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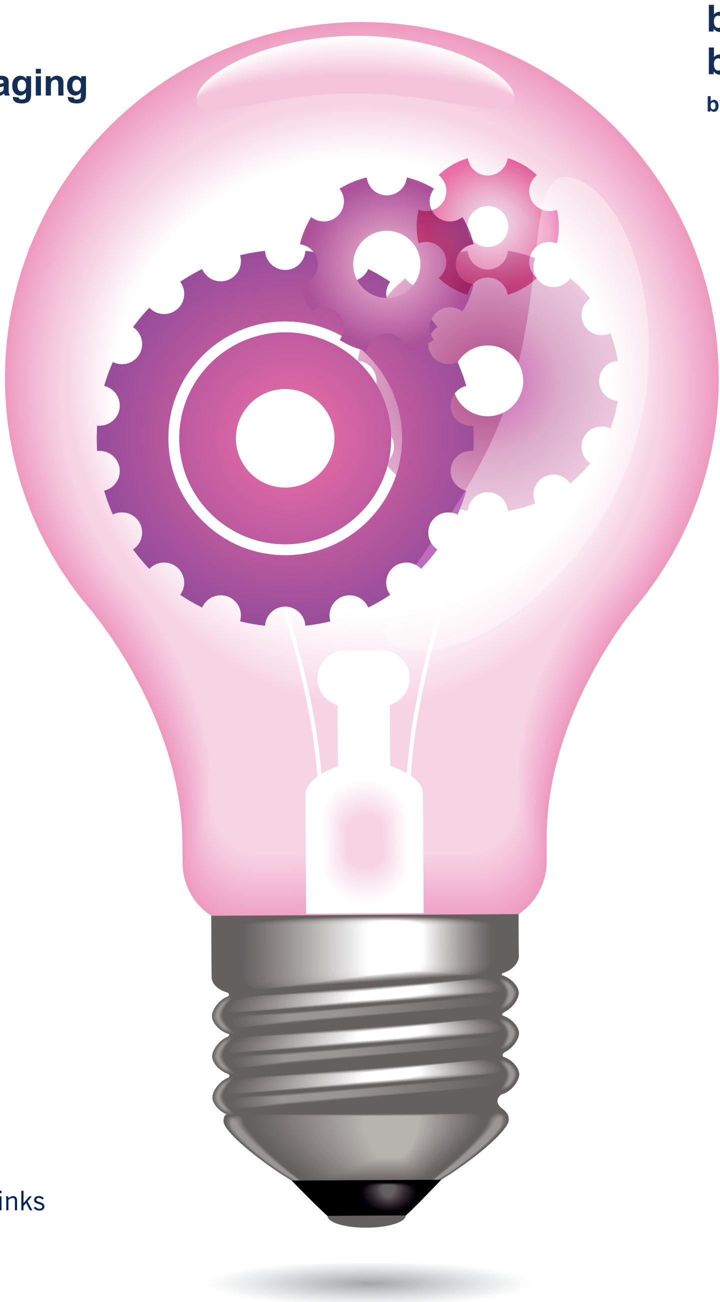

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Change for change's sake?
Internal responses to external challenges

by Henk W. Volberda

In today's increasingly volatile business environment, senior managers have to stay one step ahead by making the necessary internal organisational and strategic decisions, before it is too late to react to external changes.

Decision-makers in firms are facing an unprecedented frequency and amplitude of change in the business environment. More than ever, and in the interests of sustaining their firm's performance and competitive advantage, they must be sensitive to the nature of the marketplace, well-informed as to the latest developments, and well-equipped to respond.

Close examination of the case of Royal Dutch Shell over the period 1980-2007 suggests concrete ways in which firms can accurately assess external change and implement internal change, with a long-term strategic outlook firmly in mind.

Absorptive capacity

The first step in this process is to be fully aware of the ongoing changes in the sector and industry. This embraces such actions as constant monitoring of the competition through to regular analysis of one's own clients, their expectations and any discernible shift in expectations.

The second step is to assimilate the information obtained and understand its potential ramifications for the firm, from its internal organisation through to finances, technical operations, and overall strategy. The third step comprises the transmission of this knowledge into tangible actions for the long-term benefit of the firm.

These three steps add up to what research defines as the "absorptive capacity" of a firm, meaning its ability to not only gather and digest information about the external business world but then respond accordingly by taking operational and strategic decisions in-house to ensure that performance levels are maintained.

The in-depth look at Royal Dutch Shell across a turbulent period for the oil industry illustrates empirically the correlation between the time it takes a firm to respond internally to external change and the impact on performance.

A test case

The potential of the firm to take decisions in response to or in anticipation of change can be based upon the level of research and development (R&D) investment, specifically the intensity of investment (calculated by dividing R&D expenditure by annual revenues). The highest level of intensity (0.84 per cent, for the period 1986-1994) coincided with the oil price collapse, suggesting that forward planning was made.

More sophisticated analysis can be made by correlating this with the difference between the rate of internal and external change.

Internal changes over the period 1980-2007 comprised the launch of new products and services, process innovations, internal and external venturing and organisational restructuring. Some 465 examples were traced, and the relative percentage of each sub-category of action calculated in order to then reach an average rate of internal decision-making and actions per period. The highest internal rate of change came in the period just before the oil price collapse (17.4 per cent, for 1980-85), suggesting that strategic decisions had been taken in advance.

For the oil industry, the external rate of change can be measured via the rate of change of the price of crude oil and its subsequent impact on a firm's profitability, as reflected by its market share. The most volatile periods saw the highest external rate of change and a relatively small gap between the internal and external rates: in

reason that research also underlines the discrepancy between *potential* and *realised* absorptive capacity – having the intention to respond is one thing but if a dominant culture within a firm prevents it from translating the need to respond into action then the risks for performance and profitability are far greater.

However, the highs and lows for Shell measured in the test case suggest that by narrowing the gap between internal and external rates of change or, better still, implementing internal change at a higher rate than external change, firms can give themselves every chance to weather the storm when the business environment is at its most volatile.■

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response to the oil price collapse, the period 1986-1994 saw a 14 per cent internal rate of change compared to a 10.5 per cent external rate, proof that the industry was reacting to external change in an attempt to avert the potentially negative impact of future crises.

This observation is backed up the highest level of R&D investment for the same period and the joint-highest market share (32 per cent). To underline this point, the period marked by the largest negative gap between internal and external rates of change (8.7 per cent vs. 21.2 per cent) and the least intensive level of R&D investment (0.26 per cent) saw the lowest market share result (22 per cent).

Realising potential

On paper the above test case makes perfect sense, but the reality of business today is that not all firms are willing or able to overhaul their internal operations in response to external change.

Research suggests that larger, longer-standing firms are likelier to have the infrastructure to process information and the resources to *potentially* implement change but are often confronted with greater internal resistance to change. It is for this

This article draws its inspiration from the paper *Strategic Renewal Over Time: The Enabling Role of Potential Absorptive Capacity in Aligning Internal and External Rates of Change* by Shiko M. Ben-Menahem, Zenlin Kwee, Henk W. Volberda and Frans A.J. Van Den Bosch (2012), http://dx.doi.org/10.1016/j.lrp.2012.09.012.

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