organization achieves the necessary integration of interests for good morale. Morale is not improved by trying to make employees believe that, instead of better pay, what they really want is to serve the customer. Instead, morale is improved by showing the employee that the best way to improve his own pay is to help the organization give good customer service. The objective is not an identity of interests, it is an integration of interests.[6]

5. Business functions. The first stage tends to be built upon the operative skill of the owner-manager in one function. The second stage is built upon the exploitation of a single function. This is usually sales, followed by the development of production, and finally finance. The third stage is characterized by strength in all functions with a separation of their administrative and operative phases.

6. Organization Structure. Organization structure in the first stage of growth is free from any dominant tendencies to take a particular shape. Since roles are assigned on a basis of traditional

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[6]"The basis of the morale-building process is, accordingly, the process of integrating interests." Ralph Currier Davis, The Fundamentals of Top Management (New York: Harper Brothers 1951), p. 547.

authority, particular assignments depend upon such factors as friendship or kinship ties with the leader. In the second stage the structure takes on a flat shape, since spans are wide and levels restricted in order to support the charismatic power of the entrepreneur. Wide spans in this stage are consistent with needs by subordinates for freedom of action. As spans increase and new levels are created, functions also devolve and evolve. Because centralized control is no longer feasible under such conditions the firm moves to a decentralized, rationally organized structure. In the third stage the firm becomes longer with a narrowing of spans and decentralization of authority. A rational structure develops with clearly defined objectives, policy, functions, and authority. Personnel are hired to perform a particular set of duties for which they are held accountable. Their loyality is to the job and the system rather than to a single hero image.

7. Staff. The use of staff in the first stage is limited to housekeeping functions and, perhaps, a few technical aids. None other is needed since the idea of progress is not considered and methods are expected to continue in the same way into the future. In the second stage one may expect to find, in addition to technical and housekeeping staff, the type of general staff assistant commonly referred to as the "assistant-to." This person acts as an extension of the personality of his principal, aiding him in coordinating the efforts of those within his wide span of control. In the third stage one finds a full development of staff functions with technical and coordinative staffs, including committees, aimed at supporting the increasing mass of organization. Executive and operative spans are reduced to rational limits.

8. Invention and innovation. The process of innovation is performed by one or more persons and includes the conceptualization

of a new idea, developing it and adapting it to business use, and utilizing the idea in actual operations. Seldom does the entrepreneur of the second stage have the inventive ability to create a new invention. The entrepreneur does have a talent for recognizing the opportunities connected with a new idea, however. By the time the third stage is reached, invention and development have become a controlled process performed by corporate research and development staffs.

9. Uncertainty and risk. Uncertainty is an unmeasurable probability of gain or loss. Risk, on the other hand, is a measurable probability of gain or loss. The unimaginative small business leader seeks an absence of risk and uncertainty, and, since uncertainty is rewarded with excess profits, receives none of these consequent rewards. The entrepreneur, on the other hand, has sufficient drive for achievement and reward to induce him to step into conditions of uncertainty and exploit the situation. The executive leader is more rational in his approach, tending to calculate the risk involved in actions and to build this risk into the cost structure of the product. Staff units in the rational organization structure are devoted importantly to planning and control necessary to reduce uncertainty to a measurable risk.

During growth greater potential uncertainty develops as more resources are committed to future action. Without the trend to rational calculation of risk in the rational structure, the uncertainty that was the stimulation during early growth could lead to the failure of the larger organization.

10. Growth and size. Growth is a process while size is a state. The growing firm benefits by both economies of size and economies of growth, while the stable firm receives only the former. Merely

increasing size through greater addition of factor inputs does not necessarily result in growth, for the internal changes associated with growth would not be present in the absence of a take-off. It will be recalled that growth as it is defined in this theory does not include external acquisition; nor does it include a simple increase in size solely because of an increase in the industry demand condition. Rather growth, as defined, requires a combination of factors which induce an internally generated increase of sales, assets, and employment at an increasing rate. An increase in size results in technological economies, managerial economies, economies of power, and financial economies. Growth, on the other hand, results in economies of factor prices, economies of resource use, and economies of natural change. Small firms have the greatest potential gains from growth. Parts of large firms may similarly benefit from growth, however.

EXHIBIT X

KEY ORGANIZATIONAL FACTORS
IN SUCCESSIVE GROWTH STAGES

| Key Factors | Stage I | Stage II | Stage III |
|---|---|---|---|
| Objectives | comfort-survival | personal achievement | market-adaptation |
| Policy | traditional | personal | rational |
| Leadership | caretaker | entrepreneurial | professional |
| Work Group Bonds | fixed roles | interaction-expectation | homogeneity |
| Functional Development | single function | successive emphasis | full functional development |
| Structure | power levels | field of force | rational hierarchy |
| Staff | housekeeping | technical-personal | technical coordinative |
| Innovation | no creativity | innovation | development |
| Uncertainty Risk | non-risk | uncertainty | risk |
| Growth-Size Economics | size benefits | growth-size benefits | size benefits |

# CHAPTER V

# A GROWTH PROFILE OF THE FIRM

## The Purpose of This Chapter

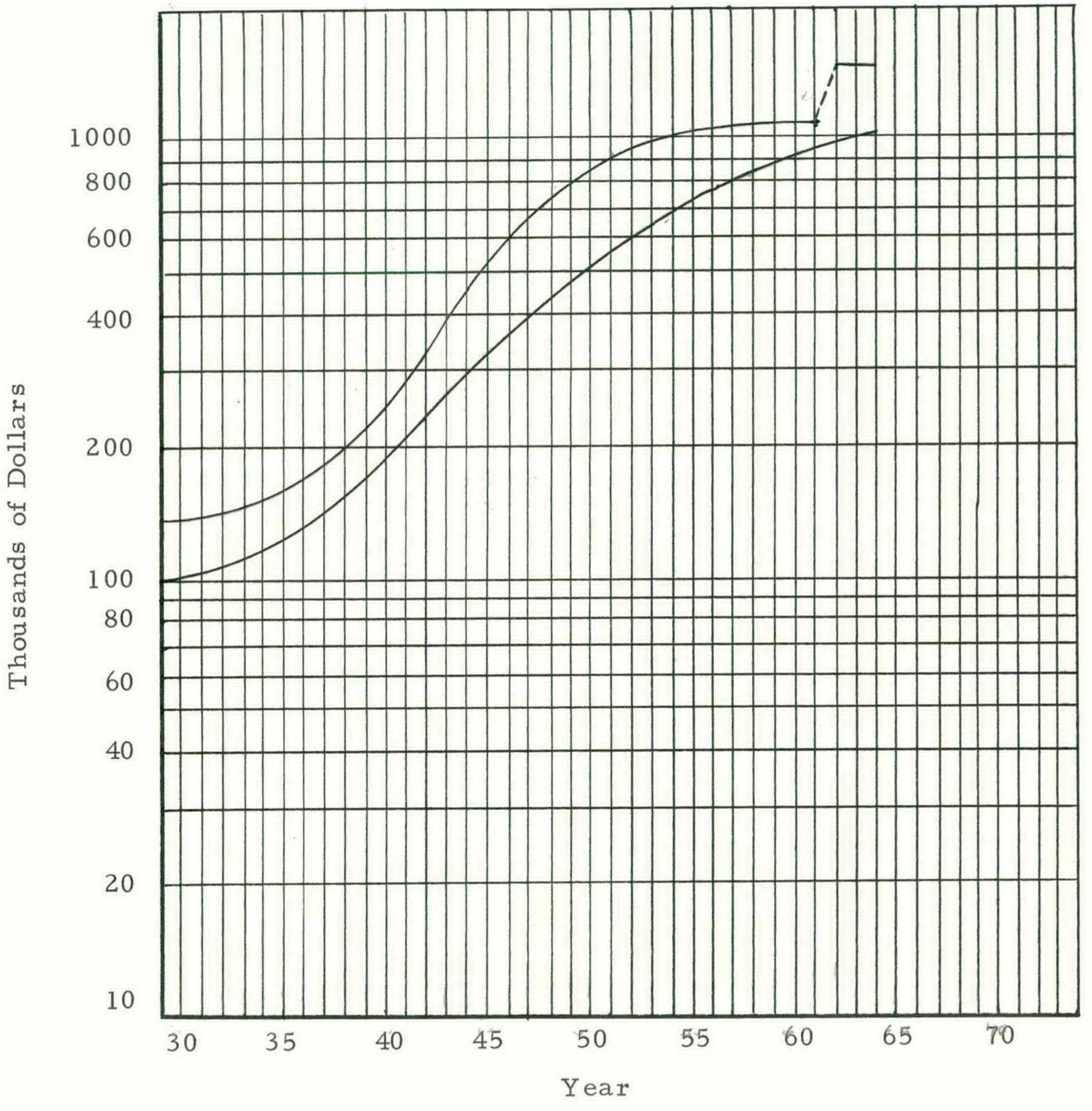
In this chapter a profile of the firm's growth is developed. Each of the key business factors are examined to determine its present stage of development. By determining the stage common to the majority of these factors, it is possible to determine the present position of the firm within its growth cycle. In areas where these factors are out of phase with each other, problems develop. This happens when a particular subfactor is either more developed or less developed than others. Examples of this will become evident in the following analysis.

## Sales Growth

Annual net sales, as shown in Exhibit XI, form a growth curve which has many characteristics consistent with the growth model. Sales figures prior to 1929 were not available. Since net sales in that year were only $144, 000, it can be assumed that the prior rate of growth was low and representative of the traditional small business stage. Following recovery from the depression, the sales curve indicates that a take-off was established. In fact, from 1935 to the present, a series of take-offs is indicated. As the firm entered new markets, sales would rise sharply. Several of these moves into new markets can be identified. The upward turn of the sales curve in 1939 coincides with the establishment of the brush division and reflects its first-year sales. The next sharp upturn came in 1945 just after

EXHIBIT XI

NET SALES AND NET ASSETS, 1929-1964



the close of World War II. Sales turned sharply upward as the firm expanded its home building actively in the post war housing market. In following years, sales reciprocated in a generally upward direction but the over-all rate of growth declined. In 1961, sales turned sharply upward again. This resulted from the firm's entry into the bowling alley market. That take-off quickly reached a peak and sales since 1962 have leveled off onto a plateau.

The sales curve in itself does not present a clear-cut picture of the present stage of growth. There was a definite tendency for sales to stabilize prior to 1961. This trend was broken by an all-out effort to cash in on the bowling alley market. Sales have declined slightly over the last three years and the President, Mr. Joel Hoge, stated that he expected net sales for 1965 to be down also. Arthur Hoge and John Hoge, on the other hand, stated that they foresaw additional substantial growth in the next few years. Plans for expanding sales are already underway. One plan involves the marketing of recreation park facilities, such as picnic tables, and shelter houses. The company has been furnishing picnic tables to the State of Ohio for the past ten years and now plans to expand its sales of these items to states along the Eastern Seaboard. Another plan calls for the establishment of a distributorship for long-span laminated wood roof trusses manufactured on the West Coast. It is believed by handling these trusses, additional sales can be generated for related building products.

The management's attitude toward the current sales picture is consistent with its reaction to sales dips in the past. When sales are down, efforts are made to locate new markets which can be exploited so that a new upsurge in sales can be obtained. On the basis of past sales growth and in light of management's plans for future sales expansion, it can be concluded that with respect to sales growth, the firm is currently in the second stage of its growth cycle.

## Asset Growth Rate Consistent With Growth Theory

The rate of asset growth exceeded the rate of sales growth as the firm entered the second stage just prior to World War II. The two rates were almost equal and the ratio of sales to assets was one to one. Through the war years, net assets declined. However, immediately following the War, asset growth again paralleled sales growth as a result of the plowing back of earnings into the firm. The rate of net investment has remained relatively constant. Net asset investment has not stabilized and plans calling for the increase of warehouse space in the future will tend to keep net investment growing. This positive investment growth rate also indicates that the company is in its second stage of growth.

## Employee Growth Rate

The relatively stable number of people employed by the firm would indicate that with respect to this measure of growth, the firm has entered a stage of equilibrium and maturity.

## Objectives

During the first thirty years of the firm's existence, the pattern of objectives was consistent with that of a traditional small business. The objectives of the firm were identical to those of the founder which were to provide a living for his family of thirteen children.

With the entry of the four sons into the business and the recovery of the economy, objectives changed. Although company objectives are not formally defined, it is obvious from the firm's record of growth and its sound financial condition, that the owner-managers have actively pursued growth. Sales have been increased primarily through market exploitation as opposed to the long-run market development. New markets were constantly sought which could be tapped for increased sales volume and earnings were plowed back into plant and inventories.

An attitude towards markets characteristic of the entrepreneur is evident from conversations with the management team. Great pride is derived in being able to find opportunities to provide a unique product or service. Production processes are kept very flexible so that almost any new product can be made. As a result, the firm enjoys a reputation for being able to produce anything from wood.

The objectives of growth through market exploitation have resulted in a series of take-offs. This type of growth reflects a policy of "opportunism" characteristic of the second stage of growth.

## Policy

No formal written policies exist to guide the operation of the firm. Questions of policy are decided on a situation by situation basis and are therefore changed frequently. This fact was brought out in a discussion with production supervisors with respect to quality standards. Acceptable quality, it was reported, often varies with the quality of the raw material. If raw material is poor, low quality is permitted in the finished product. When raw material quality is high, the product quality standards are raised. A severe problem exists in communicating quality standards since no standard quality nomenclature has been developed. Terms such as good, sound, select, clear, and similar phrases are examples of general terms used to describe quality.

Policy problems are compounded by the fact that several of the owner-managers may express conflicting opinions on a given policy issue. This leads to confusion and uncertainty as to whether one has actually heard the last word.

This unstable policy situation is typical of a firm in a stage of dynamic growth.

## Leadership

It is obvious from observations made with respect to all of the factors discussed in this chapter that the firm is led by an entrepreneur. This was already brought out with respect to the objectives of short-run market exploitation and unstable policy. Other evidence will be presented in the discussion of functions, organizational structure, and the use of staff. Perhaps a significant observation that can be made at this point is the fact that the central entrepreneurial leader, Arthur Hoge, is 69 years old and is still very active in the daily operation and control of the firm. He is a firm believer in strong central control and considers suggestions for more delegation of responsibility and authority to others as a sign of weakness and a sure way to lose control. When discussing company problems, he recognizes that many problems are generated by the wide diversity of products and activities in which the firm is engaged. However, he feels that this diversification has been the key to past success and an excellent hedge against the loss of business to competitors.

## Functions

The owner-managers place major emphasis on the sales function. Four of them are actively engaged in sales work, with each performing many tasks incident to sales activity. The production function has received increasing emphasis in recent years primarily through the provision of improved facilities. However, production planning and scheduling are still done by a plant superintendent through oral contact with sales personnel. Few functions are well defined and systemized. Many are performed by whoever has time. Responsibilities are assumed by whoever has the greatest experience in that particular area and no attempt has been made to develop job classifications consistent with rational management principals. The loose functional organization of the firm is typical of a company in the second stage of growth.

## Structure

The organizational chart on page 19 clearly depicts the present structure of the firm. The members of the management team are closely linked in a circular structure to Arthur Hoge, who is the central figure. The chart should be viewed as looking at the apex of a shallow inverted cone with Arthur Hoge on the top level and with one, and in some cases, two additional levels. Channels of authority and communication are unclear. Several of the members of the management team have an "assistant to" relationship with Arthur Hoge with varying degrees of freedom in making independent decisions. Responsibilities are assigned to these assistants and control is maintained through frequent contacts. Mr. Hoge's method of operation is typified by his handling of orders which are of particular interest to him. One example of this which occurred while I was studying the case, concerned production of park tables for the State of Ohio. In order to control production of these tables, he requested that a particular operative employee be freed of other duties to work on the order. He then bypassed the shop superintendent and shop foreman and personally instructed and supervised this employee in the processing of the order. This type of direct control in a shallow, loosely defined organization is typical of a firm in a dynamic stage of growth.

## Staff

There is only one clearly evident staff department within the firm. This is the accounting function which was differentiated from the line activities as early as 1928 when Mr. Mahn was employed to assume the bookkeeping responsibilities. Another use of staff is the employment of the "assistant to" concept. The extent to which this concept is employed can be clearly seen by an examination of the functional analysis, Exhibit XII. Mr. Arthur Hoge is actively engaged in most of the major functions necessary for the operation of the firm, however, as the firm has grown, he has developed assistants in many of these areas. He has delegated the accounting function to Mr. Mahn. In the area of farm sales, Mr. Niemeyer, was hired as an assistant and is now responsible for a substantial amount of farm sales volume. Mr. Niemeyer maintains a close working relationship with Arthur Hoge, with the latter making most of the policy decisions with respect to farm sales. A similar arrangement exists with John Hoge, who came with the firm in 1959 to assist his father sell in the industrial market with the bulk of the orders made by John.

# EXHIBIT XII

## FUNCTIONAL ANALYSIS

| | A. F. Hoge | G. A. Hoge | J. W. Hoge | O. H. Hoge | J. H. Hoge | O. H. Mahn | N. Niemeyer | H. Kuck | D. Shiley | R. Katterheinrich | C. Schrolucke | G. Bargdill |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| General Management | x | | | | x | | | | | | | |
| Office Management | x | | | | | x | | | | | | |
| Production Supervision | x | | x | x | x | | x | x | x | | | x |
| Maintenance Super. | | | | | x | | | x | x | x | | |
| Contractor Supervision | x | | x | x | | | x | | | | | |
| Financial Management | x | | | | | | | | | | | |
| Retail Sales | | | x | x | x | | x | | | | | |
| Farm Sales | x | | | | | | x | | | | | |
| Industrial Sales | x | | | | x | | | | | | | |
| Millwork Sales | | | x | x | | | | | | | | |
| Sales & Adv. Policy | x | | x | x | x | | | | | | | |
| Pricing | x | | x | | | | | | | | | |
| Credit & Collections | x | | x | x | x | x | x | | | | | |
| Drafting | x | | x | x | x | | x | x | | | | |
| Estimating | x | | x | x | x | | x | | | | | |
| Order Expediting | x | | x | x | x | | x | x | x | x | | |
| Complaint Processing | x | | x | x | x | | x | | | | | x |
| Product Design | x | | x | x | x | | x | | | | | |
| Product Development | x | | | x | x | | x | x | | | | |
| Product Scheduling | x | | x | x | x | | x | x | | | | |
| Delivery Scheduling | x | | x | | x | | x | | | | | |
| Process Improvement | x | | x | x | x | | | x | x | x | | x |
| Machine Setup | | | | | | | | x | x | | | |
| Operative Work | | x | | | | | | x | x | | x | x |
| Maintenance Work | | x | | | | | | x | x | | x | x |
| Inventory Records | | | | | | x | | | | | x | |
| Check Inventory | x | | x | x | x | | x | x | x | x | x | x |
| Mtls. Requisitioning | | | | x | x | | x | x | x | x | | |
| Interview Salesmen | x | | x | | x | | x | x | | | | |
| Purchase Contracts | | x | | | | | | | | | | |
| Issue Purchase Orders | x | | x | | x | | | | | | | |
| General Accounting | | | | | | x | | | | | | |
| Cost Accounting | | | | | | x | | | | | | |
| Wage Administration | | | x | | x | | | x | | | | |
| Salary Administration | x | | | | | | | | | | | |
| Hiring | | | | | x | | | x | | | | |
| Ship and Receive | | | | | | | | x | x | x | x | x |

The "assistant to" concept is also carried out in the production function. Mr. Kuck functions as the plant superintendent. He has been given the responsibility for seeing that production orders are filled. However, authority for making many decisions is retained by Arthur Hoge, or his assistant, John Hoge. Mr. Kuck's relationship to his own subordinate also makes use of this concept. Mr. Shiley holds the title of production foreman. However, he does not have any clearly delegated authority. It was my observation in talking with Mr. Kuck that he clearly had too many activities to accomplish well. When asked if it wouldn't be advisable to delegate more responsibility to his subordinate, he replied, "Yes, but then I wouldn't know what was going on." Mr. Kuck strongly feels his responsibility for product quality and believes that in order to insure that work is performed correctly, he must personally supervise operative employees.

Mr. Katterheinrich also has an "assistant to" relationship to Arthur Hoge in the performance of delivery supervision. Mr. Schrolucke, the yard foreman, finds himself in a dual "assistant to" relationship. He assists the plant superintendent in the drying of hardwood lumber and Arthur Hoge in his duties of receiving, inspecting and stacking of incoming materials. Mr. Bargdill also feels a dual responsibility in his responsibilities of managing sawmill operations. He receives instructions from both Arthur Hoge and John Hoge.

The functions of planning and control are performed by line personnel. Planning is very short-range in nature and is not reduced to writing. Control is maintained by face-to-face contact, for no management reports are prepared for purposes of control.

The use of limited technical staff assistants and the heavy dependence on the "assistant to" concept is typical of a firm in the dynamic stages of growth.

## Invention and Innovation

The innovative process is carried out by several of the owner-managers in connection with their other sales activity. New markets which can successfully be tapped are constantly being sought. The success in this search is evident by the recurring upsurges of sales growth. No formal research and development staff has been established. Emphasis on developing new products is the greatest when sales are declining.

The focus of innovative responsibility with the entrepreneurial owner-managers is characteristic of a firm in the second stage of growth.

## Uncertainty and Risk

Uncertainty abounds in the organization. Its extent was best brought out in a conversation with Arthur Hoge in discussing the problems of better planning and control of production operations. He commented "these are all just natural problems of job shop operations. We can't plan very far ahead, after all, we don't know what kind of products we'll be making nine months from now. Some items go strong for awhile and then just drop off. There isn't much we can do about it. When that happens we just have to find something new to make and any long-range planning we would have done would go down the drain."

Other evidence of uncertainty are reflected in the fact that there are no written policies. Policy is established on a situation to situation basis. In the absence of written policy to use as guidelines, employees are not certain how reoccurring situations and problems should be handled and they must repeatedly be taken to higher levels for decision.

As a result of these conditions, much time is spent in "putting out fires". Effective planning cannot be done and the firm must operate on a day-to-day basis. The uncertainty which abounds in the operation of the firm is typical of that found in a firm experiencing dynamic growth.

Growth and Size Advantages

The Hoge Lumber Company has benefited from both growth and size. Through the exploitation of various markets, it has been able to attain substantial returns which have been plowed back into the firm to increase its size. As a result of size, the firm has been able to capitalized on an increased ability to manufacture in larger quantities and distribute in a larger geographical area. Prefabricated farm buildings are now delivered to customers in northern Michigan. Industrial wood parts are shipped to customers on a national basis. The newest and largest bowling alley in Japan was recently constructed of wood materials furnished by the Hoge Company.

Members of the management team anticipate that growth will continue in the future. The leveling off of sales in the last three years is not seen as an indication of reaching maturity. In discussing future growth, Arthur Hoge commented, "We could increase sales orders 25 per cent next year. Problems in handling this increased volume would arise in production. Perhaps the answer here would be the initiation of a night shift to better utilize production facilities."

## Work Group Bonds

In probing for signs of work group bonds, it became obvious that morale is at a low level throughout the organization. Arthur Hoge stated "we have lost organized or good company team performance; we are not coordinated. I sense actual opposition to the operation of the business at a profit. The reasons are difficult to fathom. Losses are swept under the carpet, if convenient, with little or no concern. The office knows only a part of what is going on. It should be better informed from day to day on all matters of business." He went on to say that he thought organizational morale had dropped "ever lower" since the death of the founder of the firm.

Other indications of low morale are evident. Within the last year, eight skilled employees of the manufacturing division have terminated. Higher wages obtainable elsewhere was usually cited as the reason for leaving. The firm's wage scale has been consistently lower than those of neighboring firms throughout the history of the firm. This has not caused a serious problem in holding good employees in the past. The recent turnover may indicate that other morale factors may be the cause.

Since the firm must train its own skilled machine operators, this turnover has placed a heavy burden on the shop superintendent. In discussing production problems, Mr. Kuck stated that employee turnovers was his greatest problem and the failure to keep his best employees was very discouraging. In concluding his interview with me, he said, "If it sounds like I am tired and discouraged, I am."

The firm had been experiencing difficulty in selling homes. In addition to the turnover in the plant, two home salesmen also terminated within the last year. Oliver Hoge reports that their leaving has placed a heavy burden on him and that he would like to be relieved of his home building responsibility. When asked what he thought the problem was in the housing market, he replied, "We seemingly don't want to be creative or progressive in the housing line. In the last few years, it hasn't proven profitable in comparison to other departments. There's an attitude among my brothers of, 'just do the best you can on your own and let the rest go by'. As I see it, many of our problems are of our own making. We seemingly don't want to face the reality of a situation and plan for the future. We are reluctant to review problems in departments that are not going well, for each has his own problems."

All members of the management team were asked to prepare a list of the problems they experienced in fulfilling their responsibilities. It is significant to note the the first item on the list of Mr. Shiley, the shop foreman, was the statement, "No one seems to know what my job is." In discussing this in an interview, he brought out the point that he performs many services as an assistant to Mr. Kuck, but that he is not delegated clear-cut responsibility. "I supervise machine operators and five minutes later, Mr. Kuck is checking up himself. Why should I check if he's going to do it too?"

Mr. Schrolucke, the yard foreman, stated "What we need around here is some standard operating procedure. I don't find out about things until I should have had them done two days ago. I have the feeling my job is not too important until things are all fouled up. I get orders from Arthur Hoge and from Mr. Kuck. Sometimes I don't know what to do first."

"The characteristics which make for high morale during a period of turbelence in the second stage of growth will eventually cause low morale if continued as the organization matures. Some goals will be achieved. Employees will come to realize, however, that many can not ever be achieved. The close personal relationship with the entrepreneur is lost as organizational levels are established and lines of communication lengthened."[7]

It is obvious that the breakdown of morale in the firm is primarily due to the overextension of the entrepreneurial organization. The widespread use of assistants, with unclear responsibility and authority has created a situation where coordination and good team performance is impossible. Each person does the best he can, however, sincere effort on the part of each person will not make up for a lack of over-all planning and coordination. The condition of work group bonds provides strong evidence that this firm has moved beyond the dynamic stage of growth.

## Summary of the Growth Profile

The growth profile developed by this analysis is clearly illustrated by Exhibit XIII. With the exception of the employee growth rate and the condition of work group bonds, this firm has all the characteristics of a firm in a dynamic stage of growth. The condition of morale provides some indication that a transition to a state of maturity would be desirable. Other advantages of a transition into the stage of stabilization and maturity will be discussed in the next chapter.

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[7] Alan Case Filley, "The Theory of Small Business and Divisional Growth", An unpublished doctoral dissertation, The Ohio State University, 1962, page 221.

EXHIBIT XIII

A GROWTH PROFILE

| Growth Factors | Small Business | Take-Off | Dynamic Growth | Equil-ibrium | Maturity |
|---|---|---|---|---|---|
| Sales Growth Rate | | | X | | |
| Asset Growth Rate | | | X | | |
| Employee Growth Rate | | | | X | |
| Objectives | | | X | | |
| Policy | | | X | | |
| Leadership | | | X | | |
| Work Group Bonds | | | | X | |
| Functions | | | X | | |
| Structure | | | X | | |
| Staff | | | X | | |
| Invention and Innovation | | | X | | |
| Uncertainty and Risk | | | X | | |
| Growth and Size | | | X | | |

# CHAPTER VI

# PLANNING FOR FUTURE GROWTH

## Purpose of This Chapter

The growth profile developed in Chapter VI places the firm in the second stage of its growth cycle. In this chapter the need for a transition into the stage of maturity is more fully analyzed. Specific recommendations for changes are developed and some of the problems of transition are examined.

## Needs for Transition

There are several indicators that a transition into a stage of maturity should be initiated. Low morale indicates that good coordinated team effort does not exist. Areas of dual responsibility suggest that organized team performance has not been planned. The relatively stable number of employees is probably an indication that under present methods of operation, additional employees could not be added effectively. All of these situations are a result of extending the face-to-face leadership of an entrepreneurial organization to its limits. Coordination and control are left to the voluntary oral communication of assistants and assistants to assistants. The policy of market exploitation limits the amount of planning that can be done on any level of operations because the nature of products may change within a short time.

These conditions create many additional problem areas. Production and inventory control are done on a hand-to-mouth basis. Production schedules are changed on an hourly basis. Delivery dates are often missed and quality of output is difficult to control.

Without definite delegation of responsibility, no one can be held accountable for performance. An example of this problem is in the area of cost records. In the press of putting out "production fires" cost records are often neglected. Since measures of cost are not used to gauge performance, no one gets too concerned about obtaining them.

In spite of these problems, the firm may experience additional growth without changing significantly. If new markets are invaded, and production operations are placed on a double shift basis, a new take-off may be entered. However, problems of coordination and control will become more severe.

Perhaps the most significant indicator of the importance of a transition into maturity has still not been explored. It is revealed in the management analysis (Exhibit VIII, page 22). From this analysis, it is obvious that the leadership of the firm will be forced to change in the not-too-distant future. Arthur Hoge, age 69, is past traditional retirement age. Gustave Hoge is semi-retired and four other members of the management team will reach retirement age within the next ten years. The most alarming situation is the approaching retirement of the central entrepreneurial figure, Arthur Hoge. As he becomes less active in the firm, an already deteriorated condition of work group bonds will need a new focus. Although his leadership has not always been fully recognized by other members of the management team, he has been the guiding force within the firm. There is some indication that John Hoge may be able to fill this leadership role. However, additional nonfamily management personnel will have to be employed and led by fewer active owner-managers. Under these conditions, it will be impossible to attain additional growth or even maintain present levels of operation unless some of the characteristics of a mature rational organization are developed.

## Recommendations for Future Growth

The purpose of the following recommendations is to serve as guides developing key organizational factors characteristic of a mature organization. The growth model set forth in Chapter IV was used in developing these recommendations. Not all growth factors can be changed by immediate action of management. Some factors such as objectives, policy and organizational structure are basic, and changes in them influence changes in other factors.

### Objectives

The cornerstone of a mature organization is a statement of its objectives. Objectives are the "ends" toward which the basic management functions of planning, organizing, and controlling are applied in order to provide a "means" for their attainment. Plans are only meaningful if they relate to objectives. Objectives should spell out the nature of the service the firm will provide to its customers and the relationships which management wishes to exist between itself, stockholders, employees and the community. An important objective for this firm would be the development of a mature organization which will enable all employees to contribute effectively to the primary objectives of the firm.

### Policy

Written statements of policy should be developed. Sound and existing statements of corporate policy would provide a number of important benefits to the organization. Written policies tend to prevent deviations from planned courses of action, because it makes possible an intelligent understanding of plans. It insures consistency of action because the organization is always guided by the same basic principles in planning, organizing, controlling, and executing its work. It does not, however, go so far as to discourage initiative and creative action since the individual knows in advance the framework in which he must work. It provides for consistency of action but not uniformity of action. It promotes intelligent cooperation and facilitates coordination for much the same reason. It fosters an intelligent exercise of initiative because it provides a body of principles and rules for the analysis of situations. It provides a guide for determining equitable personnel relations. It assists executives in their performance of the work of management. It furnishes a basis, therefore, for evaluating the quality of the leadership for the executives to whom they report. Last, it provides a guide for future planning and current decision making.[8]

## The Responsibility for Policy Formulation and Application

The responsibility for policy formulation and application and, in cases, enforcement rests in the top management echelons. This function can be delegated to supporting staff groups but sole responsibility for policy preparation must remain in the upper levels of the organization.

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[8] R. C. Davis, The Fundamental of Top Management (New York: Harper and Brothers, 1951) pp 175-176.

The company currently has no existing formalized statement of corporate policy. Many policies are implied and are in practice, but uniformity of practice can not be detected from the analysis of the existing situation. The lack of stated policy and adherence to such policy has created or aided in the creation of internal problems in the firm. Among these are (1) lack of "clear" cut company objectives and individual objectives to guide personnel in their day-to-day work, (2) lack of consistency in action or managerial personnel, (3) lack of initiative and creative thinking on the part of some managerial personnel, and (4) poor personnel relations.

## Revised Organization Structure

"Organizations are the grand strategies created to bring order out of chaos when groups of people work together. Organization sets the relationships between people, work and resources. Wherever groups of people exist in a common effort, organization must be employed to get productive results."[9] An organization is the orderly arrangement and relationship between the personnel in a business organization, and the functions required to produce and sell the product. The purpose of organization is to create a situation in which people can work together in the most economical and efficient manner possible.

The analysis of the existing organization structure produced a variety of shortcomings, violations of sound organization principles, and problems caused by this lack of ineffectiveness of the company's formal organization.

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[9] Keith Davis, Human Relations at Work (New York: McGraw-Hill Book Company, Inc., 1962), p.181.

## Summary of Basic Principles of Organization

The following principles of organization are a result of the survey of opinions of current organization writers and literature. The list does not represent itself to be an exhaustive one, but one the author found useful in this section on reorganization.

1. There should be a hierarchy of organization wherein lines of authority and responsibility run upward and downward through the several levels with a broad base at the bottom and a single head at the top.

2. Every unit or person in the organization should be answerable ultimately to the chief administrative officer at the apex of the hierarchy.

3. Every necessary function involved in the mission and objectives of the organization is assigned to a unit of that organization.

4. The responsibilities assigned to a unit of that organization are specifically clear-cut and understood.

5. No function is assigned to more than one independent unit of one organization.

6. Consistent methods of organization structure should be applied at each level of the organization.

7. Each member of the organization from top to bottom knows to whom he reports and who reports to him.

8. No member of one organization should report to more than one supervisor.

9. Responsibility for a function is matched by the authority necessary to perform that function.

10. Individuals or units reporting directly to a supervisor do not exceed the number which can be feasibly and effectively coordinated and directed by the superior.

11. Channels of command are not violated by staff units although staff units should be used when possible to provide specialized service and advice.

12. Authority and responsibility for action is decentralized to the units and individuals responsible for actual performance of operations to the greatest possible extent, so long as such decentralization does not hamper necessary control over policy or the standardization of procedures.

13. Management should exercise control through attention to policy problems of exceptional importance rather than through review of actions of subordinates.

14. Organization should never be permitted to grow so elaborate as to hinder work accomplishment.

## The Revised Corporate Organization and the Organization Chart

Formal organization and organization charts are aids to effective and efficient business administration. "It should show every job or at least the most important ones, and give the sectional pattern or breakdown, including titles and names of individuals who are to perform the duties listed on the functional chart. In this step the manager brings the theoretical organization down to earth and faces the practical aspects of managing the business. He determines the current performances of his key men, aligns their work according to individual abilities and peculiarities, and establishes definite responsibilities and authorities for each."[10]

Exhibit XIV is the revised organization chart for the company. The revision takes into consideration both organization theory and principle and is designed to remedy the internal problems of the firm

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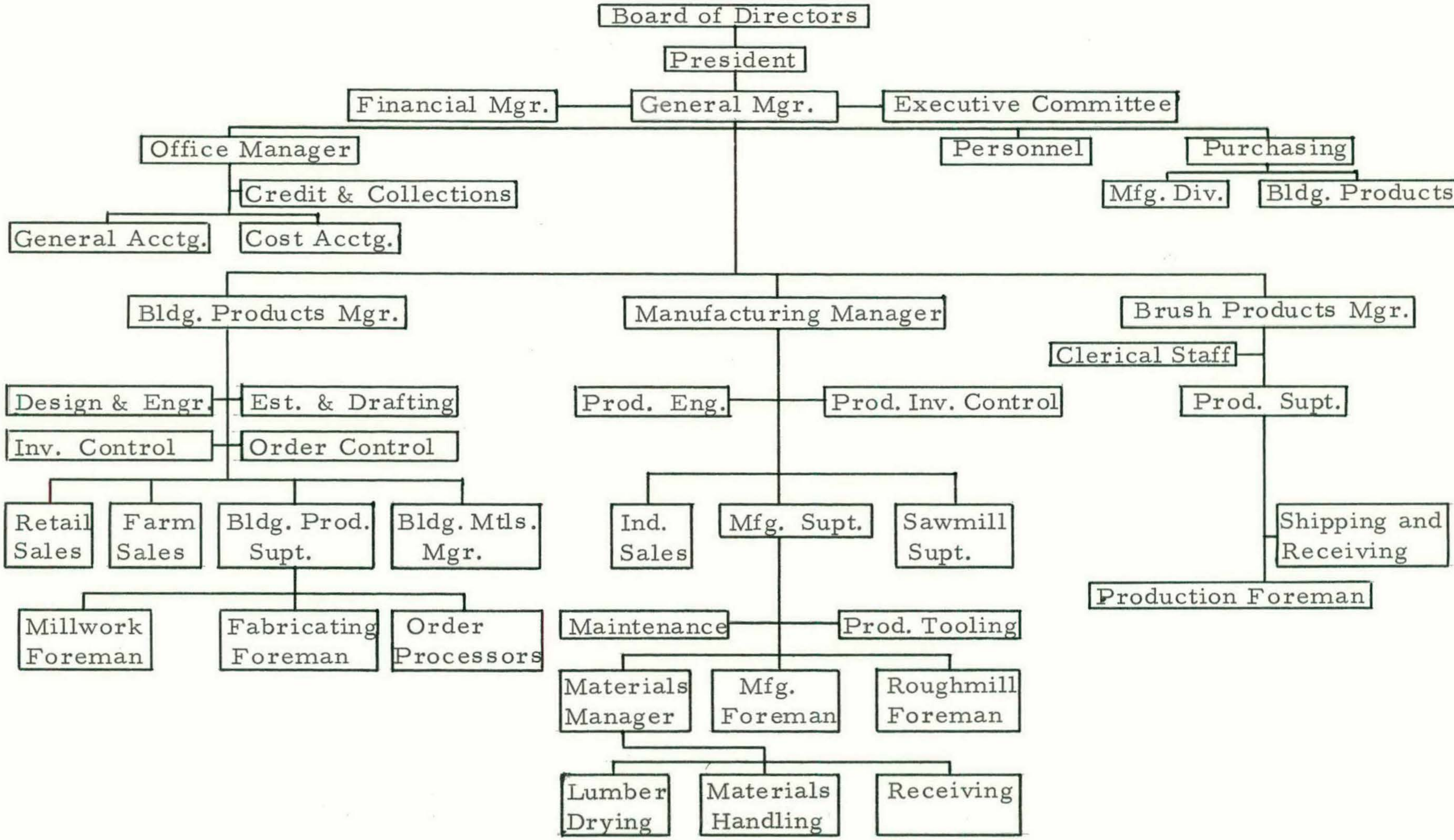
[10] James D. Mooney, "Organizing the Small Plant," Small Plant Management, ed by Edward H. Hemple (New York: McGraw-Hill, 1950) pp 154-155.

EXHIBIT XIV

REVISED ORGANIZATIONAL CHART



as well as to provide a formal statement and depiction of corporate organization for the benefit and assistance to line and staff personnel.

The Executive Committee

The revised organization includes an executive committee. The committee is comprised of the general manager and the managers of the three operating divisions of the firm. These men head the major functional departments of the company and should represent the top executive talent in the firm. The committee should be chaired by the general manager of the company. Meetings should be held at the request of the chairman or upon approval by the chairman of a request by any other committee member.

Purpose of the Committee

The primary purpose of the executive committee will be the joint solution of policy and operating problems, where such problems are sufficiently important that a number of executives should assist in their solution. The committee is also "an effective device for coordinating activities and points of view."[11] Therefore, the committee combines the experience and knowledge of top executives from the various functional areas of the firm. It gives them a chance to "air their particular views" on specific matters, suggest improvements and recommend changes. Another purpose of the

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[11] Douglas C. Basil, Organization and Control of the Small Enterprise, University of Minnesota Press, Minneapolis (1959), p. 55.

committee is to correct or eliminate operational difficulties involving coordination at the top administrative level. The committee should serve in an advisory capacity to the general manager upon his request. A collateral purpose of the committee is to strengthen corporate morale by allowing responsible executives the chance to participate in decisions which affect their jobs and their company.

## Advantages of the Executive Committee for the Company

A number of advantages should accrue to the company from the use of the executive committee.

> The first advantage is that committees can overcome some of the personality traits common to small businessmen, such as the desire for one-man control, the tendency to make snap judgments without consideration of the facts, the increase of the span of control beyond the effective control point, and the inclination to secretiveness about the affairs of the company. These shortcomings of small businessmen in general can cause the failure of the firm should it grow to the size where these are real problems of delegation and coordination.
>
> The second advantage is that the use of a committee tends to show clearly any organizational weakness that might exist in the firm. It would be quite apparent during the committee meetings if an excessive number of functions were delegated to certain executives or if there were a lack of communication or coordination between departments. Thus, one of the by-products of committees, often is the reorganization of duties and functions.
>
> The third advantage is the possibility of obtaining better decisions by the introduction and pooling of expert advice for the executive charged with the responsibility for making a decision.

The fourth advantage is the possibility of utilizing the committee as a control mechanism. One important problem found in small companies is the preoccupation of the chief executive with detail or with particular functions in which he is interested, to the detriment of control over the remainder of the functions of the firm. Unless the president is experienced enough to recognize his own limitations, he may fail to hold executives accountable for the exercise of their functions. In the large firm, this control is usually accomplished through the establishment of a routine system of reports. However, in the small firm reports are either non-existent or are kept at a minimum. The use of a committee with a definite agenda, and with the minutes of the meeting as a record of what executives have accomplished, can aid the president in his exercise of this important control function.

A fifth advantage is the creation of a sense of loyalty and a feeling of importance among the executives which will result in improved morale in the firm. The autocratic type of leadership often found in small firms kills the initiative which is so important to the continued success of the smaller firm. If the small business wishes to attract high caliber personnel to its ranks, it must permit its executives a full voice in the operations of the business and full opportunity to show their initiative. This certainly can be accomplished by committees even if these committees are only advisory in nature.

The sixth advantage is the resolution of inter-department conflicts and jealousies. Although some may be of the opinion that there are no such problems in small businesses with only five or six executives, there are many cases of such conflict in small firms. Jealousies often are cleared by committed discussion because it is difficult to be illogical and let feelings dictate opinions in a committee meeting.

The final advantage of committees is that they promote better communication. One of the most important functions of committees is that of providing information to top management concerning the various operating policy

> problems facing the firm. Too often the informal controls of the small firm with its paucity of reports and written communications results in most executives knowing very little about the over-all operation of the firm. This can be a serious problem leading to duplication of effort and a lack of coordination of company activities.[12]

Staff Departments

The revised organization chart shows the establishment of distinct staff departments for planning and control. The following functions are staff activities:

- Planning
  - Product design and engineering
  - Estimating and drafting
  - Production engineering
- Facilitative
  - Purchasing
  - Personnel
  - Maintenance
  - Production tooling
- Control
  - Accounting
  - Order, production and inventory control

The assignment of staff duties to specialized personnel frees line executives to concentrate on the production and distribution of goods to the consumer. If the volume of work required for specific staff activities is not sufficient to fully warrant separate personnel, several related activities may be grouped together. Methods and systems, however, should be developed so that activities can be easily separated as growth warrants.

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[12] Douglas C. Basil, Organization and Control of the Small Enterprise, (Minneapolis: University of Minnesota Press, 1959), pp 59-60.

## Phasing Out the Entrepreneural Organization

Five years would be a conservative estimate of the time required to accomplish the transition from a stage of dynamic growth to a stage of maturity. Even this would not be possible unless an all-out effort is made to develop the characteristics of the mature firm. Competent executive leaders will need to be secured or developed from within. These men must be charged with developing all other characteristics of a mature organization. The structure of functions outlined in previous sections was developed around the functions which need to be performed without regard to abilities of current employees. This is not totally realistic. Some functions may be grouped depending on available knowledge and skills, volume of work and functional similarity.

When objectives have been defined, policies written and a sound organizational structure designed, the actual transition can begin. It will be necessary for a period of time for the old and new organization to function in a parallel fashion. The managers of major divisions must be charged with developing personnel required to perform all functions under their command.

Owner-managers who reach retirement age will be valuable in training new men for specific tasks. Some may wish to become less active and accept limited staff responsibilities. The owner-managers should continue to serve as the board of directors with the executive committee made up of operating managers. In the reorganization, many changes will have to be made. "There is nothing more difficult of success no more dangerous to handle than to initiate a new order of things."[13] The truth of this statement is forceably felt by any manager attempting to bring about major corporate changes. The problem will also be encountered by the management of this company as the proposed changes are put into effect. Since the success of any plan is limited by the degree of acceptance and enthusiasm it receives from those who it affects, emphasis should be placed on gaining the acceptance and enthusiastic support of company personnel for these changes. The following procedure should aid in obtaining this support.

Communication. "Every effort should be made to let people know about organization changes. The best practice is to tell as much as possible as soon as possible. Internal announcements are best made through the medium of conferences, meetings, employee newspapers and bulletins."[14]

Participation. "People who have the opportunity to participate in planning for changes will have some feeling of commanding their destiny. Participation helps give the people, involved in the organization change, a feeling of importance. It makes it obvious that the company needs and wants their opinions and ideas and is unwilling to go ahead without taking them into account. As a general rule, those people who will be directly concerned or affected by the change should be given an opportunity to participate in that change before the final decision is reached."[15]

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[13] Niccolo Machiavelli, The Prince (New York: New American Library, 1952), p. 55.

[14] Louis B. Allen, Management and Organization (New York: McGraw-Hill Book Company, 1958), p. 327.

[15] Ibid., p. 329.

Education. "A large part of the task of reorganization is education. People must be indoctrinated in new relationships, taught new skills, helped to change attitudes, given the information they need to understand where they fit into the picture, and how they will be expected to operate."[16]

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[16] Ibid.

## SUMMARY AND CONCLUSIONS

As was mentioned in the introduction, the objective of this study has been the identification of basic problem areas of the subject firm and the development of recommendations for their solution. Current business growth theory was used as a framework within which analysis took place. Advantages of using growth theory as an analytical tool arises from the perspective it provides both to the analyst and the recipient of his work. More specifically, it allows the analyst to closely tailor his recommendations to the needs of the firm and to develop a hierarchy of importance for them.

From the growth profile developed for this firm, it became evident that it possesses most of the characteristics of a dynamic stage of growth. However, the condition of several key business factors indicated that a transition to a more mature organization would provide important benefits to the firm. Specific recommendations for changes in corporate objectives, policy, type of leadership and organizational structure were outlined in the closing chapter and the timing and problems of transition were discussed.

Although evidence is available to establish the desirability for this firm to accomplish a transition to a more mature organization, a transition will not automatically take place. A successful transition will only result from a conscious decision on the part of the owner-managers to facilitate one. In spite of current problems, the firm may continue to grow without changing significantly. If new markets are invaded, and production operations are placed on a double-shift basis, a new take-off may be entered. However, problems of coordination and control will become more severe. The success of the owner-managers in accomplishing a transition, if they should decide to attempt one, will depend on their willingness and ability to formulate corporate objectives distinct and separate from, but compatible with their own personal objectives. This will be the first and most important step. All other steps will depend on these objectives for their focus.

Once objectives are clearly defined, policies can be prepared to guide action toward them and an organization can be built to facilitate their accomplishment.

The usefulness of growth theory will not die when a transition is completed. A mature organization forms a solid base for the initiation of new take-offs on a divisional basis. New products can be developed or new markets tapped to promote growth of new divisions. In this way the firm can enjoy the efficiency and effectiveness of a mature basic organization and still capitalize on the growth and diversification advantages that invention and innovation may provide.

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