

# Organizational Design in Modern Firms and the Role of Corporate Management: Relationships of Organizational Change with Trust and Creative Capacity

**Nobuhiko Yamanaka,**

*Graduate School of Business Administration, Rikkyo University*

*Japan Academy of Management E-mail: n\_yamanaka@rikkyo.ac.jp*

## **Abstract**

This study seeks to determine whether employees' trust in management and the company itself has any effects on organizational change. In particular, this seeks to reveal its effects on organizational design changes undertaken in response to a major strategic challenge facing companies today: how to stimulate innovation and creative capacity.

The results of analysis demonstrate that institutional changes in an organization influences employee trust in management, which in turn acts to mediate the effectiveness of organizational changes. Initiatives that involve what this study identified as "comprehensive change" can raise trust in management, avoiding morale problems and helping companies to unleash their creative capacity. On the other hand, so-called "cost-cutting, flattening change" risks damaging employee trust in management and can bring about severe morale problems.

These findings suggest the importance of integration in organizational design and emphasize the essential roles for corporate management in the development of healthy social structures and relationships in the businesses.

**Key words:** Organizational design, morale, complementarity, trust, creative capacity

## **(1) Study Background and Purpose**

Discontinuous change in the modern business environment has forced many companies to reconsider their organizational design. Initiatives to review traditional organizational designs and explore new ones are spreading in Japanese firms as well. A business organization can be understood as an instrumental system configured to achieve a unique objective. From this perspective, we can conclude that the institutional transformations in Japanese firms today correspond

to attempts to accomplish strategic tasks more effectively in the face of environmental turbulence. Let us assume that businesses today face the dual challenge of how to innovate in order to generate added value discernible to customers, and how to unleash their organization's creative capacity to deliver that innovation. In this light, organizational change in the modern era can be interpreted as a technical challenge: what kind of organizational design(s) should businesses choose to effectively encourage employees to innovate and to

deploy this creative capacity?

However, business organizations consist of two layers, corresponding to their technical structure and their social structure. Businesses can only improve the effectiveness and efficiency in technical terms by “genuine fostering in their employees a will to work” through ensuring “development of healthy social structures and relationships in the business” (Mohri, 1965, p. 21). Viewing organizational design as a mere technical problem limits our understanding to only one side of the story. While organizational design indeed has technical aspects, it must also be recognized as a social issue: i.e., how to ensure “development of healthy social structures and relationships in the business” to instill in employees this “will to work”.

Many problems are known to occur during the organizational change process, including decreased willingness to work, uncooperative attitudes, and low morale due to resistance or opposition to the change process, or simply confusion, among employees and managers alike. This paper refers to these inclusively as “morale problems” associated with organizational change. Dealing with morale problems means addressing “social structures and relationships in the business”, which often determine the success or failure of organizational changes. Management is tasked with the important responsibility of solving them in their role as the “designers” of an organization (Roberts, 2004, p. 12).

In interpersonal relationships, when ensuring the intentions and behavior of other people are appropriate comes with certain risks and when the achievement of interests of an individual may depend on another person, trust is essential in these cases. Trust can

be defined as “a psychological state comprising the intention to accept vulnerability based upon positive expectations of the intentions or behavior of another” (Rousseau et al., 1998, p. 395). Odaka identified “trust” in work colleagues, managers, and supervisors as essential components of organizational morale (Odaka, 1981, pp. 390-391). Accordingly, “trust” in an organization and management should be essential for dealing with morale problems associated with organizational change.

Executing organizational changes is associated with high risk: while the effects are felt throughout the whole firm, there is no guarantee the efforts will be successful. The mere presence of risk can generate anxiety and confusion among employees, which in turn can easily trigger serious morale problems. Accordingly, protecting employee morale by promoting coordination and collaboration within the organization in order to improve cohesion is indispensable to the success of organizational changes.

This means that organizational change demands leadership as well, to “offer direction and then motivate others to believe and to follow” (Roberts, 2004, p. 284). Whether leadership can succeed or not would seem to depend on the level of trust employees and managers alike have in their company and its management personnel. This is because trust in a company and its management are necessary prerequisites to overcoming the morale problems associated with organizational changes and ensuring those changes take root, serving as a basis for the legitimacy of corporate leadership and a foundation for their support.

Organizational trust is also essential to

enabling innovation and unleashing the creative capacity of a company. Bellah et al. write that “the productivity of a high-tech company resides in the quality of its workforce, in the competence and responsibility of individuals, but also, critically, in the trust they have in each other to nurture creativity and innovation”, and that companies need “persons who trust each other and genuinely enjoy working together” (Bellah et al., 1991, p. 94). This claim implies that individuals within an organization need to form trusting relationships with each other in order for a given organizational design to successfully stimulate its employees to innovate and unleash their creative capacity.

This study is an attempt to address the issues defined above. Namely, it seeks to determine whether employees’ trust in management and the company itself has any effects on organizational change. In particular, it seeks to reveal its effects on organizational design changes undertaken in response to a major strategic challenge facing companies today: how to stimulate innovation and creative capacity.

## **(2) Preceding Research**

### **1. Organizational Change and Morale Problems at Japanese Firms**

Since the 1990s, Japanese firms have attempted to transform their organizational structures in various ways to adapt to rapid changes in business environments. However, few studies have endeavored to clarify the actual results of these transformations, nor their impacts or positive effects. Moreover, it is rarely obvious how the organizational changes in Japanese firms in recent years relate to the modern, strategic challenge of

stimulating innovation and unleashing an organization’s creative capacity, nor how morale problems associated with these changes relate to their success or failure.

One study whose findings bear significance on this research topic is that of Inoue (2004). Inoue analyzed the so-called “selection and concentration” strategies adopted by Japanese electronics and information-related companies, and how they were complemented by organizational changes such as hierarchical flattening, decentralization of authority, subcontracting, and departmental consolidation. He found that measures such as cost-cutting, subcontracting, and reductions of business scale were compatible with the pursuit of “efficiency” (typified by cost-cutting). He also found, however, their efforts to externalize business and reduce scale acted to inhibit their “effectiveness” (e.g. in creating market value).

One of his observations on companies’ “selective withdrawal” in particular is very interesting and relevant to the research problem at hand: corporate readiness to externalize business operations actually lowered employee morale, reducing their “commitment and tenacity to work”, and impeded their ability to solve problems creatively to generate innovative products and services (Inoue, 2004, 102). Inoue’s findings reveal that while modern Japanese firms have made considerable changes to their operational structures, those same changes have led to their own inextricable problems. At the same time, they suggest that morale issues due to certain kinds of organizational change can hinder companies from exercising their full creative capacity. The present study seeks to investigate such

morale problems from the perspective of organizational trust.

## 2. Trust in Japanese Firms

Trust has become an interdisciplinary topic, with research efforts spanning different disciplines such as economics, psychology, and sociology. Japanese organizational research is no exception. In one study, Hino focused on the relationship between “leaders” and “followers” in an organization. Along with determining several factors necessary for the formation of trust in leaders among followers, he revealed that this formation was crucially necessary for leadership to function (Hino, 2010). Another study, directly relevant to this study’s research problem, is that of Tatsumichi, who conducted a survey of employees of Japanese firms looking at changes in their attitudes towards their company and management personnel. Based on the results, he claimed that in the midst of recent reforms in personnel systems, that “a ‘chasm’ of some kind seems to have formed between employees and their company, and moreover between them and management” (Tatsumichi, 2006, p.285). His findings suggest that the trusting relationships between employees and their companies and managers may have incurred some damage in Japanese firms as they continue to evolve and implement organizational changes.

The relation between institutional transformations in Japanese firms and organizational trust was also analyzed by Miyamoto: specifically, as the relation between recent corporate governance reforms and employee trust. Finding unexpectedly high support among employees for shareholder-oriented governance, Miyamoto attributed it to

be mediated by their trust in management. In his words: “Employees support managerial behaviors intended to increase shareholder value as their trust in management grows. Conversely, their support for shareholder value-centric management falls as their trust in management decreases” (Miyamoto, 2008, pp.99-100). Miyamoto’s research demonstrates that employee attitudes, and particularly their trust in their managers and the company itself, are important factors to consider during management reforms and organizational changes, as the perspectives of organizational members can crucially impact their potential for success. Building on this body of work, the present study hypothesizes that the success and effectiveness of organizational changes intended to facilitate innovation and unleash the creative capacity of firms are mediated by trust among members of the organization.

## (3) Theoretical Framework and Variable Configuration

The theoretical framework of Whittington and Pettigrew’s “innovative forms of organizing” was adopted to guide this study’s variable configuration and analysis. These scholars argued that dramatic changes in business environments, such as the transition to the globalized economy and the knowledge-based economy, encouraged modern enterprises to introduce “innovative forms of organizing”. Along with real examples in European firms, they showed how different forms had complementary effects within organizations. Their analysis demonstrated how “complementarities” are essential to their successful introduction, and that companies could

suffer harm by failing to achieve mutual complementarity between disparate organizing forms, calling this phenomenon “the dangers of partial change” (Whittington et al., 1999). Whittington and Pettigrew’s research provides us with a useful framework for conceptualizing and analyzing structural and process changes in modern business organizations, as well as their effects, in a comprehensive way.

Variables in the present study were configured to match the dimensional configuration of related research on innovative forms of organizing, so as to capture structural and process changes in the same framework. To operationalize the variables, new scale items were created to capture real organizational changes underway in Japanese businesses today. The following were set up as *organizing forms-related variables*: *hierarchical flattening*, *strategic decentralization*, *operational decentralization*, *project-based organizational structures*, *downsizing*, *IT investment*, *communications and systems integration*, *strategic restructuring*, and *outsourcing*<sup>1</sup>.

Two other variables, corresponding to *creative activities* and *creative achievements*, were set up to examine another important factor: the relationship of organizational changes with innovation and creative capacity. For the former, employees would be asked to what extent their organization carried out initiatives and efforts aimed at creative results.

For the latter, they would be asked to what extent their organization produced real, tangible creative results. These were both subjective measures in the sense that their scores depended on the individual perceptions of respondents: thus, the variables were termed *Subjective Creative Activities* and *Subjective Creative Achievements*<sup>2</sup>.

In addition, this study used scale items adopted by Tatsumichi (2006) and Miyamoto (2008) to measure employees’ trust in management and their organization. Along with directly measuring whether or not “management is trusted”, Tatsumichi’s scale measures factors like whether an employee’s “company is completely devoted to its employees, even when their performance is bad”, and whether “employees are valued”. The scale allows users to measure employees’ positive expectations of the intentions and behavior of their corporate management, as well as their company overall. Thus, it was incorporated in the present study in the variable *Trust in Management*<sup>3</sup>.

#### (4) Survey Overview and Data Used in Analysis

Two approaches were necessary to describe and understand the actual operations of firms in terms of the underlying organizational structures and processes controlling them. First, to learn how different individuals

<sup>1</sup> There is insufficient space to describe the items composing each variable. Suffice to say, the variables had sufficiently high internal consistency for analysis purposes (the lowest reliability coefficient observed for any variable was 0.793, for “outsourcing”).

<sup>2</sup> *Subjective Creative Activities* consisted of 5 items such as “My company develops new products and services ahead of our competitors”, while *Subjective*

*Creative Achievements* consisted of 3 items such as “My company has increased the number of new products and services offered in the past 2 years”. Their respective reliability coefficients were 0.934 and 0.831.

<sup>3</sup> The reliability coefficient of this variable based on Tatsumichi’s scale items was 0.920.

within organizations perceive those structures and processes as ‘social realities’ in their workplace; second, to determine the perceptions and expectations of management, as well as an organization itself, by its constituent members.

To this end, a survey was administered to general employees and management personnel employed in different departments in a variety of organizations. The survey was administered through the internet in January 2014 to general employees and managerial personnel working at private companies in Japan<sup>4</sup>.

Sampling bias, specifically in terms of respondent attributes, is a problem that has been identified with internet surveys, and could not be avoided in this study. However, problems have also been noted for conventional surveys, such as difficulties in retrieval: the internet survey methodology was adopted based on a decision to prioritize data collection. In addition, the survey was administered to individuals, based on the study’s motive of understanding organizational realities from the perspective of individual employees: this meant sample representativeness was another potential issue with the data. Nevertheless, this method was still deemed suitable for the study, given the dual objectives of determining various organizational members’ perspectives about corporate management and company overall, and understanding their ‘organizational realities’ as the real social environment experienced by in-

dividuals within their organization. In addition, readers should also keep in mind that since data about organizational structural characteristics, perceptions of management, and creative activities and achievements were all collected from the same individuals, the potential for common method bias cannot be completely eliminated.

In total, 300 responses were collected; 186 were analyzed after excluding individuals who responded “Unknown” to questions about the capital and sales of their firm. Compared with national averages, a somewhat greater proportion of respondents were employed in the manufacturing industry, and a greater proportion at large enterprises (although there was no shortage of employees of small and medium enterprises). Further, many respondents worked in sales or R&D departments, and many were clerical workers; however, there also many individuals in professional occupations. Other notable characteristics of the sample included the fact that over 40% were senior officials (i.e., designation of “Chief/Head” or higher), and a somewhat high number over 40 years old.

The effects of industry type, company size, department, and managerial staff (yes/no) were controlled for in analysis by inserting these factors as control variables.

## **(5) Analysis Results**

### **1. Derivation of Organizational Change Patterns**

Two major characteristics of organiza-

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<sup>4</sup> This survey was conducted as part of a 2009 Strategic Research Foundation Grant-aided Project for Private Universities from the Ministry of Education, Culture, Sports, Science and Technology: *Practical*

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tional changes in Japanese firms were apparent based on whether and to what extent each of the specific organizing forms described above were confirmed by respondents:

1) Firms tended to implement changes to a project-based organizational structure, focusing on company-wide cost reductions and reviewing their businesses and operations;

2) Firms tended to emphasize rigorous review of the responsibilities of operational managers, along with information sharing, cooperation, and support within the organization. However, they seldom implemented approaches such as strategic or operational decentralization, hierarchical flattening, dis-

establishing or closing departments, or reducing the number of management personnel or official positions.

However, we know from the work of Inoue, Whittington and others that organizing forms are more effective when introduced in a mutually complementary way, rather than separately. Assuming this holds true here, we can imagine that organizing forms are put into practice in certain combinations or 'units', and further that these units tend to follow certain patterns. This study derived these 'patterns' via principal component analysis, in an attempt to determine the major trends underlying institutional transformations in Japan.

Two principal components were extrac-

**Table 1. PCA Findings for Organizing Forms**

Organizing Form Variable	PC1	PC2
hierarchical flattening	<b>0.728</b>	<b>0.492</b>
strategic decentralization	<b>0.895</b>	-0.149
operational decentralization	<b>0.848</b>	-0.270
project-based organizational structures	<b>0.786</b>	-0.211
downsizing	<b>0.655</b>	<b>0.599</b>
IT investment	<b>0.796</b>	<b>-0.376</b>
communications and systems integration	<b>0.762</b>	<b>-0.477</b>
strategic restructuring	<b>0.866</b>	0.110
outsourcing	<b>0.596</b>	<b>0.578</b>
eigenvalue	5.416	1.456
percentage of variance	60.175	16.175
cumulative variance	60.175	76.35

ted in the analysis (PC1 and PC2:Table 1).

PC1 exhibited high factor loadings and positive correlations for all organizing form-related variables. Given that all organizing forms are promoted in a comprehensive manner in this change pattern, we can term this component *Comprehensive Change*. PC2, on the other hand, showed high factor loadings and positive correlations for organizing forms such as hierarchical flattening, downsizing,

and outsourcing, but negative loadings for IT investment and communications and systems integration. In other words, this change pattern was characterized by the reduction of both business cost and operational scope, with an accompanying increase in external procurement, while failing to maintain investments in IT and efforts at intra-firm integration. Accordingly, we can term this component *Cost-cutting, Flattening Change*. The above

analysis revealed the existence of two patterns in organizational changes: *Comprehensive Change* and *Cost-Cutting, Flattening change*.

## 2. Relationship of Creative Capacity with Organizational Change and Trust in Management

The study next sought to analyze how firms' utilization of their creative capacity related to these organizational change patterns, and moreover how trust in management affected this relationship. According to our hypothetical framework outlined above, institutional transformations inevitably generate resistance, confusion, and opposition within an organization. However, the presence of trust in a firm's management can avoid the consequent dysfunction and diminished morale, allowing these transformations to take hold and effect. In short, organizational change is presumed to be mediated by trust in management, which influences the consequences of any institutional change: its effects should be especially strong on organizational changes aimed at liberating the creative capacity of a firm.

The mediating effects of trust in management were analyzed according to the procedure of Baron and Kenny (1986). Several models were constructed:

1) Independent variables = *Comprehensive Change* and *Cost-Cutting, Flattening Change* (i.e., their principal component scores); dependent variable = *Trust in Management* (Model 1);

2) Independent variables = *Comprehensive Change* and *Cost-Reducing, Flattening Change*; dependent variable = *Subjective Creative Activities* (Model 2) or *Subjective*

*Creative Achievements* (Model 4);

3) Independent variables = *Comprehensive Change, Cost-Reducing, Flattening Change*, and *Trust in Management*; dependent variable = *Subjective Creative Activities* (Model 3) or *Subjective Creative Achievements* (Model 5).

Three things needed to be shown for the mediating effects of trust in management to be confirmed: in 1), organizational change patterns needed to affect trust in management; in 2), organizational change patterns needed to affect firms' creative capacity; and in 3), trust in management needed to affect firms' creative capacity, *and* the effect of organizational change patterns on firms' creative capacity needed to be *smaller* than in 2) (Baron and Kenny, 1986, p.1177).

The results for Model 1 in Table 2 demonstrate that comprehensive change increases trust in management, while cost-cutting, flattening change decreases it.

Moreover, trust in management mediated the effects of both types of change pattern on both creative activities (Models 2, 3) and creative achievements (Models 4, 5). Besides, the value of adjusted R square is higher in mediation models (Models 3 and 5) than in models without mediator (Models 2 and 4). This suggests that mediation models explain the effect of organizational change on firms' creative capacity better than otherwise.



**Table 2. Mediation Analysis Findings for Trust in Management**

Dependent Variable	Trust in Management	Subjective Creative Activities	Subjective Creative Activities	Subjective Creative Achievements	Subjective Creative Achievements
	Model 1	Model 2	Model 3	Model 4	Model 5
Comprehensive Change	.587**	.583**	.365**	.538**	.271**
Cost-cutting, Flattening Change	-.452**	-.278**	-.102	-.199**	.016
Trust in Management			.374**		.457**
R <sup>2</sup>	.647	.532	.591	.479	.562
Adj. R <sup>2</sup>	.563	.418	.486	.354	.451
F value	7.687**	4.693**	5.633**	3.829**	5.055**
VIF	1.123-2.419	1.141-2.403	1.127-2.803	1.126-2.380	1.130-2.834
N	157	155	153	156	154

†  $p < .1$ , \*  $p < .05$ , \*\*  $p < .01$

## (6) Conclusions and Future Challenges

The study findings demonstrate that institutional changes in an organization influences employee trust in management, which in turn acts to mediate the effectiveness of these changes. Initiatives that involve what this study identified as *comprehensive change*—i.e., promoting intra-firm integration, decentralization, and IT investment alongside flattening and outsourcing—can raise trust in management, avoiding morale problems and helping companies to unleash their creative capacity. Whereas, so-called *cost-cutting, flattening change* risks damaging employee trust in management and can bring about severe morale problems. Put another way, the consequences of an institutional change seem to depend on the contents of the change itself. Poorly configured change can damage trust in management, and trigger resistance, confusion, and the loss of working motivation within an organization. However,

if the change embodies certain specific characteristics, confidence in management will be strengthened, and the effects of the change potentiated. Along with alluding to the importance of *integration* in organizational design—the *big-picture* perspective that takes into account the entire situation of an enterprise—the findings suggest that *the development of healthy social structures within businesses* serve to complement and effectuate institutional changes. Corporate management shoulder essential roles in the task of designing an organization: they must not only foster trust in management among company employees, but also ensure the development of healthy social structures and relationships within the firm, which can serve as a foundation for smooth collaboration. This fact must be acknowledged today anew.

This study nonetheless has a few limitations. For one, “trust”, “morale”, and other constructs fundamental to the study hypothe

sis were not directly measured or analyzed. New theoretical and empirical investigations of these constructs are necessary. Second, mediation analysis does not reveal anything about the cause-effect relationship of a phenomenon. Case studies and other methods should be adopted to help elucidate the causality of the relationships identified here. Third, the survey methodology meant that sample representativeness could not be ensured, and common method bias could not be controlled for. Additionally, the priority placed on effective data collection was inextricably associated with limitations on the data available for analysis, suggesting the study method could use improvement. Readers should proceed with caution to avoid generalizing the study findings in an over-simplistic way. New investigations should be conducted to improve on this study's weaknesses and validate its findings.

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