CHAPTER ONE – The Nature of Strategic Management

At the end of this chapter students will be able to:

- Define strategic management
- Describe stages of strategic management
- Explain the key terms and model of strategic management
- Describe benefits of Strategic management
- Elaborate business ethics & **corporate social responsibility.**

1.1. Defining strategy

Strategy can be defined as:

- A tool to organize & allocate an organization's resources in a viable way based on its internal competencies & shortcomings, anticipated changes in the environment.
- The use of entity's resources in the pursuit of its objectives against competition from rival organizations.
- An integrated and coordinated set of commitments and actions designed to exploit core competencies and gain a competitive advantage.

Thus, the main role of strategy is how to accomplish or achieve objectives by using the organization's resources & taking into consideration the external environment.

Generally, strategy is:

- A tool to implement policy
- The means used to achieve the ends / objectives
- A future plan that guides the scope & direction of an organization
- Integrated plan: all parts of the plan are compatible with each other & fit together well.

1.2.Defining Strategic Management

Strategic management can be defined as:

- The art and science of formulating, implementing, and evaluating cross-functional decisions that enable an organization to achieve its objectives. As this definition implies, it focuses on integrating management, marketing, finance/accounting, production/operations, research and development, and information systems to achieve organizational success.
- The on-going process of formulating, implementing and controlling broad plans guide the organizational in achieving the strategic goals given its internal and external environment.

- **Strategic management Vs strategic planning**

The term strategic management is often used synonymously with the term strategic planning. But strictly speaking, the term strategic management is used to refer to strategy formulation, implementation, and evaluation, with strategic planning referring only to strategy formulation. Moreover, strategic management is used more often in academia whereas strategic planning is used more often in the business world.

1.3.. Stages of Strategic Management

The strategic-management process consists of three stages: strategy formulation, strategy implementation, and strategy evaluation.

Stage One: Strategy Formulation

- Strategy formulation includes:
  - ✓ Developing a business mission
  - ✓ Identifying an organ's external opportunities & Threats
  - ✓ Determining internal strengths & weaknesses
  - ✓ Establishing long term objectives
  - ✓ Generating alternative strategies
  - ✓ Choosing the most strategies and allocating resources to pursue them.

Note: Strategies determine long term competitive advantages.

Stage Two: Strategy Implementation

- It is called the action stage of SM w/c includes the followings:
  - ✓ Setting annual objectives
  - ✓ Devising policies
  - ✓ Allocating resources
  - ✓ Developing a strategy supportive culture
  - ✓ Creating an effective organizational structure
  - ✓ Redirecting marketing efforts
  - ✓ Preparing budgets
  - ✓ Developing and utilizing information systems
  - ✓ Motivating and mobilizing employees & managers
  - ✓ Linking compensations to organizational performance

Note: It is the most difficult stage in SM. Why? It needs personal discipline, commitment & sacrifice.

Stage Three: Strategy Evaluation

- It is the final stage in strategic management.
- It is used to check and know whether a particular strategy is working well or not.
- It is crucial since today's success is not guarantee for tomorrows. Why? Due to dynamism hence, all strategies are subject to future modifications.
- The three strategy evaluation activities are:
  - ✓Reviewing internal and external factors (which are basis for current strategy)
  - ✓Measuring performances
  - ✓Taking corrective actions
- Stages of SM occur at three hierarchical levels in a large organization:
  - ✓ Corporate
  - ✓ Divisional or strategic business unit
  - ✓ Functional

1.4. Key Terms in Strategic Management

❖ There are nine key terms in strategic management.

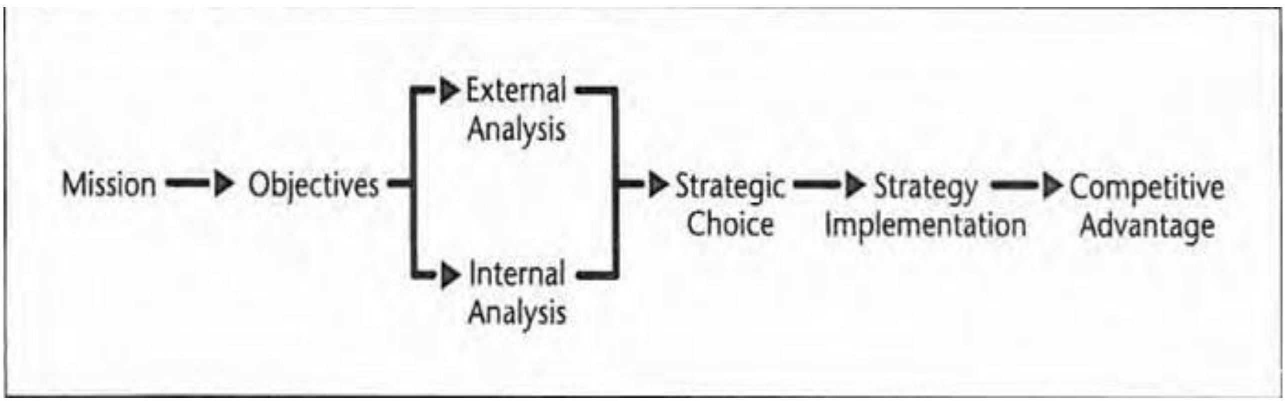
- **Strategists** are individuals who are most responsible for the success or failure of an organization and are called by different names: CEO, President, Chairman, Executive director etc.
- **Mission statement**
  - ✓ An enduring statements of purpose that distinguish one business from other similar firms.
  - ✓ It identifies the scope of a firm's operations in product and market terms.
  - ✓ It broadly charts the future direction of an organization.
- **External opportunities and threats**
  - ✓ Refer to economics, social, cultural, demographic, environmental, political, legal, governmental, technological and competitive trends and events that could significantly benefit or harm an organization in the future.
  - ✓ Opportunities and threats are largely beyond the control of a single organization. A basic **tenet/principle** of SM is that:
    - To take advantages of external opportunities, and
    - To avoid or reduce the impacts of external threats.
- **Internal strengths and weaknesses**
  - ✓ Controllable activities that are performed well or poorly relative to competitors.
  - ✓ Arise at corporate, functional & operational levels of organization.

- ✓ Can be determined in a number of ways; including: computing ratios (income, debt, equity, etc. ratios), measuring performances, employees' satisfaction and morale, production efficiency, advertising effectiveness & customer loyalty, etc.

- ➢ **Long term objectives**: Objectives can be defined as specific results that an organization seeks to achieve in pursuing its basic mission. Long term means more than one year.
- ➢ **Strategies:** are the means by which long-term objectives will be achieved. Business strategies may include geographic expansion, diversification, acquisition, product development, market penetration, retrenchment, divestiture, liquidation, and joint venture.
- ➢ **Annual objectives**: annual objectives are short term milestones that organizations must achieve to reach long term objectives.
- ➢ **Policies:** The means by which annual objectives will be achieved. It includes guidelines, rules and procedures established to support efforts to achieve stated objectives. Policies are guides to decision making and address repetitive situations.

1.5. STRATEGIC MANAGEMENT MODEL

The SM process can best be studied and applied using a model.



1.6. Benefits of Strategic Management

- ➢ **Financial Benefits**
  - ✓ More profitable & successful than those don't use SM.
  - ✓ Improved sales volume and optimum resource utilization.
  - ✓ Superior long term financial performances.
- ➢ **Non-financial Benefits:**
  - ✓ It allows an organization to be proactive than reactive in shaping its own future.
  - ✓ Enhanced awareness of external opportunities and threats.
  - ✓ An improved understandings of competitors' strategy.
  - ✓ Increased employees' productivity.
  - ✓ Reduced resistance to change.

- ✓ A clear understanding of performance-reward r/ships.

1.7. Business Ethics and Corporate Social Responsibility

Business ethics can be defined as principles of conduct within organizations ‘that guide decision making and behavior’. Good business ethics is a prerequisite for good strategic management, good ethics is good business. Strategists are the individuals primarily responsible for ensuring that high ethical principles are espoused and practiced in an organization. All strategy formulation, implementation and evaluation decisions have ethical ramifications (consequences).

- ✓ Protect the basic rights of the employees/workers
- ✓ Follow health, safety and environmental standards
- ✓ Indulge (treat) in truthful and reliable advertising
- ✓ Continuously improve product, operation, production to optimize use of resources.
- ✓ Do not replicate packing to mislead consumer.
- ✓ Strictly adhere to safety standards
- ✓ Accept new ideas, encourage feedback both from employees and customers
- ✓ Maintain accurate and true business records
- ✓ Treat everyone (employee and customer) with respect.
- ✓ Discourage black marketing, corruption and hoarding
- ✓ Do not accept child labor, forced labor and human rights abuse.

Corporate social responsibility is generally seen as the business contribution to sustainable development which has been defined as “development that meets the present needs without compromising the ability of future generations to meet their own needs”, and is generally understood as focusing on how to achieve the integration of economic, environmental, and social imperatives. Today it is generally accepted that business firms have social responsibilities that extend well beyond what in the past was commonly referred to simply as the ‘business economic function.’ In earlier times managers in most cases had only to concern themselves with the economic results of their decisions. Today, managers must also consider and weigh the legal, ethical, moral and social impact of each of their decision.

CHAPTER TWO

THE BUSINESS VISION, MISSION AND VALUES

After reading this lecture, you should be able to do the following:

- ✓ Describe the basic elements of mission statement
- ✓ Discuss the importance of vision and mission statements
- ✓ Know the process of developing mission statement.

Every organization has a unique purpose and reason for being. This uniqueness should be reflected in vision and mission statements. The nature of a business vision and mission can represent either a competitive advantage or disadvantage for the firm. An organization achieves a heightened sense of purpose when strategists, managers, and employees develop and communicate a clear business vision and mission.

2.1. Vision statement

What is Vision?

Management‘s view of the kind of company it is trying to create and its intent to stake out a particular business position represents a strategic vision for the company.

A vision statement is sometimes called a picture of your company in the future but it‘s so much more than that. Your vision statement is your inspiration, the framework for all your strategic planning. It is critically essential that management and executive agree on the basic vision, which the organization endeavors to accomplish over a period of time. A lucid and clear vision lays down a foundation on which a sound mission statement can be built. A vision statement may apply to an entire company or to a single division of that company. Whether for all or part of an organization, the vision statement answers the question, “Where do we want to go?” Vision statement also answers the question “What do we want to become?” What you are doing when creating a vision statement is articulating your dreams and hopes for your business. It reminds you of what you are trying to build.

- ➢ While a vision statement doesn‘t tell you how you‘re going to get there, it does set the direction for your business planning. That‘s why it‘s important when crafting a vision statement to let your imagination go and dare to dream – and why it‘s important that a vision statement captures your passion. Unlike the mission statement, a vision statement is for you and the other members of your company, not for your customers or clients. When writing a vision statement, your mission statement and your core competencies can be a valuable starting point for articulating your values. Be sure when you‘re creating one not to fall into the trap of only thinking ahead a year or two. Once you have one, your vision statement will have a huge influence on decision making and the way you allocate resources. A vision usually precedes the mission statement. It is usually short, concise and preferably limited to one sentence. Organization-wide management involvement is advisable. Vision defines the desired or intended future state of an organization or enterprise in terms of its fundamental objective and/ or strategic direction.

In short, vision statement;

- is a statement about a company‘s long-term direction
- hope to reality to be
- desired situation opposing the existing situation
- not realized in short or one‘s life time;
- keeps an organization moving forward;
- should be a description of the desired outcome of the strategic plan;

Organizations need a vision based on a set of values that everyone in share. Vision is used to set out a 'picture' of the organization in the future. Vision is what keeps an organization moving forward even against discouraging odds. Visions are broad, but point where to go.

Vision must be compelling, inspiring and make people want to join the organization. It is the banner, around which the organization rallies, since it is the driving force that keeps the organization move towards a feasible by inspired future conditions. If vision is vivid and meaningful enough, people can do outstanding things to bring to realization. However, if it is lacking, no amount of resources will induce people to move forward.

Vision Statement is a statement of the future ideal you are working towards. It outlines what the organization wants to be, or how it wants the world in which it operates to be. It provides inspiration and the basis for all the organization's planning. It concentrates on the future and provides clear decision-making criteria.

Purpose of Vision statement

- Shared vision is an initial force that brings people together.
- Clearly articulated vision can provide energy, momentum and strengths to individuals.
- It inspires stakeholders.
- It is life-blood of an organization.
- It helps to see what you are working towards.
- It provides bases for partnership and incentive to work through internal conflict.
- It binds an organization together in times of crises.

Therefore, a firm’s vision is determined by asking the following questions:

- What would the country lose if our organization ceased to exist?
- Why do we want to dedicate our creative energies to this organization‘s effort?
- What does our organization do to fill basic human needs?
- What does our organization do that impact the country?

A vision is the hope for ―the reality to be‖ to replace ―the reality that is‖.

Features of an effective vision statement include:

- ✓ Clarity and lack of ambiguity
- ✓ Vivid and clear picture
- ✓ Description of a bright future
- ✓ Memorable and engaging wording
- ✓ Realistic aspirations
- ✓ Alignment with organizational values and culture

To become really effective, an organizational vision statement must become assimilated into the organization's culture. Leaders have the responsibility of communicating the vision regularly; creating narratives that illustrate the vision; acting as role-models by embodying the vision; creating short-term objectives compatible with the vision; and encouraging others to craft their own personal vision compatible with the organization's overall vision.

2.2. Mission statement

What is Business Mission?

Historically mission is associated with Christian religious groups; indeed, for many years, a missionary was assumed to be a person on a specifically religious mission. The word "mission" dates from 1598, originally of Jesuits sending "missio", Latin for "act of sending" members abroad.

Mission statement-is an enduring statement of purpose distinguishes one firm from another in the same business. It is a declaration of a firm‘s reason for existence. Mission is a well convincible statement included fundamental and unique purpose which makes it different from other organization. It identifies scope of it operation in terms of product offered and market served. Mission also means what we are and what we do.

Mission Statements are also known as: Creed statement; Statement of purpose; Statement of philosophy; and Statement of business principles. Mission Statements reveal what an organization wants to be and whom it wants to serve and how? Mission Statements are essential for effectively establishing objectives and formulating strategies.

Mission statement;

- ❖ Is a general statement about the basic purpose of the organization
- ❖ Is the description of an organization‘s reasons for existence,
- ❖ Is the fundamental purpose Clarifies/ declares the purpose
- ❖ defines company‘s business; Product/ market; Territory/ geography
- ❖ Is the guiding principle that drives the processes of goal and action plan formulation, ―a pervasive, although general, expression of the philosophical objectives of the enterprise.

- ❖ Should focus on ―long – range economic potentials, attitudes toward customers, product and service quality, employee relations, and attitudes toward owners.
- ❖ Provides identity, continuity of purpose, and overall definition.

A mission statement is a statement of purpose. It will usually answer in a creative paragraph or to the following questions: What is the organization? What are core beliefs and commitments? Who is the service user? What is their need? What will be the benefit to them from this service? What will the service do to provide this benefit? Mission statements often contain the purpose and aim of the organization; the organization's primary stakeholders: clients, stockholders, congregation, etc. responsibilities of the organization toward these stakeholders; products and services offered. A mission statement is like a flag the organization can hold up that gives the essence of what it is about. Some mission statements are complex, long, and very broad; where as some mission statements are simple and direct.

According to Vern McGinis, a mission should:

- ❖ define what the company is
- ❖ define what the company aspires to be
- ❖ limited to exclude some ventures
- ❖ broad enough to allow for creative growth
- ❖ distinguish the company from all others
- ❖ serve as framework to evaluate current activities
- ❖ stated clearly so that it is understood by all

Characteristics of a good Mission Statement

In order to be effective, a mission statement should possess the following seven characteristics. Mission statement should be;

1. **Feasible**: a mission should always aim high but it should not be an impossible statement. In addition it should be realistic and achievable. Its followers must find it to be credible. But feasibility depends on the resources available to work towards a mission.
2. **Precise**: should not be so narrow to restrict the organization‘s activities nor should it be too broad to make itself meaningless.
3. **Clear**: should be clear enough to lead to action and should not be a high sounding set platitudes meant for publicity purposes.
4. **Motivating**: should be motivating for members of the organization or being its customers.
5. **Distinctive**: the indiscriminate one (random, arbitrary) is likely to have little impact. If all defined their mission in a similar fashion, there would not be much of a difference among

them. If defined as providing value for money, for years it created an important distinction in the public mind.

6. **Indicate major components of strategy**: along with the organizational purpose should indicate the major components of the strategy to be adopted.
7. **Indicate how objectives are to be accomplished**: Besides indicating the broad strategies to be adopted, it should also provide clues regarding the manner in which the objectives are to be accomplished.

Mission Statement Components

Mission statements can and do vary in length, content, format, and specificity. Most practitioners and academicians of strategic management feel that an effective statement should include nine components

1. ***Customers***—Who are the firm's customers?
2. ***Products or services***—What are the firm's major products or services?
3. ***Markets***—Geographically, where does the firm compete?
4. ***Technology***—Is the firm technologically current?
5. ***Concern for survival, growth, and profitability***—Is the firm committed to growth and financial soundness?
6. ***Philosophy***—What are the basic beliefs, values, aspirations, and ethical priorities of the firm?
7. ***Self-concept***—What is the firm's distinctive competence or major competitive advantage?
8. ***Concern for public image***—Is the firm responsive to social, community, and environmental concerns?
9. ***Concern for employees***—Are employees a valuable asset of the firm?

Strategic vision Vs mission

A strategic vision concerns	**A mission statement focuses on**
❖ a firms future business path	➢ current business activity
❖ Where are we going?	➢ Where we are & what we do?
❖ Market to be pursued	➢ Current product & service offerings
❖ Future technology-product-customer focused	➢ Customer needs being served
❖ Kind of company that management is trying to create	➢ Technological & business capabilities

2.3.Business values

It identifies the beliefs and behaviors that are reflected in all activities and define how you carry out the mission. Values are the principles and ideals that bind the organization together including the customers, employees, vendors, and all stakeholders. They are developed to frame an ethical context for the organization, and to many they are the “ethical standards” of the organization – the foundation for decision making within the organization. All leadership must operate from the same ethical frame of reference so that decisions of one will mirror the decisions of others.
Values are critically important to organizations because those who have the same value systems, or core values, tend to succeed within the organization, while those who do not share that set of values generally do not succeed. As employees are faced with daily decision-making, the core values will serve as the guidelines. When managers’ and employees’ values do not match those of the organization – stated or implied – the results could be turnover, decreased productivity, dissatisfaction.

Examples of mission and vision statement

- **Mission, vision and values of national bank Ethiopia**
  - ✓ To maintain price and exchange rate stability, to foster a sound financial system and undertake such function as are conducive to the economic growth of Ethiopia(**Mission)**
  - ✓ To be one of the strongest and most reputable central banks in Africa………. **Vision**
  - ✓ Promoting financial and monetary discipline…………………. **Values**
- **Mission, vision and values ministry of health**
  - ✓ To see healthy, productive and prosperous Ethiopian…………….. **Vision**
  - ✓ To promote health and wellbeing of Ethiopians through providing and regulating a comprehensive package of primitive, preventive, curative and rehabilitative health services of the highest possible quality in an equitable manner…………. **Mission**
  - ✓ Community first, collaboration, commitment, change, trust, continued, professional development…………**Values**

3.4. Setting goals and objectives

Goal and objectives imply the target that one’s efforts are desired to accomplish. Goals are generically for an achievement or accomplishment for which certain efforts are put. Objectives are specific targets within the general goal. Objectives are time related to achieve a certain task.

- A **goa**l is defined as the purpose of toward which an endeavor is directed. It is the result toward which effort is directed.
- An **objectives** has similar definition but is supposed to be a clear and measurable target.

Attributes of goals and objectives

- ❖ **Difference in scope:** Goal are broader than objectives in the sense that goals are general intentions and are not specific enough to be measured objectives are narrow and are set for certain tasks in particular.
- ❖ **Specificity:** Goals are general while objectives are specific
- ❖ **Tangibility:** Goal may be intangible while objectives are ought to be tangible. Goal may be directed at achieving non measurable things while objectives may be targeted at getting measurable things.
- ❖ **Time frame:** Goals usually have a longer time frame than objectives. Objectives are usually precise targets set for a short term. Goals may be set for a longer term but many objectives may be set within that goal.

Example

"I want to achieve success in the field of genetic research and do what no one has ever done"

"I want to complete the thesis on genetic research within this month"

Requirements of Sound Objectives

Objectives should SMART in short.

- ☞ **Specific;** Objectives should state the exact level of performance expected specifically. An objective must be specific with a single key result. If more than one result is to be accomplished, more than one objective should be written. Just knowing what is to be accomplished is a big step toward achieving it. What is important to you? Once you clarify what you want to achieve, your attention will be focused on the objective that you deliberately set. You will be doing something important to you.
- ☞ **Measureable;** as much as possible objectives should be expressed quantitatively, therefore, it is possible to easily determine whether or not goals have been achieved. An objective must be measurable. Only an objective that affects behavior in a measurable way can be optimally effective. If possible, state the objective as a quantity. Some objectives are more difficult to measure than others are. However, difficulty does not mean that they cannot be measured. Treatment of salespeople might be measured by looking at the absenteeism and turnover rates among the sales force. Also, salespeople could be asked to fill out a behavioral questionnaire anonymously giving their observations of the supervision they receive.
- ☞ **Achievable or acceptable;** objectives should be prepared in suitable, acceptable manner.

- ☞ **Realistic but challenging:** objectives should be attainable or real rather than fantasy. An objective must be attainable with the resources that are available. It must be realistic. Many objectives are realistic. Yet, the time it takes to achieve them may be unrealistic. For example, it is realistic to want to lose ten pounds. However, it is unrealistic to want to lose ten pounds in one week. What barriers stand between you and your objective? How will each barrier be overcome and within what time frame? It is also better to have challenging objectives as far as they could motivate workers if attained.
- ☞ **Time bounded:** objectives should be set with in specific time limits or target dates for their attainment. The objective should be traceable. Specific objectives enable time priorities to be set and time to be used on objectives that really matter. Are the time lines you have established realistic? Will other competing demands cause delay? Will you be able to overcome those demands to accomplish the objective you've set in the time frame you've established?

Advantages of Objectives

The following are some of the advantages of objectives.

- ✓ **Unified planning:** Various plans are prepared at various level in the organization. These plans are consistent with the objectives and hence objectives encourage unified planning.
- ✓ **Individual motivation:** Objectives act as motivators for individual and departments imbuing their activity with a sense of purpose.
- ✓ **Coordination:** Objectives facilitate coordinated behavior of various groups which otherwise may pull in different directions.
- ✓ **Control:** Objectives provide yardstick for performance. The actual performance is compared with standard performance and hence objectives facilitate control.
- ✓ **Basis for decentralization:** Department-wise or section wise objectives are set in order to achieve common objectives of the organization. These objectives provide basis for decentralization

CHAPTER THREE

EXTERNAL ENVIRONMENT ASSESSMENT

Strategic analysis is basically concerned with the structuring of the relationship between a business and its environment. The environment in which business operates has a greater influence on their successes failures. There is a strong linkage between the changing environment, the strategic response of the business to such changes and the performance. It is therefore important to understand the forces of external environment the way they influence this linkage. The external environment which is dynamic and changing holds both opportunities and threats for the organizations. The organizations while attempting at strategic realignments, try to capture these opportunities and avoid the emerging threats. At the same time the changes in the environment affect the attractiveness or risk levels of various investments of the organizations or the investors.

The Nature of an External Audit

The purpose of an *external audit* is to develop a finite list of opportunities that could benefit a firm and threats that should be avoided. As the term *finite* suggests, the external audit is not aimed at developing an exhaustive list of every possible factor that could influence the business; rather, it is aimed at identifying key variables that offer actionable responses. Firms should be able to respond either offensively or defensively to the factors by formulating strategies that take advantage of external opportunities or that minimize the impact of potential threats.

Environmental Scanning

There are forces of different kinds and complexities, which influence organizations and their business. The basic aim of strategic management is that a manager must adjust strategies to reflect the environment in which the business operates. Environmental scanning is one of the few ways to detect future driving forces early and this involves studying and interpreting the development of social, political, economic, ecological and technical events that could become driving forces. It attempts to figure out few radical happenings or path breaking developments which may be catching on and see their possible implications.

Environmental scanning is normally accomplished by systematically monitoring and studying current events and constructing scenarios. Constructing scenarios involves a detailed plausible view of how the business environment of an organization might develop in the future based on the groupings of key environmental influences and drivers of change about which there is high level of uncertainty. Scenarios are tools for ordering one's perceptions about alternative future environments in which today's decisions might be framed. In practice, scenarios resemble a set stories, written or spoken, built around carefully constructed plots. Scenario planning process can be understood by the following steps:-

Step-1: Identification of the Issues

Understand the effects of external factors on business are very essential. These factors are:

- Technology driven (new product, IT based integration)
- Political (deregulation, instability)
- Economic (sudden downturns, boom)
- Competitive positioning (moves from competitors)

Participants need not limit themselves to above mentioned factors only; any factor that may have an impact on the company is acceptable.

Step-2: Classification of the Issues

- ☞ Support the issue identified with reports/propositions/any other method.
- ☞ Determine the uncertainty and kind of impact of the issue.

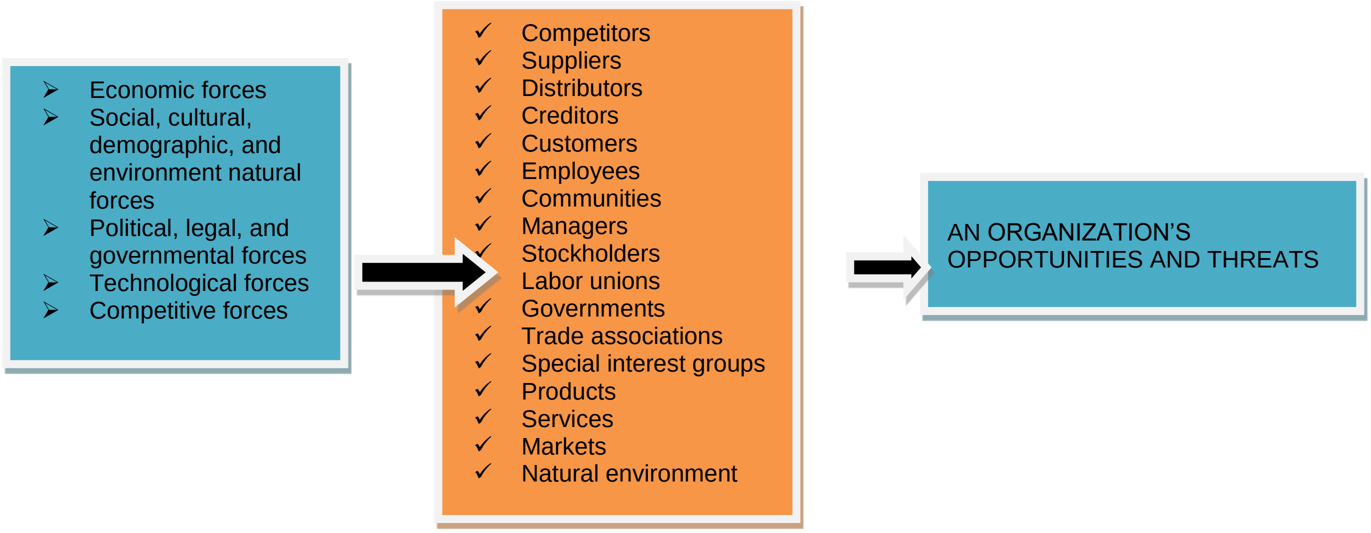
Step 3 Analyzing and Problem Solving

Analysis of key external factors

External forces can be divided into five broad categories:

1. Economic forces;
2. Social, cultural, demographic, and natural environment forces;
3. Political, governmental, and legal forces;
4. Technological forces; and
5. Competitive forces.

External trends and events such as the global economic recession, significantly affect all products, services, markets, and organizations in the world. Changes in external forces translate into changes in consumer demand for both industrial and consumer products and services. External forces affect the types of products developed, the nature of positioning and market segmentation strategies, the types of services offered, and the choice of businesses to acquire or sell. In addition, external forces directly affect both suppliers and distributors. Identifying and evaluating external opportunities and threats enables organizations to develop a clear mission, to design strategies to achieve long-term objectives, and to develop policies to achieve annual objectives.



1. ECONOMICFORCES

Refers to the nature and direction of the economy in which the business operates or competes. Because consumption patterns are affected by the relative affluence of various market segments, each firm must understand economic trends in the segments that affect its industry. Economic factors have a direct impact on the potential attractiveness of various strategies. For example, as interest rates rise, then funds needed for capital expansion become more costly or unavailable. Also, as interest rates rise, discretionary income declines, and the demand for discretionary goods falls.

Key Economic Variables to Be Monitored

- Availability of credit
- Level of disposable income
- Propensity of people to spend
- Interest rates
- Inflation rates
- Money market rates
- Federal government budget deficits
- Gross domestic product trend
- Consumption patterns
- Unemployment trends
- Worker productivity levels
- Value of the dollar in world markets
- Stock market trends
- Foreign countries' economic conditions
- Import/export factors
- Demand shifts for different categories of goods and services
- Income differences by region and consumer groups
- Price fluctuations
- Monetary policies
- Tax rates
- Organization of Petroleum Exporting Countries (OPEC) policies
- Coalitions of Lesser Developed Countries (LDC) policies

They affect the economic factors and affect the customers buying behaviors. The customers are more conscious about the economic changes and responds according to the changes in key variable factors. So, any change in the price affects the customer buying trend directly.

1. **SOCIAL, CULTURAL, DEMOGRAPHIC, AND ENVIRONMENTAL FORCES**

Social forces involve the beliefs, values, attitudes, opinions and life styles of those in firm‘s external environment as developed from ecological, demographic, religious, educational, and ethnic conditioning. Social, cultural, demographic, and environmental changes have a major impact upon virtually all products (Preferences change), services, markets, and customers. Small, large, for-profit and nonprofit organizations in all industries are being staggered and challenged by the opportunities and threats arising from changes in social, cultural, demographic, and environmental variables.

Key variables of Social, Cultural, Demographic, and Environmental Variables

- Childbearing rates
- Number of special interest groups
- Number of marriages
- Number of divorces
- Number of births
- Number of deaths
- Immigration and emigration rates
- Life expectancy rates
- Per capita income
- Location of retailing, manufacturing, and service businesses
- Attitudes toward business
- Lifestyles
- Average disposable income
- Trust in government
- Attitudes toward government
- Attitudes toward work
- Buying habits
- Ethical concerns
- Attitudes toward saving
- Sex roles
- Attitudes toward investing
- Average level of education
- Attitudes toward retirement
- Attitudes toward leisure time
- Attitudes toward product quality
- Attitudes toward customer service
- Pollution control
- Attitudes toward foreign peoples
- Energy conservation
- Social programs
- Number of churches
- Number of church members
- Social responsibility
- Population changes by race, age, sex, and level of affluence

- Population changes by city, county, state, region, and country
- Value placed on leisure time
- Regional changes in tastes and preferences
- Number of women and minority workers
- Number of high school and college graduates by geographic area
- Air and water pollution

2. POLITICAL, GOVERNMENTAL, AND LEGAL FORCES

Federal, state, local, and foreign governments are major regulators, deregulators, subsidizers, employers, and customers of organizations. Political, governmental, and legal factors, therefore, can represent key opportunities or threats for both small and large organizations.

For industries and firms that depend heavily on government contracts or subsidies, political forecasts can be the most important part of an external audit. Changes in patent laws, antitrust legislation, tax rates, and lobbying activities can affect firms significantly.

The increasing global interdependence among economies, markets, governments, and organizations makes it imperative that firms consider the possible impact of political variables on the formulation and implementation of competitive strategies.

Key variables of political, governmental, and legal forces:

- Government regulations or deregulations
- Changes in tax laws
- Special tariffs
- Political action committees
- Voter participation rates
- Number, severity, and location of government protests
- Number of patents
- Changes in patent laws
- Environmental protection laws
- Level of defense expenditures
- Legislation on equal employment
- Level of government subsidies
- Antitrust legislation
- Import-export regulations
- Political conditions in foreign countries
- Special local, state, and federal laws
- Lobbying activities
- Size of government budgets
- Location and severity of terrorist activities
- Local, state, and national elections

3. TECHNOLOGICAL FORCES

Revolutionary technological changes and discoveries are having a dramatic impact on organizations. The *Internet* has changed the very nature of opportunities and threats by altering the life cycles of products, increasing the speed of distribution, creating new products and services, erasing limitations of traditional geographic markets, and changing the historical trade-off between production standardization and flexibility. The Internet is altering economies of scale, changing entry barriers, and redefining the relationship between industries and various suppliers, creditors, customers, and competitors. Technological forces represent major opportunities and threats that must be considered in formulating strategies. Technological advancements can dramatically affect organizations' products, services, markets, suppliers, distributors, competitors, customers, manufacturing processes, marketing practices, and competitive position. Technological advancements can create new markets, result in a proliferation of new and improved products, change the relative competitive cost positions in an industry, and render existing products and services obsolete. Technological changes can reduce or eliminate cost barriers between businesses, create shorter production runs, create shortages in technical skills, and result in changing values and expectations of employees, managers, and customers. Technological advancements can create new competitive advantages that are more powerful than existing advantages. Many strategists spend countless hours determining market share, positioning products in terms of features and price, forecasting sales and market size, and monitoring distributors; yet too often, technology does not receive the same respect.

Examples of the Impact of Wireless Technology

- Airlines—many airlines now offer wireless technology in flight.
- Automotive—Vehicles are becoming wireless.
- Banking—Visa sends text message alerts after unusual transactions. Education—Many secondary (and even college) students may use smart phones for math because research shows this to be greatly helpful.
- Energy—Smart meters now provide power on demand in your home or business.
- Health Care—Patients use mobile devices to monitor their own health, such as calories consumed.
- Market Research—Cell phone respondents provide more honest answers, perhaps because they are away from eavesdropping ears.
- Politics—President Obama won the election partly by mobilizing Face book and MySpace users revolutionizing political campaigns. Obama announced his vice presidential selection of Joe Biden by a text message.
- Publishing—eBooks are increasingly available.

4. COMPETITIVE FORCES

An important part of an external audit is identifying rival firms and determining their strengths, weaknesses, capabilities, opportunities, threats, objectives, and strategies. Collecting and evaluating information on competitors is essential for successful strategy formulation. Identifying major competitors is not always easy because many firms have divisions that compete in different industries. Many multidivisional firms do not provide sales and profit information on a divisional basis for competitive reasons. *Competitive intelligence* (*CI*), as formally defined by the Society of Competitive Intelligence Professionals (SCIP), is a systematic and ethical process for gathering and analyzing information about the competition's activities and general business trends to further a business's own goals. The more information and knowledge a firm can obtain about its competitors, the more likely it is that it can formulate and implement effective strategies. Major competitors' weaknesses can represent external opportunities; major competitors' strengths may represent key threats.

Firms need an effective competitive intelligence (CI) program. The three basic objectives of a CI program are (1) to provide a general understanding of an industry and its competitors, (2) to identify areas in which competitors are vulnerable and to assess the impact strategic actions would have on competitors, and (3) to identify potential moves that a competitor might make that would endanger a firm's position in the market. Competitive information is equally applicable for strategy formulation, implementation, and evaluation decisions. An effective CI program allows all areas of a firm to access consistent and verifiable information in making decisions.

Market commonality can be defined as the number and significance of markets that a firm competes in with rivals. *Resource similarity* is the extent to which the type and amount of a firm's internal resources are comparable to a rival. One way to analyze competitiveness between two or among several firms is to investigate market commonality and resource similarity issues while looking for areas of potential competitive advantage along each firm's value chain.

Industry Analysis

An **industry** is a group of firms that produces a similar product or service, such as soft drinks or financial services. An examination of the important stakeholder groups, such as suppliers and customers, in a particular corporation's task environment is a part of industry analysis. Michael Porter, an authority on competitive strategy, contends that a corporation is most concerned with the intensity of competition within its industry. "The collective strength of these forces," he contends, "determines the ultimate profit potential in the industry, where profit potential is measured in terms of long-run return on invested capital." In carefully scanning its industry, a corporation must assess the importance to its success of each of six forces: threat of new entrants, rivalry among existing firms, threat of substitute products or services, bargaining power of buyers, bargaining power of suppliers, and relative power of other stakeholders. The stronger each of these forces, the more limited companies are in their ability to raise prices and earn greater profits. Although Porter mentions only five forces, a sixth—other stakeholders—is added here to reflect the power that governments, local communities, and other groups from the task environment wield over industry activities.

Competitors analysis: - Porter's five forces framework

The five forces framework developed by Michael porter is the most widely known tool for analyzing the competitive environment, which helps in explaining how forces in the competitive environment shape strategies and affect performance. The framework suggests that there are competitive forces other than direct rivals which shape up the competitive environment. These competitive forces are:

1. the potential new entrants
2. the substitutes products
3. the bargaining power of suppliers
4. the bargaining power of buyers
5. the rivalry among competitors in the industry

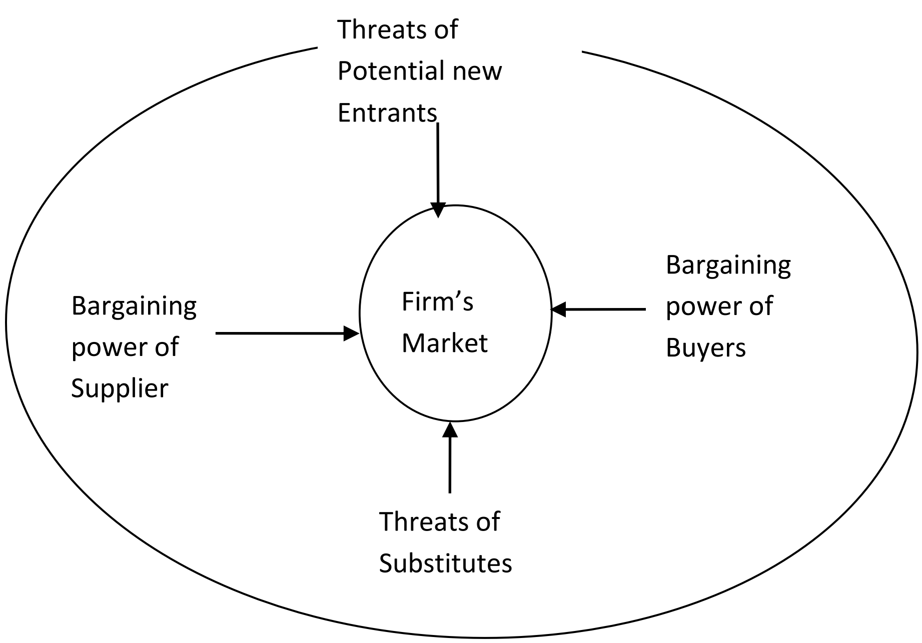


Figure 4.2: Five Force Analysis

However, these five forces are not independent of each other. Pressures from one direction can trigger off changes in another which is capable of shifting sources of competition. In the following section each of these five forces are discussed in detail as to understand how each of these forces affect an industry's environment so that one can identify the most appropriate strategic position within the industry.

1. Threat of New Entrants

Entry of a firm in and operating in a market is seen as a threat to the established firms in that market. The competitive position of the established firms is affected because the entrants may add new production capacity or it may affect their market shares. They may also bring additional resources with them which may force the existing firms to invest more than what was not required before. Altogether the situation becomes difficult for the existing firms if not threatening always and therefore they resort to raising barriers to entry. These barriers are intended to discourage new entrants and this may be done by organizations, be in any one or more ways as discussed below:

A. **Economics of scale:** - Firms which operate on a large scale get benefits of lower cost of production because of the economies scale. Since the new firm normally would start its operation at a smaller scale; and therefore will have a relatively higher cost of production, its competitive position in the industry gets adversely affected. This barrier created through large scale of operation is not only applicable for production side but it can be extended to advertising , marketing, distribution, financing, after sales customer service, raw materials, purchasing and research and development as well. For e.g., you would have noticed in durable industry the kind of investments which players like Samsung and LG do on advertising and promotions normally and specially during events like FFA world cup match. This makes it nearly impossible for any new third player to launch and sustain such intensive and investment driven marketing attack.
B. **Learning or Experience effect**: The theory explaining the experience curve or the learning curve suggests that as firms produce they grow more efficient and this brings them cost benefits. The efficiency levels are an outcome of the experience, which teaches the organization better ways of doing things. This again keeps any new entrant at a disadvantage.
C. **Cost disadvantage independent of scale**: new entrants may face disadvantages which are independent of the operations. It may be on account of the lack of proprietary product

knowledge such as patents, favorable access to raw material, favorable locations, existing plants built and equipped years earlier at lower costs, lower borrowing costs etc.

D. **Brand benefits**: buyers are often attached to established brands. Differences in physical or mere perceived value make existing products unique and the new entrants have to tire out to beat such brands and change the mindset of the customers.

E. **Capital requirements**: high investments required for start up in any business is another deterrent for new entrants bringing down the possibility of increased competition.

F. **Switching costs**: Switching costs, which is nothing but the expenses (financial or psychological) which a customer incurs in switching from one seller to another. Cases where such an expense is higher, new entrants find it difficult to establish or survive. Such costs may be because of a strong brand association or the comfort level a customer may be enjoying or it may be on account of a particular technology, which most customers use and therefore will find it inconvenient to switch to other products/service.

G. **Access to distribution channel**: any such critical activity like distribution channel in the business can be a barrier for the entrants when accessibility to them is found to be difficult. Most existing firms in Fast Moving Consumer Goods (FMCG) industry are found to have a strong favorable distribution channels which is very difficult to penetrate.

☞ In addition to the above, few general entry barriers exist in each industry's case, for example, regulatory policies, tariffs and international trade restrictions are few such additional factors.

2. The Threats of Substitutes

Often firms in an industry face competition from outside industry products, which may be close substitutes of each other. For e.g., with the new technologies in place now the electronic publishing are the direct substitutes of the texts published in print. However, the competitive pressure, which any industry may face, depends primarily on three factors:

i. Whether the substitutes available are attractively priced
ii. Whether buyers view substitutes available as satisfactory in terms of their quality and performance
iii. How easily buyers can switch to substitutes.

Generally it is observed that the availability and acceptability of substitutes determine an upper price limit to a product. When relative prices of the product in question rise above that of the substitute products, customers tend to switch away from them.

3. Bargaining Power of Suppliers

Business organizations have a large dependency on suppliers and the latter influence their profit potential significantly. Suppliers' decisions on prices, quality of goods and services and other terms and conditions of delivery and payments have significant impact on the profit trends of an industry. However, suppliers' ability to do all these depends on the bargaining power over buyers.

Suppliers' bargaining power would normally depend on:

A. ***Importance of the buyer to the supplier group***: the size of the suppliers taken by a particular buyer is likely to put the buyers in a relatively advantageous position. The same may be found true if the supplier tends to get an image advantage by supplying to a particular firm. Consequently in dealing with such buyers, suppliers' bargaining power is naturally reduced. Just opposite happens when buyer is not so important to the supplier and the later then is less likely to offer favorable terms to win or retain the customer.
B. **Importance of the Suppliers' Product to Buyer**: Here the position may just be opposite of the above situation where suppliers have a better bargaining power coming from their sheer size or image.
C. ***Greater concentration among suppliers than buyers***: an industry, which is largely dominated by a few large firms, is a highly concentrated industry. Such few firms hold greater power with them as the proportion of the industry's total output is in hands such large firms. This gives such firms greater power over those who do business with them.
D. ***High switching costs for buyers***: In this case buyers suffer b/c of the suppliers' advantageous position or by the nature of supplies itself; the buyers have to face a higher switching cost.
E. ***Credible threats of forward integration by suppliers***: Suppliers in a given situation may see an opportunity in moving up the value chain and may seriously think of getting into the business of what its buyers have been doing till now. Any indication of that nature from supplier side puts the buyers at the receiving end as they feel threatened b/c of a new player in that market and losing an assured source of supplies.

4. **Bargaining Power of Customers**

Customers with a stronger bargaining power relative to their suppliers may force supply prices down or demand better quality for the same price and may demand more favorable terms of business. For e.g., there will always be a difference in the bargaining power b/n an individual buying different construction material like cement, steel or bricks and a real estate builder buying them for the number of properties he may have been building over so many years.

1. ***Undifferentiated or standard supplies***: a supplier, given the nature of products it supplies, may have a very limited choice in providing any differentiated products and this enables a customer to get the deal at the most favorable terms
2. ***Customer's price sensitivity***: Customer's buying behavior varies with respect to their sensitivity to prices. Depending on how important the item is for the customer's usage and proportion he may spending on the item concerned, buyers' sensitivity to price varies.
3. ***Accurate information about the cost structure of suppliers***: A more informed customer is capable of negotiating with suppliers. Whenever such customers notice a decline in the supplier's cost's they would always bargain for a proportional decrease in price.
4. ***Greater concentration in buyer's industry than in supplier's industry and relatively large volume purchase***: This means that buyers are large and more powerful than suppliers.
5. ***Credible threat of backward integration by buyers***: different from forward integration which suppliers tend to attempt at, buyers in order to hold their position stronger in the market may integrate in backward manner. This will mean that the buyer extends itself to the previous stage of manufacturing or distribution for which it had been dependent on suppliers till now.

5. Competitive Rivalry

The level of rivalry is minimum in a perfectly competitive market where there are large number of buyers and sellers and the product is uniform with everyone. Same is true for a monopoly market where there is only one player and the type of product is also one. However in case of oligopoly or monopolistic competition, where you will find few players and the market conditions allow them to differentiate their products and services, competition if found to be fierce.

I. ***The Stability of Environment***: An unstable environment is likely to call for a hyper-competitive situation and of the several factors that affect stability could be technological innovation, changes in government regulations, customers' profile and their needs.

II. ***The life expectancy of competitive advantage***: There are industries for example, consumer electronics, in which the fruits of innovations do not last longer and hence the companies do not even bother to patent them. This has an adverse implication for the stability of the competitive environment leading to intense rivalry. Length of innovation cycle, patent protection or switching costs between rivals is few factors; which may impact the life expectancy of competitive advantage.

III. ***Characteristics of the strategies pursued by competitors***: this also has or may have an impact on the general approach to rivalry. For e.g., in a market segmented approach on part of the competitor leads to lesser rivalry situation. Also the kind of goals, which competitors pursue, has an impact on the rivalry.

- Lastly, few implications can be picked up from the five forces framework itself. Lower threats to entry or a higher possibility for substitutes have the potential of increasing rivalry. A lower engagement b/n supplier will result into a lesser rivalry. So will be the effect when buyers face higher switching costs.
- In an overall assessment, two critical observations regarding rivalry can be made here. First a powerful competitive strategy employed by one rival can greatly intensify the competitive pressure on other rivals. Second, the frequency and rigor with which rivals use any or all competitive weapons at their disposal can be a major determinant of whether the competitive pressures associated with rivalry are cutthroat, fierce, strong, moderate or weak.

4.4. Sources of external information

A wealth of strategic information is available to organizations from both published and unpublished sources.

- **Unpublished sources** include customer surveys, market research, speeches at professional and shareholders' meetings, television programs, interviews, and conversations with stakeholders.
- **Published sources** of strategic information include periodicals, journals, reports, government documents, abstracts, books, directories, newspapers, and manuals. The Internet has made it easier for firms to gather, assimilate, and evaluate information.

4.5 Forecasting Tools and Techniques

Forecasts are educated assumptions about future trends and events. Forecasting is a complex activity because of factors such as technological innovation, cultural changes, new products, improved services, stronger competitors, shifts in government priorities, changing social values, unstable economic conditions, and unforeseen events. Managers often must rely on published forecasts to effectively identify key external opportunities and threats. A sense of the future permeates all action and underlies every decision a person makes. People eat expecting to be satisfied and nourished in the future. People sleep assuming that in the future they will feel rested. They invest energy, money, and time because they believe their efforts will be rewarded in the future. They build highways assuming that automobiles and trucks will need them in the future. Parents educate children on the basis of forecasts that they will need certain skills, attitudes, and knowledge when they grow up. The truth is we all make implicit forecasts throughout our daily lives. The question, therefore, is not whether we should forecast but rather how we can best forecast to enable us to move beyond our ordinarily unarticulated assumptions about the future. Can we obtain information and then make educated assumptions (forecasts) to better guide our current decisions to achieve a more desirable future state of affairs? We should go into the future with our eyes and our minds open, rather than stumble into the future with our eyes closed.

Forecasting tools can be broadly categorized into two groups: quantitative techniques and qualitative techniques. Quantitative forecasts are most appropriate when historical data are available and when the relationships among key variables are expected to remain the same in the future. *Linear regression*, for example, is based on the assumption that the future will be just like the past—which, of course, it never is. As historical relationships become less stable, quantitative forecasts become less accurate. No forecast is perfect, and some forecasts are even wildly inaccurate. This fact accents the need for strategists to devote sufficient time and effort to study the underlying bases for published forecasts and to develop internal forecasts of their own. Key external opportunities and threats can be effectively identified only through good forecasts. Accurate forecasts can provide major competitive advantages for organizations. Forecasts are vital to the strategic-management process and to the success of organizations

An extrapolation technique *is* the extension of present trends into the future. It rests on the assumption that the world is reasonably consistent and changes slowly in the short run. Time-series methods are approaches of this type; they attempt to carry a series of historical events forward into the future. The basic problem with extrapolation is that a historical trend is based on a series of patterns or relationships among so many different variables that a change in any one can drastically alter the future direction of the trend. Brainstorming, expert opinion, are also very popular forecasting techniques. ***Brainstorming*** is a non-quantitative approach that requires simply the presence of people with some knowledge of the situation to be predicted. The basic ground rule is to propose ideas without first mentally screening them. No criticism is allowed. “Wild” ideas are encouraged. Ideas should build on previous ideas until a consensus is reached.84 This is a good technique to use with operating managers who have more faith in “gut feel” than in more quantitative number-crunching techniques. ***Expert opinion*** is a non quantitative technique in which experts in a particular area attempt to forecast likely developments. This type of forecast is based on the ability of a knowledgeable person(s) to construct probable future developments based on the interaction of key variables. One application, developed by the RAND Corporation, is the ***Delphi technique***, in which separated experts independently assess the likelihoods of specified events. These assessments are combined and sent back to each expert for fine tuning until agreement is reached. These assessments are most useful if they are shaped into several possible scenarios that allow decision makers to more fully understand their implication. Although very useful in the grasping of historic trends, statistical modeling, such as trend extrapolation, is based on historical data. As the patterns of relationships change, the accuracy of the forecast deteriorates. *Prediction markets* are a recent forecasting technique enabled by easy access to the Internet.

CHAPTER FOUR

INTERNAL ENVIRONMENT ASSESSMENT

4.1.The Nature of Internal Audit

Involvement in performing an internal strategic-management audit provides vehicle for understanding nature and effect of decisions in other functional business areas of the firm. All organizations have strengths and weaknesses in the functional areas of business. No enterprise is equally strong or weak in all areas. Internal strengths/weaknesses, coupled with external opportunities/threats and a clear statement of mission, provide the basis for establishing objectives and strategies. Objectives and strategies are established with the intention of capitalizing upon internal strengths and overcoming weaknesses. A firm's strengths that cannot be easily matched or imitated by competitors are called *distinctive competencies.* Building competitive advantages involves taking advantage of distinctive competencies. Four factors help a company builds and sustains competitive advantage: **superior efficiency, quality, innovation, and customer responsiveness**, each of these factors is the product of a company's distinctive competencies.

4.2. The Process of Performing an Internal Audit

The process of performing an *internal audit* closely parallels the process of performing an external audit. Representative Managers and employees from throughout the firm need to be involved in determining a firm's strengths and weaknesses. ***The internal audit requires gathering and assimilating information about the firm's management, marketing, finance/accounting, production/operations, research and development (R&D), and management information systems operations***. Compared to the external audit, the process of performing an internal audit provides more opportunity for participants to understand how their jobs, departments, and divisions fit into the whole organization. This is a great benefit because managers and employees perform better when they understand how their work affects other areas and activities of the firm. For example, when marketing and manufacturing managers jointly discuss issues related to internal strengths and weaknesses, they gain a better appreciation of issues, problems, concerns, and needs in all the functional areas. In organizations that do not use strategic management, marketing, finance, and manufacturing managers often do not interact with each other in significant ways. Performing an internal audit, thus, is an excellent vehicle or forum for improving the process of communication in the organization. ***Communication*** may be the most important word in management. Performing an internal audit requires **gathering,**

assimilating, and evaluating information about the firm's operations. Critical success factors, consisting of both strengths and weaknesses, can be identified and prioritized.

KEY INTERNAL FORCES

1. MANAGEMENT

The *functions of management* consist of five basic activities: planning, organizing, motivating, staffing, and controlling.

Planning- Planning consists of all those managerial activities related to preparing for the future. Specific tasks include forecasting, establishing objectives, devising strategies, developing policies, and setting goals. It is used in strategy formulation process.

Organizing- Organizing includes all those managerial activities that result in a structure of task and authority relationships. Specific areas include organizational design, job specialization, job descriptions, job specifications, span of the control, and unity of command, coordination, job design, and job analysis.

Motivating- Motivating involves efforts directed toward shaping human behavior. Specific topics include leadership, communication, work groups, behavior modification, and delegation of authority, job enrichment, job satisfaction, needs fulfillment, organizational change, employee morale, and managerial morale. **Strategy Implementation**

Staffing- Staffing activities are centered on personnel or human resource management. Included are wage and salary administration, employee benefits, interviewing, hiring, firing, training, management development, employee safety, affirmative action, equal employment opportunity, union relations, career development, personnel research, discipline policies, grievance procedures, and public relations. **Strategy Implementation.**

Controlling- Controlling refers to all those managerial activities directed toward ensuring that actual results are consistent with planned results. Key areas of concern include quality control, financial control, sales control, inventory control, and expense control, analysis of variances, rewards, and sanctions. **Strategy Evaluation**

Management Audit Checklist Questions

The checklists of questions provided below can help determine specific strengths and weaknesses in the functional area of business. An answer of ***NO*** to any question could indicate a potential weakness, although the strategic significance and implications of negative answers, of course, will vary by organization, industry, and severity of the weakness. Positive or ***YES*** answers to the checklist questions suggest potential areas of strength.

1. Does the firm use strategic-management concepts?
2. Are company objectives and goals measurable and well communicated?
3. Do managers at all hierarchical levels plan effectively?

4. Do managers delegate authority well?
5. Is the organization's structure appropriate?
6. Are job descriptions and job specifications clear?
7. Is employee morale high?
8. Are employee turnover and absenteeism low?
9. Are organizational reward and control mechanisms effective?

2. MARKETING

Marketing can be described as the process of defining, anticipating, creating, and fulfilling customers' needs and wants for products and services.

There are seven basic functions of marketing:

Understanding these functions helps strategists identify and evaluate marketing strengths and weaknesses.

1. **Customer analysis:** the examination and evaluation of consumer needs, desires, and wants—involves administering customer surveys, analyzing consumer information, evaluating market positioning strategies, developing customer profiles, and determining optimal market segmentation strategies. The information generated by customer analysis can be essential in developing an effective mission statement. Customer profiles can reveal the demographic characteristics of an organization's customers. Buyers, sellers, distributors, salespeople, managers, wholesalers, retailers, suppliers, and creditors can all participate in gathering information to identify customers' needs and wants successfully. Successful organizations continually monitor present and potential customers' buying patterns.
2. **Selling Products/Services--:** Successful strategy implementation generally rests upon the ability of an organization to sell some product or service. Selling includes many marketing activities such as advertising, sales promotion, publicity, personal selling, sales force management, customer relations, and dealer relations. These activities are especially critical when a firm pursues a market penetration strategy. The effectiveness of various selling tools for consumer and industrial products varies. Personal selling is most important for industrial goods companies, and advertising is most important for consumer goods companies. Determining organizational strengths and weaknesses in the selling function of marketing is an important part of performing an internal strategic management audit. With regard to advertising products and services on the internet, a new trend is to base advertising rates exclusively on sale rates. This new accountability contrasts sharply with traditional broadcast and print advertising that bases rates on the number of persons expected to see a given advertisement. The new cost per- sale online advertising rates are possible because any Web site can monitor which user clicks on which advertisement and then can record whether that

consumer actually buys the product. If there are no sales, then the advertisement is free. The most popular type of Internet advertisement is the banner.

3. **Product and Service Planning:** includes activities such as test marketing; product and brand positioning; devising warranties; packaging; determining product options, product features, product style, and product quality; deleting old products; and providing for customer service. Product and service planning is particularly important when a company is pursuing product development or diversification. One of the most effective product and service planning techniques is test marketing. Test markets allow an organization to test alternative marketing plans and to forecast future sales of new products. In conducting a test market project, an organization must decide how many cities to include, which cities to include, how long to run the test, what information to collect during the test, and what action to take after the test has been completed. Test marketing is used more frequently by consumer goods companies than by industrial goods companies. Test marketing can allow an organization to avoid substantial losses by revealing weak products and ineffective marketing approaches before large-scale production begins.
4. **Pricing:** Sometimes an organization will pursue a forward integration strategy primarily to gain better control over prices charged to consumers. Governments can impose constraints on price fixing, price discrimination, minimum prices, unit pricing, price advertising, and price controls. Competing organizations must be careful not to coordinate discounts, credit terms, or condition of sale; not to discuss prices, markups, and costs at trade association meetings; and not to arrange to issue new price lists on the same date, to rotate low bids on contracts, or to uniformly restrict production to maintain high prices. Strategists should view price from both a short-run and a long-run perspective, because competitors can copy price changes with relative ease. Often a dominant firm will aggressively match all price cuts by competitors. Five major stakeholders affect *pricing* decisions: Consumers, Governments, Suppliers, Distributors, and Competitors.
5. **Distribution:** includes warehousing, distribution channels, distribution coverage, retail site locations, sales territories, inventory levels and location, transportation carriers, wholesaling, and retailing. Most producers today do not sell their goods directly to consumers. Various marketing entities act as intermediaries; they bear a variety of names such as wholesalers, retailers, brokers, facilitators, agents, middlemen, vendors, or simply distributors. Distribution becomes especially important when a firm is striving to implement a market development or forward integration strategy. Some of the most complex and challenging decisions facing a firm concern product distribution. Strengths and weaknesses of each channel alternative should be determined according to economic, control, and adaptive

criteria. Organizations should consider the costs and benefits of various wholesaling and retailing options. They must consider the need to motivate and control channel of member and the need to adopt to change in the future. Once a marketing channel is chosen, an organization usually must adhere to it for an extended period of time.

6. **Marketing Research:** is the systematic gathering, recording, and analyzing of data about problems relating to the marketing of goods and services. Marketing research can uncover critical strengths and weaknesses, and marketing researchers employ numerous scales, instruments, procedures, concepts, and techniques to gather information. Marketing research activities support all of the major business functions of an organization. Organizations that possess excellent marketing research skills have a definite strength in pursuing generic strategies.
7. **Opportunity Analysis:** The eighth function of marketing is *opportunity analysis,* which involves assessing the costs, benefits, and risks associated with marketing decisions. Three steps are required to perform a *cost/benefit analysis:*
   - Compute the total costs associated with a decision,
   - Estimate the total benefits from the decision, and
   - Compare the total costs with the total benefits.

As expected benefits exceed total costs, an opportunity becomes more attractive. Sometimes the variables included in a cost/benefit analysis cannot be quantified or even measured, but usually reasonable estimates can be made to allow the analysis to be performed. One key factor to be considered is risk. Cost/benefit analyses should also be performed when a company is evaluating alternative ways to be socially responsible.

Marketing Audit Checklist of Questions

Similarly as provided earlier for management, the following questions about marketing are pertinent:

1. Are markets segmented effectively?
2. Is the organization positioned well among competitors?
3. Has the firm's market share been increasing?
4. Are present channels of distribution reliable and cost-effective?
5. Does the firm have an effective sales organization?
6. Does the firm conduct market research?
7. Are product quality and customer service good?
8. Are the firm's products and services priced appropriately?
9. Does the firm have an effective promotion, advertising, and publicity strategy?
10. Are marketing planning and budgeting effective?

11. Do the firm's marketing managers have adequate experience and training?

3. ACCOUNTING AND FINANCE

Objectives: Financial condition is often considered the single best measure of a firm's competitive position and overall attractiveness to investors. Determining an organization's financial strengths and weaknesses is essential to formulating strategies effectively. A firm's liquidity, leverage, working capital, profitability, asset utilization, cash flow, and equity can eliminate some strategies as being feasible alternatives. Financial factors often alter existing strategies and change implementation plans. After reading this lecture, you will be able to know that what are the basics types of ratios and who business measure its financial strength using these ratios analysis.

- Finance/Accounting Functions
- Determining financial strengths and weaknesses key to strategy formulation
- Investment decision (Capital budgeting)
- Financing decision
- Dividend decision

According to James Van Horne, the functions of finance/accounting comprise three decisions: the investment decision, the financing decision, and the dividend decision.

Financial ratio analysis is the most widely used method for determining an organization's strengths and weaknesses in the investment, financing, and dividend areas. Because, the functional areas of business are so closely related, financial ratios can signal strengths or weaknesses in management, marketing, production, research and development, and computer information systems activities.

The **investment decision**, also called **capital budgeting**, is the allocation and reallocation of capital and resources to projects, products, assets, and divisions of an organization. Once strategies are formulated, capital budgeting decisions are required to implement strategies successfully. The ***financing decision*** concerns determining the best capital structure for the firm and includes examining various methods by which the firm can raise capital (for example, by issuing stock, increasing debt, selling assets, or using a combination of these approaches). The financing decision must consider both short-term and long-term needs for working capital. Two key financial ratios that indicate whether a firm's financing decisions have been effective are the **debt-to-equity ratio and the debt-to-total-assets ratio.**

Dividend decisions; concern issues such as the percentage of earnings paid to stockholders, the stability of dividends paid over time, and the repurchase or issuance of stock. Dividend decisions determine the amount of funds that are retained in a firm compared to the amount paid out to stockholders. Three financial ratios that are helpful in evaluating a firm's dividend decisions are the **earnings-per share ratio, the dividends-per-share ratio, and the price-earnings ratio**. The benefits of paying dividends to investors must be balanced against the benefits of retaining funds internally, and there is no set formula on how to balance this trade-off. For the reasons listed here, dividends are sometimes paid out even when funds could be better reinvested in the business or when the firm has to obtain outside sources of capital:

Basic Types of Financial Ratios

Financial ratios are computed from an organization's income statement and balance sheet. Computing financial ratios is like taking a picture because the results reflect a situation at just one point in time. Comparing ratios over time and to industry averages is more likely to result in meaningful statistics that can be used to identify and evaluate strengths and weaknesses.

Key financial ratios can be classified into the following five types:

- ❖ **Liquidity ratios;** measure a firm's ability to meet maturing short-term obligations. It includes:

  Current ratio

  Quick (or acid-test) ratio

- ❖ **Leverage ratios** measure the extent to which a firm has been financed by debt.
  - ✓ Debt-to-total-assets ratio
  - ✓ Debt-to-equity ratio
  - ✓ Long-term debt-to-equity ratio
  - ✓ Times-interest-earned (or coverage) ratio
- ❖ **Activity ratios** measure how effectively a firm is using its resources.
  - ✓ Inventory-turn over
  - ✓ Fixed assets turnover
  - ✓ Total assets turnover
  - ✓ Accounts receivable turnover
  - ✓ Average collection period
- ❖ **Profitability ratios** measure management's overall effectiveness as shown by the returns generated on sales and investment.
  - ✓ Gross profit margin
  - ✓ Operating profit margin
  - ✓ Net profit margin
  - ✓ Return on total assets (ROA)
  - ✓ Return on stockholders' equity (ROE)
  - ✓ Earnings per share
  - ✓ Price-earnings ratio
- ❖ **Growth ratios** measure the firm's ability to maintain its economic position in the growth of the economy and industry.
  - ✓ Sales
  - ✓ Net income
  - ✓ Earnings per share
  - ✓ Dividends per share

Finance/Accounting Audit Checklist of Questions

Similarly as provided earlier, the following finance/accounting questions should be examined:

1. Where is the firm financially strong and weak as indicated by financial ratio analyses?
2. Can the firm raise needed short-term capital?
3. Can the firm raise needed long-term capital through debt and/or equity?
4. Does the firm have sufficient working capital?
5. Are capital budgeting procedures effective?
6. Are dividend payout policies reasonable?
7. Does the firm have good relations with its investors and stockholders?
8. Are the firm's financial managers experienced and well trained?

4. PRODUCTION/OPERATIONS

The *production/operations function* of a business consists of all those activities that transform inputs into goods and services. Production/operations management deals with inputs, transformations, and outputs that vary across industries and markets. A manufacturing operation transforms or converts inputs such as raw materials, labor, capital, machines, and facilities into finished goods and services. Production/operations management comprises five functions or decision areas: process, capacity, inventory, workforce, and quality.

The Basic Functions of Production Management

Function Description of production management includes;

Process-Process decisions concern the design of the physical production system. Specific decisions include choice of technology, facility layout, process flow analysis, facility location, line balancing, process control, and transportation analysis.

Capacity- Capacity decisions concern determination of optimal output levels for the organization—not too much and not too little. Specific decisions include forecasting, facilities planning, aggregate planning, scheduling, capacity planning, and queuing analysis.

Inventory- Inventory decisions involve managing the level of raw materials, work in process, and finished goods. Specific decisions include what to order, when to order, how much to order, and materials handling.

Workforce- Workforce decisions are concerned with managing the skilled, unskilled, clerical, and managerial employees. Specific decisions include job design, work measurement, job enrichment, work standards, and motivation techniques.

Quality- Quality decisions are aimed at ensuring that high-quality goods and services are produced. Specific decisions include quality control, sampling, testing, quality assurance, and cost control.

Production/operations activities often represent the largest part of an organization's human and capital assets. In most industries, the major costs of producing a product or service are incurred within operations, so production/operations can have great value as a competitive weapon in a company's overall strategy. Strengths and weaknesses in the five functions of production can mean the success or failure of an enterprise. Many production/operations managers are finding that cross-training of employees can help their firms respond to changing markets faster. Cross-training of workers can increase efficiency, quality, productivity, and job satisfaction. There is much reason for concern that many organizations have not taken sufficient account of the capabilities and limitations of the production/operations function in formulating strategies. Given today's decision-making environment with shortages, inflation, technological booms, and government intervention, a company's production/operations capabilities and policies may not be able to fulfill the demands dictated by strategies. In fact, they may dictate corporate strategies. It is hard to imagine that an organization can formulate strategies today without first considering the constraints and limitations imposed by its existing production/operations structure.

Production/operation audit checklist Questions

Questions such as the following should be examined:

1. Are suppliers of raw materials, parts, and subassemblies reliable and reasonable?
2. Are facilities, equipment, machinery, and offices in good condition?
3. Are inventory-control policies and procedures effective?
4. Are quality-control policies and procedures effective?
5. Are facilities, resources, and markets strategically located?
6. Does the firm have technological competencies?

5. RESEARCH AND DEVELOPMENT

The fifth major area of internal operations that should be examined for specific strengths and weaknesses is research and development (R&D). Many firms today conduct no R&D, and yet many other companies depend on successful R&D activities for survival. Firms pursuing a product development strategy especially need to have a strong R&D orientation. The purpose of research and development are as follows: Development of new products before competition; improving product quality; and improving manufacturing processes to reduce costs. Organizations invest in R&D because they believe that such investment will lead to superior product or services and give them competitive advantages. Research and development expenditures are directed at developing new products before competitors do, improving product quality, or improving manufacturing processes to reduce costs.

The best-managed firms today seek to organize R&D activities in a way that breaks the isolation of R&D from the rest of the company and promotes a spirit of partnership between R&D managers and other managers in the firm. R&D decisions and plans must be integrated and coordinated across. The strategic-management process facilitates this new cross-functional approach to managing the R&D function.

Internal and external R&D

Cost distributions among R&D activities vary by company and industry, but total R&D costs generally do not exceed manufacturing and marketing start-up costs. Four approaches to determining R&D budget allocations commonly are used:

1. Financing as many project proposals as possible,
2. Using a percentage-of-sales method,
3. Budgeting about the same amount that competitors spend for R&D, or
4. Deciding how many successful new products are needed and working backward to estimate the required R&D investment.

❖ R&D in organizations can take two basic forms:
  - ✓ **Internal R&D**, in which an organization operates its own R&D department, and/or
  - ✓ **Contract R&D**, in which a firm hires independent researchers or independent agencies to develop specific products.

Many companies use both approaches to develop new products. A widely used approach for obtaining outside R&D assistance is to pursue a joint venture with another firm. R&D strengths (capabilities) and weaknesses (limitations) play a major role in strategy formulation and strategy implementation. The focus of R&D efforts can vary greatly depending on a firm's competitive strategy. Some corporations attempt to be market leaders and innovators of new products, while others are satisfied to be market followers and developers of currently available products. The basic skills required to support these strategies will vary, depending on whether R&D becomes the driving force behind competitive strategy. In cases where new product introduction is the driving force for strategy, R&D activities must be extensive. The R&D unit must then be able to advance scientific and technological knowledge, exploit that knowledge, and manage the risks associated with ideas, products, services, and production requirements.

Research and Development Audit Checklist of Questions

Questions such as the follows should be asked in performing an R&D audit:

1. Does the firm have R&D facilities? Are they adequate?
2. If outside R&D firms are used, are they cost-effective?
3. Are the organization's R&D personnel well qualified?
4. Are R&D resources allocated effectively?
5. Are management information and computer systems adequate?
6. Is communication between R&D and other organizational units effective?
7. Are present products technologically competitive?

6. MANAGEMENT INFORMATION SYSTEMS (MIS)

MIS is a general name for the academic discipline covering the application of information technology to business problems. As an area of study it is also referred to as information technology management. The study of information systems is usually a commerce and business administration discipline, and frequently involves software engineering, but also distinguishes itself by concentrating on the integration of computer Business Policy and Strategic Management systems with the aims of the organization. The area of study should not be confused with computer science which is more theoretical in nature and deals mainly with software creation, or computer engineering, which focuses more on the design of computer hardware. IT service management is a practitioner-focused discipline centering on the same general domain. In business, information systems support business processes and operations, decision-making, and competitive strategies.

The functional support role

Information systems support business processes and operations by:

- ✓ Recording and storing accounting records including sales data, purchase data, investment data, and payroll data. Process such records into financial statements such as income statements, balance sheets, ledgers, and management reports, etc.
- ✓ Recording and storing inventory data, work in process data, equipment repair and maintenance data, supply chain data, and other production/operations records Processing these operations records into production schedules, production controllers, inventory systems, and production monitoring systems
- ✓ Recording and storing such human resource records as personnel data, salary data, and employment histories,
- ✓ Recording and storing market data, customer profiles, and customer purchase histories, marketing research data, advertising data, and other marketing records Processing these marketing records into advertising elasticity reports, marketing plans, and sales activity reports
- ✓ Recording and storing business intelligence data, competitor analysis data, industry data, corporate objectives, and other strategic management records processing these strategic management records into industry trends reports, market share reports, mission statements, and portfolio models. The bottom line is that the information systems use all of the above to implement, control, and monitor plans, strategies, tactics, new products, new business models or new business ventures.

The decision support role

The business decision-making support function goes one step further. It becomes an integral part -- even a vital part of decision-making. It allows users to ask very powerful "What if…?" questions: What if we increase the price by 5%? What if we increase price by 10%? What if we decrease price by 5%? What if we increase price by 10% now, then decrease it by 5% in three months? It also allows users to deal with contingencies: If inflation increases by 5% (instead of 2% as we are assuming), then what do we do? What do we do if we are faced with a strike or a new competitive threat? An organization succeeds or fails based on the quality of its decisions. The enhanced ability to explore "what if" a question is central to analyzing the likely results of possible decisions and choosing those most likely to shape the future as desired. "Business decision-making support function" is a phrase likely to quicken the pulse of no one but an accountant, but, in fact, it is all about turning wonderful dreams into solid realities.

Management Information Systems Audit

1. Do all managers in the firm use the information system to make decisions?
2. Is there a chief information officer or director of information systems position in the firm?
3. Are data in the information system updated regularly?
4. Do managers from all functional areas of the firm contribute input to the information system?
5. Are there effective passwords for entry into the firm‘s information system?
6. Are strategists of the firm familiar with the information systems of rival firms?
7. Is the information system user-friendly?
8. Do all users of the information system understand the competitive advantages that information can provide firms?
9. Are computer training workshops provided for users?
10. Is the firm‘s system being improved?

Relationships among the functional areas of business:

- Strategic management is a highly interactive process that requires an effective coordination among the ***units*** of an organ
- Participation of managers & employees from ***d/t depts. and division*** of an organ in internal SM audit, can result in:
  - ✓ Understanding the nature and how major functions affect one another
  - ✓ Effective strategy formulation, implementation & evaluation
  - ✓ Successful coordination and unity of direction in realizing common destination

- ✓ Better effects when an organ's size, diversity and geographic dispersion increases
- ➢ Failure to recognize r/ships among the functional areas of a business can significantly deteriorates the SM of the business
- ➢ ***Since organizational culture*** considerably affects business decisions, it should be evaluated during an internal SM audit.

In the previous chapter we discussed how to use the tools of industry and competitive analysis to strategically assess a company's external environment. In this chapter we discuss the techniques of evaluating a company's resource capabilities, relative cost position, and competitive strength versus rivals. Company situation analysis prepares the groundwork for matching the company's strategy both to its external market circumstances and to its internal resources and competitive capabilities. The spotlight of company situation analysis is trained on the following questions:

1. What are the company's resource strengths and weaknesses
2. Are the company's prices and costs competitive?
3. How strong is the company's competitive position relative to its rivals?

1. **What are the company's resource strengths and weaknesses?** Sizing up a firm's resource strengths and weaknesses and its external opportunities and threats, commonly known as *SWOT* analysis, provides a good overview of whether a firm's business position is fundamentally healthy or unhealthy.

SWOT analysis is grounded in the basic principle that *strategy making efforts must aim at producing a good fit between a company's resource capability* (as reflected by its balance of resource strengths and weaknesses) *and its external situation* (as reflected by industry and competitive conditions, the company's own market opportunities, and specific external threats to the company's profitability and market standing).

As the external environment related to opportunities and threats is somehow covered earlier, the focus of this discussion will be on the company's resource strengths and weaknesses.

Identifying Company Strengths and Resource Capabilities

Strength is something a company is good at doing or a characteristic that gives it enhanced competitiveness. Strength can take any of several forms:

- ➢ **A *skill or important expertise*:**
    - ✓ low cost manufacturing capabilities
    - ✓ strong e-commerce expertise

- ✓ Technological know-how
- ✓ a proven track record in defect free manufacture
- ✓ expertise in providing consistently good customer service
- ✓ Excellent mass merchandising skills or unique advertising and promotional talents.

➢ ***Valuable physical assets:***

- ✓ State-of-the-art plants and equipment
- ✓ Attractive real estate locations
- ✓ worldwide distribution facilities
- ✓ ownership of valuable natural resource deposits
- ✓ Cutting edge computer networks and information systems or sizable amounts of cash and marketable securities.

➢ ***Valuable human assets:***

- ✓ An experienced and capable work force
- ✓ motivated and energetic employees
- ✓ cutting edge knowledge and intellectual capital
- ✓ Astute entrepreneurship and managerial know-how or the collective learning embedded in the organization and built up over time.

➢ ***Valuable organizational assets:***

- ✓ proven quality control systems
- ✓ proprietary technology
- ✓ key patents
- ✓ a base of loyal customers
- ✓ a strong balance sheet and credit rating
- ✓ cutting edge supply chain management systems
- ✓ a well-functioning company intranet and e-commerce systems for accessing and exchanging information with suppliers and key customers
- ✓ computer assisted design and manufacturing systems
- ✓ Systems for conducting business on the Internet, or a comprehensive list of customers' e-mail addresses.

➢ ***Valuable intangible assets:***

- ✓ Brand-name image
- ✓ company reputation
- ✓ buyer good will
- ✓ a motivated and energized workforce

- ***Competitive capabilities:***
  - ✓ short development times in bringing new products to market
  - ✓ strong partnerships with key suppliers
  - ✓ an R&D organization with the ability to keep the company's pipeline full of innovative new products
  - ✓ a high degree of organizational agility in responding to shifting market conditions and emerging opportunities
  - ✓ A cadre of highly trained customer service representatives or state-of-art systems for doing business via the Internet
- ***An achievement or attribute that puts the company in a position of market advantage :***
  - ✓ Low overall costs
  - ✓ a wide product selection
  - ✓ market leadership
  - ✓ strong name recognition
  - ✓ A superior product
  - ✓ state-of-the-art e-commerce technologies and practices, or exceptional customer services
- ***Alliances or cooperative ventures:***
  - Fruitful collaborative partnerships with suppliers and marketing allies that enhance the company's own competitiveness.

The calibre of its resources and its ability to mobilize them in a manner calculated to result in competitive advantage are the biggest determinants of how well the company will be able to perform in light of the prevailing industry and competitive conditions as shown in the figure below:

Identifying Company Weaknesses and Resource Deficiencies

A *weakness* is something a company lacks or does poorly (in comparison to others) or a condition that puts it at a disadvantage. A company's internal weaknesses can relate to

1. Deficiencies in competitively important skills or expertise or intellectual capital of one kind or another
2. A lack of competitively important physical, organizational, or intangible assets, or
3. Missing or weak competitive capabilities in key areas

Internal weaknesses are thus shortcomings in a company's complement of resources.

Identifying Company Competencies

A ***company competence*** is nearly always the product of experience, representing an accumulation of learning over time and the build up over time of real *proficiency*. Competence has to be consciously built and developed – they do not just happen. For a particular company resource to qualify as the basis for sustainable competitive advantage, ***it must pass for tests of competitive value:***

- ✓ ***Is the resource hard to copy?*** The more difficult and more expensive it is to imitate a resource, the greater its potential competitive value.
- ✓ ***How long does the resource last****?* The longer a resource lasts, the greater its value. Some resources lose their value quickly because of the rapid speeds with which technologies or industry conditions are moving.
- ✓ ***Is the resource really competitively superior?*** Companies have no guard against pride fully believing that their core competences are distinctive competences or that their brand name is more powerful than the brand names of their rivals. Who can really say whether Coca-Cola's consumer marketing skills are better than Pepsi-Cola's or whether Mercedes-Benz's brand name is more powerful than BMW's or Lexus's?
- ✓ ***Can the resource be trampled by the different resources/capabilities of rivals?***

2. Are the company's prices and costs competitive?

- Strategic cost analysis and value chains
- Benchmarking the costs of key activities
- Strategic options for achieving cost competitiveness

3. How strong is the company's competitive position?

Using the tools of value chain, strategic cost analysis, and benchmarking to determine a company's cost competitiveness is necessary but not sufficient. A more broad ranging assessment needs to be made of a company's competitive position and competitive strength.

Table the signs of strength and weakness in a company's competitive position

Signs of Competitive Strength	**Signs of Competitive Weakness**
✓ Important resource strengths, core competencies , and competitive capabilities ✓ A distinctive competence in a competitively important value chain activity ✓ Strong market share (or a leading market share)	✓ Confronted with competitive disadvantage ✓ Losing ground to rival firms with stronger positions in global and /e-commerce markets ✓ Eroding market share and below average growth in revenues ✓ Short in financial resources to pursue new

✓ A pace setting or distinctive strategy that is hard for rivals to copy or match ✓ Ahead of rivals in expanding into global markets and/or in building an e-commerce presence ✓ A better known brand name reputation than rivals ✓ Growing customer base and customer loyalty ✓ Well positioned in attractive market segments ✓ Strongly differentiated products ✓ Cost advantages ✓ Above-average profit margins ✓ Above-average technological and innovation capability ✓ A creative, entrepreneurially alert management ✓ Ample financial resources	opportunities ✓ Weaker brand name recognition than rivals and/or a slipping reputation with customers ✓ Trailing/lagging in product development and product innovation capability ✓ Weak in areas where there is the most market potential – foreign markets, e-commerce ✓ A higher cost producer ✓ Too small to be a major factor in the market place ✓ Not in good position to deal with emerging threats ✓ Subpar product quality ✓ Lacking skills, resources, and competitive capabilities in key areas ✓ Weaker distribution capability than rivals.

a. **Value Chain Analysis (VCA)**

Value chain analysis (VCA) refers to the process whereby a firm determines the costs associated with organizational activities from purchasing raw materials to manufacturing product(s) to marketing those products. VCA aims to identify where low-cost advantages or disadvantages exist anywhere along the value chain from raw material to customer service activities. VCA can enable a firm to better identify its own strengths and weaknesses, especially as compared to competitors' value chain analyses and their own data examined over time. Substantial judgment may be required in performing a VCA because different items along the value chain may impact other items positively or negatively, so there exist complex interrelationships.

Conducting a VCA is supportive of the RBV's examination of a firm's assets and capabilities as sources of distinctive competence. When a major competitor or new market entrant offers products or services at very low prices, this may be because that firm has substantially lower value chain costs or perhaps the rival firm is just waging a desperate attempt to gain sales or market share. Thus value chain analysis can be critically important for a firm in monitoring whether its prices and costs are competitive.

The combined costs of all the various activities in a company's value chain define the firm's cost of doing business. Firms should determine where cost advantages and disadvantages in their value chain occur *relative to the value chain of rival firms.*

Benchmarking

Benchmarking is an analytical tool used to determine whether a firm's value chain activities are competitive compared to rivals and thus conducive to winning in the marketplace. Benchmarking entails measuring costs of value chain activities across an industry to determine "best practices" among competing firms for the purpose of duplicating or improving upon those best practices. Benchmarking enables a firm to take action to improve its competitiveness by identifying (and improving upon) value chain activities where rival firms have comparative advantages in cost, service, reputation, or operation.

The hardest part of benchmarking can be gaining access to other firms' value chain activities with associated costs. Typical sources of benchmarking information, however, include published reports, trade publications, suppliers, distributors, customers, partners, creditors, shareholders, lobbyists, and willing rival firms. Some rival firms share benchmarking data.

An Example Value Chain for a Typical Manufacturing Firm

- Production cost
- Supplier cost
- Distribution cost
- Sales and manufacturing cost
- Customer service cost
- Management cost

Evaluation (IFE) Matrix. This strategy-formulation tool summarizes and evaluates the major **strengths and weaknesses** in the functional areas of a business, and it also provides a basis for identifying and evaluating relationships among those areas. Intuitive judgments are required in developing an IFE Matrix, so the appearance of a scientific approach should not be interpreted to mean this is an all powerful technique. A thorough understanding of the factors included is more important than the actual numbers. Similar to the EFE Matrix and Competitive Profile Matrix, an IFE Matrix can be developed in five steps:

1. List key internal factors as identified in the internal-audit process. Use a total of from 10 to 20 internal factors, including both strengths and weaknesses. Always list strengths first and then weaknesses. Be as specific as possible, using percentages, ratios, and comparative numbers.
2. Assign a weight (either in %age or in numerical value) that ranges from 0.0 (not important) to 1.0 (all-important) to each factor. The weight assigned to a given factor indicates the relative importance of the factor to being successful in the firm's industry. Regardless of whether a key factor is an internal strength or weakness, factors considered to have the greatest effect on organizational performance should be assigned the highest weights. The sum of all weights must equal 1.0.
3. Assign a 1-to-4 rating (rating means what is the capability of the firm to meet its strength and weaknesses) to each factor to indicate whether that factor represents a major weakness (rating 1), a minor weakness (rating 2), a minor strength (rating 3), or a major strength (rating 4). Note: that strengths must receive a 4 (for average strength) or 3 (for normal strength) rating and weaknesses must receive a 1 (for normal weakness) or 2 rating. Ratings are, thus, company based, whereas the weights in Step 2 are industry based.
4. Multiply each factor's weight by its rating to determine a weighted score for each variable.
5. Sum the weighted scores for each variable to determine the total weighted score for the organization. Highest possible weighted score for the organization is 4.0; the lowest, 1.0. Average = 2.5. Regardless of how many factors are included in an IFE Matrix, the total weighted score can range from a low of 1.0 to a high of 4.0, with the average score being 2.5. Total weighted scores well below

Business Policy and Strategic Management 2.5 characterize organizations that are weak internally, whereas scores significantly above 2.5 indicate a strong internal position.

The number of factors has no effect upon the range of total weighted scores because the weights always sum to 1.0. When a key internal factor is both strength and a weakness, the factor should be included twice in the IFE Matrix, and a weight and rating should be assigned to each statement.

An example of an IFE Matrix for retail computer store is provided in the Table below. Note that the firm's major strengths are its size, occupancy rates, property, and long-range planning as indicated by the rating of 4. The major weaknesses are locations and recent joint venture. The total weighted score of 2.75 indicates that the firm is above average in its overall internal strength.

A **Sample Internal Factor Evaluation Matrix a Retail Computer Store**

Internal Strengths	**Weight**	**Rating**	**Weighted Score**
1. Inventory turnover increased from 5.8 to 6.7	.05	3	.15
2. Average customer purchase increased from $97 to $128	.07	4	.28
3. Employee morale is excellent	.10	3	.30
4. In-store promotions resulted in 20 percent increase in sales	.05	3	.15
5. Newspaper advertising expenditures increased 10 percent	.02	3	.06
Revenues from repair/service segment of store up 16 percent	.15	3	.45
In-store technical support personnel have MIS college degrees	.05	4	.20
Store's debt-to-total assets ratio declined to 34 percent	.03	3	.09
Revenues per employee up 19 percent	.02	3	.06
Internal Weaknesses			
1. Revenues from software segment of store down 12 percent	.10	2	.05
2. Location of store negatively impacted by new Highway 34	.15	2	.10
3. Carpet and paint in store somewhat in disrepair	.02	1	.10
4. Bathroom in store needs refurbishing	.02	1	.10
5. Revenues from businesses down 8 percent	.04	1	.10
Store has no Web site	.05	2	.10
Supplier on-time delivery increased to 2.4 days	.03	1	.03
Often customers have to wait to check out	.05	1	.05
TOTAL	1.00		2.5

Retail computer store has a total weighted score of 2.5indicating that the firm is above average in its overall internal strength

CHAPTER FIVE

STRATEGY FORMULATION: STRATEGY ANALYSIS AND CHOICE

5.1 THE NATURE OF STRATEGY ANALYSIS AND CHOICE

Strategy formulation includes developing a vision and mission, identifying an organization's external opportunities and threats, determining internal strengths and weaknesses, establishing long-term objectives, generating alternative strategies, and choosing particular strategies to pursue. Strategy-formulation issues include deciding what new businesses to enter, what businesses to abandon, how to allocate resources, whether to expand operations or diversify, whether to enter international markets, whether to merge or form a joint venture, and how to avoid a hostile takeover. Strategy analysis and choice:

- ✓ Focuses on generating and evaluating alternative strategies, as well as selecting strategies to pursue.
- ✓ Seek to determine alternative courses of action that could best enable the firm to achieve its mission and objectives.

N.B. The firm's present strategies, objectives, and mission, coupled with the external and internal audit information, provide a basis for generating and evaluating feasible alternative strategies. Participation in generating alternative strategies should be as broad as possible.

❖ **The Process of Generating and Selecting Strategies**

1. Identifying and evaluating alternative strategies should begin with involvement of many **participants** (managers and employees) who earlier assembled the organizational vision and mission statements, performed the external audit, and conducted the internal audit.
2. Participants then crystallize in their own minds particular strategies that they believe could benefit the firm most and proposed accordingly.
3. Alternative strategies proposed by participants then should be considered and discussed in a meeting or series of meetings. Proposed strategies should be listed in writing.
4. The strategies should be ranked in order of attractiveness by all participants, with 1 = should not be implemented, 2 = possibly should be implemented, 3 = probably should be implemented, and 4 = definitely should be implemented.

N.B. The above process will result in a prioritized list of best strategies that reflects the collective wisdom of the group.

5.2. TYPES OF STRATEGY

Strategic choices fall into three large categories namely **corporate**, **business**, and **functional** level strategy.

A. CORPORATE LEVEL STRATEGY

- ✓ It is also known as grand/ master strategy which intended to provide basic direction for strategic actions. Thus, they are seen as the basis of coordinated and sustained efforts directed toward achieving long term business objectives.
- ✓ Grand strategy is about the basic direction of the firm as a whole.
- ✓ In the case of the small firm it could mean the adoption of courses of action that would yield a better profit for the firm.
- ✓ The case of the large firm the corporate level strategy is about managing the various businesses to maximize their contribution to the overall corporate objectives.
- ✓ Corporate strategy is a firm's theory of how to gain competitive advantage by operating in several businesses simultaneously.
- ✓ A grand strategy at corporate level is an action taken to gain a competitive advantage through the selection & management of a mix of businesses competing in several industries or product markets
- ✓ They are three type of corporate strategy namely **growth**, **stability** and **defensive** strategy.

1. Growth /Expansion Strategy

- ✓ Involves the attainment of specific growth objectives by increasing the level of an organization's operations.
- ✓ The expansion grand strategy is followed when an organization aims at high growth by substantially broadening the scope of one or more of its businesses in terms of their respective customer groups, customer functions and alternative technologies-single or jointly-in order to improve its overall performance.
- ✓ A growth strategy is one that an enterprise pursues when it increases its level of objectives upward in significant increment, much higher than an exploration of its past achievement level. The most frequent increase indicating a growth strategy is to raise the market share and /or sales objectives upward significantly.
- ✓ In the growth strategy, the rate of growth is much faster than the past years owing to additional operational facilities in the organization.

- ✓ Typical growth objectives for businesses are increases in sales revenues, profits, & other performance measures (return on asset, return on investment & return on owner's equity).
- ✓ Growth objectives for not-for-profits are increasing clients served or patrons attracted, broadening the geographic area, & increasing programs offered.
- ✓ The following are the variants of expansion strategy:
  - Expansion through concentric expansion,
  - Expansion through integration,
  - Expansion through diversification, &
  - Expansion through internationalization.

A. Concentric Expansion

- ✓ The first route of growth is to expand the present line of business and looks for ways to meet its growth objectives through increasing its level of operation in existing business.
- ✓ Concentration strategy will be appropriate when the company concentrates on the current business.
- ✓ Concentration strategy is the most common grand strategy.

Concentration Options

		Product	
		Current	***New***
Market/Customer	***Current***	Product-Market Exploitation (market penetration)	Product Development
	New	Market Development	Product/ Market Diversification*

* Not a concentration option

Market Penetration

- The organization tries to capture market share in the existing product and aims at expanding its business at a rate higher than the industry growth.
- The firm directs its resources to the profitable growth of a single product, in a single market, with a single technology.
- In each case, the objective is to expand organization's present business.
- In general, firms that use this strategy gain competitive advantage in production skill, marketing know-how & reputation in the market place

- In fact, it refers to marketing present products with only cosmetic modifications
- Thus, penetration focuses on:
  - ✓ Increasing present customers' rate of usage
  - ✓ Attracting competitors' customers through price cuts
  - ✓ Attracting non-users through advertising, price incentives etc.

Four Guidelines When <u>Market Penetration</u> May Be an Especially Effective Strategy

- Current markets not saturated/unsaturated/;
- Usage rate of present customers can be increased significantly;
- Market shares of competitors declining while total industry sales increasing; &
- Increased economies of scale provide major competitive advantages.

Market Development

- Market development is selling present products in new markets – additional regional, national & international expansions
- Attracting other market segments through:
  - ✓ Developing product versions to appeal to other segments
  - ✓ Entering other channels of distribution
  - ✓ Advertising in other media

Six Guidelines When <u>Market Development</u> May Be an Especially Effective Strategy

- New channels of distribution that are reliable, inexpensive, and good quality;
- Firm is very successful at what it does;
- Untapped or unsaturated markets;
- Capital and human resources necessary to manage expanded operations is available;
- Excess production capacity; &
- Basic industry rapidly becoming global.

Product Development

- **Product development:** is developing new products for present markets. This involves:
  - ✓ Developing new product features:

        - Modifying (change color, form, shape, etc.)
        - Magnify & minify
        - Rearrange (layout, patterns, etc.)
    - ✓ Developing additional models & sizes (product proliferation)
- Thus, it involves substantial modification of existing products or creation of new but related items that can be marketed to current customers through established channels.
- The idea is to attract satisfied customers to new products as a result of their positive experience with company's initial offering
- The product development strategy is often adopted either to prolong the life cycle of current products or to take advantage of favorable reputation & brand name.
- Examples of **product development** can be:
    - ✓ A revised edition of a college textbook
    - ✓ A new car style
    - ✓ A second formula of shampoo for oily air etc.

Five Guidelines When <u>Product Development</u> May Be an Especially Effective Strategy

- Products in maturity stage of life cycle;
- Competes in industry characterized by rapid technological developments;
- Major competitors offer better-quality products at comparable prices;
- Compete in high-growth industry; &
- Strong research and development capabilities.

B. Integration Strategies

- Integration strategy focuses on moving to different industry level, different product & technology but the basic market remains the same
- There are two types of integrative growths:
    - Vertical integration
    - Horizontal integration

Vertical Integration Strategy

- Exists when a firm produces its own inputs (backward integration) or owns channels of distribution of outputs (forward integration).

Benefits of Vertical Integration Strategy

- ✓ Allow a firm to gain control over:
  - Distributors (forward integration), &
  - Suppliers (backward integration).

Six Guidelines When <u>Forward Integration</u> May Be an Especially Effective Strategy

- Present distributors are expensive, unreliable, or incapable of meeting firm's needs;
- Availability of quality distributors is limited;
- When firm competes in an industry that is expected to grow markedly;
- Organization has both capital and human resources needed to manage new business of distribution;
- Advantages of stable production are high; &
- Present distributors have high profit margins.

Six Guidelines When <u>Backward Integration</u> May Be an Especially Effective Strategy

- When present suppliers are expensive, unreliable, or incapable of meeting needs;
- Number of suppliers is small and number of competitors large;
- High growth in industry sector;
- Firm has both capital and human resources to manage new business;
- Advantages of stable prices are important; &
- Present supplies have high profit margins.

Horizontal Integration Strategy

- Horizontal integration refers to the acquisition of one or more similar business operating at the same stage of the production-marketing chain.
- The acquiring firm is able to greatly expand its operations, thereby achieving greater market share, improving economies of scale, and increasing efficiency of capital usage.

Acquisitions, Mergers & Joint Ventures

- Acquisition, merger & joint venture are called means of diversification and integration, in fact in addition to internal development.
  - ✓ **Merger** is a strategy through which two or more firms agree to integrate their operations on a relatively co-equal basis. Therefore, in merger, a single new company will be established with new name, organizational structure, issuing new stock & other changes. However, the shareholders of the former firms will become shareholders of the new enlarged organization.

- ✓ **Acquisition** is a strategy through which one firm buys a controlling of 100% interest in another firm with the intent of making the acquired firm a subsidiary business within its portfolio. Therefore, an acquisition is a marriage of unequal partners with one organization buying the other. The shareholders of the acquired firm cease to be owners of the acquiring company – unless payment is effect in terms of shares
- ✓ **Joint Venture strategy:** takes place when two or more companies want to operate for success in a particular competitive environment. As an example, exploring petroleum requires the cooperation of several companies – constructing the Alaskan pipeline
  - Thus, joint venture cooperative arrangements could provide:
    - The necessary funds to build the pipeline
    - The processing & marketing capacity to profitably handle the oil flow
  - **Joint venture** arrangements result in joint ownership & especially it is an important strategy to enter international markets.
  - It is also important in transferring & enhancing the **skills**, **employment**, **growth** & **profits** of local businesses.

Four Guidelines When <u>Horizontal Integration</u> May Be an Especially Effective Strategy

- Firm can gain monopolistic characteristics without being challenged by federal government;
- Competes in growing industry;
- Increased economies of scale provide major competitive advantages; &
- Faltering due to lack of managerial expertise or need for particular resources.

N.B. A primary reason for pursuing forward, backward, and horizontal integration strategies is to gain cost leadership benefits.

C. Diversification

- It is the process of entry into a business which is new to an organization either market-wise or technology wise or both.
- Diversification strategy refers to an attempt to change the characteristics of the business through either of new products, markets & technology or all the three.
- Diversification growth strategy can be classified as follow:

Concentric/related Diversification

- It represents distinctive departure from firm's existing base of operation.
- It involves the addition of a business related to the firm in terms of technology, markets or products.

- The new business is selected possess a high degree of compatibility with the current businesses.
- It seeking growth with new market & product having meaningful synergy or fit with existing business (tapes into discs, ski sports into summer sporting).

Five Guidelines When Concentric Diversification May Be an Effective Strategy

- Competes in no- or slow-growth industry;
- Adding new & related products increases sales of current products;
- New & related products offered at competitive prices;
- Current products are in decline stage of the product life cycle; &
- Strong management team.

Conglomerate/unrelated Diversification

- It is all about seeking growth by appealing to new markets with new product that have no technology relationships to current product.
  - ✓ It is unrelated diversification.
  - ✓ Example: Habesha Capital, MIDROC Ethiopia, etc.

Four Guidelines When Conglomerate Diversification May Be an Effective Strategy

- ❖ Declining annual sales and profits
- ❖ Capital and managerial talent to compete successfully in a new industry
- ❖ Financial synergy between the acquired and acquiring firms
- ❖ Existing markets for present products are saturated

C. International Strategy

- Organization can pursue international growth while pursuing other corporate growth strategies.
- It is all about competing with international business through entering in foreign market.
- Ways to enter a foreign market are exporting, importing, licensing, franchising, and direct investment.

2. Stability strategy

- It is also called **neutral strategy** occurs when an organization is satisfied with its current situation & wants to maintain the status quo. A corporation may choose stability over growth by continuing its current activities without any significant change in direction.
- Stability strategy is a strategy in which an organization maintains its current size and current level of business operations.
- They are very popular with small business owners who have found a niche and are happy with their success and the manageable size of their firms.
- Stability strategies can be very useful in the short run, but they can be dangerous if followed for too long.
- Implementing the stability strategy is all about neither slipping backward nor moving ahead.
- Under the following conditions, using stability strategy is appropriate :
  - ✓ When the organization is serving a defined market or its segments according to its mission, it can adopt stable growth strategy. Since the organization is serving the market and fulfilling its mission , it may continue to do so. Generally in such a case, the environmental factors do not show appreciable change and the organization is able to relate itself with the environment. This happens with most of the organizations in the short term because their environment does not change and they can continue in the same business.
  - ✓ If the organization continues to pursue same objectives, it is better to adopt stability strategy adjusting the level of achievement about the same percentage each year as it has achieved in the past. Thus stability strategy does not mean that business is stable, rather there is growth in limits and without really adding any substantial facilities. For example renovation of plant and machinery may add to production but by better efficiency and not through any substantial increase in the production facilities.
  - ✓ When there is scope for incremental improvement of functional performance in the same line of business, the organization should go for stability strategy. This is the motto of taking fullest advantages of the situation. For example, if an organization has got certain technological or other breakthrough, it may continue in the same line so long as it derives certain competitive advantage. The organization can look for achieving the functional improvement thereby bringing efficiency and economy in the operations which will further add to its competitive competence.
  - ✓ When the management wants to avoid additional hassles associated with growth.
  - ✓ When organizational resources have been exhausted because of earlier growth strategies.
  - **Some of the more popular of these strategies are:**
    - ✓ Pause/Proceed-with-Caution,
    - ✓ No-Change, And

- ✓ Profit Strategies.

A. Pause/Proceed with Caution Strategy

- A pause/proceed-with-caution strategy is, in effect, a timeout- an opportunity to rest before continuing a growth or retrenchment strategy.
- It is a very deliberate attempt to make only incremental improvements until a particular environmental situation changes.
- It is typically conceived as a temporary strategy to be used until the environment becomes more hospitable or to enable a company to consolidate its resources after prolonged rapid growth.

B. No-Change Strategy

- A no-change strategy is a decision to do nothing new—a choice to continue current operations and policies for the foreseeable future.
- Rarely articulated as a definite strategy, a no change strategy's success depends on a lack of significant change in a corporation's situation.
- Unless the industry is undergoing consolidation, the relative comfort a company in this situation experiences is likely to encourage the company to follow a no-change strategy in which the future is expected to continue as an extension of the present.
  - ✓ The relative stability created by the firm's modest competitive position in an industry facing little or no growth encourages the company to continue on its current course, making only small adjustments for inflation in its sales and profit objectives.
  - ✓ There are no obvious opportunities or threats, nor is there much in the way of significant strengths or weaknesses.
  - ✓ Few aggressive new competitors are likely to enter such an industry.
  - ✓ The corporation has probably found a reasonably profitable and stable niche for its products.

C. Profit Strategy

- No firm can indefinitely continue with a no-change strategy.
- A profit strategy is a decision to do nothing new in a worsening situation but instead to act as though the company's problems are only temporary.
- The profit strategy is an attempt to artificially support profits when a company's sales are declining by reducing investment and short-term discretionary expenditures.
- The profit strategy is useful only to help a company get through a temporary difficulty.
- The profit strategy is typically top management's passive, short-term, and often self-serving response to a difficult situation.
- In such situations, it is often better to face the problem directly by choosing a retrenchment strategy.

3. Decline/Renewal strategy

- It includes Harvesting, Retrenchment/turnaround, divestiture & liquidation strategies.
  - ✓ **Harvesting** occurs when future growth appears doubtful or not cost effective – the main reason could be because of new competition or changes in consumer preferences
  - ✓ In this case the firm limits additional investment & expenses but maximizes short-term profit & cash flow through maintaining market share over the short-run.
  - ✓ Conditions for harvesting strategy:
    - ▪ The business is not a major contributor of sales, stability, or prestige to the organization
    - ▪ The management may use the freed-up resources for other attractive uses
  - ✓ **Retrenchment/Turnaround** strategy is designed to reverse a negative trend & get the organization back on the track or profitability – a temporary measure until things improve
  - ✓ Turnaround strategy also known as cutback strategy, has the basic philosophy: 'hold the present business and cut the cost'.
  - ✓ This situation is needed as no organization is immune from internal hard time-stagnation or declining performance no matter what the state of economy is.
  - ✓ Major actions should be taken are:
    - ▪ Reducing the size of operations
      - • Eliminating low-margin products
      - • Selling machineries
      - • Laying off employees
    - ▪ Cutting back employee compensation or benefits
    - ▪ Replacing higher-paid employees with lower-paid employees
    - ▪ Leasing rather than buying equipment
    - ▪ Cutting back marketing expenses

Five Guidelines When Retrenchment May Be an Especially Effective Strategy

- Required when an organization has grown so large so quickly that major internal reorganization is needed
- Firm has failed to meet its objectives and goals consistently over time but has distinctive competencies
- Firm is one of the weaker competitors
- Inefficiency, low profitability, poor employee morale and pressure from stockholders to improve performance.
- When an organization's strategic managers have failed
- Very quick growth to large organization where a major internal reorganization is needed

- ✓ **Divestiture:** Sometimes, it may not be possible for the organization to carry on a particular line of business because it does not offer any potential even after turnaround action. In that case, the organization tries to get rid of that business by pursuing a divestment strategy.
- ✓ Divestiture strategy occurs when an organization sells or divests itself of a business or part of a business – previous diversification is not successful (weak growth prospects & poor profitability)
- ✓ Very popular strategy as firms try to focus on their core strengths, lessening their level of diversification.
- ✓ Moreover, when the firm is highly indebted – it might prefer to survive by selling some of its businesses by raising sufficient capital to:
    - Increase the performance of the remaining businesses
    - Settle its debt – liquidity.
- ✓ **Divestment involves selling a business unit to the highest bidder.**

Five Guidelines When Divestiture May Be an Especially Effective Strategy

- When firm has pursued retrenchment but failed to attain needed improvements
- When a division needs more resources than the firm can provide
- When a division is responsible for the firm's overall poor performance
- When a division is a misfit with the organization
- When a large amount of cash is needed and cannot be obtained from other sources.

- ✓ **Liquidation:** Selling all of a company's assets, in parts, for their tangible worth.

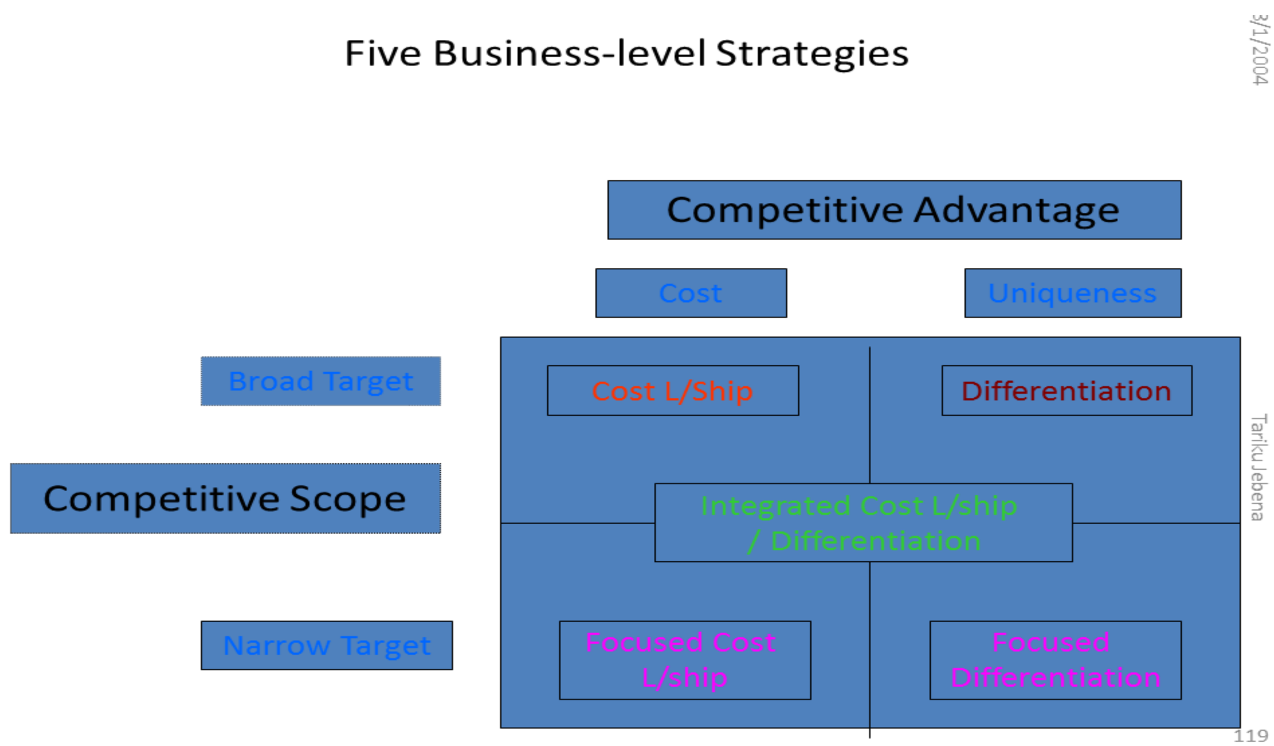
Three Guidelines When Liquidation May Be an Especially Effective Strategy

- When both retrenchment and divestiture have been pursued unsuccessfully
- If the only alternative is bankruptcy, liquidation is an orderly alternative
- When stockholders can minimize their losses by selling the firm's assets

B. BUSINESS LEVEL STRATEGY

- **Business strategy** is a strategy designed to gain competitive advantage by exploiting core competencies in specific product market for the purpose of providing value to customers.
- Business-level strategies are action firms take to gain competitive advantages in a single market or industry.

- Corporate-level strategies are actions firms take to gain competitive advantage by operating in multiple markets or industries simultaneously.
- **Business-level strategy** is a **deliberate choice** about how a firm will perform the value chain's primary & support activities in ways that create **unique value.**
- It reflects **where** & **how** the firm has an **advantage** over its rivals
- It Is intended to **create differences** b/n the firm's **position** relative those of its rivals
- Thus, the **essence** of a firm's business-level strategy is choosing to perform:
    - ✓ Perform activities differently than rivals – to achieve lowest cost or
    - ✓ Perform different (valuable) activities – being able to differentiate
- ➢ Hence, **competitive advantage** is achieved within some **scope** – firms should prefer one of the two



- Business-level strategies are called "**generic strategies**"
- The five **generic strategies** are:
    - ➢ Cost leadership
    - ➢ Differentiation
    - ➢ Focused cost leadership
    - ➢ Focused differentiation

- Integrated cost leadership & differentiation

Cost leadership strategy

- A cost leadership strategy is an integrated set of actions designed to produce or deliver goods or services at the lowest cost relative to competitors, with features that are acceptable to customers
  - ✓ Lowest competitive price
  - ✓ Features acceptable to many customers
  - ✓ Relatively standardised products
- Cost saving actions required by this strategy:
  - ✓ Building efficient scale facilities
  - ✓ Tightly controlling production & overhead costs
  - ✓ Simplifying production processes & building efficient manufacturing facilities
  - ✓ Minimising costs of sales, R&D & service
  - ✓ Monitoring costs of activities provided by outsiders

Economies of Scope

- ✓ Economies of scope occur through a firm's ability to spread costs associated with one element of the value chain across multiple products, thereby reducing costs.
- ✓ For example, Sharp achieves economies of scope through spreading the costs of running their distribution networks etc across a range of products.

Accumulated Experience

- ✓ As a person or a firm gains experience in completing a task, they become <u>more efficient</u> at doing it.
- ✓ This process can occur through:
  - Learning or experience
  - Technical progress

Competitive risks of the cost-leadership strategy

- ✓ Processes used to produce & distribute goods or services may become obsolete due to competitors' innovations.
- ✓ Focus on cost reductions may occur at expense of customers' perceptions of differentiation encouraging them to purchase competitors' products & services

Competitors, using their own core competencies, may learn to successfully imitate the cost leader's strategy.

Differentiation strategy

- A differentiation strategy is an integrated set of actions designed to produce goods or services that customers perceive as being **different** in ways that are important to them
  - ✓ The firm produces non-standardized products for customers who value differentiated features more than they value low cost
  - ✓ The ability to sell goods or services at a price that substantially exceeds the cost of creating its differentiated features allows the firm to outperform rivals & earn above-average returns

Potential entrants

- ✓ Can defend against new entrants because:
  - Entrants' new products must surpass proven products
  - Entrants' new products must be at least equal to performance of proven products, but offered at lower prices

Bargaining power of suppliers & buyers

- ✓ Can mitigate suppliers' power by:
  - Absorbing price increases due to higher margins
  - Passing along higher supplier prices because buyers are loyal to differentiated brand
- ✓ Can mitigate buyers' power by:
  - Well differentiated products reducing customer sensitivity to price increases

Product substitutes

- ✓ Well positioned relative to substitutes because:
  - Brand loyalty to a differentiated product tends to reduce customers' testing of new products or switching brands

Focus strategy

- A **focus strategy** is an integrated set of actions designed to produce or deliver goods or services that serve the needs of a **particular competitive segment**
  - ✓ Examples of specific market segments that can be targeted by a focus strategy:
    - Particular buyer group (e.g. youths or senior citizens)
    - Different segment of a product line (e.g. professional craftsmen versus do-it-yourselves)
    - Different geographic markets
  - ✓ **Types of focused strategies:**

- Focused cost leadership strategy
- Focused differentiation strategy

- ✓ To implement a focus strategy, the firm must be able to complete various primary and support value chain activities in a competitively **superior manner**, in order to develop & sustain a competitive advantage and earn above-average returns
- ✓ Competitor firms may overlook small niches
- ✓ The firm lacks resources needed to compete in the broader market, but serves a narrow segment more effectively than industry-wide competitors

Competitive risks of focus strategies

- ✓ The focuser firm may be ‘out focused’ by its competitors
- ✓ A firm competing on an industry-wide basis decides to pursue the niche market of the focuser firm
- ✓ Customer preferences in the niche market may change to more closely resemble those of the broader market

Integrated cost leadership / differentiation strategy

- A firm that successfully uses the integrated cost leadership / differentiation strategy should be in a better position to:
  - ✓ Adapt quickly to environmental changes
  - ✓ Learn new skills and technologies more quickly
  - ✓ Effectively leverage its core competencies while competing against its rivals
- A commitment to strategic flexibility is necessary for successful use of this strategy
- Examples of Integrated cost leadership / differentiation strategy
  - Southwest Airlines

C. FUNCTIONAL LEVEL STRATEGY

- **Functional strategies** include marketing strategies, new product development strategies, human resource strategies, financial strategies, legal strategies, supply-chain strategies, and information technology management strategies.
- The emphasis is on short and medium term plans and is limited to the domain of each department’s functional responsibility.
- Each functional department attempts to do its part in meeting overall corporate objectives, and hence to some extent their strategies are derived from broader corporate strategies.

1. **Marketing Strategy**: Marketing involves all the activities concerned with the identification of customer needs and making efforts to satisfy those needs with the product and services they require, in return for consideration. The most important part of a marketing strategy is the marketing mix, which covers all the steps a firm can take to increase the demand for its product. It includes product, price, place, promotion, people, process and physical evidence.

   For implementing a marketing strategy, first of all, the company's situation is analyzed thoroughly by **SWOT analysis**. It has three main elements, i.e. **planning, implementation and control**.

   There are a number of strategic marketing techniques, such as social marketing, augmented marketing, direct marketing, person marketing, place marketing, relationship marketing, Synchrony marketing, concentrated marketing, service marketing, differential marketing and demarcating.

2. **Financial Strategy**: All the areas of financial management, i.e. planning, acquiring, utilizing and controlling the financial resources of the company are covered under a financial strategy. This includes raising capital, creating budgets, sources and application of funds, investments to be made, assets to be acquired, working capital management, dividend payment, calculating the net worth of the business and so for.
3. Human Resource Strategy: Human resource strategy covers how an organization works for the development of employees and provides them with the opportunities and working conditions so that they will contribute to the organization as well. This also means to select the best employee for performing a particular task or job. It strategizes all the HR activities like recruitment, development, motivation, retention of employees, and industrial relations.
4. Production Strategy: A firm's production strategy focuses on the overall manufacturing system, operational planning and control, logistics and supply chain management. The primary objective of the production strategy is to enhance the quality, increase the quantity and reduce the overall cost of production.
5. Research and Development Strategy: The research and development strategy focuses on innovating and developing new products and improving the old one, so as to implement an effective strategy and lead the market. Product development, concentric diversification and market penetration are such business strategies which require the introduction of new products and significant changes in the old one.
   For implementing strategies, there are three Research and Development approaches:
   1. To be the first company to market a new technological product.

2. To be an innovative follower of a successful product.

~~1.~~3.To be a low-cost producer of product

5.3. Long term objectives

- Strategic managers recognize that short run profit maximization is rarely the best approach to achieving sustained corporate growth and profitability.
- An often repeated adage states that if impoverished people are given food they will enjoy eating it but will continue to be impoverished.
- However, if they are given seeds and tools and shown how to grow crops, they will be able to permanently improve their condition.
- A parallel situation confronts strategic decision makers:
- Should they eat the seeds by planting for large dividend payments, by selling off inventories, and by cutting back on R&D to improve the near term profit picture, or by laying off workers during periods of slack demand?
- Or should they sow the seeds by reinvesting profits in growth opportunities, by committing existing resources to employee training in the hope of improving performance and reducing turnover, or by increasing advertising expenditures to further penetrate a market?
- For most strategic managers the solution is clear-enjoy a small amount of profit now to maintain vitality , but sow the majority to increase the likelihood of a long-term supply. This is the most frequently used rationale in selecting objectives.
- To achieve long-term prosperity, strategic planners commonly establish long-term objectives in seven areas:
  - ✓ Profitability
  - ✓ Productivity
  - ✓ Competitive position
  - ✓ Employee Development
  - ✓ Employee Relations
  - ✓ Technological Leadership
  - ✓ Public Responsibility

Qualities of Long-term Objectives

- ✓ Achievable
- ✓ Flexible
- ✓ Measurable
- ✓ Motivating
- ✓ Suitable
- ✓ Understandable

- ✓ Acceptable

The Benefits of Having Clear Objectives

- Provide direction by revealing expectations
- Allow synergy
- Aid in evaluation by serving as standards
- Establish priorities
- Reduce uncertainty
- Minimize conflicts
- Stimulate exertion
- Aid in allocation of resources
- Aid in design of jobs
- Provide basis for consistent decision making

5.4. A Comprehensive Strategy-Formulation Framework

- Can be integrated into a three-stage decision-making framework
- Framework are applicable to all sizes and types of organizations and can help strategists identify, evaluate, and select strategies.

Stage-1 Input Stage (Formulation Framework) – Discussed in Chapters 4 & 5

1. External factor evaluation
2. Competitive matrix profile
3. Internal factor evaluation

Stage-2 (Matching stage)

1. TWOS Matrix (Threats-Opportunities-Weaknesses-Strengths)
2. SPACE Matrix (Strategic Position and Action Evaluation)
3. BCG Matrix (Boston Consulting Group)
4. IE Matrix (Internal and external)
5. GS Matrix (Grand Strategy)

Stage-3 (Decision stage)

1. QSPM (Quantitative Strategic Planning Matrix)

The Matching Stage

1. TOWS/SWOT MATRIX

A TWOS Analysis is a strategic planning tool used to evaluate the Threats, Opportunities and Strengths, Weaknesses, involved in a project or in a business venture or in any other situation requiring a decision

TOWS matrix elements

a. SO Strategies (strength-opportunities)

b. WO Strategies (weakness- opportunities)

c. ST Strategies (strength-threats), and

d. WT Strategies (weakness-threats).

The most difficult part of TOWS matrix is to match internal and external factor.

Steps for Developing Strategies

There are eight steps involved in constructing a TOWS Matrix:

1. Rank external opportunities

2. Rank external threats

3. Rank internal strength

4. Rank internal weaknesses.

5. Match internal strengths with external opportunities and mention the result in the SO Strategies cell.

6. Match internal weaknesses with external opportunities and mention the result in the WO Strategies cell..

7. Match internal strengths with external threats and mention the result in the ST Strategies cell.

8. Match internal weaknesses with external threats and mention the result in the WT strategies cell.

Blank	Strengths–S List Strengths	Weaknesses – W List Weaknesses
Opportunities – O List Opportunities	SO-Strategies Use strength to obtain opportunities	WO-Strategies Overcome weaknesses by taking advantage of opportunities
Threats – T List Threats	ST-Strategies Use strengths to avoid threats	WT-Strategies Minimize weaknesses and avoid threats

2. **SPACE MATRIX**

- **It explains that what is our strategic position and what possible action can be taken.**
- **It is not closed matrix**
- **Its four-quadrant framework indicates whether aggressive, conservative, defensive, or competitive strategies are most appropriate for a given organization**
- **The axes of the SPACE Matrix represent**

   a. **Two internal dimensions**

      i. **Financial position [FP]**

      ii. **Competitive position [CP]**

   b. **Two external dimensions**

i. **Stability position [SP]**

ii. **Industry position [IP]**

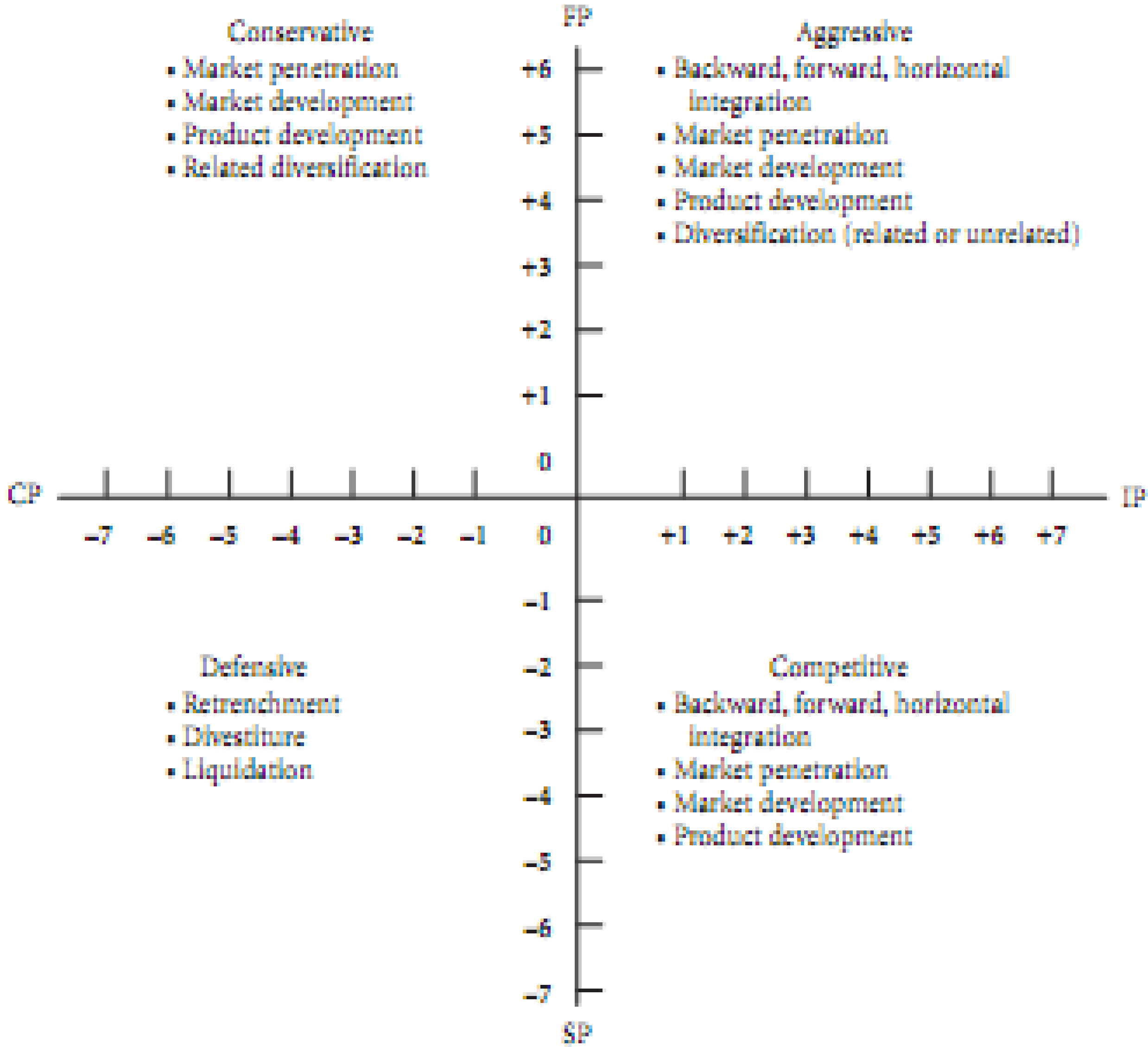
- **They are the most important determinants of an organization's overall strategic position**

Importance of Vision and Mission Statements

- Factors that were included earlier in the firm's EFE and IFE Matrices should be considered in developing a SPACE Matrix.

- Other variables commonly included are given in Table presented in the next slide

The SPACE Matrix



Source: Adapted from H. Rowe, R. Mason, and K. Dickel, *Strategic Management and Business Policy: A Methodological Approach* (Reading, MA: Addison-Wesley Publishing Co. Inc., © 1982): 155.

Example Factors That Make Up the SPACE Matrix Axes

Internal Strategic Position	External Strategic Position
Financial Position (FP)	*Stability Position (SP)*
Return on investment	Technological changes
Leverage	Rate of inflation
Liquidity	Demand variability
Working capital	Price range of competing products
Cash flow	Barriers to entry into market
Inventory turnover	Competitive pressure
Earnings per share	Ease of exit from market
Price earnings ratio	Price elasticity of demand
	Risk involved in business
Competitive Position (CP)	*Industry Position (IP)*
Market share	Growth potential
Product quality	Profit potential
Product life cycle	Financial stability
Customer loyalty	Extent leveraged
Capacity utilization	Resource utilization
Technological know-how	Ease of entry into market
Control over suppliers and distributors	Productivity, capacity utilization

Source: Adapted from H. Rowe, R. Mason, and K. Dickel, *Strategic Management and Business Policy: A Methodological Approach* (Reading, MA: Addison-Wesley Publishing Co. Inc., © 1982): 155–156.

The Steps Required to Develop a SPACE Matrix

1. Select a set of variables to define FP, CP, SP, and IP.

2. Assign a numerical value ranging from +1 (worst) to +7 (best) to each of the variables that make up the FP and IP dimensions. Assign a numerical value ranging from -1 (best) to -7 (worst) to each of the variables that make up the SP and CP dimensions. On the FP and CP axes, make comparison to competitors. On the IP and SP axes, make comparison to other industries.

3. Compute an average score for FP, CP, IP, and SP by summing the values given to the variables of each dimension and then by dividing by the number of variables included in the respective dimension.

4. Plot the average scores for FP, IP, SP, and CP on the appropriate axis in the SPACE Matrix.

5. Add the two scores on the x-axis and plot the resultant point on X. Add the two scores on the y-axis and plot the resultant point on Y. Plot the intersection of the new xy point.

6. Draw a directional vector from the origin of the SPACE Matrix through the new intersection point. This vector reveals the type of strategies recommended for the organization: aggressive, competitive, defensive, or conservative.

3. IE Matrix

- It is related to internal (IFE) and external factor evaluation (EFE)
- Positions an organization's various divisions in a nine-cell display
- Similar to BCG Matrix except the IE Matrix:

o Requires more information about the divisions

o Strategic implications of each matrix are different

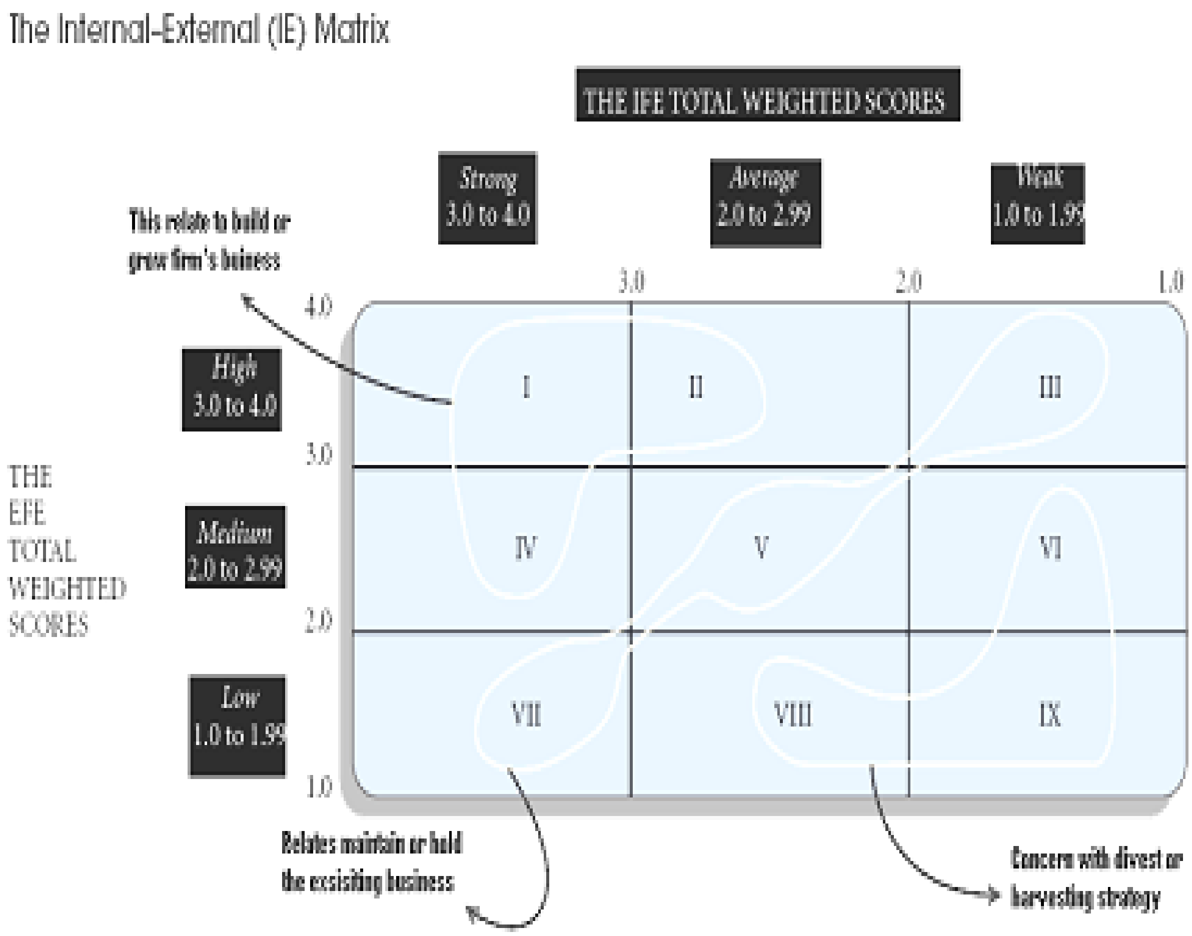
- Based on two key dimensions

o The IFE total weighted scores on the x-axis

o The EFE total weighted scores on the y-axis

Divided into three major regions

- o Grow and build – Cells I, II, or IV
- o Hold and maintain – Cells III, V, or VII
- o Harvest or divest – Cells VI, VIII, or IX



Steps for The Development of IE Matrix

1. Plot IFE total weighted scores on the x-axis and the EFE total weighted scores on the y axis

2. On the x-axis of the IE Matrix, an IFE total weighted score of 1.0 to 1.99 represents a weak internal position; a score of 2.0 to 2.99 is considered average; and a score of 3.0 to 4.0 is strong.

3. On the y-axis, an EFE total weighted score of 1.0 to 1.99 is considered low; a score of 2.0 to 2.99 is medium; and a score of 3.0 to 4.0 is high.

4. IE Matrix divided into three major regions.

    - Grow and build – Cells I, II, or IV
    - Hold and maintain – Cells III, V, or VII
    - Harvest or divest – Cells VI, VIII, or IX

4.Grand Strategy Matrix

- GS matrix is popular tool for formulating alternative strategies.
- In this matrix all organization divides into four quadrants.
- Any organization should be placed in any one of four quadrants.
- Appropriate strategies for an organization to consider are listed in sequential order of attractiveness in each quadrant of the matrix.
- It is based two major dimensions
    - 1. Market growth
    - 2. Competitive position
- All quadrant contain all possible strategies

The Grand Strategy Matrix

Source: Adapted from Roland Christensen, Norman Berg, and Malcolm Salter, *Policy Formulation and Administration* (Homewood, IL: Richard D. Irwin, 1976): 16–18.

5.5. The Decision Stage

1. **QSPM**

This technique objectively indicates which alternative strategies are best.

The QSPM uses input from Stage 1 analyses and matching results from Stage 2 analyses to decide objectively among alternative strategies

Steps in Preparation Of QSPM

1. List of the firm's key external opportunities/threats and internal strengths/weaknesses in the left column of the QSPM.

2. Assign weights to each key external and internal factor

3. Examine the Stage 2 (matching) matrices and identify alternative strategies that the organization should consider implementing

4. Determine the Attractiveness Scores (AS)

5. Compute the Total Attractiveness Scores

6. Compute the Sum Total Attractiveness Score

5.6. BSC model

- Strategy formulation, evaluation & control technique
- Balance financial measures with nonfinancial measures
- Balance shareholder objectives with customer & operational objectives
- Based on four pillars: financial, customer, business process and growth
- BSC is an integrated strategic management tool.
- It also serve as a performance measurement tool i.e. measuring organization performance from four perspective (finance, customer, internal process and learning and growth) and there by achieve balanced performance measurement.
- According to BSC, organizations can ensure integrated strategy by devising of their strategy or strategic objectives in four perspectives. Such perspectives known as BSC perspectives.

1. The *financial perspective covers the financial objectives of an organization* and allows managers to track financial success and shareholder value.

- Crudely speaking, at the highest level, the shareholders" main concerns will fall into two broad categories, one of revenue generation, the other of productivity and cost effectiveness, together yielding a level of returns demanded by the shareholder.

N.B. The financial perspective of the Balanced Scorecard expresses the requirements of the shareholder.

The *customer perspective covers the customer objectives such as customer* satisfaction, market-share goals as well as product and service attributes.

3. The *internal process perspective covers internal operational goals and outlines* the key processes necessary to deliver the customer objectives.

The *learning and growth perspective covers the intangible drivers of future* success such as human capital, organizational capital and information capital including skills, training, organizational culture, leadership, systems and databases.

N.B. Strategy maps UNDER BSC are visual representations of the causal linkages assumed between strategic objectives in the above four BSC perspectives.

- Initially, it was suggested to visualize a BSC in a four-box model as follows
- However, the classic four-box model is now outdated and has been replaced by a strategy map view.
- A strategy map places the four perspectives into a causal hierarchy to show that the objectives support each other and that delivering the right performance in the lower perspectives will help to achieve the objectives in the upper perspectives.
- For example, the objectives in the learning and growth perspective underpin the objectives in the internal process perspective, which in turn underpin the objectives in the customer perspectives. Delivering the customer objectives should then lead to the achievement of the financial objectives in the financial perspective.
- This causal logic is one of the most important elements of modern BSCs. It allows companies to create a truly integrated set of strategic objectives

5.7. The 7'S model

- ✓ **Strategy:** this is your organization's plan for building and maintaining a competitive advantage over its competitors.
- ✓ **Structure:** this how your company is organized (that is, how departments and teams are structured, including who reports to whom).
- ✓ **Systems:** the daily activities and procedures that staff uses to get the job done.
- ✓ **Shared values:** these are the core values of the organization, as shown in its corporate culture and general work ethic. They were called "superordinate goals" when the model was first developed.
- ✓ **Style:** the style of leadership adopted.
- ✓ **Staff:** the employees and their general capabilities.

- ✓ **Skills:** the actual skills and competencies of the organization's employees.

CHAPTER SIX

STRATEGY IMPLEMENTATION (implementing strategies management issues)

6.1 The Nature of Strategy Implementation

Successful strategy formulation does not guarantee successful strategy implementation. It is always more difficult to do something (strategy implementation) than to say you are going to do it (strategy formulation)! Although inextricably linked, strategy implementation is fundamentally different from strategy formulation. Strategy formulation and implementation can be contrasted in the following ways:

- Strategy formulation is positioning forces before the action.
- Strategy implementation is managing forces during the action.
- Strategy formulation focuses on effectiveness.
- Strategy implementation focuses on efficiency.
- Strategy formulation is primarily an intellectual process.
- Strategy implementation is primarily an operational process.
- Strategy formulation requires good intuitive and analytical skills.
- Strategy implementation requires special motivation and leadership skills.
- Strategy formulation requires coordination among a few individuals.
- Strategy implementation requires coordination among many individuals.

Strategy-formulation concepts and tools do not differ greatly for small, large, for-profit, or nonprofit organizations. However, strategy implementation varies substantially among different types and sizes of organizations.

6.2 Concept of Strategy Implementation

Strategy implementation is "**the process of allocating resources to support the chosen strategies**". This process includes the various management activities that are necessary to put strategy in motion, institute strategic controls that monitor progress, and ultimately achieve organizational goals.

According to McCarthy ‘strategy implementation may be said to consist of securing resources, organizing these resources and directing the use of these resources within and outside the organization. Strategy implementation can be defines as a process through which a chosen strategy is put into action.

For example, according to ***Steiner***, "the implementation process covers the entire managerial activities including such matters as motivation, compensation, management appraisal, and control processes".

As ***Higgins*** has pointed out, "almost all the management functions -planning, controlling, organizing, motivating, leading, directing, integrating, communicating, and innovation -are in some degree applied in the implementation process".

The Relation between Strategy Formulation and Strategy Implementation

In order to achieve its objectives, an organization must not only formulate but also implement its strategies effectively. The Figure represents the importance of both tasks in matrix form and suggests the probable outcomes of the four possible combinations of these variables:

	Good implementation	poor implementation
Appropriate strategy	**Success**	**Trouble**
Poor strategy	**Roulette**	**Failure**

- ☞ **Success** is the most likely outcome when strategy is appropriate and implementation good.
- ☞ **Roulette** involves situation wherein a poor strategy is implemented well.

- ☞ **Trouble** is characterized by situations wherein an appropriate strategy is poorly implemented.
- ☞ **Failure** involves situations wherein a poor strategy is poorly implemented. Diagnosing why a strategy failed in the roulette, trouble, and failure cells in order to find a remedy requires the analysis of both formulation and implementation.

6.2.1 Management Perspectives

In all but the smallest organizations, the transition from strategy formulation to strategy implementation requires a shift in responsibility from strategists to divisional and functional managers. Implementation problems can arise because of this shift in responsibility, especially if strategy-formulation decisions come as a surprise to middle- and lower-level managers. Managers and employees are motivated more by perceived self-interests than by organizational interests, unless the two coincide. Therefore, it is essential that divisional and functional managers be involved as much as possible in strategy-formulation activities. Of equal importance, strategists should be involved as much as possible in strategy-implementation activities.

management issues central to strategy implementation include establishing annual objectives, devising policies, allocating resources, altering an existing organizational structure, restructuring and reengineering, revising reward and incentive plans, minimizing resistance to change, matching managers with strategy, developing a strategy supportive culture, adapting production/operations processes, developing an effective human resources function, and, if necessary downsizing. Management changes are necessarily more extensive when strategies to be implemented move a firm in a major new direction.

Managers and employees throughout an organization should participate early and directly in strategy-implementation decisions. Their role in strategy implementation should build upon prior involvement in strategy-formulation activities. Strategists' genuine personal commitment to implementation is a necessary and powerful motivational force for managers and employees. Too often, strategists are too busy to actively support strategy-implementation efforts, and their lack of interest can be detrimental to organizational success. The rationale for objectives and strategies should be understood and clearly communicated throughout an organization. Major competitors' accomplishments, products, plans, actions, and performance should be apparent to all organizational members. Major external opportunities and threats should be clear, and managers' and employees' questions should be answered. Top down flow of communication is essential for developing bottom-up support.

A. Annual Objectives

Establishing annual objectives is a decentralized activity that directly involves all managers in an organization. Active participation in establishing annual objectives can lead to acceptance and commitment. *Annual objectives* are essential for strategy implementation because they:-

1. Represent the basis for allocating resources;
2. Are a primary mechanism for evaluating managers;
3. Are the major instrument for monitoring progress toward achieving long-term objectives; and
4. Establish organizational, divisional, and departmental priorities.

Considerable time and effort should be devoted to ensuring that annual objectives are well conceived, consistent with long-term objectives, and supportive of strategies to be implemented. Approving, revising, or rejecting annual objectives is much more than a rubber-stamp activity. The purpose of annual objectives can be summarized as follows:

- Annual objectives serve as guidelines for action, directing and channeling efforts and activities of organization members.
- They provide a source of legitimacy in an enterprise by justifying activities to stakeholders.
- They serve as standards of performance.
- They serve as an important source of employee motivation and identification.
- They give incentives for managers and employees to perform.
- They provide a basis for organizational design.

Clearly stated and communicated objectives are critical to success in all types and sizes of firms. Annual objectives, stated in terms of profitability, growth, and market share by business segment, geographic area, customer groups, and product, are common in organizations.

Objectives should be consistent across hierarchical levels and form a network of supportive aims. Annual objectives should be measurable, consistent, reasonable, challenging, clear, communicated throughout the organization, characterized by an appropriate time dimension, and accompanied by commensurate rewards and sanctions.

Clear annual objectives do not guarantee successful strategy implementation, but they do increase the likelihood that personal and organizational aims can be accomplished. Overemphasis on achieving objectives can result in undesirable conduct, such as faking the numbers, distorting the records, and letting objectives become ends in themselves. Managers must be alert to these potential problems.

B. POLICIES

Policies facilitate solving recurring problems and guide the implementation of strategy. Broadly defined, *policy* refers to specific guidelines, methods, procedures, rules, forms, and administrative practices established to support and encourage work toward stated goals. Policies are instruments for strategy implementation. Policies set boundaries, constraints, and limits on the kinds of administrative actions that can be taken to reward and sanction behavior; they clarify what can and cannot be done in pursuit of an organization's objectives.

Policies let both employees and managers know what is expected of them, thereby increasing the likelihood that strategies will be implemented successfully. They provide a basis for management control, allow coordination across organizational units, and reduce the amount of time managers spend making decisions. Policies also clarify what work is to be done and by whom. They promote delegation of decision making to appropriate managerial levels where various problems usually arise. Many organizations have a policy manual that serves to guide and direct behavior.

C. Resource Allocation

Resource allocation is a central management activity that allows for strategy execution. In organizations that do not use a strategic-management approach to decision making, resource allocation is often based on political or personal factors. Strategic management enables resources to be allocated according to priorities established by annual objectives. Nothing could be more detrimental to strategic management and to organizational success than for resources to be allocated in ways not consistent with priorities indicated by approved annual objectives.

All organizations have at least four types of resources that can be used to achieve desired objectives: financial resources, physical resources, human resources, and technological resources. Allocating resources to particular divisions and departments does not mean that strategies will be successfully implemented. A number of factors commonly prohibit effective resource allocation, including an overprotection of resources, too great an emphasis on short-run financial criteria, organizational politics, vague strategy targets, a reluctance to take risks, and a lack of sufficient knowledge.

The real value of any resource allocation program lies in the resulting accomplishment of an organization’s objectives. Effective resource allocation does not guarantee successful strategy implementation because programs, personnel, controls, and commitment must breathe life into the resources provided. Strategic management itself is sometimes referred to as a “resource allocation process.”

D. Managing Conflict

Interdependency of objectives and competition for limited resources often leads to conflict. *Conflict* can be defined as a disagreement between two or more parties on one or more issues. Establishing annual objectives can lead to conflict because individuals have different expectations and perceptions, schedules create pressure, personalities are incompatible, and misunderstandings between line managers (such as production supervisors) and staff managers (such as human resource specialists) occur.

Establishing objectives can lead to conflict because managers and strategists must make trade-offs, such as whether to emphasize short-term profits or long-term growth, profit margin or market share, market penetration or market development, growth or stability, high risk or low risk, and social responsiveness or profit maximization. Trade-offs are necessary because no firm has sufficient resources pursue all strategies to would benefit the firm.

Conflict is unavoidable in organizations, so it is important that conflict be managed and resolved before dysfunctional consequences affect organizational performance. Conflict is not always bad. An absence of conflict can signal indifference and apathy. Conflict can serve to energize opposing groups into action and may help managers identify problems.

Various approaches for managing and resolving conflict can be classified into three categories:

1. ***Avoidance*** includes such actions as ignoring the problem in hopes that the conflict will resolve itself or physically separating the conflicting individuals (or groups).
2. ***Defusion*** can include playing down differences between conflicting parties while accentuating similarities and common interests, compromising so that there is neither a clear winner nor loser, resorting to majority rule, appealing to a higher authority, or redesigning present positions.

3. ***Confrontation*** is exemplified by exchanging members of conflicting parties so that each can gain an appreciation of the other's point of view or holding a meeting at which conflicting parties present their views and work through their differences.

E. Matching Structure with Strategy

Changes in strategy often require changes in the way an organization is structured for two major reasons. First, structure largely dictates how objectives and policies will be established.

Objectives and policies are stated largely in terms of products in an organization whose structure is based on product groups. The structural format for developing objectives and policies can significantly impact all other strategy-implementation activities.

The second major reason why changes in strategy often require changes in structure is that structure dictates how resources will be allocated. If an organization's structure is based on customer groups, then resources will be allocated in that manner. Similarly, if an organization's structure is set up along functional business lines, then resources are allocated by functional areas. Unless new or revised strategies place emphasis in the same areas as old strategies, structural reorientation commonly becomes a part of strategy implementation.

Changes in strategy lead to changes in organizational structure. Structure should be designed to facilitate the strategic pursuit of a firm and, therefore, follow strategy. Without a strategy or reasons for being (mission), companies find it difficult to design an effective structure. There is no one optimal organizational design or structure for a given strategy or type of organization. What is appropriate for one organization may not be appropriate for a similar firm, although successful firms in a given industry do tend to organize themselves in a similar way. For example, **consumer goods companies** tend to emulate the divisional structure- by-product form of organization. **Small firms** tend to be functionally structured (centralized). **Medium-sized firms** tend to be divisionally structured (decentralized). **Large firms** tend to use a strategic business unit (SBU) or matrix structure. As organizations grow, their structures generally change from simple to complex as a result of concatenation, or the linking together of several basic strategies.

Numerous external and internal forces affect an organization; no firm could change its structure in response to every one of these forces, because to do so would lead to chaos. However, when a firm changes its strategy, the existing organizational structure may become ineffective.

symptoms of an ineffective organizational structure include too many levels of management, too many meetings attended by too many people, too much attention being directed toward solving interdepartmental conflicts, too large a span of control, and too many unachieved objectives. Changes in structure can facilitate strategy-implementation efforts, but changes in structure should not be expected to make a bad strategy good, to make bad managers good, or to make bad products sell. Structure undeniably can and does influence strategy. Strategies formulated must be workable, so if a certain new strategy required massive structural changes it would not be an attractive choice. In this way, structure can shape the choice of strategies. But a more important concern is determining what types of structural changes are needed to implement new strategies and how these changes can best be accomplished. We examine this issue by focusing on seven basic types of organizational structure: **functional, divisional by geographic area, divisional by product, divisional by customer, divisional process, strategic business unit (SBU), and matrix.**

A ***functional structure or centralized*** the most widely used structure is the functional or centralized type because this structure is the simplest and least expensive of the seven alternatives. In this structure groups tasks and activities by business function, such as production/operations, marketing, finance/accounting, research and development, and management information systems.

A divisional structure or decentralized as a small organization grows, it has more difficulty managing different products and services in different markets

- A ***divisional structure by geographic area*** is appropriate for organizations whose strategies need to be tailored to fit the particular needs and characteristics of customers in different geographic areas. This type of structure can be most appropriate for organizations that have similar branch facilities located in widely dispersed areas. A divisional structure by geographic area allows local participation in decision making and improved coordination within a region.
- **The *divisional structure by product (or services)*** is most effective for implementing strategies when specific products or services need special emphasis. Also, this type of structure is widely used when an organization offers only a few products or services or when an organization's products or services differ substantially. The divisional structure

allows strict control over and attention to product lines, but it may also require a more skilled management force and reduced top management control.

- **A *divisional structure by customer*** can be the most effective way to implement strategies. This structure allows an organization to cater effectively to the requirements of clearly defined customer groups.
- **The divisional structure by process** can be particularly effective in achieving objectives, when distinct production processes represent the thrust of competitiveness in an industry.

The SBU structure groups' similar divisions into strategic business units and delegates authority and responsibility for each unit to a senior executive who reports directly to the chief executive officer. This change in structure can facilitate strategy implementation by improving coordination between similar divisions and channeling accountability to distinct business units. As the number, size, and diversity of divisions in an organization increase, controlling and evaluating divisional operations become increasingly difficult for strategists. Increases in sales often are not accompanied by similar increases in profitability. The span of control becomes too large at top levels of the firm.

A *matrix structure* is the most complex of all designs because it depends upon both vertical and horizontal flows of authority and communication (hence the term *matrix*). In contrast, functional and divisional structures depend primarily on vertical flows of authority and communication.

- ***Restructuring***—also called *downsizing*, *rightsizing*, or *delayering*—involves reducing the size of the firm in terms of number of employees, number of divisions or units, and number of hierarchical levels in the firm's organizational structure. This reduction in size is intended to improve both efficiency and effectiveness. Restructuring is concerned primarily with shareholder well-being rather than employee well-being.
- **Reengineering—**also called process management, process innovation, or process redesign—involves reconfiguring or redesigning work, jobs, and processes for the purpose of improving cost, quality, service, and speed. Reengineering does not usually affect the organizational structure or chart, nor does it imply job loss or employee layoffs. *Reengineering* is concerned more with employee and customer well-being than shareholder well-being.

6.3 A General Framework for Strategy Implementation

The first step in implementation is identifying the activities, decisions, and relationships critical to accomplishing the activities. There are six principal administrative tasks that shape a manager's action agenda for implementing strategy. In general, every unit of an organization has to ask, "***What is required for us to implement our part of the overall strategic plan and how can we bets get it done*?**"

The specific components of each of the six strategy-implementation tasks:

1. Building an Organization Capable of Executing the Strategy. The organization must have the structure necessary to turn the strategy into reality. Furthermore, the firm's personnel must possess the skill needed to execute the strategy successfully. Related to this is the need to assign the responsibility for accomplishing key implementation tasks to the right individuals or groups.

2. Establishing a Strategy-Supportive Budget. If the firm is to accomplish strategic objectives, top management must provide the people, equipment, facilities, and other resources to carry out its part of the strategic plan. Further, once the strategy has been decided on, the key tasks to perform and kinds of decision required must be identified, formal plans must also be developed. The tasks should be arranged in a sequence comprising a plan of action within targets to be achieved at specific dates.

3. Installing Internal Administrative Support Systems. Internal systems are policies and procedures to establish desired types of behavior, information systems to provide strategy-critical information on a timely basis, and whatever inventory, materials management, customer service, cost accounting, and other administrative systems are needed to give the organization important strategy-executing capability. These internal systems must support the management process, the way the managers in an organization work together, as well as monitor strategic progress.

4. Devising Rewards and Incentives that are tightly linked to Objectives and Strategy. People and departments of the firm must be influenced, through incentives, constraints, control, standards, and rewards, to accomplish the strategy.

5. Shaping the Corporate Culture to Fit the Strategy. A strategy-supportive corporate culture causes the organization to work hard (and intelligently) toward the accomplishment of the strategy.

6. Exercising Strategic Leadership. Strategic leadership consists of obtaining commitment to the strategy and its accomplishment. It also involves the constructive use of power and politics, in building a consensus to support the strategy.

CHAPTER SEVEN

STRATEGY EVALUATION AND CONTROL

7.1. THE NATURE STRATEGY EVALUATION

The final stage in strategic management is strategy evaluation and control. All strategies are subject to future modification because internal and external factors are constantly changing. In the strategy evaluation and control process managers determine whether the chosen strategy is achieving the organization's objectives. The fundamental strategy evaluation and control activities are**: reviewing internal and external factors that are the bases for current strategies, measuring performance, and taking corrective actions**. In many organizations, strategy evaluation is simply an appraisal of how well an organization has performed. Strategy evaluation is necessary for all sizes and kinds of organizations. Strategy evaluation should initiate managerial questioning of expectations and assumptions, should trigger a review of objectives and values, and should stimulate creativity in generating alternatives and formulating criteria of evaluation. **Strategy-evaluation activities should be performed on a continuing basis, rather than at the end of specified periods of time or just after problems occur.** Evaluating strategies on a continuous rather than on a periodic basis allows benchmarks of progress to be established and more effectively monitored. Managers and employees of the firm should be continually aware of progress being made toward achieving the firm's objectives. As critical success factors change, organizational members should be involved in determining appropriate corrective actions. If assumptions and expectations deviate significantly from forecasts, then the firm should renew strategy-formulation activities, perhaps sooner than planned. In strategy evaluation, like strategy formulation and strategy implementation, people make the difference.

Through involvement in the process of evaluating strategies, managers and employees become committed to keeping the firm moving steadily toward achieving objectives. Richard Rumelt offered four criteria that could be used to evaluate a strategy: **consistency, consonance, feasibility, and advantage.** *Consonance* and *advantage* are mostly based on a firm's external assessment, whereas *consistency* and *feasibility* are largely based on an internal assessment.

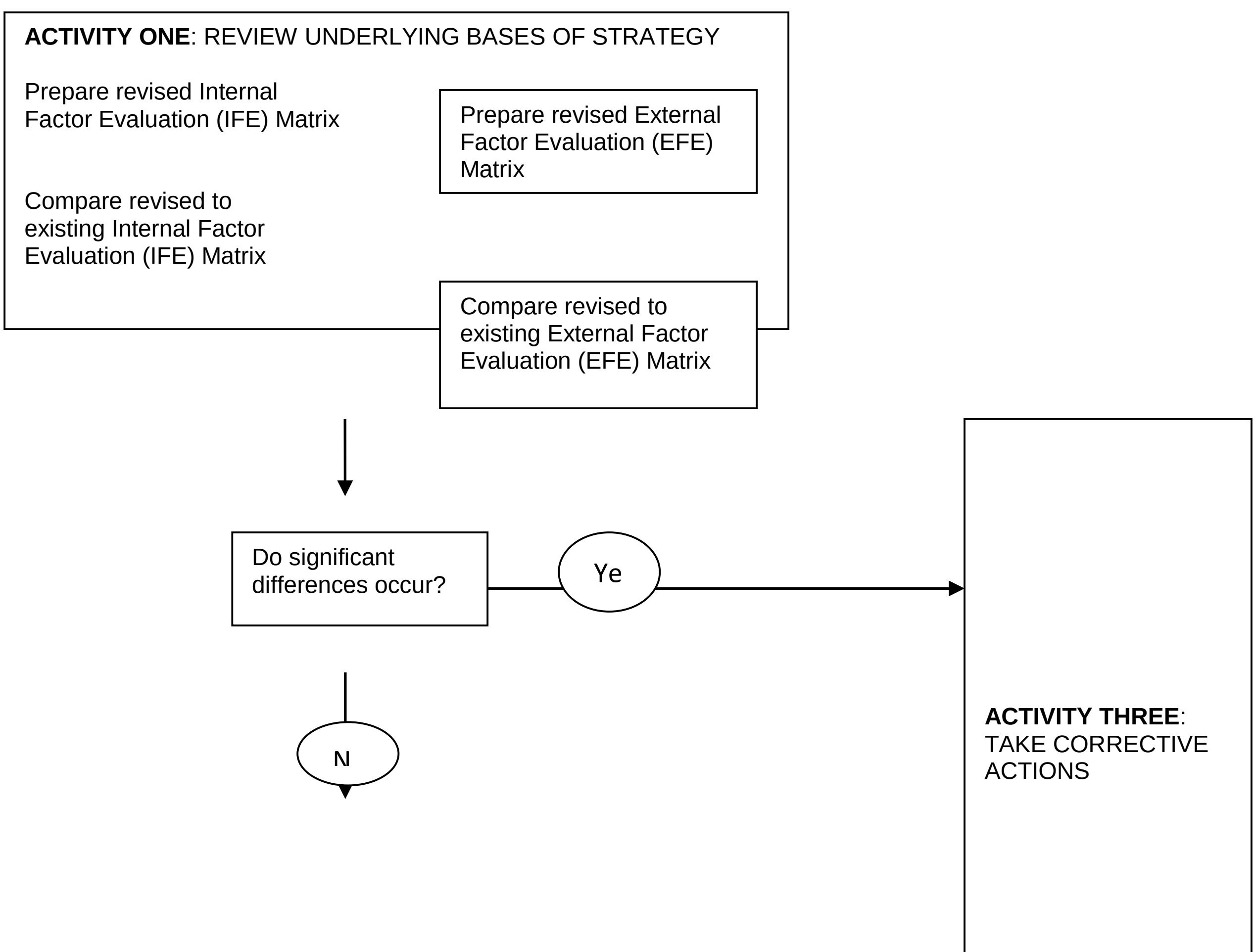
Strategy evaluation is important because organizations face dynamic environments in which key external and internal factors often change quickly and dramatically.

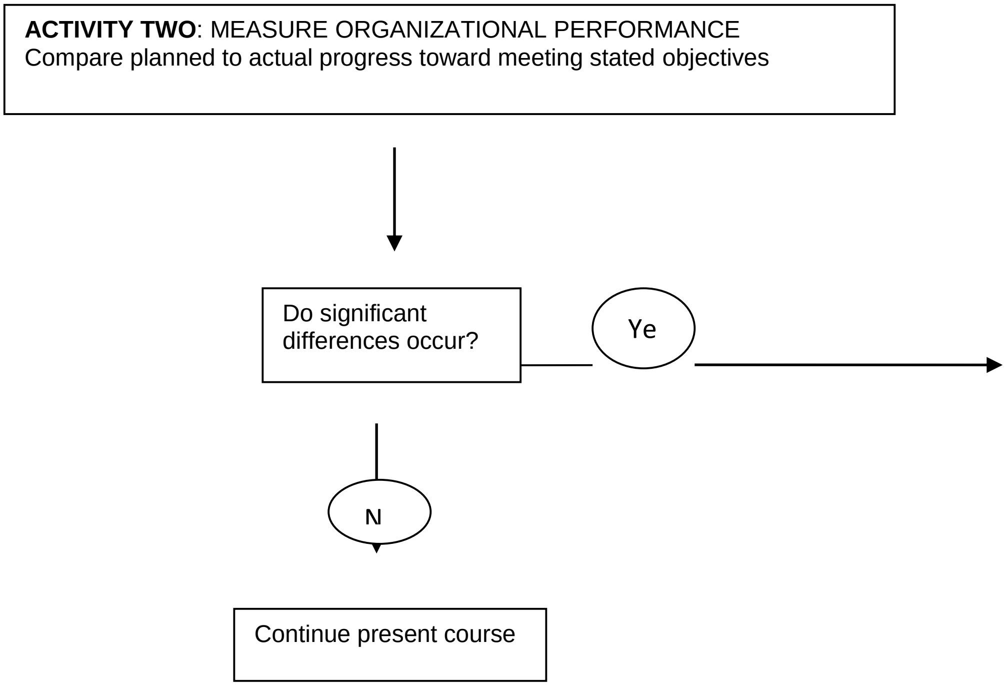
7.2. STRATEGY EVALUATION FRAMEWORK

Notice that corrective actions are almost always needed, except when

1. External and internal factors have not significantly changed and
2. The firm is progressing satisfactorily toward achieving stated objectives.

Reviewing the underlying bases of an organization's strategy could be approached by developing a revised EFE Matrix and IFE Matrix. A *revised IFE Matrix* should focus on changes in the organization's management, marketing, finance/accounting production/operations, R&D, and management information systems strengths and weaknesses. A *revised EFE Matrix* should indicate how effective a firm's strategies have been in response to key opportunities and threats. Numerous external and internal factors can prevent firms from achieving long-term and annual objectives. Externally, actions by competitors, changes in demand, changes in technology, economic changes, demographic shifts, and governmental actions may prevent objectives from being accomplished. Internally, ineffective strategies may have been chosen or implementation activities may have been poor. Objectives may have been too optimistic. External opportunities and threats and internal strengths and weaknesses that represent the bases of current strategies should continually be monitored for change. It is not really a question of whether these factors will change but rather when they will change and in what ways.





7.3. Characteristics of an effective evaluation system

Strategy evaluation must meet several basic requirements to be effective.

- Should be Economical
  - ✓ Too much information can be as bad as too little information
  - ✓ Too many controls can do harm than good
- Should be meaningful
  - ✓ Specifically related to a firm's objectives
  - ✓ Should provide managers with useful information about tasks over which they have control and influence
- Should provide timely information: Approximate info that is timely is generally more desirable for strategy evaluation than accurate information that doesn't depict the present
- Should be designed to provide a true picture of what is happing

- ✓ Should represent the reality of an organization's operation/s
- ✓ Should facilitate action & should be directed to concerned managers
- ✓ Control need to be action-oriented than information-oriented.

- ➢ Should not dominate decisions: It should foster mutual understandings, trust and common sense among divergent units and stakeholders of an organ.
- ➢ Should be simple: Not too cumbersome (bulky) and too restrictive. Complex strategy evaluation systems often confuse people; & accomplish little.
- ➢ The test of an effective SE system is its usefulness; not its complexity.

Large organizations require a more elaborate and detailed strategy-evaluation system because it is more difficult to coordinate efforts among different divisions and functional areas. Managers in small companies often communicate daily with each other and their employees and do not need extensive evaluative reporting systems.

Note: There is no one ideal strategy evaluation system: The unique characteristics of an organization; (its size, management style, purpose, problems, strengths, etc.,) can determine its SE system.

7.4. THE CONTINGENCY MODEL

A basic premise of good strategic management is that firms plan ways to deal with unfavorable and favorable events before they occur. Too many organizations prepare contingency plans just for unfavorable events; this is a mistake, because both minimizing threats and capitalizing on opportunities can improve a firm's competitive position. ***Contingency plans*** **can be defined as alternative plans that can be put into effect if certain key events do not occur as expected.** Only high-priority areas require the insurance of contingency plans. Regardless of how carefully strategies are formulated, implemented, and evaluated, unforeseen events, such as strikes, boycotts, natural disasters, arrival of foreign competitors, and government actions, can make a strategy obsolete. To minimize the impact of potential threats, organizations should develop contingency plans as part of their strategy-evaluation process. Strategists cannot and should not try to cover all bases by planning for all possible contingencies. But in any case, contingency plans should be as simple as possible.

Some contingency plans commonly established by firms include the following:

1. If a major competitor withdraws from particular markets as intelligence reports indicate, what actions should our firm take?
2. If our sales objectives are not reached, what actions should our firm take to avoid profit losses?
3. If demand for our new product exceeds plans, what actions should our firm take to meet the higher demand?
4. If certain disasters occur—such as loss of computer capabilities; a hostile takeover attempt; loss of patent protection; or destruction of manufacturing facilities because of earthquakes, tornadoes or hurricanes—what actions should our firm take?
5. If a new technological advancement makes our new product obsolete sooner than expected, what actions should our firm take?

Too many organizations discard alternative strategies not selected for implementation although the work devoted to analyzing these options would render valuable information. When strategy-evaluation activities reveal the need for a major change quickly, an appropriate contingency plan can be executed in a timely way. Contingency plans can promote a strategist's ability to respond quickly to key changes in the internal and external bases of an organization's current strategy.

7.5. STRATEGIC CONTROL

Management control refers to the process by which an organization influences its subunits and members to behave in ways that lead to the attainment of organizational objectives

What Is Control?

*Robert J. Mockler define management control as "*Management control is a systematic effort to set performance standards with planning objectives, to design information feedback systems, to compare actual performance with these predetermined standards, to determine whether there are any deviations and to measure their significance, and to take any action required to assure that all corporate resources are being used in the most effective and efficient way possible in achieving corporate objectives."

Types of Control

Management can implement controls before an activity commences/start, while the activity is going on, or after the activity has been completed. The three respective types of control based on timing are feed forward, concurrent, and feedback.

1) Feed forward Control

Feed forward control focuses on the regulation of inputs (human, material, and financial resources that flow into the organization) to ensure that they meet the standards necessary for the transformation process.

Feed forward controls are desirable because they allow management to prevent problems rather than having to cure them later. Unfortunately, these controls require timely and accurate information that is often difficult to develop. Feed forward control also is sometimes called **preliminary control**, **preventive control**, or **steering control**.

However, some authors use term "*steering control*" as separate types of control. These types of controls are designed to detect deviation from some standard or goal to allow correction to be made before a particular sequence of actions is completed.

2) Concurrent Control

Concurrent control takes place while an activity is in progress. It involves the regulation of ongoing activities that are part of transformation process to ensure that they conform to organizational standards. Concurrent control is designed to ensure that employee work activities produce the correct results.

Concurrent control sometimes is called **screening** or **yes-no control**, because it often involves checkpoints at which determinations are made about whether to continue progress, take corrective action, or stop work altogether on products or services.

3) Feedback Control

This type of control focuses on the outputs of the organization after transformation is complete. Sometimes called **post action** or **output control**, fulfils a number of important functions. For one thing, it often is used when feed forward and concurrent controls are not feasible or are too costly.

The major drawback of this type of control is that, the time the manager has the information and if there is significant problem the damage is already done. But for many activities, feedback control fulfils a number of important functions.

4) Multiple Controls

Feed forward, concurrent, and feedback control methods are not mutually exclusive. Rather, they usually are combined into a multiple control systems. Managers design control systems to define standards of performance and acquire information feedback at strategic control points.

7.6. EVALUATION AND CONTROL PROCESS

The **evaluation and control process** ensures that a company is achieving what it set out to accomplish. It compares performance with desired results and provides the feedback necessary for management to evaluate results and take corrective action, as needed. This process can be viewed as a five-step feedback model.

1. **Determine what to measure:** Top managers and operational managers need to specify what implementation processes and results will be monitored and evaluated. The processes and results must be capable of being measured in a reasonably objective and consistent manner. The focus should be on the most significant elements in a process—the ones that account for the highest proportion of expense or the greatest number of problems. Measurements must be found for all important areas, regardless of difficulty.
2. **Establish standards of performance:** Standards used to measure performance are detailed expressions of strategic objectives. They are measures of acceptable performance results. Each standard usually includes a tolerance range, which defines acceptable deviations. Standards can be set not only for final output but also for intermediate stages of production output.
3. **Measure actual performance:** Measurements must be made at predetermined times.
4. **Compare actual performance with the standard:** If actual performance results are within the desired tolerance range, the measurement process stops here.

5. **Take corrective action:** If actual results fall outside the desired tolerance range, action must be taken to correct the deviation. The following questions must be answered:
    A. Is the deviation only a chance fluctuation?
    B. Are the processes being carried out incorrectly?
    C. Are the processes appropriate to the achievement of the desired standard? Action must be taken that will not only correct the deviation but also prevent its happening again.
    D. Who is the best person to take corrective action?

Top management is often better at the first two steps of the control model than it is at the last two follow-through steps. It tends to establish a control system and then delegate the implementation to others.

7.7. STRATEGY SHOULD BE:

1. **Consistency**

A strategy should not present inconsistent goals and policies. Organizational conflict and interdepartmental bickering are often symptoms of managerial disorder, but these problems may also be a sign of strategic inconsistency. Three guidelines help determine if organizational problems are due to inconsistencies in strategy:

• If managerial problems continue despite changes in personnel and if they tend to be issue-based rather than people-based, then strategies may be inconsistent.

• If success for one organizational department means, or is interpreted to mean, failure for another department, then strategies may be inconsistent.

• If policy problems and issues continue to be brought to the top for resolution, then strategies may be inconsistent.

2. **Consonance**

Consonance refers to the need for strategists to examine *sets of trends*, as well as individual trends, in evaluating strategies. A strategy must represent an adaptive response to the external environment and to the critical changes occurring within it. One difficulty in matching a firm's key internal and external factors in the formulation of strategy is that most trends are the result of interactions among other trends. For example, the day-care explosion came about as a combined result of many trends that included a rise in the average level of education, increased inflation, and an increase in women in the workforce. Although single economic or demographic trends might appear steady for many years, there are waves of change going on at the interaction level.

3. Feasibility

A strategy must neither overtax available resources nor create unsolvable sub problems. The final broad test of strategy is its feasibility; that is, can the strategy be attempted within the physical, human, and financial resources of the enterprise? The financial resources of a business are the easiest to quantify and are normally the first limitation against which strategy is evaluated. It is sometimes forgotten, however, that innovative approaches to financing are often possible. Devices, such as captive subsidiaries, sale-leaseback arrangements, and tying plant mortgages to long-term contracts, have all been used effectively to help win key positions in suddenly expanding industries. A less quantifiable, but actually more rigid, limitation on strategic choice is that imposed by individual and organizational capabilities. In evaluating a strategy, it is important to examine whether an organization has demonstrated in the past that it possesses the abilities, competencies, skills, and talents needed to carry out a given strategy.

4. Advantage

A strategy must provide for the creation and/or maintenance of a competitive advantage in a selected area of activity. Competitive advantages normally are the result of superiority in one of three areas: (1) resources, (2) skills, or (3) position. The idea that the positioning of one's resources can enhance their combined effectiveness is familiar to military theorists, chess players, and diplomats.

Position can also play a crucial role in an organization's strategy. Once gained, a good position is defensible meaning that it is so costly to capture that rivals are deterred from full-scale attacks. Positional advantage tends to be self-sustaining as long as the key internal and environmental factors that underlie it remain stable. This is why entrenched firms can be almost impossible to unseat, even if their raw skill levels are only average. Although not all positional advantages are associated with size, it is true that larger organizations tend to operate in markets and use procedures that turn their size into advantage, while smaller firms seek product/market positions that exploit other types of advantage. The principal characteristic of good position is that it permits the firm to obtain advantage from policies that would not similarly benefit rivals without the same position. Therefore, in evaluating strategy, organizations should examine the nature of positional advantages associated with a given strategy.

THE END!!!