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OUR FEDERALIST FUTURE: THE LEADERSHIP IMPERATIVE

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Our Federalist Future: The Leadership Imperative

by

James O'Toole and Warren Bennis

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[Abstract: Is it better to be big or small? Are large organizations inherently superior because they possess greater resources to protect the interests of their constituencies against the vagaries of powerful external forces, or are small-scale organizations superior because they are more sensitive to their constituents', needs (and more adaptable to changing conditions)? That unresolved issue is at the core of a roiling controversy in both the geopolitical and corporate worlds. Efforts to resolve it in government and business present a rare opportunity for mutual learning from experiences in those two quite distinct domains. Indeed, successful resolution of this structural issue--arguably, the most critical organizational challenge of our times--will require a willingness of leaders in both sectors to examine common problems and to consider common solutions offered by a few pacesetting companies and countries.

As the issue relates to the structure of government, a creative solution was first put forward by the American Founders who, in the late 18th century, advanced a compromise that has proved eminently functional and durable: federalism. Now, after this 200-year political experiment, variations on the American theme of federalism are suddenly being tested, not only among and between governments around the world, but in new confederations of domestic and international businesses, both large and small.

While sundry forms of de-centralization have been used in large corporations since the 1920's, the emergent form of federalism is something quite different in form and content. In particular, today's federalism seems to work better than its predecessor forms because of the advent of a new style of leadership, which the authors characterize as that of "leaders of leaders." The authors conclude that such a style is "the leadership imperative of the emergent New Federalism."]

> The structure of the organization can then be symbolized by a man holding a large number of balloons in his hand. Each of the balloons has its own buoyancy and lift, and the man himself does not lord it over the balloons, but stands beneath them, yet holding all the strings firmly in his hand. Every balloon is not only an administrative but also an entrepreneurial unit.
>
> --E.F. Schumacher

<u>The Geopolitical Solution: A Template for Corporations?</u>

In these turbulent times, prudent mapmakers work on Etch-a-Sketch pads. Political boundaries change almost weekly as new nations emerge with varying degrees of anguish from the disintegrating empires of yesterday. No part of the world is exempt. From the Balkans to the British Isles, from the banks of the St. Lawrence to Guangdong Province on China's muddy Pearl River, ethnic and linguistic groups are wrestling--often at the cost of their lives--with a fundamental challenge of our era: We'll call it The Iceland Dilemma. In a sentence, the horns of that dilemma are represented by the choice between the advantages of small country autonomy, on one side, and the benefits of big country economies-of-scale, on the other.

Bleakly beautiful Iceland is being pulled and shaped by these two powerful but opposing forces. On one side is the Icelanders fierce pride in their nation's Viking heritage. This pride has led the population of Iceland (in total, some 250,000 shivering souls) to form a committee to give Viking names to concepts that even their visionary national hero, Lief Erickson, never could have imagined. Hence, in Iceland a computer screen is called a <u>skjar</u> (the ancient word for a "window" on a traditional turf house).

But that passion for what is uniquely theirs is only one side of modern Icelandic values. Even as Icelanders quote traditional sagas and support laws to require citizens to choose names for their children from an approved list of "pure" Icelandic origin, those same citizens are eager to enter into active participation in the global economy, to become a part of the highly competitive modern world of international technology, commerce and finance.

Icelandic society is thus a vivid example of what philosophers once called the tension between the tribal and the universal. How to balance tradition and the desire for economic progress, how to be true to oneself while being a partner, and how to sing solo but be in the chorus at the same time--that is the essence of The Iceland Dilemma. Indeed, the entire world today is grappling with the need to strike a balance between nationalism and globalism. And that need is likely to grow more pressing as the new millennium unfolds, considering the fact that there are over 5,000 restless "nationalities" in the world, but only 166 nation states--so far. Clearly, the number of nations should be viewed as just pencilled in, and can be expected to increase dramatically as countries divide and subdivide even further in coming years, all the while seeking simultaneously to be a part of the New Globalism.

Fortunately, there is a generic solution to The Iceland Dilemma: federation. For example, Icelanders are seeking to escape their own particular version of the dilemma through an exogamous marriage with the European Community--joining their fortunes to those of peoples who have little interest in the purity of the Icelandic tongue or in the preservation of Icelandic culture, but who can provide the political and economic clout Iceland needs to be a player in world markets. Indeed, the European Community is the surpassing model of the federalist future. With twelve member states (and counting), the EC is now seen by some three score ethnic groups living in the twenty-five nations situated between Reykjavik and Riga as the best means for them to unify for over-arching political and economic purposes, while at the same time maintaining their cultural integrity. As we shall see, not only is such confederation the most practical resolution of The Iceland Dilemma for nation states, it can be equally as beneficial as a strategy for business corporations, as well.

Government (and Corporate) Federalism

Unlike monolithic forms of government, federations are alliances of more or less independent states, often with little in common but their desire to share in the benefits of swimming in a larger pond. The most durable example of confederation is Switzer-land, where a workable union of divergent cultures has survived for more than 700 years. In modern switzerland, there are 26 semi- autonomous cantons (and half-cantons), which together comprise four major cultural groups, each with their own language and customs. Perhaps the most convincing argument in favor of federalism is that the **Confederaziun Helvetica** endures despite this remarkable diversity (tolerating even the reactionary values of one half- canton that is the last political body in the Western world to deny women the vote in local elections). In general, federations allow member units to pursue their unique--even quirky--interests, to realize their distinctive possibilities, and to address their special needs, as long as they do not compromise the rights of other members or the needs of the alliance as a whole.

In that most successful of federations--our own resilient alliance of states--the whole is greater than the sum of Alabama, Alaska, Arizona and the other disparate but essential components of the union. In these rapidly changing times, such federations as the United States work better than monolithic nations (like the former, misnamed, Union of Soviet Socialist Republics) because they offer flexibility as well as strength. By their nature, federal systems recognize the legitimacy of alternatives, of more than one possible response to a given challenge. If a federation were a poem, it would not be the epic saga of a single national hero, but something like Wallace Steven's "Thirteen Ways of Looking at a Blackbird."

Committed to a single vision and course of action, a unitary government is often too slow to respond to changing conditions. In contrast to the singular stance of the monolithic state, federations are nimble by nature, accustomed to considering a full repertoire of responses. While the unitary nation goes for all or nothing, federations multiply the options and reduce the risk. In theory, at least, federations are also less prone to the ethnic animosities that are the ugliest aspects of hyper-patriotism. The very existence of a federation is implicit recognition that there is strength in diversity. In homogeneous groups, outsiders are too often seen as monsters, devils or obstacles on the road to "racial purity." But it is much harder to dehumanize outsiders in a heterogeneous alliance in which others are viewed as peers and partners (albeit, ethnic vilification is not impossible in federations, as the former Yugoslav republics sadly demonstrate). James Madison, the guiding light of American federalism, argued that the true virtue of such a system lies in its recognition of the natural tendency toward the pursuit of self-interest--and in its built-in mechanism to counter that tendency by protecting the rights of minorities from "the tyranny of the majority."

Because federalism allows constituent units to maintain their integrity while unifying for common purposes, it is not surprising that the form is now a major trend in business as well as in government. For if "Centralization is the death-blow- of public freedom," as Disreli said, it is equally the death blow of corporate innovation. For that reason, many of the world's most influential business leaders are creating new kinds of corporate confederations with numerous semi-autonomous units, often in farflung countries, joined together only to allow them all to succeed better in an increasingly competitive global economy. Examples include: Benetton, Coca-Cola and the newly formed ABB (Asea Brown and Boveri). These companies have become models for international orchestration, influencing the likes of General Electric's CEO, Jack Welch, who uses the rhetoric of the new corporate federalism when he describes the characteristics of the "borderless" G. E. he intends to create.

Significantly, the characteristics of successful national and corporate confederations are nearly identical. Moreover, the following characteristics of federalism have remained constant since they were first described by Madison in the late Eighteenth century, and thus appear to possess almost universal validity.

*__Non-Centralization__. In federations power resides in many semi-autonomous constituent centers, deliberately diffused for the purpose of safeguarding the freedom and vitality of those units. This non-centralization should not be confused with commonplace <u>de</u>centralization (typically characterized by an all-commanding central authority which unilaterally delegates specific, limited powers to its subordinate units). In sharp contrast, a true federal system is contractual and power cannot be rescinded unilaterally or arbitrarily by the-central government (or-central headquarters). For example, the corporate staff at one of America's most truly federalized corporations--Dayton- Hudson--cannot change the rules of the game that affect its Mervyn's and Target divisions. As with the Swiss confederation, such changes may occur only as the result of mutually respectful negotiations, a process that is prescribed in Dayton-Hudson's "constitution."

*__Negotiationalism__. In federations decisions are made in an ongoing process of bargaining between the units and the central authority--and, often, between the units themselves. Thus there is shared decision-making, and the units have a guaranteed voice in defining their financial, administrative and other obligations to the central body. This doesn't mean that Coca-Cola's distributors and bottlers dictate terms to CEO Robert Goizueta; nor, as we shall see, does Goizueta dictate to them, either. Rather, it means that terms and conditions are negotiated and contractual.

*<u>**Constitutionalism**</u>. In federations there is a written (occasionally, unwritten) covenant that binds the allegiance of the units to the basic purpose, mission, philosophy and principles of the overarching institution. Often, this constitution spells out the mutual rights and responsibilities of all parties. Constituent units, in turn, may be free to have their own constitutions as long as these do not violate the basic principles of the articles of federation. Much like the U.S. Constitution, ABB has a 21-page "bible" which lays out the principles by which the company operates, and Dayton-Hudson's 118-page "Management Perspectives" serves much the same purpose.

*<u>**Territoriality**</u>. In federations there are distinct boundaries between the constituent units. In the case of nations, these geographic boundaries may be based on ethnicity or tradition. In corporations, the boundaries can be based on business or product line. (With franchisors like Coca-Cola and Benetton, the boundaries are often geographic).

*<u>**Balance of Power**</u>. Federations seek balance not only between the central authority and the units, but between the units as well (the nineteenth Century confederation of German states failed, in no small measure, because Prussia over-dominated its weaker partners). Part of the negotiations that led to the 1980's merger of Dayton-Hudson and Mervyn's concerned the relative role the California chain would play in the established, mid-west oriented, pecking order of DH's other retail units.

*<u>**Autonomy**</u>. In a federation the units are free to experiment and be self-governing to the extent they do not violate the fundamental principles necessary for the maintenance of the union. Of all the characteristics of federation, this is the most difficult to achieve and maintain. As students of the Civil War are aware, the American union was nearly dissolved because of conflicting interpre-tations of this principle. Over

far less morally significant matters, Benetton recently found itself sued by an angry franchisee who claimed that the corporation was imperiously dictating policies that ran counter to the spirit of the alliance. (We return to this important issue below).

The Necessity--and Fragility--of Federalism

Madison argued that these traits of federalism become necessities when an organization reaches a certain size. While the Founders could imagine successful unitary republics on the scale of the Athenian city state (or Renaissance Venice and Florence), they argued that even the original thirteen United States were too big to function monistically. Their insight seems apposite to corporations, as well. Small, well-managed companies like Ben and Jerry's, Herman Miller and Chaparral Steel operate effectively within a unitary structure and culture and demonstrate little need for federalism. While Madison recognized that size alone is not the only relevant criterion for choosing federalism--diversity is another--it is clearly the single most important reason. Is it coincidental that almost all large social and economic institutions which find themselves in trouble today are unitary in form? From the nation of China, to IBM, to the Los Angeles Unified School System, almost all such monolithic organizations could benefit from a heavy dose of federalism.

In this regard, it is significant that many of history's most successful giant institutions--the Catholic Church, the Roman Empire, the General Motors corporation, to cite three rather large examples--enjoyed their finest hours during periods when they were structured along roughly federal lines. For instance, G.M. reached its pinnacle in the late 1920's when it briefly approached Alfred Sloan's original concept of six confederated divisions; and G.M. was never as unsuccessful as it was in the late 1980's when it had all but abandoned the last remnants of true divisionalization (even producing Buicks on Chevrolet assemblylines).

The G.M. example also illustrates the essential fragility of federalism, an inherent instability that stems from the abovementioned tension between the needs of central authority to exert power versus the rights of the units to autonomy. The art of leadership in a federation is to preserve the balance between those ever-shifting forces. History shows how difficult that art is in practice. Like G.M., most federations have a tendency--fatal in the long term--to overcentralize and homogenize. The old U.S.S.R. is a classic political example of this pattern. And the root of the Soviet problem wasn't simply communist dogma. Under Margaret Thatcher, capitalist Great Britain also did not go far enough in the devolution of authority to the constituent parts of the United Kingdom (and the new democratic Russian "Federation" seems to be regressing toward Soviet- style centralization). The former Union of South Africa was once a relatively effective (but undemocratic) federal state. Then, in the 1950's, power was centralized in order to impose apartheid on the reluctant English-speaking provinces. The result was the erosion of autonomy and the creation of a unitary (and even more undemocratic) republic.

At the other extreme, the United Arab Republic (a short-lived marriage of convenience between Syria and Egypt) had nearly none of the characteristics of successful federations listed above, and consequently crumbled as if constructed of Arabian sand. And conglomerate corporations--like Dart Enterprises in the 1970's--typically disintegrate (or degenerate into mere holding companies) when there is no unifying vision, constitution or federal structure. As with so many conglomerates of the 1960-70 era, the parts of Justin Dart's once-mighty empire are now scattered across the Fortune 500.

The fundamental, and continuing, question facing all federations is this: What powers rightly belong with the central authority, and what powers should be reserved for the constituent units? Madison believed he had solved the question with the U.S. Constitution and Bill of Rights, which basically limited the power of Washington to matters of defense, foreign affairs and regulation of interstate and international commerce. In theory he may have been on target, but in practice he failed to anticipate a slew of complex problems that could not be relegated simply to one box (federal responsibility) or the other (states' rights). The problem came to a head over a moral issue--slavery--and has recurred time and again, particularly in relation to other issues of human rights and, more recently, to environmental questions (for example, we are now agreed that no state has the right to pollute air that blows over neighboring territory). In fact, there has been a steady erosion of the power of the states, particularly in areas of fundamental moral principle. Until recently, Americans had cherished the belief that setting educational policy was a state's right. Yet, today, George Bush--an unapologetic opponent of centralization--argues that the education of the nation's youth is of such overarching importance that it cannot be left solely to the discretion of the states Significantly, his solution to the problem is a classic example of federalist thinking: The national government will set performance standards, and the states and localities will be free to find the most effective ways and means of achieving those standards. This is a specific illustration of federalism's most basic playing rule: The central authority establishes the why and the what; the units are responsible for the how.

Significantly, it is this principle that has been violated, until recently, by almost every business corporation that has attempted to become a confederation. It was this "principle of coordination without losing the advantages of decentrali-zation" that Alfred Sloan attempted, and failed, to define for G.M. in his classic 1921 "concept of the organization" study. In trying to simultaneously achieve co-ordination and specialization Sloan later admitted (in 1963) that forty years earlier he had been "amused to see that [my] language was contradictory." While Sloan never abandoned his wish to resolve his corporate version of The Iceland Dilemma, in practice there was a steady erosion of "states' rights" at General Motors almost from the day he unveiled his federalist structure for the corporation.

In fact, Sloan, his colleagues, and their many generations of successors, were never comfortable with the leadership style required for federalism to work. The system requires several things of those in central authority: faith in the power of people to solve their problems locally; willingness to forgo the satisfaction of exercising command and control; and understanding that in complex systems and turbulent times, no one individual or group possesses enough knowledge to manage the jobs of everyone else in the organization. Sloan--and tens of thousands of managers around the world who were to become his disciples by way of the business school gospel of "specialization/ differentiation" cases--were never comfortable with such basic assumptions about organizations and leadership. Indeed, the most famous practitioner of going-through-the-motions federalism was Harold Geneen, who had the form of confederation down pat at IT&T, but who lacked the essential "feel" for the technology of collaboration to make the system function entrepreneurially.

Therefore, in spite of the rhetoric of de-centralization, neither G.M. nor IT&T (nor the countless giant corporations modeled after them) was ever a true confederation. At least not until the unprecedented turbulence of the late 1980's began to force corporate executives to re-invent Mr. Madison's (and Mr. Sloan's) marvelous notion...this time with feeling.

Resolving the Big Company vs. Small Company Dilemma

Here's the circuitous path by which corporate America has finally arrived at federalism: Historically, America has been the land of the entrepreneur. In no other country have entrepreneurs been revered in legend the way they have been in the United States. Until mid-century, the mythical Horatio Alger and the historical Henry Ford were genuine heros (almost like Napoleon in France or Lenin in the Soviet Union). But, by the end of World War II, the entrepreneur was an endangered species in this country. In the years immediately following the war, so-called "organization men"--the risk-averse children of the Depression --had little interest in chancy careers in the corporations they dominated. Surveying the structure of industry two decades after the war, the renowned Harvard economist J.K. Galbraith declared entrepreneurialism to be an anachronism, and hailed the apotheosis of professional managerialism and giantism. "The planning system" (as he called the industrial form emerging in the 60's) was to be dominated by a few monolithic corporations working in close concert with government ministries. No longer would dozens of small firms compete within a given industry or for a given market. In Galbraith's brave new world, lt would be USA, Inc. vs. Japan, Inc. vs. Germany, Inc. (or, more specifically, General Motors vs. Toyota vs. Volkswagen).

In fact, Galbraith was almost proved right: In the 60's and 70's, the big did get bigger and the number of competitors was reduced. For example, in the jet engine industry there were just three giants: G.E., Pratt and Whitney, and Rolls Royce--the first two of which built the largest factories in the Western World in pursuit of the holy grail of economies-of-scale. Similarly, by 1970, most major U.S. industries were dominated by one or two mammoth firms: G.M. (autos); U.S. Steel (metals); IBM (computers); Exxon (oil); Bank of America (finance); Sears (retailing). In Europe, the pattern was even more pronounced: The Italian government gobbled up scores of small companies and conglomerated them into giant, state-owned groups; in Britain, nearly the entire auto industry was amalgamated into one giant firm. This "New Industrial State" was the right way to go according to Galbraith--and most Europeans believed him: witness Jean-Jacques Servan Schreiber's <u>Le Defi Americain.</u>

Everyone knows what happened next: Within a decade, G.M. had been badly embarrassed not only by smaller Ford and Chrysler, but by a passel of even smaller Japanese and German firms, as well; U.S. Steel was being chopped up by mini-mills: IBM had, literally, hundreds of smaller competitors; Exxon's megalomania had led it to acquire a bushel of small, successful, high-tech companies--and then to micromanage them into failures; Bank of America was being niched to death by financial boutiques and, likewise, Sears by its numerous small competitors in the retailing industry. Thus, by the mid-l990's, the entrepreneur was not only back from the brink of extinction, he (and, now, she) was said to be in ascendancy. In the Reagan era, the giant corporation seemed destined to the fate of the Brontosaurus, and George Gilder was crowing (while J.K. Galbraith was eating crow).

While there can be no doubt that the 80's belonged to the entrepreneur, Mark Twain's oft-quoted line--"News of my death has been greatly exaggerated" --may be finding a parallel in the life cycle of large corporations. Today, it seems wildly premature to join Gilder in assigning big business to the ash heap of history. This is not to defend the past behavior of the many complacent industrial giants who squandered America's precious assets in the 60's and 70's--their self-defeating human resources policies, suicidal customer relations, misguided planning, and faulty financial assumptions are beyond rational defense. Yet, there is no evidence to suggest that the current denizens of the Fortune 500 are collectively about to go out of business--not next week, not next year, not in the next decade (and, not even in the next century). There are several reasons why large corporations continue to survive--and it behooves the enthusiasts of small business to keep these in mind:

Some Inherent Advantages of Large Corporations

* They possess economies-of-scale in finance, purchasing, distribution, advertising, service, R&D (and, arguably, in manufacturing).

* They are able to undertake <u>global</u> marketing.

* They have resources to protect themselves against crosssubsidization (dumping).

* They are able to maintain a large, diverse bank of skilled people (which allows them to invest in lengthy training for future assignments, and to survive the loss of key individuals).

* They possess the organizational wherewithal and managerial know-how to bring more than one project at a time from the idea stage into full development.

* They provide key employees with a relatively high level of security and financial benefits.

* They are able to undertake the long-term planning and commitment of resources needed for giant, capital intensive products (e.g., a jet airplane).

* They have social clout with government and unions.

* They can afford basic research, and to undertake slow, costly, incremental improvements in process technology.

* They have stability because they can afford to be integrated backwards (to suppliers) and forwards (to dealers).

* They tend to be diversified and, hence, less susceptible to vagaries of the economic cycle (and less vulnerable if one or two key products fail).

While all this stability, security, predictability, synergy and discipline are, at best, theoretical advantages of large business, sufficient examples can be supplied to support most of these claims. After all, what small firm would not want to have the financial, service, marketing; distribution, purchasing and R&D punch of an IBM? Especially--and this is the key point--if those benefits of size could come without the disbenefits of bureaucracy.

Which brings us conveniently to the advantages of small and medium-sized businesses. Because there are so many static "mom 'n pop" firms which cannot serve as models of eminence, we have in mind here the characteristics of Inc. Magazine's list of the fastest-growing entrepreneurial businesses:

Some Inherent Advantages of Small Firms

* They tend to be lean, agile, dynamic and flexible (nonbureaucratic).

* They are close to their customers and, thus, sensitive to (and fast to react to) shifts in market demand. They are run by managers who often are owners and, thus, highly motivated by their equity positions.

* From top to bottom, nearly everyone in the company has direct, going personal knowledge of most aspects of the business.

* Their employees are motivated by the human scale of the organization, by peer pressure, and by knowing how their parts contribute to overall company performance.

* They have excellent upward, downward, and lateral communications.

* They attract the most creative, energetic and risk-taking individuals (indeed, there is a "brain drain" from large _ to small companies).

* They have a focused orientation on a single product or related line of products. They have shortproduction runs and, thus, can customize products and keep a constant watch on quality.

The Big Mimic the Small

These impressive advantages are, in fact, the very characteristics of small firms that almost all large corporations today are attempting to capture through frantic attempts to alter their "corporate cultures." In order to "get close to customers," to "become people-oriented," and to "focus on quality" giant corporations around the world are experimenting with intrapreneuring, gainsharing, team approaches, spin-offs, product-line focusing, specializing, downsizing, dis-integrating, subcontracting and decentralizing--in effect, emulating what small companies do naturally.

Hence, in this paradoxical world, we are faced with yet another fine irony: While entrepreneurs are trying to capture the advantages of large firms, managers of large corporations are, at the same time, attempting to behave like entrepreneurs! Therefore, it would seem as misguided today to speak of the decline of large organizations as it proved inaccurate twenty years earlier to speak of the fall of entrepreneurs. While smallness is usually more beautiful, bigness is simply a fact of life in a world where three billion people are increasingly linked by common technologies and markets.

It may be useful to think about this issue by way of analogy: Is the mega University of California going to give way to competition from hundreds of small colleges? Is the unitary government of France going to devolve all its power to the country's myriad **departements**? Is Boeing soon to give way to smallscale manufacturers of jumbo jets? While a reasonable answer to each of these questions is negative, the most likely scenario is that the structures of giant universities, central governments and colossal corporations will change to forms beyond our current ability to envision. Although we can't imagine exactly what these new structures will look like, it nonetheless seems reasonable to expect that almost all organizations which survive and thrive in the future will possess the best characteristics of both today's big and small successes. That is why in so many well-led large organizations efforts are being made to overcome diseconomies-of-scale by creating dozens of small, independent, manageable units.

The Small Mimic the Big

While the giants attempt to avoid extinction by imitating the behavior of fast-moving small companies, the parallel challenge for entrepreneurs in coming years is to build global markets by capturing the advantages of gargantuan firms. Fortunately, meeting this challenge will be facilitated by emerging, computer- based technologies of production and distribution. Newly developed manufac- turing tools give small companies the advantages of mass production while, at the same time, allow them to customize products economically. New telecommunications technologies provide access to distant and specialized markets that were formerly out-of-reach for all-but giant firms with global distribution networks. Sophisticated data bases provide even the smallest companies with marketing information that just yesterday was affordable only to the largest. And all this technology is currently available. At present, American fabric and apparel manufacturers are linked by computer to hundreds of retailers, thus giving increased purchasing power to the small firms, and faster inventory information to the manufacturers, all of which permit U.S. companies to use technology .o help overcome Asia's competitive wage advantage.

By fine-tuning the federal strategy by which the small, semiautonomous American states combined and cooperated in order to gain the advantages of a large nation, small businesses around the world are creating networks, partnerships, consortia and federations--all designed to give them the functional equivalent of bigness. The best-known company pursuing a federal strategy is Benetton, where finance, R&D, design, purchasing and planning are centralized, while the activities of manufacturing and retailing are dispersed. The company is a unique confederation of hundreds of small, manager-owned manufacturers and franchised retailers all linked together by computer to form the United States of Benetton. Like Benetton, such companies as Nike and The Limited also have learned that it is better to achieve the benefits of forward and backward integration through confederation rather than through acquisition.

Importantly, there is no single model of confederation. As Rosabeth Moss Kanter was the first to observe, companies around the world are "becoming PALs: Pooling, Allying and Linking" across corporate and national boundaries.[1] Small

[1]Rosabeth Moss Kanter, When Giants Learn to Dance, Simon and Schuster, 1989. (Chapter 5)

companies, in particular, are inventing all manner of joint ventures, subcontracting, franchising, R&D consortia, and strategic partnerships. These are taking the form of cooperation between customers and suppliers, between domestic and foreign entities, between large and small organizations--and even among competitors: after all, entrepreneurs are willing to do whatever it takes in order to combine the advantages of big and small. Some examples: small record and book publishers (and film producers) use the services of large distributors to gain economies-of-scale in marketing; small airlines form consortia to buy jet aircraft from brokers in order to gain economies-of-scale in purchasing; small "hollow" corporations design furniture, contract to have it made in Third World countries, and then wholesale it to large department stores in Europe and America (or market their products themselves in stores-within-stores). As our colleague Jay Galbraith explains, the common thread in each of these examples is that small companies "buy the power of bigness"--that is, they have someone else provide the scale in marketing, purchasing, financing, or manufacturing that is uneconomical for the small company to attempt itself.

The federal form has applications not only for manufacturing and retailing, but for service industries, as well. American Airlines' SABRE system uses high technology to link the worldwide fortunes of numerous large and small competitors in the airline industry. In the U.S., early every service from real estate to plumbing has been successfully franchised, and international professional services firms like Arthur Anderson are, in fact, prime examples of the federal system. And Coca-Cola, with its global network of franchised bottlers and distributors, is the longest-standing--and most successful--example of the advantages of confederation.

Federalism as a Re-Vitalization Strategy

Of more recent origin--and less-conventional structure--is the confederation ABB which employs more people around the world than live in the entire country of Iceland. Although some components of the company are over a hundred years old, ABB's CEO, Percy Barnevik, has demonstrated the validity of federalism as a strategy to re-vitalize old-line manufacturing firms for competition in today's world markets.[2] Barnevik explains that ABB "is a company with no geographic center, no national ax to grind. We are a federation of national companies with a global communications center." Barnevik is not worried by the contradictions that led Sloan to abandon federalism: "ABB is an organization with three internal contradictions. We want to be global and local, big and small, radically decentralized with centralized reporting and control."

The managerial secret that allows ABB to turn these contradictions into what Barnevik calls "real organizational advantage" is federalism with a vengeance.

ABB's operations are divided "into nearly 1,200 companies, with an average of 200 employees. These companies are divided into 4,500 profit center with an average of 50 employees." With only 100 professionals in their Zurich headquarters, the company is not unified by the efforts of an all-powerful central staff a'la G.M. Rather, this non-centralized confederation of semi-autonomous units is held together by common vision of globalism, excellence, and clearly enunciated responsibilities for performance. What is role of central headquarters? "To operate as lean as is humanly possible,: says Barnevik. And the role of leadership? To give managers "well-defined sets of responsibilities, clear accountability, and maximum degrees of freedom to execute."

The Leadership Imperative

The sharpest image of the new federal leader that comes to mind is that of Coca-Cola's Robert Goizueta at a recent meeting of the company's bottlers and distributors where he was observed to implore those fiercely independent folks at least three times in one speech to "please paint your trucks red." How's that? In the year in which he earned some $80 million, the CEO of Coca-Cola had to plead with "his troops" to adhere to standards of corporate conformity? Clearly something new is going on here. And that something is that leaders of federations don't think of their associates as troops--and the associates don't think of their leaders as generals.

2William Taylor, "The Logic of Global Business: An Interview with ABB's Percy Barnevik," HBR March-April 1991

Like ABB, Coca-Cola's federalism is effective in a way that Sloan never could never have imagined because of a factor that emerged nearly three decades after the G.M. chief's death: A new concept of leadership. Sloan was a brilliant leader of G.M., but therein lay the fatal flaw in his attempts to install federalism: Sloan was also the only leader at G.M. In sharp contrast, the new leaders of the emerging federal corporations are leaders of leaders who, like Percy Barnevik and Robert Goizueta, are willingly followed by other leaders who have subscribed to their "vision."

It became commonplace in the 1980's that the new leader is one who has the ability to generate a compelling, moving and unifying vision. This means the ability to establish a climate and structure that gives all members of the organization a clear sense of what they are doing and why. What has not been fully appreciated about "the vision thing" is that the purpose of a clearly communicated vision is to give meaning and alignment to the organization and, thus, to enhance the ability of *all* employees to make decisions and to create change. The new leader does not make all decisions herself; rather, she removes the obstacles that prevent her followers from making effective decisions <u>themselves</u>. Thus, not only is the standard military leadership metaphor of generals and troops wrong, so is the classical peacetime metaphor of shepherds and sheep. The new leaders are no more shepherds than their followers are sheep. A more fitting metaphor is Schumacher's balloon man--now, a woman-- who holds a fist-full of strings attached to countless units, each tugging away because it is filled with the helium of entrepreneurial spirit.

Indeed, when we describe the emerging leadership relationship in today's federal organizations we come closest when we speak of *leaders of leaders*. In these organizations, senior leaders are followed willingly by other leaders by virtue of the formers' vision, integrity and courage (and not just by the organizational equivalent of a yank of the crook or the nipping of a sheepdog at the heels). Importantly, because people at *all* levels are leaders in their own right, there is little of the resistance to change that characterizes the middle ranks of most hierarchical organizations headed by a single commander -in-chief and staffed by layers of resentful sheep. In the emerging leadership relationship, it is far from easy for the outsider to identify the leader. As the Chairman of Herman Miller, Inc., Max De Pree, explains, "The signs of outstanding leadership appear primarily among the followers. Are the followers reaching their potential? Are they learning? Serving? Do they achieve the desired results? Do they change with grace? Manage conflict?" If so, the organization is blessed with an outstanding leader of leaders.

In the successful federal organization, a central--perhaps <u>the</u> central--task of the leader of leaders thus becomes the development of other leaders. At Dayton Hudson, Kenneth Macke spends about half of his time on the career development of the firm's top one hundred managers. With 4,500 employees in potential leadership positions, Percy Barnevik's job becomes one of creating the conditions in which all those people can succeed in their jobs. In effect, federalism provides a structural skeleton for the rhetorical goal of "empowerment." Thus, Federalism does not obviate the need for leadership; instead, it focuses and redefines the task of the leader. The success of the current president of the European Commission of the EC, Jacques Delors, illustrates the necessity of federal leadership characterized by the provision of inspiring vision--coupled with the identification, nurturing and development of future leaders empowered to carry out that vision.

Ultimately, federalism also may pave the path toward more democratic organizations. When we ask, "Is democracy inevitable?", the answer is a more resounding and immediate "yes" in federal systems.[3] For as Jefferson and Madison recognized, democracy is more natural in smaller units, and less-wieldy in large, unitary states. Lest this federalism sound like soft-headed, "touchy-feely" management, it is worth noting that George Will has called for a marked return to federalism in the American system of government: "That is the future--congressional ascendancy and vigorous federalism. We can live with that. The Founders said we should."

[3]Warren Bennis, "Is Democracy Inevitable?" HBR Sept.-Oct. 1990

" A Pretty Good Alliance."

In essence, federalism allows nations and corporations to have their organizational cake and eat it, too. Given proper leadership, the new federalism--whether in the guise of ABB or the EC--illustrates that it is possible to pursue innovation, self-governance and autonomy, while at the same time enjoying the advantages of effective coordination, economies-of-scale and the protection of cherished freedoms that only pluralism can provide. From a business perspective, federalism erases the false "big versus small" dichotomy that has for too long preoccupied those engaged in debate about the essential traits needed for international competitiveness, much as it points the way towards variations on the theme of confederation that could lead to truly effective performance in the global economy.

Finally, we can imagine a time when corporations such as ABB--which are simultaneously global and deeply rooted in local cultures--serve as models for nations that aspire both to national self-expression and to survival in the world economy. These new confederations could resolve The Iceland Dilemma, and the only cost would be the loss of the jingoistic rhetoric of which national mottoes and state anthems traditionally have been composed. The slogans of the federations of the future probably won't be as stirring as the national slogans of the past. It is true that "My federation, a pretty good alliance" doesn't have the ring of "My country, right or wrong." But a world of overlapping and interwoven corporate and national federations would be a far better place in which to work and live.