THESES

Péter Füzes

Strategic renewal and disruptive innovation

Ph.D. Thesis

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2. Research background

A key question of strategic research is what makes certain companies successful in the long run, and what are the reasons that lead others to failure, bankruptcy, or being acquired. How can a successful, profitable company with substantial resources, experienced managers, good market reputation that continues to apply the strategy that led them to success end up in failure and acquisition?

Since 2000 more than half of the companies of the Fortune 500 list have ceased to exist. (Nanterme, 2016). Over the past decades iconic companies went bankrupt or were acquired like Kodak or Polaroid (LoPucki and Doherty, 2007), so understanding the survival of a firm is more important than ever before.

2.1. Disruptive innovation

The failure of successful companies is often caused by rapid change in the external environment. In general, companies can handle slow environmental changes with their innovation activity, however, they often identify fast, radical changes too late and fail to give adequate responses to them. The driving force behind the radical change of the environment is often a sharp technological development, a disruptive innovation (Christensen, 1997).

Disruptive innovation usually results in new products or services that are inferior to the current market-leading products in terms of quality and key parameters, but provide radically new functionality to the users.

Incumbent companies often fail to sense the challenge posed by disruptive innovation in time, since the disruptive innovation does not constitute a direct
threat in their markets initially, due to the lower quality and the weaker key parameters. However, over time the products created with disruptive invocation become acceptable to the mainstream users as well, and they threaten the market of the incumbent companies.

If a company senses the disruptive innovation, it may choose from several possible responses. According to Charitou and Markides (2003), these responses can be: (1) focusing on and investing in the traditional business, (2) ignoring innovation, (3) counterattack – disrupting disruption, (4) adoption of the innovation while keeping the traditional solutions, and (4) complete adoption of the innovation.

2.2. Strategic renewal

The execution of a response which includes the adoption of the innovation usually requires a significant transformation of the company. That is the strategic renewal, which changes path dependence by altering capabilities and strategic goals. The strategic renewal may affect and renew the organisational structure of the company, its internal processes and systems, as well as the portfolio, suppliers, markets and the partner relationship of the firm.

Strategic renewal is a process rather than an immediate change (Volberda et al., 2001). Researches about this process can be categorised in three main areas: (1) antecedents, (2) processes and (3) outcomes of strategic renewal (Schmitt et al., 2018).
2.2.1. Antecedents of strategic renewal

The antecedents of strategic renewal are examined by academic literature using two different approaches: from the perspective of (1) organisational learning and (2) resources.

According to the first approach, organisational learning is the primary way and an essential condition of strategic renewal (Crossan et al., 1999). The fundamental challenge related to organisational learning is, that the knowledge required to maintain continuity and implement change need to be ensured simultaneously (March, 1991). In this respect, companies are required to gain new knowledge for strategic renewal while exploiting what they have already learned (Crossan and Berdrow, 2003). Simultaneous pursuit of the two contradictory learning processes is called organisational ambidexterity (Duncan, 1976).

Ambidexterity means performing exploitation and exploration activities simultaneously. Thus, enabling a company to generate profit continuously while developing and changing in the long run and adapt to the changing environment (March, 1991).

The second approach examines the process that leads to renewal from the perspective of resources. Based on the Resource-Based Theory (Barney, 1991), strategic renewal is the result of the attempts made to reconfigure corporate resources. The core skills of the company ensure daily operation while the so-called dynamic capabilities facilitate reconfiguration of the resources. Core capabilities include, for example, routine activities, administration and basic corporate processes. Effective development of new
products or strategic decision-making are examples of dynamic capabilities (Eisenhardt and Martin, 2000). Dynamic capabilities allow companies to cope with the fast-changing environment (Teece et al., 1997), thus execute strategic renewal (Agarwal and Helfat, 2009).

2.2.2. Processes of strategic renewal

Regarding the process of strategic renewal, the question who initiates and manages the process is a fundamental one: senior management or lower-level managers and employees. Both models can be successful, renewal initiated by senior managers (Kwee et al., 2011; Mitchell et al., 2009) or by members working at lower levels of the hierarchy (Pappas and Wooldridge, 2007).

2.2.3. Outcomes of strategic renewal

The general purpose of strategic renewal is long-term survival of the company (Agarwal and Helfat, 2009). This requires a change in path dependency and decrease of the gap between the external environment and the strategic goals and skills of the company.

The gap can be reduced using two approaches: (1) co-evolutionary way, considering the external environment as it is (Gilbert, 2005), or (2) with co-creation, influencing the external environment using the strategic renewal of the company (Crossan and Hurst, 2006).

2.2.4. Renewal model of Volberda et al.

Considering the management process options (top-down or autonomous) of strategic renewal and their relations to the environment (co-evolutionary or affect the market environment), Volberda et al. suggested four idealised
strategic renewal processes or “journeys” as they described them (Volberda et al., 2001). Those four recommend renewal journeys are the (1) emergent, (2) directed, (3) facilitated and (4) transformational.

<table>
<thead>
<tr>
<th>Middle management passive (acts as executor in the renewal)</th>
<th>Top Management is Passive with respect to Environment</th>
<th>Top Management is Active with respect to Environment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emergent renewal (applicable in stable competitive environment)</td>
<td>Directed renewal (applicable in stable competitive environment)</td>
<td></td>
</tr>
<tr>
<td>Middle management active (act as creator in the renewal)</td>
<td>Facilitated renewal (applicable in rapidly changing competitive environment)</td>
<td>Transformational renewal (applicable in rapidly changing competitive environment)</td>
</tr>
</tbody>
</table>

Table 1 - Summary of renewal model of Volberda et al.
Source: personal collection based on Volberda et al. (2001)

2.3. The research gap

There is only a limited overlap and connection between the literature of strategic renewal and disruptive innovation. Researches dealing with disruptive innovation examine innovation as a phenomenon (Christensen et al., 2018), its appearance and expansion (Schmidt and Druehl, 2008; Markides, 2012), develop prediction models to the expected effects of innovation (Schmidt and Druehl, 2008; Nagy et al., 2016) and make recommendations to companies how to respond (Charitou and Markides, 2003). On the other hand, professional literature dealing with disruptive innovation does not deal with issues regarding actions, processes, capabilities and structures that allow successful renewal once the need for a response is recognised.
Researches dealing with strategic renewal seek answers to the questions listed based on the frameworks of ambidexterity and dynamic capabilities as well as the Attention Based View (March, 1991; Teece et al., 1997; Ocasio, 1997; Volberda, 2017). However, in these researches, the need for strategic renewal as a response to disruptive innovation is a fundamental requirement; they do not examine the potential responses and their conditions.

In view of this, based on a systematic review of the literature, the author concluded that the research results available provide limited guidance for the issues arising in the intersection of the research areas of strategic renewal and disruptive innovation.

Issues such as what specific dynamic capabilities are required for the successful implementation of the responses listed by Charitou and Markides (2003) are not covered by professional literature. As dynamic capabilities are not universal, they rather depend on the given environment, structure and situation (Birkinshaw et al., 2016), different dynamic capabilities may be required if the response is “adapting innovation while keeping traditional solutions” or “counterattack – disrupting disruption”. Further questions arise: where does the initiative come from within the organisation, what is the role of senior and middle management, is it a co-evolutionary change or one that co-creates the environment, and how ambidexterity is implemented during the execution of the specific responses?
2.4. Research questions

The dissertation is drawn up in the intersection of the two research areas, strategic renewal and disruptive innovation with the aim of reducing the described research gap. During the exploratory research, the author seeks an answer to the question of what the relationship between the process of strategic renewal and various responses to disruptive innovation is.

Within the topic of the connection between strategic renewal and the responses to be given to disruptive innovation, the author researches specifically that process of the strategic renewal which can ensure the realisation of the response strategy that constitutes the ‘complete adoption of the innovation’.
The author examines this process through the three main areas of strategic renewal (antecedents, processes, outcomes).

Based on the above, the following three research questions are raised:

RQ1: Which combination of organisational ambidexterity and dynamic capabilities allows the implementation of the response strategy “complete adoption of the innovation” during a strategic renewal process triggered by disruptive innovation?

RQ2: What is the attitude of the company towards the external environment during a successful renewal?

RQ2: What is the role of senior management and lower levels of the hierarchy?

2.5. Propositions

The author forms the following three propositions with regard to the research questions:

H1 – In the course of the realisation of the response strategy that constitutes the ‘complete adoption of the innovation’, a combination of the key characteristics of the strategic renewal can be identified, which combination can ensure the success of the response strategy.

The three research questions formed to analyse the realisation of the response strategy that constitutes the complete adoption of the innovation in the three key areas of research of strategic renewal. According to the first proposition, such a combination of antecedents, processes, and outcomes can be identified with which the response strategy can be successful.
H2 – A company can not only follow the technological development and the market changes induced by the disruptive innovation but can also actively shape the external environment

The second research question is aimed at the relationship between the company and the external environment. According to the renewal model of Volberda et al. (2001), during the strategic renewal the senior management may follow the market changes passively (emergent and facilitated renewal), but it may also strive to actively influence those (directed and transformational renewal). The second proposition is that the complete adoption of the innovation response strategy may mean not only the adaptation to the external environment, but the company may also actively shape the external environment when it adopts the innovation.

H3 – In a rapidly changing competitive environment success requires the active role of both the senior management and the lower levels of the hierarchy, since in this way the identification of the fast changes of the external environment can be ensured.

According to the renewal model of Volberda et al. (2001), the facilitated and the transformational renewal methods can be used in a rapidly changing competitive environment. Both renewal methods assume the active role of middle management. According to the third proposition, in a rapidly changing competitive environment the realisation of the response method of complete adoption of the innovation – in line with the model of Volberda et al. – requires the active, strategy-forming role of the middle management.
3. Research methodology

The author answers the research questions by performing a longitudinal examination of a global IT company. The company at the heart of the research performed a strategic renewal between 2010 and 2018 as a result of a disruptive innovation – cloud computing - that changed the external environment.

The research questions are answered by exploring the strategic renewal of the company, using a single case study based research that provides an understanding of how strategic changes are performed and what specific actions affected them (Johnson et al., 2003; Jarzabkowski et al., 2007).

As the goal is a profound exploration of strategic renewal, the research relies on qualitative methodology. In the first phase of the author explores the history and strategic renewal of the company, based on publicly available articles, statements and press releases between 2002 and 2018. The strategic renewal took place between 2010 and 2018; however, knowing the preceding period is also necessary to understand the renewal. For this reason, the author starts the processing of the sources in 2002, in the post-‘dotcom’ crisis period, which was relatively calm for the company.

In this phase, the author discovered what happened during the researched time interval. In that phase, systematic data collection was performed using the following resources:

- EBSCO research databases: Business Source Complete, Academic Search Complete, Regional Business News, Newswires
• Corporate websites: press releases, financial results, product catalogues

In the second phase of the data collection, through personal interviews, the author collected data in order to understand how the renewal had happened. The author processed the data collected in the interviews with the Grounded Theory research method. NVivo v12 software was used to support GT analysis. The aim of using the GT method was to reveal a deeper connection and processes within the case study by raising the data to a conceptual level and avoid stopping at trivial results.

4. Research findings

4.1. Answers given to the research questions

4.1.1. RQ1: What combination of organisational ambidexterity and dynamic capabilities allows the realisation of the response strategy constituting the ‘complete adoption of innovation’ in course of strategic renewal carried out as a response to disruptive innovation?

The transformation of the corporate strategy started during a period when the market transformation caused by disruptive innovation had not had its effect on the corporate results yet. In this situation, the senior management was able to sense the danger, seize the opportunity and transform the strategy and the operation of the company. This process was enabled by dynamic capabilities - which were especially important in the given situation – such as strategic decision-making, the development and marketing of radically new products and the integration of acquired companies. In addition to these, the corporate culture built on frequent changes created dynamic capabilities such as the
institutionalisation of the integration of learning and knowledge, the fast organisation of the cooperation, and the renewal of the value offer within a short period of time.

The company chose a novel renewal model, in which the centralised IT systems of the company replaced the active participation of the middle managers in the development of the strategy. This was facilitated by special dynamic capabilities: IT-aided data collection, decision-making and implementation, which aligned with the corporate culture. These dynamic capabilities were especially important in the given situation because the majority of the middle management did not sense the impending market changes, therefore they did not consider it necessary to realise the response strategy which constituted the complete adoption of the innovation. Without the dynamic capabilities of IT-aided data collection, decision-making and implementation, the senior manager would have had to rely on the active support of the middle management, and without those dynamic capabilities, the strategic transformation could have become unsuccessful.

Having made use of the dynamic capabilities, the company aimed at realising ambidexterity, with particular emphasis on exploration. To this end, the company first established a contextually ambidextrous organisation, and then it used structural separation as well simultaneously.

In summation, the realisation of the response strategy constituting the complete adoption of the innovation was made possible by the combination of the dynamic capabilities listed above and the two kinds of realisation (contextual and structural) of ambidexterity.
4.1.2. **RQ2: What relationship does the company have with the external renewal during the successful renewal?**

During the strategic renewal, the company definitively strived for influencing the external environment.

The renewal was triggered by a disruptive innovation appearing in the external environment, the appearance of cloud services. However, the disruptive innovation had not had a significant effect on the market yet when the senior management of the company foresaw the future and started the renewal of the company. By making a determined stand for cloud services and the often forced marketing of the cloud services the company not only followed the changes but also expedited them itself. Therefore, the company evolved together with the environment not in a co-evolutionary manner but affected the development of the industry and the market proactively through ‘co-creation’.

4.1.3. **RQ3: What roles do the senior management and the lower levels of the hierarchy have in the process?**

The strategic renewal process was initiated, managed and controlled by the senior management. The middle management was given the executor role in the implementation of the changes. This was allowed by the special dynamic capabilities and the corporate culture of the company.

Taking into consideration that the company carried out the strategic renewal in a rapidly changing and hyper-competitive environment, due to the passive role of the middle management the renewal model chosen does not fit into the series of idealised renewal processes defined by Volberda et al. (2001).
4.2. Verification of the propositions

4.2.1. H1 – In course of the realisation of the response strategy that constitutes the ‘complete adoption of the innovation’, a combination of the key characteristics of the strategic renewal can be identified, which combination can ensure the success of the response strategy

This proposition was successfully verified through answering the three research questions. The three research questions covered the three main areas of strategic renewal (antecedents, processes and outcomes). All three research questions could be answered based on the research data collection, therefore the combination of antecedents, processes and desired outcomes which ensured the success of the response strategy in case of the company analysed could be identified.

4.2.2. H2 – A company can not only follow the technological development and the market changes induced by the disruptive innovation but can also actively shape the external environment

The answer given to research question RQ2 verified this proposition. During the strategic renewal the company not only followed innovation but proactively facilitated the spread thereof, thereby altering the external environment.
4.2.3. **H3 - In a rapidly changing competition environment success requires the active role of both the senior management and the lower levels of the hierarchy, since in this way the identification of the fast changes of the external environment can be ensured**

The author was unable to verify this proposition, the case study proves the opposite of this. As it was pointed out by the answer given to research questions RQ3, in addition to the active strategy creating role of the senior management, the lower levels of the hierarchy were given passive, executor roles.

**4.3. New discoveries of the dissertation**

4.3.1. **The controlled renewal method**

The renewal of the company was directed by the senior management, with the intention to influence the rapidly changing, turbulent and hyper-competitive external environment. In contrast, the middle management was given a passive, executor role in the development of the strategy. Based on this, the company analysed does not fit any of the four renewal methods described by Volberda et al. (2001), therefore it can be defined as a new approach.

The renewal method used by the company combines the elements of the directed and the transformational renewal methods described by Volberda et al. (2001). The senior management which intends to actively influence the environment and which makes centralised decisions, as well as the middle management passive in the development of the strategy are characteristics of the directed renewal. The transformation affecting the entire company as a
response to a radical market change, with the ability to react fast to the changes of the external environment is characteristic for the transformational renewal.

The method used by the company analysed, the combination of the directed and the transformational renewals can also be defined as a novel, ‘controlled’ renewal method.

During the controlled renewal the objective of the senior management is the fast and deliberate transformation of the corporate strategy, for example, as a response to a disruptive innovation. The senior managers intend to actively influence the industry and the market environment. The development and direction of the strategy are managed by the senior management, while the middle managers are given a passive, executor role in them. The renewal affects the entire company, and it is carried out by the senior management through the harmonisation of internal processes and the transformation of the sub-systems so that they facilitate the new strategy. The focus is on the exploration activity. This renewal method can be used well in rapidly changing, turbulent, hyper-competitive environments, since during the transformation closely commanded by the senior management, the company is able to react and make adjustments fast.

In the case of controlled renewal, the change in direction is commanded by a small strategic core, even in case of a company consisting of multiple units and having several tens of thousands of employees. The main advantage of this type of renewal is that the organisation recognises the advantage of the highly centralised planning and direction completely, while it remains flexible. This could mean a new competitive advantage for the company.
The controlled renewal method recommended can be added to the model of Volberda et al. (2001). The extended model is presented by Table 2.

| Source: own edition, based on Volberda et al. (2001) (the extension is marked in Italics) |

Table 2 - The extension of the renewal model of Volberda et al.

<table>
<thead>
<tr>
<th>Middle management <em>passive</em> (stable competitive environment)</th>
<th>Company is <strong>Passive</strong> with respect to Environment</th>
<th>Company is <strong>Active</strong> with respect to Environment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emergent renewal</td>
<td>Directed renewal</td>
<td></td>
</tr>
<tr>
<td><strong>Middle management passive</strong></td>
<td></td>
<td><strong>Controlled renewal</strong></td>
</tr>
<tr>
<td>(rapidly changing competitive environment)</td>
<td></td>
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</tr>
<tr>
<td><strong>Middle management active</strong></td>
<td></td>
<td><strong>Transformational renewal</strong></td>
</tr>
<tr>
<td>(rapidly changing competitive environment)</td>
<td></td>
<td></td>
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<tr>
<td>Facilitated renewal</td>
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</tbody>
</table>

4.3.2. **Specific dynamic capabilities**

With regard to the controlled renewal model it is an important question how the senior management which keeps a firm hand on the transformation can sense the rapidly changing, turbulent environment, and in the absence of decision-making powers vested in the middle management, how can the company react and make adjustments fast.

The research showed that the widespread use of the modern and sophisticated business intelligence systems, which cover the entire company had an essential role in this. The data-centred and automated IT systems rendered the senior management able to learn fast from the feedbacks, so that it required less effort to coordinate the activities and execute the modifications.
The business intelligence systems provided accurate, real-time information to the decision-makers, while the other centralised internal systems of the company (financial, human resources, individual compensation systems, marketing planning) enabled the fast execution of the decisions made. Therefore, the IT systems and the centralised processes facilitated by them gave specific dynamic capabilities to the company, thereby replacing the necessity of active middle management participation in the transformation process.

The sophisticated business IT systems which align with the corporate structure and facilitate the company-wide information collection, decision-making and implementation should be considered as dynamic capabilities, that enable the controlled strategic renewal journey.
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