

CHANGE IN THE PRESENCE OF FIT: THE RISE, THE FALL, AND THE RENAISSANCE OF LIZ CLAIBORNE

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A new framework that addresses how tight fit among a firm's activities affects the firm's ability to react to environmental changes is presented. As part of the framework, a new classification scheme for environmental changes is developed. I argue that fit-conserving change, which leaves the internal fit among a firm's activities intact yet decreases the appropriateness of the set of choices as a whole, poses a particularly difficult challenge for managers. A longitudinal case study of the fashion apparel company Liz Claiborne illustrates the framework.

The last years have seen a remarkable upsurge of interest in the concepts of interaction and fit. Within the management and organization literatures, the notion of fit has a long-standing presence. In particular, the internal fit between the strategy and the structure of firms (e.g., Chandler, 1962; Learned, Christensen, Andrews, & Guth, 1965) and the external fit between the structure and the environment of firms (e.g., Lawrence & Lorsch, 1967; Pennings, 1987) have received much attention. During the late 1980s and 1990s, originally spurred by analyses of Japanese manufacturing methods, researchers revived the topic of fit. The emphasis shifted to studying internal fit at a very fine-grained level of analysis. The importance of replicating entire systems of practices, including production, supply, and human resource policies, rather than single elements, was recognized (e.g., Jaikumar, 1986; MacDuffie, 1995). Expanding the concept of fit beyond manufacturing and ascribing to it a central role in strategy formulation, Porter (1996) stressed the importance of mutually reinforcing activities in creating and sustaining a competitive advantage. Over the same time period, economists as well have become interested in the issues of fit and interdependence among firm choices and have started to create mathematical frameworks that allow rigorous modeling of at least certain types of

mutually reinforcing interactions (e.g., Milgrom & Roberts, 1990, 1995).

The common theme of these approaches is that to understand the performance of a firm, one must analyze the firm as a *system* of interconnected choices: choices with respect to activities, policies and organizational structures, capabilities, and resources. Internal fit among choices can lead to a sustainable competitive advantage because it makes imitation difficult (Porter & Rivkin, 1998; Rivkin, 2000). However, the implications of tight fit for the sustainability of a competitive advantage given environmental change are ambiguous. On the one hand, "Firms may have difficulty navigating a changing environment not only because the changes in the environment negate the value of the organization's assets, but also because a tightly coupled organization may have difficulty adapting to such changes" (Levinthal, 1997: 936). Tight coupling requires a firm to modify many choices simultaneously, an inherently difficult task (Nadler, Shaw, & Walton, 1994). On the other hand, tight fit raises the incentive for management to optimally configure and adjust all of its choices. Since each choice influences the payoff of many other choices, the marginal payoff to adjusting each choice in response to some external change is increased in the presence of tighter fit (Porter, 1995). Moreover, tight fit can make a firm more sensitive to environmental change (Weick, 1976). Changes are quickly detected, since the repercussions are felt in multiple areas in the firm.

This article presents a new framework for thinking about the relationship between fit and organizational inertia when a firm is confronted with environmental change. As part of the framework, a new classification scheme for environmental changes is developed. In line with the more recent literature on fit, we examine fit at a very detailed

I would like to thank Kim Cameron (the editor), Giovanni Gavetti, Pankaj Ghemawat, Bruce Kogut, Daniel Levinthal, Johannes Pennings, Michael Porter, Daniel Raff, Jan Rivkin, Harbir Singh, Sidney Winter, and three anonymous referees for their helpful comments. Any remaining errors are mine. Financial support by the Division of Research of the Harvard Business School and the Reginald H. Jones Center for Management Strategy, Policy and Organization at the University of Pennsylvania is gratefully acknowledged.

level of analysis—at the level of individual choices. To illustrate the framework, we present a longitudinal study of how a firm that created a system of tightly interconnected choices responded (or failed to respond) to environmental changes. I studied the developmental journey of Liz Claiborne, the largest U.S. manufacturer of women's fashion apparel, from its inception in 1976 to late 1997. I analyze the initial success of Liz Claiborne, the environmental changes it faced in the early 1990s, its first responses, and its subsequent actions in the late 1990s.

LITERATURE REVIEW AND CHANGE FRAMEWORK

Before I examine the historical journey of Liz Claiborne, it will be helpful to briefly review the literature on organizational change that is concerned with changes in systems of interconnected choices. Following the review, I present a new framework for thinking about the relationship between fit and organizational responses given different types of environmental changes.

Logically prior to any theory about *changes* in systems of interrelated parts is the notion that internal fit should not be thought of as “pairwise” associations between variables, but as *gestalts*, or configurations, describing sets of elements and their relationships (Drazin & Van de Ven, 1985; Khandwalla, 1973; Miller, 1986; Miller & Friesen, 1984; Nadler & Tushman, 1992). Whereas the term “fit” is used in the literature on configurations to describe the internal relationship among activities, in the contingency literature the term is used to describe the relationship between a firm's choices and its environment. To gain clarity on the concept of fit, I suggest making the distinction between *internal fit* among activities—that is, whether a firm has a coherent configuration of activities—and *external fit*, that is, the appropriateness of the configuration given the environmental conditions facing the firm.

Building on the idea that firms consist of systems of interrelated parts, Miller and Friesen (1982) analyzed the change processes of these systems. They hypothesized and empirically found that quantum changes (changes in many attributes over a short period of time) yielded better performance than piecemeal incremental approaches. Following a similar line of thinking, Tushman and Romanelli (1985) proposed that firms follow a developmental path best described by a punctuated equilibrium model of organizational evolution: Firms engage in incremental changes during most of their history, yet sporadically undergo relatively rapid and fun-

damental transformations (Gersick, 1991). Empirical support of this developmental pattern has been provided by Tushman, Newman, and Romanelli (1986), Pettigrew (1987), and Romanelli and Tushman (1994).

Intimately tied to the process of change is the issue of firms' inertia. For the purpose of this discussion, I focus on factors that may cause senior management to fail to respond to environmental changes. Hambrick and Mason (1984) proposed a helpful framework for understanding management inertia. In short, managers are thought of as having mental maps that influence both the information they perceive and the way they process it. As a consequence, managers, especially those with long tenure, may be unable to “unlearn” outdated views of the world (Nystrom & Starbuck, 1984). Past success, in particular, reinforces and eventually ossifies mental maps, leading to increased inertia (Murnighan & Tushman, 1997). Studies have shown that past success leads to a reduction in information processing (Miller, 1993) and a heightened belief that environmental changes are not going to affect an organization negatively (Milliken, 1990). Moreover, past success can lead to the accumulation of slack resources, which reduce the perceived need to change (Milliken & Lant, 1991), and to the creation of a strong organizational identity or culture. Both past success and strong organizational identities have been found to increase belief in an organization's relative invulnerability to environmental changes (Miller, 1994; Milliken, 1990).

In sum, a variety of psychological reasons have been described in the literature as leading to firm inertia. In the following framework, I develop a link between the work on inertia and the previously described literature on fit. As described by Tushman and Romanelli (1985), inertial forces lead firms along a process of convergence to a specific configuration of strategic position and organizational form. The value of this process has been previously analyzed with respect to two different environmental conditions: stability and turbulence (Miller, Lant, Milliken, & Korn, 1996; Tushman & Romanelli, 1985; Tushman & Rosenkopf, 1996). As long as an environment is relatively stable, convergence, and hence inertial forces, are found to be beneficial. However, in turbulent environments, inertial forces are a liability.

Rather than distinguishing between stable and turbulent environments, the following framework characterizes changes in the environment in terms of their impact on internal and external fit. This characterization scheme can offer new insights into the mediating role that fit plays in the relationship between environmental changes and the ensuing

changes (or inertia) at the firm level. In particular, the framework points toward the difficulty of managers' perceiving and reacting to environmental changes that leave the internal fit among the elements within a firm's set of choices intact, yet decrease the value of the set of choices as a whole—that is, destroy external fit.

For the following discussion, the notion of a "performance landscape" is useful. The concept of a performance or fitness landscape was first developed in the realm of evolutionary biology by Sewall Wright (1932). The concept has been further developed and formalized by Kauffman (1993) and has found application in, for instance, studies of organizational adaptation (Levinthal, 1997), organizational variety (Westhoff, Yarbrough, & Yarbrough, 1996), and the difficulty of imitating complex strategies (Rivkin, 2000). In our context, the performance landscape is a multidimensional space in which each dimension represents the values of a particular choice that a firm can make and a final dimension indicating the performance value. For illustration, consider a simple example in which a firm can make only two choices: the breadth of product variety and the flexibility of the production set-up. Imagine the breadth of product variety is on the x-axis, the degree of flexibility is on the y-axis, and the ensuing performance is on the vertical z-axis. The performance landscape maps each pair of variety and flexibility choices onto a performance value (see Figure 1a). Similarly, for each set

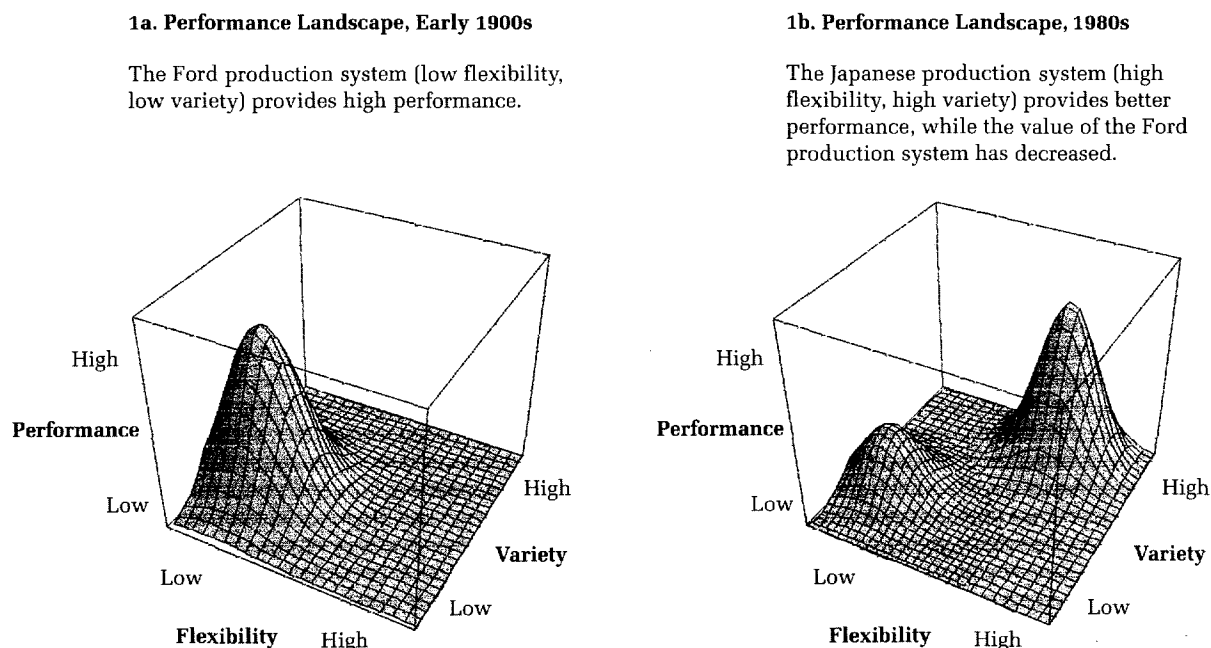
of N choices, the performance landscape would attach a performance value to it in a $N+1$ dimensional space.

Performance landscapes provide a suggestive way to illustrate the concepts of internal and external fit. External fit—the appropriateness of a set of choices given environmental conditions—is represented by the height of a particular point on the landscape. Environmental conditions encompass all factors that affect the relative profitability of a firm's set of choices, including competitors' actions, customer preferences, and available technologies. As shown in Figure 1a, certain combinations of flexibility and product variety lead to higher performance than other combinations.

Consistency among choices—that is, internal fit—is represented by a peak in the landscape. Internal fit corresponds to a peak, because changing any single element (and not changing any other element) within a consistent set of choices leads to a decline in performance. Two examples of consistent sets of choices are the Ford mass production system and the Japanese lean manufacturing system (Milgrom & Roberts, 1990). In our simple two-dimensional example, the mass production system is represented by low variety and low flexibility, and the lean production system is represented by high variety and high flexibility (see Figure 1b).

The shape of each peak contains further information: the stronger the degree of interaction among a particular set of choices, the steeper the associated

FIGURE 1
Performance Landscapes



peak. This feature results from the fact that in systems with strong interactions, the performance penalties for misalignments are particularly high because the value of many activities is affected.¹

Environmental changes can be thought of as changing the landscape: the height, shape, or location of peaks changes, new peaks arise, and so forth (Levinthal & Siggelkow, 2001). For instance, in the early 1900s, with the information and production technologies available at the time, the choice of low variety and low flexibility could be implemented very efficiently: the Ford production system represented a high peak in the performance landscape, whereas the high variety–high flexibility choice was technologically very difficult (or even infeasible) to implement for high-volume production. Thus, high variety–high flexibility represented a very low point on the performance landscape (Figure 1a). By the 1980s, choosing high variety with high flexibility had become technologically feasible; moreover, it provided substantial advantages in the marketplace. The landscape had changed: the value of the Ford production system had declined, and a new peak, the Japanese production system, had arisen and formed a higher-performance set of choices (Figure 1b).

For a firm that occupies a peak, environmental change can affect both external and internal fit. Logically, we can distinguish four cases, which are depicted in Figure 2. (1) *No change*: If neither external nor internal fit is affected, the environmental change has no relevance to the firm in question.

¹ For formal models of performance landscapes with these features, see Kauffman (1993).

(2) *Detrimental fit-destroying change*: If both external and internal fit are affected, the firm finds itself at a lower elevation (lower external fit) and located away from a peak (lower internal fit). (3) *Benign fit-destroying change*: In this case, the firm's performance has not decreased, yet internal fit has been compromised by the environmental change. (4) *Fit-conserving change*: Although internal fit has not been affected, external fit has decreased. In other words, the environmental change has left the internal logic of the firm's system of choices intact while decreasing the appropriateness of the system as a whole.

In sum, with fit-destroying change the firm no longer occupies a peak; with fit-conserving change, the firm still occupies a peak, the height of which has declined, however. The distinction between these two types of changes is important, since firms' reactions to them can differ significantly. After fit-destroying change, a firm will attempt, either through local, incremental search or through long-range search, to change its activities in order to climb onto a new peak. A firm might react quickly in such a situation, since its financial performance has deteriorated (in the case of detrimental fit-destroying change), and internal misfits can be identified. In other words, it is clear that something should be done, and at least some clues as to what should be done might exist, since various elements are misaligned. Moreover, for changes that only nudge a firm away from a peak, one can hypothesize that a firm with a high degree of internal fit reacts faster than a firm with a loosely coupled system. Since peaks are steeper for firms with high internal fit, their incentive to find realignment

FIGURE 2
Change Framework

| | | External Fit | |
|--------------|-----------|------------------------------|-----------------------------------|
| | | No Change | Change |
| Internal Fit | No Change | No change | Fit-conserving change |
| | Change | Benign fit-destroying change | Detrimental fit-destroying change |

is large. On a smaller scale, a lean production line provides a good example of tight fit leading to fast response. The absence of inventory (or work-in-process) between individual workstations creates a tightly coupled system. A problem at any workstation is detected very quickly, as the entire line comes to a halt. In addition, incentives to improve each individual production step are high, since the cost of stopping the entire line is large (Womack, Jones, & Roos, 1990).

The situation is different, however, in the case of fit-conserving change: even though the firm's financial performance has declined, no obvious misfits can be detected because the internal logic of the old system remains intact. In this situation, a firm can react in three ways. (1) *Playing the old game*: The firm does not change anything. It keeps its old system of choices, which still displays internal fit though creating suboptimal performance. Graphically, the firm stays on its old, lower peak. (2) *Playing an incomplete game*: The firm changes single elements in its activity system with the consequence of an even further performance decline; the firm moves incrementally away and down from its peak. (3) *Playing a new game*: The firm changes a whole range of its elements and locates on a new and higher peak.

The first two reactions, though destructive, are easily defensible, as managers continue to rely on their old mental maps. Within the landscape metaphor, the term "mental map" is particularly apt: the mental map can be thought of as a manager's map of the performance landscape. In the first option, playing the old game, managers continue to rely on previously successful practices and choices. Moreover, managers may rightly point out that any incremental change would lead to a performance decline. This is the result of their systems already being fully aligned. In a sense, firms are held captive by their existing systems—they have fallen into a competency trap (Levinthal, 1992; Levitt & March, 1988).

Managers who choose the option of playing an incomplete game feel compelled to act, since performance has declined. Yet, in this case, incremental changes only lead to further performance declines. For instance, the American automobile industry recognized that the height of the peak associated with their production system had decreased, even though the internal logic of the mass production system was still intact. Yet, by copying only a few elements of the Japanese production system, the American automobile industry played an incomplete game for many years that did not generated the hoped-for benefits (Hayes & Jaikumar, 1988). In sum, after fit-conserving change, lo-

cal search and incremental adaptations are not effective.

Only through the third reaction, playing a new game, by comprehensively rearranging a large part of its system of choices, can a firm achieve a significant performance improvement. Graphically, the firm locates itself on a new peak. Such an approach is, however, very difficult to undertake. It requires that managers perceive the systemic nature of the needed changes. Moreover, they need to be willing to act on a broad scale, potentially contradicting some of their past actions. Thus, they have to overcome both their own behavioral "blind spots" (Zajac & Bazerman, 1991) and establish internal legitimacy for their actions (Suchman, 1995). In addition, this broad set of changes has to be implemented successfully; this is a difficult undertaking, as is discussed in the organizational ecology literature on "core changes" (Hannan & Freeman, 1984; Singh, House, & Tucker, 1986). Lastly, these changes have to take place over a short period of time for the firm not to experience large performance deficits caused by misfits during the transition period (Miller & Friesen, 1982, 1984). As a result, managers of firms with tightly coupled activity systems face a formidable task—structurally, cognitively, and psychologically—if they are to respond successfully to fit-conserving environmental change.

The following case study illustrates the change framework. After providing a methodological note on the case research, I present a brief sketch of Liz Claiborne's history and then an analysis of the firm's success. I describe Liz Claiborne's choices within five important stages along its value chain: design, production and distribution, the process of selling to retailers, the presentation of merchandise, and marketing. The section concludes with a description of the internal fit within Liz Claiborne's set of choices and a map displaying the interaction among the choices. To use the terminology of the framework, I establish that Liz Claiborne was located on a peak. Moreover, I show that the system of choices had high external fit given the environmental conditions at the time—that is, Liz Claiborne's chosen peak was high. The environmental factors considered are customer taste and demand, retailers' requirements, and the available technology.

In the second section, I describe how these three environmental factors changed in the early 1990s. In other words, Liz Claiborne's performance landscape was shifting. More specifically, Liz Claiborne faced fit-conserving change. The internal logic of its system remained intact, yet the external fit of its system decreased. Moreover, a new peak, which

involved a host of different choices with respect to distribution and production, had arisen. The company's management responded to the fit-conserving change by playing an incomplete game: Liz Claiborne attempted to partially change its set of choices, with the consequence of a further performance decline.

In the third main section, I use the same five categories of choices (design, production and distribution, the process of selling to retailers, the presentation of its merchandise, and marketing) to systematically describe the actions, beginning in 1994, of Liz Claiborne's new leadership team, which eventually moved Liz Claiborne to a new peak. This section concludes with another map, displaying the particular choices and the interactions among them. In the final section, I further discuss the framework and outline future research opportunities.

The data for the case study were obtained from several primary and secondary sources. Over a period of one and a half years, between 1996 and 1997, I conducted personal interviews, ranging from one hour to several hours, and shorter follow-up telephone interviews with members of Liz Claiborne's management team. Interviewees included the CEO, the CFO, (chief financial officer), the vice president for corporate planning, and several division presidents. The tenure at Liz Claiborne of the interviewees ranged from one year to ten years. After completing the fact gathering from secondary sources (about 900 articles about Liz Claiborne in trade journals and magazines, in addition to security analysts' reports) and company documents (annual reports, 10Ks, and documents provided by management), a several-hour interview was conducted with one of the founders of the company (Jerome Chazen). Early drafts of the case study were circulated among members of Liz Claiborne's management in addition to Chazen, all of whom provided additions and corrections on factual data in the case. Subsequent discussions with industry experts were used to confirm the outlined changes, in particular those occurring at the industry level.

BRIEF HISTORICAL OVERVIEW

Founded in 1976 with a starting capital of \$250,000, Liz Claiborne reached revenues of \$116 million in 1981, the year it went public. Five years later, the company became part of the *Fortune* 500 list, the first company started by a woman (the designer Liz Claiborne) to do so. In 1989, *Fortune* reported that Liz Claiborne had achieved the highest average return on year-end equity during the

1980s of all *Fortune* 500 industrial companies: 40.3 percent. In 1991, Liz Claiborne's sales surpassed the \$2 billion mark for the first time and its stock price reached record heights: in May of that year, an investment of \$10,000 in shares bought at the initial offering had a market value of over \$610,000 (see Table 1 for financial data).

Beginning in 1992, however, problems in Liz Claiborne's performance surfaced. Its sales stagnated and its net income declined. Over the next three years, Liz Claiborne's market capitalization dropped from \$3.5 billion at the end of 1992 to \$1.3 billion at the end of 1994. In 1994, Paul Charron, the former executive vice president of VF Corporation, was hired, and he became the new CEO at Liz Claiborne one year later. The implementation of a series of operational and marketing changes led to a marked increase in net income and to a renaissance of Liz Claiborne's stock. By May 1997, Liz Claiborne was trading close to a record high, giving it a market capitalization of \$3.2 billion.

LIZ CLAIBORNE'S RISE

How was Liz Claiborne able to achieve its remarkable success in its early years? To summarize, in the late 1970s, Liz Claiborne identified a growing customer group (professional women), and created a new market segment (a segment between moderate and designer sportswear). Unlike the designers of many fashion houses, Ms. Claiborne designed apparel to fit the actual shapes of her customers. She made a mark on the apparel industry with the pronouncement that "the American woman is pear-shaped" (Hass, 1992). Moreover, Liz Claiborne pioneered overseas production for fashion items, thereby allowing it to offer its apparel at lower prices. Lastly, the practice of presenting the lines of apparel as collections within which customers could mix and match made shopping for career clothes easier. As a result, the company garnered the loyalty of customers, who considered Ms. Claiborne to be a personal friend whose taste they could trust when it came to purchasing career clothes (Belkin, 1986). In the words of Liz Claiborne's current CEO, for an entire generation of professional women, Ms. Claiborne provided the imprimatur on clothes acceptable to wear in the workplace (Paul R. Charron, personal communication, February 30, 1997).

In the following subsections, I will describe in detail Liz Claiborne's positioning and the choices its management took with respect to five stages of the company's value chain: design, presentation of its merchandise, selling to retailers, marketing, and production/distribution choices. In the concluding

TABLE 1
Financial Data for Liz Claiborne^a

| | 1996 | 1995 | 1994 | 1993 | 1992 | 1991 | 1990 | 1989 | 1988 | 1987 | 1986 | 1985 | 1984 | 1983 | 1982 | 1981 |
|---|---------|---------|----------|----------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| Sales | 2,217.0 | 2,081.0 | 2,163.0 | 2,204.0 | 2,194.0 | 2,007.0 | 1,729.0 | 1,411.0 | 1,184.0 | 1,053.0 | 813.0 | 557.0 | 391.0 | 228.0 | 160.0 | 116.0 |
| Sales growth | (6.5%) | (-3.8%) | (-1.9%) | (0.5%) | (9.3%) | (16.1%) | (22.5%) | (19.2%) | (12.4%) | (29.5%) | (46.0%) | (42.3%) | (71.1%) | (42.9%) | (37.0%) | (46.0%) |
| Cost of goods sold | 1,341.1 | 1,290.9 | 1,407.7 | 1,452.4 | 1,364.2 | 1,207.5 | 1,030.8 | 841.7 | 758.3 | 655.6 | 502.2 | 341.7 | 243.8 | 144.7 | 109.6 | 76.2 |
| Gross margin | 39.52% | 37.99% | 34.92% | 34.10% | 37.82% | 39.84% | 40.38% | 40.35% | 35.95% | 37.74% | 38.23% | 38.65% | 37.69% | 36.73% | 31.50% | 34.76% |
| Selling, general, & administrative expenses | 641.7 | 600.5 | 604.4 | 568.3 | 507.5 | 471.1 | 393.1 | 321.9 | 255.5 | 194.7 | 146.3 | 97.3 | 66.3 | 40.1 | 27.0 | 18.2 |
| Selling, general, & administrative expenses/sales | 28.94% | 28.85% | 27.94% | 25.78% | 23.13% | 23.47% | 22.74% | 22.81% | 21.58% | 18.49% | 18.00% | 17.47% | 16.94% | 17.53% | 16.88% | 15.58% |
| Net income | 155.7 | 126.9 | 82.9 | 126.9 | 218.8 | 222.7 | 205.8 | 164.6 | 110.3 | 114.4 | 86.2 | 60.6 | 41.9 | 22.4 | 14.1 | 10.2 |
| Net income growth | (22.7%) | (53.1%) | (-34.7%) | (-42.0%) | (-1.8%) | (8.2%) | (25.0%) | (49.2%) | (-3.6%) | (32.7%) | (42.2%) | (44.6%) | (87.1%) | (59.2%) | (37.9%) | (64.5%) |
| Net income | 7.02% | 6.10% | 3.83% | 5.76% | 9.97% | 11.10% | 11.90% | 11.67% | 9.32% | 10.86% | 10.60% | 10.88% | 10.71% | 9.79% | 8.79% | 8.73% |
| Earnings per share | 2.15 | 1.69 | 1.06 | 1.56 | 2.61 | 2.61 | 2.37 | 1.87 | 1.26 | 1.32 | 1.00 | 0.71 | 0.50 | 0.27 | 0.17 | 0.13 |
| Return on equity | 15.3% | 12.8% | 8.4% | 13.0% | 21.9% | 24.5% | 28.9% | 26.9% | 24.1% | 32.0% | 34.8% | 37.2% | 40.1% | 34.7% | 34.2% | 38.1% |
| Cash and securities | 528.8 | 437.8 | 330.3 | 309.2 | 425.6 | 471.5 | 431.8 | 372.9 | 278.3 | 160.4 | 104.0 | 56.2 | 19.0 | 11.2 | | |
| Inventory | 349.4 | 393.3 | 423.0 | 436.6 | 385.9 | 322.0 | 265.7 | 198.2 | 168.0 | 156.4 | 114.9 | 72.8 | 73.4 | 34.2 | 21.3 | |
| Inventory days | 95.1 | 111.2 | 109.7 | 109.7 | 103.2 | 97.3 | 94.1 | 85.9 | 80.9 | 87.1 | 83.5 | 77.8 | 109.9 | 86.3 | 70.9 | 0.0 |
| Long-term debt | 1.0 | 1.1 | 1.2 | 1.3 | 1.4 | 1.6 | 15.1 | 15.6 | 14.1 | 14.5 | 0.0 | 10.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Debt/equity | 0.10% | 0.11% | 0.12% | 0.13% | 0.14% | 0.18% | 2.12% | 2.55% | 3.08% | 4.06% | 0.00% | 6.15% | 0.00% | 0.00% | 0.00% | 0.00% |
| Market value | 2,796.8 | 2,064.9 | 1,335.0 | 1,844.1 | 3,495.0 | 3,610.6 | 2,581.8 | 2,109.8 | 1,509.1 | 1,434.4 | 1,844.0 | 1,035.4 | 539.2 | 357.0 | 194.6 | 97.3 |
| Share price | 38.63 | 27.50 | 17.00 | 22.63 | 41.63 | 42.25 | 29.75 | 24.00 | 17.25 | 16.50 | 21.38 | 12.13 | 6.38 | 4.25 | 2.33 | 1.22 |

^a All figures are in millions of dollars, except for earnings per share and share price.

paragraph of this section, I will illustrate the internal and external fit of these choices.

Liz Claiborne's Positioning in a Growing Niche

Liz Claiborne took full advantage of the change in the demographics of the American workforce. In 1960, only 21.9 million American women were employed. By 1990, 53.5 million American women were working, making up 45 percent of the U.S. workforce. In the mid-1970s, as this process was unfolding, the professional woman did not have much choice with respect to career clothing. There was a large void between the classic dark-blue suit (made, for instance, by Evan-Picone) and the haute couture of, for instance, Carol Horn. Ms. Claiborne, who had spent 16 years as a women's sportswear designer at Youth Guild, a division of Jonathan Logan, was aware of this increasingly expanding niche (Bratman, 1983). In 1976, after Youth Guild closed, Ms. Claiborne decided to pursue this opportunity together with her husband, Arthur Ortenberg, a former consultant in the apparel industry. Within the first months they recruited Leonard Boxer, who had apparel production expertise and connections to overseas suppliers from running production at Susan Thomas Inc., and Jerome Chazen, who knew the marketing side of the women's sportswear industry. With this team of industry experts, Liz Claiborne enjoyed some up-front trust in the industry. Department stores knew Ms. Claiborne's design skills and were willing to give her coveted floor space (Bratman, 1983). In its first year, Liz Claiborne was already generating \$2.2 million in sales and operating with a profit.

Design Choices

In 1980, Ms. Claiborne described her offerings as "classic enough that a woman can wear them for several years. They aren't moderate in price, but aren't exorbitant, either" (Ettorre, 1980). In her first collections, no item sold for more than \$100. Although the clothes did not fit the formal "dress for success" mold, they were not too far-out to be worn to the office. At the same time, customers perceived the moderately priced Liz Claiborne label as competing against top designers whose clothes cost more than twice as much (Byrne, 1982).

Ms. Claiborne had two goals in mind. She wanted to provide high value to her customers, and she wanted to make shopping easier (Bratman, 1983). It turned out that both could be achieved by an innovative kind of "color-by-the-numbers fashion" that saved the customers both time and anxiety (Traub & Newman, 1985). Ms. Claiborne de-

signed clusters of skirts, shirts, blouses and sweaters that could be mixed and matched. More precisely, each season's line comprised four to seven concept groups, each of which consisted of a balance of items such as blouses, shirts, skirts, and pants. Within each concept group, the mix-and-match design was practiced—that is, each group told a different "color story." Customers could put together an outfit not only in terms of the total look but also in terms of size, by choosing different sizes for tops and bottoms, thereby avoiding the need for alterations. Moreover, sizes were the same across styles, and colors never changed: Navy blue remained the same navy blue, so that a jacket bought in one year would match a skirt or blouse bought two years before.

Presentation Choices

From the beginning, Liz Claiborne focused on selling its merchandise in large, upscale department stores. In 1994, Liz Claiborne's products were offered in more than 9,500 locations in the United States and Canada, yet its four largest customers (Dillard's, the May Department Stores Company, Macy's, and Federated Department Stores) accounted for 44 percent of its sales. For the end customer to reap the benefits of Liz Claiborne's mix-and-match design, it was important that collections be presented together and not split up. Hence, Liz Claiborne pushed for a new presentation format at its retailers. Department stores were traditionally organized around classifications, such as blouses and pants, but Liz Claiborne required a dedicated space to present its entire collection. Liz Claiborne was actually not the first company that tried to convince retailers to present an entire collection. Chazen had learned that Evan-Picone had put together a small collection of very classic merchandise and had received small dedicated areas from department stores. By and large, however, "Retailers were not sure what to do with these collections and were looking for a complementary resource which would allow them to enlarge the floor space dedicated to collection presentation." (Jerome Chazen, personal communication, October 7, 1997). Consequently, retailers were willing to listen to Chazen when he tried to convince them to present Liz Claiborne's merchandise as a collection.

To help retailers with the presentation of the collections, Liz Claiborne distributed Claiboards or Lizmap diagrams that included sketches, photos, and text showing how merchandise should be displayed in groups. Other innovations included simple measures such as naming the groups and at-

taching these names to hangers, thus allowing customers to quickly see which pieces of apparel belonged to each group. Moreover, a dedicated staff supported the retailers: Over 20 consultants traveled throughout the country to ensure that clothes and displays were arranged in department stores correctly. These consultants were also engaged in product information seminars for the department stores' sales personnel. In addition, 150 retail specialists who were employed by the stores in which they worked yet received training from Liz Claiborne helped with merchandise presentation, provided instruction for sales help, and relayed customer feedback to Liz Claiborne's headquarters (Better, 1992).

Creating dedicated areas for Liz Claiborne merchandise was a first step toward gaining control over product presentation. Beginning in 1987, Liz Claiborne took its efforts towards product presentation one step further. In Jordan Marsh's flagship store in Boston, Liz Claiborne opened its first store within a store. The 7,200-square-foot LizWorld shop housed Liz Claiborne's full range of merchandise: Liz Collection, LizSport, LizWear, dresses, accessories, shoes, hosiery, eyewear, and fragrance. Within the next few years, Liz Claiborne set up over 200 concept shops within department stores. Moreover, since these shops increased business for retailers, Liz Claiborne successfully argued for the department stores' covering the costs of adding the concept shops. Liz Claiborne's accessories division copied the presentation format and introduced its first concept shop within a department store in 1990. The shop featured a full range of handbags and small leather goods, and Liz Claiborne's latest fashion looks—fully accessorized—decorated the walls.

Selling Process

Since Liz Claiborne believed its merchandise had the greatest impact if presented as a collection, it rejected orders from department stores that were not willing to present the Claiborne line the way Liz Claiborne saw fit. For instance, a store always had to buy a number of tops that matched its order of bottoms (Belkin, 1986). Moreover, buyers were required to purchase an entire group and could not pick and choose among the garments shown.

Liz Claiborne never had a road sales force, making it the only leading garment house in the country that functioned without one (Birmingham, 1985). Retailers who wanted to look at the new Liz Claiborne line had to come to the showrooms in New

York,² where they were welcomed by a 80–90 person sales force, which won the title "America's Best Sales Force" from *Sales & Marketing Management* in 1987. Its centralized selling location enabled Liz Claiborne to establish relationships at a higher level than would otherwise have been possible. As Chazen explained, "On the road a salesman is lucky if he sees the buyer. But when retailers come to New York, top management often comes to see the market" (Skolnik, 1985). As a result, although stores' buyers still placed the orders, every major store president in the country visited Liz Claiborne several times a year and met with Liz Claiborne's management.

Liz Claiborne not only demanded the purchase of entire groups, but also enforced a rigid noncancellation policy: if spring merchandise did not sell well in stores, retailers could not cut previous orders for the summer line (Better, 1992). The company created further leverage by pursuing a strict production policy of manufacturing about 5 percent less merchandise than there was demand (orders) for (Hass, 1992). This policy had two effects. First, it increased Liz Claiborne's "sell-through" (the percentage of clothes sold at full price), which some industry observers pegged at 75 percent as compared to an industry average of 50 percent (Deveny, 1989). Second, the policy created a climate of fear among its customers, giving Liz Claiborne a credible weapon with which to ensure that its desires, such as those with respect to retail presentation, were met.

Customer Contact and Marketing

Despite being a company that originally had no direct retailing contact with its end customers, Liz Claiborne sought feedback from them. Its consultants and retail specialists talked to customers daily, and they also arranged, during so-called LizWeeks, in-store events for career women, such as full-blown fashion shows in which 25–30 outfits were shown, and "breakfast clinics" during which women had the chance to see the newest collection and to shop before they went to work. In total, Claiborne sponsored over 100 in-store events each month across the country.

² Until 1990, all of Liz Claiborne's domestic sales were performed through its New York showroom. In order to reach smaller specialty stores, Liz Claiborne decided to open two small showrooms in Atlanta and Dallas in 1990 and 1992. However, in these showrooms only dresses, accessories, jewelry, and Liz & Co. better casual knitwear were displayed. The sportswear line was not shown, since the minimum orders were too high for most specialty stores.

In addition, Liz Claiborne established a point-of-sales data collection system in 1985. Its Systematic Updated Retail Feedback (SURF) system provided management with details on clothes sold in 16 representative stores around the country (Skolnik, 1985).

Owing to its high name recognition and extensive coverage in the editorial pages of many fashion magazines, Liz Claiborne was able to refrain from running expensive corporate advertising campaigns. Moreover, the absence of splashy, "fantasy-driven" advertising campaigns fit well with Liz Claiborne's image as a "trusted friend." It presented all its products in "co-op ads" produced in conjunction with local department stores.

Production and Distribution Choices

Since its inception, Liz Claiborne had contracted out the production of its merchandise. Moreover, it was one of the first big apparel makers in the 1980s to outsource production across the globe—mainly into Taiwan, Hong Kong, and South Korea. In its first year of operation, Liz Claiborne had used domestic manufacturers exclusively but encountered problems. The domestic suppliers were inflexible and unwilling to work with Liz Claiborne's new designs. Since Leonard Boxer had experience in apparel assembly in the Far East, he started to move production overseas. In 1982 Liz Claiborne was still sourcing about 50 percent of its merchandise domestically, but by 1994 only 14 percent of its merchandise was produced in the United States. Liz Claiborne had contracts with over 500 suppliers in 38 countries, with most of its suppliers being situated in China, South Korea, Sri Lanka, Hong Kong, and Indonesia. Twenty-four percent of its purchases were manufactured by its ten largest suppliers, with none of its suppliers accounting for more than 5 percent.

The company provided some support to contractors, but it did not engage directly in production until 1992. In that year, Liz Claiborne opened its first major production enterprise, a 270,000-square-foot plant in Augusta, Georgia, that annually turned out 500,000 to 1,000,000 pounds of cotton circular-knitted fabrics (jerseys, fleeces, and other types). One advantage of local production lay in response time: this factory was able to fill an order in 20 to 25 days, whereas it took Liz Claiborne's Asian suppliers often as long as 60 days plus shipping (Lee, 1994).

Liz Claiborne also differed from its competitors with respect to how often it offered its merchandise to its retailers. The apparel industry was used to a four-season buying cycle. Liz Claiborne, however,

invented two more seasons, pre-spring and pre-fall, to let stores buy six smaller inventory batches of fresh merchandise instead of four larger ones. While reducing inventory costs for the stores, this choice also helped Claiborne's suppliers, who operated more efficiently with two extra cycles filling their slack periods. In addition to offering two more collections, Liz Claiborne offered the collections later than its competitors, with the intent that clothes appropriate for the current season be available in the stores (Birmingham, 1985). Thus, instead of delivering fall goods in July, the company would ship them in late August and September. In other words, Liz Claiborne offered a new season every two months, with, for instance, the clothes delivered in January and February intended to be sold and worn during February and March.

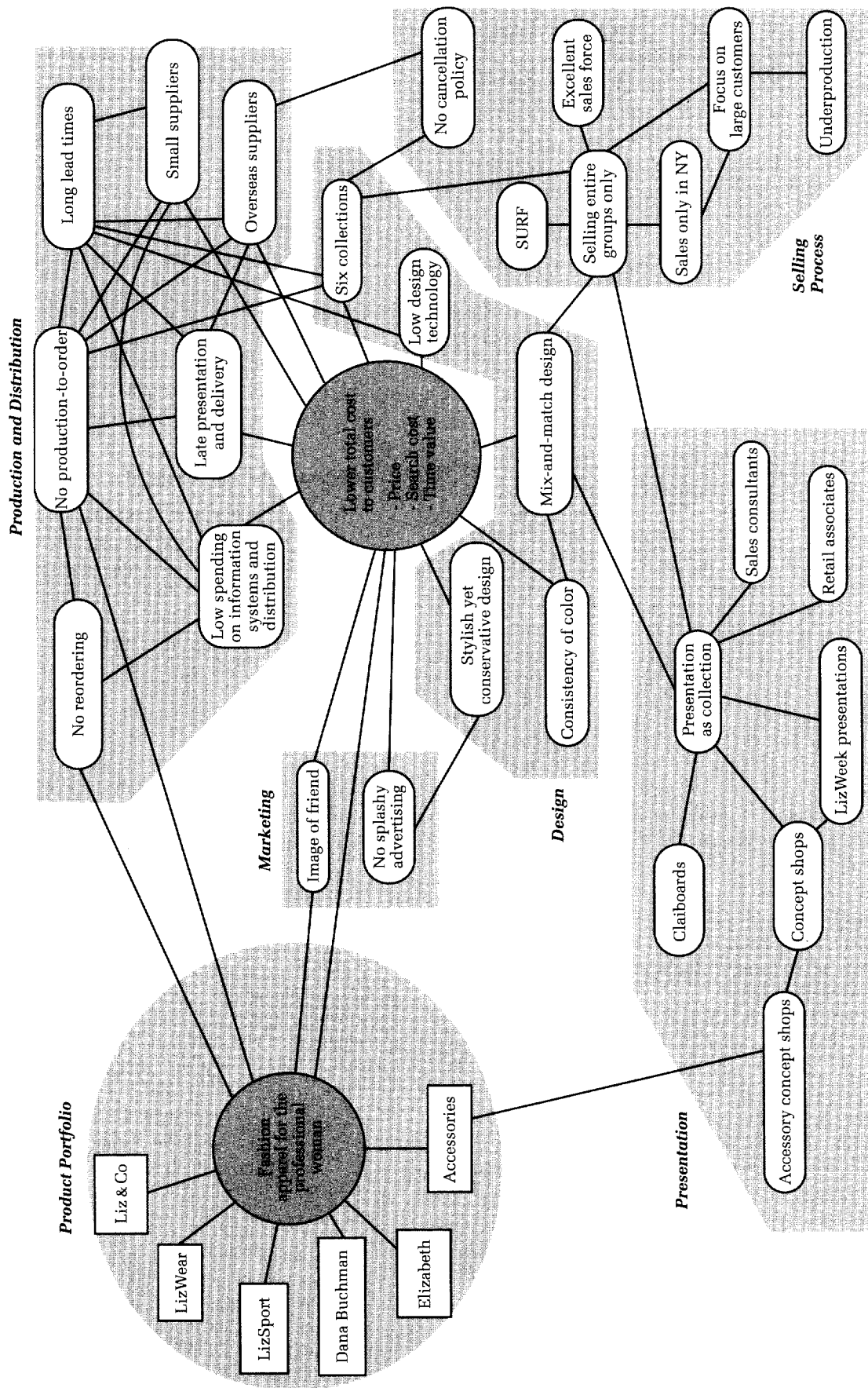
Internal and External Fit

As described in the previous subsections, Liz Claiborne's goal of dressing the professional woman with products that provided high value was implemented through a series of choices that particularly suited its strategy. To systematize the analysis, I grouped Liz Claiborne's choices into five categories: design, presentation, selling, marketing, and production/distribution. Figure 3 summarizes the choices within each category and displays the interactions among the choices. The following discussion elaborates on several of the interactions indicated in Figure 3, showing the high *internal fit* among Liz Claiborne's choices. A discussion of *external fit* is provided in the second half of this section.

Liz Claiborne's mix-and-match design could only be appreciated if the entire collection was presented together. Hence, it was important (and valuable) to push for a collection rather than a classification presentation. It should also be noted that once a collection presentation was in place, the returns to a mix-and-match design were increased. Thus, formally, collection presentation and mix-and-match design were complementary (Milgrom & Roberts, 1990).³ The collection-presentation format was supported by a host of other choices, such as concept shops, Clai-boards, retail associates, sales consultants, and Liz-Week department store presentations. Again, a complementarity existed: the value of these activities was increased by the presence of a collection presen-

³ Two elements, A and B, are complementary if the marginal benefit of A increases with the level of B, and vice versa. This concept can be extended to noncontinuous cases as long as A and B and their combinations can be ordered (Milgrom & Roberts, 1990).

FIGURE 3
Map of Interactions among Liz Claiborne's Choices in the Early 1990s



tation and, at the same time, the value of the collection presentation was increased by the support activities. Similarly, the apparel could provide its mix-and-match value only if the department store carried the full collection.

In this light, one can understand Liz Claiborne's strict policy of selling only complete groups to its customers. An incidental effect of this requirement was that end customers always saw a full collection in the department store, which strengthened confidence in the brand and increased its perceived value. A consequence of this vending policy with respect to Liz Claiborne's sales organization was that the company had to focus on large buyers. In addition, success with such an inflexible order policy necessitated a high level of trust in its customers. Liz Claiborne's decision to sell only in its New York show room addressed these concerns. On the one hand, senior department store management would come to New York to establish the required trust. On the other hand, the lost customers (those not willing to pay for the trip to New York) were small customers who were not able to buy a full line anyhow. The trust level was further bolstered by an expert sales force and its SURF system, which provided a closer contact with end customers than most other apparel designers could offer at the time. Lastly, Liz Claiborne's decision to offer six collections a year alleviated the inflexibility of being required to buy full lines, since a larger number of lines was offered. The ability to choose from six lines also lessened the impact of the no-cancellation policy, because each order could be smaller than would have been the case with four lines. The no-cancellation policy, in turn, made long-term planning possible, which was important for Liz Claiborne's overseas sourcing strategy. Since its overseas supply system implied longer lead times and inability to react quickly to demand changes, a steady demand was beneficial. In return, Liz Claiborne could provide high value (and achieve high margins), owing to the lower production costs of its overseas suppliers.

Since Liz Claiborne focused on large buyers, there was a potential risk of being squeezed by its customers. By following a strict underproduction policy, however, the company retained leverage over its customers. Moreover, this strategy had beneficial side effects. By producing slightly below demand, the sell-through was increased, which meant that Liz Claiborne merchandise was less frequently on sale (or was on sale in lower quantities). This in turn fortified the company's "everyday value" claim.

It is important to note that Liz Claiborne's set of choices involved trade-offs. Its decision to use mainly suppliers located in the Far East and to

invest little in design, distribution, and information technology all helped to keep costs down but led to three disadvantages: (1) it generated long lead times between the start of design to the delivery of the finished product, (2) retailers could not reorder, and (3) no merchandise could be made to order.

In evaluating the severity of these disadvantages, the external fit of Liz Claiborne's set of choices becomes apparent. All the disadvantages were alleviated by external factors: customer demand, retailers' requirements, available technology, and competitors' strengths. First, the impossibility of reordering was not crucial, since Liz Claiborne faced high customer demand mainly for fashion apparel that was not reordered anyway. Second, the health of Liz Claiborne's primary retail channel, department stores, was relatively solid during the 1980s. As a consequence, department stores were not (yet) concerned with reducing inventory, which would have put pressure on Liz Claiborne to offer reordering. Third, the information and design technology that would allow an efficient reordering system coupled with shortened design cycles was only in its early stages of development. As a result, there did not exist a feasible alternative set-up (in other words, a different peak) with which competitors could attack Liz Claiborne's position. Yet imitating Liz Claiborne (trying to climb the same peak and competing on the same terms) was very difficult, because the entire system of choices would have to be duplicated (Porter & Rivkin, 1998; Rivkin, 2000). Consequently, Liz Claiborne enjoyed a strong competitive position that enabled it to easily sell the majority of its output. In turn, with such "guaranteed demand," long lead times and no production-to-order did not pose a problem.

In sum, Liz Claiborne's choices showed high internal fit and—given the environmental conditions at the time—high external fit. In the 1980s, Liz Claiborne had positioned itself on a high peak in the performance landscape. However, during the late 1980s and early 1990s, changes in customer demand, retailers' economic health, and technological advances reduced the external fit of this coherent system: the height of Liz Claiborne's peak started to decrease when a new peak arose in the performance landscape.

LIZ CLAIBORNE'S FALL

Changes in Customer Demand and Product Portfolio

By the early 1990s, the trend towards "casualization" of the workplace had picked up momentum—a development that Liz Claiborne had first

underestimated (J. Lewis [president, Liz Claiborne Casual], personal communication, February 30, 1997). More and more companies allowed their employees to dress casually, yet customers could not find an attractive assortment of Liz Claiborne apparel to fulfill this need. Liz Claiborne eventually responded to this shift in customer demand and increased its offerings in the casual and more basic categories. In addition, in May 1992, Liz Claiborne acquired for \$31 million Russ Togs, Inc., which had filed for Chapter 11 protection the previous November. Russ Togs manufactured moderately priced women's sportswear under the Russ Togs and The Villager labels. The acquisition was intended to take Liz Claiborne into national and regional chain department stores and the moderate areas of traditional department stores.

These shifts in product portfolio appeared to be natural responses to changes in customer demands, but they had far-reaching consequences. The company increased its presence in apparel categories in which reordering had become a convenience offered by many competitors, yet it was not set up to offer efficient reordering.

Changes in the Retail Channel

During the late 1980s and early 1990s, Liz Claiborne's main distribution channel, the traditional department stores, underwent wrenching change. Several hostile takeovers and leveraged buyouts stretched the liquidity of many department store chains, often to the point of bankruptcy. Prominent examples of this development included Federated Department Stores, which filed for Chapter 11 protection in January 1990, R. H. Macy, which declared bankruptcy in January 1991, and Carter Hawley Hale, which filed for bankruptcy protection in February 1991. As a result, department stores tried to save cash wherever they could.

First, the stores cut down the retail support they provided to their vendors. For instance, much less attention was spent on the presentation and restocking of goods on the floor. Liz Claiborne, being accustomed to having retailers pay for concept shops and presentation support, failed to compensate for this deficit. Since careful presentation of Liz Claiborne's apparel as a collection was essential to its value proposition, the deterioration of shop-floor presentation was particularly detrimental for the company.

Secondly, department stores demanded larger discounts from their vendors. As well as refusing to pay for retailing support, Liz Claiborne refused to cut prices (J. Chazen, personal communication, October 7, 1997). Past success had created a sense of

infallibility, coupled with a tinge of hubris, at Liz Claiborne, as it has at many other successful companies (Miller, 1994). In 1989, Jay Margolis, the highest executive at the firm, after the remaining founders, proudly proclaimed: "We like to think of ourselves as the IBM of the garment district" (Deveny, 1989). Liz Claiborne's strong internal culture—the company directory still listed its employees alphabetically by first name—had created a belief in the organization's near invulnerability to environmental changes (Milliken, 1990). Moreover, negative performance was frequently attributed to external factors rather than to internal problems, another common pattern in firms responding to downturns (Ford, 1985). A former Claiborne executive commented as follows: "If the product didn't sell, it was always someone else's fault. The buyer didn't show it right, or it wasn't delivered the right way" (Caminiti, 1994). Yet, Liz Claiborne's apparel, with sagging sales and with lower margins for its retailers than other vendors' apparel provided, became less attractive to department stores and received even less attention and, eventually, less floor space.

Third, to alleviate their liquidity problems, department stores aggressively pursued inventory reduction. Increasingly, they demanded that manufacturers let them reorder items, so they could avoid buying in bulk and having to store merchandise in their stockrooms.

The Old Peak Declines, and a New Peak Arises

In addition to the retailers' demand for reordering, Liz Claiborne faced new competitors who employed a production paradigm allowing them to offer reordering efficiently. Improvements in information, design, and production technology, as well as the spread of standards in bar coding and point-of-sales-terminals, had made short reordering cycles, shorter design cycles, and partial production-to-order economically feasible (Abernathy, Dunlop, Hammond, & Weil, 1995). In other words, technological changes had created a new peak in the performance landscape that required a different set of choices. For instance, Jones Apparel, one of Liz Claiborne's strongest new competitors, sourced 55 percent of its products domestically, as compared to 14 percent for Liz Claiborne (D'Innocenzio, 1994). This sourcing strategy, in addition to heavy investments in design technology, allowed Jones to react quickly to new trends in the marketplace.

At the same time, with the demands of retailers and customers shifting, Liz Claiborne's set of choices, although still internally consistent, had become less appropriate to the environment. The

company's disadvantages, in particular the long design cycles and lack of reordering and production-to-order, had become more costly. In the 1980s, these disadvantages were small, given the Claiborne product portfolio, but by the 1990s the new requirements of retailers and the decreased costs of a lean production model had magnified the disadvantages: the relative height of Liz Claiborne's peak had declined.

Playing an Incomplete Game

In 1991, faced with increasing demands from retailers for reordering, Liz Claiborne initiated a reordering program for items in its casual division. The company's management followed the path described in the change framework as "playing an incomplete game": Liz Claiborne changed single elements in its activity system, with the consequence of a further performance decline. The firm moved down from its local peak to even lower performance.

The only elements of "quick response"—as these reordering programs became known in the apparel industry—that Liz Claiborne implemented were enabling stores' buyers to submit their orders electronically and promising to fill orders within two weeks. On the production side, no changes were made. The company produced a warehouse full of merchandise and then sold it as orders came in. Since inventory costs had never entered Liz Claiborne's profitability measurements, the inefficiency of this reordering process remained financially hidden (James Lewis, personal communication, February 30, 1997). Moreover, past success had created a buffer of \$300–\$500 million in cash and securities on Liz Claiborne's balance sheet (see Table 1). With this buffer, Liz Claiborne never experienced the liquidity problems that could have resulted from having funds tied up in inventory. Slack resources had reduced the necessity for Liz Claiborne's management to act upon this inefficiency—a common pitfall of past success, as Milliken and Lant (1991) pointed out.

In addition, allowing department store buyers to place orders (rather than having a vendor-driven continuous replenishment program) caused large swings in the volume of orders, which in turn meant either orders went unfilled or inventory was increased even further. Moreover, department store buyers whose allotted purchasing budget was exhausted often would not reorder at all—even styles which had been sold out—thus leaving popular styles out of stock.

As Figure 3 illustrates, the choice of "no reordering" was intimately tied to many other choices Liz Claiborne had made. Simply offering reordering to

retailers without making further changes in the system as a whole was bound to create problems. As Hammond (1993) outlined, partial production-to-order and a shortened product development cycle are necessary if a company is to pursue a quick-response strategy efficiently. Otherwise, inventory at the manufacturer starts to accumulate. However, Liz Claiborne's lead times were nine months, about three months longer than lead times of some of its competitors (D'Innocenzio, 1994). Figure 3 is also helpful in identifying the reasons for Liz Claiborne's long design-to-market cycle: the location of most of its suppliers in the Far East, the small size of its suppliers, who did not invest in information technology that would have reduced cycle times, and its small investments in technology, such as CAD systems that could reduce time to market. As this example illustrates, incremental changes in a tightly coupled system rarely lead to the desired result. Not until a new management had changed a whole series of choices in the design, distribution, and production set-up, moving Liz Claiborne to a new peak, did performance improve.

LIZ CLAIBORNE'S RENAISSANCE

In 1994, with Liz Claiborne's sales declining and net income plummeting by 35 percent, Paul Charron was hired as new chief operating officer. Charron had previously worked for Procter & Gamble and General Foods and had most recently been executive vice president at VF Corporation, the manufacturer of Wrangler and Lee jeans. In 1995, Charron replaced Chazen as CEO, while Chazen remained chairman of the company. This position was also taken on by Charron in 1996, when Chazen retired.

From the beginning of his tenure as CEO in 1995, Charron pursued three avenues of change within Liz Claiborne: (1) revitalization and modernization of choices within presentation and design that had been neglected over the previous years, (2) a shift in product portfolio, and (3) a wide-ranging restructuring of the company's production and distribution set-up.

Revitalization of Presentation and Design

In 1995, Charron created, under the name LizEdge, a new in-store marketing department. The company hired 125 sales associates, each responsible for in-store presentation of better sportswear in four locations. At the same time, Liz Claiborne started to install new in-store fixtures (LizView) in department stores around the country. By April 1997, 200 LizView shops had been installed, and

setting up another 400 by the end of 1997 was planned. As had occurred in the mid-1980s with the LizWorld shops, sales increased after the LizView shops were installed, going up an average 19 percent. In addition to providing the new fixtures, the firm began a training program (Liz & Learn) that provided sales support and incentives for department store salespeople.

To obtain a better understanding of the marketplace, Charron commissioned a study on the characteristics and shopping behavior of Liz Claiborne's customers. One of the study's findings was that customer confidence about picking outfits had risen considerably. In the early 1980s, Liz Claiborne's function had been to show what apparel was suitable for the workplace; now, customers asked to be presented with options. In the words of Charron, the customer "has gained confidence to 'put it together' by herself if she is provided with cues" (personal communication, February 30, 1997). These insights were taken into account in designing the new LizView in-store display units.

Another finding of the consumer study was that a typical customer played a large number of roles during the day (professional woman, soccer mom, and so forth) without having much time to change clothes. Hence, versatility of apparel and the ability to dress up or down quickly (for instance, by adding accessories or changing a top) were valued very highly. As a result, Liz Claiborne strengthened its efforts to allow its customers to mix and match across divisions (between LizSport and LizWear, for example).

To ensure that colors were held constant across collections and groups, designers of all units were required to use the same color card, which guaranteed consistency of color. Moreover, meetings among designers from all the companies' businesses were held on a regular monthly schedule; previously, they had met haphazardly.

Changes in Product Portfolio

For the long term, Charron was concerned that the current trend in retailing—the decline of the department stores and the rise of the discount stores such as Wal-Mart—would continue. Concurrent with the consolidation in the retail market, he expected a consolidation in the apparel supply market. As noted, prior to Charron's arrival, Liz Claiborne had acquired Russ Togs. The sales of this division, called the Special Markets Unit, increased to \$112 million by the end of 1994 (partly inflated by sell-offs of excess inventory) and decreased to \$77.3 million by the end of 1996. Charron decided to enlarge this unit. His vision was to have a differ-

ent Liz Claiborne brand for every retail channel and every price point: the Russ label for the "budget" segment (to be sold at stores like Wal-Mart); Villager and a new brand, First Issue, intended for the "moderate" segment (to be sold, for instance, at Sears); another new brand, Emma James, for the "upper-moderate" segment (to be sold at stores like Federated Department Stores); the traditional Liz Claiborne Collection and the casual lines, including LizWear, for the "better" segment (to be sold, for instance, at Dillard's); and the successful Dana Buchman line for the "bridge" segment (to be sold, for instance, at Saks Fifth Avenue) (Paul Charron, personal communication, February 30, 1997).

In order to increase general brand awareness, national brand advertising was increased substantially. Using the model Niki Taylor as the centerpiece of its advertising strategy, Liz Claiborne tried to rejuvenate its image, which had grown stale, especially in the eyes of the new generation of professional women. In addition to the public media campaign, at the end of 1994 the company made a statement within the fashion industry by opening a 19,000-square-foot flagship store at 650 Fifth Avenue.

Production and Distribution Changes

Whereas the new initiatives with respect to presentation consisted mainly of the modernization of previous practices, fundamental changes occurred in the way Liz Claiborne orchestrated its production and distribution. In 1995, Charron announced a comprehensive program, LizFirst, which was geared toward increasing efficiency. Its goals were to reduce excess inventories by 40 percent, cut cycle time by 25 percent, and reduce selling, general, and administrative expenses (SG&A) by \$100 million over three years. Two ways in which Liz Claiborne sought to fulfill its goals were to reduce the number of suppliers by half and to shift 50 percent of its production to the Western Hemisphere. By concentrating production within larger suppliers who could afford and were willing to invest in information and production technology, and by moving production closer to the region of retail, cycle times could be shortened.

Liz Claiborne also switched back to four instead of six production and design cycles. With six seasons, or a two-month delivery period, none of the merchandise could be made to order. With four seasons, the three-month delivery period allowed the company to produce at least some items to order for the third month of a season. Liz Claiborne also started with some of its clients a vendor-based restocking system, or retail inventory management

program (LizRim), in which the firm automatically replenished basic merchandise (mainly jeans, slacks, and shorts) to prior negotiated inventory levels at department stores. This system dramatically lowered "stock-outs" and kept inventory levels at department stores small, without causing huge production and order swings for Liz Claiborne.

One of the pioneers of such a vendor-based system had been Procter & Gamble (in cooperation with Wal-Mart). Later, VF Corporation and Haggar were among the first to adopt a similar system in the basic apparel industry. Charron's prior work experience at Procter & Gamble and VF Corporation provided him with valuable knowledge about the activities needed to support a successful implementation. At Liz Claiborne, the program was spearheaded by the casual wear division, whose new president had been recruited by Charron from Haggar in December 1994. Charron also brought further expertise in-house by hiring a new chief information officer who had previously been an executive vice president for business systems/logistics at a leading apparel retailer, and a new senior vice president for manufacturing and sourcing who had a background in low-cost private label manufacturing.

By 1997, LizFirst showed good results: Excess inventory had been cut by 47 percent from 1994 levels, its retail management program was in 1,200 stores, operating expenses had been reduced by \$82 million, and cycle time in certain key processes had been cut by 40 percent. Moreover, the number of factories Liz Claiborne used had been cut by half.

Internal Fit on a New Peak

Following the structure of Figure 3, Figure 4 depicts Liz Claiborne's choices as of 1997 in the five categories of design, presentation, selling, marketing, and production/distribution and displays the interactions between the choices. The locations of the five categories on the two maps have been kept approximately constant to facilitate comparison of the choices between the two time points depicted.

We find a familiar cluster of reinforcing choices dealing with the strengthening of the retail presentation. As noted above, Liz Claiborne was rejuvenating its former successful formula: mix-and-match design coupled with a careful presentation strategy involving, among other features, new displays and sales associates. The main changes within these categories were that mix-and-match was extended across divisions and that Liz Claiborne, rather than the retailers, paid for presentation support.

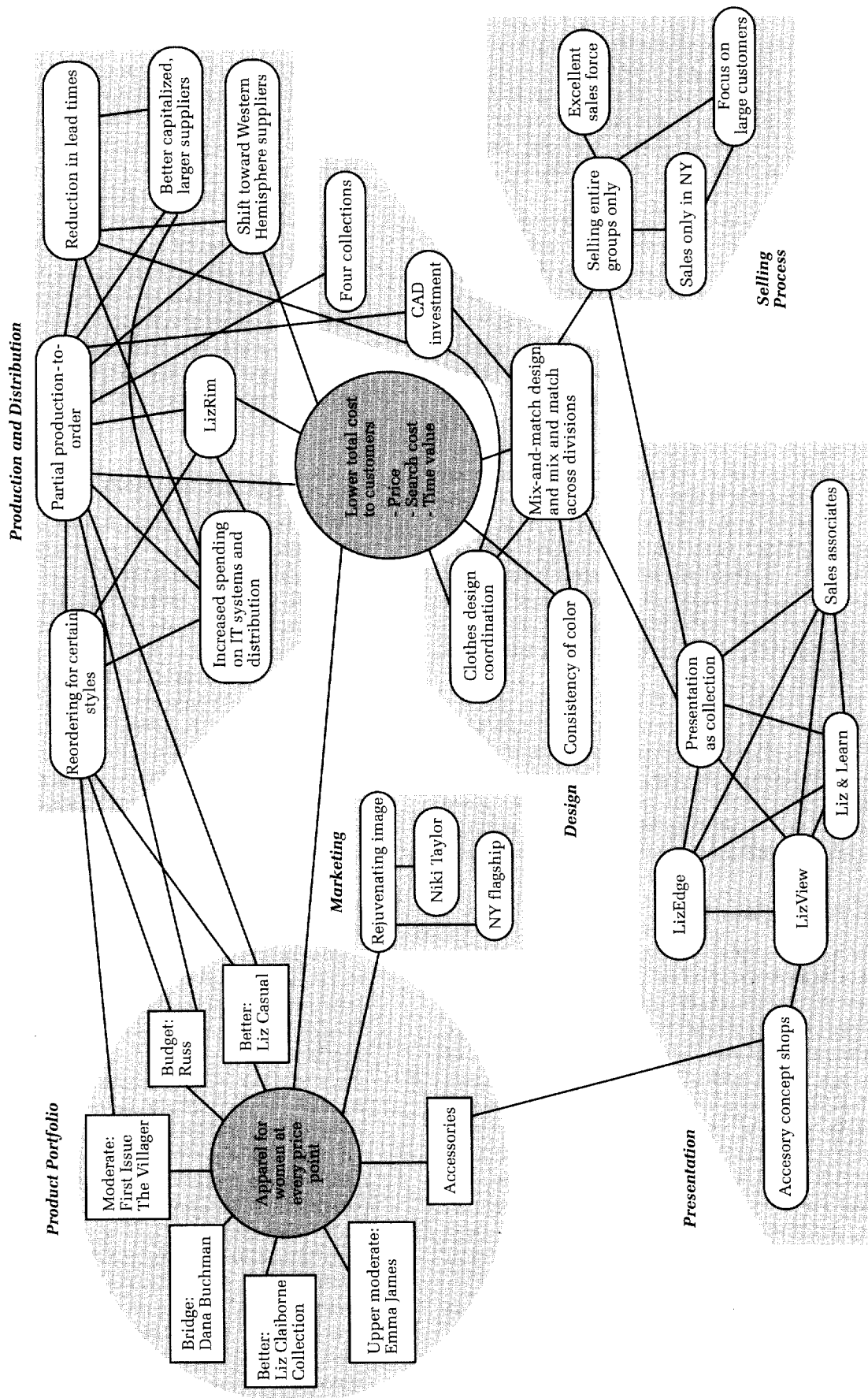
The largest number of new choices clustered around Liz Claiborne's new reordering process (LizRim) and around the system to allow partial production-to-order. Whereas the presentation support was mainly geared toward Liz Claiborne's traditional better sportswear, LizRim was designed to fulfill the requirements of the mass merchants that would carry its budget brands. However, because of its large size, the Liz Casual division, which belonged to the better sportswear division, was initially accounting for the largest use of LizRim. By keeping out-of-stock positions low, LizRim reinforced efforts with respect to the renewed presentation format—the best-trained salespeople and most cleverly designed display units could not sell merchandise that was out of stock.

DISCUSSION AND CONCLUSION

Why was Liz Claiborne's old management, like many other managements of declining organizations (Cameron, Whetten, & Kim, 1987), unable to respond to environmental changes? The analysis presented above suggests that a major contributing factor was that Liz Claiborne's management faced fit-conserving change. Environmental changes had decreased the value of a part of Liz Claiborne's set of choices (in particular, those concerning production and distribution). Small, incremental changes—exploring the local neighborhood of the current position—no longer sufficed. At the same time, larger, systemic changes lay outside the mental maps of existing management. Different mental maps of the changed performance landscape were required to move Liz Claiborne to a new performance peak.

The purpose of the framework developed in this article is to explore how fit influences the link between environmental changes and ensuing firm change. To this end, I suggested that a useful distinction can be made between environmental changes that affect external and/or internal fit. Whereas environments have been differentiated in the existing literature in terms of stability and turbulence, a distinction based on how *frequently* the performance landscape changes, I instead suggest classifying environmental changes with respect to the *impact* they have on the landscape. The framework thus offers an alternative and complementary classification. With this classification, the effect of environmental change on firms can be described as fit-destroying or fit-conserving—a useful distinction, since managers react differently to these two types of changes. Managers will have a particularly difficult time reacting to fit-conserving change be-

FIGURE 4
Map of Interactions among Liz Claiborne's Choices in 1997



cause the internal logic of the existing system of choices remains intact.

The argument outlined in this article finds a parallel in the conceptual approach of Henderson and Clark (1990), who studied a particular type of environmental change (a technological innovation) and its effects on incumbent firms. They suggest that, rather than distinguishing between incremental and radical innovations (thus measuring the magnitude of change), it is useful to classify innovations with respect to their impact on interactions within existing product systems. Analogously, we argue for the classification of environmental changes according to their impact on internal and external fit, rather than by their frequency. The new distinction Henderson and Clark (1990) introduced is whether an innovation changes architectural knowledge (how parts interact) or component knowledge (how parts work). This distinction allowed Henderson (1993) to explain the inertia of incumbent firms facing innovations in the photolithographic alignment equipment industry. Similarly, it is hoped that the framework proposed here and the distinction between fit-conserving and fit-destroying change will provide a new lens through which the impact of environmental changes on firms with high internal fit can be better understood.

In addition to providing a framework, concerning environmental change I believe that the maps of the firm's choices and their interactions can provide a helpful tool for understanding the structural requirements of change in a system with tight internal fit. For instance, in the present case, Liz Claiborne wanted to offer reordering. As Figures 3 and 4 illustrate, the choice of whether or not to offer reordering was tied to many other choices. Figure 3 can be used to predict the changes that were necessary to implement an efficient reordering process. Directly affected were the previous choices to keep spending on information and distribution technology low and the decision not to produce any apparel to order. One could call these "first-order" changes. However, to produce some merchandise to order, other choices had to be changed: part of the supplier base had to be shifted to the Western Hemisphere, the number of collections had to be reduced to four (which had implications for the design process), the delivery dates had to be moved up in time to allow information gathering early in the season for production delivered late in the season, and lead times had to be reduced. In turn, to reduce lead time, increased investments in design technology, and a shift to larger, better-capitalized suppliers who could invest in information and production technology had to follow. Thus, not

only first-order, but also second- and third-order changes were necessary. The mapping of choices and their interactions in Figures 3 and 4 make these ripple effects clearly visible. At the same time, these maps point out those choices that did *not* have to be changed. For instance, the presentation format, which was mainly connected to the design concept of mix and match, was not affected by changes in the production set-up.

The goal of this study was to outline a new framework and to use an in-depth case analysis for illustration. Clearly, more empirical work needs to be done to illustrate the contrasting effects of fit-conserving and fit-destroying change. For instance, according to the framework, in the face of benign fit-destroying change, firms with tight fit might react faster than firms with loosely coupled systems. On the conceptual side, conditions need to be identified under which fit-conserving and fit-destroying change are likely to arise. A first hypothesis, suggested by our framework and our empirical observations, is that fit-conserving change can be observed if technological change allows rival firms to compete with new *systems* of activities. In landscape terminology, fit-conserving change appears likely if new, high peaks are rising in the landscape. At the same time, moderate fit-destroying change is associated with environmental developments (such as technological improvements) that affect only individual activities.

A further extension of the framework would incorporate a more explicit description of how managers create mental maps of performance landscapes. With faulty representations, new questions arise. For instance, what are the performance consequences of faulty maps, given tight internal fit? What types of misrepresentations are particularly costly, and what are the implications for organizational design? In current work (Siggelkow, 2001), I am pursuing this line of research.

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