

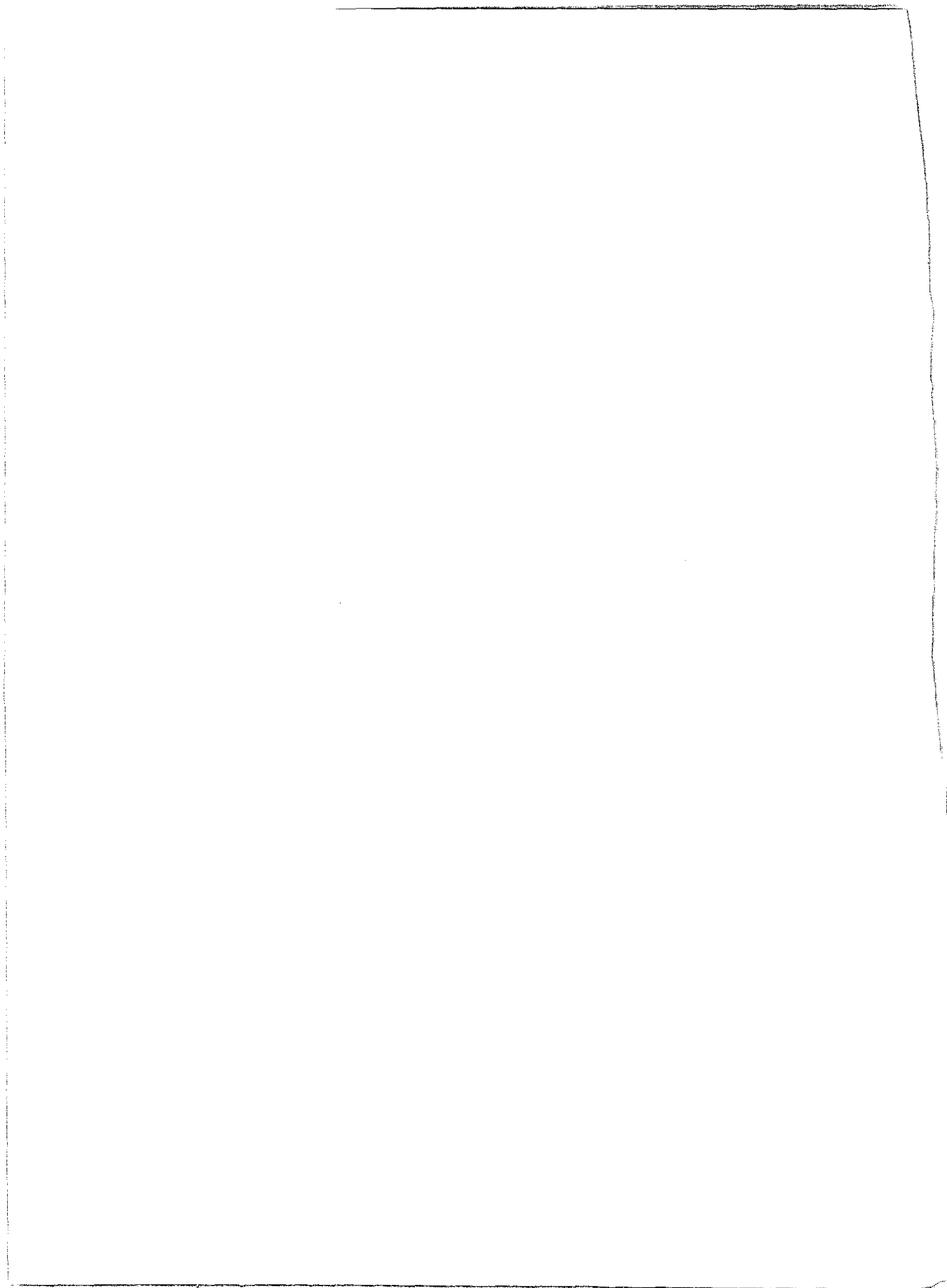
Strategic Management

M.Com. (Final)

Paper-7



**Directorate of Distance Education
Maharshi Dayanand University, Rohtak**



STRATEGIC MANAGEMENT

M.Com. (Final)

**Directorate of Distance Education
Maharshi Dayanand University
ROHTAK – 124 001**

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Strategic Management

Paper-7

Max. Marks.: 100

Time: 3 Hrs

Note: There will be three sections of the question paper. In section A there will be 10 short answer questions of 2 marks each. All questions of this section are compulsory. Section B will comprise of 10 questions of 5 marks each out of which candidates are required to attempt any seven questions. Section C will be having 5 questions of 15 marks each out of which candidates are required to attempt any three questions. The examiner will set the questions in all the three sections by covering the entire syllabus of the concerned subject.

Course Inputs

Unit-1 Strategic Management Process: Defining Strategy, Levels at which Strategy operates, Approaches to Strategic Decision making, Process of Strategic Management, Roles of Strategists in Strategic Management; Mission and purpose, Objectives and goals, Strategic Business Unit.

Unit-2 Environment and Organisational Appraisal: Concept of Environment and its components. Environmental Scanning and Appraisal; Organisational appraisal-its Dynamics, Considerations, Methods and Techniques. Structuring Organisational Appraisal, SWOT Analysis.

Unit-3 Strategy Formulation: Corporate level Strategies; Grand Strategies, Stability Strategies, Expansion Strategies, Retrenchment Strategies, Combination Strategies, Corporate Restructuring; Business level Strategies and Tactics.

Strategic Analysis and Choice: The Process of Strategic Choice, Corporate Level Strategic Analysis, Business Level Strategic Analysis, Subjective Factors in Strategic Choice, Contingency Strategy, Strategic Plan.

Unit-4 Strategy Implementation: Inter relationship between formulation and Implementation. Aspects of Strategic Implementation, Project Implementation, Procedural Implementation, Resource Allocation.

Strategy and Structures: Structural Considerations, Structures for Strategies; Organisational Design and Change.

Behavioural Implementation: Leadership Implementation, Corporate Culture, Corporate Politics and Use of Power, Personal values and Business Ethics.

Unit-5 Functional Implementation: Functional Strategies, Functional Plans and Policies, Marketing Plans and Policies, Financial Plans and Policies, Personnel Plans and Policies, Operations Plans and Policies.

Strategic Evaluation and Control: An Overview of Strategic Evaluation and Control, Techniques of Strategic Evaluation and Control.

Chapter 1

Strategic Management – An Introduction

Strategic management is the process by which an organisation formulates its objectives and manages to achieve them. Strategy is the means to achieve the organisational ends.

A strategy is a route to the destination viz., the “objectives of the firm”. Picking a destination means choosing an objective. Objectives and strategies evolve as problems and opportunities are identified, resolved and exploited.

The interlocking of objectives and strategies characterise the effective management of an organisation. The process binds, coordinates and integrates the parts into a whole. Effective organisations are tied by means-ends chains into a purposeful whole. The strategies to achieve corporate goals at higher levels often provides strategies for managers at lower levels.

Managers must have strategic vision to become strategic managers and thereby to manage the organisation strategically. Strategic vision is a pre-requisite of the strategic managers. Strategic vision implies a profound scanning ability of the environment in which the company is in i.e., knowing the objectives and values of the organisation stakeholders and bringing that knowledge into future projections and plans of the organisation. The managers strategic vision involves:

- The ability to solve complex and more complex problems;
- The knowledge to be more anticipatory in perspective and approach, and
- The willingness to develop options for the future.

Strategic management can be defined as the art and science of formulating, implementing, and evaluating cross-functional decisions that enable an organisation to achieve its objectives. As this definition implies, strategic management focuses on integrating management, marketing, finance/accounting, production/operations, research and development, and information systems aspects of a business to achieve organisational success. The term “strategic management” is used at many colleges and universities as the title to the capstone course in business administration, “business policy,” which integrates material from all business courses.

The strategic-management process consists of three stages: strategy formulation, strategy evaluation. Strategy formulation includes developing a business mission, identifying an organisation’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 implementation requires a firm to establish annual objectives, devise policies, motivate employees, and allocate resources so that formulated strategies can be executed; strategy implementation includes developing a strategy-supportive culture, creating an effective organisational structure, redirecting marketing efforts, preparing budgets, developing and utilizing information systems, and motivating individuals to action.

Strategy evaluation monitors the results of formulation and implementation activities and includes measuring individual and organisational performance and taking corrective actions when necessary. Although making good strategic decisions is the major responsibility of an organisation’s owner or chief executive officer, managers and employees both must also be involved in strategy formulation, implementation, and evaluation activities. Participation is a key to gaining commitment for needed changes.

Peter Drucker says the prime task of strategic management is thinking through the overall mission of a business.

. . . that is, of asking the question "What is our Business?" This leads to the setting of objectives, the development of strategies, and the making of today's decisions for tomorrow's results. This clearly must be done by a part of the organisation that can see the entire business; that can balance objectives and the needs of today against the needs of tomorrow; and that can allocate resources of men and money to key results.

The strategic-management process must be a people process to be successful! People, including all managers and employees, make the difference! The chief executive officer of Rock Well International explains, "We believe that fundamental to effective strategic management is fully informed employees at all organisational levels. We expect every business segment to inform every employee about the business objectives, the direction of the business, progress towards achieving objectives, and customers, competitors and product plans."

The strategic-management process can be described as an objective, logical, systematic approach for making major decisions in an organisation. It attempts to organise qualitative and quantitative information in a way that allows effective decisions to be made under conditions of uncertainty. Yet, strategic management is not a pure science that lends itself to a nice, neat, one-two-three approach.

Based on past experiences, judgment, and feelings, intuition is essential to making good strategic decisions. Intuition is particularly useful for making decisions in situations of great uncertainty or little precedent, or when highly interrelated variables exist, there is immense pressure to be right, or it is necessary to choose from several plausible alternatives. These situations describe the very nature and heart of strategic management.

Some managers and owners of businesses profess to have extraordinary abilities for using intuition alone in devising brilliant strategies. For example, Will Durant, who organised General Motors Corporation, was described by Alfred Sloan as "a man who would proceed on a course of action guided solely, as far as I could tell, by some intuitive flash of brilliance. He never felt obliged to make an engineering hunt for the facts. Yet at times he was astoundingly correct in his judgment". Albert Einstein acknowledged the importance of intuition when he said, "I believe in intuition and inspiration. At times I feel certain that I am right while not knowing the reason. Imagination is more important than knowledge, because knowledge is limited, whereas imagination embraces the entire world."

Although some organisations today may survive and prosper because they have intuitive geniuses managing them, most are not so fortunate. Most organisations can benefit from strategic management, which is based upon integrating intuition and analysis in decision making. Choosing an intuitive or analytical approach to decision making is not an either-or proposition. Managers at all levels in an organisation should inject their intuition and judgment into strategic-management analyses. Analytical thinking and intuitive thinking complement each other.

Operating from the "I've already made up my mind, don't bother me with the facts" mode is not management by intuition; it is management by ignorance. Drucker says, "I believe in intuition only if you discipline it. 'Hunch' artists, who make a diagnosis but don't check it out with the facts, are the ones in medicine who kill people, and in management kill businesses." In a sense, the strategic-management process is an attempt to duplicate what goes on in the mind of a brilliant intuitive person who knows the business. Successful strategic management hinges upon effective integration of intuition and analysis, as Henderson notes below:

The accelerating rate of change today is producing a business world in which customary managerial habits in organisations are increasingly inadequate. Experience alone was an adequate guide when changes could be made in small increments. But intuitive and experience-based management philosophies are grossly inadequate when decisions are strategic and have major, irreversible consequences.

The strategic-management process is based on the belief that organisations should continually monitor internal and external events and trends so that timely changes can be made as needed. The rate and magnitude of changes that affect organisations are increasing dramatically. Consider, for example, merger/acquisition mania, hostile takeovers, cellular phones, monoclonal antibodies, fiber optics, the aging population, taxes on services, computer technology, and the unification of Western Europe in 1992. To survive, all organisations must be capable of astutely identifying and adapting to

change. The strategic-management process is aimed at allowing organisations to effectively adapt to change over the long run.

In today's business environment, more than any preceding era, the only constant is change. Successful organisations effectively manage change, continuously adapting their bureaucracies, strategies, systems, products, and cultures to survive the shocks and prosper from the forces that decimate the competition.

Information technology and globalisation are environmental changes that are transforming business and society today. On a political map, the boundaries between countries are as clear as ever, but on a competitive map showing the real flows of financial and industrial activity, the boundaries have largely disappeared. Speedy flow of information has eaten away at national boundaries so that people worldwide readily see for themselves how other people live. People are traveling abroad more; ten million Japanese travel abroad annually. People are emigrating more; East Germans to West Germany and Mexicans to the United States are examples. We are becoming a borderless world with global citizens, global competitors, global customers, global suppliers, and global distributors!

The world is changing, and businesses must adapt to these changes or face extinction. The need to adapt to change leads organisations to key strategic-management questions, such as: What kind of business should we become? Are we in the right fields? Should we reshape our business? What new competitors are entering our industry? What strategies should we pursue? How are our customers changing? Are new technologies being developed that could put us out of business?

The history of business and industrial management is one of decision-making under ever increasing environmental turbulence. At each phase of such turbulence, management practices have been developed to successfully meet the impacts of the environment. The evolution of management from budget-based management to strategic management through corporate planning, long-range planning, strategic long-range planning, and strategic planning is a continuous picture of this development process.

Environmental Turbulences Management Strategy Interaction

The discussion of evolution of the planning process from budgetary and financial control through corporate planning to strategic management can best be initiated by referring to an article by three members of McKinsey & Company (1) which is diagrammatically depicted in Exhibit. 1.1.

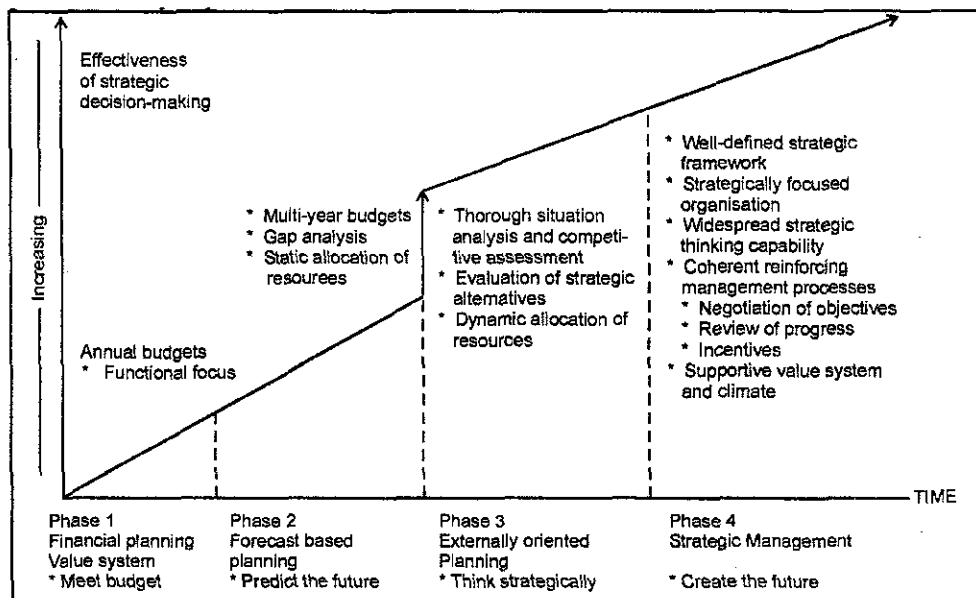


Exhibit 1.1: Phases in the Evolution of Strategic Planning

The phases shown in the Exhibit. 1.1 can be separated into two parts. In the first phase, a target, usually a financial

one, is set out for the year and limits are placed on what a divisional manager and his/her people are expected to achieve and to spend in the form of expenses or in capital expenditure to achieve the desired bottom line. Reviews of how closely the performance is keeping to the programme are made quarterly or sometimes even monthly. Such efforts are often tied to corporate targets relating to annual capital budgets, desired rates of return to shareholders' equity or investment. Likewise, activities such as employment, training, appraisals, and compensation of management are closely tied to this annual cycle. Operationally this is termed budgeting or budgetary control, practised during the earlier days of managerial evolution.

The implications of interaction between tempos in environmental change and the intensity of management control systems would be clear from Exhibit 1.2. Budgeting and financial control on an annual basis were created during phase 1: the stable environment. Soon, however, it was found that environmental change was registering an accelerating rates, and by and large the environment entered the transitional stage. While all segments of environment go through the same cycle: stable → transitional → turbulent → unstable, the rates of change for the segments are however different. For instance consumer behaviour or market may change at a rate quite different than technology, or competition, or employee attitude.

Man and his creation, society, abhor uncertainty. But change creates uncertainties, often great uncertainties. Historically, during the post-budget phase, depicted in Exhibit 1.1 by phase 2, while the technological segment continued to be fairly stable, other segments depicted a fairly unstable environment. Many managers, unable to face this uncertainty preferred to go back to the old rules of budgeting, even if there was a feeling that the system was fast becoming obsolete. Others opted for formal schedules of goal definition, environmental scanning, strategy formulation, in short, for formalised corporate planning, with the entire strategy of planning being based on forecast with the assumption of a fairly stable technology base.

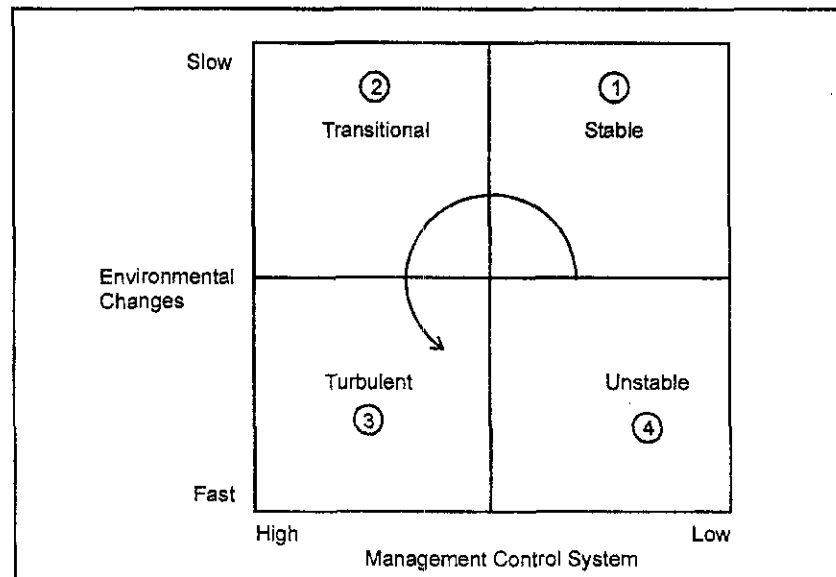


Exhibit 1.2 Accelerating Environmental Change

Budgeting

Budgeting is best understood in the context of time of development and use. In its early manifestation, a budget can be regarded as primarily a plan to reach a goal or objective and is perhaps best defined as a basic planning and control system.

In its later manifestation, budgeting forms a part of the strategic planning process, unlike the earlier manifestation when budgeting and budgetary management constituted a 'stand alone' planning and control system.

Budgeting is, in fact, a tool for running the activities of a firm systematically. It carefully looks at the resources available or within reach, decides upon the allocation of these resources (within the constraints of availability) to the

various activities in order that the desired objectives may be fulfilled. In consequence, comparison of the actuals against the budget also provides a basis of managerial control. Thus, a sales budget will indicate the volume of sales the company expects to achieve. This clearly leads to the allocation of resources to production and purchasing and, therefore, budgets for these activities. Simultaneously, the summation of the resources allocated to various component activities should indicate whether or not the total resources allocated obey the constraints of availability. For ease in operation and control, budgets are mainly formulated in financial terms.

Budgets are basically of two types:

- i. 'Static budget', based on a single estimate of sales and production, i.e., a single performance estimate.
- ii. 'Flexible budgets' reflecting different production and sales volumes. The following sets of information form the building blocks for a flexible budget.
 - a. Revenues, expenses and income for a number of levels of sales volumes.
 - b. Manufacturing costs for a corresponding number of production volumes.
 - c. Manufacturing costs adjusted to what they should have been for a recent actual production volume.

The major budget concerning all the significant activities of the firm, and usually for a period of one year, is the 'master budget'. The following is a schematic listing of all the supplementary budgets.

Operational	Capital
● Production budget	● Capital expenditure
● Inventory budget	● Allocation of funds
● Direct labour budget	● Management of funds
● Direct materials budget	
● Manufacturing overhead budget	
● Procurement budget	
● Sales budget (by products and departments)	
● Selling and distribution expense budget	
● Administrative expense budget	
● Other incomes and expenses budget	

Simultaneously, cash flow is budgeted through a cash flow budget showing budgeted receipts, outgoings, and balances on a short-term basis. Similarly, investment decisions and the expenses they entail tend to be monitored and controlled by a capital expenditure budget, showing project, yearly expense, and total capital expense budgeted, so that the actual outlays may be monitored project by project.

The master budget is summarised in two forms:

- i. The budgeted income and expenditure statement: showing total revenues, cost of goods sold, other costs broken down under major heads, and the budgeted profits.
- ii. The budgeted balance sheet showing annual assets and liabilities.

Budgetary Control

Since the objective of budgeting is to monitor and control the performance of the firm, the first step is to determine budget figures. Efficiency standards with regard to all the activities enumerated above are implicit in the budgetary projections. The estimated productivity figures are commonly based on standards of performance either derived from historical observations or computations from the firm's internal data, or from figures obtained based on financial statements of competitors (inter-firm comparisons). Other approaches are to base these on predetermined performance standards or from negotiations conducted within the management by objectives (MBO) framework.

For control purposes, it is not enough to evaluate the budget figures carefully. As Ackoff puts it, 'control is the evaluation of decisions after they have been implemented. It involves predicting the outcome of the decisions, comparing of it with the actual outcome, and taking corrective actions when the match is poor'. In a budgetary control system, the budgets are the predictions of the outcome of the contemplated decisions. The actuals are plotted against the budget. The differences are the variances, and corrective actions are taken when the variances are large and significant.

Financial Control

Like budgets and budgetary control, financial control operates using monetary figures. Initially designed to manage and control cash, it now provides the basis for control of many other functions. To enable financial control to be better utilised, any economic entity/corporation is usually subdivided into well-defined segments with clearly defined scope of activities entrusted to responsible individual managers. These become responsibility centres, and depending on the nature of the functions, are called costs centres, expense centres, activity centres, revenue centres, profit centres, investment centres, and the like.

The financial control system is built around a rather small number of key variables which, when carefully monitored, allow managers to track over a stipulated period the performance of the various functional activities and business units of the firm. These indicators are derived from the basic information compiled for assembling the budget.

A valuable tool in exercising financial control is the use of financial ratios both for assessment of the company's own financial performance and status, as also to compare them with similar companies. These ratios are divided into the following major groups:

- Liquidity ratios
- Leverage/capital structure ratios
- Profitability ratios
- Turnover ratios

The major weakness of budget and budgetary control is their short time horizon. In the scenario in which it was originally initiated, the environment was comparatively less turbulent, and competition was less intense. It seemed adequate to look after a particular year's business and performance. References to a possible change in direction in future, capital investment spreading over successive years, easing out of weakening activities etc. were comparatively less important, if not considered entirely irrelevant in the context of Budgetary Control. Refixing budgetary figures ab initio each year was also considered unnecessary. It was enough to build on previous years' figures, suitably adjusting and updating these.

With years, both environmental turbulence and competitive pressures have increased significantly. Short time-span budgetary control was no longer considered adequate. A much longer horizon began to be considered necessary not only for a firm's well-being, but even for its survival. As a logical corollary, corporate planning supplanted budget and budgetary control as a basic tool for planning and monitoring a firm's performance.

Budgeting did not, however, lose all its relevance. With corporate planning and strategic planning as a later development, budgeting and budgetary control became the principal arm of action plans at the implementation and control stages. A new approach to budgeting required the use not only of historic data but, for the establishment or emergence of commitments arising out of the strategic or corporate plan, it also called for negotiations conducted within the framework of management by objectives (MBO).

Meanwhile, the very process of budget preparation has gone through stages of refinement. New concepts have been introduced. These include the concept of flexible budgeting which permits the original standards used to measure performance to be modified with changes in the actual level of operations. Similarly Zero-Base Budgeting (ZBB) establishes a set of very comprehensive rules to force managers to justify their budgetary allocations from base zero, rather than defining the new budget incrementally.

Resort to financial measures and a total preoccupation with budgetary control for a particular year has left managers overly preoccupied with profitability as the key criterion for measurement of the firm's and hence their own performances. This trend has, however, continued into the corporate planning phase, when ROI has tended to become the all important preoccupation of management. The result has been that too many firms have, in their preoccupation with ROI, inadvertently weakened their asset base and discouraged necessary investments by compromising the long-term competitive standing of the firm in exchange for a hefty ROI for the following year. The peculiar standing of executive management with shareholders in many countries, together with the behaviour of the share market where immediate profit-taking becomes the all engrossing consideration as also taxation policies of many governments discouraging capital gains, has only encouraged this tendency. Indeed, an immediate sure return versus long-term risk of increased return and growth tended to dichotomize management attitude and policy, as also the government attitude in many companies and states.

Firms which depend entirely on budgetary and financial control measurements for planning purposes are exceedingly vulnerable to falling into the near-sighted ROI traps. Unless these are clear articulations of the business's competitive spirit and strategy, properly understood at all organisational levels, a pure budgeting and financial control system will prove inadequate in warding off undesirable consequences.

Corporate Planning

To assist a sharp definition and consideration of the Corporate Planning Process, we refer to Exhibit 1.3. The explanation of the steps follows.

Objectives

Before discussing the planning process and the objective setting, a few factors perhaps justify early consideration and emphasis.

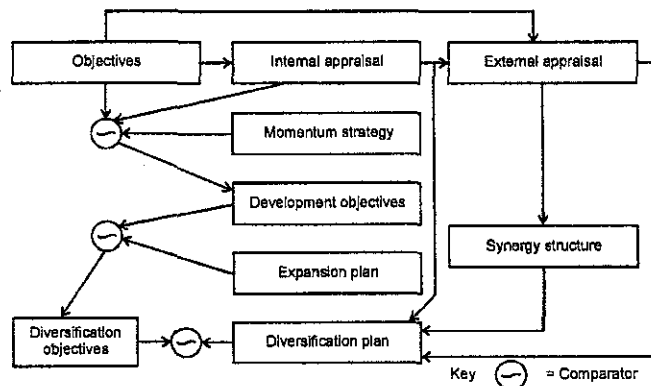


Exhibit 1.3: The Total Corporate Plan Development Process

- i. The process is being undertaken in the context of changing environment, based on forecast. Hence the plan is being drawn up in the context of partial ignorance.

- ii. As the planning horizon elongates and extends into the future, the uncertainty and ignorance impinging upon the forecasting process increases, thereby putting the reliability and credibility of results of the forecasting process increasingly at risk. This puts an effective upper limit on the planning horizon – if the plan is to function as an effective instrument of control. On the other hand, the weaknesses of annual planning or budgeting are manifest and have already been discussed, indeed, the practice is overwhelmingly in support of a five year planning horizon. However, the horizon is partially dependent on the investment horizon, a time period necessary for investment to start yielding a reasonable revenue. With a short investment horizon, therefore, a three year planning horizon is also in practice.
- iii. A corporation is a purposive organisation, and it is evident, therefore, that efficient utilization of the resources at its disposal towards fulfilment of its objective(s) should be its purpose.

This brings us squarely into the arena of objective setting. The setting up of objective(s) is not however, an ad hoc decision, but the culmination of a process. It would perhaps be useful at this stage to consider this entire process.

The concept of a corporation being a purposive organisation, and the efficient utilisation of resources as the path to achieving its objectives, invariably brings forward the concept of strategy.

It is perhaps useful to subdivide objectives into a few basic divisions, e.g.

- The primary, or profit objective of the business, set in advance of strategy.
- The secondary objectives, largely narrative, again set in advance of strategy. (This would include economic, social, technological, etc. objectives.)
- Goals that are time-assigned targets derived from the strategy.
- Standards of performance (often coterminous with goals) assigned to particular individuals.

Primary or Profit Objectives

When considering profit objective, two aspects require attention:

- a. The philosophy of profit—namely that it is not simply one of short-term gains but of long-term profit growth allowing for corporate renewal.
- b. The dimensional aspects of profit—quantity and efficiency. An efficiency target may be return-on capital employed with further qualification on the time period and the trend. The quantity dimension, qualified for similar time period, linked to efficiency becomes a good dimensional measure of profit. A similar quantitative measure of profit target would be earning per share.

A number of factors should be borne in mind when setting the profit target.

- Trends over previous years.
- Progress by other firms of similar size or in the same industry.
- Performance of leading companies quoted on the stock exchange.
- Opportunities for profitable investments elsewhere.
- The ambitions of the chief executive.
- The strategic need for growth to reach a size that enables the company to at least maintain its position of influence in its trade.
- Rates of inflation.

Once the profit objectives have been set for the company, it should be followed up with objectives of the divisions and subsidiaries.

Secondary Objectives

Secondary objectives are descriptive and attempt to set out the key elements of the business of the future. These examine the nature and scope of the business, the geographical sphere of operation, and some of the key factors about the company. These include statement of the way the company intends to conduct its relations with its employees, customers, and society, as also the concept of moral and ethical standards it proposes to adopt.

Also part of the secondary objective is that the company's attitude to technology, in the context of the business it is in, is stated unequivocally.

Goals

If we regard objectives as the map reference, goals may be considered to be the landmarks and milestones that the firm must pass as it progresses along the chosen route.

In effect, a network of goals provides a model of the company's strategy over the whole period of the plan. Some possible definitions or measures of goals would be:

- Percentage market share (by products and/or country).
- A ratio, such as return on sales.
- An absolute figure for sales.
- A minimum figure for customer complaint.
- A maximum figure for hours lost in industrial disputes.
- A labour productivity ratio.
- Total number of employees.
- A maximum employee 'wastage' rate.
- A standard cost.
- A cost reduction target.
- A date by which a particular event must take place (e.g. a new product launch).
- Quantified values of some of the financial ratios would also constitute measures and definitions of goals.

Standards of Performance

Standards of performance are essentially derivations from goals. While a goal is a corporate, divisional or departmental target, a standard of performance is something which is individually assigned to a named person. Some times the personal standard may be something which is coterminous with the corporate goal. For instance, a market share goal may be assigned to the product manager responsible. Sometimes the standard may be something derived from the goal: splitting up the corporate target and making individuals responsible for each segment (for instance the personal sales target assigned to a representative). Frequently, these are time-assigned tasks. The overall concept may be visualised as a network of targets, all interlinked in some way to the company's primary and secondary objectives.

The importance of personal standards is that they provide a tool for ensuring that plans are converted into tasks people can perform. A direct link is thus established between the task of the individual persons and the total corporate strategy.

It is also important to realise the relation between the system of personal standards, as briefly described above, and the technique of 'management by objectives' (MBO) developed by Humble. Personal standards as a system is essentially a simple variant of MBO, although its aims are narrower.

The Appraisal Process

It has already been briefly mentioned how the comparatively stable technology base accompanied by an unstable, indeed turbulent, environment in the corporate segments gave rise to the felt need for formalized or informal environmental scanning. Also, the plan is a projection of the company's performance and expectations into the future based on the planned strategy. Essentially, therefore, the appraisal process consists of the following major elements:

- External appraisal
 - Internal appraisal
 - SWOT analysis
 - Gap analysis
 - Forecasting
- } Together comprising
} environmental analysis

Environment monitoring and analysis can perhaps be depicted in a concentric diagram (Exhibit 1.4). In Exhibit 1.4, everything except the internal environment is a constituent of the external environment.

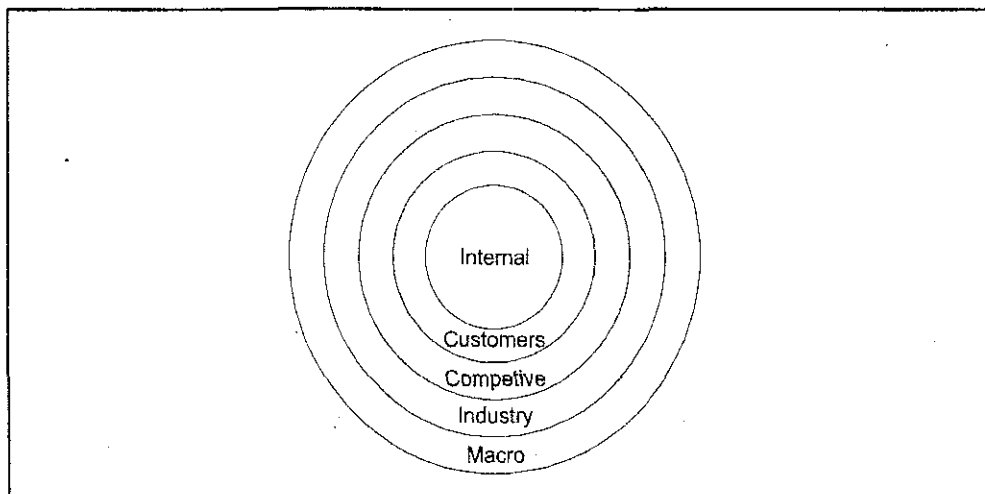


Exhibit 1.4: Environments to be Monitored

External appraisal is carried out to evaluate and judge the external environment both in regard to existing activities and also new opportunities for new products and activities. It thus provides the basis for evaluating the scope, opportunities, threats, etc.

Internal Appraisal

It is basically to evaluate the firm's own capacities and to meet the requirements of existing activities efficiently and effectively; and also to meet the challenges or threats indicated on the basis of external appraisal. It further identifies the strengths, weaknesses, and resources of the company keeping the objectives, the external environment, and the forecast in view; the strengths to be utilised, the weaknesses to be corrected.

It is important to realise that although there is interrelationship between internal appraisal and environment analysis,

the two are really different and isolated from each other. In effect, internal appraisal is best done against the background of environment analysis. A number of basic concepts should be borne in mind as the appraisal progresses, and performance rated against them.

- It should always be assumed that there might be a better way of doing something until the contrary is proved.
- It is usually a relatively small amount of effort that produces most of the returns. Usually, around 80 percent of the profit comes from, say, 20 per cent of effort, the remaining 20 percent requiring the balance 80 percent effort. Any action that reduces the amount of less profitable action should lead to corporate improvement. This, in effect, is an illustration of the ‘Pareto Principle’.
- Often knowledge of what is being done is not as perfect as managers within a company believe. One of the tasks of corporate appraisal should be to ascertain the facts.
- When what is being done has been established, the question why should be asked.
- The future is more important than the present where the trends and effects on the aspects studied can be foreseen.
- The appraisal should cover all aspects of the company.

The following factors should be considered as part of the internal appraisal:

1. **Trends of results:** For example, trends in profits, sales, capital employed, and the various commonly used ratios. This will show whether the company is improving or worsening in its performance.
2. **Sources of profit:** This analysis should be mostly marketing oriented.
3. **Risk:** Arising from such factors as the bulk of profit coming from a single product, over-dependence on a single market, too few customers for a product, raw materials difficulty varying from difficulty of supply, duty, shortage, to over-dependence on one supplier, other market risks, technological risks not only in product obsolescence but in production processes, etc.
4. **Manufacturing activity:** The purpose being production cost reduction, consideration of the process should include, apart from the manufacturing process, plant and equipment appropriateness and efficiency, correct labour deployment and efficiency, also the raw materials, the standards set for their purchase and the efficiency of the company as buyer (skills, technology absorption creation).
5. **Rationalisation of resources:** This involves rationalisation relocations of facilities, plants and building, distribution depots, supply and demand patterns, etc.
6. **Organisation and management structure:** This involves studying the basic organisational structure, assessment of managerial capabilities, the company’s labour relations, company’s relation with its trade unions, morale of employees, corporate motivation, etc.
7. **Financial resources:** Study of the company’s liquid resources and expected future cash-flow position.
8. **Corporate capability:** This is brought out in the analysis of the company’s synergy structure.
9. **Systems:** This would involve assessment of the formal and informal systems and communications, authorities and participation within the company.
10. **Use of resources:** This essentially involves a study of allocation of resources between the products and a comparison of this with their real profit contribution. Resources here mean not only money, building, and plant, but also what are probably the scarce resources of management talent, capability, and technical skills.
11. **Skills and technology:** This refers to the availability of the required technology in the organisation, as also the

specialised skills for the technology absorption, adaptation, and creation.

Internal appraisal should also include the following:

- a. *The organisation climate and culture:* Whether this is compatible with the environment at large. This is an area in particular where a shift in either the organisational climate or of the environment surrounding it and the consequent incompatibility may prove disastrous or near disastrous.
- b. *A shift in organisational leadership:* Such a shift within an unchanged organisational culture may again produce wasting conflicts, often leading to a decrease in efficiency which, once identified, requires considerable effort and internal readjustment to correct.

Internal Appraisal

Customer environment: The scanning should include the following:

- Tracking customer complaints and compliments.
- Monitoring return rates.
- Listening to customer needs and concerns.
- Extent of quality improvement/maintenance/deterioration as reflected in customer reactions.
- Extent of competitive pressures from possible substitutes, as reflected in customer reaction.

Competitive environment: Surveillance of competitive environment should include consideration of:

- Competitor profile.
- Market segment pattern.
- Trend in market shares.
- Research and development trends.
- Emergence of new competitors.
- Threat through possible emergence of new substitutes.

Industry environment: Industry environment monitoring should include the following:

- Structure of the industry.
- How is the industry financed.
- Changes in the degree of government regulations.
- Changes in the typical products offered by the industry.
- Changes in typical industry marketing strategies and techniques.
- Trends in the total market for the industry.

Macro environment: Macro environment surveillance should include the following:

- Social factors, e.g. demographic changes.
- Technological factors.
- Economic factors, e.g. prime interest rates; consumer price index, etc.
- Political factors, e.g. increases or decreases in government regulations and

control, taxation laws, etc.

- Social factors, e.g. awareness about environment, etc.

Forecasting

As corporate planning extends to a firm's activities into the quite distant future, perhaps five years or so, it will be realised that there is need for forecasting of sales into these years. These forecasts of the product or industry sales and the deductions from these of the company's expected sales or planned sales would determine the planning of resources.

These forecasts may be of products already on sale production by the company; products on the same or similar lines which the company may take up, products currently in the research and development stage, or products the company may take up for diversification. Depending on the status of the product vis-a-vis the company's actions, plans or intentions, the forecasts would extend to or extend over varying time periods into the future. Also, an exact knowledge of the product attribute will vary accordingly.

All forecasts project into the future and hence are subject to uncertainty. The degree of uncertainty depends considerably on how far into the future the forecast extends and the status of knowledge of the product attributes.

Before discussing forecasting methods, however, it is important to emphasise the difference between forecast and market share. Forecast is directly a projection of anticipated sales. It is thus independent of how the market itself grows or changes. Market share is a derivative of the combined effects of sales forecast and change in the volume of total market. Market share is an important driver for the process of strategy formulations.

All products usually go through a life cycle with a general shape such as that shown in Exhibit 1.5.

It is easy to realise that for any sales forecast of any existing product it is important to find out the phase of the product life cycle that the product is in. There are, however, three difficulties, namely

- Determining the phase the product is in.
- Determining the duration of the various time phases— which are dependent on many external factors.
- Actions which can be taken by the company to extend and modify the life cycle.

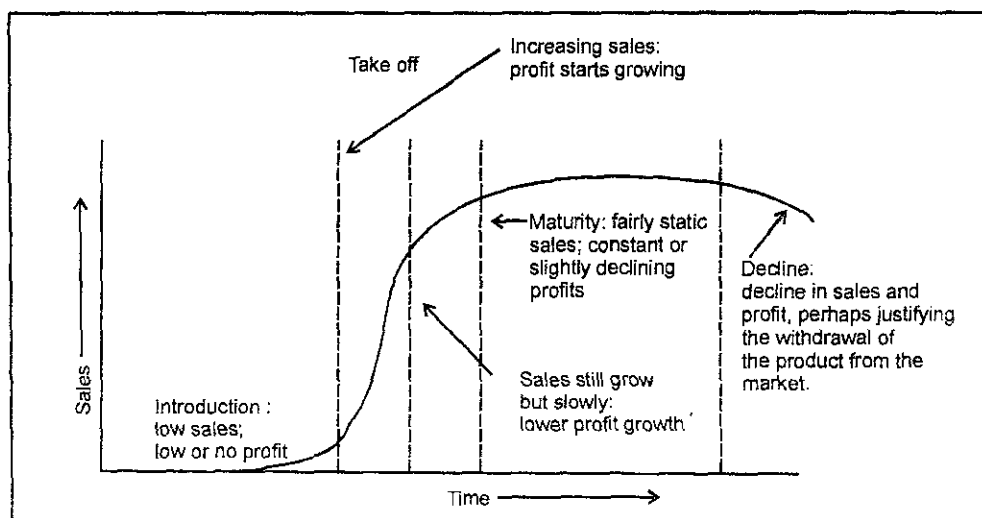


Exhibit 1.5: The Product Life Cycle

Forecasting Methods

1. Statistical Projections

This methodology is based on past data and can assume increasing sophistication as follows:

Trend Analysis

i. Simple growth pattern

This is quite useful for short-term forecasts, say for instance, for a few months, particularly to gain a perspective of the future prospects.

This method is based on the average annual growth rate, calculated over a period, worked out simply by expressing the latest year as an index of the earliest and correcting out for the erratic factor.

ii. Moving averages

In it the seasonal or cyclical pattern is eliminated by obtaining a smooth underlying trend for twelve months. Then, for each advancing month or quarter, etc. the data for the same period is added and the data for the corresponding period at the tail end is eliminated and a fresh trend line is worked out.

iii. Exponential smoothing

This method is in concept the same as moving averages, except that the average is exponentially weighted so that the more recent data is given a greater weightage, and the past forecasting error is taken into account in each successive period.

iv. Mathematical trends

Mathematical trends are methods in which a mathematical fit is used to express the past data. Some of the methods of using mathematics with increasing complexity are as follows:

- Simple regression model

In this, model, a dependent variable (sale) is expressed as a mathematical function of a second variable (say year, or GNP), This function may take any form, e.g.

* linear, $Y = a + bx$;

* exponential, $Y = e^{a+bx}$; or for computational ease,
 $\log_e Y = (a+bx)(\log_e e) = a+bx$;

* quadratic, $Y = a + bx^2$;

* cubic, $Y = a + bx + cx^2 + dx^3$, etc.

- Multiple Regression Model

A multiple regression model is applicable when the dependent variable (sale) is a function of two or more independent variables (GNP, sale of steel, etc.).

Thus, for two independent variables, the functional form would be, $Y = a + b_1 x_1 + b_2 x_2$

This functional form may also be non-linear, but in most instances, particularly for computational purposes, these can be transformed into linear forms.

The advantage of mathematical regressions (both simple and multiple) is that their fit may be statistically tested.

- Auto-regressive Schemes:

An auto-regressive scheme is a method of regression where the dependent variable is a function of past values of the same variable with increasing time lags. Thus the general form is,

$$Y_t = a_1 + b_1 Y_{t-1} + b_2 Y_{t-2} \dots + b_k Y_{t-k} + \dots + U_t$$

2. Econometric Models

In this method, the dependent variable is expressed through a system of equations involving several independent variables, themselves dependent on one another.

Thus for example, the interdependencies of the dependent and independent variable may take the following form

Sales = $f(\text{GNP, Price, Advertising})$

Production cost = $f(\text{Number of units produced, inventories, labour costs, material cost})$

Selling expenses = $f(\text{Advertising, other expenses})$

Advertising = $f(\text{Sales})$

Price = $f(\text{Production cost, selling expenses, administrative overhead, profit})$

In econometric models, we are faced with many tasks similar to those in multiple regression analysis. These tasks include:

1. Determining which variables to include in each equation.
2. Determining the functional form (e.g., linear, exponential, logarithmic, etc.) of each of the equations.
3. Checking the validity of the assumptions involved.
4. Estimating simultaneously the parameters of the equations.
5. Testing the statistical significance of the results.

Input-output method

The input-output model is a special type of econometric model, in which a number of inputs are chosen, and for each relationship the quantities of a number of different inputs are related to quantities of a number of different outputs through linear relationships. The inputs being independent variables, the outputs would be the forecasted dependent variables.

End-use method

In end-use method, the product for which demand is to be forecast is related to the various end uses to which it is put and the quantitative relationship between units of the product and corresponding units of the end-use product is established. This relationship is known as the bridging factor. The projected demand of the end-use product over the forecasting period is now obtained and worked backwards to obtain the demand forecast of the product.

An example will make the procedure clear. Suppose it is desired to project the demand forecast for forging steel over a forecasting interval. It is easy to list the different end products in which forged steel is used, e.g. automobiles (classified into trucks, LCVs, passenger cars, etc.), railway engines, 3 wheelers, motorcycles and cycles. It is also

possible to establish the number of kilogrammes of forged steel required per unit of these end products, giving the bridging factor. Once bridging factors have been established, demand projection of the different end products will enable demand forecast of forged steel to be determined.

It will be seen that there is considerable similarity between input-output analysis and the end-use method. A major obvious difference is that whereas in input-output analysis, the inputs are the independent variables, in the end-use method, the position is reversed. Also, in the input-output method, multiple inputs and outputs are considered simultaneously, any output having one or more inputs, just as any input may be related to one or more outputs. As against that, in the end use method a single product is considered and is related to all the end products which have significant requirement of the product. The forecast derivation of the end-use method is thus more direct and data requirement is often less.

Both the methods, it may be mentioned, are extremely important and significant, having extensive use in forecasting.

3. Marketing and Market Research Methods

The forecasting methods discussed till now are all based on projections based on past data, either of the product itself, or of the industry together with models of their relationship with one or more independent variables, established statistically or through causal analysis based on economic logic and tested statistically.

Another source of possible forecast for future sales can, however, be through direct contact with the existing or prospective market through variations of market analysis and market research. Some of these are briefly described below:

i. Analysis of estimates submitted by field salesmen

For an existing product, in a fairly known marketing environment, the estimates of future sales submitted by field salesmen, properly filtered and analysed, provide a fairly satisfactory basis for short-term forecasting.

ii. Comparative studies

A useful forecasting method is to examine the performance of something similar to the item being forecast. Thus a company launching, say, a new cough mixture, would find it useful to study the price, promotion, and progress of other cough mixtures, or similar products introduced during the past five years.

iii. Leading indicator

The leading indicator is indeed very akin to an econometric method except that it tends to be qualitative and largely subjective. A leading indicator is an event which always precedes an event of another type, thus giving prior warning of change. Thus the fast pace of rural electrification and the creation of a succession of low and medium capacity TV relay stations, providing extensive rural coverage for television in India, would be a sure indication of surge in demand for television sets; particularly black and white TV sets.

iv. Experimental market research

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The disadvantage of such tests is that while a true experiment eliminates all variables except those being measured, this is not always possible for such experiments. Also the source of inaccuracy creeping in through sampling error is ever present.

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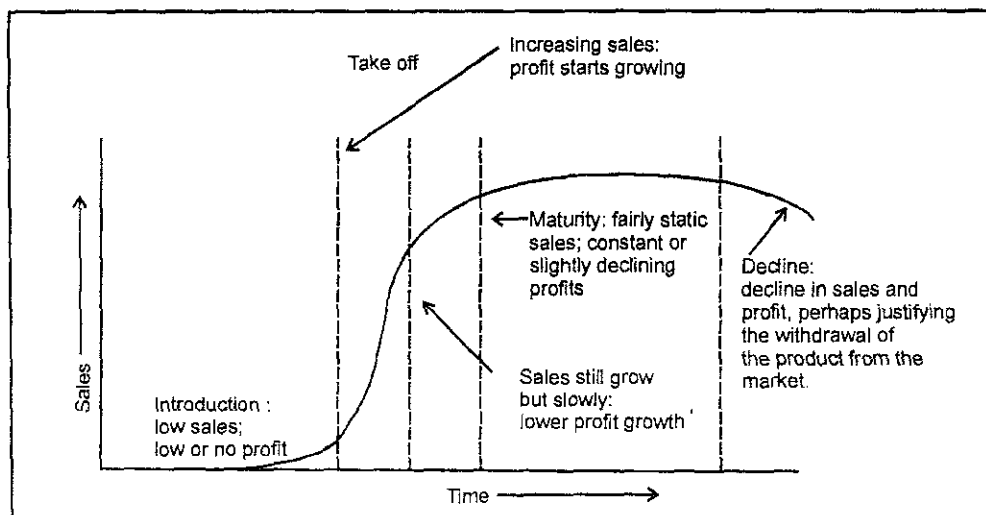


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The disadvantage of such tests is that while a true experiment eliminates all variables except those being measured, this is not always possible for such experiments. Also the source of inaccuracy creeping in through sampling error is ever present.

v. Intention-to-buy surveys

These may be used for both consumer and industrial goods. There are two major uses:

- a. To obtain information about proposed new products, both to assess their potential as also to verify or obtain information on product attribute suitability, need for change, product placement, etc.
- b. To obtain an index about their market acceptance vis-a-vis competitive products which can be related to actual performance and guide both the forecast and marketing strategy.

A pitfall is that an interviewee's reactions during interview may be widely divergent from his/her behaviour at the time of actual purchase.

vi. Marketing judgements

There are many occasions where little or no data exist on which to base a forecast of a product or environmental event, but where the knowledge of the company's employees can be called upon, or when common sense can be used to forecast bands of possible results based on some other data. Indeed, this can be further refined to quantify 'judgement' by building a subjective demand curve. Its accuracy may be questioned, but its usefulness, in the absence of any constructive alternatives is underivable.

4. Technological Forecasting

This is useful for forecasts for the comparatively distant future. Indeed, the term 'technological' forecasting is rather loosely formulated, since it may be used to forecast not only a technology but also matters of nontechnical interest.

Since it is a forecast of a comparatively distant future, the uncertainty surrounding it is consequently greater. A technological forecast should therefore not usually be a prediction of what will happen, but of what is possible and what can be made to happen. It is thus a guide to catalyse strategic leadership vision rather than an operating methodology.

When technical, it often provides a guide to action on what can be made to happen and serves as an invaluable aid to a visionary strategic leader and decision-maker in times of discontinuity.

Defining Strategy and Other Key Terms

The word strategy is derived from the Greek word "Strategia", which was used first around 400 B.C. This connotes the art and science of directing military forces. The strategy, according to a survey conducted in 1974 which asked corporate planners to define what they meant by strategy, "includes the determination and evaluation of alternative paths to an already established mission or objective and eventually, choice of the alternative to be adopted." Simply put, a strategy outlines how management plans to achieve its objectives. Strategy is the product of the strategic management process. Generally, when we talk of organisational strategy, it refers to organisation's top level strategy. However, strategies exist at other levels also.

Chandler made a comprehensive analysis of interrelationships among environment, strategy, and organisational structure. He analysed the history of organisational change in 70 manufacturing firms in the US. While doing so, Chandler defined strategy as: "The determination of the basic long-term goals and objectives of an enterprise and the adoption of the courses of action and the allocation of resources necessary for carrying out these goals". Chandler refers to three aspects.

- Determination of basic long-term goals and objectives.
- adoption of courses of action to achieve these objectives, and
- allocation of resources necessary for adopting the courses of action.

Professor Ansoff is a well-known authority in the field of strategic management and has been a prolific writer for the last four decades. In one of his earlier books, *Corporate Strategy* (1965), he explained the concept of strategy as: "The common thread among the organisation's activities and product-markets . . . that defines the essential nature of business that the organisation was or planned to be in future".

Ansoff has stressed on the commonality of approach that exists in diverse organisational activities including the products and markets that define the current and planned nature of business.

Andrews belongs to the group of professors at Harvard Business School who were responsible for developing the subject of business policy and its dissemination through the case study method. Andrew defines strategy as: "The pattern of objectives, purpose, goals and the major policies and plans for achieving these goals stated in such a way so as to define what business the company is in or is to be and the kind of company it is or is to be". This definition refers to the 'business definition', which is a way of stating the current and desired future position of company, and the objectives, purposes, goals, major policies and plans required to take the company from where it is to where it wants to be.

Another well-known author in the area of strategic management was Glueck, who was a Distinguished Professor of Management at the University of Georgia till his death in 1980. He defined strategy precisely as: "A unified, comprehensive and integrated plan designed to assure that the basic objectives of the enterprise are achieved". The three adjectives which Glueck has used to define a plan make the definition quite adequate. 'Unified' means that the plan joins all the parts of an enterprise together, 'comprehensive' means it covers all the major aspects of the enterprise, and 'integrated' means that all parts of the plan are compatible with each other. Michael Porter of the Harvard Business School has made invaluable contributions to the development of the concept of strategy. His ideas on competitive advantage, the five-forces model, generic strategies, and value chain are quite popular. He opines that the core of general management is strategy, which he elaborates as: "... developing and communicating the company's unique position, making trade-offs, and forging fit among activities".

Strategic position is based on customers' needs, customers' accessibility, or the variety of a company's products and services. A company's unique position relates to choosing activities that are different from those of the rivals, or to performing similar activities in different ways. However, a sustainable strategic position requires a trade-off when the activities that a firm performs are incompatible. Creation of fit among the different activities is done to ensure that they relate to each other.

It must be noted that the different approaches referred to above to define strategy cover nearly a quarter of a century. This is an indication of what a complex concept strategy is and how various authors have attempted to define it. To put it in another way, there are as many definitions as there are experts. The same authors may change the approach they had earlier adopted. Witness what Ansoff said 19 years later in 1984 (his earlier definition is of 1965): "Basically, a strategy is a set of decision making rules for the guidance of organisational behaviour".

We have tried to give you an assortment of definitions out of the many available. Rather than an assortment, it may be more appropriate to call this section a bouquet of definitions and explanations of strategy. Each flower (definition) is resplendent by itself yet contributes synergistically to the overall beauty of the bouquet. The field of strategy is indeed fascinating, prompting an author to give the title — "What is Strategy and does it matter?" — to his thought-provoking book, Drucker goes to the extent of terming the strategy of an organisation as its "theory of the business".

By means of the deeper insight that the authors have developed through years of experience and thinking, they have attempted to define the concept of strategy with greater clarity and precision. This comment is valid for most of the concepts in strategic management since this discipline is in the process of evolution and a uniform terminology is still evolving.

By combining the above definitions we do not attempt to define strategy in a novel way but we shall try to analyse all the elements that we have come across. Strategy may be summarised as follows:

- a plan or course of action or a set of decision rules forming pattern or creating a common thread,
- the pattern or common thread related to the organisation's activities which are derived from its policies, objectives and goals,
- related to pursuing those activities which move an organisation from its current position to a desired future state,
- concerned with the resources necessary for implementing a plan or following a course of action, and
- connected to the strategic positioning of a firm, making trade-offs between its different activities, and creating a fit among these activities.

Strategists are individuals who are most responsible for the success or failure of an organisation. Strategists have various job titles, such as chief executive officer, president, chairman of the board, executive director, chancellor, dean or entrepreneur. Strategists differ as much as organisations themselves, and these differences must be considered in the formulation, implementation, and evaluation of strategies. Strategists differ in their attitudes, values, ethics, willingness to take risks, concern for social responsibility, concern for profitability, concern for short-run versus long-run aims, and management style. Some strategists will not consider some types of strategies due to their personal philosophy.

Mission Statements

Mission statements are "enduring statements of purpose that distinguish one business from other similar firms. A mission statement identifies the scope of a firm's operations in product and market terms." It addresses the basic question that faces all strategists: "What is our Business?" A clear mission statement describes the values and priorities of an organisation. Developing a business mission compels strategists to think about the nature and scope of present operations and to assess the potential attractiveness of future markets and activities. A mission statement broadly charts the future direction of an organisation.

External Opportunities and Threats

Other key terms in our study of strategic management are *external opportunities* and *external threats*. These terms refer to economic, social, political, technological, and competitive trends and events that could significantly benefit or harm an organisation in the future. Opportunities and threats are largely beyond the control of a single organisation, thus the term "external." The computer revolution, biotechnology, population shifts, changing work values and attitudes, space exploration, and increased competition from foreign companies are examples of opportunities or threats for companies. These types of changes are creating a different type of consumer and consequently a need for different types of products, services, and strategies. Other opportunities and threats may include the passage of a new law, the introduction of a new product by a competitor, a national catastrophe, or the declining value of the dollar. A competitor's strength could be a threat. Unrest in Latin America, rising interest rates, or the war against drugs could represent an opportunity or a threat.

A basic tenet of strategic management is that firms need to formulate strategies to take advantage of external opportunities and to avoid or reduce the impact of external threats. For this reason, identifying, monitoring, and evaluating external opportunities and threats is essential for success.

Internal Strengths and Weaknesses

Internal strengths and *internal weaknesses* are controllable activities within an organisation that are performed especially well or poorly. Management, marketing, finance/accounting, production/operations, research and development, and information systems activities of a business are areas where internal strengths or weaknesses arise. The process

of identifying and evaluating organisational strengths and weaknesses in the functional areas of a business is an essential strategic-management activity. Organisations strive to pursue strategies that capitalise on internal strengths and improve on internal weaknesses.

Strengths and weaknesses are determined relative to competitors. "Relative" deficiency or superiority is important information. Also, strengths and weaknesses can be determined by elements of "being rather than performance." For example, a strength may involve ownership of natural resources or a historic reputation for quality. Strengths and weaknesses may be determined relative to a firm's own objectives. For example, high levels of inventory turnover may not be a strength to a firm that seeks never to stock-out.

Long-term Objectives

Objectives can be defined as specific results that an organisation seeks to achieve in pursuing its basic mission. Long-term means more than one year. Objectives are essential for organisational success because they provide direction, aid in evaluation, create synergy, reveal priorities, allow coordination, and provide a basis for effective planning, organising, motivating, and controlling activities. Objectives should be challenging, measurable, consistent, reasonable, and clear. In a multidivisional firm, objectives should be established for the overall company and for each division.

Annual Objectives

Annual objectives are short-term milestones that organisations must achieve to reach long-term objectives. Like long-term objectives, annual objectives should be measurable, quantitative, challenging, realistic, consistent, and prioritised. They should be established at the corporate, divisional, and functional level in a large organisation. Annual objectives should be stated in terms of management, marketing, finance/accounting, production/operations, research and development, and information systems accomplishments. A set of annual objectives is needed for each long-term objective. Annual objectives are especially important in strategy implementation, whereas long-term objectives are particularly important in strategy formulation. Annual objectives represent the basis for allocating resources.

Policies

The final key term to be highlighted here is *policies*—the means by which annual objectives will be achieved. Policies include guidelines, rules, and procedures established to support efforts to achieve stated objectives. Policies are guides to decision making and address repetitive or recurring situations.

Policies are most often stated in terms of management, marketing, finance/accounting, production/operations, research and development, and information systems activities. Policies can be established at the corporate level and apply to an entire organisation, at the divisional level and apply to a single division, or at the functional level and apply to particular operational activities or departments. Policies, like annual objectives, are especially important in strategy implementation because they outline an organisation's expectations of its employees and managers. Policies allow consistency and coordination within and between organisational departments.

Chapter 2

Levels and Approaches to Strategic Decision Making

The definitions of strategy, varied in nature, depth and coverage, offer us a glimpse of the complexity involved in understanding this daunting, yet interesting and challenging, concept. In this section, we shall learn about the different levels at which strategy can be formulated.

Levels of Strategies

The strategic planning process culminates into formulation of strategies for the organisation. A business strategy must contain well-coordinated action programs aimed at securing a long-term competitive edge and which should be sustained by the company (Refer Exhibit 2.1)

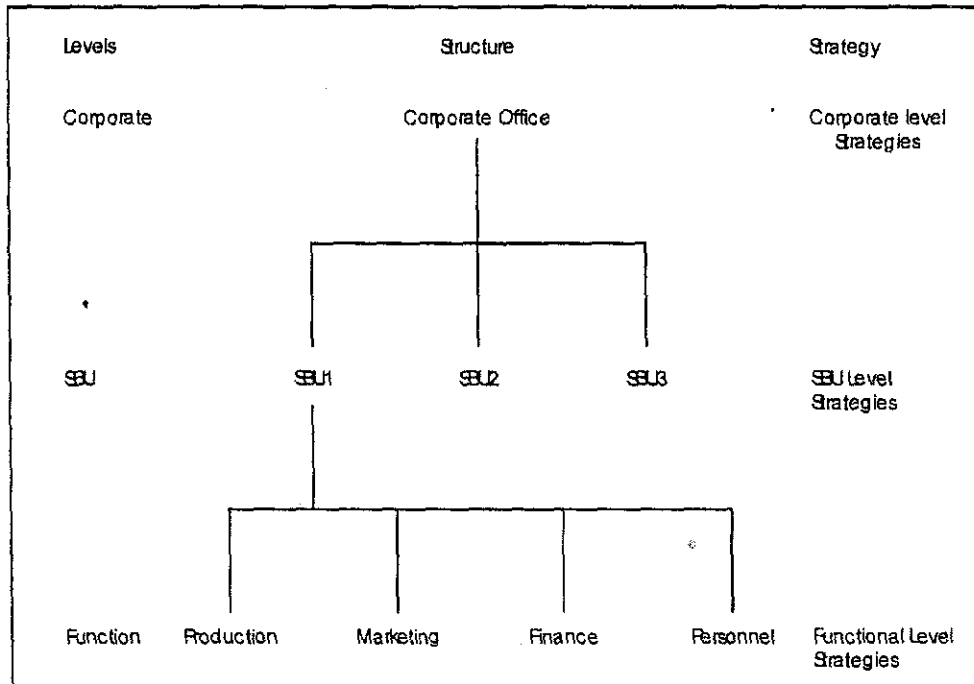


Exhibit 2.1: Levels of Strategies

Corporate Level

In an organisation, there are basically three levels. The top level of the organisation consists of chief executive officer of the company, the board of directors, and administrative officers. The responsibility of the top management is to keep the organisation healthy. This implies that their responsibility is to achieve the planned financial performance of the company in addition to meeting the nonfinancial goals viz. social responsibility and the organisational image. The issues pertaining to business ethics, integrity, and social commitment are dealt with, at this level of strategic decisions. The corporate level strategies translates the orientation of the stakeholders and the society into the forms of strategies for functional or business levels (Refer Exhibit 2.2).

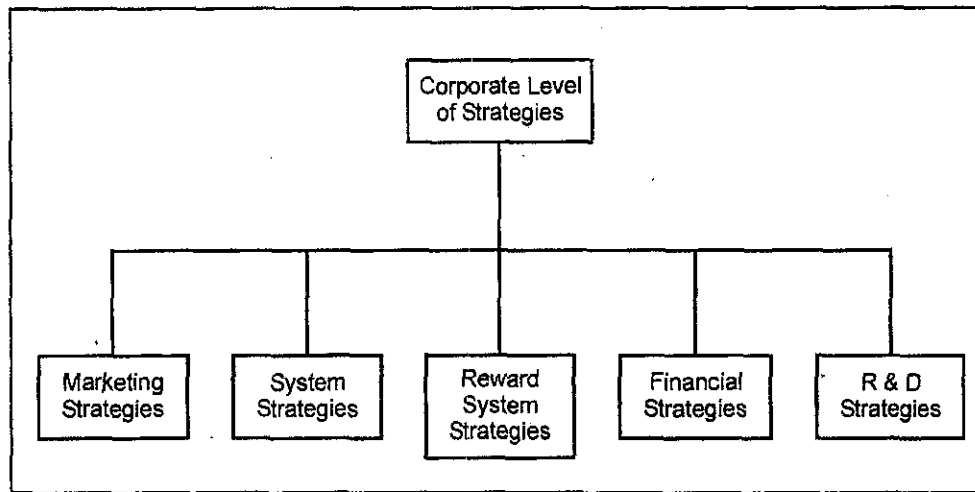


Exhibit 2.2: Corporate Level Strategies

By using portfolio approach, a set of natural and generic strategies are generated that must be considered by each business group, depending on their position in the industry attractiveness and competitive strength dimensions. This is the level where vision statement of the companies emerges. Exhibit 2.3 shows typical levels of strategy-making in an organisation.

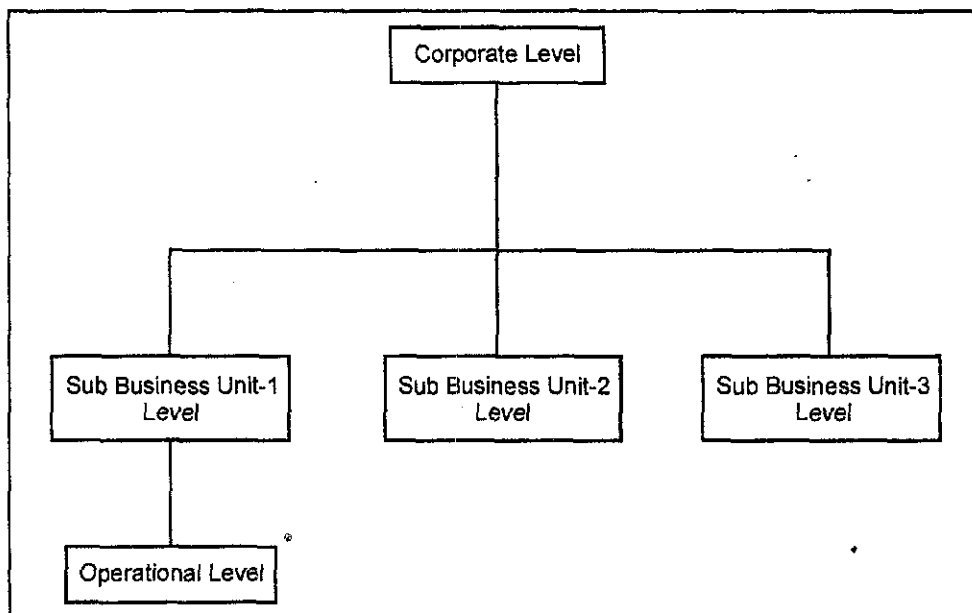


Exhibit 2.3: Levels of Strategy-Making

Business Level

This level consists of primarily the business managers or managers of Strategic Business units. Here strategies are about how to meet the competitions in a particular product market and strategies have to be related to a unit within an organisation. The managers at this level translate the general statements of direction and intent churned out at corporate level. They identify the most profitable market segment, where they can excel, keeping in focus the vision of the company. The corporate values, managerial capabilities, organisational responsibilities, and administrative systems that link strategic and operational decision-making level at all the levels of hierarchy, encompassing all business and functional lines of authority in a company are dealt with at this level of strategy formulation. The managerial style, beliefs, values, ethics, and accepted forms of behaviour must be congruent with the

organisational culture and at this level, these aspects are diligently taken care of by strategic managers.

Operational Level

Planning alone cannot create massive mobilisation of resources and people and can never generate high quality of strategic thinking required in complex organisational context. For this to happen, the planning should be carefully dovetailed and integrated with significant administrative systems viz. management control, communication, information management, motivation, rewards etc. It is also vital that all these systems are supported by organisational structure that define various authority and responsibility relationships, among various members of the company and specifically at operational level. The culture of the organisation should be accounted for, and these systems should find adaptability with the culture of the organisation.

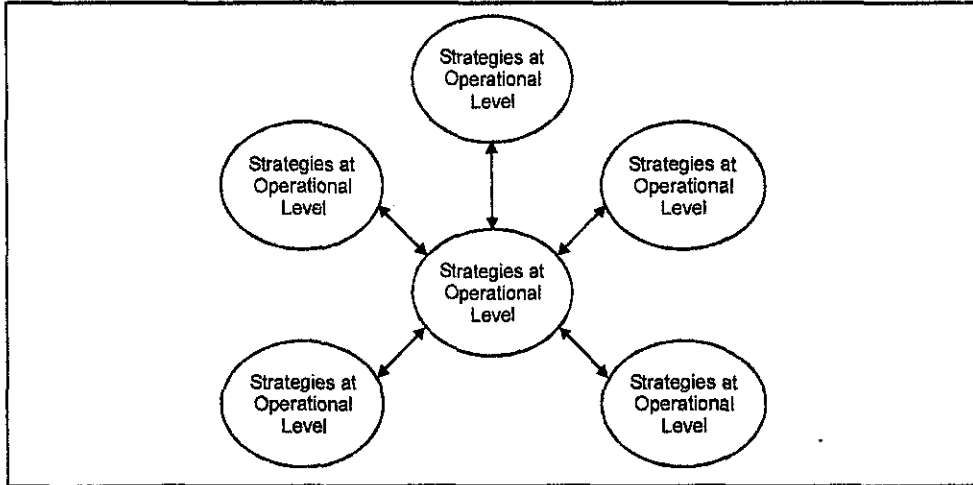


Exhibit 2.4: Interaction of Various Functions

The managers at this level of product, geographic, and functional areas develop annual objective and short-term strategies. The strategies are designed in each area of research and development, finance and accounting, marketing and human relations etc. The responsibilities also include integrating among administrative systems and organisational structure and strategic and operational modes and seek for congruency between managerial infrastructure and the corporate culture. Exhibit 2.4 shows the interaction of various functions for deciding strategies at the operational level.

Characteristics of Strategic Decisions

The three levels of strategic decision have varying characteristics due to the varying responsibility and authority at different levels of management functioning (Refer Exhibit 2.5).

Characteristic	Corporate Level	Business Unit Level	Functional Level
Nature	Conceptual	Conceptual but related to business unit	Totally operational
Measurability	Non-measurable	Measurable to some extent	Quantifiable
Frequency	Large spans 5-10 years	Periodic	Annually
Adeptability	Poor	Average	High
Character	Innovative and Creative	Action-oriented	Totally action oriented
Risk	High	Moderate	Low
Profit	Large	Moderate	Low
Flexibility	High	Moderate	Low
Time	Long range	Medium range	Short range
Costs Involved	High	Medium	Low
Cooperation needed	High	Medium	Low

Exhibit 2.5: Characteristics of Corporate, Business and Functional Level Strategies

The nature of decisions taken at corporate level give a vision to the organisation. The decisions taken are visionary in nature and hence are highly subjective. The vision of a company evolves after a lot of deliberations among the directors who decide that how their company would be known after a long period of time, say after ten to fifteen years. The decisions at this level are therefore vital for selecting the directions of growth of a company. Since it is very difficult to foresee what would happen to a company after a long period of time, the decision essentially should have built-in flexibility as these would have far-reaching consequences on the operations of the company. The decisions at this level also involve greater risks, costs, potential profits etc. The characteristic strategies at this level may include the following in a typical organisation.

- Business scope and an expression of competitive leadership.
- Identification of product market segments.
- Corporate strategic thrusts and planning challenges relevant to the business unit.
- Internal security at the business level that includes identification and evaluation of critical success factors and assessment of competitive position.
- Environmental scan at business level and identification of product markets and industry attractiveness.
- Formulation of business strategy is a set of multi-year broad action programmes.

At the functional level, the decisions involve action-oriented operational issues. Essentially these are short-term type and hence periodically made. They reflect some or all part of the strategy at corporate level. These decisions are also comparatively of low risk and involve lower costs as the resources to be used by them are from the organisation itself. The company as a whole is rarely involved in these decisions. They are more concrete, clear, simple to implement and do not disturb the ongoing processes of the company. The decisions at this level are more critically examined, in spite of being less profitable.

Approaches to Strategic Decision Making

Strategic planning tools have developed enormously over the past 20 years. Such techniques as the growth/share matrix and the experience curve are in widespread use, and other planning techniques allow the manager to evaluate the impact of alternative strategies on the stock price of the corporation. Management consulting firms offer strategic planning on a commodity basis, and any new M.B.A. comes equipped with at least one method for developing such plans.

Unfortunately, the tools for implementing strategies have not developed as quickly as the tools we use for planning. The result of this discrepancy—failed plans and abandoned planning efforts—is all too visible:

A major diversified manufacturer concluded that a steady stream of new products was the most important factor in improving the stock price, yet the performance measures and management reports imposed on the division heads stress quarterly profit. As a result, division managers don't make the long-term investment required for successful new product development.

A leading consumer goods company committed itself to strategic planning and built a staff of over 30 planners, many with M.B.A.s, and experience in consulting firms. Unfortunately, the expected benefits of planning failed to materialise; in less than two years, the department was disbanded and planning responsibility returned to the operating units.

Recently, business writers have begun to pay more attention to the problems of strategy implementation. Corporate culture is now widely acknowledged as an important force in the success or failure of business ventures; studies of Japanese management practices point out the effectiveness of participative methods in securing wholehearted commitment to new strategies at all levels of the organisation.

Despite this interest, three critical questions remain unanswered:

- How can executives be more effective in putting chosen strategies into action?
- How can the planning process be managed so that the strategies which emerge are realistic/ not only in terms of the market place, but also in terms of the politics, culture, and competence of the organisation?
- Research shows that managers do not analyse opportunities exhaustively before taking action; rather, they shape strategy through a continuing stream of individual decisions and actions. How can we reconcile the static academic dogma, "First formulate strategy, then implement it," with the dynamic reality of managerial work?

To shed some light on these questions, we studied management practice at a number of companies. We have found that their approaches to strategy implementation can be categorised into one of five basic descriptions. In each one, the chief executive officer plays a somewhat different role and uses distinctive methods for developing and implementing strategies. The approaches differ in a number of other dimensions as well (see Exhibit 2.6). We have given each description a title to distinguish its main characteristics.

The first two descriptions represent traditional approaches to implementation.

Here the CEO formulates strategy first, and then thinks about implementation later.

1. **The commander approach**—The CEO concentrates on formulating the strategy, applying rigorous logic and analysis. He either develops the strategy himself or supervises a team of planners. Once he's satisfied that he has the "best" strategy, he passes it along to those who are instructed to "make it happen."
2. **The organisational change approach**—Once a strategy has been developed, the executive puts it into effect by taking such steps as reorganising the company structure, changing incentive compensation schemes, or hiring personnel.

The next two approaches involve more recent attempts to enhance implementation by broadening the bases of participation in the planning process:

3. **The collaborative approach**—Rather than develop the strategy in a vacuum, the CEO enlists the help of his senior managers during the planning process in order to assure that all the key players will back the final plan.

Factor	Approaches				
	Commander	Change	Collaborative	Cultural	Creative
How are goals set? Where in the organisation (top or bottom) are the strategic goals established?	Dictated from top.	Dictated from top.	Negotiated among top team.	Embodied in culture.	Stated loosely from top; refined from bottom.
What signifies success? What signifies a successful outcome to the strategic planning/implementation process?	A good plan, as judged on economic criteria.	Organisation and structure which fit the Strategy.	An acceptable plan with broad top management support.	An army of busy implementers.	Sound strategies with champions behind them.
What factors are considered? What are the kinds of factors, or types of rationality used in developing a strategy for resolving conflicts between alternative proposed strategies?	Economic.	Economic, political.	Economic, social, Political.	Economic, social.	Economic, social, political; behavioral.
What is the typical level of organisation wide effort required?					
During the planning phase	Low	Low	High	High	High
During the implementation Phase	N/A	High	Low	Low	Low
How stringent are the requirements placed on the CEO in order for the approach to succeed?					
Required CEO knowledge. To what extent must the CEO be able to maintain personal awareness of all significant strategic opportunities or threats?	High	High	Moderate	Low	Low
Required CEO power. To what extent must the CEO have the power to impose a detailed implementation plan on the organisation?	High	High	Moderate	Moderate	Moderate

Exhibit 2.6: Comparison of Five Approaches

4. **The cultural approach**—This is an extension of the collaborative model to involve people at middle and sometimes lower levels of the organisation. It seeks to implement strategy through the development of a corporate culture throughout the organisation.

The final approach begins to answer some of the questions posed above by taking advantage of managers' natural inclination to develop opportunities as they are encountered. While it has not been widely recognised or studied up to now, we think it may represent the next major advancement in the art of strategic management.

5. **The creative approach**—In this approach, the CEO addresses strategy planning and implementation simultaneously. He is not interested in strategising alone, or even in leading others through a protracted planning process. Rather, he tries, through his statements and actions, to guide his managers into coming forward as champions of sound strategies. (Since this involves "growing" strategies from within the firm, the label comes from the Latin *crescere*, to grow.)

In these five approaches we see a trend toward the CEO playing an increasingly indirect and more subtle role in strategy development. We question the recentralisation of strategy making at headquarters, a trend documented (and encouraged) by some recent writers. We think, at least for some firms, that this might be a mistake.

Various theories have been suggested about how decisions are made. Let us examine, these first. Most writers focus on three approaches: rational-analytical, intuitive-emotional, and behavioral-political.

Rational-Analytical Decision Maker

In this model, the decision maker is a unique actor whose behavior is intelligent and rational. The decision is the choice this actor makes, in full awareness of all available feasible alternatives, to maximise advantages. The decision

maker there to considers all the alternatives as well as the consequences of all the possible choices, orders these consequences in the light of a fixed scale of preferences, and chooses the alternative that procures the maximum gain.

This is the oldest decision theory. It prescribes a rational, conscious, systematic, and analytical approach. It has been criticised because

1. The decision maker is often not a unique actor but part of a multiparty decision situation.
2. Decision makers are not rational enough or informed enough to consider all alternatives or know all the consequences. And information is costly.
3. Decision makers make decisions with more than a maximisation of objectives in mind. They tend to "satisfice," that is, make a decision expected to yield a satisfactory, as opposed to an "optimal," outcome. Besides, the objectives may change.

So descriptions of actual decision making question the validity of "rational" processes.

Intuitive-Emotional Decision Maker

The opposite of the rational decision maker is the intuitive decision maker. This decision maker prefers habit or experience, gut feeling, reflective thinking, and in-stinct, using the unconscious mental processes. Intuitive decision makers consider a number of alternatives and options, simultaneously jumping from one step in analysis or search to another and back again.

Some who prescribe intuition or judgment as the preferred approach point out that in many, cases, judgment may lead to "better" decisions than "optimizing" techniques. For example, consider sensitivity analysis on a tool such as the economic order quantity (EOQ). EOQ models suggest that there is an optimal order quantity considering trade-offs of ordering and holding costs. Yet you can stray far from optimal in most cases without a very significant impact on total cost differentials. Here, then, judgment concerning other factors in the decision situation could lead to a better *overall* decision about order quantities, rather than holding fast to deciding what the rational model prescribes. In fact, the timing of when to implement a decision based on the analysis may require an intuitive feel for what the data are telling you. In many cases, judgment such as this might be preferable to relying on the analysis. Recognize, then, that analytical models are tools to *help* the decision maker refine judgment.

Those opposed to this approach argue that

1. It does not effectively use all the tools available to modern decision makers.
2. The rational approach ensures that adequate attention is given to consequences of decisions before big mistakes are made.

Political-Behavioral Decision Making

A third point of view suggests that real decision makers must consider a variety of pressures from other people affected by their decisions. An organisation interacts with a variety of stakeholders in a series of interdependent exchange relationships. Unions exchange labor for decent wages and job security. Customers exchange money for products and services. Owners exchange capital for expected returns on investment. Suppliers exchange inputs for money and continued business. Government exchanges protection and economic security for taxes. Even competitors exchange information with one another through trade associations or other contacts. The list of agents and expectations goes on. *A stakeholder is any group or individual who can affect or is affected by the achievement of an organisation's purpose.*

Each stakeholder gives the organisation something and expects something in return. To the extent an organisation has a favorable exchange relationship (gets a bit more than given) compared with other organisations and stakeholders, it has more power. More powerful stakeholders have more influence over decisions because the organisation is more dependent on these stakeholders. A majority stockholder can have a greater influence on decisions about reinvestment versus dividend payout than if stock is widely held by many small owners. If the firm is labor-intensive, more attention may be paid to union leaders' demands for better wages than to the desires of stock-holders for more profit, because the union might shut the firm down.

Given these realities, decision makers do a juggling act to meet the demands of the various stakeholders. Through political compromise, they attempt to merge competing demands so that a coalition of interests emerges that will support the decision.

This mode of decision making is a descriptive theory suggesting that the organisation in which the decision maker works limits the choices available. Decisions are made when the several people involved in the process agree that they have found a solution. They do this by mutual adjustment and negotiation following the rules of the game—the way decisions have been made in the organisation in the past. The decision maker must consider whether the decision outcome can be implemented politically.

A Synthesis on Decision Making

The human being is a mix of the rational and the emotional. The environment is a mixture of the analysable and of chaotic change and pressures. Strategic management decisions therefore are made in a typically human way: using the rational, conscious analysis and intuitive, unconscious “gut,” in light of political realities.

As stated earlier, some prescribe that one component or another should be larger. However, because of individual differences and differences in the stability of the environment, the amount of the rational versus the intuitive versus the political varies by the decision maker and the decision situation. In some cases the analytical component is very large; in others, the emotional set may dominate. For example, Bil Ziff, the magnate behind the billion dollar Ziff-Davis Publishing Company, sold off much of his empire because he became “more and more bored.” He put TV station up for sale because, he says, “they were not a turn on.” But as Exhibit 1.12 suggest the interaction of the three approaches (shaded area) defines where we think much decision making probably occurs. We would prefer that the analytical component be larger than the others. In fact, we prescribe an analytical-rational approach, tempered by realities in the situation. Thus when you set about to make decisions, you should apply the tools you learn. But truly rational analysis will also incorporate analysis of the political-behavioral and intuitive dimensions in the decision situation. Indeed various techniques such as dialectic inquiry, devil's advocacy, hierarchical analysis, and influence diagrams have evolved to help managers with these complex and messy problems. These systems allow managers to recognise and rationally structure the judgmental and political factors which will undoubtedly influence them.

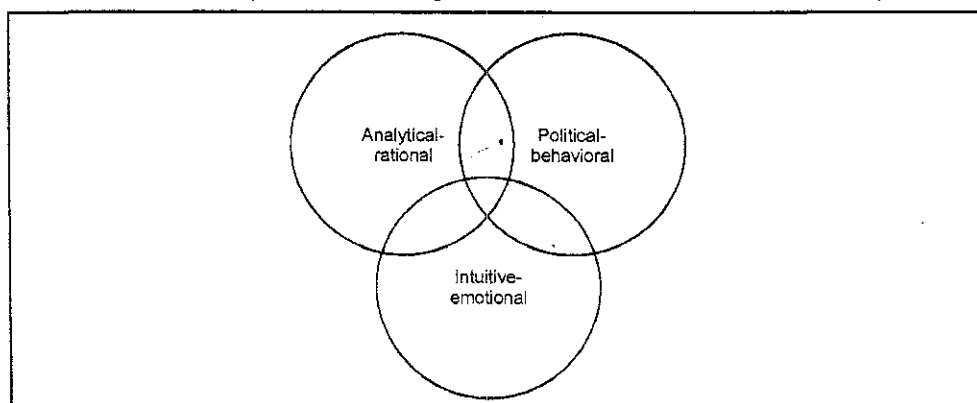


Exhibit 2.7: Components of Strategic Decision Processes

Thus a blending of these prescriptive and descriptive approaches helps to better understand how decision makers operate. And as you assess cases or business problems, attempt to diagnose the political or emotional realities of the situation in addition to using the analytical tools at your disposal. The recommendations you make are likely to be much more meaningful if you do this.

As strategic decision-making is a complex process, it is difficult to perform. It is incomprehensible; it cannot be analysed and explained easily. Decision-makers are unable to describe the exact manner in which strategic decisions are made. Like the working of the human mind, strategic decision-making is fathomless. And rightly so, for it is based on complex mental processes which are not exposed to the view. While commenting on the nature of strategic decision-making Henry Mintzberg says that "the key managerial processes are enormously complex and mysterious, drawing on the vaguest of information and using the least articulated of mental processes. These processes seem to be more relational and holistic than ordered and sequential, and more intuitive than intellectual...."

For these reasons, no theoretical model, however painstakingly formulated, can adequately represent the different dimensions of the process of strategic decision-making. Despite these limitations, we can still attempt to understand strategic decision-making by considering some important issues related to it. Six such issues are:

1. *Criteria for decision-making.* The process of decision-making requires objective-setting. These objectives serve as yardsticks to measure the efficiency and effectiveness of the decision-making process. In this way, objectives serve as the criteria for decision-making. There are three major viewpoints regarding setting criteria for decision-making.
 - (a) The first is the concept of maximisation. It is based on the thinking of economists who consider objectives as those attributes which are set at the highest point. The behaviour of the firm is oriented towards achieving these objectives and, in the process, maximising its returns.
 - (b) The second view is based on the concept of satisficing. This envisages setting objectives in such a manner that the firm can achieve them realistically through a process of optimisation.
 - (c) The third viewpoint is that of the concept of incrementalism. According to this view, the behaviour of a firm is complex and the process of decision-making, which includes objective-setting, is essentially a continually-evolving political consensus-building. Through such an approach, the firm moves towards its objectives in small, logical and incremental steps.
2. *Rationality in decision-making.* In the context of strategic decision-making, rationality means exercising a choice from among various alternative courses of action in such a way that it may lead to the achievement of the objectives in the best possible manner. Those economists who support the maximizing criterion consider a decision to be rational if it leads to profit maximisation. Behaviourists, who are proponents of the satisfying concept, believe that rationality takes into account the constraints under which a decision-maker operates. Incrementalists are of the opinion that the achievement of objectives depends on the bargaining process between different interested coalition groups existing in an organisation, and therefore a rational decision-making process should take all these interests into consideration.
3. *Creativity in decision-making.* To be creative, a decision must be original and different. A creative strategic decision-making process may considerably affect the search for alternatives where novel and untried means may be looked for and adopted to achieve objectives in an exceptional manner. Creativity as a trait is normally associated with individuals and is sought to be developed through techniques such as brainstorming. One of the attitudinal objectives of a business policy course is to develop the ability to go beyond and think, which, in other words, is using creativity in strategic decision-making.

4. *Variability in decision-making.* It is a common observation that given an identical set of conditions two decision-makers may reach totally different conclusions. This often happens during case discussions too. A case may be analysed differently by individuals in a group of learners, and, depending on the differing perceptions of the problem and its solutions, they may arrive at different conclusions. This happens due to variability in decision-making. It also suggests that every situation is unique and there are no set formulas that can be applied in strategic decision-making.
5. *Person-related factors in decision-making.* There are a host of person-related factors that play a role in decision-making. Some of these are age, education, intelligence, personal values, cognitive styles, risk-taking ability, and creativity. Attributes like age, knowledge, intelligence, risk-taking ability, and creativity are generally supposed to play a positive role in strategic decision-making. A cognitive style which enables a person to assimilate a lot of information, interrelate complex variables, and develop an integrated view of the situation is specially helpful in strategic decision-making. Values, as enduring prescriptive beliefs, are culture-specific and important in matters of social responsibility and business ethics— issues that are important to strategic management.
6. *Individual versus group decision-making.* Owing to person-related factors, there are individual differences among decision-makers. These differences matter in strategic decision-making. An organisation, as it possesses special characteristics, operates in a unique environment. Decision-makers who understand an organisation's characteristics and its environment are in advantage position to undertake strategic decision-making. Individuals such as chief executives or entrepreneurs play the most important role as strategic decision-makers. But as organisations become bigger and more complex, and face an increasingly turbulent environment, individuals come together in groups for the purpose of strategic decision-making.

Schools of Thought on Strategy Formation

The subject of strategic management is in the midst of an evolutionary process. In the course of its development, several strands of thinking are emerging which are gradually leading to a convergence of views. This is a subtle indication of the maturing of this subject. We now have a wealth of insight into the complexities of strategic behaviour—the observable characteristics of the manner in which, an organisation performs decision-making and planning functions with regard to the issues that are of strategic importance to its survival, growth and profitability. Strategic decision-making is the core of managerial activity, strategic behaviour is its manifestation, while the outcome is the formation of strategy.

Here, in this section, we dwell upon the compendium of various perspectives to strategy formation that have evolved over a period of time. Several persons, among whom are the doyens in the field of strategy, have contributed to the formulation of these perspectives. These offer the reader, a meaningful insight into the development of the concept of strategy. Indeed, Mintzberg and his associates, from whose writings these perspectives have been adopted here, call them the 10 schools of thought on strategy formation.

The schools of thought can be classified under three groups as below.

The Prescriptive Schools

1. Design school where strategy formation is a process of conception
2. Planning school where strategy formation is a formal process
3. Positioning school where strategy formation is an analytical process

The Descriptive Schools

4. Entrepreneurial school where strategy formation is a visionary process
5. Cognitive school where strategy formation is a mental process
6. Learning school where strategy formation *is* an emergent process
7. Power school where strategy formation is a negotiation process
8. Cultural school where strategy formation is a collective process
9. Environmental school where strategy formation is a reactive process
10. Configuration school where strategy formation is a process of transformation.

The Integrative School

Given below is a description and explanation of each school of thought.

1. *The design school*, which perceives strategy formation as a process of conception developed mainly in the late 1950s and 60s. Under this school, strategy is seen as something unique which is in the form of a planned perspective. The CEO as the main architect guides the process of strategy formation. The process of strategy formation is simple and informal and based on judgement and thinking. The major contributors to the design school are Selznick (1957) and Andrews (1965).
2. *The planning school*, which perceives strategy formation as a formal process developed mainly in the 1960s. Under this school, strategy is seen as a plan divided into substrategies and programmes. The planners play the lead role in strategy formation. The process of strategy formation is formal and deliberate. The major contributor to the planning school is Ansoff (1965).
3. *The positioning school*, which perceives strategy formation as an analytical process developed mainly in the 1970s and 80s. Under this school, strategy is seen as a set of planned generic positions chosen by a firm on the basis of an analysis of the competition and the industry in which they operate. The lead role in strategy formation is played by the analysts. The process of strategy formation is analytical, systematic and deliberate. The major contributors to the positioning school are Schendel and Hatten (1970s), and Porter (1980s).
4. *The entrepreneurial school*, which perceives strategy formation as a visionary process developed mainly in the 1950s. Under this school, strategy is seen as the outcome of a personal and unique perspective often aimed at the creation of a niche. The lead role in strategy formation is played by the entrepreneur/ leader. The process of strategy formation is intuitive, visionary, and largely deliberate. The major contributors to the entrepreneurial school are Schumpeter (1950s), Cole (1959) and several others, most of whom are economists.
5. *The cognitive school*, which perceives strategy formation as a mental process, developed mainly in the 1940s and 50s. Under this school, strategy is seen as an individual concept that is the outcome of a mental perspective. The lead role in strategy formation is played by the thinker-philosopher. The process of strategy formation is mental and emergent. The major contributors to the cognitive school are Simon (1947 and 1957), and March and Simon (1958).
6. *The learning school* which perceives strategy formation as an emergent process has had a legacy from the 1950s through the 1990s. Under this school, strategy is seen as a pattern that is unique. The lead role is played by the learner within the organisation whoever that might be. The process of strategy formation is emergent, informal and messy. The major contributors to the learning school are Lindblom (1959, 1960), Cyert and March (1963), Weick (1969), Quinn (1980), Senge (1990), and Prahalad and Hamel (early 1990s).

7. *The power school*, which perceives strategy formation as a negotiation process, developed mainly during the 1970s and 80s. Under this school, strategy is seen as a political and cooperative process or pattern. The lead role in strategy formation is played by any person in power (at the micro level) and the whole organisation (at the macro level). The process of strategy formation is messy, consisting of conflict, aggression and cooperation. At the micro level the process of strategy formation is emergent while at the macro level it is deliberate. The major contributors to the power school are Allison (1971), Pfeffer and Salancik (1978), and Astley (1984).
8. *The cultural school*, which perceives strategy formation as a collective process developed mainly in the 1960s. Under this school, strategy is seen as a unique and collective perspective. The lead role in strategy formation is played by the collectivity displayed within the organisation. The process of strategy formation is ideological, constrained, collective and deliberate. The major contributors to the cultural school are Rhenman and Normann (late 1960s).
9. *The environmental school*, which perceives strategy formation as a reactive process, developed mainly in the late 1960s and 70s. Under this school, strategy is seen as something generic occupying a specific position or niche in relation to the environment. The lead role in strategy formation is played by the environment as an entity. The process of strategy formation is passive and imposed, and hence, emergent. The major contributions to the environmental school are Hannan and Freeman (1977) and contingency theorists like Pugh et al. (late 1970s).
10. *The configuration school*, which perceives strategy formation as a transformation process developed during the 1960s and 70s. Under this school, strategy is viewed in relation to a specific context and thus could be in a form that corresponds to any process visualised under any of the other nine schools. The lead role may be played by any actor identified in the other nine schools. The process of strategy formation is integrative, episodic and sequential. In addition, the process could incorporate the elements pointed out under the other nine schools of thought. The major contributors to the configuration school are Chandler (1962), Mintzberg and Miller (late 1970s), and Miles and Snow (1978).

Chapter 3

Process of Strategic Management

“Business policy” is a term traditionally associated with the course in business schools devoted to integrating the educational program of these schools and understanding what today is called strategic management. In most businesses in earlier times (and in many smaller firms today), the focus of the manager’s job was on today’s decisions for today’s world in today’s business. That may have been satisfactory then instead of focusing all their time on today, managers began to see the value of trying to anticipate the future and to prepare for it. They did this in several ways.

- They prepared systems and procedures manuals for decisions that must be made repeatedly. This allowed time for more important decisions and ensured more or less consistent decisions.
- They prepared budgets. They tried to anticipate future sales and flows of funds. In sum, they created a planning and control system.

Budgeting and control systems helped, but they tended to be based on the status quo—the present business and conditions—and did not by themselves deal well with change. These systems did provide better financial controls and are still in use. Later variations included capital budgeting and management-by-objectives systems.

Because of the lack of emphasis on the future in budgeting, long-range planning appeared. This movement focused on forecasting the future by using economic and technological tools. Long-range planning tended to be performed primarily by corporate staff groups, whose reports were forwarded to top management. Sometimes their reports and advice were heeded (when they were understood and were credible); otherwise, they were ignored. Since the corporate planners were not the decision makers, long-range planning had some impact, but not as much as would be expected if top management were involved. Then, too, they were producing first-generation plans.

“First-generation planning” means that the firm chooses the most probable appraisal and diagnosis of the future environment and of its own strengths and weaknesses. From this, it evolves the best strategy for a match of the environment and the firm—a single plan for the most likely future.

Today’s approach is called “strategic planning” or, more frequently, “strategic management.” The board of directors and corporate planners have parts to play in strategic management. But the starring roles are for the general managers of the corporation and its major operating divisions. Strategic management focuses on “second-generation planning,” that is, analysis of the business and the preparation of several scenarios for the future. Contingency strategies are then prepared for each of these likely future scenarios.

Strategy formulation is the process of establishing a business mission, conducting research to determine critical external and internal factors, establishing long-term objectives, and choosing among alternative strategies. Sometimes the strategy formula stage of strategic management is called “strategic planning.” The difference between strategic planning and strategic management is that the latter includes strategy implementation and strategy evaluation.

As illustrated below three basic strategy-formulation activities are conducting research, integrating intuition with analysis, and making decisions. Conducting research involves gathering and assimilating information about a given firm’s industry and markets. This process is sometimes called *environmental scanning*. Internally, research is conducted to identify key strengths and weaknesses in the functional areas of business. Internal factors can be determined in a number of ways that include computing ratios, measuring performance, and comparing to past periods and industry averages. Various types of surveys can also be developed and administered to examine internal factors such as employee morale, production efficiency, advertising effectiveness, and customer loyalty.

There are numerous strategic-management techniques that allow strategists to integrate intuition with analysis in generating and choosing among feasible alternative strategies. Some of these tools are the External Factor Evaluation (EFE) Matrix, the Internal Factor Evaluation (IFE) Matrix, the Strategic Position and Action Evaluation (SPACE) Matrix, the Boston Consulting Group (BCG) Matrix, and the Quantitative Strategic Planning Matrix (QSPM).

Since no organisation has unlimited resources, strategists must make decisions regarding which alternative strategies will benefit the firm most. Strategy-formulation decisions commit an organisation to specific products, markets, resources, and technologies over an extended period of time. Strategies determine long-term competitive advantages. For better or worse, strategic decisions have enduring effects on an organisation and major multifunctional consequences. Strategists have the best perspective to fully understand the ramifications of formulation decisions; they have the authority to commit the resources necessary for implementation.

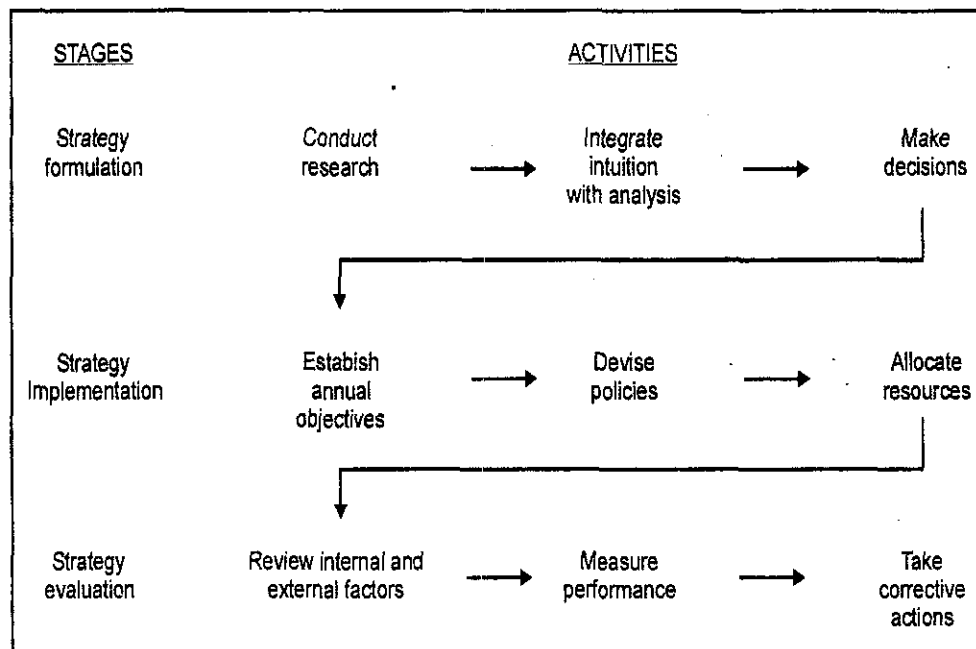


Exhibit 3.1: Stages and Activities in the Strategic-Management Process

Strategy Implementation

Strategy implementation is often called the action stage of strategic management. Implementing means mobilising employees and managers to put formulated strategies into action. Three basic strategy-implementation activities are establishing annual objectives, devising policies, and allocating resources. Often considered to be the most difficult stage in strategic management, strategy implementation requires personal discipline, commitment, and sacrifice. Successful strategy implementation hinges upon managers' ability to motivate employees, which is more an art than a science. *Strategies formulated but not implemented serve no useful purpose.*

Interpersonal skills are especially critical for successful strategy implementation. Strategy implementation includes developing strategy—supportive budgets, programs, and cultures, and linking motivation and reward systems to both long-term and annual objectives. Strategy-implementation activities affect all employees and managers in an organisation. Every division and department must decide on answers to questions such as “What must we do to implement our part of the organization’s strategy?” and “How best can we get the job done?” The challenge of implementation is to stimulate managers and employees throughout an organisation to work with pride and enthusiasm toward achieving stated objectives.

Strategy Evaluation

The final stage in strategic management is strategy evaluation. All strategies are subject to future modification because external and internal factors are constantly changing. Three fundamental strategy-evaluation activities are (1) reviewing external and internal factors that are the bases for current strategies, (2) measuring performance, and (3) taking corrective actions. Strategy evaluation is needed because success today is no guarantee of success tomorrow! Success always creates new and different problems; complacent organisations experience demise.

Strategy formulation, implementation, and evaluation activities occur at three hierarchical levels in a large diversified organisation: corporate, divisional or strategic business unit, and functional. By fostering communication and interaction among managers and employees across hierarchical levels, strategic management helps a firm function as a competitive team. Most small businesses and some large businesses do not have divisions or strategic business units, so these organisations have only two hierarchical levels.

The strategic-management process can best be studied and applied using a model. Every model represents some kind of process. The framework illustrated below is a widely accepted, comprehensive model of the strategic-management process. This model does not guarantee success, but it does represent a clear and practical approach for formulating, implementing, and evaluating strategies. Relationships among major components of the strategic-management process are shown in the model. (Exhibit 3.2)

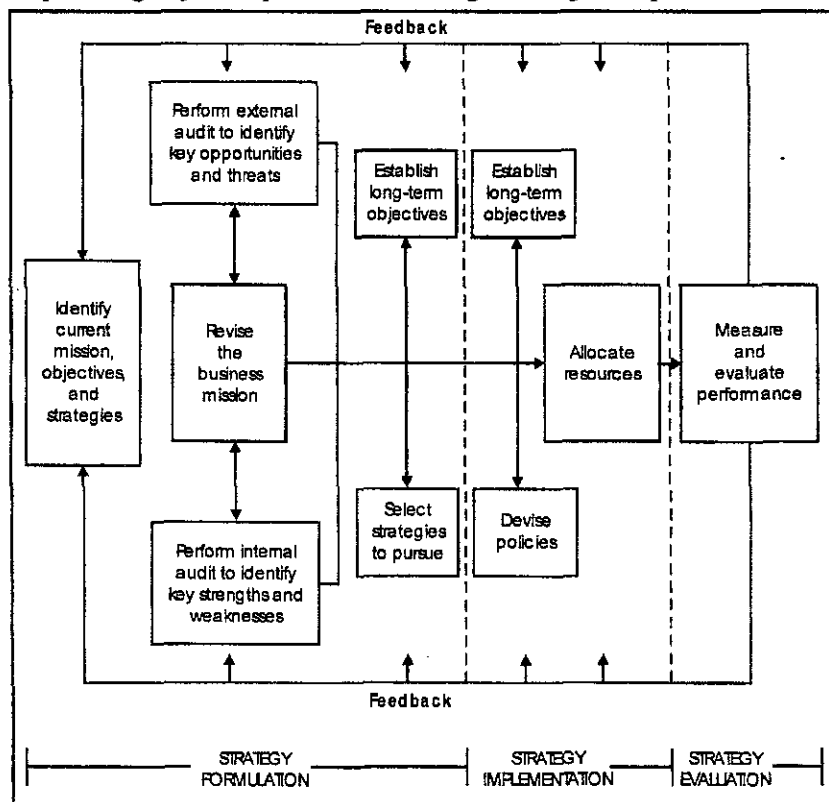


Exhibit 3.2: A Comprehensive Strategic Management Model

Identifying an organisation's existing mission, objectives, and strategies is the logical starting point for strategic management because a firm's present situation and condition may preclude certain strategies and may even dictate a particular course of action? Every organisation has a mission, objectives, and strategy, even if these elements are not consciously designed, written, or communicated. The answer to where an organisation is going can be determined largely by where an organisation has been.

The strategic-management process is dynamic and continuous. A change in any one of the major components in the model can necessitate a change in any or all of the other components. For instance, a shift in the economy could represent a major opportunity and require a change in long-term objectives and strategies; or a failure to obtain annual objectives could require a change in policies; or a major competitor could announce a change in strategy that requires a change in the firm's mission. Therefore, strategy formulation, implementation, and evaluation activities should be performed on a continual basis, not just at the end of the year. The strategic-management process never really ends.

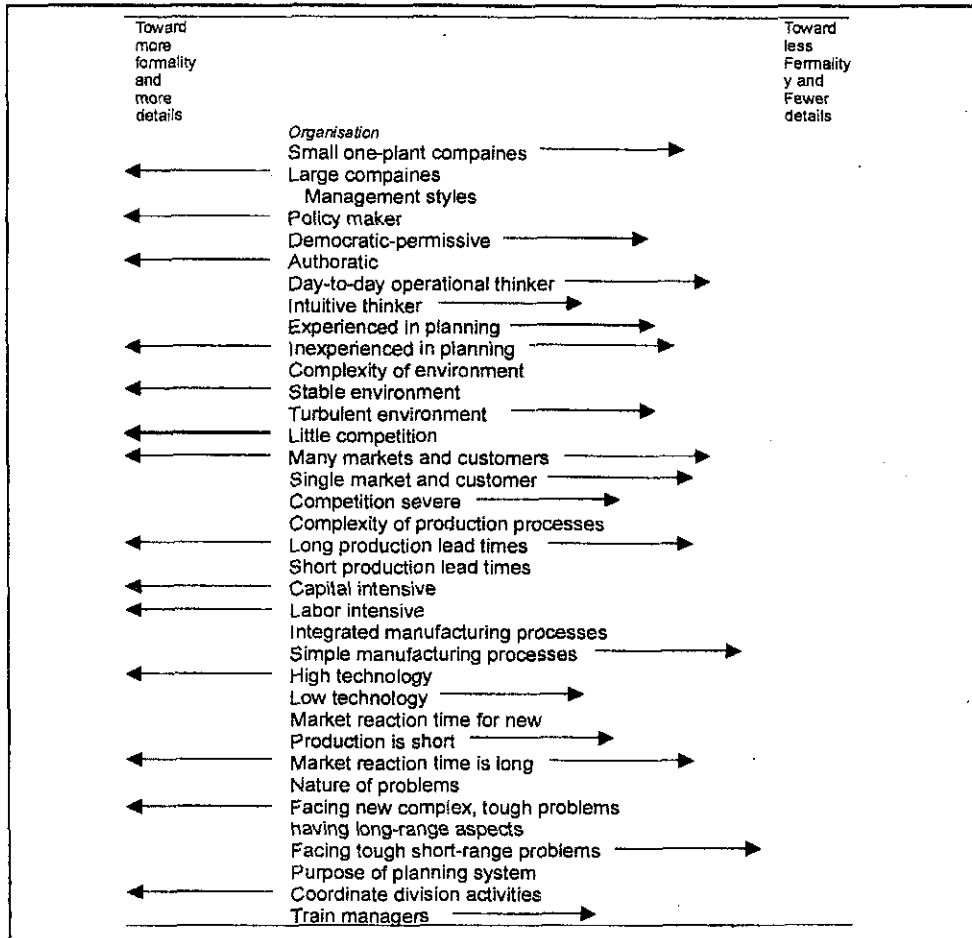


Exhibit 3.3: Forces Influencing Design of Strategic Management Systems

The strategic-management process is not as cleanly divided and neatly performed in practice as the strategic-management model suggests. Strategists do not go through the process in lockstep fashion. Generally, there is give-and-take among hierarchical levels of an organisation. Many organisations conduct formal meetings semiannually to discuss and update the firm's mission, opportunities/threats, strengths/weaknesses, strategies, objectives, policies, and performance. These meetings are commonly held off-premises and called "retreats." The rationale for periodically conducting strategic-management meetings away from the work site is to encourage more creativity and candor among participants. Multidirectional arrows in Exhibit 3.3 illustrate the importance of good communication and feedback throughout the strategic-management process.

As shown in Exhibit 3.3 a number of different forces affect the formality of strategic management in organisations. Size of organisation is a key factor: smaller firms are less formal in performing strategic-management tasks. Other variables that affect formality are management styles, complexity of environment, complexity of production processes, nature of problems, and purpose of planning system.

Chapter 4

Roles of Strategists, Mission and Objectives

Strategists are individuals or groups who are primarily involved in the formulation, implementation, and evaluation of strategy. In a limited sense, all managers are strategists. There are persons outside the organisation who are also involved in various aspects of strategic management. They too are referred to as strategists.

The top management function is usually performed by the Chief Executive Officer (CEO) of the organisation, by whatever name called, in coordination with the Chief Operating Officer (COO) or President, Vice-Presidents, and divisional and departmental heads. The top managers are also known as general manager.

Top management especially the CEO is responsible to the board of directors for overall management of the organisation. The job of the top management is multi-dimensional and oriented towards the welfare of the total organisation. Though the specific top management functions may vary from organisation to organisation, one could have a good idea about it from an analysis of an organisation's mission, objectives, strategies and key activities.

The Chief Executive in most of the companies is called the Managing Director (Chairman-cum-Managing Director, or President. Where the executive head of the organisation is the Managing Director or Chairman-cum-Managing Director, the President is usually in the position of the Chief Operating Officer (COO). The Executive leader, of a major segment of the organisation such as a division, department or unit is typically called a general manager.

The Chief Executive Officer (CEO) is a strategist, organisational builder and leader. The CEO is the principal strategist of his organisation. Although the BODs and other members of the top management play an important role, the CEO cannot really delegate all his strategic responsibilities to anyone else. He is in fact a strategic thinker. He is the person who links the internal world of the corporation with the external world. This role can be described as the "gate keeping" role of the CEO; it is both "flag flying" and "transmitting" to and receiving signals from the external environment. It is he who has both the corporate understanding and the vantage joint perspective which is required to translate the signals from the outside world. These signals may often be subtle, and not very perceptible. He has to sow seeds for new thoughts within the organisation and has to nurture and sustain those which come from outside.

Many CEOs are so involved in the day-to-day operations that they hardly have any time left for strategic matters, it has been rightly said that routine drives out creativity. The CEO has to see to it that he is left with sufficient time for strategic responsibilities. An American Survey indicated that the executives who reached to the top allocated the largest part of their time to long range planning and policy setting. They even wished that they had more time for long range planning and human resource management.

While operating within the environment and the resources at hand, the CEO has to build the organisation. Organisation building is a continuous process involving organisational change. Some of organisational building responsibility can certainly be delegated but the CEO, being at the helm of the affairs, has to remain the initiator for experimenting with new ideas, approaches and systems. He is the key person in the organisation. The organisational changes should be made gradually and regularly, and not suddenly or sporadically. It is a human tendency to resist change for a variety of reasons, the main being uncertainty. It is therefore important to recognise resistance to change prior to attempting to make organisational changes.

The common reasons for people resisting change are: vested interests, differing perceptions, misunderstanding and lack of trust, and low tolerance for change. Some useful ways to deal with resistance are: education and communication.

participation and involvement, and facilitation and support. All these ultimately lead to the creation of a climate of better confidence.

The CEO is the first among leaders of his organisation. He must have the will to manage. "To manage well a person has to want to manage; he has to really love it". How a Chief Executive can turn around a company is amply revealed in a case history. An expatriate was called to India to boost the performance of an Indian subsidiary in the processing-marketing, industry. The company had tremendous goodwill in the market but its performance was wholly out of alignment with its image. In spite of good products, the company was not able to do well because of traditional management which was characterised by lethargy and lack of articulation. The new CEO, who was gentle in his speech, sensitive to human relations and had charming social manners, was often perceived by company executives as an academic who had somehow strayed into the world of business. However, soon after joining his new position, the new CEO started questioning the current assumptions relating to product strategies, marketing and distribution. He started the system of target setting and performance appraisal.

It soon became clear that the velvet glove concealed an iron fist. He left nobody in doubt about his conviction that if the company had to move forward it had to be sensitive to the environment and regulatory policies, and pull itself up by the organisational boot straps. He redefined product-market posture and reconstituted product groups into divisions with profit responsibility, after taking into consideration the technological, marketing and managerial dimensions which have an impact on performance. He selected the heads of the new divisions carefully. Planning systems were streamlined, targets regarding sales, cost, profit, product development etc. were developed on the basis of open discussion and information sharing. Considerable autonomy was devolved upon the divisional heads with regard to staffing, resource allocation, and marketing strategies.

Many eyebrows were raised about his style of tough-minded behaviour, quite unknown in the history of the organisation. Within a period of less than two years the organisation turned the corner and was found attempting for market leadership in the industry.

Mentoring and helping others along the road to success is an important activity of managers and more so of CEO. The higher a manager gets in an organisation, the more responsibility he has for such helping activities. It is a characteristic of a really genuine leader at any level to lift others up, even beyond his own level at every legitimate opportunity.

Thus, a CEO is simultaneously a strategic thinker, an organisational builder, and a leader. He is also a spokesman, an innovator, a father figure and a prime decision maker, as will be borne out in our later discussion.

Top management comprises a team of people, including the CEO, who perform certain vital tasks. Although there may be differences among writers as to whether people holding certain positions in a body corporate can be regarded as members of top management or not, yet there is a good deal of agreement on tasks performed by them. The tasks performed by the team or group of people who can be regarded as constituting top management are:

- Providing direction
- Setting vision
- Setting standards.

Direction

Top management, undoubtedly, is expected to give direction to the organisation. Should the organisation continue to produce goods and services provided hitherto?

Should there be a change in products supplied? What are the areas, from which the organisation should withdraw?

What are the new areas into which it should enter?

In a reasonably stable environment these questions are not that relevant. But in a changing environment there is a need to keep a close watch. Some products/ businesses which were doing well in recent years may not continue to do so. What should the organisation do? Disinvest, but what are the new areas into which it could go? Most big industrial houses have gradually withdrawn from textiles or are in the process of doing so. These include Birlas, Tatas, Shri Ram Group, Modis. They have entered into new areas such as chemicals, automobiles, tyres, electronics, reprographics. Who decided about these? Of course the top management or more specifically top management team.

Vision Setting

Having given the direction to the organisation, top management team is expected to set standards for the short run and the long run. What is to be achieved, say 5 to 10 years from now? What are the targets for the given years?

Can you guess which task is more important—setting standards for the short run or the long run? Of course, both are equally important and are interconnected. An over-emphasis on the achievement in the short run may mean that the organisation is not able to initiate action in time for moving into more promising areas in the long run. Similarly, an overly concern for achievements in the long run may put the organisation, in difficulty for meeting the short term requirements of cash and other facilities. Evolving a balanced perspective of the short term and long term interests has been emphasised in the literature. It is argued that the top management needs to have bifocal glasses which help it in managing the short term as well as long term interests of the organisation simultaneously.

Standard Setting

Top management not only sets standards but evaluates the performance of various units or groups of businesses. Setting standards has no meaning without some system of control. Developing a system of control is one of the tasks of top management. The frequency of such exercise on evaluation differs from situation to situation. However, the evaluation should provide scope for initiating corrective action.

One of the formal ways of having a system of evaluation is provided by Management by Objectives. In this approach an attempt is made to arrive at an agreement on what is to be achieved. These targets, then constitute the basis on which evaluation is attempted.

The dimension relating to the managerially derived expectations of the Board of Director's role seems to be of relatively recent origin. In the last two decades or so, industrial development has been marked by far-reaching technological changes, leading to equally fundamental competitive reorientation at the global level. As a result, many erstwhile great names in industry have been humbled. With such rapidly mounting changes and uncertainties, the role of BODs has begun to be viewed from much wider and long-term perspective—beyond the minimum requirements of law. Probably, upto the 1970's, the duty of BODs to 'superintend, control and direct' had gone by default. Stable environment had helped this key role to remain dormant. What are then the renewed ramifications of this role at present? These are meant to ensure that:

- the enterprise continues to remain effective on the standpoint of technology parameters.
- the enterprise continues to achieve healthy market growth in competitive conditions,
- divestment and diversification take place on sound lines.

- long-term productivity and quality are never sacrificed at the altar of short-term profitability.
- judicious earnings retention policy is adopted for financing growth, modernisation etc.
- serious and sustained attention is devoted towards building a sound system of human values and exalted corporate culture.

It is a common observation that BODs function rather passively. Often the members are selected not because of their knowledge of the specific functioning of the company which they are supposed to oversee but because of their compatibility, prestige or esteem in the community. Traditionally, as it happens, the board members are expected (or requested) to approve the proposals put forward to them by top management. Usually, the Chief Executive Officer (CEO) or the group of promoters have a free reign in choosing the directors and in having them elected by the shareholders. The CEO or the promoter group may select board members who in their opinion, will not disturb the company's policies and functioning. The directors so selected often feel that they should go along with any proposals made by the CEO and his group. Thus, a strange or somewhat paradoxical situation arises. The board members find themselves accountable to the very management they are expected to oversee.

Even today, the boards in India, especially in family owned or closely held companies, are mere figureheads. Over the recent past, however, lending institutions, financial media and corporate analysts have seriously questioned the role of BODs. The investors and government in general are now better aware of the role of BODs. In general, it is felt that there is a critical lack of responsibility on the part of BODs. Though the Companies Act throws some light on the powers of BODs and the restrictions placed on those powers, it does not specify to whom they are responsible and what for. However, there is a broad agreement that BODs appointed or elected by the shareholders are expected to:

- oversee the management of the company's assets
- establish or approve the company's mission, objectives, strategy and policies
- review management actions and financial performance of the company
- hire and fire the principal executive and operating officers of the company.

An important issue in this context is : should BODs merely 'direct' or may they 'manage' also? Many experts and practicing top managers say that BODs should only oversee and direct, and never get involved with detailed management. There are others who feel that, for direction to be realistic and sensible, some in-depth involvement with details is necessary. The majority view, however, is in favour of directors directing the affairs of the company and not managing them.

Probably, in the majority of cases in India, the real problem is one of non-involvement of board members—almost to the extent of callousness—in enterprise affairs. Especially in those enterprises which are sick, or are near to this state, it should be clearly decided whether their BODs will merely 'direct' and feel satisfied, for such enterprises often lack competent managers at all levels. So, whom would BODs direct? Is there a need, therefore, for the BODs here to spend more time and 'manage' such enterprises too—for a stipulated period of time?

The board is expected to act with "due care". That is they "must act with that degree of diligence, care, and skill which ordinarily prudent men would exercise under similar circumstances in like positions." If a director or the Board as a whole fails to act with due care and, as a result, the company in some way is harmed, the careless director or directors may be held personally liable for the harm done.

Further, they may be held personally responsible not only for their own actions but also for the actions of the company as a whole.

In addition, directors must make certain that the company is managed in accordance with the laws and regulations of the land. They must also be aware of the needs and demands of the constituent groups so that they can bring about a judicious balance between the interests of these diverse groups, while ensuring at the same time that the company continues to function.

According to Bacon and Brown, a BODs, in terms of strategic management, has three basic tasks.

- **To initiate and determine:** A board can delineate an organisation’s mission and specify strategic options to its management.
- **To evaluate and influence:** A board can examine management proposals, decisions and actions; agree or disagree with them; give advice and offer suggestions; develop alternatives.
- **To monitor:** By acting through its committees, a board can keep abreast of developments, both inside and outside the organisation. It can thus bring new developments to the attention of the management which it might have overlooked.

The members of the board may be having varying commitments to the organisation in terms of their involvement with the above strategic tasks. The degree of involvement of the board in the organisation’s strategic affairs can be viewed as a continuum, ranging from “phantom” boards, with no real involvement, to catalyst boards, with a very high degree of involvement. Expectedly, highly involved boards tend to be very active. They take their task of initiating, evaluating and influencing, and monitoring seriously and provide advice to management whenever it is felt necessary and keep them alert. As depicted in Exhibit 4.1, a catalyst board may be deeply involved in the strategic management process. The BODs of some public enterprises (e.g., BHEL and HMT) and some private sector companies with multinational links (e.g., Hindustan Lever and L&T) have a reputation for their active involvement in strategic affairs. You will see that the degree of involvement lessens as we move further to the left of the continuum. The three types of boards towards the left of the continuum can be described as passive boards. Such boards in general do not initiate or determine strategy. The Board members interest may be aroused only when a crisis overtakes the company. Very few companies are fortunate to have catalyst boards or even boards with active participation, The boards of most of the companies in the private sector will fall in any one of the four categories on the left side of the continuum.

DEGREE OF INVOLVEMENT IN STRATEGIC MANAGEMENT					
Low (passive)			HIGH (Active)		
Phantom	Rubber Stamp	Minimal Review	Nominal Participation	Active Participation	Catalyst
Never knows what to do, if anything, no degree of involvement.	Permits officers to make all decisions. It votes as the officers recommend on action issues.	Formally reviews selected issues that officers bring to its attention	Involved to a limited degree in the performance or review of selected key decisions, indicators, or programs of management	Approves, questions, and makes final decisions on mission, strategy, policies, and objectives. Has an active board committees. Performs fiscal and management audits.	Takes the leading role in establishing and modifying the mission, Objectives, Strategy, and policies. It may have a very active strategy committee.

Exhibit 4.1: Board of Directors Continuum

A great responsibility lies on the chairman of the BODs. It is he who can ensure that the board functions effectively. The influential shareholders, financial institutions, managements of holding companies can also play an important role in this regard.

While a BODs is not expected to involve itself in day-to-day operating decisions, they are nonetheless expected to consider and give their views on all such matters that have long-term connotations. In fact, such matters by convention are referred to the board. These relate to issues such as introduction of a new product, new technology, collaboration agreements, senior management appointments and major decisions regarding industrial relations.

The "directing" function of the board has internal and external components. Internal component relates to various actions taken by the executives and their implications for the organisation, including R&D, capital budgeting, new projects, new competitive thrusts, relationships with financial institutions and banks, foreign collaborators, major customers and suppliers. External component -relates to identifying broad emerging opportunities and threats in the environment and feeding them to the management so that "strategic mismatches" do not occur. The board should see that the organisation always remains in alignment with the social, economic and political milieu.

It is quite likely that many Chief Executive Officers (CEOs) and some board members may not want the board to be involved in strategic matters at more than a superficial level. The reasons are not far to seek. Many companies may not have an explicit or well articulated strategy. The management of such companies take strategic decisions intuitively rather than through a rigorous process of search and analysis. Further, the managements of some companies do not like outside directors to know enough about the new strategic decisions or postures. They may perceive the involvement of board members in strategic decision making as a threat to their power.

Role of Entrepreneurs

According to Drucker, "the entrepreneur always searches for change, responds to it and exploits it as an opportunity". The entrepreneur has been usually considered as the person who starts a new business, is a venture capitalist, has a high level of achievement-motivation, and is naturally endowed with the qualities of enthusiasm, idealism, sense of purpose, and independence of thought and action. However, not all of these qualities are present in all entrepreneurs nor are these found uniformly. An entrepreneur may also demonstrate these qualities in different measures at different stages of life. Contrary to the generally accepted view of entrepreneurship, entrepreneurs are not to be found only in small businesses or new ventures. They are also present in established and large businesses, in service institutions, and also in the bureaucracy and government.

By their very nature, entrepreneurs play a proactive role in strategic management. As initiators, they provide a sense of direction to the organisation, and set objectives and formulate strategies to achieve them. They are major implementers and evaluators of strategies. The strategic management process adopted by entrepreneurs is generally not based on a formal system, and usually they play all strategic roles simultaneously. Strategic decision-making is quick and the entrepreneurs generate a sense of purpose among their subordinates.

Role of SBU-level Executives

The rationale for organising the structure according to SBUs is to be able to manage a diversified company as a portfolio of businesses, each business having a clearly defined product-market segment and a unique strategy. The role that the SBU-level executives play is, therefore, important in strategic management. SBU-level executives, also known as either profit-center heads or divisional heads, are considered the chief executives of a defined business unit for the purpose of strategic management. In practice, however, the concept of an SBU is adapted to suit traditions, shared facilities and distribution channels, and manpower constraints. Therefore, an SBU-level executive wields considerable authority within the SBU while maintaining co-ordination with the other SBUs in the organisation.

With regard to strategic management, SBU-level strategy formulation and implementation are the primary responsibilities of the SBU-level executives. Many public and private sector companies have adopted the SBU concept in some form or the other. "There are several family-managed groups today who boast of their professionally-managed organisation structure. Each of their companies has a chief executive who... has total responsibility.. and authority over the profit center. There are even separate management boards to review the performance of each profit center". At Shriram Fibres, the strategic planning system covered the different businesses ranging from

nylon yarn manufacture to the provision of financial services. Strategic plans were formulated at the level of each SBU as well as at the corporate level. The corporate planning department at the head office coordinated the strategic planning exercise at the SBU level. Each SBU had its own strategic planning cell.

Role of Consultants

Many organisations which do not have a corporate planning department owing to reasons like small size, infrequent requirements, financial constraints, and so on, take the help of external consultants in strategic management. These consultants may be individuals, academicians or consultancy companies specialising in strategic management activities. According to the Management Consultants Association of India, management consultancy is "a professional service performed by specially trained and experienced persons to advise and assist managers and administrators to improve their performance and effectiveness and that of their organisations". Among the many functions that management consultants perform, corporate strategy and planning is one of the important services rendered. The main advantages of hiring consultants are: getting an unbiased and objective opinion from a knowledgeable outsider, cost-effectiveness, and the availability of specialists' skills. According to a senior consultant of a large consultancy firm, the trend is that "family-owned companies and the public sector are relying more heavily on consultancy services than the multinationals". There are many consultancy organisations, large and small, that offer consultancy services in the area of strategic management in India. Instances of companies seeking the help of consultants in various strategic exercises such as diversification, restructuring, and so on, are legion.

It should be noted that consultants do not perform strategic management, they only assist the organisations and their managers in strategic management by working of specific time-bound consultancy assignments.

Role of Corporate Planning Staff

David Hussey has enlisted the many and varied principal responsibilities of corporate planners. Essentially, the corporate-planning staff plays a supporting role in strategic management. It assists the management in all aspects of strategy formulation, implementation and evaluation. Besides this, they are responsible for the preparation and communication of strategic plans, and for conducting special studies and research pertaining to strategic management. It is important to note that the corporate planning department is not responsible for strategic management and usually does not initiate the process on its own. By providing administrative support, it fulfills its functions of assisting the introduction, working, and maintenance of the strategic management system

Role of Middle-level Managers

The major functions of middle-level managers relate to operational matters and, therefore, they rarely play an active role in strategic management. They may, at best, be involved as 'sounding boards' for departmental plans, as implementers of the decisions taken above, followers of policy guidelines, and passive receivers of communication about functional strategic plans. As they are basically involved in the implementation of functional strategies, the middle-level managers are rarely employed for any other purpose in strategic management. This does not, however, preclude the possibility of using their expertise. Many of the examples that we have provided in the previous sub-sections show that managers and assistant managers can also contribute to the generation of ideas, the development of strategic alternatives, the refinement of business, functional and development plans, target-setting at departmental levels, and for various other purposes. The importance of the middle management cadres lies in the fact that they form the catchment areas for developing future strategists for the organisation.

Role of Executive Assistant

The emergence of executive assistants in the managerial hierarchy is a relatively recent phenomenon. An executive assistant is a person who assists the chief executive in the performance of his duties in various ways. These could be: to assist the chief executive in data collection and analysis, suggesting alternatives where decisions are required, preparing briefs of various proposals, projects and reports, helping in public relations and liaison functions, coordinating activities with the internal staff and outsiders, and acting as a filter for the information coming from different sources. Among these "the most important and what one manager labels the 'bread and butter role' of EA (executive assistant) could be that of corporate planner". The reason being that the increasing complexity of business and strategic decision-making has led to a situation where "it is the function of the executive assistant to monitor the changing context and evolve strategies in tandem with senior management". But in companies where a corporate planning department exists, this function not assigned to the executive assistants. Since executive assistants assist the chief executive they help to optimise their time utilisation. In terms of skills and attitudes, the requirements for an executive assistant include a generalist's orientation, a few years' line experience, exposure to different functional areas, excellent written and oral communication ability, and a pleasing personality. Generally the qualification required is an MBA or a CA. The position of an executive assistant offers a unique advantage to young managers as nowhere else can he or she gain a comprehensive view of the organisation, which can help in career planning and development, and rapid advancement to the senior levels of management. We end this chapter on this encouraging note.

Mission and Objectives

The two most basic questions faced by corporate-level strategists are, (1) What business are we in? and (2) Why are we in business?

An answer to the first question requires a consideration of the mission definition, or the scope of the business activities the firm pursues. The second question involves establishing objectives to be accomplished. Both questions help define the nature of the business and provide a framework for analysis, choice, implementation, and evaluation processes.

Mission and Business

For long-term survival (often viewed as the ultimate objective), most organisations must legitimise themselves. This is normally done by performing some function which is valued by society. Of course, some functions are valued more highly than others, and priorities can change over time. In the United States, professional sports teams are valued for their entertainment function, and they have become big business.

Organisations which make a net contribution to society are likely to be called "Legitimate." These organisations are likely to be allowed to survive over the long term. Challenges to legitimacy are not frequent, but once made they can damage survival potential or limit the scope of action and increase the cost of doing business. For example, over a dozen of the largest U.S. defense contractors were under investigation in 1985 for cost and labor mischarges, bribery and kickbacks, defective pricing, and so on. Congress acted to stop payments on some contracts and made it harder to acquire the more lucrative contracts because the legitimacy of the action of these firms was called into question.

Many organisations define the basic reason for their existence in terms of a mission statement. Such a definition can provide the basic philosophy of what the firm is all about. It usually emanates from the entrepreneur who founded the firm or from major strategists in the firm's development over time. The mission can be seen as a link between performing some social function and more specific targets or objectives of the organization. Thus the mission can be used to legitimize the organisation.

When the mission of a business is carefully defined, it provides a statement to insiders and outsiders of what the company stands for—its purpose, image, and character.

Mission definitions can be so broad as to be meaningless, or they can merely be public pronouncements of ideals, which few could ever reach. The specificity and breadth of goal or mission statements are important considerations for strategists. But a good mission statement focuses around customer needs and utilities. For example, AT&T is in communications, not telephones; Tenneco is in energy, not just oil and gas; MGM provides entertainment, not just movies. The customer needs for communication, energy, or entertainment are not product-specific—nor are mission statements. Avon defines itself as being in the beauty business. The mission of most public universities is to provide teaching, research, and public service—but many also provide entertainment (sports teams).

The mission must be clear enough so that it leads to action. Organisations must at some point establish specific targets to shoot for which will be used as guides for evaluating progress. NASA's mission in the 1960s was to begin space exploration and land a man on the moon. Without establishing specific goals to get to along the way, we might be still waiting for that first "small step." So firms also must express their mission and philosophy by establishing statements about the grand design, quality orientation, atmosphere of the enterprise, and the firm's role in society.

After Roger Smith took over as chairman of General Motors, he moved quickly to solve some problems at GM and altered its strategy. As part of the process, he distributed "culture cards" to be carried in the pockets of executives to remind them of their new mission. The card reads

The fundamental purpose of General Motors is to provide products and services of such quality that our customers will receive superior value, our employees and business partners will share in our success, and our stockholders will receive a sustained, superior return on their investment.

Other firms consciously (or subconsciously) develop "core principles," or norms, which guide decision making or behavior. These principles serve as mechanisms for self-control to guide managers at all levels of the organisation. Hence, if quick decisions are needed at lower levels of an organisation, such core principles serve as guides to making decisions or taking action consistent with the overriding mission and strategy of the business. These are different from policies in that they are frequently part of the culture, or ways of doing things, that emerge in the informal organisation.

In practical, everyday decision making, most organisations are not immediately concerned with questions of continued existence. Survival for most is relatively assured within the time frame of thinking of those in charge. And the mission tends to become an ideological position statement which is only occasionally referred to in support of legitimisation. So what tends to occupy the minds of the molders of organisation purpose are various objectives to improve performance. However, prescriptively, a mission statement and core principles ought to serve as guidelines for strategic decisions rather than as a set of platitudes. Otherwise, short-term thinking can get in the way of the long-term best interests of the organisation in society.

Business

Part of the mission statement is the definition of the business itself. By this we mean a description of the products, activities, or functions and markets that the firm presently pursues. Products (or services) are the outputs of value created by the system to be sold to customers. Markets can refer to classes or types of customers or geographic regions where the product and/or service is sold. When we refer to functions, we mean the technologies or processes used to create and add value. For example, in agriculture one might plant and grow seeds, harvest crops, mill grain, process grain into various food products, and distribute or retail the finished product. Each stage adds value and represents a separate function. Some firms do all the functions while others do a limited number or only one. Consider a full-service airline versus a no-frills carrier. One operates full-service ticket counters in airports and downtown locations; the other may ticket on the plane, offer no interline ticketing, offer few fare options, and so on. The no-frills airline may use first come-first-serve seating versus ticketing at gates. On board, the no-frills carrier may not serve

food or drink or charge extra for the service. The full-line carrier may provide free baggage checking while the no-frill firm charges or provides no interline baggage connection. Each of these options represents a service or function configuration. Functions of ticketing, gate operations, on-board service, and baggage handling can provide options for adding value to services provided.

A good business definition will include a statement of products, markets, and functions. For example, a business definition for Apple might state the following: *We design, develop, produce, market, and service microprocessor-based personal computers in United States and foreign countries.* In contrast, Tandy might be defined as *a U.S. manufacturer and retailer of consumer electronic equipment.* Note that Tandy performs fewer functions than Apple and is a bit more restricted geographically, but it has a wider product definition. *Westinghouse manufactures, sells, and services equipment and components which generate, transmit, distribute, utilize, and control electricity.* Note that this definition includes a very broad line: it specifies a locus around which the products are related but ignores market issues (except for the notion that its markets involve electricity). In its 1985 Annual Report, Schulerberger asks, What are our businesses? The answer:

First, we are an oilfield services company, bringing technology to the oil industry anywhere, anytime. [We are] also an electronics company. We are ready to expand in the international markets through leadership in electricity, . . . electronic payments, . . . instruments, bringing technology to the utilities, to the aerospace industry, to the banking community. . .

A good statement of the business definition of the firm should meet certain criteria: it should be as precise as possible and indicate major components of strategy (products, markets, and functions). Some go a bit further than this by also indicating how the mission is to be accomplished.

Defining the mission and business definition is the starting point of strategy analysis. It answers the question, What business are we in? When performing the initial gap analysis we find that such a statement indicates where the firm's current strategy has been going up to this point is time and what results might be expected if it continues. From there, once objectives have been specified and other analyses have been performed, determinations can be made about whether such a definition can continue successfully, or must be altered to close gaps. In other words, the strategic management process starts with the current business definition but proceeds with other questions: What business should we be in? Who are our customers? How do we serve them? That is, some conditions might call for a strategic change in products, markets, or functions, or changes in the way in which that business definition is going to be accomplished (competitive strategy and policies). For example, long after cars, interstate highways, and airplanes sent many railroad companies into bankruptcy court, some railroad companies are reemerging with new corporate identities. The Reading Company, a major regional railroad established in 1833, now owns only 16 miles of track. Like many former railroad firms, Reading is now a major real estate operator (even though the Monopoly game board earns it immortality as a railroad).

A problem many firms find themselves with is that through acquiring a series of businesses unrelated to their mission or business definition, they become conglomerates, with little to tie them together other than financial objectives. Many firms have found a need to return to basic business definitions because they cannot effectively manage the diversity. It took General Mills longer than most, but after 17 years of trying they finally sold off their toy division and nonfood lines to "get back to the kitchen," which they knew best about.

Changing the business definition is one of the basic strategy alternatives. But before strategy determination is made, the other major aspect of strategic gap analysis is a determination of whether desired objectives will be attained. Analysts must determine if continuation with the mission and adherence to the business definition will lead to expected outcomes close to those desired.

What Objectives and Goals Are Pursued?

Objectives are the ends which the organisation seeks to achieve through its existence and operations. A variety of

different objectives are pursued by business organisations. Some examples include continuity of profits; efficiency (for example, lowest costs); employee satisfaction and development; quality products or services for customers or clients; good corporate citizenship and social responsibility; market leadership (for example, to be first to market with innovations); maximization of dividends or share prices for stockholders; control over assets; adaptability and flexibility; service to society.

It is important that several points be made about objectives so that you understand their nature fully. These are as follows:

- The list just given contains 10 objectives, which is not to suggest that most organisations pursue 10 objectives or these exact 10. But research clearly demonstrates that firms have many objectives. *All but the simplest organisations pursue multiple objectives.*
- Many organisations pursue some objectives in the short run and others in long run. For example, with respect to the list of 10 objectives, many firms would view efficiency and employee satisfaction as short-run objectives. They would probably view profit continuity, service to society, and good corporate citizenship as long-run objectives. Some other objectives such as adaptability or asset control may be medium-range objectives. *In sum, the objectives pursued are given a time weighting by strategists.*

One of the major dilemmas of corporate-level strategists is the short-term-long-term trade-off decision. With the logic of net present value and the importance of return on investment, combined with pressures from Wall Street and corporate raiders for good quick profits and cash flows, modern managers have been pressured toward short-term thinking. This kind of thinking also filters down to the business level where a desire for quick returns may influence SBU managers. There appears to be less patience to invest in the future in the United States than there is in other countries (such as Japan). This lack of patience can have a severe impact on strategic decision making; and the timing of goal accomplishment needs careful analysis in this regard

- Since there are multiple objectives in the short run at any one time, normally some of the objectives are weighted more highly than others. The strategists are responsible for establishing the priorities of the objectives. Priorities are crucial when resources and time are limited. At such times, trade-offs between profitability and market share, etc., must be known so that the major objective of the particular time is achieved. Thus *strategists should establish priorities for each objective among all the objectives at corporate and SBU levels*
- There are many ways to measure and define the achievement of each objective. For example, some objectives can be measured through the use of an efficiency criterion; others may be measured in terms of effectiveness. Efficiency is the ratio of inputs to outputs. Effectiveness refers to the degree of achievement of a goal in relation to some ideal. At times, trade-offs between efficiency and effectiveness are required. For example, installing pollution-control equipment may be effective in achieving clean-air goals, but these goals may be achieved at the expense of a goal of efficient plant operation. At other times, trade-offs of efficiency goals within units of an organisation are required. This is a basic factor in *suboptimisation*. As each subsystem seeks efficiency, the entire system may lose effectiveness. For example, a credit manager is charged with establishing a policy to minimise credit losses; a sales manager is asked to maximise sales. If they both maximise in their own way, conflict is likely. Sales to some classes of customers will increase credit risk. Trade-offs in the goals of each unit may be called for. Here, goal priorities of the whole organisation need to take precedence. In each part of the organisation such goal conflicts are likely and require resolution. The guidance should come from mission definitions. *The implementation phase of strategic management involves clarifying the measurement of achievement, of objectives.*
- There is a difference between official objectives and operative objectives. Operative objectives are ends *actually* sought by the organisation. They can be determined by analysing the behavior of the executives in

allocating resources. Official objectives are ends which firms *say they seek* on official occasions such as public statements to general audiences. The objectives that *count* are those the strategists put their money and time behind. For instance, executives' official goals may focus on providing employees with a quality work environment; whether operative goals are the same depends on how much money is spent to improve actual working conditions.

An official goal may be to contribute to social responsibility; yet a firm may fail to spend money on pollution-control equipment or even fight regulations designed to prevent acid rain because of the costs involved. Or a firm may state that it wishes to integrate activities of SBUs to achieve synergy while its organisation structure grants decentralised autonomy to divisions which prevent this from happening. Anderson, Clayton & Co. has searched for an acquisition in the food business for a decade; but analysis suggest its refusal to take on a debt to clinch a big acquisition really suggests that its operative goal is to not discourage potential buyers of the firm itself. According to one former officer, "they are managing the company to be sold."

- *There may be limits to the attainment of some goals.* Some firms may try to maximise shareholder wealth but find that they are constrained by the need for funds to achieve lower-cost operations to meet competition. Excessive increases in market share might come at the cost of unpleasant antitrust consequences, which, in effect, could be counterproductive from a survival perspective. Again, there are trade-offs among goals which managers must make.
- Finally, *objectives are not strategies.* Strategies are means to an end. Note that expansion was not among the objectives listed. Expansion is one type of strategy but not an end in itself. In itself, expansion of sales or assets may not improve performance. But cutting back (retrenchment) in certain areas of the operation could also be a way to increase efficiency and improve performance. So expansion and retrenchment are ways in which goals can be achieved, and both can lead to performance increases (e.g., growth in returns). Not all managers agree with this distinction, but we believe it is an important one. (This is a problem with strategic management terminology in general.)

One other issue regarding objectives which has become important to strategists is the priority attached to objectives relating to social responsibility. Social responsibility is an ill-defined term, but the basic idea is that the economic functions provided by business *ought to be* performed in such a way that other social functions are, at worst, unharmed and, at best, promoted. Thus businesses are urged to be as concerned with human rights, environmental protection, equality of opportunity, and the like, as they are with providing outcomes such as economic efficiency.

Several dilemmas arise. A major problem is how to define socially responsive behavior. Value systems are so diverse that achieving consensus on this issue is difficult. Equally problematic is the fact that economic organisations automatically take resources from organisations in other sectors and often detract from performing other societal functions. Businesses weren't designed to promote public health, safety and welfare (though some use charitable giving as a marketing ploy). A common example is detrimental health effects from pollution created by the production of goods. Do we stop producing goods? Do we increase costs to the extent that other societal goals are adversely affected? For instance, a completely safe automobile might be so expensive that possible cost increases to protect human safety become detrimental to economic well-being. Cost-benefit trade-offs are extremely difficult to make.

In some cases, external threats can be so severe as to call into question the legitimacy of the mission of the organisation, as in the case of utilities which generate power with nuclear plants. Policies to deal with these concerns include ignoring the issue, using public relations campaigns to try to mitigate unfavorable publicity, and altering goal priorities and changing strategies. Some creative strategists try to turn these kinds of threats into opportunities. For instance, some coal companies have increased the value of land originally used for strip-mining by converting the strip mines into recreation complexes. But these options are not always available. In any case, decision makers are being urged to increase the priority given to these concerns by some.

On the other hand, businesses are also criticised if they stray too far from their economic function. For instance, business firms are chastised for creating political action committees as a means to influence their environment.

While research evidence is mixed, the predominant view is that social responsibility bears little (positive or negative) relationship to financial performance objectives. Clearly, then, establishing goal priorities and resource allocation requires a consideration of issues beyond simple economic efficiencies.

Objectives

Why do firms have objectives, and why are they important to strategic management? There are four reasons.

- 1 *Objectives help define the organisation in its environment.* Most organisations need to justify their existence, to legitimise themselves in the eyes of the government, customers, and society at large. And by stating objectives, they also attract people who identify with the objectives to work for them. Thus objectives define the enterprise.
- 2 *Objectives help in coordinating decisions and decision makers.* Stated objectives direct the attention of employees to desirable standards of behavior. It may reduce conflict in decision making if all employees know what the objectives are. Objectives become constraints on decisions.
- 3 *Objectives provide standards for assessing organisational performance.* Objectives provide the ultimate standard by which the organisation judges itself. Without objectives, the organisation has no clear basis for evaluating its success.
- 4 *Objectives are more tangible targets than mission statements.* The products of an organisation or the services it performs (outputs) are probably the most familiar terms in which people tend to think of objectives or goals. (It's easier to see Hallmark as a producer of cards and gifts than to imagine the company as being in "the social-expression business.") Output goals may also be thought of in terms of quality, variety, and the types of customers or clients who are the intended target. Nonetheless, it may be deceptively easy to link output goals with mission definitions. For instance, Henry Ford's original mission of "providing transportation for the common man" was easily seen through the production of the Model A. But the private hospital offering a large range of services with the best doctors and equipment may be available to only a few rich clients; it may be profitable with these services and judged effective by some, but others will argue that it fails to satisfy a larger mission of equal health care treatment (note the social responsibility element here).

Mission and objectives ought to be considered at each stage of the strategic management process. In the assessment of environmental conditions, expected changes may force rethinking about goal priorities (e.g., changing government tax regulations may suggest a different treatment of dividend payout or retained earnings). In an analysis of internal conditions, a goal of employee welfare might alter perceptions about unionisation. In choosing alternative strategies, a change in business definition could lead to decisions to get out of some businesses in favor of others. If a goal of flexibility is desired, the implementation of a strategy could lead to a new form of organisation structure. So at each stage of the process, mission, business definition, and objectives should guide decision-making.

To carry this a bit further and illustrate how objectives relate to the process as a whole, we consider the gap analysis as outlined in Exhibit 4.2. Point *A* is the current level of attainment an enterprise has reached at this time (t_1). Point *B* is the ideal point at which management would like to see itself at some point in the future (t_2). If, as a result of following the strategic management process, the firm sees itself pursuing the *same strategy* with a given set of assumptions about its environment management may believe it will arrive at point *C* at t_2 . The gap of interest which could trigger either *strategic change* or *goal change* is that between *B* and *C*. Note that the gap between the existing state and the desired state is not as important as the gap between the *expected state* and the *desired state*.

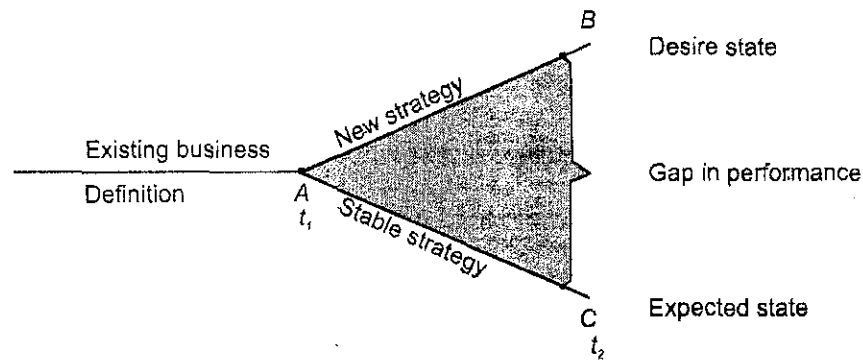


Exhibit 4.2: Gap Analysis for Objectives

The perception of this gap is important in terms of significance, importance, and reducibility. With these conditions in mind, note that several basic choices are available, if the gap is significant, important, and reducible an attempt could be made to alter strategy so that the expected state (point C) will come closer to the desired state (B). If the gap is significant and important but not reducible, point B might be altered (e.g., expectations might be lowered). If the gap is significant and reducible but not important, once again point B can be altered. The goal that is sought becomes less critical when compared with other goals. If the gap is *neither* significant, important, nor reducible, no change will occur—a stability strategy (continuing past approaches in similar ways) is likely to be followed.

This is a prescriptive way to examine the analysis of objectives as a component of the strategic management process. But other factors influence the nature of the perceptions of these gaps as objectives are formulated.

How Are Mission and Objectives Formulated?

We believe that missions and objectives are formulated by the corporate-level strategists. But these executives do not make choices in a vacuum. Their choices are affected by several factors: the realities of the external environment and external power relationships, the realities of the enterprise's resources and internal power relationships, the value systems and goals of the top executives, and past strategy and development of the enterprise.

The first factor affecting the formulation of mission and objectives is *forces in the environment*. The stakeholders with whom the organization has an exchange relationship will present demands or claims (expectations). These can be thought of as constraints on objectives. The stakeholders may vary, the nature of their constraints (expectations or claims) can change, and their power vis-a-vis the organization and one another may change. Taken together, they represent one set of forces within which managerial objectives must be established. The claims of the most powerful stakeholders will be met, so long as the entire set of objectives falls within the constraints imposed by the set of stakeholders.

Suppose that managers want to choose maximization of sales as an objective. They may have to modify this objective because of governmental regulations regarding excess profits, antitrust legislation, consumer labeling, and so on. Trade unions may require higher-than-market wage rates or fringe benefits which lead to higher costs (possibly reducing sales). Competitors may sell other products or services at unrealistically low prices and spend excessive amounts on advertising. Suppliers may become monopolized and charge outrageous prices. If the organization is more dependent on suppliers than on any other stakeholders, the operative objective may very well be limited by the availability and cost of supplies.

So the prudent strategist will ask a variety of questions when establishing mission, objectives, and strategy: Who are the critical stakeholders? What are our critical assumptions about each stakeholder? How do stakeholders affect each division, business, or function at various points in time. And what changes can be expected among the stakeholder groups in the future?

The second factor affecting the formulation of mission and objectives is the *realities of the enterprise's resources and internal power relationships*. Larger and more profitable firms have more resources with which to respond to forces in the environment than do smaller or poorer firms.

In addition to this, the internal political relationships affect mission and objectives. First, how much support does management have relative to others in the organisation? Does the management have the full support of the stockholders? For example, Paul Smucker has the support of the Smucker family stockholders to emphasize quality as an objective for his jam and preserves firm. If the management has developed the support of employees and key employee groups like the professional employees' lower and middle management, then it can set higher objectives that employees will help achieve.

Mission and objectives are also influenced by the power relationships among the strategists either as individuals or as representatives of units within the organisation. Thus if there is a difference of opinion on which objectives to seek or the trade-offs among them, power relationships may help settle the difference.

A final internal factor is the potential power of lower-level participants to withhold information and ideas. To the extent that this occurs, the evaluation of past goal attainment and expectations about the future can be affected. For instance, consider the sales manager who tries to hide the fact that a competitor's new product is starting to hurt sales. This might be an attempt to protect the unit, but it could mislead top managers regarding future goals and strategies. Or lower-level managers might decide whether or not to forward a proposal which could lead to goal changes on the basis of what they *think* top management is (or is not) ready to accept. Thus the exercise of this type of informal power can play a role in the selection of objectives.

Mintzberg has advanced a theory about formulation of objectives that combines the stakeholder forces described earlier with the internal power relationships. He believes that power plays result from interactions of internal and external coalitions.

External coalition	Internal Coalition	Power Configuration
Dominated	Bureaucratic	The Instrument
Passive	Bureaucratic	The Closed System
Passive	Personalised	The Autocracy
Passive	Ideological	The Missionary
Passive	Professional	The Meritocracy
Divided	Politicised	The Political Arena

Exhibit 4.3: Six Pure Power Configuration Affecting Objectives Formulation

- The external coalition includes owners, suppliers, unions, and the public. These groups influence the firm through social norms, specific constraints, pressure campaigns, direct controls, and membership on the board of directors. Mintzberg specifies three types of external coalitions, noted in Exhibit 4.3.
- The internal coalition includes top management, middle-line managers, operators, analysts, and support staff. These groups influence the firm through the personnel control system, the bureaucratic control system, the political system, and the system of ideology. Mintzberg specifies 5 types of internal coalitions, shown in Exhibit 4.3.

Mintzberg says that there are six basic power configurations, as shown in Exhibit 4.3 In the instrument power configuration, one external influence with clear objectives, typically the owner, is able to strongly influence objectives through the top manager. In a closed-system power configuration, power to set objectives rests with the top manager, who sets the objectives. This is also true in the autocracy power configuration. In the missionary power configuration, objectives are strongly influenced by past ideology and a charismatic leader. Ideology tends to dictate the objectives. In the meritocracy power configuration, the objectives are set by a consensus of the members, most of whom are professionals.

Thus the formulation of mission and objectives can be a simple process: the top manager sets them subject to the

environment. Or, more frequently, they are set by a complex interplay of past and present, internal and external role players. The third factor affecting the formulation of mission and objectives is the value *system of the top executives*. Enterprises with strong value systems or ideologies will attract and retain managers whose values are similar. These values are essentially set of attitudes about what is good or bad, desirable or undesirable. These in turn will influence the perception of the advantages and disadvantages of strategic action and the choice of objectives. Exhibit 4.4 lists the extremes of six selected values. Let's look at each of these to see how they might affect objectives.

1	Very combative	Very passive
2	Very innovative	No innovative
3	Risk-oriented	Risk-averse
4	Quality	Quantity
5	Autocratic	Participative
6	Personal goals	Shareholder goals

Exhibit 4.4: Values Toward Various Groups In The Strategic Situation

The following list corresponds to the continuum in Exhibit 4.4. Each dimension is explained below:

1. Some executives believe that to be successful a firm must attack in the market-place. Others believe that you "go along to get along."
2. Some executives believe that to succeed a firm must innovate. Others prefer to "let others make the mistakes first."
3. Some executives know that to "win big, you must take big risks." Others comment, "Risk runs both ways."
4. Some executives believe that one becomes successful by producing quality. Others go for volume.
5. Some executives believe that one should treat employees in a manner that makes them know who the boss is. Others believe that cooperation comes from a participative style.
6. Some executives believe that they should be primary beneficiaries of corporate success while others think the business is operated for the benefit of stockholders.

You can see that one set of executives with the set of values on the left would be inclined to emphasize a different set or different level of objectives than those who accept the set of values on the right in Exhibit 4.4. For instance, risk-oriented innovators might see significantly larger gaps between where they want to be and where they expect to be than risk averters. Managers on the left on number 6 will avoid hostile takeovers to protect their jobs, even if it comes at the expense of shareholder loss. Corporate raiders often recognize this, and receive "greenmail" for their effort.

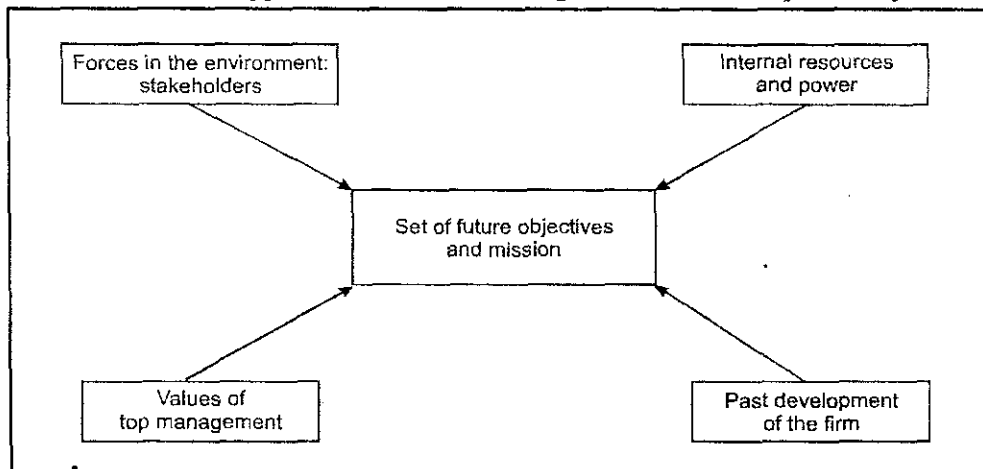
Prescriptively, from a "maximizing" decision perspective, these and other kinds of values *ought not* be considered when goals are being established. Yet some believe that it is better to recognize the inevitability of their influence on decision makers. That is, even if they are not explicitly stated, value assumptions will be implicit in decision premises and the types and forms of data collected. Consequently, stating these values in the form of assumptions is one technique recommended to force these values explicitly into the open, if they are included, the bases upon which decisions are made can be considered "more, rational" than if decision makers pretended that these factors don't exist.

The fourth factor affecting the formulation of mission and objectives is the *awareness by management of the past development of the firm*. Management does not begin from scratch each year. It begins with the most recent mission and objectives. These may have been set by strong leaders in the past. The leaders consider incremental changes from the present, given the current environment and current demands of the conflicting groups. The managers have developed aspiration levels of what the objectives ought to be in a future period. But by muddling through, they

Roles of Strategists, Mission and Objectives

set the current set of objectives to satisfy as many of the demands and their wishes as they can. The momentum of the large organisation and its strategies and policies are all current designed to accomplish the existing mission and objectives. Just as it takes time to turn a large ship around, it usually takes time to make major corporate change.

Let's summarise what has been said so far on how mission and objectives are established. The factors are shown in Exhibit 4.5. Mission and objectives are not the result of managerial power alone. These result from the managers' trying to satisfy the needs of all groups involved with the enterprise. These coalitions of interest (stockholders, employees, suppliers, customers, and others) sometimes have conflicting interests. As the strongest coalition group, managers try to reconcile the conflicts. Management cannot settle them once and for all. Management "bargains" with the various groups and tries to produce a set of objectives and a mission which can satisfy the groups at that time. The goals of these groups are considered in relation to past goals. This is a very complicated, largely consensus-building process with no precise beginning or end. And at any given time, only a few specific goals can be grasped and comprehended by any single executive. Thus there appears to be a need for a grander vision as expressed by a mission definition.



Note: Each of these factors represents a set of constraints on the establishment of the priorities among future objectives. The set of mission and objectives considered at any one time is also limited.

Exhibit 4.5: Factors Influencing the Formulation of Objectives and Mission

Mission and objectives will become a meaningful part of the strategic management process only if corporate strategists formulate them well and communicate them and reinforce them throughout the enterprise. The strategic management process will be successful to the extent that general managers participate in formulating the mission and objectives and to the extent that these reflect the values of management and the realities of the organisation's situation. These factors also play a role in strategic choice.

Why Do Mission and Objectives Change?

Although organisations tend toward stability, mission and objectives change over time. As discussed before, objectives could change on the basis of a rational analysis of a gap between expected and desired states. That is a normative approach. But what might lead to the determination of the states themselves? Are there some factors which would lead to different perceptions regarding the gaps between goals and how the future goal states might be arrived at?

On the basis of the foregoing discussion of how mission and objectives are formulated, we can present some descriptive reasons why mission or objectives might change.

- The aspiration levels of managers could alter goal orientations. They may begin to extrapolate past achievement and say that the enterprise can do more. Or they may look at what relevant competitors or other enterprises have achieved and decide to match or exceed these levels. The arrival of a new CEO from outside the

organisation is the most prevalent condition under which mission and goals are reconsidered. New managers from the outside who are not tied or committed to past strategy and ideology are more likely to alter the mission, objectives, and strategies of an organisation than are new CEOs from the inside.

- *The mission can change in a crisis.* When a firm's market disappears, for example, or its reason for being ceases, a crisis exists. Some firms supplying equipment to the oil industry discovered this in 1974 and again in 1982 and 1986. Faced with an uncertain future, their objectives have begun to focus on flexibility. When the cure for polio was found, the mission of the National Foundation for Infantile Paralysis changed. So the attainment of objectives can also lead to a crisis or new opportunities can create an identity crisis if a firm seeks to take advantage of them.
- *Demands from coalition groups that make up the enterprise can change.* This often occurs as the membership or leadership of groups changes or as internal power groups change. For instance, new government or labor leaders or new competitors can alter the way a business sets its goal-priorities. Similarly, if the comptroller becomes more powerful internally, the firm might begin to stress shorter-term financial goals.
- Normal life-cycle changes may occur which alter goal orientations. Though the analogy with humans can be taken too far, there may be changes in objectives or strategies which "naturally" occur in the aging process. Of course, organisations may have more control over the sequencing and timing of these stages than humans. Yet it is often difficult for an organisation to know what stage it is in. And we're not sure what might precipitate organisational aging or movement. We do know that commitment to the past may hinder change, and new agents in coalition groups are likely to hasten it.

These four classes of factors—*aspirations, crisis, demands, and development*—can be used to predict the likelihood that mission and objectives will remain similar to those of the past or be subject to redefinition. Thus in considering how mission and objectives are formulated, we must examine various pressures for stability or change before a gap analysis can be effectively done.

Chapter 5

Strategic Business Unit

A strategic business unit (SBU) is an operating division of firm which serves a distinct product-market segment or a well-defined set of customers or a geographic area. The SBU is given the authority to make its own strategic decisions within corporate guidelines as long as it meets corporate objectives.

Generally, SBUs are involved in a single line of business. A complementary cept to the SBU, valid for the external environment of a company, is a strategic business area (SBA). It is defined as "a distinctive segment of the environment in which the firm does (or may want to do) business".

A number of SBUs, relevant for different SBAs form a cluster of units under a corporate umbrella. Each one of the SBUs has its own functional departments, or a few major functional departments, while common functions are grouped under the corporate level. These different levels are illustrated in Exhibit 5.1. Two types of levels are depicted in this exhibit. One relates to the organisational levels and the other to the strategic levels. The organisational levels are those of the corporate, SBU and functions! levels. The strategic levels are those of the corporate, SBU and functional level strategies.

Corporate level strategy is an overarching plan of action covering the various functions performed by different SBUs. The plan deals with the objectives of the company, allocation of resources and coordination of the SBUs for optimal performance.

SBU level (or business) strategy is a comprehensive plan providing objectives for SBUs, allocation of resources among functional areas, and coordination between them for making an optimal contribution to the achievement of corporate level objectives.

Functional strategy deals with a relatively restricted plan providing objectives for a specific function, allocation of resources among different operations within that functional area, and coordination between them for optimal contribution to the achievement of SBU and corporate-level objectives.

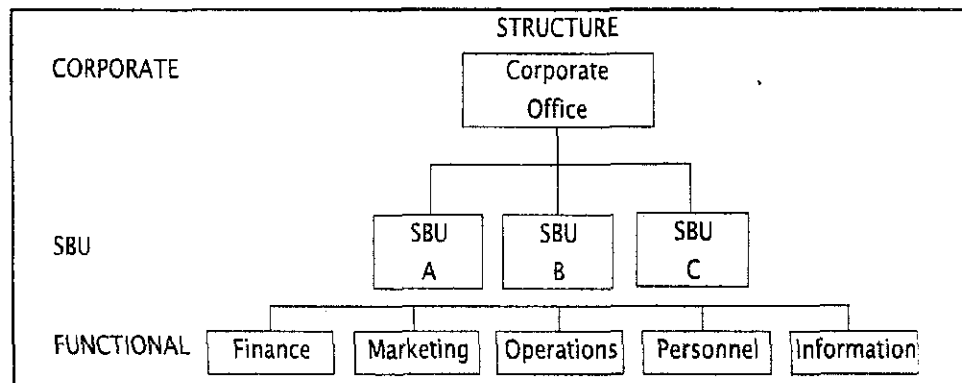


Exhibit 5.1: Different Levels of SBUs

Apart from the three levels at which strategic plans are made, occasionally companies plan at some other levels too. Firms often set strategies at a level higher than the corporate level. These are called the societal strategies. Based on a mission statement, a societal strategy is a generalised view of how the corporation relates itself to society in terms of a particular need or a set of needs that it strives to fulfill. Corporate-level strategies could then be based on the societal strategy. Suppose a corporation decides to provide alternative sources of energy for society at an optimum price and based on the latest available technology. On the basis of its societal strategy, the corporation has a number

of alternatives with regard to the businesses it can take up. It can either be a manufacturer of nuclear power reactors, a maker of equipments used for tapping solar energy, or a builder of windmills, among other alternatives. The choice is wide and being in one of these diverse fields would still keep the corporation within the limits set by its societal strategy. Corporate- and business-level strategies derive their rationale from the societal strategy.

Some strategies are also required to be set at lower levels. One step down the functional level, a company could set its operations-level strategies. Each functional area could have a number of operational strategies. These would deal with a highly specific and narrowly-defined area. For instance, a functional strategy at the marketing level could be subdivided into sales, distribution, pricing, product and advertising strategies. Activities in each of the operational areas of marketing, whether sales or advertising, could be performed in such a way that they contribute to the functional objectives of the marketing department. The functional strategy of marketing is interlinked with those of the finance, production and personnel departments. All these functional strategies operate under the SBU-level. Different SBU-level strategies are put into action under the corporate-level strategy which, in turn, is derived from the societal-level strategy of a corporation. Ideally, a perfect match is envisaged among all strategies at different levels so that a corporation, its constituent companies, their different SBUs, the functions in each SBU, and various operational areas in every functional area are synchronised. Perceived in this manner, an organisation moves ahead towards its objectives and mission like a well-oiled piece of machinery. Such an ideal, though extremely difficult—if not impossible of attainment—is the intent of strategic management.

Societal strategies are manifest in the form of vision and mission statements, while functional and operational strategies take the shape of functional and operational implementation, respectively.

Strategic Management in Multiple-SBU Businesses

In small businesses or in businesses which focus on one product or service line, the “corporate-level” strategy serves the whole business. This strategy is implemented at the next lower level by functional plans and policies. This relationship is illustrated in Exhibit 5.2.

In conglomerates and multiple-industry firms, the business often inserts a level of management between the corporate and functional levels. In some firms, these units are called “operating divisions” or, more commonly, strategic business units (SBUs). In these firms, the strategies of these units are guided by the corporate strategies, but they may differ from one another. This situation operates as shown in Exhibit 5.3.

Each SBU sets its own business strategies to make the best use of its resources (its strategic advantages) given the environment it faces. The overall corporate strategy sets the long-term objectives of the firm and the broad constraints and resources within which the SBU operates. The corporate level will help the SBU define its scope of operations. It also limits or enhances the SBU’s operations by means of the resources it assigns to the SBU. Thus at the corporate level in multiple-SBU firms, the strategy focuses on the “portfolio” of SBUs the firm wishes to put together to accomplish its objectives.

For example, Mobil Corporation hired a new chief executive with the charge of revitalising Montgomery Ward, one of its poor-performing SBUs. The SBU is being pared down and turned into a specialty retailer since it has not been able to compete well as a general merchandiser. Corporate-level management set goals and has its own strategy (that of divesting Ward if it doesn’t perform); but the SBU has determined its own strategy for how to redefine its business and compete effectively.

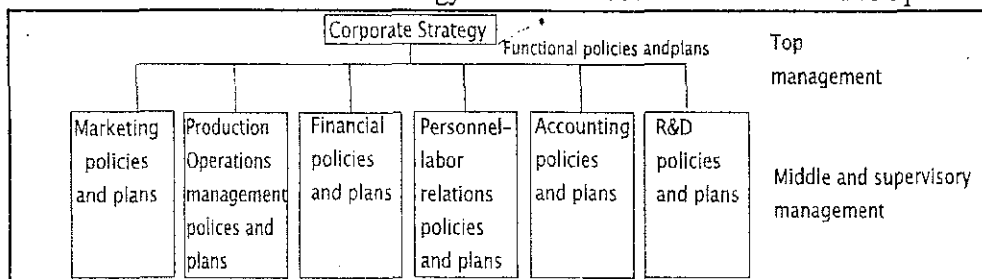


Exhibit 5.2: Relationship of Corporate Strategy and Functional Plans and Policies at Single-SBU Firms

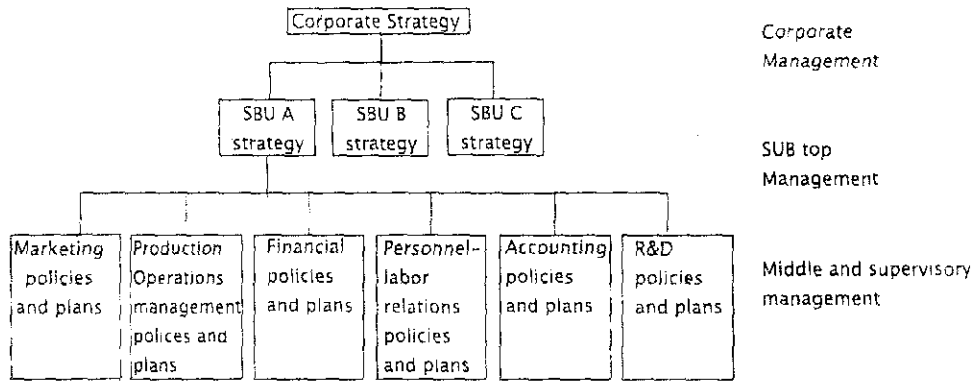


Exhibit 5.3. Relationship Among Strategies and Policies and Plans in Firms with Multiple SBUs.

Some writers make distinctions between corporate strategy, business strategy, and functional-level strategy, maintaining that corporate strategy focuses on the mission of the firm, the businesses that it enters or exits, and the mix of SBUs and resource allocations. Business strategy, then, focuses on how to compete in an industry or strategic subgroup, and how to achieve competitive advantage. At the functional level, plans and policies to be carried out (by marketing, manufacturing, personnel, and so on) are designed to implement corporate and business strategy to make the firm competitive.

Roger Smith, chairman of GM, has stated, "Unless we want to play a perpetual game of catch-up, we ... have to do more than just meet our competition on a day-to-day basis. We have to beat them in long-term strategy." Choices about how to compete should be considered in the decision about whether to exit or enter a business, as our earlier example about Montgomery Ward illustrated. And the implementation of a strategy will determine how effectively the choice will be carried out. Hence, we believe that the process described here can assist in the reader's thinking about business and competitive strategy.

As mentioned before, the model in Exhibit 5.2 is for a single-SBU firm. For a multiple-SBU firm the model is adjusted so that the process is conducted at corporate and SBU levels. The results of these processes feed into one another. However, at both levels, the process involves appraisal, choice, implementation, and evaluation.

Strategic decision making in multiple-SBU firms involves interrelationships between corporate-level and business-level planning. As can be seen in Exhibit 5.4 the corporate-level executives first determine the overall corporate strategy. They do this after examining the level of achievement of objectives relative to their SBUs and other businesses they could enter. Next they assess how the SBUs are doing relative to each other and potential SBUs. Then they allocate funds to the SBUs and establish policies and objectives with them.

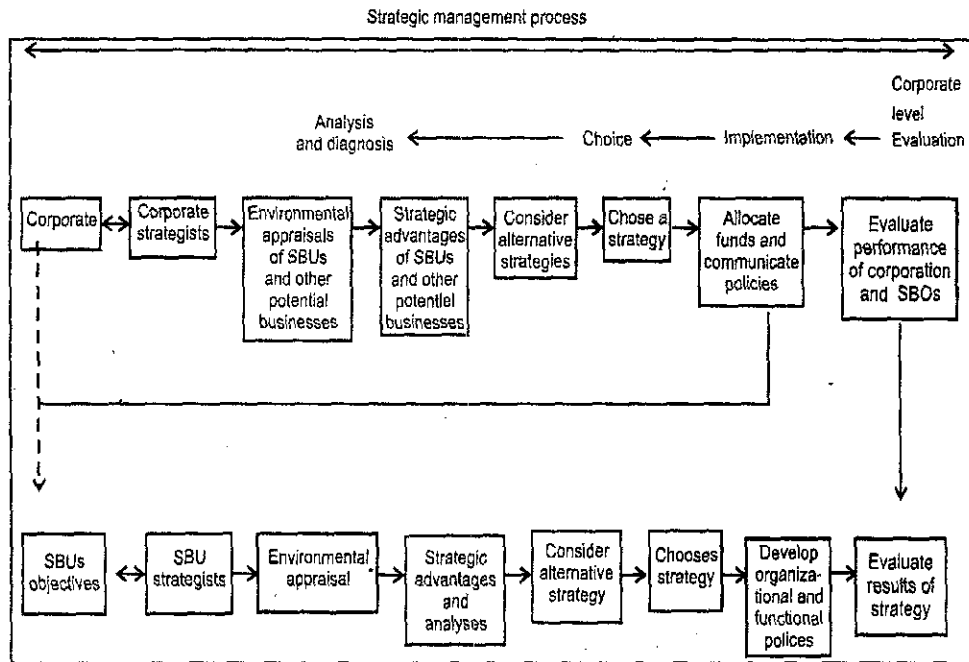


Exhibit 5.4: A Model of the Strategic Management Process for a Firm with Multiple SBUs using First-Generation Planning

At this point the SBUs analyse, within the guidelines set by the corporate level, how they can create the most effective strategy to achieve their objectives.

This model is, of course, a simplified representation. Depending on various organisation designs, the interrelationships among units and planning processes can be quite complex in a series of iterative interactions across levels and subunits. Moreover, conflicts between the corporate level and the SBU level can create problems for both. SBU managers usually seek greater resource allocations in an attempt to expand their units. Corporate level, however, may wish to stabilize a unit or use cash flows from one unit to support another SBU. For example, while the head of the tobacco unit at Philip Morris in the early 1980s wanted growth in cigarette volume and new-product development, funds were being used to promote sales of the Miller Brewing acquisition. Discussions between SBUs and corporate level must consider overall goals and resource needs.

Chapter 6

Environment - Concept, Components and Appraisal

Understanding the environmental context of a company is of immense significance. *Successful strategies are those where the company adapts to its environment.* Companies that fail to adapt to their environment are unlikely to survive in the long run, and tend, like dinosaurs, to disappear.

An example of this type of failure is provided by the near demise of the UK motorcycle industry, which failed because it did not mount an effective strategic reaction to a major environmental change—namely the emergence of its Japanese counterpart. Japanese producers planned and managed their motorcycle industry on an international basis, i.e. they built factories that were designed to serve the world market rather than just their domestic market, thus having the advantage of economies of scale. Such a development was a major competitive innovation to which the UK companies, with their much less automated production and smaller sales targets, were unable to respond effectively.

Environment would be classified as follows :

- Macro environment
- Industry environment
- Competitive environment
- Internal environment

We further classified these individual classes or segments. Thus, for instance, the macro environment was further classified into:

- Social factors, e.g. demographic changes
- Technological factors
- Economic factors, e.g. prime interest rates, consumer price index, etc.
- Political factors

The process of environmental analysis presents the strategic planner with a dilemma: if all those environmental elements that *could* have some influence on a company are included, then the analysis becomes extremely complex and unwieldy. Alternatively, if, in the interest of reducing the level of complexity, certain environmental elements are omitted, then certain crucial environmental forces may be left out of the analysis. In practice, deciding upon the appropriate balance between the width of environmental analysis and its depth is frequently a function of the nature of the industry, and requires knowledge, experience, and judgement on the part of the strategic planner.

In the discussion to follow, we would adopt a three stage approach to analysing the environment:

- Stage I: Segmenting the environment
- Stage II: Analysing the segments
- Stage III: Attributing weights to each segment.

Above, we have already segmented the environment. In what follows, we provide some elaboration of each segment and thereafter analyse it, ending with a discussion of the method of attributing weight to each segment.

Segmenting Environment and Analysing Environmental Segments

Macro Environment

Social Factors

Demographic Changes

The decade of the eighties has seen the impact of the post War baby boom generation throughout The world. The age of the prime workforce and prime consumer population belonged to this generation, and their tastes and habits influenced the habits and purchasing choices in the market, on the one hand, and motivated the manufacturing sector, on the other. Some features of this impact are worth listing.

- A general increase in the educational level.
- A distinct shift in the value system, resulting in discernable cultural dissatisfaction at the workplace, which in turn affected productivity.
- Increase in productivity, even if at a less than expected pace, augmented by automation.

Simultaneously, changes in the value system and education have brought in their wake increased employee participation and involvement in decision-making activities. The growth of the service industry has only height-ened the process. Such changes require changed operating procedures, shared information services, and shared authority.

A Model of Ethics: Perhaps some of these changes in the social environment may be systematically viewed somewhat differently, we may approach it through a model of ethics, as shown in Exhibit 6.1. From the figure, it can be seen that ethics consists principally of two relationships, indicated by arrows in the figure. A person or organisation is ethical if these relationships are strong.

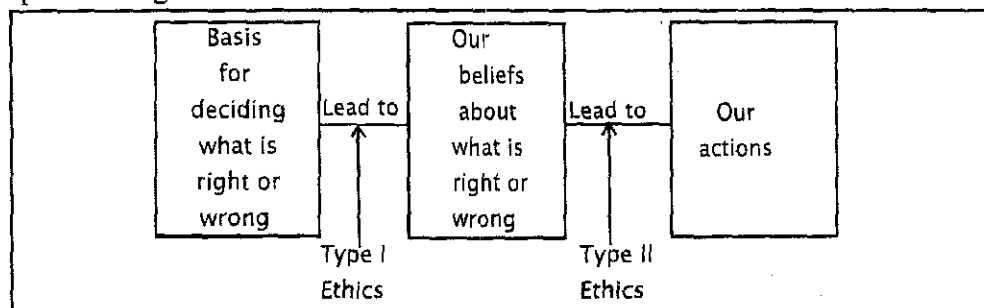


Exhibit 6.1: Model of Ethics

There are a number of sources that could be used to determine what is right or wrong, good or bad, moral or immoral behaviour. These include, for instance, the 'holy' books, the still small voice that many refer to as conscience. Indeed millions believe that conscience is a strong guiding force. Others simply see conscience as a developed response based on the internalization of social mores. Other sources of ethical guidance are what psychologists call 'significant others'—our parents, friends, role models, members of our clubs, associations, codes of ethics for organisations, etc.

Whatever the source, there is general agreement that persons have a responsibility to avail themselves of the sources of ethical guidance, and individuals should care about right and wrong rather than just be concerned about what is expedient. *The strength of the relationship between what an individual or an organisation believes to be moral or correct and what available sources of guidance suggest is morally correct is Type I ethics.*

Type II ethics is the strength of the relationship between what an individual believes in and the way he behaves. Generally, a person is not considered ethical unless possessed of both types of ethics.

Social Responsibility

Organisational strategists have great influence over what is right or wrong because they normally establish policies, develop, the company's mission statement, and so forth.

When a corporation behaves as if it had a conscience, it is said to be socially responsible. *Social responsibility is the implied, enforced, or felt obligation of managers, acting in their official capacities, to serve or protect the interests of stakeholder groups other than themselves.*

Business ethics is the application of ethical principles to business relationships and activities.

Changing values towards social responsibility To understand the social responsibility of a corporation, it is useful to begin by understanding an *organisational constituency*. *An organisational constituency is an identifiable group towards which organizational managers either have or acknowledge a responsibility.*

Clearly, every business organisation has a large number of stakeholders, some of whom are recognised as constituencies and some of whom are not. *An organisational stakeholder is an individual or a group whose interests are affected by organisational activities.* Exhibit 6.2 depicts a typical illustration of organizational stake-holders, those marked with asterisks being likely to be considered constituencies.

Even though no manager can reasonably consider all stakeholder interests at a time, some strategists claim to try. The great questions a strategist has to face would go like this, 'During an economic downtrend, should employees be afforded continuous employment even when this is not in the long-term best interest of the owners of the corporation and does not accord with their preferences? Should managers be concerned about whether suppliers receive a reasonable profit on items purchased from them or should management simply buy the best inputs at the lowest price possible?' Many corporate strategists cop out on such questions by simply assuming that the long-term best interest of the common stakeholders should reign supreme. What happens, however, when stakeholders have interests that are in conflict? That is when the ethical considerations

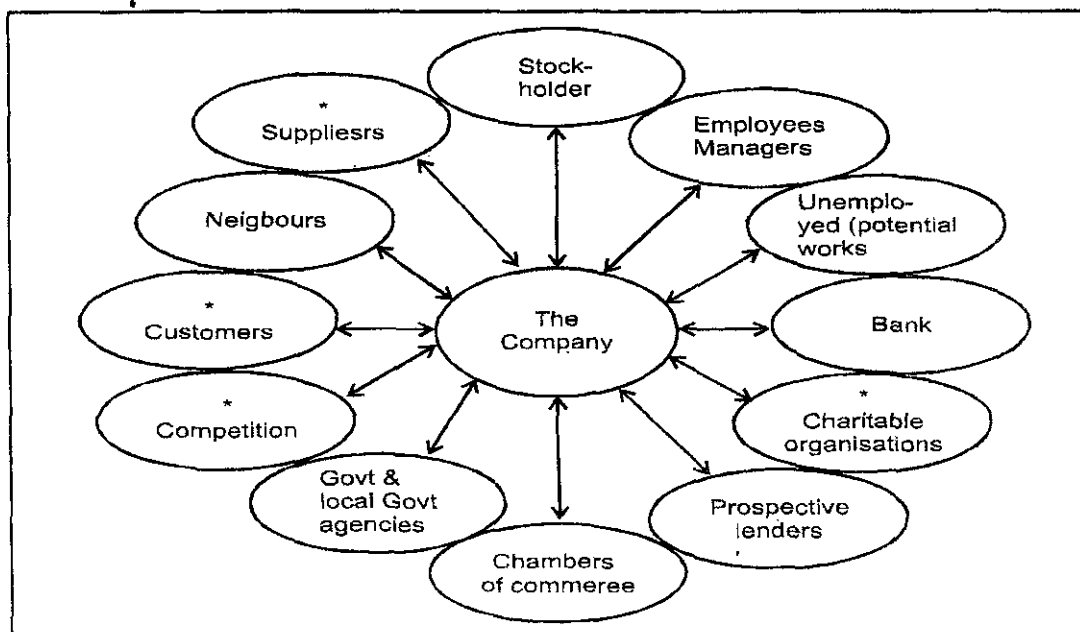


Exhibit 6.2: The Company Stakeholders

of the strategist become the important deciding factor. Before proceeding any further, we list some accepted ethical principles and stake-holders in Exhibit 6.3 and 6.4.

<i>Wrong, Unethical, Immoral</i>	<i>Right, Ethical, Moral</i>
Murder	Giving to the poor or disadvantaged
Rape	Working hard
Lying under oath	Gathering knowledge and wisdom
Theft	Repaying obligations
Incest	Being truthful
Severely hurting someone economically, psychologically physically	Caring for offspring or Caring for forebears
Violating a trust	Considering the long-term outcomes of behaviour
Anarchy	
Violating laws	
Sacrificing the future for today	

Exhibit 6.3: Accepted Ethical Principles

An open system is an organisation or an assemblage of things that affects and is affected by external events, it is now more or less universally recognised that a corporate organisation is an open system. Indeed, most corporate strategists recognise the existence of the grapevine or the informal communication system within and outside an organization.

The open system view involves recognising the relationships between organisations and their environments, and evaluating those relationships in an intelligent, not necessarily moral, way. It is not an ethical concept. It is,

Common shareholders	Intermediate (Business)
Preferred shareholders	Customers
Trade creditors	Final (consumer) customers
Holders of secured debt securities	Suppliers
Past employees	Employees
Retirees	Corporate management
Competitors	The organizational strategists themselves
Neighbours	
The immediate community	The chief executives
	The Board of Directors
The national society	Government
The world society	Special interest groups
	Local government agencies

Exhibit 6.4: Stakeholders (Potential Constituents)

however, clear that the organisation has obligations to other elements of society, some of which are not spelt out in law or in any other formal way. This is termed *social contract*.

The Social Contract

In a sense, organisations and society enter into a contract. *This social contract is the set of written or unwritten*

rules and assumptions about behaviour patterns among various elements of society.

Thinking of the social contract from the standpoint of the business or non-business organisation, organisational strategists should contemplate expected or prescribed relationships with individuals, with government, with other organisations and with society at large. This is illustrated in Exhibit 6.5.

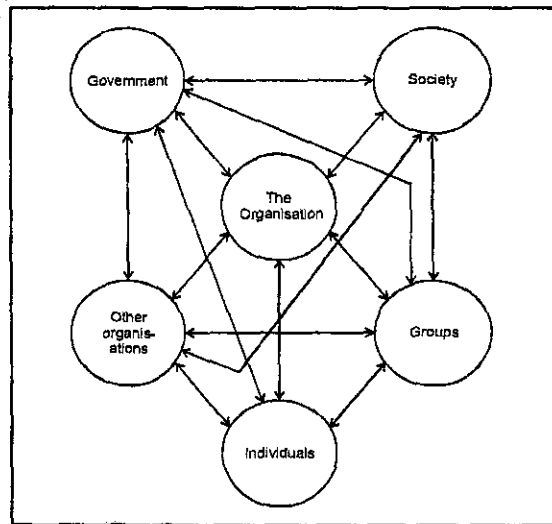


Exhibit. 6.5 The Social Contract

Obligations to Individuals

It is through joining organisations that individuals find healthy outlets for their energies. From the church they expect guidance, ministerial services, and fellowship, and they devote time and money for its sustenance. From their employers they expect a fair day's pay for a fair day's work—and perhaps much more. Many expect to be given time off, usually with pay, to vote, perform jury service, and so forth. Clubs and associations provide opportunities for fellowship and for community service. To the extent that these expectations are acknowledged as responsibilities by the organisations involved, they become part of the social contract.

Obligations to Other Organisations

Organisational strategists must be concerned with relationships involving organisations of similar kinds—such as competitors—and vastly differing organisations. Commercial businesses are expected to compete with one another on an honourable basis, without subterfuges or reckless lack of concern for their mutual rights. Charities expect support from businesses, customer organisations expect to be treated as 'Customers'.

Obligations to Government

Government is the most important party to the social contract. Under the auspices of the government, companies have licence to do business. They have written patent rights, trade marks, and so forth. Churches are often incorporated under state laws and given non-profit status. Many quasi-governmental agencies, such as the Federal Depository Insurance Corporation, Regional Planning Commission, Levy Boards, have been allocated special missions by the government. In addition, organisations are expected to recognise the need for order rather than anarchy and to accept some degree of government intervention in organisational affairs. The inspection rights of Occupational Safety and Health Administration function-aries are cases in point.

Obligations to Society in General

Businesses are expected to creatively abide by laws that are passed for the good of society. That is, as responsible corporate citizens, businesses should follow the spirit as well as the letter of the law. This has emerged abundantly sharply in recent cases where defence against charges of dumping of dangerous waste has tended to take the line of its being within 'legal' limits. It is now clear that society considers such pleas simply unacceptable.

Indeed, views now appear to be veering towards the concept that protecting the public is simply a matter of 'managerial self-interest'. It is the clear consensus among developed economies today that corporate strategists must protect other stakeholders, even when doing so collides with managerial self-interest or even the interest of stockholders.

Up to now, we have basically considered the organisation's obligations to its stakeholders, government, and society, arising out of moral and ethical considerations. It is also important to consider the influence government and society may have on the strategic posture of the company.

Government and Its Role

It is convenient to divide the role of government into two categories: government acting as an aid to business and government acting as impediment to business; although the government may simultaneously be performing both acts.

Government as Aid to Business

Government as Buyer

Government is frequently a major purchaser of goods and services, and is generally regarded by business as an excellent customer because it will not default on payment and also because government purchases, as well as being a mark of approval, are also frequently relatively large.

Government as Sustainer of R&D

In many industries today the cost of engaging in the R&D necessary for successful development of new products and processes is frequently beyond the financial capacities of individual companies. In such circumstances, the government may frequently help out by providing subsidies or even partially bearing the cost of R&D by directly participating in joint research. MITI of Japan, particularly in the early days, would be a case in point.

Government as Provider of Protection

This is usually in the form of provision of subsidies to the threatened industry, through erection of tariff barriers against foreign products; through imposition of quotas against foreign goods; and through exercise of preferential procurement practices.

Government as Aid to Controlling Wage Cost

This takes the form of government policies introducing income norms that ease the difficulties of businesses in meeting wage demands they believe to be excessive.

Government Assistance in Training

Independent of trade and industry, many governments have sponsored training programmes aimed at raising the skill levels of existing and potential workers. Occasionally there are also tax reliefs and grants given to companies running their own training schemes.

Government Assistance in Start-up Business

In many regions of high unemployment, government provides special concessions and assistance to start up new businesses. A similar situation arises in 'backward' or 'no-industry' areas in developing countries, where special facilities or concessions are given for setting up new industries.

Government as Provider of New Business Opportunities

Since the eighties, in many Western countries and in some developing countries there has been a general trend favouring privatization of new industries. This automatically creates new business opportunity for prospective investors.

Government as Impediment to Business

The development of the web of regulations: Frequently government increases its intervention in society through legislations and regulations. Often these work to the detriment of industries, increasing not only costs, but procedural impediments; examples would be regulations controlling inter-state or inter-country movement of goods and levy of excise duties on goods produced.

Government as controller of prices: Income policies are also frequently complemented by price policies, which is generally regarded by industry with some hostility. The major argument is that this conflicts directly with the influence of market forces on prices.

Government as protector of the environment: Nations around the world are increasingly becoming aware of the long-term cost of industrial pollution. This has resulted in a spate of legislations curbing activities believed to be causing pollution. Many industries resent this as being undue intervention.

Government as guarantor of health and safety at work: This concern for health and safety of workers manifests itself through various acts of legislation, invariably resulting in increased cost to the company, and is often resented as undue penalty.

Government as guarantor of equal opportunity: Legislation conforming to equal opportunity, i.e. equal rights to employment and promotion without regard to sex, age, race, or religion, has been enacted in most countries in the Western world. This is again often resented by companies as undue interference and cost-enhancing measures.

Government as defender of competition against monopoly: Governments in many countries seek to restrict monopoly by legislation in the interest of maintaining competition, from the social point of view and as protection for small firms. This is often considered by large companies as a negative step, particularly in the context of globalization when national monopoly (and hence larger size) is often considered as a prerequisite for global success. (It may be mentioned that contrary cases abound around the world.)

Government as defender of the rights of consumers: Many Western governments have enacted legislation to protect the consumer against unscrupulous business practices. It may involve insistence on honest labelling of goods, contents of advertising, standardisation of contents in pharmaceutical and food products, and price regulation in the case of utility companies. The more extensive these laws are, the more hostile business tends to become towards these.

In view of this ambivalence in government attitude to industries (sometimes beneficial, sometimes creating impediments), instead of generalizing, it would be useful to see the role of government in terms of changing participation in strategic decisions. In this, a distinction must be drawn between political influence and strategic leadership. The key difference is that the former calls primarily for exercise of political skills on behalf of a constituency, while the latter, in addition to political skills, requires a clear perception of the common purposes of an organisation, and of ways of attaining them. It is common to refer to such perceptions as the 'vision' of the organisation's future.

Exhibit 6.6 summarises Ansoff's conception of changing participation in strategic decisions by different management levels in different types of industries.

Effects of Society and Culture

Like the environmental effect of government, the social/ cultural effects on products and services should also be considered somewhat more specifically. This is now done under a few important heads.

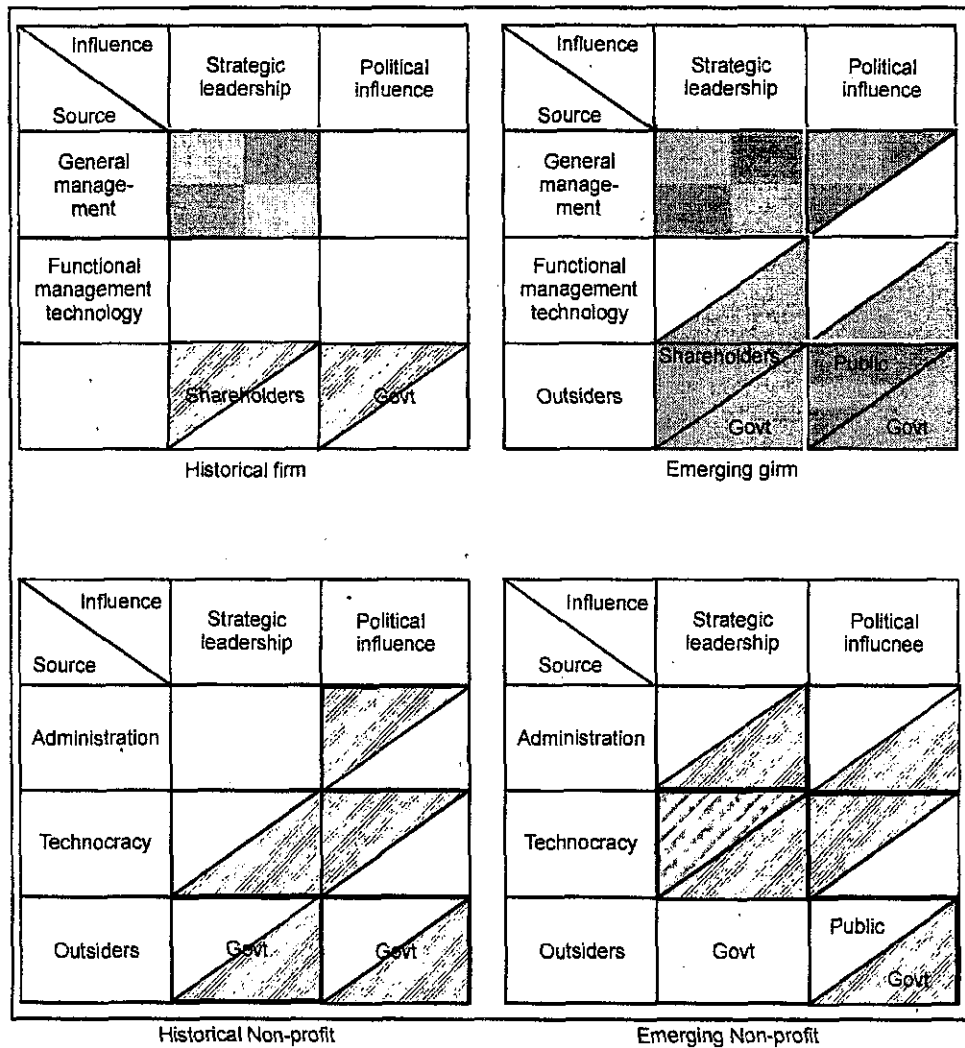


Exhibit 6.6: Changing Participation in Strategic Decisions

Education: The level, availability and participation rate in education can have major implications for many products and services. Indeed, the impact of education is being increasingly felt in most industries.

Health and fitness: People’s concern for health and fitness has become extremely important in recent times. This social/cultural change has implications not just for sports-related business, but also for how other products and services are promoted, and how potentially ‘unhealthy’ products overcome their poor image; for example, the tobacco industry is a major sponsor of sporting events.

Family size: Family size has been decreasing almost all around the world. This has implications not just for suppliers of children’s goods—baby food, prams, clothes, etc.—but also for seemingly unrelated products, such as houses and cars, where design and size is frequently a function of family need.

Family units: Family units have generally become less stable; there has been an increase in the level of divorce and increasing tendency of young people to leave home and live apart from their parents. This has implications for promotion, packaging, etc.

Religion: There has been a decrease in the power of churches and their appeal, especially to young people. This has had a major influence on such issues as how people spend their leisure, the types of moral attitudes that are socially acceptable, retail opening hours.

Geographical mobility: The advent of cheap international travel has greatly increased scope for international travel both for business and pleasure. It has also greatly increased peoples' knowledge of foreign environments and tended to make goods and services more 'cosmopolitan'.

Domestic mobility: The development of mass motoring has meant a major social change not just in recreation but also in retailing. This has been helped by a rise in freezer ownership. Thus many retailers have moved from downtown sites to out-of-town shopping centres with good parking facilities. Similar increased ownership of freezers has tended to change daily 'necessity' shopping to the weekly shopping trip.

The role of women in society: With the great increase in proportion of women working outside the home and the development of equal opportunity legislation, there has also been a change both in society's attitude to the role of women as also women's personal attitude about themselves. Thus there has been a diminution in the domestic role of women and an increase in their broader role in society. This has found reflection in their purchasing habits and product choices.

Attitude to work: is evident that there has been a distinct change in workers' attitude to work and the consequent need for strategic change to accommodate it.

Economic Environment

The significant indicators of the economic environment would include:

- Growth rate in productivity
- Rate of inflation
- Individual savings rate
- R&D expenditure as a percentage of GNP

The key domestic social and economic goals would include:

- Revitalisation of cities
- Cleaner environment
- Quality education
- Old age security

The key economic environmental problems of recent and current times appear to be:

- Controlling inflation
- Modernising industry
- Taking care of energy shortages
- Growing international interdependence
- National economic factors.

These are now slightly elaborated.

Controlling Inflation

A major long-term political issue in combating inflation is whether high employment and non-inflationary economic growth can be achieved simultaneously. The continuation of economic restraint and unemployment to suppress inflation can only lead to further development of a 'welfare state' and the trend appears to be exactly the opposite the world over. The inflationary impact of demand expansion policies, however, will require greater wage-price flexibility,

productivity and advance capital investment to ensure supply availability. Such growth policies would, therefore, require changes in environmental and other regulatory provisions.

Modernising Industry

To be internationally competitive, industry must seek economies of scale to sustain comparative advantages in efficiency and productivity. This requires continued capital investments and the application of technological innovations from research and development to reduce unit cost and to lead to the introduction of new and more efficient products and processes.

Living with Energy Shortages

The world economies at large will be living in a world of gradually depleting oil, gas and, ultimately, coal reserves. This demands special action and incentives for the development of renewable energy sources such as solar and fusion energy. Until such alternatives are able to meet future needs, special attention will be necessary to deal with the interim supply and demand problems, including national energy policies for the conservation and development of alternative supplies. The problem has been further complicated by the changed social value system and newly awakened awareness about pollution and environmental degradation through extensive use of fossil fuel, on the one hand, and damage to the ecosystem through large dam- or barrage- based hydroelectric projects, on the other.

Better Labour-management Relationships

The growing complexity and interrelatedness of today's economic problems are likely to increase pressure for joint labour-management problem solving. A common concern is developing for increased productivity that may lead to productivity bargaining.

Growing International Interdependence

The rapid increase in movement of goods, people, money, ideas, and problems across national boundaries is complicating the ability of nations to manage their own economic affairs without reference to other nations and national interests. Thus the economic export policies of Japan, for example, have significantly influenced US and Western steel, auto, radio, and electronics industries. The transfer of Eurodollars to high interest paying countries can significantly affect exchange rates and corresponding corporate currency adjustments (often forcing significant accounting losses or gains). The growth in world trade also causes inflation to spread rapidly from one economy to another.

Less developed countries that control scarce resources such as oil have increased the abundance of capital at their disposal. Important exporting nations such as Brazil, Korea, Taiwan, and now the South East Asian countries like Indonesia, Malaysia, Thailand, and Singapore are becoming industrialised and thus prospective members of the developed world. Simultaneously a host of less developed countries mostly in Africa are near bankruptcy. Intervention by international financial Institutions like the International Monetary Fund or the World Bank are hardly assisting in countering the trend. Countries with balance-of-payments surpluses are becoming significant world bankers. Those with balance-of-payments difficulties are being forced into severe financial difficulties and basic problems of survival.

In sum, because of the influence of global economic events, it is usually inadequate to consider national economic policies without taking cognizance of the broader global economic context in which all national economies must exist. This broader economic context must include an assessment of such fundamental indices as:

- Performance of the major industrial countries in their
 - Rates of inflation
 - Real growth rate of GNP
 - Current account balances
 - Levels of employment
 - Interest rates

Such an appraisal should enable a judgement to be made about the general state of world economy and its stage in the 'business cycle'.

- Information on and analysis of other global issues such as
 - The economic development and performance of nations
 - Global efforts at monetary reforms
 - The behaviour of currency markets
 - Commodities
 - Trade talks
 - Activities of the International Monetary Fund
 - Activities of the World Bank
 - Third World indebtedness

The State of the National Economy

The analysis of the global economy can form the economic context within which the national economy can be appraised.

This can be done on a hierarchical basis, as discussed below:

- The top economic goals of the government are assessed. Information for this can be obtained from party manifestos, government statements, budget statements, etc.
- The specific policies advocated and implemented to achieve these goals are studied. The policies fall under the following principal headings:

Fiscal policies: What is the level of government spending and what are its policies on taxation? For example, is government, through public expenditure, attempting to raise the level of demand and hence reduce unemployment? Is the government's tax strategy designed to increase investment or increase public spending power?

Monetary policies: How tightly are monetary measures such as the money supply and PSBR being constrained?

Inflation policies: What is the government's attitude towards inflation and what does it believe are its causes? What steps is it taking to influence the level of inflation?

Foreign exchange and balance-of-payments policies: What is the government's attitude towards stability in the value of the national currency? How do changes in the value of national currency affect the economy in general and the organization under analysis in particular?

Unemployment policies: How committed is the government to full employment, and what policies does it use to achieve employment goals?

Privatisation policies: How strongly committed to privatisation of nationalized industries is the government? What is the objective of privatisation: to increase competitiveness, to raise revenues for the government, or to underpin an ideological theory?

Regional policies: How committed is the government to strong regional policies to prevent the concentration of industry and commerce in favored locations?

The operation of most of the above indicators can be quantitatively assessed. Once the impact of the economic segment has been assessed, it can be weighted.

The rate of inflation that prevails can be a significant environmental influence. It is, however, not enough only to know the rate of inflation; it is also necessary to understand and appreciate its impact on the workings of a particular company. This is because inflation tends to act as a 'tax' on current assets and as a 'subsidy' on fixed assets. Thus, for example, a banker, a financial company, the assets of which are skewed towards money and other similar products, must earn a return on equity at least as large as the rate of inflation, otherwise their net worth would be eroded by inflation. In contrast, a property company, for instance, would find its fixed assets constantly understated in its balance sheet during inflation, as the realisation on sale would be that much higher.

Proposals are often heard of for the use of a world currency to replace all national currencies. Indeed, this appears to be becoming a reality for EEC countries. This may seem far-fetched, but it is reflective of the fact that the economic facet of the environment is influenced by worldwide forces. The US and European auto and electronic industries have been severely impacted by foreign competition, mostly Japanese. Recently, when it appeared that the oil producers and exporters' cartel (OPEC) was about to fall apart, there was fear that this would result in a number of developing countries defaulting on their debts to major US banks, with consequent increase in US interest rates. The recession which began in 1979 was a worldwide phenomenon, and this was also the case with the recovery which began in 1983. International travel is more feasible than it has ever been in the past, and more and more companies engage in international business. Every organisation is affected by worldwide forces.

In short, the economic facet of the environment is a rapidly changing one, but the more it changes, the more it remains the same. Organisational strategists must still compete on an economic basis. As long as prices for goods and services are set in free markets, it will be on the basis of economic variables that an organisation sets its goals and measures its performance.

Political Environment

In democratic countries, business excesses generated disenchantment and a growing demand for more 'humanist' goals to equalise income distribution and end poverty and suffering. Such pressures had caused the trend towards the 'welfare states' in which the state (a) diverts resources into various welfare projects, (b) establishes compulsory insurance schemes, e.g. national health care, and (c) affects worker motivations to contribute. Thus, in the USA, rent subsidy, negative income tax, welfare payments, and a food stamps programme were established to raise the living standard of the poor.

Continued pressure for 'welfare states' will in all probability grow and affect many nations, organisations and individuals in the following ways:

- i. Total taxes and government spending will increase drastically,
- ii. Worker penalties for welfare recipients will create dysfunctional worker motivation,
- iii. Any government administration will find it well nigh impossible to reverse the trend towards greater welfare benefits,
- iv. Resource allocation decisions will increasingly be made on philosophical or political grounds rather than on economic criteria,
- v. Increased worker taxation on incremental income will encourage worker absenteeism.
- vi. Government dependence will decrease worker motivation through lack of 'care' or worry.

This trend may, however, result in business sales stagnation leading to economic and industrial decline and depression. In short, carried too far and without compatibility with economic considerations, the 'welfare state' trend would in all probability conflict with economic progress and viability. Indeed, in more recent times it has already happened in many countries and the trend towards the welfare state has been reversed.

Perhaps the political environment needs to be looked at from certain other viewpoints as well. Corporations today spend hundreds of millions of dollars on political contributions and lobbying. These contributions are some-times designed to support principles that corporate executives believe are worthwhile for society. More often, however, they tend to be self-serving. This is evident from the fact that few political contributions are made anonymously. The political facet of environment is also con-cerned with the organisation's relationships with government officials and other individuals and groups who hold political power.

In recent times there has been fear that political action committees (PACs) are likely to subvert governmental processes by causing elected officials to serve the interests of those groups that make contributions. *Political action committees* are tax-favoured organisations formed by special interest groups to accept contributions and influence governmental actions. The growth of PACs has afforded an avenue for corporations to contribute hundreds of millions of dollars to political candidates. The returns received in the form of subsidies and price support to various industries are also enormous.

While the general public is justifiably concerned about the influence of PACs and other private organisations on government, most managers express greater concern for the pervasive involvement of government in business activities. One prominent law school dean, Thomas Erlich of Stanford University, complained that the increasing 'legal pollution' in America unduly constrains business. Not only have laws become more numerous, but the propensity of citizens to litigate has become greater. Business and non-business organizations find themselves in a sea of political forces. The organisational strategist must take account, if not advantage, of these forces.

The decade of the sixties up to the mid-seventies has seen vast expansion in the scope and detail of government regulation of business decisions, beyond those of the New Deal era, beyond regulating public utility industry, and beyond temporary periods of wage and price controls. This regulation has undoubtedly cost US business heavily. Indeed, the problem is much more severe in the USA than in European countries.

It is now acknowledged by more balanced people in government that the government appears to be an opponent rather than friend or even neutral force vis-a-vis business and industry. The government view is of course different, namely that it has to protect public interest. Indeed, it is suggested that businessmen can serve their political interests better by looking beyond the very narrow interests of the individual company and offering some connection between what businessmen want and the broader public interest.

Certainly, the business-government interface is often an abrasive one. The very recent trend, however, is towards lessening regulation and reducing government interfer-ence in business and private activities. Incidentally, it is noteworthy the deregulated industries themselves tend to be the most vehement opponents of deregulation, it is likely that this opposition arises from a fear of rapid and unmanageable change.

Technological Environment

Technological change results when new ideas are applied to existing problems for the purpose of economic and social development. As with all economic and social changes, the acceptance of technological innovations takes a significant period of time, and it is also a reflection of rapidly increasing environmental turbulence that this time span is constantly decreasing.

Recent times have seen the development of new products and processes with increasing frequency. The uncertainties and slow pace of development of technological innovations make investments on them high risk. The potential pay-off for winning innovations can, however, be significant and continues to encourage investment in research and development.

Looking carefully, the competitive advantage of Japan in many industrial and business areas would be largely attributable to their emphatic and consistent policy on research and development. Some of the attributable factors would be:

- i. There is a national policy for setting up research and development facilities for new technologies,
- ii. There are tax and interest incentives for investors in designated technologies.
- ii. Capital is made available for designated technological investments at preferred interest rates,
- iv. Investment in new technology is readily accepted by employees.
- v. Growth in new technologies has become part of the culture and economic system.

Future developments have a wide range of technologies to draw upon. Predicting new developments and innovations will be increasingly important. Consider the problem of depleting oil resources and their increasing costs. Consider the simultaneous awareness about issues related to pollution control and environmental protection. We are beginning to see a new emphasis on energy-related technologies that have yet to become commercial. Consider the following classes of technology:

- i. Nuclear fission (breeder reactors)
- ii. Nuclear fusion
- iii. Synthetic hydrocarbon fuels
- iv. Solar energy
- v. Wind energy.
- vi. Geothermal energy
- vii. Hydrostatic, tidal, and ocean current energy
- viii. Temperature gradient energy
- ix. Advanced energy storage and distribution

Today deciding, which of these technologies research and development funds should be invested in, is a real gamble.

Let us look at the impact of technology on business and industry a little more closely.

With today's modern computers it is possible to obtain strategic information on a real-time basis for the first time in history. Most major merchandises now have 'point-of-sale' electronic accounting systems. When a customer order is checked out at the cash register, the inventory is immediately updated. An order for a replacement item is entered if necessary, and the impact on sales, profitability, and other strategic variables immediately calculated. In this final analysis, as unsettling as many of the advances is that most of these result in the production of goods and services at lower cost both in terms of time and materials. If economic endeavour has a single goal, this has to be it.

Organisational strategists who ignore technological changes do so at their peril. Manufacturers of mechanical adding machines, large propeller driven aircraft, or plastic-reinforced automobile safety glass will find almost no market today.

Three possible effects, of technological change are easily discernible:

- It can change relative competitive positions within a given business.
- It can create new markets and new business segments.
- It can collapse or merge previously independent businesses by reducing or eliminating their segment cost barriers.

In any event, when technology advances, all participants in the respective business segments are affected. To survive today companies must continually innovate. This is not because of some external force which has imposed

upon the world a new and fearsome order of things, but because technological improvement is possible. When improvement is possible in a free economy, someone will attempt it. The company or person who does, and succeeds in producing a better product at the same cost or a cheaper version of the same product, will be able to dominate the market place. Companies that do not, will be driven from the economic scene. Even when competitors make appropriate but delayed technological response, lost market shares may not be regained.

Although it is difficult to measure, except with hind-sight, the importance of technological change to an industry, two measures that may give reasonable indication are suggested :

- The amount the industry spends on R&D. This could either be an absolute amount or it could be a relative measure such as R&D expenditure as a proportion of sales. The latter basis is increasingly becoming the more standard practice.
- The PIMS measure of innovation. This measure defines the level of innovation as the proportion of revenues that accrue from products that have been introduced during the past three years. This measure is good indication of the relative importance to the industry of new products.

When the analysis of the technological environment has been completed, the threats and opportunities that prevail should be weighed.

Industry Environment

To analyse industrial environment we should begin by understanding its purpose. The purpose of studying industrial environment or analysing industry structure is to gain an understanding of the competitive relationships among groups of firms that compete for a specific market. The first step is a broad analysis of industry environment. This is illustrated in Exhibit 6.7.

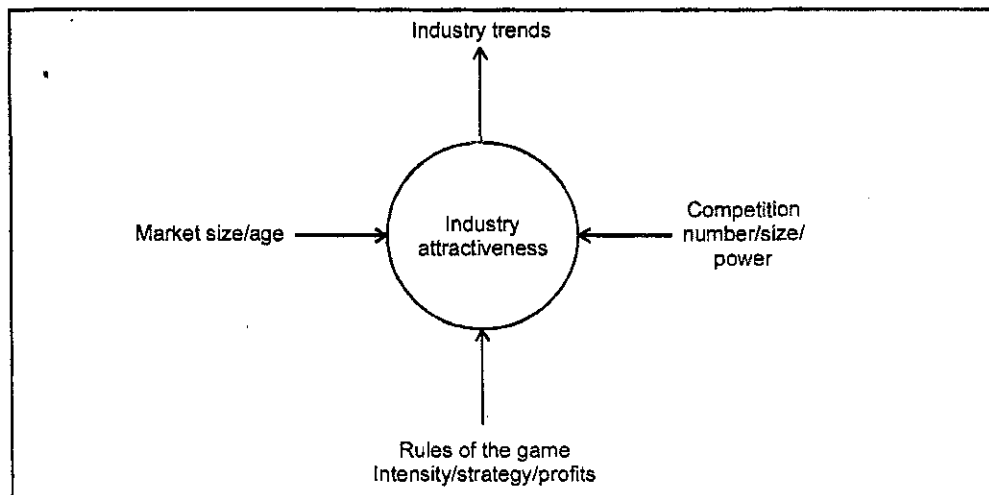


Exhibit 6.7: Industry Structure

A slight elaboration of the factors may be helpful.

Market size/age: Is the market relatively small or large, and can it be broadly characterised by its stage of development (start-up, emerging, growth, maturing, declining)?

Number of competitors: What is the level of competition for the market? Are there many small rivals or a few large, dominant ones? Also, how easy is it for new players to enter the industry? Some industries are easy to enter, others difficult.

The rules of the game: How do firms compete in this market? Do they compete on price, quality, technology.

service, etc? What is the average level of profitability? Is it a profitable market or is it a high volume, low margin field? As an industry matures there is usually a movement towards the cost advantage of economies of scale. When there is a major change in the cost or profit structure, competition will tend to intensify, as, for instance, if price cutting strategies are used.

Industry trends/driving forces: What are the industry trends and how rapidly do they change? Is the industry growing and innovative or stable and slow to change? The rate of market growth is a critical factor because it influences the equilibrium between demand and supply. In a slow-growth industry, competition tends to increase because any growth must be taken from a rival's share.

Industry attractiveness: The overall attractiveness of an industry is determined by the interaction of these key structural forces. The higher the rate of growth and the weaker the competition, the more attractive the industry.

Techniques of Industry Structure Analysis

The initial analysis of industry structure provides a map of the competitive environment. The strategist also needs to anticipate future trends: new developments that may change the existing structure.

There are several techniques that may be employed to identify the underlying competitive alignment and the major players. Below, We briefly discuss two such.

Structural Mapping

One method that may be used to examine industry structure is termed *structural group mapping*. The map is developed by plotting competing firms on two industry dimensions; for example, product quality versus distribution channels. To give an added dimension of strategic input, the area of each circle representing a company may be made proportional to its market share. When these two-dimensional plottings are stretched together, the dominant strategy of each competitor and its effectiveness shows up quite distinctly.

Competitive Arena Mapping

A second industry analysis technique is termed competitive arena mapping. The total market segment is diagrammed around customer needs and product offerings. This map of the information-communication arena allows the strategist to examine all the likely moves by key players and to anticipate possible changes in competitive forces. By highlighting the largest markets, it is possible to visually portray the strategy and direction of key competitors, such mapping of the information-communication arena is shown in Exhibit 6.8. It will be seen from this illustration that competitors from all directions are converging on the growing microcomputers and office-automation markets.

What is more important is the sure indication of increased competition in the future from giants converging on the attractive markets, and therefore this advance information enables a choice to be made of the suitable strategic response.

Strategic Group Analysis

The problem that the strategic analyst will face is conceiving of the nature of competition that the organisation faces. In particular, who are the most direct competitors and on what basis is competition likely. Given this understanding it is then possible to gauge the extent to which strategy is appropriate in the competitive circumstances. One problem here is that the idea of the industry is not particularly helpful. The boundaries of an industry can be very unclear and may not provide any precise delineation of competition. In a given industry there may be many companies each with different interests and competing on different bases. There is a need for some intermediate mapping of the basis of competition between the individual firm and the industrial level.

Strategic group analysis is one means of providing this intermediate level of analysis. The idea is to identify more

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finely defined groupings of organisations so that each grouping represents those with similar strategic characteristics, following similar strategies or competing on similar bases. Porter argues that such groups can usually be identified using two, or perhaps three, sets of key characteristics as a basis of competition. It is useful to consider the extent to which organisations differ in terms of such characteristics and also show similarities. Some examples of such characteristics would be:

- extent of *product (or service) diversity*;
- extent of *geographic coverage*;
- number of *market segments served*;
- *distribution channels used*;
- extent (number) of *branding*;
- *marketing effort* (e.g. advertising spread, size of sales force, etc.);
- extent of *vertical integration*;
- *product or service quality*;
- *technological leadership* (a leader or follower);

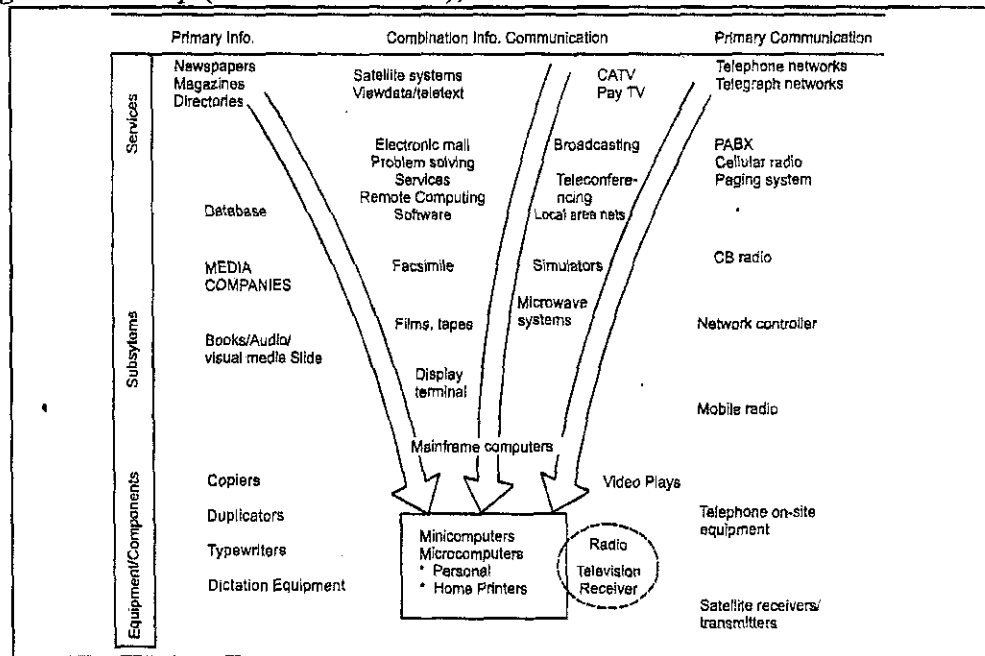


Exhibit 6.8: Competitive Arena Map

- *R&D capability* (extent of innovation in product or process);
- *cost position* (e.g. extent of investment in cost reduction)
- utilisation of *capacity*;
- pricing policy;
- level of *gearing*;
- ownership structure (separate company or relationship with parent);
- relationship to *interest groups* (e.g. government, the city);
- *size of organisation*.

This sort of analysis is useful for all organizations that seek to understand competition. What the analyst is looking for

is to establish which characteristics most differentiate firms or groupings of firms from one another. Moreover, it is likely to yield a better understanding of the competitive characteristics of competitors. It also allows the analyst to ask how likely or possible it is for the organization to move from one strategic group to another. Mobility between groups is of course a matter of considering the extent to which there are real barriers to entry between one group and another in terms of how they compete.

We discuss here two models for strategy formulation in which industry and industrial environment analysis plays a key role.

The BCG Growth/Share Matrix

One of the most widely used portfolio approaches to corporate strategic analysis has been the growth/share matrix pioneered by the Boston Consulting Group and illustrated in Exhibit 6.9.

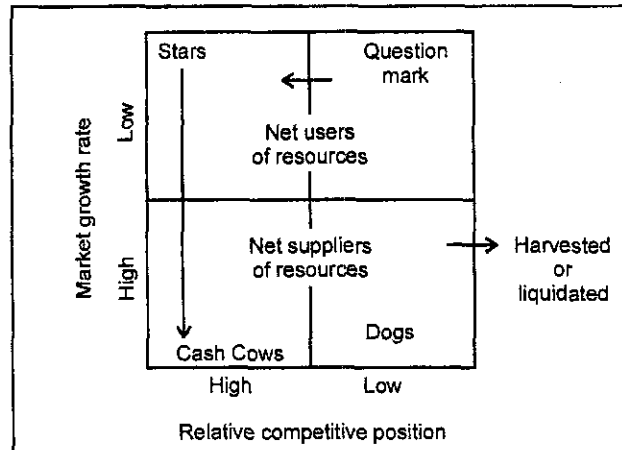


Exhibit 6.9: BCG Growth/Share Matrix

The BCG matrix facilitates strategic analysis of likely 'generators' and 'optimum users' of corporate resources. Market growth rate is the projected rate of sales growth for the market to be served by a particular business. Market growth rate provides an indicator of the relative attractiveness of the market served by each of the businesses in the corporation's portfolio. The relative competitive position is usually expressed as the ratio of a business' market share divided by the market share of the largest competitor in the market. Each business unit can also be represented as a circle in the matrix. The size of the circle represents the proportion of corporate revenue generated by that business unit. This provides visualisation of the current importance of each business as a revenue generator.

Market growth rate is frequently separated into 'high' and 'low' areas by an arbitrary 10 percent growth line. The relative competitive position is usually divided as a relative market share between 1.0 and 1.5 so that a high position signifies market leadership. Once plotted, business units will be in one of the four cells with differing implications for their role in an overall corporate-level strategy.

The GE-Mckinsey Nine-cell Planning Grid (Directional Policy Matrix)

General Electric, assisted by McKinsey, developed a strategic planning grid which attempted to correct some of the limitations of the BCG matrix approach. The grid is illustrated in Exhibit 6.10.

First the GE grid uses multiple factors to assess industry attractiveness and business strength, rather than the single measures (market share and market growth, respectively) employed by the BCG matrix. Second, GE expanded the matrix from four cells to nine, replacing the high/low axis with a high/medium/low one to draw finer distinctions between business portfolio positions.

To determine which axis a business unit falls under, the company's business unit is rated on multiple sets of strategic factors within each axis of the grid.

Competitive Environment

The best method for carrying out a study of the competitive environment is through a structural analysis. Exhibit 6.11 provides a model.

Competitive Advantage Analysis

The choice of competitive strategy is determined first by the long-term profitability of an industry, an essential ingredient in predicting the profitability of the firm, and second, its relative competitive position within an industry. Hoffer and Schendel have suggested four steps for analysis of these factors.

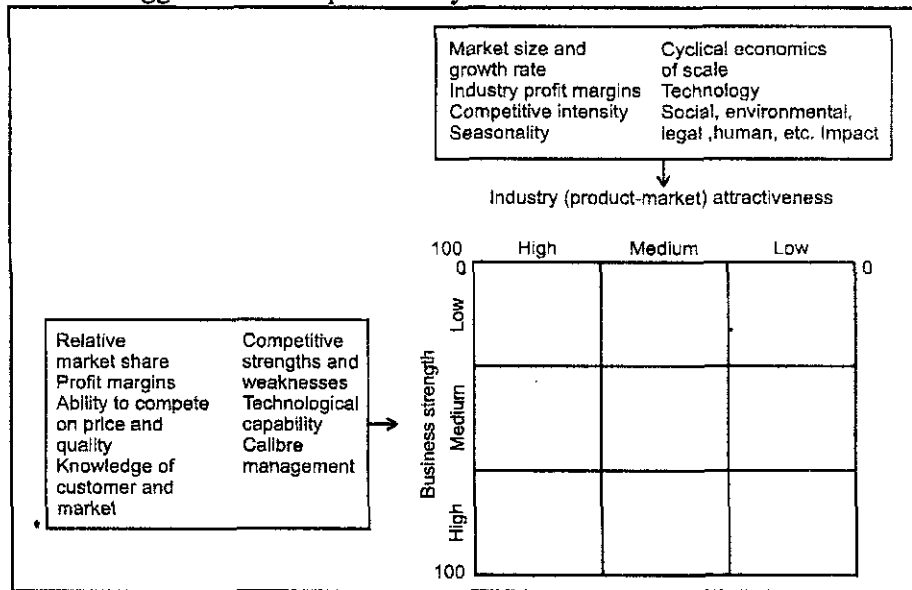


Exhibit 6.10: General Electric/McKinsey Nine-Cell Planning Grid

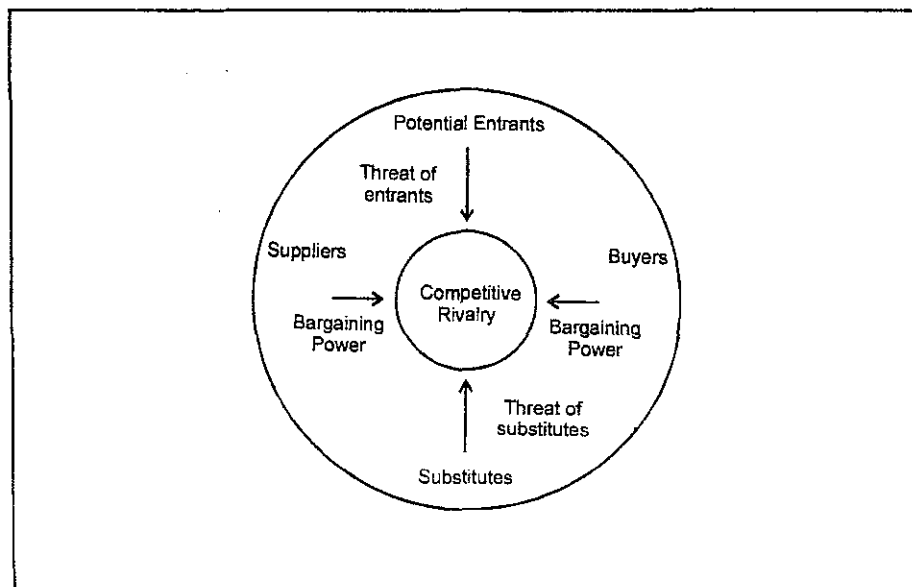


Exhibit 6.11: A Model for Structural Analysis of the Competitive Environment

- i. Develop an internal analysis profile of the organisation's principal resources and skills in several broad areas such as financial, marketing, organisational, production, human resources, and technological.
- ii. Determine the *key success requirements* of the product/market segments in which the organisation competes.
- iii. Compare the internal profile to the key success requirements to determine the major strengths on which an effective strategy can be based, and the major weaknesses to be overcome.
- iv. Compare the organisation's strengths and weaknesses with those of its major competitors to identify which key policies are sufficient to yield a competitive advantage in the market place.

Perhaps the idea of competitive advantage requires some elucidation. A competitive advantage is a position that offers an opportunity for higher profits in relation to competitors by:

- Differentiating products from competition.
- Concentrating on specific market segments.
- Focusing on production or distribution channels.
- Using selective price/cost structures.

Whatever the method used, the objective is to establish a distinct, favourable differentiation from rival firms.

This, however, raises a basic strategic issue: how can we strengthen our competitive position in relation to competitors?

Four basic managerial issues have been suggested:

- i. *The ability to understand competitive interaction as a complete dynamic system*, including competitors, customers, money, people, and resources. In other words, how does the firm compete in each of its basic businesses or product groups?
- ii. *The ability to use this understanding to predict the consequences of a given intervention in that system*. In effect, how does the firm respond to changing conditions? How will it take advantage of new opportunities, reduce competitive threats, and strengthen the firm's own competitiveness?
- iii. *The availability of uncommitted resources* that can be dedicated to different uses and purposes in the current circumstances.
- iv. *The willingness to deliberately act to make the commitment*. Integrating the activities of various divisions, products, and functions into a committed corporate culture and strategy.

The purpose of strategy is to maintain or gain a position of advantage in relation to competitors. An advantage is gained by seizing opportunities in the environment so that the organisation can capitalise upon its areas of strength. The ability of firms to identify and capitalise on the underlying industry structure varies tremendously. Most industries are characterized by one or more profitable leader, a group of smaller, more focused competitors, and a large number of firms holding in the mid-ranges with lower performances. This pattern emerges clearly when comparing sales volume with profitability. Large firms tend to dominate industry by achieving economies of scale, with resulting cost advantages. Smaller firms maintain a high profit with lower volume by focusing on a specialized market segment.

Mid-range firms remain at the bottom, being unable to realize competitive advantage. Being unable to take advantage of economies of scale and not having adopted the focusing strategy, they are 'stuck in the middle'.

Competitive analysis provides the framework for diagnosing strategic forces in the environment. It can help prioritize strengths and weaknesses, and locate possible vulnerabilities of rivals: a 'strategic window' of opportunities that the strategist may be able to exploit. Competitive analysis should be an ongoing process if strategy formulation is to be

effective. The strategy maker must identify the key success requirements for each industry situation.

The strategic window concept refers to the timing of marketing opportunities. It is easier to enter when the window opens and difficult to do so after it closes. Thus IBM missed the laptop PC market window, the opportunity being taken by Zenith's Z-181. By the time the IBM laptop PC came to the market, the window was closed.

The important and related aspects of 'timing' and 'when' require reference at this point. While discussing the concept of strategic windows, we referred to the failure of the IBM laptop PC as against Zenith's Z 181. It is not as if IBM lacked the resources or key success requirements, nor was there any error in choosing the field of diversification. What was missing, however, was an adequate strategic concept about the 'timing' of the move. In all strategic decisions, it is not enough only to look at opportunities and strengths. The third and critical element of successful crafting of strategy is choosing the time element correctly.

The Marketing Segment

The marketing segment falls somewhere between the industry and competitive segments. Because of its significance and importance, it is being considered under a separate heading.

The following environmental indicators are usually considered to be the fundamental determinants of the demand for goods and services:

- *The size and affluence of the market:* A primary determinant of demand is the absolute size and affluence of the market for the product. The size and the affluence of the market have led to globalisation, and most global companies seeking roles in the US market. The factor of size has also been instrumental in the development of a single European market.
- *The trends in the market:* Within all markets there are other indicators and trends that are of great significance when considering the potential of the market. Among the more important are the following:
 - *Total population trends:* growing, static, or declining?
 - *Trends in segments of the population:* products largely tend not to be targeted at 'the whole population' but rather at particular segments. It is, therefore, important to know how the different target segments are changing.
 - *Income trends:* e.g. is the level of income in the population increasing, decreasing or static, and how is the distribution of income among the various segments changing?
 - *Stage in industry/product life cycle:* from the perspective of environmental assessment it is important for managers to be informed about the stage at which their industry is in its life cycle.

Market Identification

At this stage the company attempts to identify in its environment market opportunities that it may be able to successfully exploit. This is when marketing research is undertaken in order to ascertain the extent and nature of opportunities, and to assess the company's internal ability to exploit them. At this stage there is general lack of detail in the proposed actions; it is essentially exploratory and is really concerned with seeing if there is a possible match between the market and the company's capabilities, including its existing (and potential) range of products or services.

Market Segmentation

Frequently used bases of segmentation for consumer goods include:

- *Demography:* age, sex, family size, income, occupation, religion, race, etc.

- *Geography*: country, region, city, town, climate, etc.
- *Social basis*: class, education, occupation, etc.
- *Product function*: use sought, benefit sought, rate of usage, etc.
- *Buyer behaviour*: of actual and potential consumers.

It should be noted that market segmentation is often more straightforward for consumer goods than for industrial goods because of the great range of uses to which many industrial goods can be put and also because there is much greater customer heterogeneity.

The criteria for deciding which segments are most attractive will vary from industry to industry, but in general the following tend to be considered important influences:

- Current and future growth rate of the segment in terms of volume and value.
- The degree and nature of existing competition: threats of new entrants, threats of substitutes, power of buyers, level of rivalry among existing competition, levels of profitability.

Product Positioning

Once a company has decided upon the target markets, the next stage is to determine how it ought to position its products in these in relation to competitors' offerings. This involves assessing how competitors' products meet customers' needs and then developing marketing strategies to meet these needs better. Product positioning is a vital part of the process, because it is here that managers must 'see to the heart' of the reason for competitors' success and more importantly, decide upon how they will position their own products or services so that consumers are induced to buy these. It is suggested that this can be accomplished in three steps:

- Decide upon the criteria that distinguish the various products currently available in the target market.
- Draw up a series of product pricing maps for competitors. This graphically shows how products compete, using two key customer criteria as axes. The products are represented by circles whose areas are proportional to their annual sales. Exhibit 6.12 illustrates such a map.
- Decide upon possible positions for the company's product on the product positioning map and define the qualities associated with the position chosen.

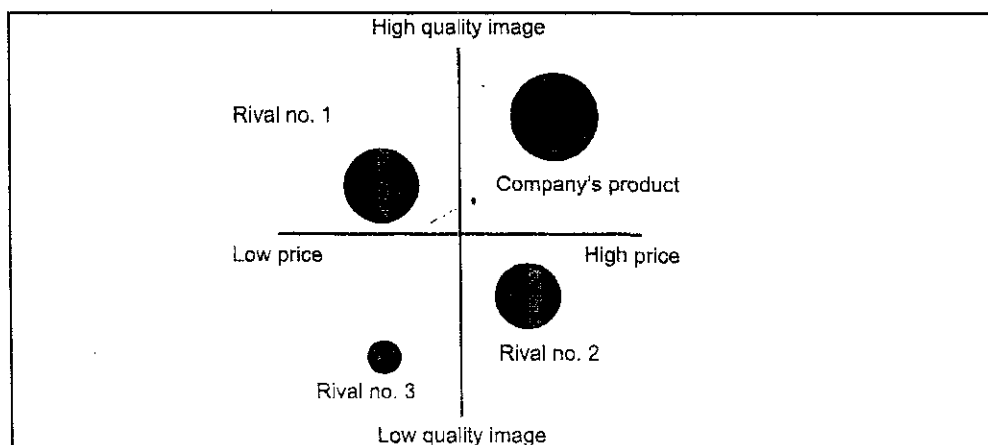


Exhibit 6.12: The Product Positioning Map

Marketing Mix Strategy

In order to position a product in a desired location in its target market segment, a company has at its disposal a great number of instruments. These include:

- the quality of the product in terms of features such as style and image;
- the distribution, i.e. by wholesaler, agent, etc.;
- the promotion of the product in terms of advertising, methods of selling;
- the price of the product.

These various instruments, which are used to influence consumers have been grouped together by McCarthy under four headings: *product, place, promotion, and price*, and these broader sets of strategy instruments have become known as marketing mix. The most commonly used elements of the marketing mix are shown in Exhibit 6.13.

At this stage, the task is to blend various elements from the marketing mix into a combination that enables the company to position its products in markets by an appropriate mix of the products, place, promotion, and price variables, so that it achieves its goals.

Product Strategy

'Product' activities are concerned with developing products (and their associated services) or services that satisfy customer needs effectively. Among the more important features that distinguish products are the following:

Quality: What is the relative quality of the product and its associated services, in relation to the competing products that are available?

Features: What particular features does the product have that distinguish it from competing products?

Options: Are there options that are not available on competing products?

Product	Place	Promotion	Price
Quality	Distribution channel	Advertising	Level
Features and options	Distribution coverage	Personal selling	Discount and allowances
Style	Outlet location	Sales promotion	Payment terms
Brand name	Sales territories	Publicity	
Packaging	Inventory, levels	and location	
Product line	Transportation carriers		
Warranty			
Service level			
Other services			

Exhibit 6.13: The Marketing Mix

Style: How well is the product styled in relation to immediate and other non-immediate competing products?

Brand Name: Does the product have a brand name with connotations?

Packaging: What is the quality of packaging of the product in relation to that offered by competitors?

Product line: Is the product just a single offering or is it part of a wider and more comprehensive product line or basket?

Warranty: What is the warranty period and the quality of warranty in comparison with warranties offered on competing products?

Service Level: Is the level of service that accompanies the product inferior or superior to that of comparable products?

Place Strategy

'Place' activities are concerned with deciding upon where the product will be sold, the method of distribution, and associated discussions such as inventory levels.

The distribution strategy and practices adopted by a company should flow from its corporate marketing strategies. It is important that the relationship has this direction, because discussions about distribution have such far-reaching strategic implications. The more important of these include:

- *Responsiveness to customers' needs and wishes:* The nature, level, and quality of customer service will be strongly influenced by the chosen method of distribution.
- *Profitability:* The method of distribution chosen: in most cases there is a choice of method, usually calling for a trade-off between the costs and benefits of alternatives.
- *Costs:* Distribution costs are significant in most industries. Fifteen percent of the turnover is perhaps a representative figure.
- *Product:* The characteristics of the product will be influenced by the method of distribution chosen.
- *Pricing:* The pricing policy adopted will be influenced not just by manufacturing and actual distribution costs but also by the nature of the distribution adopted. Thus a decision by an organisation to have broad, intensive, natural distribution will tend to demand a lower level of unit distribution costs and hence lower pricing than a decision to have limited distribution with a small number of exclusive quality outlets.
- *Promotion:* The promotional requirements of a product or service are also a function of the distribution methods employed. Thus the promotional requirements of intensive national distribution are very different from those required for smaller regional sales.
- *Relationship with other firms:* The degree to which an organization subcontracts its distribution will have major long-term implications for its relationship with other firms and its flexibility towards strategic change. Thus an organization that contracts out its distribution may have to enter long-term legal contracts that cannot easily be changed.
- *Control:* The greater the use a company makes of intermediaries to carry out its distribution the less control will it have over the marketing of its products.

Because of these and other strategically important aspects of distribution it is important that distribution policies reflect corporate policies rather than constrain or set them.

Promotion Strategy

The third element in the marketing mix is 'promotion'. This could be considered the process through which a company communicates with and influences its target market segments, with the goal of helping to position its products and services in their desired locations and generating the desired responses from them.

Promotion, apart from having the goal of generating maximum sales at minimum cost, also has the following generic goals:

Awareness

Companies frequently wish to develop in their target audience just an awareness of their products, their brands, their services, and even their existence. This may be used to,

- i. Develop potential customers' memories of the existence of a new product or service, particularly at the time when it is first offered.

- ii. Refreshing existing customers' memories of the existence of a company, a brand, a product or a service, through reminders of its existence. This is often the goal behind the promotion of products that are at a mature stage in their product life cycle.

Attitude

The generic goal 'attitude' is somewhat similar to the 'awareness' goal, in that when a promotion has such a goal, its aim is to leave primarily the targeted sector with a desired attitude of mind towards a product, a service or, indeed, an issue, and the desired attitude may not result in action. Thus, for instance in a campaign about AIDS (acquired immuno-deficiency syndrome,), the goal could conceivably be to develop twofold attitudes: to prevent the spread of AIDS and to allay people's fears and misconceptions about its transmission.

Competitive Signals

In general, the primary goal of any promotion strategy should be to help the company achieve its marketing goals. More specifically, it will often be the case that the promotion goals will be to ensure that blend of promotional devices which will achieve the maximum degree of influence in targeted market segments at minimum cost. Thus any promotion strategy should contribute to the marketing process by:

- being appropriate to the product and to the market segment that has been identified and is being targeted;
- helping position the product in the desired location in the segment;
- being appropriate to the means of distribution chosen;
- being appropriate to the resources which the company has.

Companies may, however, use promotion to signal to their competition, and other interested parties, selected information about themselves. The information could include strategic intentions, future goals, or internal health.

Price Strategy

Traditional economic theory claims that price is the primary basis of competition and the primary determinant of demand. Empirical evidence and casual observation suggests that this is often not true. Indeed, price is just one element of the marketing mix that may be employed to achieve the company's marketing objectives. A quotation from Porter would be relevant in this connection.

'Some forms of competition, notably price competition, are highly unstable and quite likely to leave the entire industry worse off from the standpoint of profitability. Price cuts are quickly and easily matched by rivals, and once matched they lower the revenues for all firms unless industry price elasticity of demand is high enough. Advertising battles, on the other hand, may well expand demand or enhance level of product differentiation in the industry for the benefit of all firms.'

This is primarily why a more satisfactory approach is to use price in conjunction with other complementary elements — product, place and promotion—in the marketing mix.

A company's pricing strategy should:

- help the company achieve its corporate goals in such areas as profitability, market share, growth, range of products, etc;
- help the company achieve its more specific marketing goals such as market share, market growth rate, etc

- materially contribute to the marketing process through:
 - being appropriate for the market segment that has been identified and is being targeted;
 - helping position the product in the desired location in the segment;
 - being appropriate to the means of distribution chosen;
 - being consistent with the means of promotion chosen for the product.

In most companies, pricing strategy and practices tend to be determined by one or more of the following major sets of influences:

- Demand influences
- Competitive influences
- Cost influences

Demand Influences

This is the area where the concept of 'elasticity' most comes into play. The demand for a product is a fundamental influence on pricing strategy, just as price of a product is a fundamental influence on the demand for it. The two are mutually dependent. Generally, the higher the price charged for a product, the less will be the volume of demand and vice-versa. Consequently, when planning price strategies for products that have high price elasticity of demand (such as international air travel), particular attention must be paid to the consequences of price changes. When such a view of pricing prevails, companies should endeavour to develop accurate sales forecasts or simulation of the demand consequences that different pricing strategies are likely to have.

Competitive Influence

Most products and services are not unique: they must compete with rivals or substitutes. Consequently, pricing strategies will normally require response to the nature of competition. This type of pricing strategy is one where the price charged for a product or service is strongly influenced by prices charged by competitors. There may, however, be two exceptions:

- Prices charged by the market leader, who sets the tone for prices charged by competitors and hence decides his own price based on other strategic considerations.
- Markets of differentiated products, in which case the impact of competitive prices is less significant. The price fixed in such cases is strongly influenced by demand considerations, superimposed by the fact that a higher price tends to signal superior quality.

Cost Influences

The cost of manufacturing a product or providing a service will be a fundamental influence in pricing strategy. A price below cost will ultimately lead to extinction while a price too high in relation to cost will encourage new entrants and stimulate customers to use substitutes. The principal types of cost-based strategies are:

- Cost plus pricing
- Target pricing
- Marginal cost pricing

Cost Plus Pricing

A cost plus pricing strategy determines the total cost per unit produced and then arrives at a price by adding to that cost a fixed percentage for profit margin. The total cost per unit is normally composed of the variable costs of production and marketing plus an allocation of overheads to cover fixed costs.

Target Pricing

The kernel of this strategy is that the price to be charged for a product should be set by meeting the predetermined return on capital employed to produce and market it.

Target pricing has an underlying assumption that the company setting the target price has the power to see that it is indeed followed in the industry and that its sales volume and market share remain unimpaired. Consequently, this type of pricing strategy tends to be adopted successfully only by companies that have this degree of power.

Marginal Cost Pricing

In marginal cost pricing, all the variable costs of production and marketing are covered, but fixed costs may be partly covered or not covered at all. There are a number of situations in which this type of pricing strategy may be particularly appropriate—although a generalised application of this strategy is potentially dangerous.

Pricing New Products or Services

A unique new product does not have the benchmarks of demand and competition; the only element known with certainty is the cost. In such an eventuality, the following approach may be adopted:

- Assume that the price of the product will at least cover marginal costs.
- Through market research—say test marketing—analysis of substitute products and the estimation of competitive reactions of the producers of substitutes—make estimates of the likely demand for the new product at different price levels, with different means of distribution and with alternative methods of promotion.
- Choose a pricing structure, method of distribution, and method of promotion that promise to generate maximum profitability based on the market research and cost analysis embodied in steps 1 and 2 above.

In general any pricing strategy should be integrated with all the elements of the marketing mix, and the price structure itself should be regarded as a variable that dynamically responds to its changing internal and external circumstances, particularly the following:

Internal: The resources the organisation has available to pursue its chosen price strategy; and the relationship between pricing strategy and the cost of production and marketing.

External: The product's stage in life cycle, the level and nature of competition, and the price elasticity of demand for the product.

Attributing Weights to Each Segment

At this stage of environmental analysis, the segments of the environment that have been selected and analysed are given weights that summarize the impact each segment is expected to have on the company under analysis, as depicted in Exhibit 6.14.

Segment	Importance	Strength	Overall score (Importance Strength)
Competitive	1	+4	+4
Marketing	1	+3	+3
Economic	5	-2	-10
Legal/Govt	2	-3	-6
Technological	3	-4	-12

Exhibit 6.14: Assigning Weights to Environmental Segments

- The *importance* to the company under analysis of each segment of the environment that has been analysed is ranked on an ordinal scale ranging from 0 to 5. Thus a segment considered to be of crucial importance is ranked 5; one of average importance scored 3, and one of no importance is scored 0.
- Once the importance of each segment has been determined, the *strength* of each factor in the period under analysis is then ranked on an ordinal scale from -5 to +5. The lower limit indicates that this factor is likely to have as strong a negative influence on the company as possible. A score of +5 indicates that the segment under consideration is likely to have as strong a positive influence on the company as possible. Finally, a score of 0 indicates that the factor does not have any influence whatsoever.
- When the importance and strength of each factor have been determined, these two numbers are multiplied and the *ordinal score* for each relevant segment in the environment is obtained. However, these scores cannot be summed up. Rather, they show individually the likely relative impact of each segment on the company. This can also be graphically depicted on the environment assessment diagram Exhibit 6.15 for a more 'live' demonstration.

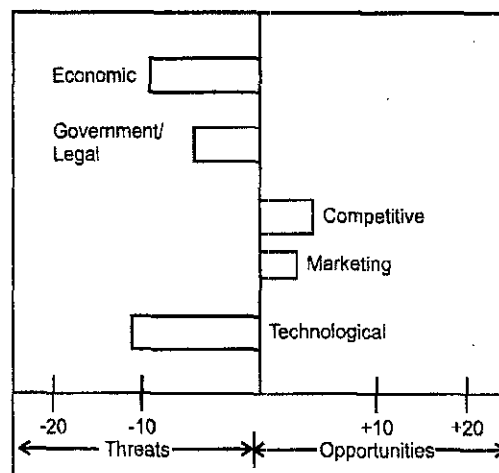


Exhibit 6.15: Environment Assessment Diagram

Environmental Analysis; Taking the Stakeholders into Account

The competitive analysis touched upon earlier in the study may be somewhat broadened as stakeholder analysis. Listing the generic stakeholders, the broad classification would be:

- Shareholders
- Suppliers
- Lenders
- Employees
- Competitors
- Society
- Government
- Customers
- Industry

Stakeholders can be classified into one of two orientation categories, depending on whether they are in favour of the organisation meeting its own objectives or not. The organization's strategy has also to be oriented accordingly. Where management has the option of an alternative course of action, stakeholders do not possess the power to dictate their terms. This means that stakeholders, in an attempt to achieve their aims, often attempt to limit the choices open to management. For instance, unions attempt to dictate management's alternatives by using picket lines and threats of violence to prevent non-union replacements from entering the firm's premises.

Stakeholders and Environmental Scanning

Changes in stakeholder needs should be tracked in the same way as environmental scanning because they could alter the perspective of the stakeholder vis-a-vis the corporation. Failure on the part of the corporation to keep up with the changing needs of stakeholders may give rise to stakeholder dissatisfaction. In turn, a dissatisfied stakeholder may attempt to change the manner in which the company relates to him/her by, for instance, altering its business terms. In order to anticipate impending changes, it is necessary to analyse the basis on which stakeholders derive their power and hence the issues causing the changes. Thus, for example, emerging technology resulting in the availability of substitute raw materials would reduce the power base of suppliers of existing materials.

The influence of shareholders is obvious. They actively or passively influence the determination of goals, objectives and missions of the organisation. They also influence the choice and tenure of the CEO and senior management, and consequently the strategies chosen by management must significantly satisfy the objectives of shareholders.

Predicting Environmental Change

As we move towards greater interdependences and growing concern for the individual, we may find it more difficult to control our economic destiny. Poor economic performance will also lead to capital shortages and to further restriction on investments in technology. Interactions between the social, political, technical, and economic environments of today's organisation will place greater pressure on strategists to monitor and forecast the organisation's future business environment. It is important to understand that most national legislation—that action which may affect us most directly—requires six to ten years to move from a social concern to legislative action. Ten years are likely to elapse before confrontation causes enough momentum and pressure to force government to take action. International issues involve even longer time spans for action to be taken unless a national crisis occurs.

Graham Molitor in his 1977 article suggests that public policy issues can be anticipated and forecasted through proper tracking of issues. By understanding the development process for public policy, organisations should be able to foresee public policy changes and accommodate them with minimal disruption. The Molitor Model includes:

- a. Tracking events or time that begin to attract leading authorities or advocates. The frequency of such events as thalidomide poisoning eventually reaches a 'critical' level, and it is then that the 'take-off point' for political action is reached and becomes 'virtually irreversible', Exhibit 6.16 shows the sequence of events.
- b. Leading authorities and advocates eventually recognize an event's significance and begin interpreting the implications of the event. Victims, though less capable of articulating the problem, are able to generate emotional support for the cause. Politicians are relatively late to join in comparison with other groups and institutions. Exhibit 6.17.
- c. Written documentation and publication of events serve to fully explore the issues involved and eventually reach the mass media for public exposure and consumption. 'Early Warnings' about emerging problems can thus be obtained from a careful review of the literature. Once scientific, technical, or professional publications confirm the details, public exposure and take-off are not far behind, as is shown in Exhibit 6.18.

- d. Institutional support for action generally forces public policy officials to consider the issue seriously. Such support generally begins at the local level, and moves to broader state and national coverage. Exhibit 6.19 shows that once these organisations, people, and resources support the action the 'point of no return' has been reached and the implementation of change is not far behind.
- e. Along with growth in institutional support over larger geographic areas comes increased concern by local, state, national, and international governments. Local legislation will be diffused to other domestic or international governments. Countries such as Sweden have become 'early adopters' of social legislation. The US has been rather slow to implement some two thousand consumer issues, some of which were implemented twenty years earlier in Sweden, as suggested in Exhibit 6.20.

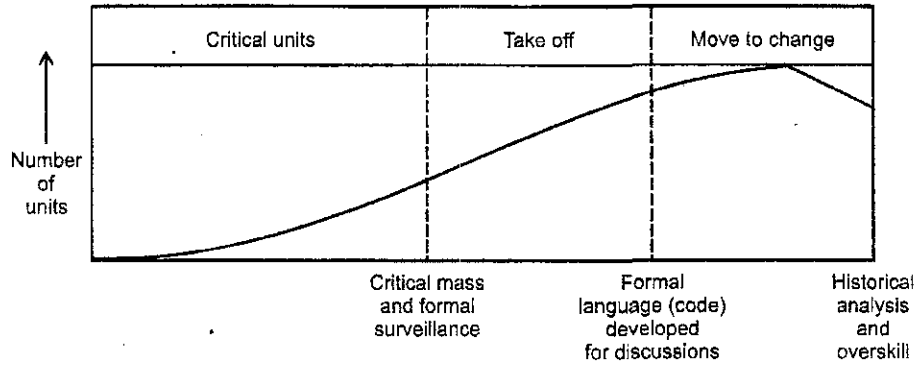


Exhibit 6.16: Leading Events Build to Take-off

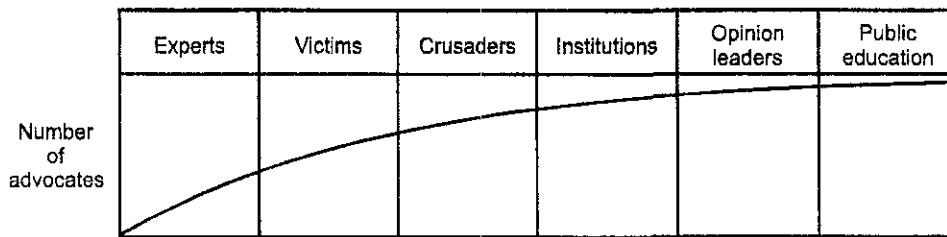


Exhibit 6.17: Leading Authorities and Advocates for Change

Exhibit 6.21 summarises the effect that public issues can have on political action. By overlaying the five dimensions of political actions, the point at which a 'critical mass of support comes together can be identified as the 'take off point for action. From that point on, momentum can be expected to increase and create intense

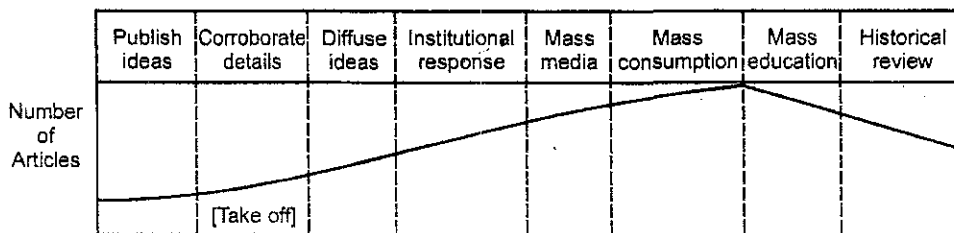


Exhibit 6.18: Leading Literature Support for Change

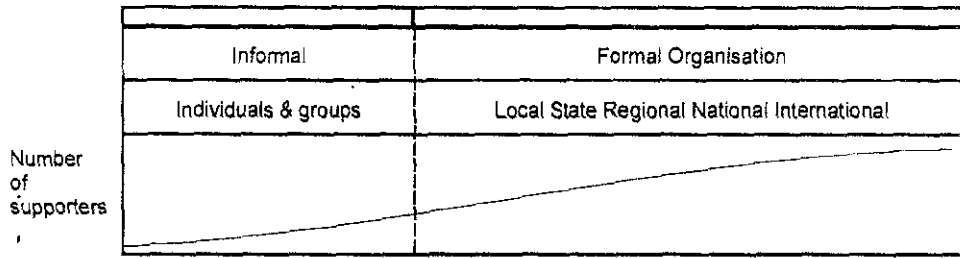


Exhibit 6.19: Organisational Support for Change

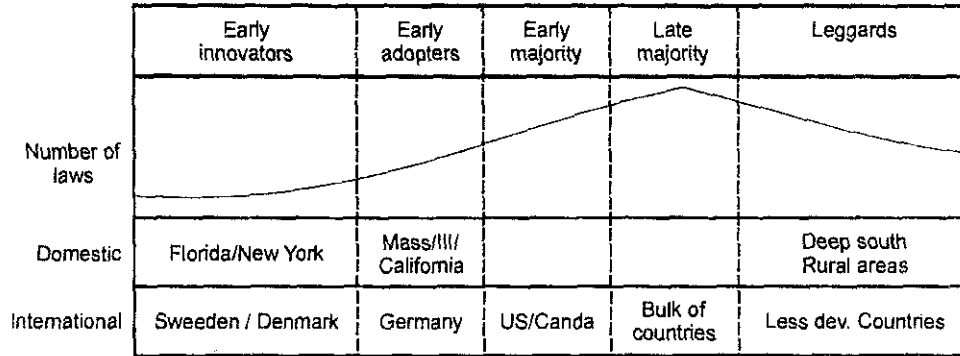


Exhibit 6.20: Political Leaders in Implanting Change

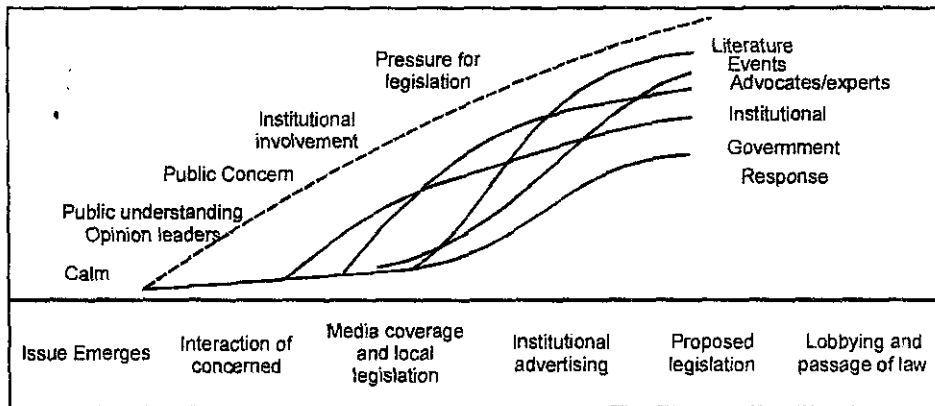


Exhibit 6.21: Forecasting Political Actions

pressure for action. From this point onwards, there is little possibility of changing the direction of action. By tracking the social pressure for political action, organisations have ample time to either (a) attempt to impact the direction of change, (b) plan alternatives, or (c) reallocate resources to deal with expected change.

The importance of tracking social issues should be apparent. Without recognising the currents of change, managers are quite likely to be caught off guard, surprised at the implementation of new policies, and unable to adapt effectively. This approach, therefore, simply outlines a methodology for environmental scanning in a complex, rapidly changing environment.

Tracking Environment Issues

The growing interdependence and speed of economic changes will require greater adjustments and more efficient means of adjusting to change. Some of the changes that will impact economic decisions include:

- i. changing trade and investment patterns,
- ii. changing the economic importance of various regions and nations,
- iii. changing the impact of productivity and technology on employment and locations, and
- iv. changing government intervention into pricing and production decisions. Such changes will impose hardships on affected individuals, firms, industries, communities, and nations that cannot adjust effectively to the new conditions.

Given the variety of changes taking place in the general business environment, it will be difficult for management to set priorities and decide what strategies are required to cope with complex environmental problems. It will be necessary, therefore, for managers to develop a methodology for tracking environmental issues and determining priorities for action. One method for managers to prioritise those issues they will track more specially is shown in Exhibit 6.22. For a given organisation, environmental issues can be placed in one of the nine cells of the matrix. Those issues that will have high impact on the business and have a probability of political action are 'critical' to management and need formal attention and specific strategies developed to cope with imminent change. Issues in the moderate impact cells need high priority attention in order to possibly influence political outcomes. Low priority issues still need watching in case they develop in combination with other issues which may change their importance.

We are, however interested in environmental analysis from the point of view of strategic implementation and consequent strategy formulation. For that we have to look at,

- i. environmental evolution,
- ii. the process of environmental analysis and, finally,
- iii. integrate environmental analysis into strategic analysis.

We briefly elaborate these three stages.

i. *Environmental Evolution*

Three constructs are useful to describe changes in the environmental segments:

- Types of changes,
- forces driving change, and
- types of future evolution.

Changes in the macro-environmental segments may be *systematic* or *discontinuous*. Gradual, continuous, and potentially predictable changes are termed *systematic*. While random, unpredictable, sudden changes are termed *discontinuous*.

For analytical purposes, it is important to go beyond description of change to assess the forces driving it.

		← Impact on Business		
		High	Medium	Low
Probability of action	High	Critical	High priority	Low priority
	Medium	High priority	High priority	Low priority
	Low	To be watched	Low priority	Low priority

Exhibit 6.22: Identifying High Priority Environmental Issues.

Sometimes, forces driving change in one segment, lie in changes in other segments. Thus shifts in social segments (for example migration of the population) may affect the political segment (for example distribution of regional power). Usually, however, each segment evolves quasi-autonomously. That is why the existence of inducements and autonomous evolution resulting in changes in segments should be analysed independently as well as in conjunction with identifying the underlying forces.

Often, driving forces interact with one another. Such interaction may be *reinforcing*, *conflicting* or *disjoined*. When the forces support one another in terms of their effect on changes in a third segment, the effect may be reinforcing. When they dampen one another, they are conflicting, and when they do not affect one another, they are disjoined. In addition, the effects of changes in one segment may have *primary* or *secondary* consequences for other segments. When the effects are direct, they are termed primary consequences. In some cases, changes may not have a direct impact on other segments; however, consequences may ensue as a result of direct effect on a third segment. These are termed secondary consequences. Finally, in charting the evolution of change in the future, it is important to characterize whether such evolution is completely predictable from the present trends or whether it is contingent upon actions of the firm or other entities in the environment. This refers to *closed* and *open* versions of the future, respectively. This distinction is often critical: in contrast to the closed version, the open version should alert organisations to potential action domains that needs further analysis, or where firm-level responses may enable it to shape the future evolution of the change.

Process of Environmental Analysis

Conceptually, the process of environmental analysis can be divided into four analytical stages:

- scanning the environment to detect warning signals,
- monitoring specific environmental trends,
- forecasting the direction of future environmental changes, and
- assessing current and future environmental changes for their organisational implications.

A conceptual overview of these four activities and their interactions is shown in Exhibit 6.23.

Scanning

In its *prospective mode* scanning focuses on identifying precursors or indicators of potential environmental changes and issues. Environmental scanning is thus aimed at alerting the organisation to potentially significant external impingement *before* it has fully formed or crystallised. Successful environmental scanning draws attention to possible changes and events well before occurrence, allowing time for suitable strategic actions.

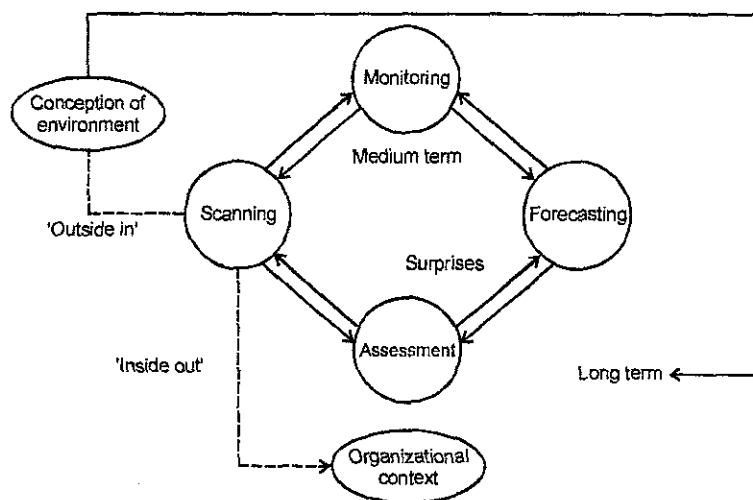


Exhibit 6.23: Environmental Analysis Activities

In the prospective mode, scanning is part of an analytical activity and becomes useful when environmental changes take time to unfold, as is indeed often the case. For example, social value shifts do not occur in just days or even months, technological changes often take years, as may the development of large-scale social movements.

Scanning in the *current* and *retrospective* sense identifies surprises or strategic issues requiring immediate action on the part of an organisation. In this case, the out-puts may feed directly into assessment and influence the current and imminent strategic decisions of an organisation. Scanning frequently detects environmental change that is already in an *advanced* stage; a change that has already evolved to a point where it is actual or imminent rather than potential at some, as yet unspecified date. Thus a scan of demographic data might pick up population movement or changes in household formation. Scanning frequently unearths actual or imminent environmental change because it explicitly focuses an organisation's antennae on areas that may previously have been neglected, or it challenges the organisation to rethink areas to which it had earlier paid attention.

It is important to recognise that scanning is the most *ill-structured* and ambiguous environmental analysis activity. The data sources are many and varied. Moreover, a common feature of scanning is that early signals often show up in unexpected places. Thus *the purview of search must be broad*.

Partly in consequence, the noise level of scanning is likely to be high. In consequence, the fundamental challenge for the analyst in scanning is to make sense of vague, ambiguous, and unconnected data, and to infuse meaning into it.

Three critical decisions during scanning need high-lighting.

First, the scope and breadth of data and data sources inevitably influence the analyst's perceptions. Second, the data *do not speak by themselves: the analyst has to breathe life into them*. Third, *critical acts of judgement are required of the analyst in his or her choice of events and/ or precursors to consider for monitoring, forecasting, and/ or assessment*. All these entail skill and expertise on the part of the analyst.

Monitoring

Monitoring entails tracking the evolution of environmental trends, the sequences of events, or streams of activity. It frequently involves following the signals or indicators unearthed during environmental scanning, and in this sense is a follow up process.

The purpose of monitoring is to assemble sufficient data to discern whether certain patterns are emerging. Two comments are relevant in this regard.

First, they are likely to be a complex of discrete trends. For example, an emergent life-style pattern may include changes in entertainment, education, consumption, work habits and domicile—location preferences. In the initial stages of monitoring, the patterns are likely to be hazy because they are the outputs of scanning: the analyst has only a vague notion of what to look for. Second, highly formalised and quantified databases usually found in archives of organisations represent a characterisation based on a previously identified pattern and may be of only limited utility in tracking emergent patterns.

In monitoring, the data search is focused and much more systematic than in scanning. By *focused*, it is meant that the analyst is guided by a priori hunches. *Systematic* refers to the notion that the analyst has the general sense of the pattern/ (s) he is looking for and collects data regarding the evolution of the pattern.

As monitoring progresses, the data frequently move from the imprecise and unbounded to reasonably specific and focused. Thus, for example, in tracking the emergence of social issues, the first indicators are feelings of discontent or loosely distributed concerns expressed by a few individuals. These sentiments gather support and gradually what is often referred to as a *social movement* begins to evolve. Environmentalist movements at national levels are a case in point.

A number of data interpretations or judgements are unavoidable in monitoring. These judgements are often complex, further confounded when individuals within the same organization make different and often conflicting judgements.

The outputs of monitoring are threefold:

- i. a specific description of environmental patterns to be forecast,
- ii. identification of trends for further monitoring, and
- iii. identification of patterns requiring further scanning.

Forecasting

Scanning and monitoring provide a picture of what has already taken place and what is currently happening. However, strategic decision-making requires a further orientation; it needs a picture of what is likely to happen. Thus forecasting is an essential element in environment analysis.

Forecasting is concerned with the development of plausible *projections* of directions, scope, speed, and intensity of environmental change, to lay out the evolutionary path of anticipatory change. There are two conceptually separable, though integrally related, activity elements in forecasting. The first concerns projections based on trends that are evident and can be expected, with some margin of error, to continue unabated in a given period of time into the future. Demographic trends would be suitable examples. The second relates to *alternative futures* that may come about not only on the basis of current trends but judgements regarding events that may take place or that may be made to happen by an organisation or entities outside it. Forecasting, based on projections, involves a closed perspective whereas forecasting based on alternate futures corresponds to a version of open perspective.

There are a number of key analytic tasks and outputs involved in forecasting. The first concerns untangling of *forces* that drive the evolution of a trend. This is a necessary prerequisite to charting out the trend's evolutionary path. The second concerns understanding the *nature of the evolutionary path*: that is whether the change is a fad or of some duration, or cyclical or systematic in character. The third concerns more or less clearly *delimiting the evolutionary path* or paths leading to projections and alternative futures. The critical outputs of forecasting are specific understanding of future implications of current and anticipated environmental changes and decision-relevant assumptions, projections, and information.

Since the focus, scope, and goals of forecasting are more specific than in scanning and monitoring, forecasting is usually a much more *deductive* and rigorous activity. A wide variety of forecasting techniques are available, ranging from simple extrapolation to methodologies involving multiple participants making forecasts in a number of iterations such as Delphi or scenario development.

Assessment

Scanning, monitoring, and forecasting are not ends in themselves, unless their outputs are assessed for their implications for the organisation's current and potential strategies. Scanning, monitoring, and forecasting merely provide *niche-to-know* information. Assessment involves identifying and evaluating how and why current and projected environmental changes will affect strategic management of an organisation. In assessment, the frame of reference moves from understanding the environment—the focus of scanning, monitoring and forecasting—to identifying what that understanding of environment means for the organisation. Assessment thus endeavours to answer the question: what are the implications of our analysis of the environment for our organisation?

From the perspective of linking environmental analysis and strategic management, the critical question is: what is likely to be the positive or negative impact of environmental patterns on the firm's strategies? This question compels linking of environmental patterns and the organisation's context. Those patterns judged to have already had an impact on the organisation's strategy or to possess the potential to do so are deemed to be *issues* for the organisation.

Criteria against which specific patterns should be judged include the following:

- How might the pattern have an impact on the organisation?
- What is the probability that the pattern will develop and become clearly recognisable?
- How great will be the eventual impact on the organisation?
- When is the issue likely to peak—near term, medium term, long term?

The intention of the first criterion is to determine whether the pattern has or will have an impact on the organisation. The other criteria follow in the analysis in logical sequence. Issues can then be conveniently arrayed on a probability-impact matrix, as shown in Exhibit 6.24, with a separate matrix being prepared for each of the three planning periods: short, medium, and long term. The merits of the matrix display are that it provides a comprehensive, at-a-glance array of issues, orders them in a way that facilitates discussion and planning, and places them in time-frames appropriate to the allocation of resources and management attention.

Two Approaches to Environmental Analysis

It is possible to conceptualise and execute two distinct though related approaches to environmental analysis—an *outside-in or macro approach* and an *inside-out or micro approach*. The outside-in approach adopts a broad view of the environment, focused on longer term trends, develops alternative views or scenarios of the future environment, and then derives implications for the industry surrounding the firm, and, of course for the firm itself. The inside-out view adopts a narrow view of the environment, develops a picture of what is currently happening through ongoing monitoring as a basis for forecasting the immediate future environment and then derives implications for the industry and the firms within it. A characterisation of these two approaches is clear from the discussion above. A little introspection will, show the integral relationship between the two approaches.

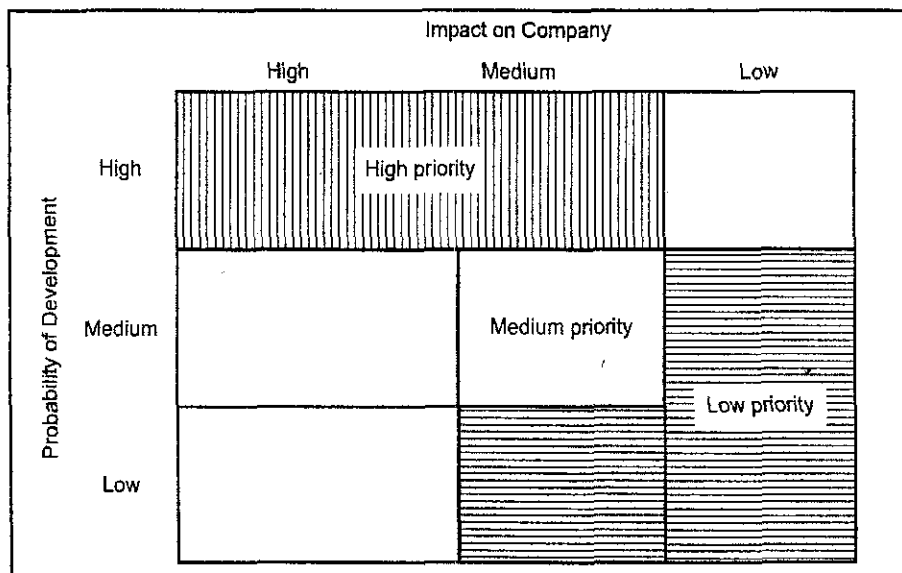


Exhibit 6.24: Probability Impact Matrix

Temporal Cycles

Exhibit 6.23 portrays the multiple time-bound cycles in environmental analysis. Surprises or discrete issues encountered during early scanning activities may require immediate action on the part of the organisation, implying the short time cycle. Similarly, monitoring activities may engender short and medium-term actions. What is important to emphasise is that they have to be considered in entirety and their implications considered separately.

Differences among Environmental Segments

Exhibit 6.24 makes it clear that there are different environmental segments and activities within them assume different characteristics. They have their primary impact on different parts of the organisation requiring different strategic responses. These are now briefly touched upon.

Integrating Environmental Analysis into Strategic-Analysis

The integration is primarily inside-out in character and three points need to be borne in mind regarding it. First, environmental analysis, although often intrinsically interesting, is useful only to the extent that it results in strategy-related insights and action. Second, integration does not just happen, it is *made to happen*. The specific linkages to various kinds of actions need to be thought through and not left to evolve in an unplanned manner. Third, integration needs to take place in short-, medium- and long-run horizons.

The implications of environmental issues need to be assessed for strategic planning at three levels:

- i. corporate strategy where product-market decisions are usually the focus;
- ii. business strategy, where the focus is on how to compete within an industry and,
- iii. functional-level strategy where operational decisions are the concern.

Corporate Strategy

At the level of corporate strategy, environmental impact on three key issues needs to be considered:

- i. patterns of diversification,
- ii. portfolio planning, and
- iii. risk-return trade-offs.

Patterns of Diversification

There are at least three modes by which the environment influences patterns of diversification. First, firms differ in terms of the synergies they seek to exploit across their businesses. These synergies could be upset or enhanced by macro-environmental change. Second, different patterns of diversification manifest different vulnerabilities. Macro-environmental changes may amplify these vulnerabilities. Third, macro-environmental trends may open up or close out existing patterns of diversification. Deregulation of industries is one such change.

Portfolio Planning

Macro-environmental trends have important implications for the bases of portfolio planning. Typical portfolio approaches focus on a business' competitive advantages within an existing industry, constrained by the financial resources of the firm. Ansoff notes that macro-environmental trends may necessitate portfolio planning based on such bases as resources or technology.

Environmental analyses are also particularly important for planning the potential future portfolio. Product portfolio approaches are useful for portfolio planning *within* the existing set of businesses, or at best pointing out the direction of search for additional businesses. The specific businesses to be targeted need to be considered in the light of macroenvironmental forecasts and predictions.

Risk-Return Trade-offs

Political, economic, technological, and demographic shifts have an impact on the returns and risks of existing and planned portfolios. It is important to consider environmental impacts on each of these characteristics of corporate-level strategy.

Business Strategy

Industry structure changes in the macro-environment may affect

- the boundaries of the industry,
- the forces shaping industry structure, such as suppliers, customers, rivalry and product substitution, entry barriers,
- strategic groups,
- the key success factors, and
- the general expectations within the industry.

It is elaborated briefly below:

- i. Perhaps of greatest importance is the impact of environmental change on the survival of an industry or specific industry segments. For instance, technology advances underlying frozen foods and personal com-puters have irrevocably altered our conceptions of the food and computer industries.
- ii. Environmental trends directly influence the *forces shaping industry structure*: suppliers, consumers, new entrants and substitutes. Environmental changes can affect:
 - a. the number, types, and location of suppliers, their products and supply costs, and the competitive dynamics of suppliers;
 - b. the size, characteristics and behaviour of a firm's customers;
 - c. the rate and trend of product substitution, and
 - d. change in entry barriers.
- iii. Environmental changes have a differential impact on various *strategic groups* within the industry. Changes, to the extent that they affect customer preferences, supplier capabilities, substitute products, and so forth could potentially enlarge or decimate product market arenas in which different strategic groups operate. For example, deregulation of the airline industry in the USA in the late 1970s had an adverse impact on longer-haul firms in relation to those with shorter hauls.
- iv. Environmental change can potentially affect the key success factors in almost any industry or industry segment. It can affect relative cost positions, reputation, and resource requirements for major product market segments.
- v. Environmental changes potentially *affect general expectations about an industry*. For instance, since the deregulation of the telecommunication industry in the USA, many telephone companies are discovering that their assessment of competitors' responses, shaped by their past behaviour, are no longer valid.

Impact on Business unit Strategy

Such impact becomes manifest in (a) business definition, (b) assumption, and (c) general strategic thrust. These assessments are likely to be medium- or short-term oriented.

Business definitions are in terms of what customers are served, the customer needs that are satisfied, and the technology employed for the purpose.

The assumptions are in terms of the anticipated actions of suppliers, customers, competitors, or new entrants to the industry.

Examples of a general strategic thrust would be building, maintaining, etc. of market share.

Functional Level Strategy

Macro-environmental changes have implications for the functional level strategies of an organization, over and beyond business strategies.

Consider the following examples:

- a. Changes in demographics, life-styles, values with birth of a totally new set of customers.
- b. Changes in general expectations regarding working hours resulting in the birth of flextime, alternative work schedules, increase in the proportion of working women resulting in creation of childcare centers.

Mega Trends

Finally, certain broad trends in the external environment having consequent impacts on a firm's working need to be noted and accounted for. Ten such trends or influences are a movement from:

- i. an industrial to information society;
- ii. forced technology to a matching of each new technology with a compensatory human response ('hi-tech—high touch');
- iii. a national to world economy;
- iv. short-term to long-term considerations, with emphasis on strategic planning;
- v. a period of centralisation to decentralisation of power;
- vi. reliance on institutional help to greater self-reliance;
- vii. representative democracy to more participative democracy, in politics as well as at the workplace.
- viii. our dependence on traditional hierarchical structures to an informal network of contracts;
- ix. the north and west to the south and east geographically and economically;
- x. a society with a limited number of personal choices to a multiple-option society.

The final product of environmental analysis is its contribution to strategic thinking and its input for the development of a strategic plan for the business. Merely interesting studies will not suffice. More relevant and specific contributions include the development of planning assumptions, the framing of issues for strategy development, and the pursuit of studies of strategic environmental issues. A possible matrix approach to issue identification is presented in Exhibit 6-25.

When a set of coherent and comprehensive environmental assumptions is developed, it becomes the first and most obvious input in the strategic plan. This is one leg of the three-legged stool on which strategy development rests (the other two being resource analysis and strategy concept), so it is important that it should be sturdy. The environment analysis chapter of the strategic plan should, at the very minimum:

- identify the key forces operating in the business environment (past, present, and future);
- make explicit the assumptions about their future course;
- analyse the strategic significance of these factors—the threats, opportunities, and issues that they pose;
- highlight the major contingencies (and their trigger points) for which contingency plans should be developed.

Issues should be framed in an orderly and disciplined way, so that constructive strategies can be developed to respond to these. A suggested framework for this framing is the following eight-step sequence which organizes the necessary information to focus on the necessary strategic responses:

- Definition of the issue: a succinct (one-sentence) statement of the issue, from the point of view of business strategy.

- **Strategic significance:** identification of the threats and opportunities posed by the issue.
 - **Driving forces:** the key environmental forces that converge (now and in the future) to make this an issue.
 - **Prospects:** the potential outcomes and developments of the issue under alternative scenarios.
- Impact on industry } Sectors of the industry and/or aspects of the business most likely to
 - Impact on Company } be affected by the threats and opportunities.

Micro-environment	Trends, Events, Developments in the Macro-environment			
	Social	Economic	Political	Technological
Markets				
Customers				
Employees				
Competitors				
Technology				
Materials & supplies				
Production				
Finances				
Shareholders				
Public & government relations				

Exhibit 6.25: A Matrix Approach to Issue Identification

- **Planning challenges:** a set of 'need to....' statements listing out the overall actions required of the business to maximise the opportunities and minimise the threats.
- **Strategic responses:** a set of specific strategy alternatives to be considered as ways of implementing the 'need to....' statements.

Finally, environmental analysis should be the source of those in-depth studies of critical external trends and factors—*inflation energy prospects, global competition, new technology*—which may require detailed and specific analysis because of their special significance for business strategy.

Chapter 7

Organisational Dynamics and Structuring Organisational Appraisal

The appraisal of the external environment of a firm helps it to think of what it might choose to do. The appraisal of the internal environment, on the other hand, enables a firm to decide about what it can do.

This chapter deals with the internal environment of an organisation. We shall build a foundation for understanding the internal environment through an explanation of its dynamics. This has been done by referring to the resource-based view of strategy.

The resources, behaviour, strengths and weaknesses, synergy, and competencies constitute the internal environment, and we shall deal briefly with each of these aspects initially. All these together determine the organisational capability that leads to strategic advantage.

Organisational capability could be understood in terms of the strengths and weaknesses existing in the different functional areas of an organisation. We shall consider six such areas: finance, marketing, operations, personnel, information management and general management. For each of these, we shall mention the important factors influencing them and clarify the nature of the various functional capability factors through illustrations.

We deal with the factors that affect appraisal, the approaches adopted for appraisal, and the sources of information used to perform organisational appraisal. With regard to the methods and techniques used for organisational appraisal, we consider a range of factors grouped under the three headings of internal analysis, comparative analysis, and comprehensive analysis. The application of these methods results in highlighting the strengths and weaknesses that exist in different functional areas.

We attempt to understand the internal environment of an organisation in terms of the organisational resources and behaviour, strengths and weaknesses, synergistic effects, and competencies.

An organisation uses different types of resources and exhibits a certain type of behaviour. The interplay of these different resources along with the prevalent behaviour produces synergy or dysergy within an organisation, which leads to the development of strengths or weaknesses over a period of time. Some of these strengths make an organisation specially competent in a particular area of its activity causing it to develop competencies. Organisational capability rests on an organisation's capacity and ability to use its competencies to excel in a particular field.

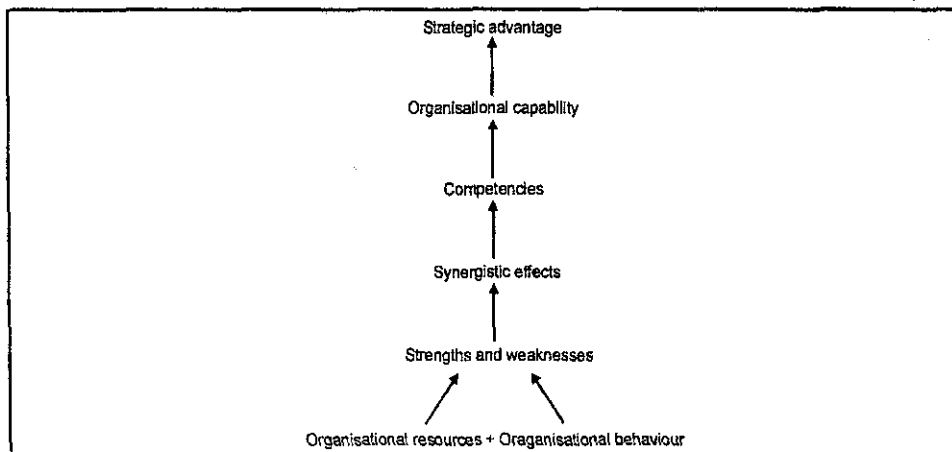


Exhibit 7.1: Framework for the Development of Strategic Advantage by an Organisation.

The resources, behaviour, strengths and weaknesses, synergistic effects and competencies of an organisation determine the nature of its internal environment. Exhibit 7.1 depicts a diagram showing the framework that we have adopted for the explanation of the process of development of strategic advantage by an organisation. It is (expected that the readers of this book are aware of these terms in general. However, explain each of these terms here to place them in the specific context of strategic management.

Organisational Resources

The dynamics of the internal environment of an organisation can be best understood in the context of the resource-based view of strategy, According & Barney (1991), who is credited with developing this view of strategy as a theory, a firm is a bundle of resources—tangible and intangible—that include all assets, capabilities, organisational processes, information, knowledge, and so on. These resources could be classified as physical, human, and organisational resources. The physical resources are the technology, plant and equipment, geographic location, access to raw materials, among others. The human resources are training, experience, judgement, intelligence, relationships, and so on, present in an organisation. The organisational resources are the formal systems and structures as well as informal relations among groups. Elsewhere, Barney has said that the resources of an organisation can ultimately lead to a strategic advantage for it if they possess four characteristics, that is, if these resources are valuable, rare, costly to imitate, and non-substitutable.

Like individuals, very few organisations are born with a silver spoon in the mouth; most organisations have to acquire resources the hard way. The cost and availability of resources are the most important factors on which the success of an organisation depends. If an organisation is favourably placed with respect to the cost and availability of a particular type of resource, it possesses an enduring strength which may be used as a strategic weapon by it against its competitors. Conversely, the high cost and scarce availability of a resource are handicaps which cause a persistent strategic weakness in an organisation.

But the mere possession of resources does not make an organisation capable. Much depends on their usage within an organisation.

Organisational Behaviour

Organisational behaviour is the manifestation of the various forces and influences operating in the internal environment of an organisation that create the ability for, or place constraints in the usage of resources. Organisational behaviour is unique in the sense that it leads to the development of a special identity and character of an organisation. Some of the important forces and influences that affect organisational behaviour are: the quality of leadership, management philosophy, shared values and culture, quality of work environment and organisational climate, organisational politics, use of power, among others.

The perceptive reader would note that what we are proposing here is a marriage of the hard side of an organisation—its resource configuration—with the soft side of behaviour. The resources and behaviour are thus the yin and yang of organisations. What they collectively produce are the strengths and weaknesses.

Strengths and Weaknesses

Organisational resources and behaviour do not exist in isolation. They combine in a complex fashion to create strengths and weaknesses within the internal environment of an organisation. A strength is an inherent capability which an organisation can use to gain strategic advantage. A weakness, on the other hand, is an inherent limitation or constraint

which creates a strategic disadvantage for an organisation. Financial strength, for example, is a result of the availability of sources of finance, low cost of capital, efficient use of funds, and so on. Another example is of a weakness in the operations area which results due to inappropriate plant location and layout, obsolete plants and machinery, uneconomical operations, and so on. In the following sections, we will take up a detailed discussion of the strengths and weaknesses in different functional areas within an organisation.

Strengths and weaknesses do not exist in isolation but combine within a functional area, and also across different functional areas, to create synergistic effects.

Synergistic Effects

It is the inherent nature of organisations that strengths and weaknesses, like resources and behaviour, do not exist individually but combine in a variety of ways. For instance, two strong points in a particular functional area add up to something more than double the strength. Likewise, two weaknesses acting in tandem result in more than double the damage. In effect, what we have is a situation where attributes do not add mathematically but combine to produce an enhanced or a reduced impact. Such a phenomenon is known as the synergistic effect. Synergy is the idea that the whole is greater or lesser than the sum of its parts. It is also expressed as the two-plus-two-is-equal-to-five-or-three effect'.

Within an organisation, synergistic effects occur in a number of ways. For example, within a functional area, say of marketing, the synergistic effect may occur when the product, pricing, distribution, and promotion aspects support each other, resulting in a high level of marketing synergy. At a higher level, the marketing and production areas may support each other leading to operating synergy. On the other hand, marketing inefficiency reduces production efficiency, the overall impact being negative, in which case dysynergy (or negative synergy) occurs. In this manner, synergistic effects are an important determinant of the quality and type of the internal environment existing within an organisation and may lead to the development of competencies.

Competencies

On the basis of its resources and behaviour, an organisation develops certain strengths and weaknesses which when combined lead to synergistic effects. Such effects manifest themselves in terms of organisational competencies. Competencies are special qualities possessed by an organisation that make them withstand pressures of competition in the marketplace. In other words, the net results of the strategic advantages and disadvantages that exist for an organisation determine its ability to compete with its rivals. Other terms frequently used as being synonymous to competencies are unique resources, core capabilities, invisible assets, embedded knowledge, and so on.

When an organisation develops its competencies over a period of time and hones them into a fine art of competing with its rivals it tends to use these competencies exceedingly well. The capability to use the competencies exceedingly well turns them into core competencies.

When a specific ability is possessed by a particular organisation exclusively, or in a relatively large measure, it is called a distinctive competence. Many organisations achieve strategic success by building distinctive competencies around the CSFs. CSFs are those factors which are crucial for organisational success. A few examples of distinctive competencies are given below.

- Superior product quality in a particular attribute, say, a two-wheeler, which is more fuel-efficient than its competitor products.
- Creation of a market niche by supplying highly-specialised products to a particular market segment
- Differential advantages, based on the superior R&D skills of an organisation not possessed by its competitors.
- An organisation's access to a low-cost financial source like equity shareholders, not available to its competitors.

A distinctive competence is “any advantage a company has over its competitors because it can do something which they cannot or it can do something better than they can”. It is not necessary, of course, for all organisations to possess a distinctive competence. Neither do all the organisations, which possess certain distinctive competencies, use them for strategic purposes. Nevertheless, the concept of distinctive competence is useful for the purpose of strategy formulation. The importance of distinctive competence in strategy formulation rests with “the unique capability it gives an organisation in capitalising upon a particular opportunity; the competitive edge it may give a firm in the market place; and the potential for building a distinctive competence and making it the cornerstone of strategy”.

To some of you, we may seem to be making a hairline distinction here between the three terms: competencies, core competencies, and distinctive competencies. The difference, as you must have noted, lies in the degree of uniqueness associated with the net synergistic effects occurring within an organisation. You could think of them as being synonymous so long as you are able to make a distinction among them when necessary. Among the three, it is the term “core competence” that has gained greater currency and popularity. The term “core competence” has been popularised by Prahalad and Hamel as an idea around which strategies could be formulated by an organisation.

Several Indian companies have taken to the idea of core competence in right earnest. Examples abound of companies shedding businesses that are not in line with their perceived core competencies and focussing upon those that are. Kumar Mangalam Birla, of the A V Birla group, sees the group’s core competencies in a wide array of skills related to process industries, project management, operations, raw material sourcing, distribution and logistics, setting up dealer networks commodity branding, and raising finance at a competitive cost. S Kumar sees its core competence in textile processing, Nandas of Escorts in light engineering, and Reliance Industries in skillful project management and execution.

The idea of Core Competence seems to be a brilliant way to focus upon the latent strength of an organisation. Yet there are pitfalls of which an organisation has to be aware. Core competencies can be developed but also lost. They cannot be taken for granted. The ability of a core competence to provide strategic advantage can diminish over time as they do not exist perpetually. A dilemma associated with all core competencies is that they have the potential of turning into core rigidities. The external environment is responsible for this sad turn of events. New competitors may figure out a way to serve customers or new technologies may emerge causing the existing company to lose its strategic advantage. Over-reliance on core competencies to the extent of becoming prisoners of one’s own excellence may result in strategic myopia.

That core competence acts as a double-edged sword is demonstrated by the concept of strategic commitment enunciated by Pankaj Ghemawat. This means an organisation’s commitment to a particular way of doing business, that is, developing a particular set of resources and capabilities. Ghemawat’s contention is that once a company has made a strategic commitment it finds it difficult to respond to new competition if doing so requires a break with its commitment.

Core or distinctive competencies serve a useful purpose if they are used to develop sustained strategic advantages through building up organisational capability

Organisational Capability

Organisational capability is the inherent capacity or potential of an organisation to use its strengths and overcome its weaknesses in order to exploit opportunities and face threats in its external environment. It is also viewed as a skill for coordinating resources and putting them to productive use. Without capability, resources, even though valuable and unique, may be worthless. Since organisational capability is the capacity or potential of an organisation, it means that it is a measurable attribute. And since it can be measured, it follows that organisational capability can be compared. Yet it is very difficult to measure organisational capability as it is, in the ultimate analysis, a subjective attribute. As an attribute, it is the sum total of resources and behaviour, strengths and weaknesses, synergistic effects occurring in and the competencies of any organisation.

Several thinkers in the field of strategy favour the line that capabilities are the outcome of an organisation's knowledge base, that is, the skills and knowledge of its employees. There is a growing body of opinion that considers organisations as reservoirs of knowledge in which case they are all learning organisations. In fact, the concept of organisational learning has spawned a whole school of strategy thought.

It is to be noted that while the concept of a learning organisation is applicable to strategic management in a wider sense at several places, here we are referring to it in the specific context of capability that is seen as an outcome of organisational learning.

Strategists are primarily interested in organisational capability because of two reasons. Firstly, they wish to know what capacity exists within the organisation to exploit opportunities or face threats in its environment. Secondly, they are interested in knowing what potentials should be developed within the organisation so that opportunities could be exploited and threats should be faced in future.

Organisational capability is measured and compared through the process of organisational appraisal which is the subject matter of this chapter. A feasible approach to appraising the organisation is to start with the factors and influences operating within the organisation. These could be called the organisational capability factors.

Strategic Advantage

Strategic advantages are the outcome of organisational capabilities. They are the result of organisational activities leading to rewards in terms of financial parameters, such as, profit or shareholder value, and/or non-financial parameters, such as, market share or reputation. In contrast, strategic disadvantages are penalties in the form of financial loss or damage to market share. Clearly, such advantages or disadvantages are the outcome of the presence or absence of organisational capabilities. Strategic advantages are measurable in absolute terms using the parameters in which they are expressed. So, profitability could be used to measure strategic advantage—the higher the profitability the better the strategic advantage. They are comparable in terms of the historical performance of an organisation or its current performance with respect to its competitors.

Competitive advantage is a special case of strategic advantage where there are one or more identified rivals against whom rewards or penalties could be measured. So, outperforming rivals in profitability or market standing could be a competitive advantage for an organisation. Competitive advantage is relative rather than absolute, and it is to be measured and compared with respect to other rivals in an industry.

With rising competitiveness in the industry, mainly owing to liberalisation and the reform process, the usage of the term "competitive advantage" has become more pronounced. The term "competitive advantage" is more popular since it has been used as an important concept by the proponents of the positioning school of thought in strategy

Structuring Organisational Appraisal

Just as environmental appraisal is structured through an environmental threat and opportunity profile organisational appraisal can also be structured through various techniques. For instance, Glueck proposes a preparation of the strategic advantage profile (SAP) where the results of organisational appraisal are presented in a summarised form. Another approach, suggested by Rowe et al., is to prepare a company capability profile as a means for assessing a company's strengths and weakness in dealing with the opportunities and threats in the external environment. Here we propose a similar approach of making an organisational capability profile which can be summarised in the form of a SAP. The SAP is then matched with the environmental threats and opportunity profile, which may have been prepared while structuring the environmental appraisal, in order to look for strategic alternatives and exercise a strategic choice.

Preparing the Organisational Capability Profile

The organisational capability profile (OCP) is drawn in the form of a chart as depicted in Exhibit 7.2 which shows a summarised OCP. The strategists are required to systematically assess the various functional areas and subjectively assign values to the different functional capability factors and sub factors along a scale ranging from the values of -5 to +5. A detailed OCP may run into several pages where each of the sub factors constituting the different functional capability factors can be assessed. In this manner, a summarised OCP, as shown Exhibit 7.2, may be prepared.

	Capability factors		
	Weakness -5	Normal 0	Strength +5
1. Financial capability factors			
(a) Sources of funds			
(b) Usage of funds			
(c) Management of funds			
2. Marketing capability factors			
(a) Product-related			
(b) Price-related			
(c) Promotion-related			
(d) Integrative and systematic			
3. Operations capability factors			
(a) Production system			
(b) Operations and control system			
(c) R&D system			
4. Personnel capability factors			
(a) Personnel system			
(b) Organisational and employee characteristics			
(c) Industrial relations			
5. Information management capability factors			
(a) Acquisition and retention of information			
(b) Processing and synthesis of information			
(c) Retrieval and usage of information			
(d) Transmission and dissemination of information			
(e) Integrative, systemic, and supportive			
6. General management capability factors			
(a) General management system			
(b) External relations			
(c) Organisational climate			

Exhibit 7.2: Summarised Form of Organisational Capability Profile

After the completion of the chart, the strategists are in a position to assess the relative strengths and weaknesses of an organisation in each of the six functional areas and identify the gaps that need to be filled or the opportunities that could be used. The preparation of an OCP provides a convenient method to determine the relative priorities of an organisation vis-a-vis its competitors, its vulnerability to outside influences, the factors that support or pose a threat to its existence, and its over all capability to compete in a given industry.

Preparing the Strategic Advantages Profile

Based on the detailed information presented in the OCP, it is possible to prepare a concise chart of a strategic advantage profile. An SAP can also be prepared directly when students analyse cases during classroom learning without making a detailed OCP. A SAP provides "a picture of the more critical areas, which can have a relationship to the strategic posture of the firm in the future".

In Exhibit 7.3, we provide an illustration of an SAP drawn for a hypothetical company in the bicycle industry. The main business of the company is in the sports cycle manufacturing for domestic and exports markets. This example relates to a hypothetical company but the illustration is realistic.

Capability factor	Competitive strengths or weaknesses
1. Finance	↓ High cost of capital; reserves and surplus position unsatisfactory
2. Marketing	→ Fierce competition in industry; company's position secure at present
3. Operations	↑ Plant and machinery in excellent condition; captive sources for parts and components available
4. Personnel	→ Quality of managers and workers comparable with that in competitor companies
5. Information	→ Computerised management information system in the process of development; traditional functions such as payroll and accounting computerized
6. General management	↑ High quality and experienced top management; generally adopts a proactive stance with regard to decision-making

Exhibit 7.3: Strategic Advantage Profile (SAP) for a Bicycle Company

Note: Up arrow indicates strength, down arrow indicates weakness, while horizontal arrow indicates a neutral position.

The SAP presented in Exhibit 7.3 clearly shows the strengths and weaknesses in different functional areas. For instance, the company has to use its strengths in the area of operations and in general management areas. A gap is also indicated in the finance area which has to be overcome if the company has to survive and prosper in a competitive industry like bicycle manufacturing. In marketing, though the competitive position is secure at present, it cannot be said that it will remain so in the future. The SAP indicates that strategists can initiate action to cover the gaps and use the company's strengths in the light of environmental threats and opportunities.

The probable line of action to be adopted for covering the gaps and using the company's strengths in the light of environmental threats and opportunities is found through considering strategic alternatives at the corporate-level and the business level and exercising a strategic choice.

Organisational Appraisal

- The analysis of internal resources has five objectives.
- To outline the role that a company's resources and capabilities play in the formulation of its strategy and to pinpoint their crucial importance in establishing competitive advantage.
- To show how the firm can identify, classify, and explore the characteristics of its base of resources and capabilities
- To develop a set of criteria to analyse the potential of the firm's resources and capabilities to yield long-term profits/returns.
- To identify weaknesses in resources in the context of the external environment and strategy formulated, and to show how strategy is concerned not only with deploying the firm's resources to yield returns over the long term but also with augmenting and strengthening the firm's resources and capabilities.
- To develop a framework for resource analysis that integrates the above themes into a practical guide for the formulation of strategies that build competitive advantage.

The Role of Resource Analysis in Strategy Formulation

It is interesting that during the past two decades, most of the developments in strategy analysis have concentrated upon the industry environment of the firm and its competitive position in relation to rivals. The analysis of industry and competition has been based primarily on concepts and theories of microeconomics and has been closely associated with the works of Michael Porter, the Boston Consulting Group, McKinsey & Co., and the Strategic Planning Institute's linking of market share, quality, and other positional variables to profitability through the PIMS project.

In contrast, strategic analysis of the firm's internal environment is surprisingly underdeveloped. Analysis of the internal environment has, for the most part, been concerned with issues of strategy implementation (partly associated with objective four listed in the introduction above). Internal characteristics of firms such as organisational structure, systems of control and incentives, and top management skill and style, have been viewed primarily as consequences of the strategy adopted and to some extent as constraints upon the range of strategies that can be adopted. Interestingly again, this comparative neglect of internal resources by business strategists contrasts sharply with the approach of military strategy which has always given primacy to resource analysis and followed one underlying principle of war: 'concentration on strength against weakness';

The case for making the resources and capabilities of the firm the foundation of its long-term strategy rests upon two premises:

- *The first concerns the role of resources in defining the identity of the firm. Conventionally, the definition of the business has been in terms of the market served by the firm: 'who are our customers?' and 'which of their needs are we seeking to serve?' But when the external environment is in a state of flux, the market itself is liable to change and the firm itself, defined in terms of its resources and capabilities, may be a much more stable basis on which to define its identity.*

Thus the basis of a resource-based approach to strategy is a definition of the firm, not in terms of the needs it is seeking to satisfy, but in terms of its capabilities. The primary issue for strategy is determining what the firm can do. The second is deciding in which industries and through which types of competitive strategy the firm can best exploit those capabilities.

Evidently this approach is in contrast to that, proposed by Theodore Levitt¹ in his classic article 'Marketing Myopia' in which he has proposed broadening the concept of the market served as the key to successful adjustment. Experience shows, however, that companies basing their strategies on the development and application of specific capabilities have usually shown a remarkable capacity to adjust to external changes. Companies like Honda or 3M are cases in point.

- *The second reason for focusing upon resources as the foundation for an enterprise's strategy is that profits are ultimately a return to the resources owned and controlled by the firm. Profits are usually derived from two sources: the attractiveness of the industry in which the firm is located, and the achievement of competitive advantage over other firms within the industry. If, however, we probe deeper into both competitive advantage and industry attractiveness, we can trace the origins of both sources of profit back to the firm's resources.*

Let us, therefore, consider competitive advantage. The ability to establish a cost advantage over competition rests upon the possession of scale-efficient plant, superior process technology, ownership of low cost sources of raw materials, or locational advantages in relation to low wage labour or proximity to markets. Differentiation advantage is similarly based upon ownership or control over certain resources, brand names, patents, or a wide distribution and service network. Hence the superior profits that a firm gains as a result of competitive advantage over rivals are really returns generated by these resources. Once these resources depreciate, become obsolete, or are replicated by other firms, returns also disappear.

Superior profits associated with attractive industry environments are typically thought of as accruing to the industry

rather than to individual firms. Profitability above the competitive level is typically the result of market power. But what is the source of market power? Contemporary industrial economists regard barriers to entry as its fundamental prerequisite. Barriers to entry have one major basis in economies of scale, in capital equipment, patents, experience brand loyalty, or some other resource that incumbent firms possess but which entrants can acquire only slowly or at a disproportionate expense. In Exhibit 7.4 graphically detail, resources as the basis of superior profitability.

Thus the case for resource analysis rests not only upon the observation that contemporary developments in strategy have overemphasised external analysis to the near exclusion of internal analysis, but also that resources are the fountain from which a firm's profits flow. We provide below the outlines of a resource-based approach to strategy formulation. This comprises three key elements:

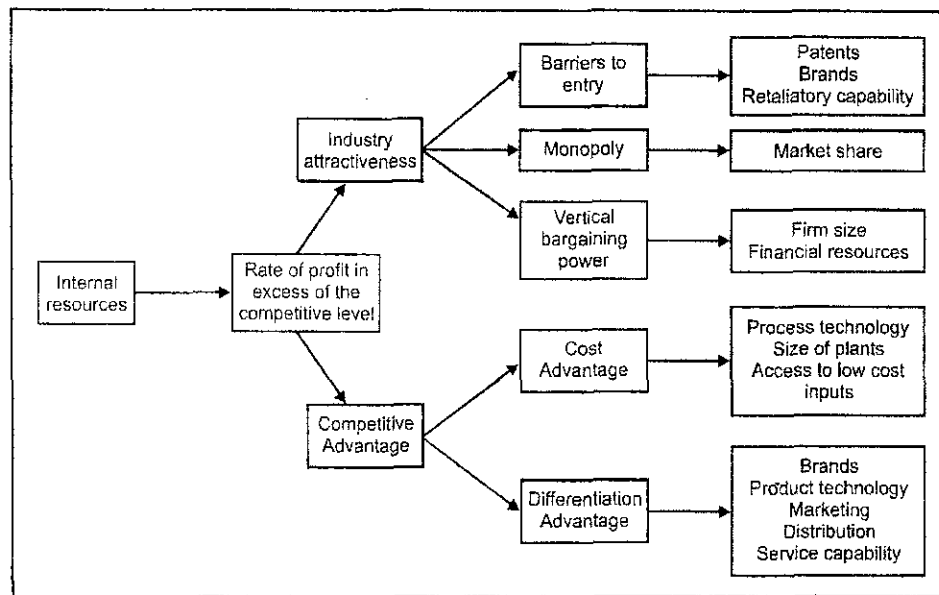


Exhibit 7.4: Resources as the Basis of Superior Profitability

- Selecting a strategy that exploits a company's principal resources and competencies. Successful examples are: IBM and Marks & Spencer (who concentrated on their core competencies of manufacture and software development in the first case and marketing in the second). Failures (the strategies going beyond close linkage with their resource base) are Chrysler which over-extended itself and ITT whose concentration on conglomerate development depended solely on the capability of its CEO (who created no successor) during the seventies.
- Ensuring that the firm's resources are fully employed and its profit potential is exploited to the utmost. Walt Disney's remarkable turnaround between 1984 and 1987 (after four successive years of declining net income and other declining financial indicators) involved very little change in basic strategies.
- Building the company's resource base: Resource analysis is not just about deploying assets, it is crucially concerned with filling current resource gaps and building the company's future resource base. The continuing dominance of IBM & Procter and Gamble in their respective fields of business owes much to these companies' commitment to nurturing talent, augmenting technologies, and adjusting capabilities to fit emerging market trends. This is also evident in the deliberate build up of core competencies in successful companies like NEC, Canon, Honda, 3M.

Taking Stock of the Firm's Resources and Capabilities

Resource analysis takes place at two levels of integration. The basic units of analysis are the individual resources of the firm: items of capital equipment, skills of individual employees, patents, brand names, etc., but to examine how the firm can create competitive advantage, we must look at how groups of resources work together to create capabilities. Exhibit 7.5 shows the relationship between resources, capabilities, and competitive advantage.

Tangible Resources

Tangible resources are the easiest to identify and to evaluate: financial resources and physical assets are identified in the firm's financial statement. At the same time, company financial statements are renowned for their propensity to obscure strategically relevant information and to mis-value assets.

A strategic assessment of tangible resources is directed towards answering two key questions:

- What opportunities exist for economy in the use of finance, inventions, and fixed assets?
- What are the possibilities of employing existing assets more profitably?

The first may involve using fewer tangible resources to support the same level of business, or using existing resources to support a larger volume of business. The success of companies that have pursued growth through acquisitions within mature industries has been due to management's ability to vigorously prune the cash and assets needed to support the turnover of acquired businesses.

The returns to a company's tangible resources can be increased in many ways. Resources can be utilised more productively, they can be transferred to more profitable uses within the company, and finally, can be sold to other companies. The opportunities for breaking up asset-rich, low-profit companies encouraged many company acquisitions during the eighties.

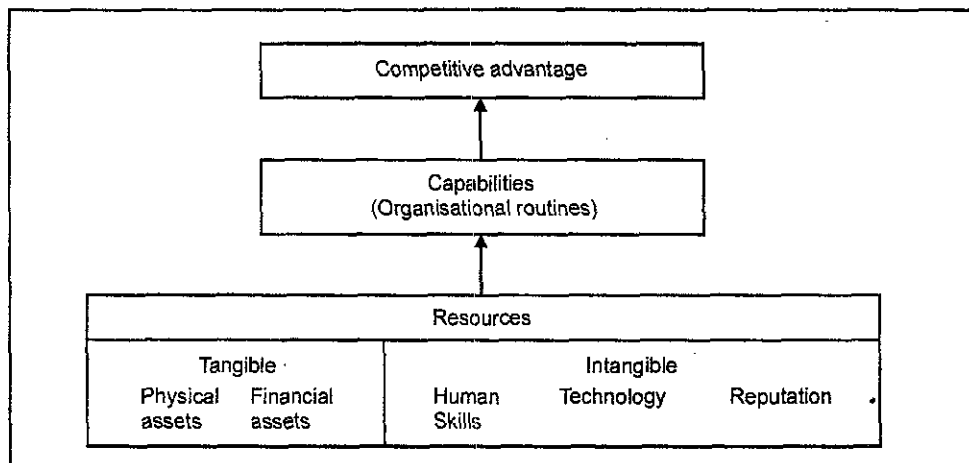


Exhibit 7.5: The Two Levels of Resource Analysis: Resources and Capabilities

Intangible Resources

Over time, working capital, fixed capital, and other tangible assets are becoming less important to the firm, both in value and as a basis for competitive advantage. At the same time, inversely, the value of intangible resources is increasing. However, intangible resources remain invisible to accountants and auditors. Hence, accounting evaluation of net worth increasingly bears little or no relationship to the true value of a firm's resources. To illustrate, the most valuable assets owned by consumer goods firms are likely to be their brand names; yet these either receive no valuation in a company's balance sheet or are valued only when they are acquired. It is perhaps not surprising that

when Nestle acquired the British chocolate manufacturer Rowntree in 1988, the bid price exceeded the book value of Rowntree's assets by over 500 per cent. This is but an indication of the value of Rowntree's brand names such as Kitkat and Quality Street.

To identify and appraise intangible resources, it is useful to distinguish between human and non-human intangibles. While people are clearly tangible, the resources that they offer to the firm are their skills, knowledge, reasoning, and decision-making capabilities which are clear intangibles. In economists' terminology, the productive capability of human beings is referred to as 'human capital'. Identifying and appraising the stock of human capital within a firm is complex and difficult. Individual skills and capabilities can be assessed from their job performance, from their experience, and from their qualifications. These are, however, only an indication of an individual's potential, and in a firm people work together in a way that makes it difficult to directly observe the contribution of the individual to overall corporate performance. Yet, if a company is to develop, to adjust to changing environmental conditions, and to exploit new opportunities, it must have knowledge not only of how its employees perform in their present and past jobs, but of their repertoire of skills and abilities. Dave Ulrich of the University of Michigan points to the role of a human resource information system as a valuable tool for sustaining a company's competitive advantage.

While intangible resources receive scant recognition from accountants, their value is being increasingly recognised by the stock market, as evident from the significantly high ratio of stock prices to book values of successful companies. Indeed, any evaluation of this ratio in the stock market will show that two types of companies dominate such a list: those with valuable technical resources (notably pharmaceutical companies, an industry where patents are particularly effective), and companies with very strong brand names (especially in nondurable goods).

Hofer has identified five types of resources: financial, physical, human, technological, and organisational. Exhibit 7.6 illustrates and slightly modifies his classification of resource types, and points to their principal characteristics and key indicators.

Resource Audit

The strategic capability of the organisation is built largely around those activities that add value to a product. Other activities are also useful and necessary but they are not the ones through which the organisation sustains its distinctive production/service values.

In this context, the relative roles of primary and support activities of the organization need to be appreciated. It will be obvious that resources contributing to the value system of the organization will be dispersed amongst various primary activities. The role of support activities would be to marshal them and use them effectively and efficiently. The checklist in Exhibit 7.7 would provide broad coverage of the resources to be audited.

It will be noticed that within an activity different types of resources are identified:

Physical resources: Physical resource assessment should go way beyond mere listing. It should indicate the nature of these resources, their age, condition, capability, location, and, where relevant, specialty.

Human resources: An analysis of human resources must examine a number of relevant questions. An assessment of the number and types of different skills within the organization is undoubtedly important. Equally important, however, are questions such as adaptability (to different external circumstances). There is also the question of retrenchment, retraining, and relocation under conditions of economic distress and flexibility, as also of location, often for skilled operatives in high wage countries in multinational companies.

Thus consider the case of Japanese multinationals. In the context of the continuously rising value of the yen, it would soon become unavoidable for many such Japanese companies to move their manufacturing facilities to lower wage

countries to maintain competitiveness. Some of their skilled operators would also have to go along, particularly in the initial stages. The ready acceptance by employees of such relocation is an important consideration in human relations.

Resource (s)	Principal Characteristics	Key Indicators
Financial	The firm's borrowing capacity and its internal fund generation determine its investment capacity and its cyclical resilience.	Debt-equity ratio. Ratio of net cash to capital expenditure. Credit rating
Physical	The size, location, technical sophistication, and flexibility of plant and equipment, location and alternative uses for land and buildings; resources of raw materials constrain the firm's set of production possibilities and determine its potential for cost and quality advantage.	Educational, technical, and professional qualifications of employees. Pay rates in relation to industry average. Record of labour disputes. Rate of employee turnover.
Human	The training and expertise of employees determine the skills available to the firm. The adaptability of employees determines the strategic flexibility of the firm. The commitment and loyalty of employees determine the firm's ability to maintain competitive advantage.	Resale values of fixed assets, vintage of capital equipment. Scale of plants. Alternative uses of fixed assets.
Technological	Stock of technology, including proprietary technology (patents, copyrights, trade secrets), and expertise in its application of know-how. Resources for innovation, research facilities, technical and scientific employees.	Number and significance of patents. Revenue from patent licenses. R&D staff as a percentage of total employment.
Reputation	Reputation with customers, through the ownership of brands, established relationship with customers, the association of the firm's products with quality, reliability etc. The reputation of the company with the suppliers of components, finance, labour resources, and other inputs.	Brand recognition. Price premium user competing brands. Percentage of repeat purchases. Objective measures of product performance, level and consistency of company performance

Exhibit 7.6: Classifying and Appraising the Firm's Resources

Primary Activities					
Support activities	Inbound logistics	Operations	Outbound logistics	Marketing and sales	Service
Procurement	Transport Warehousing Capital	Machines Consumables	Transport Warehousing	Product/Service Patents/Licenses Brand names Market research	Franchise Credit facilities
Technology development	Know-how. Design Technology. Transfer (in)	Process development	Shipments	Networks of contacts Information systems	Fault diagnosis
Human resource development	Recruitment Supplier Vetting Shareholders Creditors relation Image in city	Team spirit Job satisfaction Subcontractors	Subcontractors	Agents Sales force Distributors. Merchandisers goodwill	Maintenance staff
Management systems	Purchasing systems Vehicle Scheduling Material handling	Production Planning Quality control Cash management Stock control Facilities layout	Delivery scheduling	Order processing Debtor control	Customer service systems

Exhibit 7.7: A Checklist for Resource Auditing

Financial resources: This would include the sources and uses of money within the value chain, such as obtaining capital, managing cash, the control of debtors and creditors, and management of relationships with suppliers of money (shareholders, bankers, concepts of convertibility, creditworthiness, etc.).

In resource analysis, the importance of intangibles should never be overlooked. In some businesses, particularly services such as solicitors, retail shops, and the catering industry, goodwill could represent the major asset of the company and may stem from brand names, good contacts, company image, and many other sources. Even in others, where it may not constitute a major asset, it is still significant. Thus where a company adopts the strategy of differentiation to gain competitive advantage, a considerable portion of the value associated with differentiation is perceived difference, such perception being largely subjective and somewhat intangible in nature. Similarly, where quality is a major plank of the strategy adopted, one of its major components is perceived quality, once again based on intangibles.

Resource Utilisation

It is evident that an organisation's resources have practically no value unless organised into *systems*, to ensure that they are utilised to produce goods, products, or services that are valued by the final consumer/user. There are various ways of measuring resource utilisation; some are mentioned below.

Capacity Fill

It is often a prime measure of efficiency of organisations whose major costs are overheads. This is particularly important for those industries where the additional or marginal cost of additional occupancy of unoccupied capacity is extremely small. Examples would be transport industries and hotels. It may also be noted that capacity fill often becomes the major criterion for cost competitiveness of such organisations.

Working Capital Utilisation

Working capital utilisation is a good indicator of the way in which the financial resources of the company are used strategically. It is readily realized that operating at a low level of working capital involves considerable risk; on the other hand, having too much capital is patently inefficient. It is therefore important to achieve a balance between these extremes. An assessment of how well this balance has been achieved will be a measure of the efficiency of working capital utilisation. This balance is sometimes changed by factoring certain aspects such as debtors in return for cash. This, in effect, means redefining the boundaries of the organisation's value chain to maintain efficiency.

Production Systems

An essential precondition of the ability to assess the efficiency of the production system of a company is to have a thorough and clear understanding of the various aspects of a company's production system, such as job design, layout, and materials flow. It may be found, for example, that excessive costs have been incurred through unnecessary handling and transportation of materials during manufacture, or that the company can take advantage of new operational methods. In other words, job simplification, job elimination, methods improvement are distinct possibilities. Instances of the application of these industrial engineering concepts and consequent improvement in efficiency with corresponding enhancement of cost-competitiveness are too numerous to require any specific illustration.

Effectiveness

A complete understanding of a company's use of resources also requires an analysis of the *effectiveness* with which these resources have been used. The effectiveness of an organisation can be critically influenced by the ability to get all parts of the value chain working in harmony—including those key activities that are within the value chains of suppliers, channels, or customers. This is a key task of management and is largely concerned with development and sustenance of common attitudes and values amongst all those in the value chain so that people see the purpose of the products/services in similar ways and have a common view on which activities are critical to success. It is really the differences in attitudes and perceptions on these issues which are often the root causes of misunderstandings. Some of them are now discussed.

Use of People

There are many situations where people may be used ineffectively. For instance, an engineering design team may be designing for the lowest cost whilst the organisation is competing on uniqueness of product. Taking the example to a degree of refinement, there may be misunderstanding on the concept of uniqueness itself. Thus the design staff may be designing for durability, whereas the organisation's perception of the "market choice is reliability.

Use of Capital

An analysis of a company's long-term funding (capital structure) may provide useful insights. A company may be foregoing the opportunity of additional long-term funds (loans or share issues) and, in consequence, facing difficulty in carrying out its necessary investment programmes. Sometimes the opposite is true, when a company may be too highly geared for the realities of the markets in which it is operating. Many companies have found that when 'general levels of profitability are low and interest rates high, the conventional wisdom of gearing to improve profitability is impossible to achieve. Organisations that have grown by a series of mergers and takeovers are particularly astute at putting together packages of finance (money and share options) that are regarded as attractive by shareholders of the organisations being taken over.

Use of Marketing and Distribution Resources

The effectiveness with which a sales force is being used might be judged by assessing the volume of sales that each salesperson produces. However, expenditure on other items like advertising or distribution may be more difficult to assess. Companies often use rules of thumb like percentage of turnover spent on advertising, or might sometimes attempt more rigorous and expensive analysis such as advertising effectiveness research. A crucial judgement when analysing the value chain is whether the marketing effort could have been delivered more effectively in a different way—for example would appointing sales agents have been better than having an in-house sales force?

Use of Research Knowledge

An assessment of how effectively research knowledge is used is equally problematic. Tangible measures are available, such as the number of product and process changes developed internally or the competitive advantage that has been gained from technical improvements resulting in better quality or lower cost. Companies are increasingly trying to cope with their worries about underutilisation of the R&D resource by providing better links with the commercial function and improving monitoring and control arrangements. There is often a tendency towards *technology transfers* rather than in-house R&D development. This has some obvious advantages, such as time saved and non-commitment of internal resources. The disadvantages should not be lost sight of either; the obvious one being that *technology transfer is a static process and which it may include the minutest details, it would still be missing the essential element.* Further, the R&D department would be ill-equipped to carry out any improvement, since it would not know the process and would not be in a position to comment on it.

Use of Production Systems

Poor utilisation of resources may result from the choice of an inappropriate system of production. This, in effect, means that the production system should be designed as one appropriate for the volume it is expected to handle, and the correctness of that estimated value is of critical concern.

A production system needs to be geared to the basis on which the organisation competes. Where cost competitiveness is crucial, highly integrated production systems may be essential. However, a more flexible system will be required if the quality of service (e.g. delivery time) is the principal competitive weapon.

Exploitation of Intangible Assets

In case of intangible assets such as image, brand name, and market information, their exploitation is a measure of effectiveness.

Exhibit 7.8 gives the measure of efficiency and effectiveness for different resources.

Control of Resources

It is not enough to look at resource audit and utilisation; it is necessary to ensure that resources are controlled properly according to the strategic intent. Otherwise, there would be situations where good quality resources have been deployed the right way and used efficiently, but still performance is poor as resources are poorly controlled. Exhibit 7.9 lists some aspects of resource control.

The ways in which linkages within the value chain and with the value chains of supplies, channels, or customers are controlled can also be important. Often financial control systems of an organization tend to discourage such linkages because they do not fit the compartmentalised concept of resource control. Some important aspects of resource control are discussed below.

Control of Key Personnel

Often key creative and professional people, while essential for the efficient functioning of organisations, are a bad fit in the organisational structure and culture because their personal concepts of their jobs are somewhat different from those of the company. In such situations, it may be preferable to have these people outside the organisation (as advisors or consultants) whilst continuing to be key resources within the value chain.

Resource	Efficiency	Effectiveness
Physical resources	Capacity fill	Match between production/marketing resources and nature of work.
Buildings	Capacity fill, unit costs.	
Plant & machinery	Job design, layout, materials flow	
Financial	Profitability, use of working capital	Capital structure
Materials	Yield	Suitability of materials.
Products	Damage (e.g. in transit)	Match between product and market needs
Marketing and distribution	Sales per area	Choice of channels.
	Sales per outlet	Choice of advertising method.
Human resources	Labour productivity	Allocation of jobs to people.
	Relative size of departments	Duplication of efforts.
Intangibles		Exploitation of image, brand name market information, research knowledge, etc. Consumer complaints level.

Exhibit 7.8: Some Measures of Resource Utilisation

Resource Area	Typical Control to Investigate
<i>Physical resources</i>	
Buildings	Security, maintenance.
Plant & machinery	Production control; maintenance system
Financial	Costing systems, Budgets, Investment appraisal
Materials	Supplier Control (quantity, quality, and cost) Control of stock
Products	Stock control, quality control, losses (e.g. thefts)
<i>Human resources</i>	
	Control of key personnel
	Leadership
	Working agreements
	Control of outlets (e.g. distribution)
	Control of image (e.g. public relations)
<i>Intangibles</i>	
	Industrial relations celiac
	Control of vital information

Exhibit 7.9: Aspects of Resource Control

Costing

This is an area of particular importance and significance for small, fast-growing organisations and yet this is where they often fail. The management knows what resources are needed to establish the company in the market and how to deploy these to good effect. It is, however, unaware of how its method of operation will influence costs and

revenue, and hence the profitability of the company. It is important to emphasize that costing is a means of resource control, not obstructing resource utilisation. Often, in organisations, there is confusion between cost effectiveness and cost minimisation. Whereas cost effectiveness is invariably desirable, cost minimisation may lead to blind cost pruning, frequently resulting in a downward spiral, leading to a product/service that is valued less by consumers/buyers/users, creating a fall in demand, a worsening cost structure, and so on. This is where a proper appreciation of costing as a resource control measure comes of age.

Quality of Materials

In most industries, the quality of the finished product is highly dependent on the quality of certain key materials and components that are bought in. Establishing strict quality control measures on these materials (and components) is therefore essential to ensure the quality of the final product. In the context of the value chain there are different ways in which this might be achieved; for instance by establishing rigid quality specifications; and subsequent inspection of incoming materials, by inspecting the suppliers' quality control systems or by inspection of incoming materials. The relative cost and effectiveness of the alternatives is an important consideration. In many cases, it becomes necessary to 'roll-back' the control of quality to the supplier. One can conceive the supplier-company value chain linkage through joint or combined research for developing 'suitable' quality material and the consequent quality control procedures.

Marketing Outlets

Many manufacturers fail to exert sufficient control over the way in which their outlets present and sell their products. Retail outlets often sell 5000 to 10,000 different products, including many that directly compete with one another. Monitoring and controlling the marketing efforts of outlets is important, but often difficult. Again, different approaches are possible ranging from the ownership of outlets (i.e. bringing distribution into the organisation's own value chain), the Bata shoe store chain in India is an example; appointment of approved dealers; the provision of customer training; and the use of merchandising teams.

Stock and Production Control

There may be occasions when a company's poor performance can be due to poor control of stock or the system of production. Poor stock control means tied up capital and accrued interest on this with consequent interest burden. A good stock control system, by controlling inventory levels, can substantially reduce working capital requirements resulting in substantial benefits.

Even if the raw materials or finished goods inventory control procedure may be satisfactory, poor production control systems may result in poor delivery record and high 'buffer' stock between the various steps of production. This is equally harmful and demands installation of proper production control system.

Control of Leakage

Most companies face this problem. Retailers are particularly vulnerable. Organisations face a real dilemma since the introduction of more stringent controls and checks could be counterproductive in reducing the 'value' of the service in the eyes of consumers.

Control of Intangibles

The company's ability to control its image through its public relations activities is one example. The 'industrial relations' record can indicate how well 'team spirit' or 'organisational culture' are controlled. In some cases, the control of vital information that may be of commercial benefit to competitors would be particularly important to monitor.

Financial Analysis

Financial analysis is useful at all stages of resource analysis, and not only as part of value analysis. For example, the forecasting of the cash requirements of different activities is an important measure of how well an organization's resources are balanced (portfolio analysis). Equally, financial measures such as profitability, gearing, or liquidity are used to compare the performance of a company with its competitors as a means of analysing that company's resource position.

The key value activities change over time. Key financial measures to monitor will change accordingly. Thus, as a new product launch goes through introduction, growth, and decline, the key measures shift through *sales volume*, *profit/unit*, and *cash flow*. Exhibit 7.10 provides some financial ratios in relation to a company's strategic resources and capabilities.

Financial Ratio	Used to Assess
<i>Return on capital</i>	Overall measure of Performance
Cost structure	
Sales profitability	Sales performance.
Gross margin	Direct costs.
Sales expenses	1. Indirect cost
Overheads	2. Value of expenditure
Labour	1. Labour productivity
	2. Relation to 'value'
Materials	1. Purchasing policies
	2. Quality of materials
	3. Relation to 'value'
Dividends	Power of shareholders
Interest	Capital structure
Asset turnover	
Fixed assets	Capital intensity
Stock	1. Cash tied up
	2. Delivery performance
	3. Risk of write-offs
Debtors	1. Cash tied up
	2. Use of credit
	3. Risk of bad debts
Creditors	Choice of suppliers
<i>Liquidity</i>	Short-term risk
<i>Capital structure</i>	1. Long-term risk
<i>(gearing)</i>	2. Using available resources

Exhibit 7.10: Financial Ratio and Resource Analysis

Comparative Analysis

To adequately comprehend the strategic capability of an organisation, it is useful to carry out a comparative analysis, with (i) itself in the past to see how the resource basis has shifted over time, (ii) other competitive organisations, and (iii) industry norms.

Historical Analysis

Historical analysis looks at the deployment of the resources of a business in comparison with previous years in order to identify any significant changes in the overall levels of resources. Typically, measures like sales-capital ratio, sales-employees ratio are used, as well as identification of any significant variations in the proportions of resources devoted to different activities. Such analysis appears straightforward, but in a tabulated form often discloses drifts normally not visible. Thus a company, basically in manufacturing and retailing its own products, finding the retail market relatively favourable may gradually emphasise on retailing to such a degree as to drift away from the traditional base of manufacturing. It is only when resource utilisation is compared across the years that the drift becomes apparent. It is now for the company to reassess where its major thrust of business should lie in the future. In other words, the company has gradually redefined the boundaries of its value chain over time.

Comparison with Industry Norms

The historical analysis discussed above is upgraded considerably by additional comparison with the industry as a whole. It helps to put the company's resources and performance in perspective and provides the company with a broad idea about its competitive position in relation to the industry.

The dangers of such comparison with the industry as a whole are, however, several.

- i. It may overlook the fact that the industry as a whole is doing badly and is losing out competitively to other industries and other countries with better resources and with the capability to satisfy customer needs better.
- ii. The industry norms, averaging out companies with different strategies, often average out different things and in the process hide more than they reveal. Thus, for instance, comparing labour costs; for companies with cost competitiveness as the critical strategy, labour cost should necessarily be low, whereas for companies with differentiation as the critical strategy, labour cost, is no longer critical and can easily be somewhat higher, so long as it is more than compensated by the added value gained by differentiation, duly reflected in higher price.

What is more important, therefore, is to compare similar *value activities* between organisations if the strategic context is not forgotten. This would, however, mean keeping detailed profiles of competitors' resources, and may prove very difficult and expensive.

We now discuss certain concepts related to the analysis of internal resources.

The Experience Curve

The concept of the experience curve was propounded by the Boston Consulting Group, as the end result of studies of company performances showing a direct and consistent relationship between aggregate growth in volume of production and declining cost of production. This relationship resembles that shown in Exhibit 7.11.

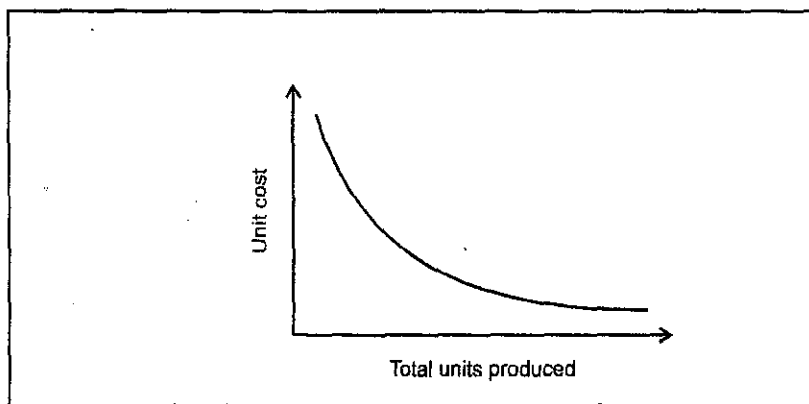


Exhibit 7.11: The Experience Curve

In analysing the reasons contributing to the shape of the curve, the major reasons identified by the BCG are the following:

The learning function: Anyone doing a job learns to do it better over time and given increased experience. Labour cost should, in fact, decline by about 10 to 15 per cent every time cumulative experience doubles.

Specialisation: As scale of production increases, so it becomes possible to split jobs into more and more specialist ones. 'Doing half as much but twice as often' equals the same amount of effort but twice the experience with the task.

Scale: The capital costs required to finance additional capacity diminish as that capacity grows.

Cost is thus, in general, a function of experience. It is also a function of volume and particularly of market share, specially when the product is competing in a definable relevant market segment.

There are, however, some significant reservations expressed about the value of experience curve ideas. Some of the conventional reasons are the following:

- i. Some of the key variables such as market growth and share are not always easy to be precise about.
- ii. There is risk that managers interpret the conclusions too simplistically, e.g. by failing to recognise the opportunities afforded by market segmentation and/or product differentiation.

A more profound and up-to-date objection would, however, be that the ever increasing trend of technological innovation would tend to establish rapid obsolescence of yesterday's technology. In consequence, a company, whose products may claim reduced labour cost achieved through the impact of the experience curve, may find itself in competition with another company just commencing production. Whereas, as the normal consequences of the experience curve, the old company should-enjoy a cost advantage, this would be totally negated through faster and better machines.

Assessing the Balance of Resources

While value chain analysis is undoubtedly important, there is an additional resource issue that is of equal and complementary importance: namely the extent to which the organisation's resources are balanced overall. Three important aspects of such analysis are:

- The extent to which the various activities and resources of an organisation complement one another. *Portfolio analysis* is particularly useful here.
- The degree of balance of the *people* within the organisation both in terms of individual skills and personality types

- Whether the *degree of flexibility* in the organisation's resources is appropriate for the level of uncertainty in the environment and the degree of risk the company is prepared to take.

Portfolio Analysis

Let us consider the market share, market growth rate BCG matrix together with the concept of the experience curve discussed above. The experience curve underlines the importance of the relationship between market dominance and profitability. It will be evident that there is not much sense in market dominance unless the market is in a growth stage. Evidently, all competitors would be trying to gain in market shares, competition would be fierce, the investment and resource deployment requirement higher, and profitability would be low. Cash generation would perhaps even be negative. And yet, in expectation of a future high profit (and perhaps cash generation), resource deployment and investment would have to be made. Evidently, that cash would have to be generated by some other product/market segment. This is how the BCG matrix suggests the model for product portfolio or the growth share matrix as a tool by which to consider product strategy.

Portfolio analysis is particularly useful inasmuch as it raises some important questions about resources. For example:

- Whether the mix of products, services or businesses is balanced across the organisation. The idea of a portfolio of interests emphasises the importance of having areas of activity that provide security of funds (cash cows) and others that provide for the future of the business, (star and question mark).
- Drucker has long emphasised the importance of reviewing activities to ensure that the appropriate amount of management and physical and financial resources are being allocated to the activities, that management is not providing excessive resources to 'dogs' while starving 'question marks' and thus reducing the chances of turning them into 'stars'.
- Whether the balance of a company's products/markets matches the resources available to the company. If a company is particularly good at development and design this may not match the analysis of product/market position which indicates a predominance of mature products in a static market. This may suggest the need to move funds from the development area into a greater emphasis on promotion or market development.

Skills Analysis

Organisations must possess the necessary balance of skills needed to run a business successfully. Companies need the capability to manage their production and marketing systems as well as control the financial and personnel aspects properly. There is another aspect to the balance of human resources, namely the extent to which teams contain an adequate balance of personality types to operate effectively. Some of the common personality types needed within an effective team are identified in Exhibit 7.12.

Flexibility Analysis

Another important aspect of organisational resources is the extent to which they are flexible and adaptable. It is also important to assess how far this flexibility is balanced with the uncertainty faced by the organisation. Since this uncertainty is wholly concerned with the external environment and disturbances in it, flexibility has no meaning without an understanding of the uncertainty involved or apprehended. Thus flexibility involves resources and their utilisation in the uncertainty of the external environment in the content of the management strategy specifically adopted with an end object in view.

Chairman/team leader	Company worker
Stable, dominant, extrovert. Concentrates on objectives. Does not originate ideas. Focuses people on what they do best.	Stable, controlled. Practical organizer. Can be inflexible but likely to adapt to established systems. Not an innovator.
Plant Manager Dominant, high IQ, introvert. A 'scattered of seeds'; originates ideas. Misses out on details. Trustful but easily offended.	Monitor evaluator High IQ, stable, introvert. Measured analyses not innovation. Unambitious and lacking enthusiasm. Solid, dependable.
Resource investigator Stable, dominant, extrovert, Sociable. Contacts with outside world. Salesperson/diplomat/liaison officer. Not an original thinker.	Team worker Stable, extrovert, low dominance. Concerned with Individuals' needs Builds on others' ideas. Cools things down.
Shaper Anxious, dominant, extrovert, emotional, impulsive. Quick to challenge and respond to challenge. Unites ideas, objectives and possibilities. Competitive, Intolerant of wooliness and vagueness.	Finisher Anxious, introvert. Worries over what will go wrong. Permanent sense of urgency. Preoccupied with order. Concerned with 'following through'.

Exhibit 7.12: Personality Types for an Effective Team

Flexibility analysis is usually not a sophisticated exercise. Often it is a simple listing of the major areas of uncertainty and the extent to which the company's resources are geared to cope with each of these. An example is shown in Exhibit 7.13.

Value Chain Analysis

The concept of value relates to how the ultimate consumer/user views the organisation's products/source in relation to competitive offerings. An analysis of resources must be undertaken in a way that establishes how such competitive differences are achieved throughout the value chain. Many of the value activities will be performed outside the organisation (e.g. by suppliers, channels or customers). It is essential that the organisation's own *value chain* is seen in this wider context.

The *linkages* and relationships between various activities are often the basis on which competitive advantage is achieved. This also applies to linkages of the value chain of an organisation with those of its suppliers, channels, and customers.

Major areas of Uncertainty	Flexibility Required	Actual (at present)	Comments
Demand for Product A.	Capacity (possibility +20 per cent) or stocks	Overtime could cover. Low	Probably OK
Price of raw materials from present supplier.	New supplies. New materials.	None known at present. Production cannot cope.	Problem area Seek information on new suppliers.
Long-term loan may not be renewed next year.	Other sources of Capital.	Good image on stock market.	New share issue looks favourable.
Major customer may go bankrupt.	Replacement customer	No leads	Sound out potential customer.
Chief design engineer may retire.	Design capability for products presently in development.	Deputy not suitable Chief may agree to part time 'consultancy' arrangements.	Tracing and/ or recruitment needs urgent attention.

Exhibit 7.13: Flexibility Analysis

Exhibit 7.14 and 7.15 show the value system and an illustration of an organisation's value chain. Exhibit 7.15 a schematic representation of the value chain showing its constituent parts. The *primary activities* of the organisation are grouped into five principal areas: inbound logistics, operations, outbound logistics, marketing and sales, and lastly service.

Inbound logistics: are the activities concerned with receiving, storing, and distributing inputs to the product/ service. This includes materials handling, stock control, transport, etc.

Operations: transform these various inputs into the final product or service. For example, this would include machining, packaging, assembly, and testing.

Outbound logistics: collect, store, and distribute the product to customers. For tangible products this could be warehousing, materials handling, and transport. In case of services, it may be more concerned with arrangements for bringing customers to the service if it is a fixed location (e.g. sports events).

Marketing and sales: provide the menus whereby customers/users are made aware of the product/service, etc., and on completion of sales take in hand the requirements concerned with collection of dues, data registration, etc. In utility services, the communication networks which help users access a particular service are often important.

Service: all the activities that enhance or maintain the value of a product/service such as installation, repair, training, spares, etc.

Each of these groups of primary activities is linked to support activities. These can be divided into four areas.

Procurement: refers to the process of acquisition of various resource inputs that go into primary activities (not to resources themselves). As such, it occurs in many parts of the organisation.

Technology development: all value activities have a 'technology' even if it is simply 'know-how'. The key technologies may be concerned with the product (e.g. R&D, product design), or with process (e.g. process development), or with a particular resource (e.g. raw materials improvement).

Human resource management: high quality training and development, recruitment of the right people, and appropriate reward systems that motivate people.

Firm's infrastructure: support from senior executives in customer relations, investment in suitable physical facilities to improve working conditions, and investment in carefully designed information technology systems.

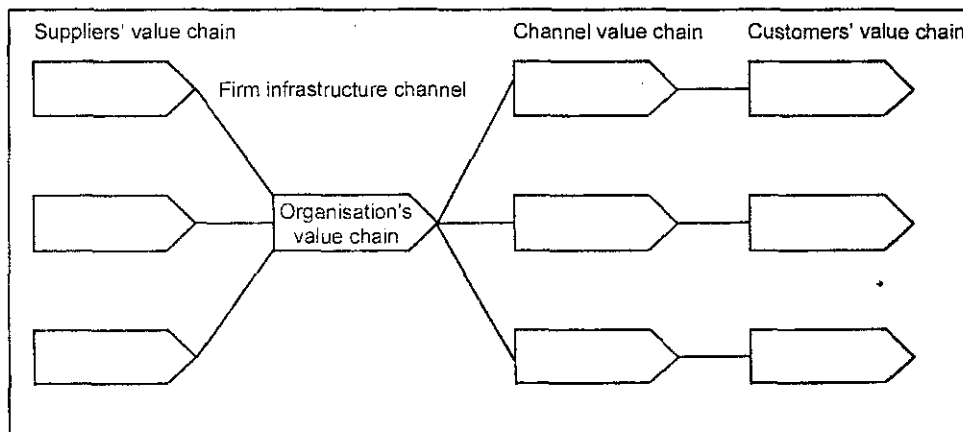


Exhibit 7.14: The Value System

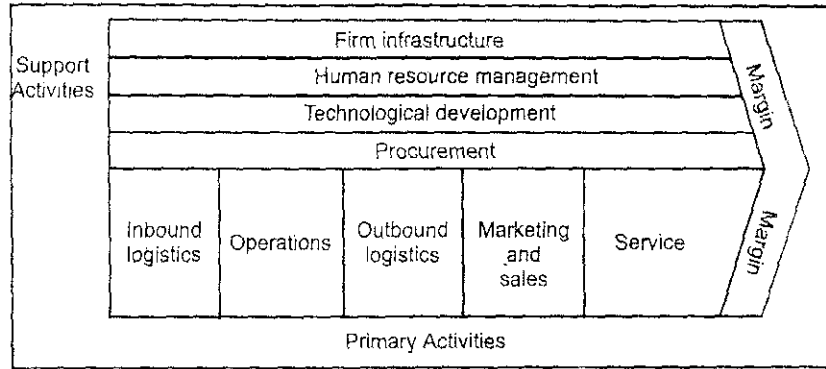
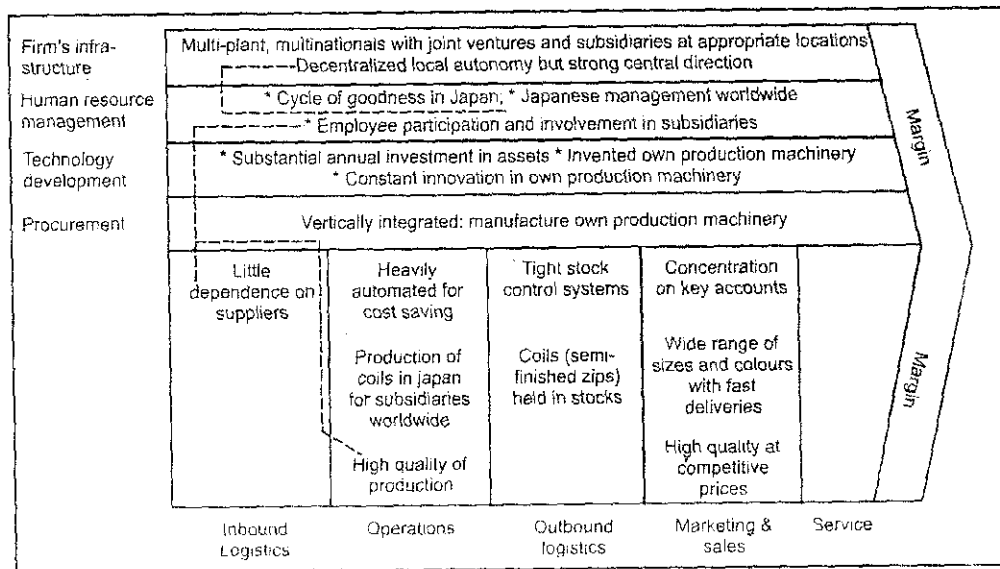


Exhibit 7.15: The Value Chain

It would seem evident that in searching for the most appropriate means, of differentiating for competitive advantage it is important to look at which activities are the most essential as far as consumers and customers are concerned, and to isolate the key success factors. It is a search for opportunities to be different from competitors in ways that matter, and through this the creation of a superior competitive position. It is perhaps best illustrated by the case of YKK, the Japanese Zip manufacturer, the world market leader. Their value chain is shown in Exhibit 7.16. The idea behind their use of a value chain for the creation of both cost leadership and substantial differentiation might be illustrated as in Exhibit 7.17. The essential components of the strategy illustrated in Exhibit 7.16 are,

- heavily automated plants;
- production of coils in Japan for world supply;
- little dependence on supplies;
- competitive pricing of finished products;
- vertical information design and manufacture of own machinery;
- wide range of colours and sizes.



The broken lines (-----) illustrate linkages

Exhibit 7.16. YKK's Competitive Advantage and the Value Chain

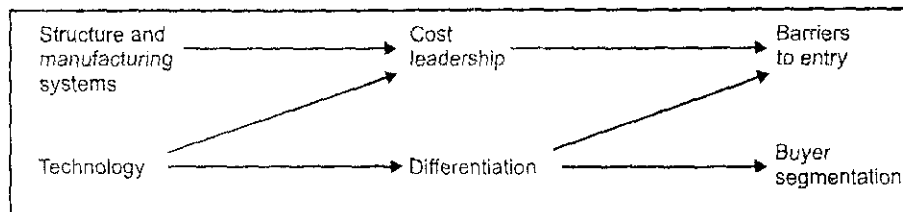


Exhibit 7.17: Use of Value Chain

it is only at this stage that a sensible assessment can be made of the major strengths and weaknesses of an organisation and an indication of their strategic importance derived. It is then that resource analysis begins to be useful as a basis against which to judge future courses of action. Strengths and weaknesses can be identified under readily identifiable heads. An illustrative list would be:

Strengths	Weaknesses
● Company/brand name	● Status of market
● Market share	● Territorial performances.
● Advertising effectiveness circles.	● Credibility in business
● Financial management.	● Plant location
● New products launched	● Functional capabilities, etc.
● New product under development, etc.	
● Technology	
● Saleability of divisions for ready cash generation	
● Industrial relations, etc.	

Each of the strengths could in a particular case be a weakness or vice versa.

There are several analyses or assessments that can be made. In this context, SWOT analysis has already been referred to earlier. This can be a very useful way of summarizing many of the previous analyses and combining them with key issues from environmental analysis. One of the benefits of using *value chain* analysis is that it should help avoid some of the common pitfalls of SWOT analysis. In particular, the analysis must be clear on

- a. the reasons why particular activities or resources are identified as strengths or weaknesses;
- b. that the value activities are more important than resources per se, i.e. it is the use to which resources are being put that is critical;
- c. that the *linkages* between various value activities are likely to be key strengths (or weaknesses) of the organization. This would include linkages with value chains of suppliers, channels, and customers.

A strength and weakness analysis can be particularly valuable if it incorporates a comparison with competitors. This can be done by using the concept of *distinctive competence*. Distinctive competence is concerned with identification of those particular strengths that give the company an edge over its competitors and those areas of particular weakness that are to be avoided. This may require a parallel analysis of the competitor's resources.

A Functional Approach

Strategic internal factors are a firm's basic capabilities, limitations, and characteristics. Thus Exhibit 7.18 lists typical factors, broken along functional lines, some of which would be the focus of internal analysis in most business firms. To develop or revise a strategy, managers would identify the few factors on which success will most likely depend. These factors are the *key strategic factors*.

Strategists examine past performance to isolate key internal contributors to favourable (or unfavourable) results. The same examination and questions can be applied to a firm's current situation, with particular emphasis on changes in the importance of key dimensions over time. Analysis of past trends of sales, costs and profitability is also of major importance in identifying strategic internal factors. Identification of strategic factors also requires an external focus. When a strategist isolates key internal factors through analysis of past and present performance, industry conditions/trends and comparison with competitors also provide insights. Changing industry conditions can lead to the need to re-examine internal strengths and weaknesses in the light of newly emerging determinants of success in the industry. Furthermore, strategic internal factors are often chosen for in-depth evaluation because firms are contemplating expansion of products or markets, diversification, and so forth. Clearly scrutinizing the industry under consideration and current competitors is a key means of identifying strategic factors if a firm is evaluating a move into unfamiliar markets.

Key Internal Factors

Marketing

- Firm's products/services: breadth of product line.
- Concentration of sales in a few products or to a few customers.
- Ability to gather needed information about markets.
- Market share or sub-market shares.
- Product/service mix and expansion potential: life cycle of key products
- Services: profit/sales balance in product/service.
- Channels of distribution: number, coverage and control.
- Effective sales organisation: knowledge of customer needs.
- Product/service image, reputation, and quality.
- Pricing strategy and pricing flexibility.
- Procedures for digesting market feedback and developing new products, services, or markets.
- After sales service and follow-up.
- Goodwill/brand loyalty.

Finance and Accounting

- Ability to raise short-term capital.
- Ability to raise long-term capital: debt/equity.
- Corporate level resources (multi-business firm).
- Cost of capital in relation to industry and competitors.
- Tax considerations.
- Relations with owners, investors, and stockholders.
- Leverage position: capacity to utilize alternative financial strategies such as lease, or sale and lease back.
- Cost of entry and barriers to entry.
- Price-earnings ratio.
- Working capital: flexibility of capital structure.
- Effective cost control: ability to reduce cost.
- Financial size.
- Efficient and effective accounting system for cost, budget and profit planning.*

Production/Operation/Technical

- Raw material cost and availability; supplier relationship.
- Inventory control systems; inventory turnover.
- Location of facilities; layout and utilization of facilities.
- Economies of scale.
- Technical efficiency of facilities and utilization of capacity.
- Effective use of subcontracting.
- Degree of vertical integration; value added and profit margin.
- Efficiency and cost-benefit of equipment.
- Effective operation control procedures: design, scheduling, purchasing, quality control, and efficiency.
- Costs and technological competencies in relation to industry and competitors.
- Research and development/technology/innovation.
- Patents, trademarks, and similar legal protection.

Personnel

- Management personnel.

Orma

<p>Employees' skill and morale.</p> <p>Labour relations costs in comparison to industry and competition.</p> <p>Efficient and effective personnel policies.</p> <p>Effective use of incentives to motivate performance.</p> <p>Ability to level peaks and valleys of employment.</p> <p>Employee turnover and absenteeism.</p> <p>Specialized skills.</p> <p>Experience.</p> <p>Organisation of general management</p> <p>Organisational structure.</p> <p>Firm's image and prestige.</p> <p>Firm's record of achieving objectives.</p> <p>Organisation of communication system.</p> <p>Overall organisational control system (effectiveness and utilization).</p> <p>Organisational climate: culture.</p> <p>Use of systematic procedures and techniques in decision-making.</p> <p>Top management skills, capabilities, and interest.</p> <p>Strategic planning system</p> <p>Inter-organisational synergy (multi-business firm).</p>

Exhibit 7.18: Internal Factors: Potential Strengths and Weaknesses.

Historical Analysis Revisited, Stages in Product/ Market Evolution

The requirements for success in product/market segments evolve and change over time. In consequence, strategists can use these changing patterns associated with different stages in product/market evolution as a framework for identification and evaluation of the firm's strengths and weaknesses.

Exhibit 7.19 depicts four general stages of product/market evolution and the typical changes in functional capabilities often associated with business success at each stage. The early development of a product/market, for example, entails minimal growth in sales, major R&D emphasis, rapid technological change in the product, operating losses, and a need for sufficient resources or slack to support a temporarily unprofitable operation. Success at this stage may be associated with technical skill, with being first in new markets, or with having a marketing advantage that creates widespread awareness.

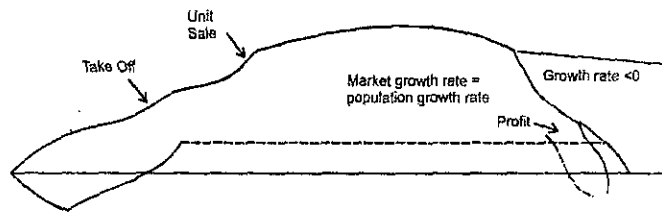
The strengths necessary for success change in the growth stage. Rapid growth brings new competitors in the market. Such factors as brand recognition, product/market differentiation, and the financial resources to support both heavy marketing expenses and the effect of price competition on cash flow can be key strengths at this stage.

As the product/market moves through a 'shake-out' phase and into the maturity phase, market growth continues but at a decreasing rate. The number of market segments begins to expand, while technological change in product design slows down considerably. The result is usually more intense competition and promotional or pricing advantages or differentiation become key internal strengths. Technological changes in process design become intense as the many competitors seek to provide the product in the most efficient manner. Where R&D was critical in the development stage, efficient production has now become crucial to a business' continued success in the broad market segments.

When product/markets move towards a saturation/ decline stage, strengths and weaknesses centre on cost advantages, superior supplier or customer relationships, and financial control. Competitive advantage can exist at this stage, at least temporarily, if a firm serves gradually shrinking markets that competitors are choosing to leave.

Exhibit 7.19 is rather a simple model of the stages of product/market evolution. These stages can and do vary. It is, however, important to realize that the relative importance of various determinants of success differs across the stages of product/market evolution, and therefore these must be considered in internal analysis. Exhibit 7.19 suggests different dimensions that are particularly deserving of in-depth consideration while developing a company profile.

Exhibit 7.20 suggests steps in the development of a company profile.



Functional Area	Introduction	Growth	Maturity	Decline
• Marketing	Resources/skills to create widespread awareness and <i>find acceptance with</i> customers; advantageous access to distribution.	Ability to establish brand recognition; find niche; reduce price; solidify strong distribution relations and develop new channels.	Skill in aggressively promoting product in new markets and holding existing markets; pricing flexibility, skills in differentiating products and holding customer loyalty.	Cost effective means of efficient access to selected channels and market; strong customer loyalty or dependence; strong company image.
Production operations	Ability to expand capacity effectively; limit number of designs; develop standards.	Ability to add product variants; centralize production or otherwise lower costs; improve product quality; seasonal subcontracting capacity.	Improve products and reduce costs, ability to share or reduce capacity; advantageous supplier relationships; subcontracting.	Ability to prune product line cost advantage in production, location, or distribution; simplified inventory control; subcontracting or long production runs.
Finance	Resources to support high net cash overflow and initial losses; ability to use leverage effectively.	Ability to finance rapid expansion, still have net cash outflow but increasing profits; resources to support product improvements	Ability to generate and redistribute net cash inflows; effective cash control systems.	Ability to rescue or liquidate unneeded equipment; advantage in cost of liabilities, control system accuracy; streamlined management control.
Personnel	Flexibility in staffing and training new management; existence of employees with key skills in new products or markets.	Existence and ability to add skilled personnel; motivated and loyal workforce.	Ability to cost effectively reduce workforce; increase efficiency.	Capacity to reduce and reallocate personnel; cost advantage.
Engineering and research and development	Ability to make engineering changes, have technical bugs in products and process resolved.	Skill in quality and few feature development state; developing successor product.	Reduce costs; develop variants in differentiated products.	Support to other group areas or apply to unique customer needs.
Key functional areas and strategy focus	Engineering; market penetration.	Sales; consumer loyalty; market share.	Production efficiency; successor products.	Finance: maximum investment recovery.

Exhibit 7.19: Sources of Distinctive Competence at Different Stages of Product/Market Evolution

Organisational Routines: The Basis of a Company's Capabilities

Strategic capabilities or distinctive competencies are activities that the firm can perform better than competitors, but what is their basis and their nature? We have observed that capability is the consequence of different resources working together in a complementary team. But what is the nature of the interrelationships and interactions that these resources have? What determines the ability of resources to work together to perform complex activities within the organisations? And how does a firm go about creating capability in a particular activity?

Richard Nelson and Sidney Winter of Yale University have developed the concept of 'organisational routines' in this connection. Organisations' routines are regular and predictable patterns of activity made up of a sequence of coordinated actions by individuals. The behaviour of the organisation may be viewed as huge networks of routines. This is true of manufacturing, sales, ordering, distribution, customer service, top management activities such as monitoring of business unit performance, capital budgeting, employee appraisal and promotion. Even the strategy of a corporation may be viewed as a routine: as a set of guidelines that precondition the firm's responses to events.

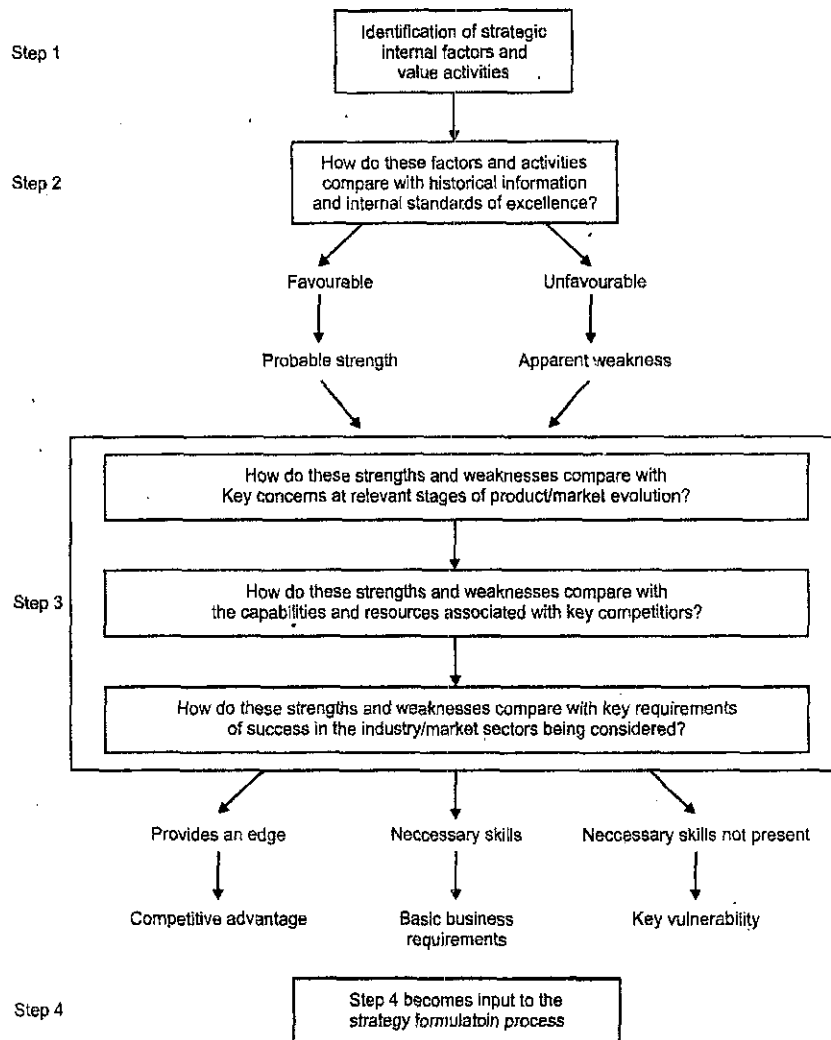


Exhibit 7.20: Steps in the Development of a Company Profile

Routines also fulfill other functions within the firm. They represent the truce between conflicting interests of different members of the organisation and provide a means through which management can control the activities of the organisation. In particular, they establish standards for the smooth functioning of the organization, notwithstanding the fact that resources (especially people) are so heterogeneous.

The concept of organizational routines offers illuminating insights into the relationships between resources, capabilities, and comparative advantage.

The Relationship Between Resources and Capabilities

An important implication of organisational routines is the appreciation that the firm's competencies are not simply the consequences of a collection of industrial resources that the firm controls. The types, amounts, and qualities of resources available to the firm have an important bearing on what the firm can do. They place constraints upon the range of organizational routines that can be performed and the standard to which they are performed. Resources do not, however, exclusively determine what the firm can do and how well it can do it. A key ingredient in the relationship

between resources and capabilities is the management's ability to achieve cooperation and coordination between resources required for the development of organizational routines. The ability of the firm to motivate and socialize its members in order to win their cooperation and commitment depends upon the organization's style, culture, leadership, systems of control, reward, and communication.

The Trade-off between Efficiency and Flexibility Routines are to the organization what skills are to the individual. Just as the individual's skills are carried out semi-automatically, without conscious coordination, so organisational routines involve a large component of tacit knowledge, implying limits on the extent to which the organisation's capabilities can be articulated. Just as individual skills become rusty when not exercised, so it is difficult for organizations to retain coordinated responses to contingencies that only rarely arise. Hence there may be a trade-off between efficiency and flexibility. A limited repertoire of routines can be performed highly efficiently with near perfect coordination—all in the absence of significant intervention by top management. The same organisation may find it extremely difficult to respond to novel situations.

Economics of Experience

Just as individual skills are acquired through practice over time, so an organisation's capabilities are developed and sustained only through experience. The advantage of an established firm over a newcomer is primarily with regard to the routines that it has been perfecting over time. The Boston Consulting Group's 'experience curve' is a naive and mechanistic representation of this relationship of experience to performance. A much more insightful and predictably valid understanding is possible through investigating the characteristics and evolution of underlying routines. This would also explain, for instance in industries where technological change is rapid, why new firms may possess an advantage over established firms. They have a potential for faster learning of new routines because they are less committed to old ones.

The Complexity of Capabilities

Some capabilities derive directly from individual resources. Thus the reputation of Harley-Davidson is primarily in consequence of its status as a sole surviving remnant of the US motorcycle industry. In other cases, a capability may require complex interaction between heterogeneous resources, or may perhaps involve an integrated set of routines. Each routine typically requires a number of resources such as operating skills, customer service skills, communication skills, transportation equipment, and communication and data processing equipments. In addition, it requires commitment, coordination, and responsiveness within its department, and a close, complex link between manufacturing, product design and development, marketing, service functions, effective employee training, management information systems, and a deeply entrenched set of values that have been nurtured over time. The complexity of capabilities in terms of the interrelationships between resources and routines is critical to firm's ability to sustain a competitive advantage and to reap profits from such a competitive advantage.

Appraising The Profit-earning Capacity of Resources and Capabilities

By identifying the firm's resources and capabilities, and establishing areas of strength in relation to competitors, the firm can adjust its strategy to ensure that its strengths are fully utilized and weaknesses protected.

In appraising the capacity of the firm's resources and capability to yield profits over the long term, we need to evaluate these; first in relation to the firm's ability to appropriate returns from its resources; and second in relation to the sustainability of the competitive advantage. Exhibit 7.21 summarises the relationships to be discussed according to four criteria.

Appropriability

In drawing up an inventory of the firm's resources, an immediate problem is determination of the boundaries of the firm's resource base. As we have indicated earlier, a firm's balance sheet is a very poor and unreliable source of information in this connection.

Once we go beyond financial and physical assets, ownership becomes less clear. The firm can establish property rights in certain intangible assets: patents, copy-rights, and brand names for example. Typically, however, only a fraction of the firm's reputation and knowledge is protected by legally enforceable ownership. The primary basis of a company's capabilities is the skills of its employees. The consequences for the firm are twofold: first, the employee is mobile between firms so the firm cannot reliably base a strategy upon the specific skills of individuals; secondly, the employee is in a good position to ensure that his or her full contribution to the prosperity of the enterprise is reflected in the salary and benefits received.

The Four Key Criteria

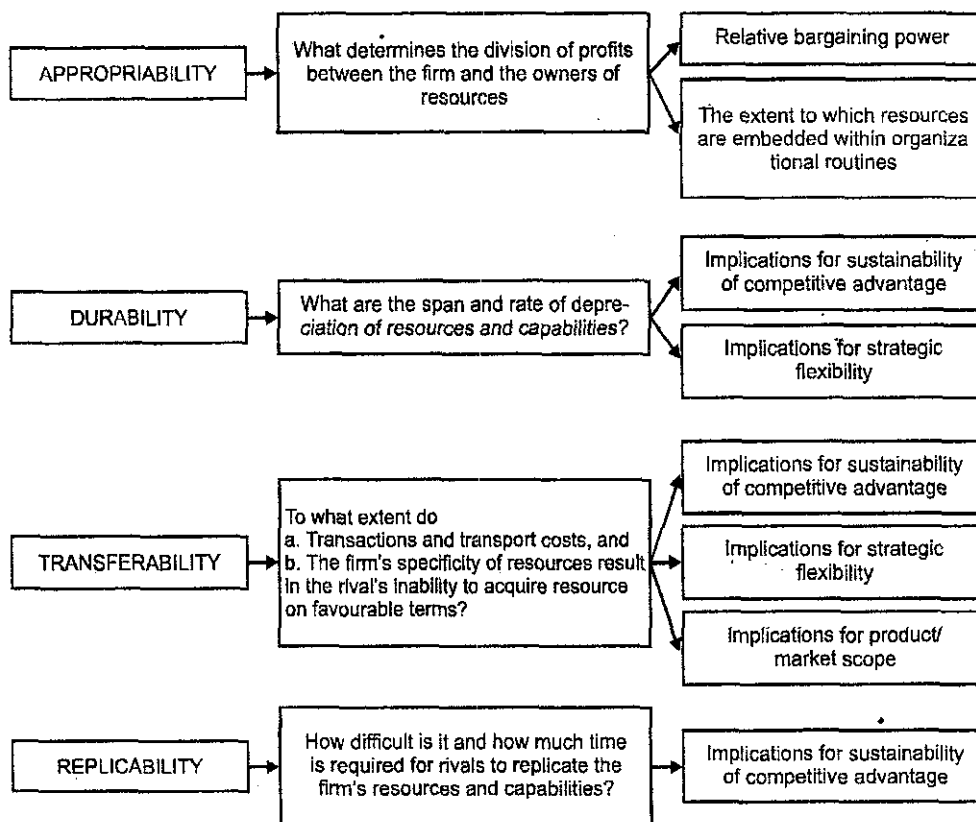


Exhibit 7.21: Appraising the Profit Earning Capacity of Resources and Capabilities

But the capabilities of firms are located within groups of individuals and supported by other sources such as reputation, corporate management systems, and the systems of values that mesh together the employees of departments and companies. From the point of view of the firm, the key issue is the degree of control which the firm can exercise and the extent to which the capability can be maintained when individual employees leave. A firm's dependence upon skills possessed by key highly trained and highly mobile employees is particularly important in the case of professional service companies. An advertising company would be an apt example.

Such issues would also arise in relation to high technology start-up companies that have been such a conspicuous

feature in the evolution of the US electronic industry. Typically, these companies are founded by technologists and managers who leave large, established electronic companies in order to develop and exploit ideas and products that they conceived of when they were with their former employers. The tendency of large, US technology-based companies to spin off numerous entrepreneurial start-ups (for instance the Silicon Valley) rather than being a tribute to the dynamism of American business enterprise, represents a failure of leading US micro-electronic companies to maintain ownership and control over technologies that they develop internally.

Faced with ambiguity over property rights in key resources, an important strategic issue for the firm is the means by which it can secure control over such resources and ensure that it obtains an adequate share of the return from these assets. The issue of the firm's control over its resources is clearly critical to the firm's ability to use its resources as a secure base for formulation and implementation of strategy. But ambiguity over ownership and control is also important from another perspective: the firm's ability to appropriate returns to its resources. An implication of a resource-based concept of the firm is that profits from it are a return to resources owned by the firm. A critical consequence of ambiguity over ownership and control of resources is indeterminacy over the allocation of returns to the resources. For instance, when individuals at 3M pioneer the development of commercially successful products such as reflective traffic signs and Post-it notes, to what extent does 3M profit?

The division of returns between the firm and its employees depends upon relative bargaining power. If the individual employee's contribution to productivity is clearly identifiable, if the employee is mobile, and if s/he could offer similar productivity to other firms, then s/he is in a strong bargaining position to expropriate a substantial proportion of the contribution in salary, bonus, or commission.

Conversely, the less easy it is to identify the individual's contribution and the more firm-specific are the skills being applied, the greater is the proportion of returns that accrue to the firm. A recent trend among investment banking firms has been to reduce the image and reputation of individual stars and gurus and increase the identity and reputation of the firm and the team. Conflicts with senior employees at City Bank, Merrill Lynch, First Boston, etc. have been a consequence. It is also to be noted that the tendency of professional service firms is to be organised as partnerships rather than corporations, partly to reflect the superiority of a partnership in avoiding bargaining conflict between owners and employees in enterprises where the capital stock is primarily human skills.

Durability

Some resources are more durable than others and, hence, are a securer basis for competitive advantage.

Intangible assets vary substantially in durability. Thus while the value of patents is increasingly being curtailed by technological leapfrogging, consumer brand names show remarkable durability (brands like Kelloggs and Coca Cola are examples). Corporate reputation is similarly long enduring (General Electric, Du Pont, IBM are examples). The reputation of being a well-managed, socially responsible, financially sound company, producing reliable products and taking good care of its employees and customers, gives a company credibility and attention in every field of business it enters.

Transferability

The firm's ability to sustain its competitive advantage over time depends upon the speed with which rivals can acquire the resources and capabilities needed to imitate the success of the initiating firm. The primary means of doing so is the hire and purchase of required inputs. The ability to do so depends upon the transferability of resources and capabilities. Some resources such as raw materials, components, machines performing standard operations, and certain types of

human resources are easily transferable and can be purchased readily. Some other resources such as special types of machinery and costly equipment are not easily transferable. Yet other resources such as technical knowledge and brand names may be firm-specific in the sense that their value declines on transfer to another firm. Other resources such as the reputation of the firm, may be completely firm-specific and although valuable to the firm itself, may have doubtful value for an intending purchaser.

Transfer of capabilities is particularly difficult where a firm's capability is the consequence of resources working together as a team. This would mean transfer of the whole team, which is possible but very improbable.

If resources and capabilities are highly differentiated and are firm-specific, other consequences for strategy follow. In such cases, these resources play an important role both in limiting the flexibility of the firm in changing its strategy and in providing an important incentive to diversify in order to more fully exploit any underutilised resources and skills.

Replicability

The firm-specificity of a resource or routine limits the ability of a firm to acquire it simply by purchase in the market. The second route by which a firm can acquire a resource or capability is by creating it itself through investment. Some capabilities can be easily initiated through replication. If legal barriers exist to replication, as in the case of patented products, then replication can be more difficult. Probably the least replicable capabilities are those that are based upon the exercise of highly complex organizational routines. The complex nature of these routines and the fact that they are based upon tacit rather than codified knowledge means that diagnosing and recreating them is exceedingly difficult. Even when codified, it may still be very difficult to imitate a competitor's superior performance. Thus McDonald's success is based upon a highly sophisticated and detailed operating system that regulates the operations of every McDonald outlet, from employee behaviour and dress to cleaning procedures to the placing of pickles on the burger. Yet the system is only one aspect; equally important is ensuring its implementation through management information, incentives, and controls.

Similar difficulties of imitation have applied to Western firms' adoption of successful Japanese industrial practices. Two of the simplest and best known Japanese manufacturing practices are just-in-time inventory systems and quality circles. Both are simple ideas that require neither sophisticated knowledge nor complex operating systems. Indeed, the concept and design originally came from the US. Yet the successful operation of both requires a degree of cooperation and set of attitudes that few American or European firms have been successful in introducing with the same degree of success as their Japanese counterparts.

Thus 3M Corporation's approach to the development of new products is distinctive competences that are located not in a particular department or unit, but permeate the whole corporation and are built into the fabric and culture of the organisation. Moreover, because these routines are broadly based and not particular to any one product or production technology, they are not as constraining and/or subject to obsolescence as more specific routines.

Identifying the Resource Gaps and Developing the Resource Base

A resource-based approach to strategy must be concerned not only with deploying existing resources but with investing in resources that secure a long-term future for the firm. Such investment is concerned not just with maintenance but augmentation of the firm's resources so that positions of competitive advantage can be strengthened and the firm's strategic opportunity set broadened. Therefore a key feature of resource analysis is that once a strategy has been formulated based upon a matching of the firm's capabilities with opportunities available in the external environment. The firm must reconsider the implications of the strategy for the firm's resource needs. In other words, what resource gaps need to be filled?

Thus General Motor's strategy for regeneration, automation, and quality enhancement has placed great emphasis on identifying and filling the resource deficiencies that its strategy caused. GM's needs for electronic technology was the principal stimulus for its acquisition of Electronic Data Systems. Likewise, its quest for improved quality encouraged its strategic alliance with Toyota. These are aspects of core competency, a concept that will be elaborated below.

The implications of the firm's strategy for its resources are not only in terms of the emergence of resource gaps. The pursuit of a particular strategy not only utilises a firm's resources, but also augments resources through the creation of skills and knowledge that are the products of experience. In the words of Hiroyaki Itami who introduced the concept of *'dynamic resources fit'*: 'Effective strategy in the present builds invisible assets, and the expanded stock enables the firm to plan its future strategy to be carried out. And the future strategy must make effective use of the resources that have been amassed.' Matsushita's multinational expansions have closely followed this principle of parallel and sequential development of strategy and resources. Arataroh Takahashi explained the strategy

In every country batteries are a necessity, so they sell well. As long as we bring a few advanced automated pieces of equipment for the process vital to final product quality, even unskilled labour can produce good products. As they work on this rather simple product, the workers get trained, and this increased skill level then permits us to gradually expand production to items with increasingly higher technology level, first radio, then television.

This dynamic resource fit may also provide a strong basis for a firm's diversification. Sequential additions as expertise and knowledge are acquired are prominent features of Honda's strategies in extending its product range from motorcycles to cars, to lawn mowers, and boat engines, as also 3M's in expanding from abrasive, to adhesive, to computer disks, video and audio tape, and a broad range of consumer and producer goods.

Core Competence

Prahalad and Hamel, in impressing the importance of 'invisible' resources in global competition, have introduced the impressive concept of Core Competency. Core competencies are the collective learning in organisations, especially on how to coordinate diverse production skills and integrate multiple streams of technologies. The philosophy behind the concept is simple and can be likened to a tree. The diversified corporation is a large tree. The trunk and major limbs are core products, the smaller branches are business units; the leaves, flowers, and fruit are end products. The root system that provides nourishment, sustenance and stability is the core competency.

It thus involves not only harmonizing streams of technology but is also about the organization of work and delivery of value. The force of core competency is felt as decisively in services as in manufacturing. It is also communication, involvement, and a deep commitment to working across organizational boundaries. The skills that together constitute core competency must coalesce around individuals whose efforts are not so narrowly focused that they cannot recognize the opportunities for blending their functional expertise with that of others in new and interesting ways.

Two fallouts from core competencies are important.

- core products;
- strategic architecture.

Core Products

The tangible link between identified core competencies and end products is what is called core products: the physical embodiments of one or more core competences. Core products are the components or sub-assemblies that actually contribute to the value of end products. If a company maintains world manufacturing dominance in core products it reserves the power to shape the evolution of end products.

Thus Canon is reputed to have an 84 per cent world manufacturing share in desktop laser printer 'engines' even though its brand share in the laser printer business is miniscule. Similarly, Matsushita has a world manufacturing share of about 45 per cent in key VCR components, far in excess of its brand share of 20 per cent, and a commanding core product share in compressors worldwide, estimated at 40 per cent, even though its brand share in both the air-conditioning and refrigerator businesses is quite small.

To sustain leadership in their chosen core competence areas, these companies *seek to maximize their world manufacturing share in core products*. The manufacture of core products for a wide variety of external (and internal) customers yields the revenues and market feed-back that, at least partially, determine the pace at which core competences can be enhanced and extended.

Strategic Architecture

The fragmentation of core competencies becomes inevitable when a diversified company's information system, patterns of communication, career paths, managerial rewards, and process of strategy development do not transcend SBU lines.

By providing an impetus for learning from alliance and a focus for internal development efforts, strategic architecture like NEC's C&C can dramatically reduce the investment necessary to secure future market leadership. The answers to the following questions will help us visualize what strategic architecture looks like. How long could we preserve our competitiveness in the business if we did not control a particular core competency? How central is this core competence to perceived customer benefits? What future opportunities would be foreclosed if we were to lose this particular competence?

This strategic architecture provides a logic for product and market diversification. It should make resource allocation priorities transparent to the entire organisation. It provides a template for allocation decision by top management. It helps lower level managers understand the logic of allocation priorities and disciplines senior management to maintain consistency. In short, it yields a definition of the company and the market it serves.

SBU and Core Competency

The implications of two alternate concepts of the corporation are summarised in SBU or core competence.

As an SBU evolves, it often develops unique competences. Typically, the people who embody this competence are seen as the sole property of the business in which they grew up. They are usually not available for the benefit of the company as a whole.

When competences become thus imprisoned, the people who carry the competences do not get assigned to the most exciting opportunities and their skills begin to atrophy. When the organisation is conceived of as a multiplicity of SBUs, no single business may feel responsible for maintaining a viable portion in core products nor be able to justify the investment required to build world leadership in some core competency. There is thus need for a more comprehensive view imposed by corporate management to be superimposed on the SBU concept and a suitable organizational form to allow this.

	SBU	Core Competence
Basis for competition	Competitiveness of today's products	Inter-firm competition to build competencies.
Corporate structure	Portfolio of businesses related in product market terms	Portfolio of competencies, core products, and businesses.
Status of the business unit	Autonomy is sacrosanct: the SBU owns all resources other than cash	SBU is a potential reservoir of core competencies.
Resource allocation	Discrete businesses are the unit of analysis; capital is allocated business by business	Business and competencies are the units of analysis; top management allocates capital and talent
Value added of top management	Optimizing corporate returns through capital allocation trade-offs among businesses	Enunciating strategic architecture and building competencies to secure the future.

Exhibit 7.22: Two Concepts of the Corporation – SBU and Core Competence

Chapter 8

SWOT Analysis

In looking at various aspects of the external and internal environment, we have to look at the strengths and weaknesses of the company and as also, to an extent, opportunities and threats. We nevertheless, again reemphasize their importance in the corporate planning process to make the concept much more self contained.

There are several ways to undertake such analysis. One approach is to look at the corporate identity and view the strengths, weaknesses, opportunities and threats from there. The second way is to scrutinize all aspects of the company's activities and resources, and look at the strengths and shortfalls.

- i. When looking at the corporate identity, it is relatively simple to see that the allocation of resources, and the orientation of activities in the market place must maintain a close identification and alignment with the company's missions, and consequent statement of objectives. Any contradiction in this anywhere would be a symptom of weakness.
- ii. When looking at the various aspects of the company, it is possible to identify and analyse these strengths and weaknesses systematically. We provide here a brief description.

Strengths

A strength is a resource, skill, or other advantage in relation to the competition and the needs of markets a firm serves or anticipates serving. A strength is a *distinctive competence* that affords the firm a comparative advantage in the market place. Financial resources, image, market leadership and buyer-supplier relations are examples.

Weaknesses

A weakness is a limitation or deficiency in resources, skills, and capabilities that seriously impedes effective performance. Facilities, financial resources, management capabilities, marketing skills, and brand image could be sources of weakness.

Strengths and weaknesses can be identified by careful analysis of the firm's activities. A few examples follow:

a. Source of profit

- i. If the bulk of the profit comes from a single product, that in itself is a symptom of weakness deserving further analysis:

What is its status in the life cycle? What is the status of competition? What is the status of industry sale? Product quality? Is the market share currently enjoyed commensurate with quality, competition, price status? Is there scope for further growth in sales through product development?
- ii. What is the scope for development of other profit-yielding products?
- iii. Is the technology continuing to be up-to-date or is there a risk, of better technology appearing in the market place in the near future? What is the danger of substitution?
- iv. Is the product itself in any danger of becoming obsolete or out of style in the near future?

b. Risks

The analysis of the source of profits invariably exposes the risks looming ahead. These may be:

- i. For the product, the dangers of obsolescence;
- ii. the danger of being priced out because of quality, cost, and backdated technology;
- iii. the danger of substitution.
- iv. For the market, the style and desirability changing; the danger of new competition coming in; the market itself reaching maturity or its decaying state, etc.

Opportunities

An opportunity is a major favourable situation in the firm's environment. Key trends represent one source of opportunity. The identification of a previously overlooked market segment, changes in competitive or regulatory circumstances, technological changes, and improved buyer and/or supplier relationships could represent opportunities for the firm.

Threats

A threat is a major unfavourable situation in the firm's environment. It is a key impediment to the firm's current and/or desired future position. The entrance of a new competitor, slow market growth, increased bargaining power of key buyers or suppliers, major technological change, and changing regulations could represent major threats to the firm's future success.

Opportunity for one firm could be a strategic threat to another. Thus regulation in India reserving some product ranges for the small-scale sector would represent an opportunity for the small-scale industries in that sector and a threat to large industries in it also, the same factor can be seen as both a potential opportunity and a potential threat. Thus the entry of Caterpillar through a joint venture with Mitsubishi in the Japanese market was a threat to Komatsu whose products were then distinctly inferior in quality by comparison. It was also an opportunity for Komatsu to employ its *R&D* efforts to match Caterpillar quality and thus not only confidently face Caterpillar in the domestic market, but also expand to become a competitor to Caterpillar internationally. This is a classic example of a 'threat' being converted into an 'opportunity'.

Understanding the key opportunities and threats facing a firm helps managers identify realistic options from which to choose an appropriate strategy. Such understanding clarifies the identification of the most effective niche of the firm.

SWOT analysis can be used in at least three ways in strategic choice decisions.

- i. The commonest application provides a logical framework guiding systematic discussions of the business situation, alternative strategies, and, ultimately choice of strategy. What one manager sees as an opportunity, another may see as a potential threat. Likewise, a strength to one manager may be a weakness from another perspective. Different assessments may reflect underlying power considerations within the organization, as well as differing factual perspectives. The key point is that systematic SWOT analysis ranges across all aspects of a firm's situation, providing thereby a dynamic and useful framework for choosing a strategy.
- ii. In a second application of SWOT analysis, key external opportunities and threats are systematically compared to internal strengths and weaknesses in a structured approach. The objective, is identification of one of four distinct patterns in the match between the firm's internal and external situations. These patterns are represented by the four cells in Exhibit 8.1. Cell I is the most favourable situation; the firm faces several environmental opportunities and has numerous strengths that encourage pursuit of these. This condition suggests growth-oriented strategies to exploit the favourable match. Cell 4 is the least favourable situation, with the firm facing major environmental threats from a position of relative weakness. This condition clearly demands strategies to reduce or redirect involvement in the products/markets examined using SWOT analysis.

In Cell 2, a firm with key strength faces an unfavourable environment. In this situation, strategies would use current strength to build long-term opportunities in other products/markets—a clear call for diversification. A business in Cell 3 faces

impressive market opportunity but is constrained by several initial weaknesses. A business in this predicament is like the question mark in the BCG matrix. The focus of strategy for such firms is eliminating internal weaknesses to more effectively pursue market opportunity.

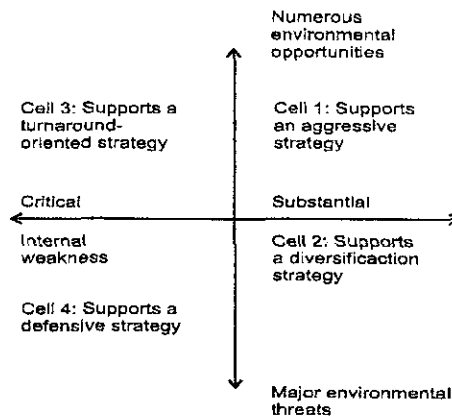


Exhibit 8.1: SWOT Analysis Diagram

- iii. A major challenge in using SWOT analysis is in identifying the position the business is actually in. A business that faces major opportunities may likewise face some key threats in its environment. It may have numerous internal weaknesses but also have one or two major strengths in relation to key competition. Fortunately, the value of SWOT analysis does not rest solely on careful placement of a firm in one particular cell. Rather, it lets the strategist visualise the overall position of the firm in terms of the products/market conditions for which a strategy is being considered. Does the SWOT analysis suggest that the firm is dealing from a position of major strength? Or must a firm overcome numerous weaknesses to match external and internal conditions? In answering these questions, SWOT analysis helps resolve one fundamental concern in selecting a strategy: *What will be the principal purpose of the grand strategy?* Is it to take advantage of a strong position or to overcome a weak one? SWOT analysis provides a means of answering this fundamental question, and this answer becomes an input to one dimension in a second, more specific, tool for selecting grand strategies; *the grand strategy selection matrix*.

The basic idea underlying the matrix is that two variables are of central concern in the selection process: (a) The principal purpose of the grand strategy and (b) the choice of an internal and external emphasis for growth and/or profitability. It is important to note that even early approaches to strategy selection were based on matching a concern for internal versus external growth, with a principal desire to either overcome weakness or maximize strength. The same concerns lead to the development of the grand strategy selection matrix, as shown in Exhibit 8.2.

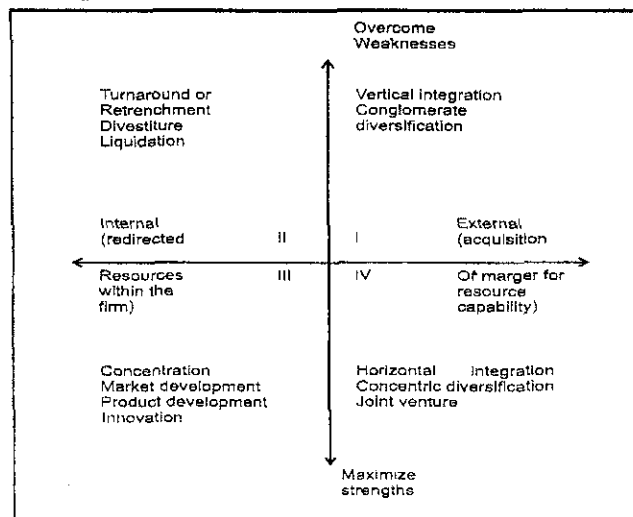


Exhibit 8.2: Grand Strategy Selection Matrix

A firm in quadrant I often views itself as overly committed to a particular business with limited growth opportunities or involving high risks because the company has 'all its eggs in one basket'. One reasonable solution is *vertical integration* which enables the firm to reduce risk by reducing uncertainty either about inputs or about access to customers. Alternatively, a firm may choose *conglomerate diversification*, which provides a profitable alternative for investment without diverting management attention from the original business.

A more conservative approach to overcoming weakness is to be found in Quadrant II. Firms often choose to redirect resources from one business activity to another within the company. While this approach does not reduce the company's commitment to its basic mission, it does reward success and enables further developments of proven competitive advantage. The least disruptive of Quadrant II strategies is *retrenchment*; the pruning of current business activities.

If weakness results from inefficiencies, retrenchment can actually serve as a *turnaround strategy*, meaning the business gains new strength by streamlining its operation and eliminating waste. However, when the weaknesses are a major obstruction to success in the industry, and when the costs of overcoming the weaknesses are unaffordable or are not justified by a cost-benefit analysis, then eliminating the business must be considered.

It need scarcely be emphasized that a company should build from strength. The premise is that growth and survival depend on an ability to capture a market share that is large enough for essential economies of scale. If the firm prefers an internal emphasis holding to this approach, as shown in Quadrant III, the commonest strategy is *concentration* or market penetration.

Two other approaches in Quadrant III are *market* and *product development*. Both strategies attempt to broaden operation. Market development is chosen if it is felt that existing products would be well received by new customer groups. Product development is preferred when existing customers are believed to have an interest in new products connected with the current product lines. The dual strategy in Quadrant III is *innovation*, where the business's strengths are in creative product design or unique production technologies.

Maximizing a business's strength by aggressively expanding its basis of operation usually requires an external emphasis in selecting a grand strategy. Preferred options, as shown in Quadrant IV, are *horizontal integration*, *concentric diversification* and *joint venture*. All three enable the firm to quickly increase output capability.

Resource Analysis

a. *Manufacturing Activities*

This usually provides considerable cost reduction potentials through making the process more efficient, reducing wastage and often by streamlining the manufacturing process, raw materials, the standards set for their purchase, etc.

b. *Rationalisation of Resources*

This essentially means matching the resources to the requirements in the most efficient and cost effective way. It includes sizing up of the manufacturing and other facilities, relocation of facilities, etc.

c. *Organisation and Management Structure*

This includes the quality of human resources, management succession, strengths and weaknesses of key managers, communications systems, style of management, style of decision-making, relationship with trade unions and personnel, etc.

d. *Financial Resources*

The financial resources, particularly the liquid resources that are available and/or can be commandeered, and their adequacy or otherwise when matched against requirements is an area of strength or weakness. This should not only be true for existing activities, but also for activities that may additionally be taken up during the plan period.

e. Corporate Capability

In addition to company mission and motivation, every company has, often for no easily discernible design or reason, a number of areas in which it is good and a number at which it is mediocre or poor. Thus one company may be particularly effective in its customer service, another may be excellent at physical distribution. It may be possible for one company to utilise design skills more skilfully than its competitor. Another may have a particular and unique marketing flair. A company may have the market reputation to give confidence to and attract share capital for new ventures, another may have the confidence of institutional financial organisations.

These capabilities are extra strengths, providing clues to the possible future orientation or activity of the company.

f. Systems

The systems and procedures prevalent in the organization are sources of efficiency or otherwise, and are consequently areas of strength and weakness that need to be analysed.

Understanding the key strengths and weaknesses of the firm further aids in narrowing the choice of alternatives and selecting a strategy. Distinct competence and critical weakness are identified in relation to key determinants of success for different market segments. This provides a useful framework for making the best strategic choice. Simultaneously, identification of major weaknesses enables specific action plans to be drawn up to rectify them.

Strategy and Gap Analysis

Considering the market situation, strengths and weaknesses, etc., and assuming efficient working into the future, it is possible to project for the company the likely achievements during the plan period with the existing products. Plotting against this the target or objectives during the same period, would provide a clear picture of the gap. For planning purposes, it is now necessary to analyse this gap, particularise the strategy of the company, and suggest a realistic plan of action. Perhaps this is better illustrated by a simple diagram, Exhibit 8.3

Let us say that line A represents the cumulated profit target over the planning horizon and hence is one aspect or facet of the corporate planning objective.

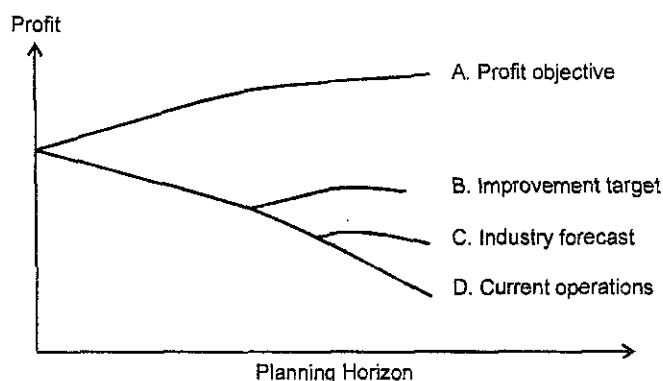


Exhibit 8.3: Gap Analysis

Line D represents the cumulative impact on profit outcome of the current operations, which indicates a trend towards oblivion. The reasons for such trend would be evident if one recalls the points made during the discussions on internal assessment, including the product life cycle.

Line B represents the improvement target, which can be set on the basis of the analysis of the company's strengths and weaknesses. This would be partially assisted by a projection of the industry forecast, as reflected in Line C.

The gap between Line A and Line B represents the *strategic gap*, which must be filled through proper strategic thinking, usually by the top management. Usually, it is better to plan for some *reserve* in excess of Line A, in apprehension that some of the plans adopted might not succeed up to expectation and planning exactly up to Line A which would automatically result in a shortfall, whereas the reserve would act as a cushion.

Filling the Gap

a. *Momentum strategy*: This effectively means exploiting to the utmost the scope provided by existing products. Evidently, this would be the most straightforward and simple strategy: the products are known, the market is understood. The most straight forward would be (i) exploitation of existing market. The next stage would be (ii) exploitation of new markets with existing products. The capital investments which might be necessary would be to expand the manufacturing facilities and the marketing set up, as necessary.

b. *Expansion plan*: The expansion plan is next in the hierarchy of strategic decisions. This relates to making the product range more complete in the same, similar, and related products. This is expected to generate growth in sales and profit not only in new products but also in existing products, both in existing and new geographically expanded markets.

Since this stage involves both new markets and new products, knowledge of market acceptability of products (both old products in new markets and new products in all markets) is significantly less. Hence a greater uncertainty is involved. The capital investment requirement both for manufacturing (including R & D work preceding this) and marketing activities would be that much higher.

c. *Diversification strategies*: It is reasonable to assume that the two strategies briefly discussed above would not close the gap in a realistically drawn up corporate plan. Thus the third step in the hierarchy of strategies would be necessary; the one covered under the all embracing name diversification strategy.

d. *Synergy structure*: As we have already discussed under corporate capability, for no obviously discernible reason, companies develop distinct capabilities in a number of areas: a number of activities. It is useful to chart this capability profile for a company and bear it in mind when considering diversification, so that the capability or competence profile becomes the basic reference profile of the firm, to be utilised to advantage whenever possible. Thus the profile may be discussed in terms of:

- general management and finance;
- research and development;
- operations;
- marketing.

Once a search has uncovered a promising acquisition or a new product, a measurement of the synergy of the product with the competence of the company is made as a contributing factor to potential joint profitability. The resulting pattern may be compared with the competitive profile of a successful competitor in the firm's own business. This will indicate whether the pattern of reinforcement will make any significant contribution to the firm's competitive position.

Alternative Paths to Strategic Decisions

Under the overall title of diversification strategies, we are really looking at alternative paths to filling the gap. This would include:

- divestment;
- obtaining manufacturing and/or marketing rights;
- granting manufacturing and/or marketing rights;
- a simple expansion;

SWOT Analysis

- research and development seeking expansion/diversification;
- acquisition and merger.

We briefly discuss these.

- Divestment:** Divestment, although seemingly an anomaly, is also a possible component of the effort at bridging the gap. Thus divestment may be part of the tidying up operation after corporate appraisal and evaluation have been made. The activity, although profitable, might not fit in with the company's profile of mission or the profitability may be significantly short of expectation or acceptability in terms of resources and assets being blocked up. The divestment may be the result of desire to reduce risk, or to release much sought liquid resources, etc.
- Obtaining Franchises:** Obtaining manufacturing and/or trading rights may save time in putting the product in the market. The quality of the product is already known, as also its performance in other markets. The avoidance of R&D expenses is another advantage, and it may also reduce competition or a possible threat of competition. This strategy may also give the company access to technical knowledge and possibly skilled personnel which would otherwise be difficult or impossible to obtain, and may provide a back up service which might otherwise have been beyond the resources of the company.

Perhaps the biggest problem of all is of finding some-one who wants to franchise out a product which is compatible with the mission, culture, and synergic structure of the company. Other problems are cost, continuity, and security of information, legislation and availability. It becomes a risk area because a major product area may disappear overnight if the agreement is cancelled or lapses. This is further heightened by the fact that the franchise holder must provide information to the principal about the market which may become attractive enough for the principal to go into it on his own. Possible security against such threats can be technology transfer/outright purchase or equity participation by the principal.

- Granting Franchise:** This is the least risky way of extending existing products to new markets. No capital is tied up in production or market development work and profit comes in through various forms of franchising fees. The risk is any change in government policy regarding royalty payment to external companies.
- A simple Expansion:** A simple expansion policy may be considered to be synonymous with diversification strategies. To consider the possibilities the strategy alternatives as shown in Exhibit 8.4 may be studied.

Market \ Product	Current	New
	Current	New
Current	(A)	(C)
New	(B)	(D)

Exhibit 8.4: Analysis of Strategic Alternatives

In the matrix, the current current box (a) is covered under momentum strategy. Box (c) (current product/new market) is covered under development strategy, while boxes (b) and (d) are diversification strategies.

The important point is to choose a product which should have the following essential attributes:

- i. It should match the synergic structure of the company,
- ii. It should have a good market and a good market potential,
- iii. The product itself should have the potential of being expanded into a viable product group with consistently expanding growth potential.

It is also important for the new product or product group to have adequate affinity with existing product orientation. A quick way of checking this is by the Who/What/How (Y) model shown in Exhibit 8.5

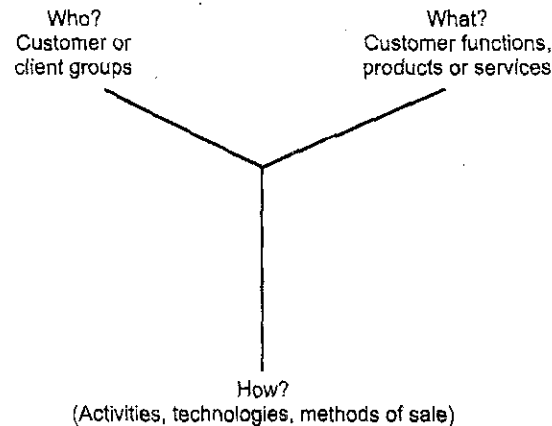


Exhibit 8.5: Who/What/How (Y) Model

During the gap analysis, the planning team should develop a Who/What/How analysis for each major product line of business the company is currently dealing in. Thereafter, for any proposed area of growth in the business plan, the team should compare its who/what/how model with ones prepared for each of the major areas of the current business/product range. Comparing with the most similar line of business in the current product range, it should then attempt to find out how many of the three dimensions would need to change. Changing only one axis (with whom business is done, or what is sold, or how business is done) carries with it the least risk. Changing two dimensions at once is riskier and is, in most cases, imprudent; and a three dimensional switch generally proves to be almost foolhardy even if the organisation has massive resources at hand to simultaneously learn about new customers, new products, and a new delivery system.

Examples of changing only one dimension are innumerable in India among the successful diversification cases. Ceiling fan manufacturing companies introducing table or pedestal fans is one such example of single dimensional change. Britannia Biscuits company manufacturing and marketing cooking oil is an example of simultaneous change in two dimensions (product, customer). Metal Box making ball bearings and ITC venturing into marine products are examples of simultaneous change in all three dimensions and both ended in failure. The first in disaster, the second in heavy loss and withdrawal. ITC venturing into cooking oils is an example of successful simultaneous change in three dimensions. It, however, required careful and meticulous preparation.

e. Research and Development

Research and development is really a means rather than an end in seeking expansion. For this to be successful and cost effective, the planning process should provide the framework for research and development planning by:

- Specifying the product or business areas to which research is to be directed.
- Setting priorities for research and development projects.

- Assigning time targets for R&D.
- Setting the cost framework in terms of both revenue and capital requirements.
The intensity of R&D efforts would be modulated by the strategic approach of the company. Thus it may be.
- 'offensive' (the intention to be first in the field with a major innovation);
- 'defensive' (the intention to avoid mistakes by following the leaders: never being first but reacting quickly enough to be second);
- 'adsorption' (obtaining developments on licence and carrying out minimum R&D work to further develop them).

f. Acquisition and Merger

Another area of strategic choice open to a company is acquisition, or its variant, merger.

There are quite a number of positive and genuine benefits of acquisition strategy and it can provide a sound bridge to the future. Acquisition can provide:

- existing products new markets—to provide an easier means of entry;
- new products/existing markets—providing complete integration with the present operations;
- existing products/existing markets -backward integration to control supplies or forward integration to take on a further step in the distribution process;
- new products/new markets—complete diversification through acquisition of a company in an entirely new field.

Whatever the reasons, the benefits of acquisition would include.

- i. **Reduction of Risk:** new product introduction or a new market is always fraught with risk of failure. Acquisition of a company manufacturing a product in the desired market would obviate that risk of failure.
- ii. **Avoidance of a Profit Slump:** Acquisition may be a way of buying immediate profits, where one of the other alternatives would have resulted in a period of reduced earning.
- iii. **A Means of Entry into a New Area:** Entering a new area, the company invariably faces barriers to entry, the extent of resistance depending upon the nature of the product, the size of the market, and the strength and nature of the incumbents. Acquisition may be a strategy that is attractive in this context and makes it simpler to overcome such a barrier.
- iv. **A Means of Obtaining Cash:** Certain types of companies may have healthy cash flow, a large liquid reserve, and a relatively poor history of profit. Acquisition by a company with a compatible synergy structure would enable profits to be improved, share-holders kept happy, and surplus cash to be availed of.
- v. **Welding together a fragmented Industry:** Some industries are highly fragmented. This makes it difficult for any company to gain a major share of the market by any internal strategy. The only way of building up a sizeable operating unit is through a process of acquisition and rationalisation.
- vi. **Removal of Competition:** The above and similar steps may also be taken as a means of removing competition.
- vii. **Opportunity for Synergy:** Acquisition may be planned because the company has spotted a synergistic opportunity, in cash resources, research and development, production, distribution, or marketing.
- viii. **To Obtain New Ideas:** A sterile company may turn to acquisition for growth because it lacks creativity and has no ideas of its own. This is, however, only a short-term opportunity and may prove to be quite unsatisfactory unless the company's top management in the meanwhile makes a radical change in creativity, etc.
- ix. **To Obtain New People:** Sometimes the reason for acquisition is to acquire particular management skills.
- x. **Reduction of Time to Mature:** Acquisition may provide the company entry into a new product/market area with a

reduced gestation period and mature technology and management set up. This provides a considerable gain in time.

- xi. **Capital Cost of Growth:** Acquisition may also be chosen for strategic financial reasons. A business with a poor cash flow may not have the capital to choose, for example, the R&D route, but may be able to acquire by an exchange of shares without cash.

Risk and Dangers of Acquisition

Apart from the usual dangers, a major reason, not often easily anticipated beforehand, is the possible cultural conflict and lack of empathy, particularly for a hi-tech company. A notable case is that of the recent acquisition of NCR Computers Division by AT&T Computers Division. The otherwise much more resourceful AT&T is technologically much weaker than NCR in this field. Cultural absorption and amalgamation were just not taking place. Ultimately the problem was, at least in the short term, resolved by AT&T management inviting NCR technologists to consider AT&T resources as their own and mould it the way they wished. Thus the merger has effectively amounted to an extension of NCR's market under the AT&T umbrella and brand name.

If the Gap Cannot be Closed It scarcely needs emphasising that development of application of the three classes of strategies, momentum, developmental, and diversification, proceeds simultaneously with matching these with available and mobilizable resources, so that the plan developed may not fail or be hindered by a resource crunch, on the one hand, and function with significant idle resources, on the other.

If the gap between the current state and the desired state seems too large to bridge, then one of two actions is necessary,

- i. creative solutions for closing the gap must be developed; or
- ii. the desired future must be redefined, with focus on those aspects of the strategic business model that are more likely to be accomplished and that will also have the most significant impact.

Recycling between gap analysis and reworking the strategic business model should continue until a strategic business model emerges that is feasible and realistic. When this happens, two other things require to be done. Contingency plans need to be developed to prepare the organization to adjust to significant changes in the internal and external environment, and functional plans must be developed to carry the carefully defined plan to the operational level.

From Plan to Actions

Action must be the end product of planning. For without action, planning is a pointless and empty exercise. A planning system without a formal method of creating action is likely to lead to poor quality planning. Yet, moving from plans to actions and controlling against results is not an easy task in any company, and may become extremely complex in large or diversified organisations. It is also an area which may meet unusually strong opposition from managers, because life for them would be easier if the implementation was left to them on a purely informal basis.

Some particular steps are recommended, specifically seven of these are essential and one optional, which may be taken as an alternative to one of the essential steps. These are listed, and thereafter briefly discussed.

Essentials

- i. Conversion of long range plans into short range tactical and functional plans;
 - ii. assignment of tasks to individuals (standards of performance);
 - iii. budgetary control;
 - iv. monitoring performance against plan;
 - v. monitoring assumptions;
 - vi. updating and reconsidering the plan as required;
 - vii. time bound report on planning activity.
- i. **Tactical plans:** The corporate plan, as it is, cannot be easily implemented because there are many key actions which are not defined in detail and broken down into tasks which can be assigned to particular individuals. This is usually done by tactical plans, which are usually of two types: short-term operating plan and project plan.

- a. A short-term operating plan usually covers a year. These are organized around functional areas, must translate to the immediate future the strategies of the long term, and should not be used as a means of introducing additional strategies unless the corporate plan is also modified.

The quality of the annual operating plan would be improved by careful attention to procedure. A comprehensive timetable should be issued by the planner, so that every person understands the part he has to play and the date by which his contribution must be received.

- b. Project plans are meant for specific projects incorporated in the corporate plan. They have a time span dictated by the implementation time of the projects themselves. They usually involve many different functions. The stages in project planning for marketing-oriented assignments would include:

<i>Stage</i>	<i>Action</i>
● Identification of idea	
● Initial project study	Personnel/department to be specified including desk research depending on type of project; say new product introduction – then action is to be taken by marketing
● Preliminary product marketing	Marketing concept
● Definition of Research and development objective	R&D Top management
● Decision to proceed	
● Refined product marketing concept	Marketing assisted by appropriate department
● Decision to proceed	Marketing or top management as appropriate
● Feasibility study, including market research. Process development. further R&D work. Technical feasibility improvement needs, packaging, development, Revised costing	Marketing R&D, Process Engineering, R&D, Accounts as appropriate
● Marketing plan and project evaluation	Marketing, planning/accounting
● Decision to proceed	Top management
● Completion of test market re-evaluation	As appropriate
● Final decision	Top management
ii. <i>Assignment of task to individual:</i> Quantified goals and the assignment of tasks to particular people provide the company with a means of controlling all aspects of the plan. All personal standards of performance should be grouped by organisational responsibilities so that controls can be exercised through normal management reporting lines. It also follows that the person who is expected to perform the task must be properly informed about .	
iii. <i>Budgetary control:</i> The annual budget is, perhaps ideally, the quantification in financial terms of the annual operating plan. In this manner the budget defines the expected effects of a planned course of action and ties it with longer-term strategies and the expected achievement of certain profit targets.	

The annual budget goes into much greater details than the corporate plan; it has to, as it is a control document and must provide control information for many responsibility centres, split down to all meaningful items of expense and income. The budget is, of course, broken down into time periods. Monitoring results against the budget, considering the effects of these on the chances of hitting targets, and identifying action areas to bring a company veering off course back on track are well known and are aspects of a budgetary control procedure. At any reporting period during the year the company should have a latest estimate of expected results.

There may be three principal reasons for a deviation between budgets and results: faulty implementation, wrong assumption, or an erroneous expectation of results arising from a faulty forecast. The combination of planning and budgeting makes it easier to identify which of the three causes of deviation actually applies (including a combination, if any), thus making it easier for management to decide what needs to be done.

- iv. *Monitoring performance:* The goals and standards of performance, including tasks that have to be completed, set during the process of preparing the annual operating plan are there for a purpose. Because these are defined and assigned, they can be monitored.

The planner has a number of factors to consider when he designs a monitoring procedure.

- How far can he use existing set-ups (e.g. committees) for review and discussion?
- How far can the process of monitoring be delegated to line management?
- Should reporting be on a total or exception basis?
- The frequency of the monitoring procedure.
- Whether the feedback procedure should be formal or informal, written or verbal.
- How far the management information system has to be changed in order that it regularly provides data needed to measure progress?

In an organisation there may be managers who consistently fail to implement. It is up to the chief executive to deal with them, and he should be aware that failure to enforce some form of discipline will endanger all the planning efforts of the company. If no one appears to really care about implementation, the whole process of monitoring becomes an empty administrative exercise, and the plans themselves are debased.

- v. *Monitoring Assumptions:* It is evident that inherent in the process of corporate planning are certain basic assumptions regarding the environment which, it will be recalled, is changing, though its different segments will be changing at different rates.

One important aspect of control of plan is to continue to study and assess environmental trends so that the company may know whether the assumptions are still valid and correct. If there are fundamental changes, they may suggest that the plan should be reconsidered, or altered, or replaced with a contingency plan, as necessary.

- vi. *Updating and reconsideration of plans as required:* Usually, annual updating, as would evidently be necessary due to environment changes, is achieved through the system of rolling plan, dropping the year just ended from the corporate plan and adding another year at the end.

However, fundamental changes may have to be made outside the planning cycle, necessitated by such violent changes in environment that the normal modification achieved through the annual changes would be inadequate. This is made easier if the company has a contingency plan. Otherwise a total look at the planning process may be necessary.

Chapter 9

Strategy Formulation

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:

1. Should they eat the seeds by planning for large dividend payments, by selling off inventories, and by cutting back on research and development to improve the near-term profit picture, or by laying off workers during periods of slack demand?
2. 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

The ability of any business to operate in the long run depends on attaining an acceptable level of profits. Strategically managed firms characteristically have a profit objective usually expressed in earning per share or return on equity.

Productivity

Strategic managers constantly try to improve the productivity of their systems. Companies that can improve the input-output relationship normally increase profitability. Thus, businesses almost always state an objective for productivity. Number of items produced or number of services rendered per unit of input are commonly used. However, productivity objectives are sometimes stated in terms of desired decreases in cost. This is an equally effective way to increase profitability if unit output is maintained. For example, objectives may be set for reducing defective items, customer complaints leading to litigation, or overtime.

Competitive Position

One measure of corporate success is relative dominance in the marketplace. Larger firms often establish an objective in terms of competitive position to gauge their comparative ability for growth and profitability. Total sales or market share are often used; and an objective describing competitive position may indicate a company's priorities in the term. The company mission was described as encompassing the broad aims of organization. The most specific statement of wants appeared as the goals of the firm. However, these goals, which commonly dealt with profitability, growth, and survival, were stated without specific targets or time frames. They were always to be pursued but could never be fully attained. So, while they gave a general sense of direction, goals were not intended to provide specific benchmarks for evaluating the company's progress in achieving its aims. That is the function of objectives.

Employee Development

Employee value growth and career opportunities in an organization. With such opportunities, productivity is often increased and expensive turnover decreased. Therefore, strategic decision makers frequently include an employee development objective in their long-range plans. For example, PPG has declared in objective of developing highly skilled and flexible employees, thereby providing steady employment for a reduced number of workers.

Employee Relations

Companies activity seek good employee relations, whether or not they are bound by union contracts. In fact, a characteristic concern of strategic managers is taking proactive steps in anticipation of employee needs and expectations. Strategic managers believe productivity is partially tied to employee loyalty and perceived management interest in worker welfare. Therefore, strategic managers set objectives to improve employee relations. For example, safety programs, worker representation on management committees, and employee stock option plans are all normal outgrowths of employee relations objectives.

Technological Leadership

Businesses must decide whether to lead or follow in the marketplace. While either can be a successful approach, each requires a different strategic posture. Therefore, many businesses state an objective in terms of technological leadership. For example, Caterpillar Tractor Company, which manufactures large earth movers, established its early reputation and dominant position in the industry in being a forerunner in technological innovation.

Public Responsibility

Businesses recognize their responsibilities to customers and society at large. In fact, many actively seek to exceed the minimum demands made by government. Not only do they work to develop reputations for fairly priced products and services, but they also attempt to establish themselves as responsible corporate citizens. For example, they may establish objectives for charitable and educational contributions, minority training, public or political activity, community welfare, and urban renewal.

Qualities of Long-Term Objectives

What distinguishes a good objective from a bad one? What qualities of an objective improve its chances of being attained?

Perhaps the best answer to these questions is found in relation to seven criteria that should be used in preparing long-term objectives: acceptable, flexible, measurable over time, motivating, suitable, understandable, and achievable.

Acceptable

Managers are most likely to pursue objectives that are consistent with perceptions and preferences. If managers are offended by the objectives (e.g., promoting a non-nutritional food product) or believe them to be inappropriate or unfair (e.g., reducing spoilage to offset a disproportionate fixed overhead allocation), they may ignore or even obstruct achievement. In addition, certain long-term corporate objectives are frequently designed to be acceptable to major interest groups external to the firm. An example might involve air-pollution abatement efforts undertaken at the insistence of the Environment Protection Agency.

Flexible

Objectives should be modifiable in the event of unforeseen or extraordinary changes in the firm's competitive or environmental forecasts. At the same time, flexibility is usually increased at the expense of specificity. Likewise, employee confidence may be tempered because adjustment of a flexible objective may affect their job. One recommendation for providing flexibility while minimizing associated negative effects is to allow for adjustments in the level rather than the nature of an objective. For example, an objective for a personnel department "to provide managerial development training for 15 supervisors per year over the next five-year period" can easily be adjusted by changing the number of people to be trained. In contrast, changing the personnel department's objective after three months to "assisting production supervisors in reducing job-related injuries by 10 percent per year" would understandably create dissatisfaction.

Measurable

Objectives must clearly and concretely state what will be achieved and within what time frame. Numerical specificity minimizes misunderstandings; thus, objectives should be measurable over time. For example, an objective to "substantially improve our return on investment" would be better stated as "increase the return on investment on our line of paper products by a minimum of 1 percent a year and a total of 5 percent over the next three years."

Motivating

Studies have shown that people are most productive when objectives are set at a motivating level—one high enough to challenge but not so high as to frustrate or so low as to be easily attained. The problem is that individuals and groups differ in their perceptions of high enough. A broad objective that challenges one group frustrates another and minimally interests a third. One valuable recommendation is to develop multiple objectives, some aimed at specific groups. More sweeping statements are usually seen as lacking appreciation for individual somewhat unique situations. Such tailor-made objectives require time and involvement from the decision maker, but they are more likely to serve as motivational forces.

Suitable

Objectives must be suited to the broad aims of the organization, which are expressed in the statement of company mission. Each objective should be a step toward attainment of overall goals. In fact, objectives that do not coincide with company or corporate missions can subvert the aims of the firm. For example, if the mission is growth oriented, an objective of reducing the debt-to-equity ratio to 1.00 to improve stability would probably be unsuitable and counterproductive.

Understandable

Strategic managers at all levels must have a clear understanding of what is to be achieved. They must also understand the major criteria by which their performance will be evaluated. Thus, objectives must be stated so that they are understandable to the recipient as they are to the giver. Consider the potential misunderstandings over an objective "to increase the productivity of the credit card department by 20 percent within five years." Does this mean: Increases the number of cards outstanding? Increase the use of outstanding cards? Increase the employee workload? Make productivity gains each year? Or hope that the new computer-assisted system, which should automatically improve productivity, is approved by year five? As this simple example illustrates, objectives must be prepared in clear, meaningful, and unambiguous fashion.

Achievable

Finally, objectives must be possible to achieve. This is easier said than done. Turbulence in the remote and operating environments adds to the dynamic nature of a business's internal operations. This creates uncertainty, limiting strategic management's accuracy in setting feasible objectives. For example, the wildly fluctuating prime interest rates in 1980 made objective setting extremely difficult for 1981 to 1985, particularly in such areas as sales projections for consumer durable goods companies like General Motors and General Electric as shown in Exhibit 9.1 in a corporation the primary generator of strategic alternatives is the top manager, and in a suitable-SBU firm, the primary generators are the SBU top managers and the corporate top manager. Lower-level managers are involved to the extent that they prepare proposals for consideration by top managers. For instance, an R&D unit may propose that additional resources be allocated for the development of a new product. Top managers need to analyze these proposals, taking into account strategic considerations that are broader than the merits of any single project. Functional-level managers are also involved to the extent that plans to implement strategies are considered as part of the strategy formulation process, and strengths and weaknesses coming from functional levels are evaluated by these managers as inputs to the total process.

Whether dealing with corporate-or business- level strategy, there are four generic ways in which alternatives can be considered: stability, expansion, retrenchment, and combinations. These are options for the pace or level of effort in the current business definition, or for changing the mission. Exhibit 9.2 shows a matrix of these basic options with some representative examples of approaches for carrying out the strategy. That is, the firm may decide to change its business definition by expanding or retrenching the scope of its products, markets, or functions. If it chooses to maintain its definition, it still may alter its strategy by changing the pace of effort within the stable business definition in order to become more efficient or effective in the way it carries out its mission. Of course, combinations of options are possible at the same time or over time.

Strategists	Generate strategy alternatives	Analyse strategy alternatives
SBU-levels managers	Regularly	Regularly
Top managers	Regularly	Regularly
Corporate planners	Occasionally	Regularly
Board of directors	Rarely	Occasionally
Consultants	Occasionally hired to advise	Rarely
Functional-level managers	Prepare proposals	Regularly

Exhibit 9.1: The Role of Strategists In Considering Strategy Alternatives

	Expand		Retrench		Stabilize		Combinations Definition and/or pace
	Business Definition	Pace	Business Definition	Pace	Business Definition	Pace	
Products	Add new Products	Find new uses	Drop old products	Decrease product development	Maintain	Make package Changes, quality improvements	Drop old while adding new products
Markets	Find new Territories	Penetrate markets	Drop distribution channels	Reduce market shares	Maintain	Protect market shares, focus on market niches	Drop old Customers while finding new ones
Functions	Forward vertical integration	Increases capacity	Become captive company	Decreases process R&D	Maintain	Improve production efficiency	Increases capacity and improve efficiency

Exhibit 9.2: Matrix

For smaller firms, this business definition is simple enough. The product or service, market, and functions are usually limited to one category or a few categories. This is true for many medium-sized organizations as well. A majority of large firms are involved in multiple businesses. So their business definition is more complex.

Some firms are in so many businesses that it is hard if not impossible to describe the "business" they are in. In one study of three conglomerates (Litton, India Head, and Bangor Punta) it was found that their strategy making did not involve delineating specific businesses. Their definition of business involved only the specifications in detail of the corporate objectives in terms of growth rates, financial policies to guide their acquisition of funds and firms, and organizational policies.

Decisions regarding business definition and mission are made at the corporate level. Corporate-level strategies involve issues of which businesses to be in. Business-level strategies involve questions of what to do with those businesses—expand them, retrench them, or stabilize them. At the functional level within business units, alternative plans and policies are set forth to specify ways in which the strategies will be made to work. Thus corporate-level strategies alternatives revolve around the question of whether to continue or change the business (es) the enterprise is currently in. Business-level strategies alternatives involve improving the efficiency or effectiveness with which the firm achieves its corporate objectives in its chosen business sector.

The central strategies alternatives to consider are the following:

1. What is our business? What should it be? What business should we be in 5 years from now? 10 years?
2. Should we stay in the same business (es) with a similar level of effort? (stability)
3. Should we get out of this business entirely or some parts of it? (retrenchment)
4. Should we expand into new business areas by adding new functions, products, and/or markets? (expansion)
5. Should we carry out alternatives 3 and 4, 2 and 4, or 2 and 3? Simultaneously or sequentially? (combination)

Grand Strategies

Despite variations in implementing the strategies management approach, designers of planning systems generally agree about the critical role of grand strategies. Grand strategies, which are often called master or business strategies, are intended to provide basic direction for strategies actions. Thus, they are seen as the basic of coordinated and sustained efforts directed towards achieving long-term business objectives.

As theoretically and conceptually attractive as the idea of grand strategies has proved to be, two problems have limited use of this approach in practice. First, decision makers often do not recognize the range of alternative grand strategies available. Strategic managers tend to build incrementally from the status quo. This often unnecessarily limits their search for ways to improve corporate performance. Other executives have simply never considered the options available as attractive grand strategies.

Second, strategies decision makers may generate lists of promising grand strategies but lack a logical and systematic approach to selecting an alternative. Few planning experts have attempted to proffer viable evaluative criteria and selection tools.

The purpose of this section is therefore twofold: (1) to list, describe, and discuss 12 business-level grand strategies that should be considered by strategic planners and (2) to present approaches to the selection of an optimal grand strategy from available alternatives.

Grand strategies indicate how long-range objectives will be achieved. Thus, a grand strategy can be defined as comprehensive general approach that guides major actions.

Any one of the 12 principal grand strategies could serve as the basis for achieving major long-term objectives of a single business: concentration, market development, product development, innovation, horizontal integration, vertical integration, joint venture, concentric diversification, conglomerate diversification, retrenchment/turnaround, divestiture, and liquidation. When a company is involved with multiple industries, businesses, product lines, or customer groups-as many firms are-several grand strategies are usually combined. However, for clarity, each of these grand strategies is described independently in this section with examples to indicate some of their relative strengths and weaknesses.

Concentration

The most common grand strategy is concentration on the current business. The firm directs its resources to the profitable growth of a single product, in a single market, and with a single technology. Some of America's largest and most successful companies have traditionally adopted the concentration approach. Examples include W. K. Kellogg and Gerber Foods, which are known for their product; Shaklee, which concentrates on geographic expansion; and Lincoln Electric, which bases its growth on technological advances.

The reasons for selecting a concentration grand strategy are easy to understand. Concentration is typically lowest in risk and in additional resources required. It is also based on the known competencies of the firm. On the negative side, for most companies concentration tends to result in steady but slow increases in growth and profitability and a narrow range of investment options. Further, because of their narrow base of competition, concentrated firms are especially susceptible to performance variations resulting from industry trends.

Concentration strategies succeed for so many businesses-including the vast majority of smaller firms-because of the advantages of business-level specialization. By concentrating on one product, in one market, and with one technology, a firm can gain competitive advantages over its more diversified competitors in production skill, marketing know-how, customer sensitivity, and reputation in the marketplace.

A grand strategy of concentration allows for a considerable range of action. Broadly speaking, the business can attempt to capture a large market share by increasing present customers' rate of usage, by attracting competitors' customers, or by interesting nonusers in the product or service. In turn, each of these actions suggests a more specific set of alternatives are listed in the top section of Exhibit 9.3.

When strategic managers forecast that the combination of their current products and their markets will not provide the basis for achieving the company mission, they have two options that involve moderate cost and risk: market development and product development.

Market Development

Market development commonly ranks second only to concentration as the least costly and least risky of the 12 grand strategies. It consists of marketing present products, often with only cosmetic modifications, to customers in related market areas by adding different channels of distribution or by changing the content of advertising or the promotional media. Several specific approaches are listed under this heading in Exhibit 9.3. Thus, as suggested by the figure, businesses that open branch offices in new cities, states, or countries are practicing market development. Likewise, companies that switch from advertising in trade publications to newspaper or add jobbers to supplement their mail-order sales efforts are using a market development approach.

Concentration (increasing use of present products in present markets);

1. Increasing present customers rate of usage.
 - a. Increasing the size of purchase.
 - b. Increasing the rate of product obsolescence.

Contd...

- c. Advertising other uses.
- d. Giving price incentives for increased use.
- 2. Attracting competitors' customers.
 - a. Establishing sharper brand differentiation.
 - b. Increasing promotional effort.
 - c. Initiating price cuts.
- 3. Attracting nonusers to buy the product.
 - a. Including trial use through sampling, price incentives, and so on.
 - b. Pricing up or down.
 - c. Advertising new uses.

Market development (selling present products in new markets):

- 1. Opening additional geographical markets.
 - a. Regional expansion.
 - b. National expansion.
 - c. International expansion.
- 2. Attracting other market segments.
 - a. Developing products versions to appeal to other segments.
 - b. Entering other channels of distribution.
 - c. Advertising in other media.

Product development (developing new products for present markets):

- 1. Developing new product features.
 - a. Adapt (to other ideas, developments).
 - b. Modify (change color, motion, sound, odor, form, shape).
 - c. Magnify (stronger, longer, thicker, extra value).
 - d. Minify (smaller, shorter, lighter).
 - e. Substitute (other ingredients, process, power).
 - f. Rearrange (other patterns, layout, sequence, components).
 - g. Reverse (inside out).
 - h. Combine (blend, alloy, assortment, ensemble; combine units, purposes, appeals, ideas).
- 2. Developing quality variations.
- 3. Developing additional models and sizes (product proliferation).

Exhibit 9.3: Options under the Grand Strategies

Product Development

Product development involves substantial modification of existing products or creation of new but related items that can be marketed to current customers through established channels. The product development strategy is often adopted either to prolong the life cycle of current products or to take advantage of favorable reputation and brand name. The idea is to attract satisfied customers to new products as a result of their positive experience with the company's initial offering. The bottom section of Exhibit 3.3 lists some of the many specific options available to businesses undertaking product development. Thus, a revised edition of a college textbook, a new car style, and a second formula of shampoo for oily hair each represents a product development strategy.

Innovation

In many industries it is increasingly risky not to innovate. Consumer as well as industrial markets have come to expect periodic changes and improvements in the products offered. As a result, some businesses find it profitable to base their grand strategy on innovation. They seek to reap the initially high profits associated with customer acceptance of a new or greatly improved product. Then, rather than face stiffening competition as the basis of profitability shifts from innovation to production or marketing competence, they move on to search for other original or novel ideas. The underlying philosophy of a grand strategy of innovation in creating a new product life cycle, thereby making any similar existing products obsolete. Thus, this approach differs from the product development strategy of extending an existing product's life cycle. The automobile industry provides many excellent examples. Ford Motor Company's 1981 introduction of the sporty, economical, two-seater EXP was an effort to interest a segment of American drivers who traditionally bought foreign-made sports cars in trying a Ford product. This was an innovation strategy because a new life cycle had been started for Ford. At the same time, Ford modified the Fairmont to make it lighter and more fuel-efficient. This was a product development strategy since the Fairmont life cycle was extended.

While most growth-oriented firms appreciate the need to be innovative occasionally, a few companies use it as their fundamental way of relating to their markets. An outstanding example is Polaroid, which heavily promotes each of its new cameras until competitors are able to match technological innovation. By this time, Polaroid is normally prepared to introduce a dramatically new or improved product. For example, in short succession consumers were introduced to the Swinger, the SX-70, the one step, and the Sun Camera 660.

Few innovative ideas prove profitable because research, development, and premarketing costs incurred in converting a promising idea into a profitable product are extremely high. A study by the management research department of Booz Allen & Hamilton Inc. provides some understanding of the risks. As shown in Exhibit 9.4 Booz Allen & Hamilton Inc. studied 51 companies and found that less than 2 percent of the innovative projects initially considered eventually reached the marketplace. Specifically, out of every 58 new product ideas, only 12 pass an initial screening test that finds them compatible with the company's mission and long-term objectives. Only seven of these remain after an evaluation of their product potential, and only three survive actual attempts to develop the product. Two of these still appear to have profit potential after test marketing; but, on the average, only one will be commercially successful. In fact, other studies show this success rate to be overly optimistic. For example, the results of one research project disclosed failure rates for commercial products to be as high as 89 percent.

Horizontal Integration

When the long-term strategy of a firm is based on growth through the acquisition of one or more similar businesses operating at the same stage of the production-marketing chain, its grand strategy is called horizontal integration. Such acquisitions provide access to new markets for the acquiring firm and eliminate competitors. For example, Warner-Lambert Pharmaceutical Company's acquisition of Parke Davis reduced competition in the ethical drugs field for Chilcott Laboratories, a company Warner-Lambert had previously acquired. A second example is the long-range acquisition pattern of White Consolidated Industries, which expanded in the refrigerator and freezer market through a grand strategy of horizontal integration. In 1967 it acquired the Franklin Appliance Division of Studebaker, in 1978 it bought the Kelvinator Appliance Division of America Motors, in 1971 it acquired the Refrigerator Products Division of Bendix Westinghouse Automotive Air Brake, and finally in 1979 it bought Frigidaire Appliance from General Motors.

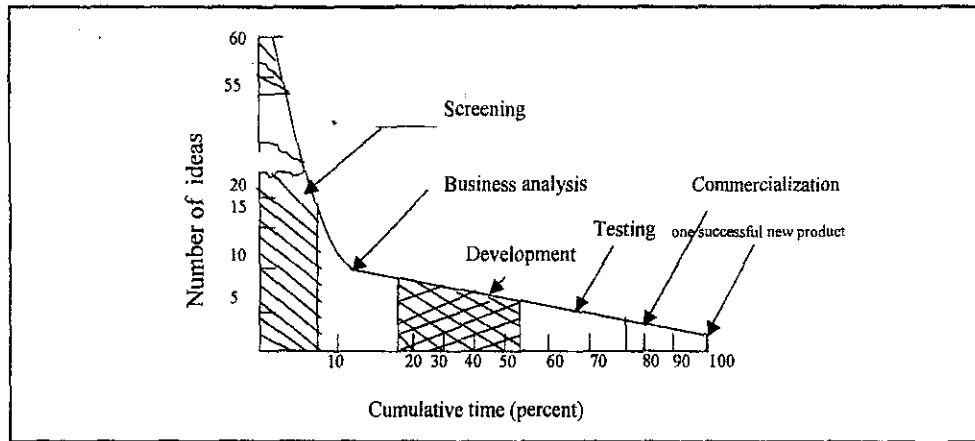


Exhibit 9.4: Decay of New Product Ideas (51 Companies)

Thus, the combinations of two textile procedures, two shirts manufactures, or two clothing store chains would be classified as horizontal integrations.

Vertical Integration

When the grand strategy of a firm involves the acquisition of businesses that either supply the firm with inputs (such as raw materials) or serve as a customer for the firm's outputs (such as warehouses for finished products), vertical integration is involved. For example, if a shirt manufacturer acquires a textile procedure-by purchasing its common stock, buying its assets, or through an exchange of ownership interests- the strategy is a vertical integration. In this case it is a backward vertical integration since the business acquired operates at an earlier stage of the production/ marketing process. If the shirt manufacturer had merged with a clothing store, it would have been an example of forward vertical integration-the acquisition of a business nearer to the ultimate consumer.

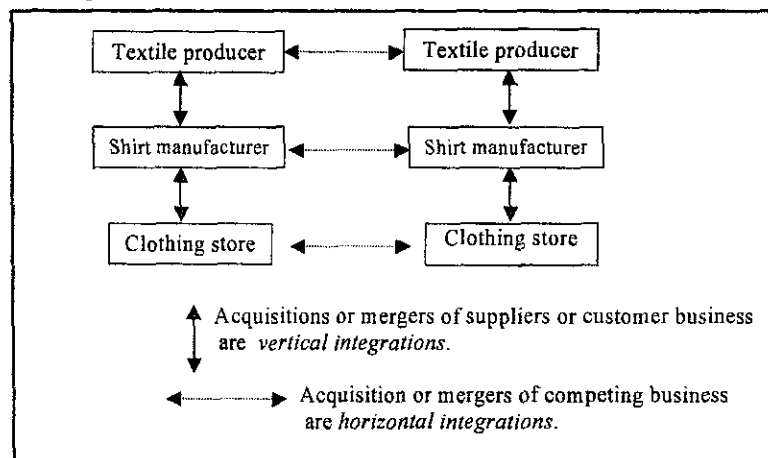


Exhibit 9.5: Vertical and Horizontal Integrations

Exhibit 9.5 depicts both horizontal and vertical integration. The principle attractions of a horizontal integration grand strategy are readily apparent. The acquiring firm is able to greatly expand its operations, thereby achieving greater market share, improving economies of scale, and increasing efficiency of capital usages. Additionally, these benefits are achieved with only moderately increased risk, since the success of the expansion is principle dependent on proven abilities. The reasons for choosing a vertical integration grand strategy are more varied and sometimes less obvious. The main reason for backward integration is the desire to increase the dependability of supply or quality of raw materials or

production inputs. The concern is particularly great when the number of suppliers is small and the number of competitors is large. In this situation, the vertically integrating firm can better control its costs and thereby improve the profit margin of the expanded production/marketing system. Forward integration is a preferred grand strategy if the advantages of stable production are particularly high. A business can increase the predictability of demand for its output through forward integration, that is, through ownership of the next stage of its production/marketing chain.

Some increased risks are associated with both types of integration grand strategies. For horizontally integrated firms, the risks stem from the increased commitment to one type of business. For vertically integrated firms, the risks result from expansion of the company into areas requiring strategic managers to broaden the base of their competencies and assume additional responsibilities.

Joint Venture

Occasionally two or more capable companies lack a necessary component for success in a particular competitive environment. For example, no single petroleum firm controlled sufficient resources to construct the Alaskan pipeline. Nor was any single firm capable of processing and marketing the volume of oil that would flow through the pipeline. The solution was a set of joint ventures. As shown in Exhibit 9.6, these cooperative arrangements could provide both the necessary funds to build the pipeline and the processing and marketing capacity to profitably handle the oil flow. The particular form of joint venture discussed above is joint ownership. In recent years it has become increasingly appealing for domestic firms to join foreign businesses through this form. For example, Bethlehem Steel acquired an interest in a Brazilian mining venture to secure a raw material source. The stimulus for this joint ownership venture was grand strategy, but such is not always the case. Certain countries virtually mandate that foreign companies entering their markets do so on a joint ownership basis. India and Mexico are good examples. The rationale of these countries is that joint ventures minimize the threat of foreign domination and enhance the skills, employment, growth, and profits of local businesses. One final note: Strategic managers in the typical firm rarely seek joint ventures. This approach admittedly presents new opportunities with risks that can be shared. On the other hand, joint ventures often limit partner discretion, control, and profit potential while demanding managerial attention and other resources that might otherwise be directed toward the mainstream activities of the firm. Nevertheless, increasing nationalism in many foreign markets may require greater consideration of the joint venture approach if a firm intends to diversify internationally.

Pipeline company (assets in Rs. millions)	Co-owner	Percent held by each
Colonial Pipeline Co. (Rs. 480.0)	Amoco	14.3
	Atlantic Richfield	1.6
	Cities Service	14.0
	Continental	7.5
	Philips	7.1
	Texaco	14.3
	Gulf	16.8
	Sohio	9.0
	Mobil	11.5
	Union Oil	4.0
Olympic Pipeline Co (Rs. 30.7)	Shell	43.5
	Mobile	29.5
West Texas Gulf Pipeline Co. (Rs. 19.8)	Texaco	27.0
	Gulf	57.7
	Cities Service	11.4
	Sun	12.6
	Union Oil	9.0
Texas-New Mexico Pipeline Co. (Rs. 30.5)	Sohio	9.2
	Texaco	45.0
	Atlantic Richfield	35.0
	Cities Service	10.0
	Getty	10.0

Exhibit 9.6: Typical joint ventures in the oil pipeline industry

Concentric Diversification

Grand strategies involving diversification represent distinctive departures from a firm's existing base of operations, typically the acquisition or internal generation (spin-off) of a separate business with synergistic possibilities counterbalancing the two businesses' strengths and weaknesses. For example, Head Ski initially sought to diversify into summer sporting goods and clothing to offset the seasonality of its snow business. However, diversifications are occasionally undertaken as unrelated investments because of their otherwise minimal resource demands and high profit potential.

Regardless of the approach taken, the motivations of the acquiring firms are the same:

Increase the firm's stock value. Often in the past, mergers have led to increases in the stock price and/or price-earnings ratio.

Increase the growth rate of the firm.

Make an investment that represents better use of funds than plowing them into internal growth.

Improve the stability of earnings and sales by acquiring firms whose earnings and sales complement the firm's peaks and valleys.

Balance or fill out the product line.

Diversify the product line when the life cycle of current products has peaked.

Acquire a needed resource quickly; for example, high-quality technology or highly innovative management.

Tax reasons, purchasing a firm with tax losses that will offset current or future earnings.

Increase efficiency and profitability, especially if there is synergy between the two companies.

When diversification involves the addition of a business related to the firm in terms of technology, markets, or products, it is a concentric diversification. With this type of grand strategy, the new businesses selected possess a high degree of compatibility with the current businesses. The ideal concentric diversification occurs when the combined company profits increase strengths and opportunities, as well as decrease weakness and exposure to risk. Thus, the acquiring company searches for new businesses with products, markets, distribution channels, technologies, and resource requirements that are familiar but not identical, synergistic but not wholly interdependent.

Conglomerate Diversification

Occasionally a firm, particularly a very large one, plans to acquire a business because it represents the most promising investment opportunity available. This type of grand strategy is commonly known as conglomerate diversification. This principle and often sole concern of the acquiring firm is the profit pattern of the venture. There is little concern given to creating product/market synergy with existing businesses, unlike the approaches taken in concentric diversification. Financial synergy is what is sought by conglomerate diversifiers such as ITT, Textron, American Brands, Litton, U. S. Industries, Fuqua, and I. C. Industries. For example, they may seek a balance in their portfolios between current businesses with cyclical sales and acquired businesses with counter cyclical sales, between high-cash/low-opportunity and low-cash/high-opportunity businesses, or between debt-free and highly leveraged businesses.

The principal difference between the two types of diversification is that concentric acquisitions emphasize some commonality in markets, products, or technology, whereas conglomerate acquisitions are based principally on profit considerations.

Retrenchment/Turnaround

For any of a large number of reasons a business can find itself with declining profits. Economic recessions, production inefficiencies, and innovative breakthroughs by competitors are only three causes. In many cases strategic managers believe the firm can survive and eventually recover if a concerted effort is made over a period of a few years to fortify basic distinctive competencies. This type of grand strategy is known as retrenchment. It is typically accomplished in one of two ways, employed singly or in combination:

1. Cost reduction. Examples include decreasing the work through employee attrition, leasing rather than purchasing equipment, extending the life of machinery, and eliminating elaborate promotional activities.
2. Asset reducing. Examples include the sale of land, buildings, and equipment not essential to the basic activity of the business, and elimination of "perks" like the company airplane and executive cars.

If the initial approaches fail to achieve the required reductions, more drastic action may be necessary. It is sometimes essential to lay off employee, drop items from a production line, and even eliminate low-margin customers.

Since the underlying purpose of retrenchment is to reverse current negative trends, the method is often referred to as a turnaround strategy. Interestingly, the turnaround most commonly associated with this approach is in management positions. In a study of 58 large firms, researchers Schendel, Patton, and Riggs found that turnaround was almost always associated with changes in top management. Bringing in new managers was believed to introduce needed new perspectives of the firm's situation, to raise employee morale, and to facilitate drastic actions, such as deep budgetary cuts in established programs.

Divestiture

A divestiture strategy involves the sale of a business or a major business component. When retrenchment fails to accomplish the desired turnaround, strategic managers often decide to sell the business. However, because the intent is to find a buyer willing to pay a premium above the value of fixed assets for a going concern, the term marketing for sale is more appropriate. Prospective buyers must be convinced that because of their skills and resources, or the synergy with their existing businesses, they will be able to profit from the acquisition.

The reasons for divestiture vary. Often they arise because of partial mismatches between the acquired business and the parent corporation. Some of the mismatched parts cannot be integrated into the corporation's mainstream and thus must be spun off. A second reason is corporation financial needs. Sometimes the cash flow or financial stability of the corporation as a whole can be greatly improved if businesses with high market value can be sacrificed. A third, less frequent reason for divestiture is government antitrust action when a corporation is believed to monopolize or unfairly dominate a particular market.

Although examples of grand strategies of divestiture are numerous, an outstanding example in the last decade is Chrysler Corporation, which in quick succession divested itself of several major businesses to protect its mission as a domestic automobile manufacturer. Among major Chrysler sales were its Airtemp air-conditioning business to Fedders and its automotive subsidiaries in France, Spain, and England to Peugeot-Citroen. These divestitures yielded Chrysler a total of almost Rs 500 million in cash, notes, and stock and, ratios that have recently pursued this type of grand strategy include Esmark, which divested Swift and Company, and White Motors, which divested White Farm.

Liquidation

When the grand strategy is that of liquidation, the business is typically sold in parts, only occasionally as a whole, but for its tangible asset value and not as a going concern. In selecting liquidation, owners and strategic managers of a

business are admitting failure and recognize that this action is likely to result in great hardships to themselves and their employees. For these reasons liquidation is usually seen as the least attractive of all grand strategies. However, as a long-term strategy it minimizes the loss to all stakeholders of the firm. Usually faced with bankruptcy, the liquidation business tries to develop a planned and orderly system that will result in the greatest possible return and cash conversion as the business slowly relinquishes its market share.

Combination Strategies

Essentially, combination strategies are a mixture of stability, expansion or retrenchment strategies applied either simultaneously (at the same time in different business) or sequentially (at difference times in the same business).

It would be difficult to find any organisation that has survived and grown by adopting a single 'pure' strategy. The complexity of doing business demands that different strategies be adopted to suit the situational demands made upon the organisation. An organisation which has followed a stability strategy for quite some time has to think of expansion. Any organisation which has been on an expansion path for long has to pause to consolidate its businesses. Multibusiness organisation-as most large and medium India companies are now-have to follow multiple strategies either sequentially or simultaneously.

Consider these cases of companies which have adopted multipronged strategies to deal with the complexity of the environment they face.

- The tube Investment of India (TI), a Murugappa group company, has created strategies alliances in its three major businesses: tubes, cycles, and strips. In cycles, it has entered into regional outsourcing arrangements with the UP based Avon (which we could term as co-operation, as Avon is TI's competitor in the cycle industry) and Hamilton Cycle in the western region. In steel strips, TI has entered into a manufacturing contract with Steel Tubes of India, Steel Authority of India, and the Jindals.
- Post-1996, the revival of Peerless General Finance and Investment Company, hinges on the rationalisation restructurings of its several businesses, like hotels, housing, hospitals, retailing, and travel, besides its mainline business as the country's largest private sector non-banking financial institution. The idea was to focus on its core competence of financial services. It placed emphasis on just three or four businesses. Two companies, Peerless Technologies and Peerless Shipping were divested. Tie-ups with several international companies to leverage the utilisation of its huge data base and models on the Indian rural sector was also on the cards.
- ITC decide to maintain a corporate portfolio consisting of four businesses: cigarettes, hotels and tourism, paperboards, and packing and printing. A turnaround strategy was adopted for the specialty paper business, Triveni Tissues, while the financial services and agri-business were to be divested.
- Pidilite Industries, the maker of Fevicol adhesives, contemplated expansion by related diversification through extension of its product portfolio across three business segments: adhesives and sealants, construction paints and chemicals, and art materials. It divested its specially chemicals business and acquired M-Seal from the Mahindras.

The examples offer just a glimpse of the constant moves that companies in India make in order to survive, grow, and be profitable.

Organisations do not depend on the strategy alone and evolve a complex network of combination strategies to deal with the changing environment. In fact, how to deal with, and adapt to, environment changes is what strategic management is all about.

It is easy to recognize that a complex network of strategies would have sequential as well as simultaneous strategies which have to be formulated to deal with the complexities of business.

Corporate Restructuring

Restructuring is a popular term and is used in different contexts. Let us first try to quickly understand the various meanings of the term 'restructuring' so that we do not confuse between the different usages of the term. Literature in management and allied discipline also uses other terms synonymous with restructuring, such as, revamping, regrouping, rationalisation, or consolidation.

Different Usages of the Term

When referred to at the global or country level, that is, the macro level, economic restructuring means the reform process used to make structural adjustments in the economy of a country, such as, reduction or phasing out of subsidies, dismantling of price controls, and other such actions. At the micro level, restructuring has three connotations: *corporate or business-level restructuring, financial restructuring, and organisational restructuring*. First, *corporate or business-level restructuring* means changes in the composition of a firm's set of businesses in order to create a more profitable enterprises. Within the firm, restructuring takes place in two forms. Financial restructuring deals with the changes in the equity pattern, equity holdings and crossholding pattern, debt-servicing schedule, and the like. Organisational restructuring deals with changes in the structure of the organisation (i.e., the organogram), reducing hierarchies or delayering, reducing the number of employees or downsizing, redesignating positions and altering reporting relationships.

Here, we are only concerned with corporate-or business-level restructuring, that is, with the business portfolio changes that firms undertake in order to either deal with the problems they face or to create a more profitable enterprise. Business portfolio changes could deal to the firm acquiring some businesses.

Rationale for Restructuring

We could try to understand the rationale for restructuring at two levels. The first is a deeper level reasoning relating to the fundamental ways in which organisation work. The second is a more practical reasoning that attempts to analyse the changes in the environment and the organisation, and relate such changes to strategies action that organisations need to take.

Peter Drucker states that organisations have to implicit or explicit 'theories' for their business, incorporating assumptions about:

- (a) the environment, specifically markets, customers, and important technologies
- (b) the mission or purpose
- (c) core (content) competencies required to fulfill the mission

Drucker further states that these assumptions must be realistic, congruent, communicated and understood. These assumptions need to be evaluated regularly and rigorously so that they prove to be correct.

In the course of functioning, managers within organisations create mental models about the ways of doing business. Mental models, according to Walsh, "represent the knowledge managers have about the industry and the organisation, and how specific actions relate to desired outcomes". The 'assumptions' of Drucker and the 'mental models' of Walsh are derived experiences with past successes and failures contributing to the overall picture. As long as these assumptions and mental models do not change they are a useful basis for further managerial decision making and strategic

management. But as soon as changes occur, these turn out to be of little value. Rather, these may prove to be harmful if managers insist on sticking to them. Since change is a fact of life, it follows that the assumptions and mental models also need to be revised continually. Restructuring is the result of such a continual revision.

Environmental changes, such as the ones we are witnessing around the world and in India, are causing organisations to revise their assumption and mental models. It is for this reasons that restructuring is being done at various levels so that organisations and the strategies they employ are aligned with the environmental realities.

The second way to understand the rationale for restructuring is to note that, in the past, diversification had been the preferred route for growth and expansion for companies around the world. In the U.S. diversification began in the 1960s and lasted until the early 1980s, resulting in several overdiversified conglomerates. Contemporary Indian companies, mostly belonging to the family business groups and multinational subsidiaries, also diversified owing to the limitations imposed on expanding in one or a few sectors by the licensing and regulatory systems. But international level economic and geopolitical changes led to a spree of economic reforms around the world. The composition and natures of markets also changed causing the organisations to make an intense assessment and reorientation of their assumptions and mental models. It was clear that these would no longer work in the emerging environmental context. What was needed was a new set of assumptions and mental models that are synchronised with the context in which organisations functions now. Hence the need to realign to as restructuring. Often, such restructuring is done through a combination of expansion strategies (intensification, cooperation), and retrenchment strategies of turnaround and divestment. Overdiversification is sought to be reversed by downscoping, which involves reducing the scope of diversification by divestment on non-core businesses and creating a focused organisation.

Looking at the contemporary Indian context what we find is that most companies are in the throes of intense change. More often we find the older companies restructuring as these were the one which had overdiversified in the first case. Newer companies, set up in the 1990s and in the new millennium, do not find much need for restructuring. But this does not mean that these companies can afford to be complacent. They too need to be on their guard and continually assess the assumptions and mental models they use to devise their organisations and strategies.

Reasons for Pursuing Stability Strategy

1. The firm is doing well or perceivers itself as successful. Management does not always know what combinations of decisions is responsible for this. So "we continue the way we always have around here".
2. A stability strategy is less risky. A high percentage of changes fail, whether we are talking about new products or new ways of doing things. So conditions must be really bad (or opportunities good) if a firm decides to take the additional risk. The larger the firm and the more successful it has been, the greater is the resistance to the risk.
3. Managers prefer action to thought. A stability strategy can evolve because the executives never get around to considering any other alternatives. Many of the firms that pursue this strategy do unconsciously. They react to forces in the environment and will change their business definition only in extraordinary times.
4. It is easier and more comfortable for all concerned to pursue a stability strategy. No disruptions in routines take place.
5. The environment is received to be relatively stable, with few threats to cause problems or few opportunities the firm wishes to take advantage of.
6. Too much expansion can lead to inefficiencies. In effect, many decision makers do not perceive a significant gap between the future level of goal attainment they expect to reach and their ideal objectives.

A firm's executives may also believe that resources of other environmental changes prohibit the continuation of expansion in the business definition that may have occurred in the past. Here the analysis could suggest that continued expansion could actually increase the performance gap. Thus stability in the pace of activity becomes desirable. Executives may realize that the consequences of expansion could become dysfunctional. For instance, expansion (for example, by some types of acquisitions) could lead to antitrust pressure from government or attacks from competitors or pressure groups. Or the firm may need a breathing spell. It may have expended so fast that it must stabilize for a while or else become inefficient and unmanageable. Its costs may have gotten out of hand, especially if it appears that hard times are coming. This is a particularly difficult problem for aggressive entrepreneurs of successful small firms which have been expanding rapidly.

Stability is not the kind of strategy that makes news. It is news to say that 8 million are unemployed, and it is not news to write about 110 million employed. So articles and research usually do not focus on this strategy. However, we should have to infer that since most firms pursued this strategy at some point, stability is effective when the firm is doing well and the environment is not excessively volatile. This means that for many industries and many companies and SBUs, the stability strategy is effective. As one owner of a successful private firm put it. "I have only one egg in my basket and I watch that basket very carefully."

Reasons for Pursuing Expansion Strategies

After reading the list of reasons for pursuing the stability strategy, it may be hard to imagine reasons for adopting an expansion strategy. Stability has a number of things going for it.

The reasons given for adopting expansion are as follow:

1. In volatile industries, a stability strategy can mean short-run success, long-run death. So expansion may be necessary for survival if environments are volatile.
2. Many executives equate expansion with effectiveness.
3. Some believe that society benefits from expansion.
4. Managerial motivation. It is true that there is less risk with stability. But there are also fewer financial and other rewards. There are many managers who wish to be remembered, who wish to leave a monument to themselves in the workplace. Who remembers the executive who stood at the helm for 5 years "steady as it goes"? Strategies may result from the power needs of many executives; the recognition needs are strong in these executives too. Thus the needs or drives encourage some executives to gamble and choose a strategy of expansion. Their companies also become better known, may attract better management, and often leads to higher pay.
5. Belief in the experience curve. There is some evidence that as a firm grows in size and experience, it gets better at what it's doing and reduces costs and improves productivity.
6. Belief that growth will yield monopoly power.
7. External pressure from stockholders or securities analysts.

Perhaps the major reason for its popularity is the belief that rapid environmental change requires expansion. Further, there is a belief and some evidence that expansion results in performance improvements. However, some suggest that volatility is not as great as it seems, and other prescribe stability to avoid overreaction to change. Also, critics of expansion point to firms "engulfed in a growth syndrome"- expansion at any cost- which they believe leads to inefficiencies and a lower quality of life due to harm from the environment.

Reasons for Pursuing Retrenchment Strategy

The strategy is the hardest to pursue; it goes against the grain of most strategists. It implies failure. Just as most business executives hate to cut price, they hate a retrenchment strategy. Who do they follow it, then? A few reasons are as follow:

1. The firm is not doing well or perceives itself as doing poorly.
2. The firm has not met its objectives by following one of the other generic strategies, and there is pressure from stockholders, customers, or other to improve performance.
3. The environment is seen to be so threatening that internal strengths are insufficient to meet the problems.
4. Better opportunities in the environment are perceived elsewhere, where a firm's strengths can be utilized.

Any strategy, if chosen at the right time and implemented properly, will be effective. However, the retrenchment strategy tends to be reserved for dealing with crises, even though there can be positive reasons for its use. The retrenchment strategy is the best strategy for the firm which has tried everything, has made some mistakes, and is now ready to do something about its problems. The more serious the crisis, the more serious the retrenchment strategy needs to be. For minor crises, pace retrenchment will do. For moderate crises, divestiture of some divisions or units may be necessary. For serious crises, a liquidation may be necessary. Exhibit 9.6 describes a firm which believes that its crisis is serious enough to warrant a retrenchment in pace, which could lead to liquidation.

The retrenchment strategy is the hardest strategy for the business executives to follow. It implies that someone or something has failed, and no one wants to be labeled a failure. But retrenchment can be used to reverse the negative trends and set the stage for more positive strategic alternatives. Many U. S. business firms began withdrawing from Europe in the early 1980s due to the stubborn recession, high labor costs, high taxes, and competition from government-subsidized industries. And in the mid-1980s many conglomerates began "asset redeployments" to get out of old businesses and into new ones, or to get back to basics.

Foreign managers appear more willing to consider retrenchment than U. S. managers. The first question the Japanese, German, or French strategies asks is likely to be "What are the old things we are going to abandon?" This provides resources for innovation, new products, or new markets.

Reasons for Pursuing Combination Strategy

A combination strategy is not an easy strategy to use. It is much easier to keep a firm in one set of values or one strategy at a time. But when a company faces many environments and these environments are changing at different rates, and the company's products are in different stages of the life-cycle, it is easy to visualize conditions under which a combination strategy makes sense.

Thus it is possible that when the economy is performing well, most industries are doing well. Therefore, the generic strategy might be expansion. But at the start of a combination strategy makes sense for a multiple-industry firm at that time.

In the case of time-phased combination strategies, several scenarios come to mind. For example, a firm realize that some of its main product lines are beyond the optimum point in the product life cycle and that it is not worth the investment to "prop the product up". The firm may choose to retrench in this area and follow an expansion strategy in a new product area.

Most large firms such as Fortune's 500 largest industrials are probably the most frequent users of combination strategies. Even here, it is the multiple-industry firm that is most likely to use them. The medium-sized firm that is

multiple-industry-based is also a likely user. An example is NCR, which sold a unit to buy back some debt and then expanded.

All strategies can be effective. The question is, When is a combination strategy most likely to be effective? What should have become clearer in this section is that combination strategies are most likely to be effective for larger, multiple-SBU firms in periods of economic transition or periods of transition in the product service life cycle. The combination strategy is the best strategy for a firm whose divisions perform unevenly or do not have the same future potential.

Relationship of Different Strategies

The exhibit 9.7 graphically presents the alternatives which are possible and each dimension represent on overlay so that they all intersect one another. That is, expansion, stability, or retrenchment can be applied to products, markets, or functions. And combinations of these are possible. If change occurs, it may be in the pace or the business definition. Our intent is to convey the idea that there is overlap in how these strategies approaches can be put together for any given firm. The particular configuration of alternatives considered by any firm will not be this large, however. Managers are more likely to focus on a few of these for a detailed analysis.

Second, keep in mind that any alternative or combination has the potential to improve performance. One is not necessarily superior to another in all circumstances. Naturally, if substantial growth in size is the objective, expansion is a more likely alternative. But this may come at the expense of other objectives, at least in the short run. Growth in profits could be enhanced by a retrenchment. For instance, financial theory suggests that if the net present value of a liquidation is greater than the expected value of continued operations, selling assets to gain funds to invest elsewhere will be a good alternative for the goal of improving cash value. The breakup value of some firms may be large due to "hidden" assets or unrealistic book values. So retrenchment may ultimately lead to growth (in terms of cash goals). Some tax laws give companies a reason to spin off subsidiaries to shareholders or sell assets and distribute proceeds, because companies liquidated within a year of an asset sale are exempt from taxation on related capital gains. Of course, such tax laws can change, and analysis of these laws should be an integral part of environmental analysis. If an entrepreneur's objective is to maintain control of a business, stability may enhance this more than expansion. If the goal is to spread risk, business definition changes may be in order. Thus it is inappropriate to necessarily equate "growth" with "expansion". And retrenchment should not be considered a sign of failure or pursued only when threats appear. Stability does not imply that goal improvements are not being accomplished. In other words, don't confuse the strategy, as a means to an end, with the objective.

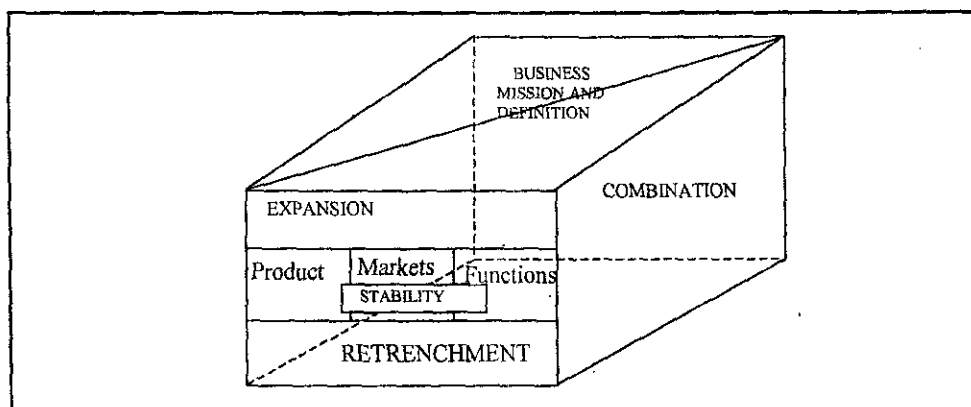


Exhibit 9.7: Overlays of Strategy Alternatives

Selection of Long-Term Objectives and Grand Strategy Sets

At first glance the strategic management model, which provides the framework for study throughout this book, seems to suggest that strategic choice decision making leads to the sequential selections of long-term objectives and grand strategy. In fact, however, strategic choice is the simultaneous selection of long-range objectives and grand strategy. When strategic planners study their opportunities, they try to determine which are most likely to result in achieving various long-range objectives. Almost simultaneously they try to forecast whether an available grand strategy can be met. In essence, then, three distinct but highly interdependent choices are being made at one time. Usually several triads or sets of possible decisions are considered.

A simplified example of this process is shown in Exhibit 9.10. In this example the business has determined that six strategic choice options are available. These options stem from three different interactive opportunities (e.g., West Coast markets) that present little competition. Because each of these interactive opportunities can be approached through different grand strategies- in option 1 and 2 they are horizontal integration and market development- each offers the potential for achieving long-range objectives to varying degrees. Thus, a business can rarely make a strategic choice only on the basis of its preferred opportunities, long-range objectives, or grand strategy. Instead, the three elements must be considered simultaneously because only in combination do they constitute a strategic choice.

In an actual decision situation the strategic choice would be complicated by a wider variety of interactive opportunities, feasible company objectives, promising grand strategy option, and evaluative criteria. Nevertheless, Exhibit 9.8 does partially reflect the nature and complexity of the process by which long-term objectives and grand strategy are selected.

	Six strategic choice options					
	1	2	3	4	5	6
Interactive opportunities	West Coast markets present little competitions		Current markets sensitive to price competition		Current industry product lines offer too narrow a range of markets	
Appropriate long-range objectives (limited sample): average 5-years ROI Company sales by year 5 Risk of negative profit	15% +50% .30	19% +40% .25	13% +20% .10	17% +0% .15	23% +35% .20	15% +25% .05
Grand strategies	Horizontal integration	Market development	Concentration	Selective retrenchment	Product development	Concentration

Exhibit 9.8: A Practical of Strategic Choice Options

Sequence of Objectives and Strategy Selection

The selection of long-term objectives and grand strategies involves simultaneous rather than sequential decisions. While it is true that objectives are needed so that the company's direction and progress are not determined by random forces, it is equally true that objectives are valuable only if strategies can be implemented, making achievement of objectives realistic. In fact, the selection of long-term objectives and grand strategies is so interdependent that until the 1970s most business consultants and academicians did not stress the need to distinguish between them. Most popular business literature and practicing executives still combine long-term objectives and grand strategies under the heading of company strategy.

However, the distinction has merit. Objectives indicate what strategic managers want but provide few insights as to how this will be achieved. Conversely, strategies indicates what type of actions will be taken but do not define what ends will be pursued or what criteria will serve as constraints in refining the strategic plan.

The latter view of objectives as constraints on strategy formulation rather than as ends towards which strategies are

directed is stressed by several prominent management experts. They argue that strategic decisions are designed (1) to satisfy the minimum requirements of different company groups, for example, the production department's need for more inventory capacity, or the marketing department's need to increase the sales force and (2) to create synergistic profit potential given these constraints.

Does it matter whether strategic decisions are made to achieve objectives or to satisfy constraints? No, because constraints are objectives themselves. The constraints of increased inventory capacity is a desire (an objective), not a certainty. Likewise, the constraints of a larger sales force does not assure that it will be achieved given such factors as other company priorities, labor market conditions, and the firm's profit performance.

Business-level Strategies

Business strategies are the courses of action adopted by a firm for each of its businesses separately to serve identified customer groups and provide value to the customer by a satisfaction of their needs. In the process the firm uses its competencies to gain, sustain, and enhance its strategic or competitive advantage.

The source of competitive advantage for any business operating in an industry arises from the skillful use of its core competencies. These competencies are used to gain a competitive advantage against rivals in an industry. Competitive advantage results in above-average returns to the company. Business needs a set of strategies to secure competitive advantage.

Michael E Porter is credited with extension pioneering work in the area of business strategies or, what he calls, *competitive strategies*. His writing in the form of books, research papers, and articles have deeply influenced contemporary thinking in the area of industry analysis, competitive dynamics, and competitive strategies. He is also considered a major proponent of the positioning school of strategy thought. We have adopted the approach he suggested by him in order to discuss the different aspects related to business strategies in this chapter.

First of all, let us see what Porter has to say about competition. He believes that the basic unit of analysis for understanding competition is the industry, which, according to him, is a group of competitors producing products or services that compete directly with each other. It is the industry where competitive advantage is ultimately won or lost. Through competitive strategy, the firms attempt to define and establish an approach to compete in their industry.

The dynamic factors that determine the choice of a competitive strategy, according to Porter, are two, namely, the industry structure, and the positioning of a firm in the industry.

Industry structure, according to Porter, is determined by the competitive forces. These forces are five in number: the threat of new entrants; the threat of substitute products or services, the bargaining power of suppliers, the bargaining power of buyers, and the rivalry among the existing competitors in an industry. We will go into the details of structural analysis of industries in the next chapter. Suffice it to say here that these five forces vary industry to industry, that is, every industry has a unique structure and these factors determine the long-term profitability of firms in an industry.

The second factor that determines the choice of a competitive strategy of a firm is its positioning within the industry. Porter terms positioning as the firm's overall approach to competing. It is designed to gain sustainable competitive advantage and is based on two variables: the competitive advantage and the competitive scope. Competitive advantage can arise due to two factors: lower cost and differentiation. Competitive scope can be in terms of two factors: lower cost and differentiation. Competitive scope can be in terms of two factors: broad target and narrow target.

In order to understand competitive positioning, we can visualise a situation in which a firm has to compete in a market with other rival firms. One type of positioning approach may be to offer mass-produced products distributed through mass-marketing thereby resulting in a lower cost per unit. The other type of positioning approach could be marketing relatively higher-priced products of a limited variety but intensely focussed on identified customer groups who are

willing to pay the higher price. These are produced through batch production and marketed through specialised distribution channels. What the firm does is to differentiate its products or services on some tangible basis from what its rivals have to offer so that the customer purchases the products even at a premium.

What these approaches show is that there is an overall approach to competing within an industry which is consciously by a firm. These approaches are termed as the two generic types of competitive advantages that a firm could plan for: the lower-cost approach and the differentiation approach. According to Porter, lower-cost is based on the competence of a firm to design, produce, and market a comparable product more efficiently than its competitors. Differentiation is the competence of the firm to provide unique and superior value to the buyer in terms of product quality, special features, or after-sales service.

Apart from competitive advantage, the other factor is the competitive scope which Porter defines as the breadth of a firm's target within its industry. By the breadth of a firm's target is meant the range of products, distribution channels, types of buyers, the geographic areas served, and the array of related industries in which the firm would also compete. The basic reason why competitive scope is important is that industries are segmented, have differing needs, and require different sets of competencies and strategies to satisfy the needs of customers.

In order to understand competitive scope, once again one could visualise a firm competing in a market with other rival firms. Here the firm can choose a range of products to offer, the customers groups to cater to, the distribution channels to employ, and the geographical areas to serve. Depending on the scale of a firm's operations, we could say that the firm can either adopt a broad-target approach or a narrow-target approach. Under broad targeting, the firm can offer a full range of products/services to a wide range of customer groups located in a widely-scattered geographical area. Under narrow targeting, the firm can choose to offer a limited range of products/services to a few customer groups in a restricted geographical area.

When the two factors of positioning—the competitive advantage and competitive scope—are combined, what results is a set of generic competitive strategies. These are what are known as the business-level strategies.

Tactics for Business Strategies

A tactic is a sub-strategy. It is a specific operating plan detailing how a strategy is to be implemented in terms of when and where it is to be put into action. By their nature, tactics are narrower in their scope and shorter in their time horizon than are strategies. We shall consider here the two tactics of timing (when) and market location (where) used in formulating and implementing business strategies.

Timing Tactics

When to make a business strategy move is often as important as what move to make. It is here that the timing of the application of a business strategy becomes important. A business strategy of low-cost or differentiation may be essentially a right move but only if it is made at the right time.

The recognition of time as a strategic weapon and a source of strategic advantage came about in the late-1980s as a result of the ideas proposed by George Stalk Jr., the head of innovation and marketing at the Boston Consulting Group.

The first company to manufacture and sell a new product or service is called the pioneer or the first-mover firm. The firms which enter the industry subsequently are late-mover firms. Sometimes an intermediate category of second-movers is also considered to include those firms which reach immediately to the first-movers. Each industry has its first-movers, second-movers and late-movers. Our discussion here will, however, be limited to the first-movers and the late-movers. Our discussion here will, however, be limited to the first-movers and the late-movers only.

second-movers, howsoever quick they might be to react, are in any case late-movers.

Consider the example of Parle which is the first mover in the mineral water industry in India which has attracted companies, such as, Coca Cola (with the Kinley brand) and Pepsi (with the Aquafina brand). Parle has dominated a major share of the mineral water market leading to its Bisleri brand becoming generic to the product category. A case of a late-mover in this industry is nestle which planned to introduce its brand Pure Life by the end of 2000. Likewise, in the mutual funds industry, Unit trust of India (UTI), set up in 1964, is the first-mover with a clear lead of several years over other mutual funds in the public and private sectors. IIM Ahmedabad is the first-mover in the autonomous institutions segment in the management education industry.

Being the first mover does not always constitute an advantage. UTI might be the first-mover but there are many number of late-movers, such as, the Kotak Mahindra group, which have posed a stiff challenge to it. Similarly, the Indian School of Business at Hyderabad is likely to challenge the dominant position of the IIMs. Late-movers such as ICICI-Prudential Life Insurance, HDFC Standard Life Insurance, and Max New Life Insurance are likely to make life difficult for the first-mover Life Insurance Corporation (LIC) of India.

There are advantages and disadvantages associated with being the first-mover or late-mover. Often the advantages of one type are the disadvantages for the other. This means that the advantages enjoyed by the late-movers can be disadvantages for the first-mover firms.

First let us see the advantages that might accrue to the first-mover firms.

1. They can establish a position as the market leaders. They can establish business models and gain valuable experiences that can enable them to reap the benefits of a learning curve that can help them in assuming cost leadership.
2. Moving first in an industry results in forming early commitments to suppliers of raw materials, new technology, and distribution channels creating cost advantages over late-movers.
3. They develop an image of being pioneers which helps to build image and reputation. First-movers create standards in different areas for all subsequent products and services in the industry.
4. Moving first constitutes a pre-emptive strike and creates lead for the first-movers. For the late-movers, imitation may be difficult and risky.
5. First-time customers are likely to remain loyal.

The disadvantages of being a first mover are listed below. Note that these may be the advantages for the late-movers.

1. Being a pioneer is often costlier than being a follower. Pioneering firms have to spend resources on creating customer awareness and education regarding the products, specially if these are new products. Late-movers face lesser risks when the markets are already developed.
2. Late-movers can imitate technological advances, skills, know-how and marketing approaches easily negating the advantages that first-movers are likely to have.
3. Technological change is often rapid creating obsolescence for the first-movers. Late-movers can jump the technological thresholds and use the latest technology available.
4. Customer loyalty is not guaranteed and can often prove to be ephemeral. Late-movers can snatch the market share from the first-mover. If the first-movers have to retain market share and customer loyalty then additional efforts have to be put in.

The advantages and disadvantages for a first-mover show that good timing is important. But advantages cannot just flow to the first-movers. In case conditions are conducive to being a first-mover, then what matters are the strategies, positioning, and entry barriers that the first-mover firm is able to create. It is not always that a firm has to be a first-mover even if it has the opportunity. Smart late-movers can overturn the apple-cart and beat the first-movers at their own game. Sometimes fence-sitting till some other firm has tested the waters in an industry may be a prudent business strategy than jumping straight away in order to be the first-mover. Late-movers can succeed if they have the staying power, can learn from the mistakes of the first movers and fine tune their business tactics accordingly.

Market Location Tactics

The second important aspect of business tactics is market location. This aspect deals with the issue of where to compete. By this is meant the target market the firm aims at while applying its business strategies. Every industry has a number of firms that offer the same or substitute products or services. The total market share in an industry is carved up by these firms. One firm has the largest market share, some others firms have a relatively larger market share, a few others have a small market share, and there are firms that operate only on the fringes and not in the mainstream markets.

Market location could be classified according to the role that firms play in the target market and the types of business tactics they adopt to play such a role. We have adopted the classification of market location tactics provided by the marketing guru, Philip Kotler. He terms these tactics as competitive strategies. We expect that you have studied these strategies in your marketing management courses and so we will only review them here. It would be helpful if you review your marketing text as you read further.

On the basis of the role that firms play in the target market, market location tactics could be of four types: *leader*, *challenger*, *follower*, and *nichers*. As you will note, the essence of these tactics has been derived from military science. This is understandable since the competitive industries are virtual battlefields for competing firms. At this point let us recall that the term strategy too is a gift to management studies from military science. A brief description of the four types of market location tactics follow below.

1. **Market leaders** are firms that have the largest market share in the relevant product market and usually lead the industry in factors, such as, technological developments, product and service attributes, price benchmarks, or distribution channel design. In order to take up the market leader position and to retain it, Kotler proposes these three strategies (we would prefer to call these 'approaches' to distinguish these from 'strategy' which has a much broader meaning for us in business policy and strategic management):
 - Expanding the total market through new users, new uses, and more usage
 - Defending the market share through position defense, flank defense, counteroffensive defense, mobile defense and contraction defense
 - Expanding the market share through the enhancement of operational effectiveness by means of new product development, raising manufacturing efficiency, improving product quality, providing superior support services, or increasing marketing expenditure.
2. **Market challengers** are firms that have the second, third or lower ranking in the industry. These firms can either challenge the market leaders or choose to follow them. When they seek to challenge the market leader they do so in the hope that they would be able to gain the market share. The tactics adopted by the market challenger have several components. First, the challenger has to define the objective and the opponents, choose a general attack strategy, and then choose a specific attack strategy. The most common objective of the challenger is to increase the market share, but it could also have a somewhat devious aim, say to drive the opponent out of the industry. A general attack strategy could be of five types:

- Frontal attack involving matching the opponent in terms of the product, price, promotion, and distribution
 - Flank attack involving challenging the opponent's weak or uncovered geographical or segmental areas
 - *Encirclement attack* involving a grand move to capture the opponent's market share through means, such as, launching an advertising blitzkrieg, making an unbeatable product-related offering, or presenting a unique service guarantee
 - *Bypass attack* involving ignoring the opponent and attacking the easier markets by means of diversifying into unrelated products, moving into new geographical areas or leapfrogging into new technologies.
 - *Guerrilla attack* involving small, intermittent attacks to harass and demoralise the opponent firm, and eventually secure a firm foothold in the industry. This could be done by means of price cuts, price discounts, intensive comparative advertising, or initiating legal action.
3. **Market followers** are firms that imitate the market leaders but do not upset the balance of competitive power in the industry. They prefer to avoid direct attack, keep out of the way of other firms, and reap the benefits of the innovations made by the market leaders through imitation. The market follower may adopt four broad strategies as under.
- *Counterfeiter strategy* involving duplicating the market leader's product and packaging and selling it in the black market.
 - *Cloner strategy* involving emulating the market leader's products, name, and packaging
 - *Imitator strategy* involving copying some things from the market leader while retaining some other features, such as, pricing, a packaging or advertising
 - *Adapter strategy* involves adapting one's own products to those of the market leader and selling them in different markets
4. **Market nichers** are firms that carve out a distinct niche for themselves, which has been left uncovered by the other firms in the industry, or a niche that is of little or no interest to others. The niche strategies are akin to the 'focus' business strategies as they target a market position that is small and unique and requires special competencies in order to be served. There are several means by which the specialization for serving a niche market can be developed. Excelling in providing a special product or service attribute, serving a distinct geographical area, or offering customised products or services to a select group of customers are some such means. Market niche strategies carry the risks that we have identified for focus business strategies. For instance, a market leader may choose to expand its own market coverage to serve a niche thereby negating the advantages enjoyed by the market nicher. Market nichers have to adopt three strategies which are as under.
- *Creating niches* involves looking for ways and means by which niches can be identified or created in an industry.
 - *Expanding niches* involves enhancing the coverage of the present niche to include similar market niches or new niches.
 - *Protecting niches* involves shielding the niches served from attacks by other firms in the industry.

Chapter 10

Strategy Analysis and Choice

Strategies analysis and choice largely involves making subjective decisions based on objective information. The chapter introduces important concepts that can help strategists generate feasible alternatives, evaluate those alternatives, and choose a specific course of action. Behavioral aspects of strategy formulation are described, including politics, culture, ethics, and social reasonability considerations. Modern tools for formulating strategies are described, and the appropriate role of a board of directors is discussed.

As indicated by the shaded portion of Exhibit 10.1 this section focuses on establishing long-term objectives, generating alternative strategies, and selecting strategies to pursue. Strategy analysis and choice seeks to determine alternative course of action that could best enable the firm to achieve its mission and objectives. 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.

Unless a desperate situation faces the firm, alternative strategies will likely represent incremental steps to move the firm from its present position to a desired future position. For example, Kindercare Learning Centers has a strategy to open one hundred new centers this year, thus expanding from current markets into new areas. Alternative strategies do not come out of the wild blue yonder; they are derived from the firm's mission, objectives, external audit, and internal audit; they are consistent with, or build upon, past strategies that have worked well!

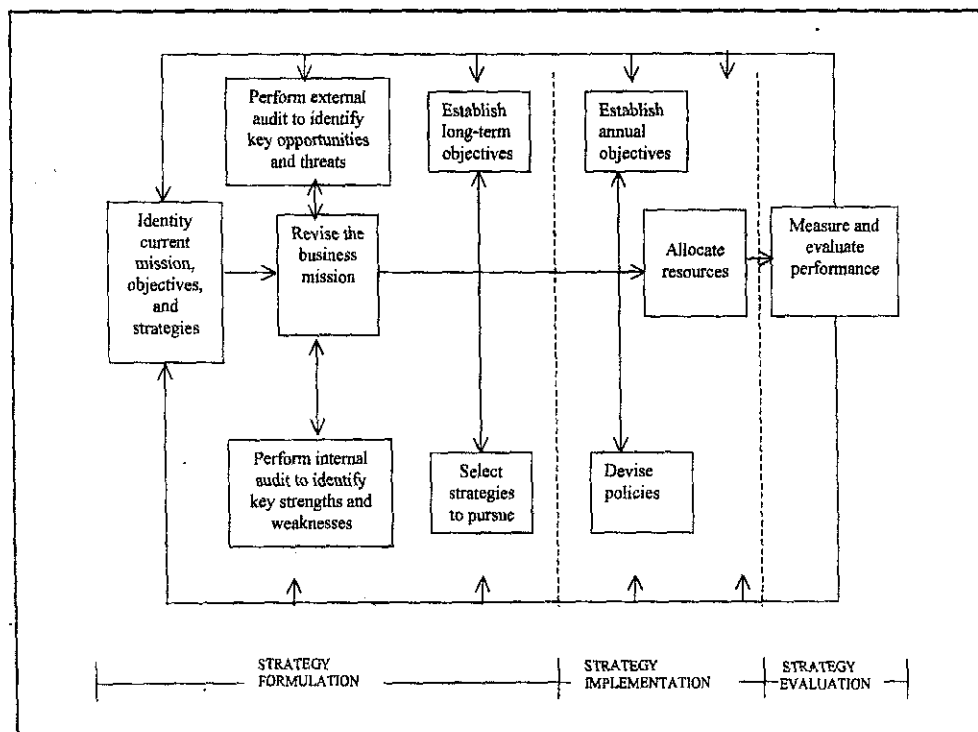


Exhibit 10.1: A Comprehensive Strategic Management Model

The Process of Strategy Choice

Strategists never consider all feasible alternatives that could benefit the firm, because there are an infinite number of

possible actions and an infinite number of ways to implement those actions. Therefore, a manageable set of the most attractive alternative strategies must be developed. The advantages, disadvantages, trade-offs, costs, and benefits to these strategies should be determined. This section discusses the process that many firms use to determine an appropriate set of alternative strategies.

Identifying and evaluating alternative strategies should involve many of the managers and employees who earlier assembled the organizational mission statement, performed the external audit, and conducted the internal audit. Representatives from each department and division of the firm should be included in this process, as was the case in previous strategy-formulation activities. Recall that involvement provides the best opportunity for managers and employees to gain an understanding of what the firm is doing and why, and to become committed to helping the firm accomplish its objectives.

All participants in the strategy analysis and choice activity should have the firm's external and internal audit information by their side. This information, coupled with the firm's mission statement, will help participants crystallize in their own minds particular strategies that they believe could benefit the firm most. Creativity should be encouraged in this through process.

Alternative strategies proposed by participants should be considered and discussed in a meeting or series of meetings. Proposed strategies should be listed in writing. When all feasible strategies identified by participants are given and understood, the strategies should be ranked in order of attractiveness by all participants, with 1 = should not be implemented, 2 = should possibly be implemented, 3 = should probably be implemented, and 4 = should definitely be implemented. This process will result in a prioritized list of "best" strategies that reflects the collective wisdom of the group. Long-term objectives represent the results expected from pursuing certain strategies. Strategies represent the actions to be taken to accomplish long-term objectives. The time frame for objectives and strategies should be consistent, usually from 2 to 5 years.

An increasing number of firms recognize that establishing long-term objectives and strategies must be a give-and-take process. In practice, organisations generally establish objectives and strategies concurrently. The strategic-management model thus illustrates with multidirectional arrow a symbiotic relationship between establishing objectives and establishing strategies. Objectives become crystallized as feasible strategies are formulated and selected.

Objectives should be quantitative, measurable, realistic, understandable, challenging, hierarchical, obtainable, and congruent among organizational units. Each objective should also be associated with a time line. Objectives are commonly stated in terms such as growth in assets, growth in sales, profitability, market share, degree and nature of diversification, degree and nature of vertical integration, earnings per share, and social responsibility. Clearly established objectives offer many benefits. They provide direction, allow synergy, aid in evaluation, establish priorities, reduce uncertainty, minimize conflicts, stimulate exertion, and aid in both the allocation of resources and the design of jobs.

Long-term objectives are needed at the corporate, divisional, and functional levels in an organization. They are an important measure of managerial performance. Many practitioners and academicians attribute a significant part of American industry's competitive decline to the short-term, rather than long-term, strategy orientation of American managers. Arthur D. Little argues that bonuses or merit pay for managers today must be based to a greater extent on long-term objectives and strategies. A general framework for relating objectives to performance evaluation is provided in Exhibit 10.2 A particular organisation could tailor these guidelines to meet its own needs, but incentives should be attached to both long-term and annual objectives.

Clearly stated and communicated objectives are vital to success for many reasons. First, objectives help stakeholders understand their role in an organization's future. Objectives also provide a basis for consistent decision making by managers whose values and attitudes differ. By reaching a consensus on objectives during strategy-formulation

activities, an organization can minimize potential conflicts later during implementation. Objectives set forth organizational priorities and stimulate exertion and accomplishment. They serve as standards by which individuals, groups, departments, divisions, and entire organizations can be evaluated. Objectives provide the basis for designing jobs and organising activities to be performed in an organization. Objectives provide direction and allow for organisational synergy. Without long-term objectives, an organization would drift aimlessly toward some unknown end! It is hard to imagine an organization or individual being successful without clear objectives. Success only rarely occurs by accident, but rather is the result of hard work directed toward achieving certain objectives.

Organizational Level	Basis for Annual bonus or Merit Pay
Corporate	75% based on long-term objectives 25% based on annual objectives
Divisional	50% based on objectives 50% based on goals
Functional	25% based on objectives 75% based on goals

Exhibit 10.2: Varying Performance Measures by Organizational Level

Managing by Objectives

An unknown educator once said, 'If you think education is expensive, try ignorance.' The idea behind this saying also applies to establishing objectives. Strategies should avoid the following alternative ways to "not managing by objectives:"

- Managing by Extrapolation—adheres to the principle "If it ain't broke, don't fix it." The idea is to keep on doing about the same things in the same ways, because things are going well.
- Managing by Crisis—based on the belief that the true measure of a really good strategist is the ability to solve problems. Since there are plenty of crises and problems to go around for every person and every organization, strategists ought to bring their time and creative energy to bear on solving the most pressing problems of the day. Managing by crisis is actually a form of reacting rather than acting and of letting events dictate the what's and whens of management decisions.
- Managing by Subjectives—built on the idea that there is no general plan for which way to go and what to do, just do the best you can to accomplish what you think should be done. In short, "do your own thing, the best way you know how," (sometimes referred to as "the mystery approach to decision making" because subordinates are left to figure out what is happening and why).
- Managing by Hope—based on the fact that the future is laden with great uncertainty and that if we try and do not succeed, then we hope our second (or third) attempt will succeed. Decisions are predicted on the hope that they will work and that good times are just around the corner, especially if luck and good fortune are on our side.

Important strategy-formulation techniques can be integrated into a three-stage decision-making framework, as shown in Exhibit 10.3. The tools presented in this framework are applicable to all sizes and types of organizations and can help strategists identify, evaluate, and select strategies.

Stage 1 of the formulation framework consists of the EFE Matrix, Competitive Profile matrix, and the IFE Matrix. Called the *Input stage*, Stage 1 summarizes the basic input information needed to formulate strategies. Stage 2, called the *Matching Stage*, focuses upon generating feasible alternative strategies by aligning key external and internal factors. Stage 2 techniques include the Threats-Opportunities-Weaknesses-Strengths (TOWS) Matrix, the Strategic Position and Action Evaluation (SPACE) Matrix, the Boston Consulting Group (BCG) Matrix, the Internal-External (IE) Matrix, and the Grand Strategy Matrix. Stage 3, called the *Decision Stage*, involves a single technique.

the Quantitative Strategies Planning Matrix (QSPM). A QSPM uses input information derived from Stage 1 to objectively evaluate feasible alternative strategies identified in Stage 2. A QSPM reveals the relative attractiveness of alternative strategies and thus provides an objective basis for selecting specific strategies.

All nine techniques included in the strategy-formulation framework require integration of intuition and analysis. Autonomous divisions in an organization commonly use strategy-formulation techniques to develop strategies and objectives. Divisional analyses provide a basis for identifying, evaluating, and selecting among alternative corporate-level strategies.

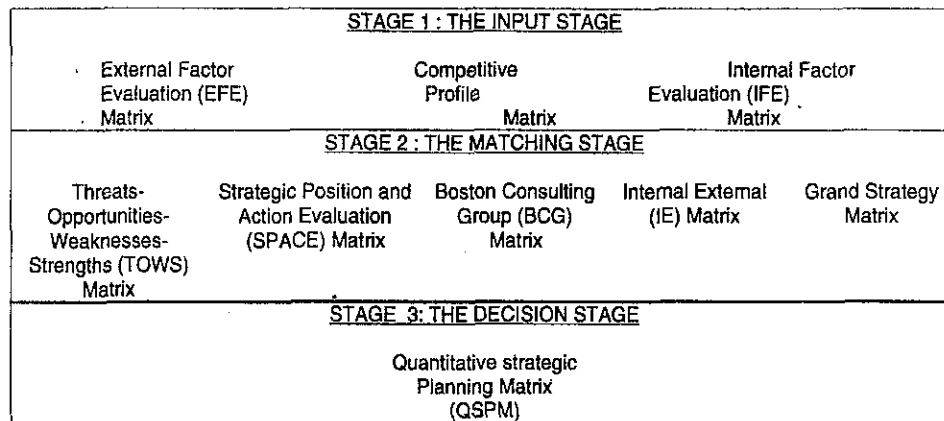


Exhibit 10.3: The Strategy Formulation Analytical Framework

Strategists themselves, not analytical tools, are always responsible and accountable for strategic decisions. Lenz emphasizes that the shift from a words-oriented to a numbers-oriented planning process can give rise to a false sense of certainty; it can reduce dialogue, discussions, and argument as means to explore understandings, text assumptions, and foster organizational learning. Strategists therefore must be wary of this possibility and use analytical tools to facilitate, rather than diminish, communication. Without objective information and analysis, personal biases, politics, emotions, personalities, and *halo error* (the tendency to put too much weight on a single factor) unfortunately may play a dominant role in the strategy-formulation process.

Procedures for developing an EFE matrix, a Competitive Profile Matrix, and an IFE Matrix were presented in the previous two chapters. These tools require strategists to quantify subjectivity during early stages of the strategy-formulation process. Making "small" decisions in the input matrices regarding the relative importance of external and internal factors allows strategists to make final strategy decisions more effectively. Good intuitive judgement is always needed in determining appropriate weights and ratings.

Sometimes a key internal factor can be both a strength and a weakness; a key external factor can be both an opportunity and a threat. When this is so, the factor should be included twice in the appropriate matrix, and a weight and rating should be assigned to each statement. For example, the Playboy logo both helps and hurts Playboy Enterprises: the logo attracts customers to Playboy casinos, clubs, and the magazine, but it keeps the Playboy cable channel out of many markets. Playboy's net income has fallen from Rs. 11 million, to Rs. 2.6 million, to negative Rs. 3.8 million in 1987, 1988, and 1989 respectively.

The matching stage of the strategy-formulation framework consists of five techniques that can be used in any sequence: the TOWS matrix, the SPACE Matrix, the BOG Matrix, IE Matrix, and the Grand Strategy Matrix. The tools rely upon input information derived from State 1 (the EFE Matrix, competitive Profile Matrix, and IFE Matrix) to match external opportunities and threats with internal strengths and weaknesses. Matching external and internal critical success factors is the key to effectively generating feasible alternative strategies! For example, a firm with

excess working capital (an internal strength) could take advantage of the aerospace industry growing 40 percent annually (an external opportunity) by acquiring a firm in the aerospace industry. This example portrays simple on-to-one matching. In most situations, external and internal relationships are more complex, and the matching process requires multiple alignments for each strategy generated. The basic concept of matching is exemplified in Exhibit 10.4.

Key Internal Factor		Key External Factor		Resultant Strategy
Excess working capital (an internal strength)	+	40% annual growth of the aerospace industry (an external opportunity)	=	Acquire Aerospace, Inc.
Insufficient capacity (an internal weakness)	+	Exit of two major foreign competitors from the industry (an external opportunity)	=	Pursue horizontal integration by buying competitors' facilities
Strong R & D expertise (an internal strength)	+	Decreasing number of young adults (an external threat)	=	Develop new products for older adults
Poor employee morale (an internal weakness)	+	Strong union activity (an external threat)	=	Develop a new employee-benefits package

Exhibit 10.4: Matching Key Internal and External Factors to Formulate Alternative Strategies

Any organization, whether military, product-oriented, service-oriented, governmental, or even athletic, must develop and execute good strategies to win. A good offense without a good defense, or vice versa, usually leads to defeat. Every organization has some external opportunities and threats and internal strengths and weaknesses that can be aligned to formulate feasible alternative strategies.

The Threats-Opportunities-Weaknesses-Strengths (TOWS) Matrix

The Threats-Opportunities-Weaknesses-Strengths (*TOWS*) Matrix is an important matching tool that helps managers develop four types of strategies : SO Strategies, WO strategies, ST Strategies, and WT Strategies.³ Matching key external and internal factors is the most difficult part of developing a TOWS Matrix and requires good judgement, and there is no one best set of matches. Note in Table 6-2 that the first, second, third, and fourth strategies are SO, WO, ST, and WT Strategies respectively.

SO Strategies use a firm's internal strengths to take advantage of external opportunities. All managers would like their organizations to be in a position where internal strengths can be used to take advantage of trends and events in the environment. For example, Mercedes Benz, with its technical know-how and reputation for quality (internal strengths), could take advantage of the increasing demand for luxury cars (external opportunity) by building a new manufacturing plant (SO Strategy). Organizations generally will pursue WO, ST, or WT Strategies in order to get into a situation where they can apply SO Strategies. When a firm has major weaknesses, it will strive to overcome them, making them strengths. When an organization faces major threats, it will seek to avoid them in order to concentrate on opportunities.

WO Strategies aim at improving internal weaknesses by taking advantage of external opportunities. Sometimes key external opportunities exist, but a firm has internal weaknesses that prevent it from exploiting those opportunities. For example, there may be a high demand for electronic devices to control the amount and timing of fuel injection in automobile engines (opportunity), but a certain auto parts manufacturer may lack the technology required for producing these devices (weakness). One possible WO Strategy would be to acquire this technology by forming a joint venture with a firm having competency in this area. An alternative WO strategy would be to hire and train people with the required technical capabilities.

ST Strategies use a firm's strengths to avoid or reduce the impact of external threats. This does not mean that a strong organization should always meet threats in the external environment head-on. General Motors found this out in the 1960s when Ralph Nader (an external threat) exposed safety hazards of the Corvair automobile. GM used its strength (size and influence) to ridicule Nader, and the direct confrontation caused more problems than expected. In retrospect, this ST Strategy was probably inappropriate for GM at the time.

WT Strategies are defensive tactics directed at reducing internal weaknesses and avoiding environmental threats. An organization faced with numerous external threats and internal weaknesses may indeed be in a precarious position. In fact, such a firm may have to fight for its survival, merge, retrench, declare bankruptcy, or choose liquidation.

A schematic representation of the TOWS matrix is provided in Exhibit 10.5. Note that a TOWS Matrix is composed of nine cells. As shown, there are four key factor cells, four strategy cells, and one cell that is always left blank (the upper left cell). The four strategy cells, labeled SO, WO, ST, and WT, are developed after completing four key factor cells, labeled S, W, O, and T. There are eight steps involved in constructing a TOWS Matrix:

Always leave blank	STRENGTHS-S		WEAKNESSES-W		
	1.		1.		
	2.		2.		
	3.		3.		
	4.		4.		
	5.		5.		
	6.	List strengths	6.	List weaknesses	
	7.		7.		
	8.		8.		
	9.		9.		
10.		10.			
OPPORTUNITIES-O		SO STRATEGIES		WO STRATEGIES	
1.		1.		1.	
2.		2.		2.	
3.		3.		3.	
4.	List opportunities	4.	Use strengths to take advantage of opportunities	4.	Overcome weaknesses by taking advantage of opportunities
5.		5.		5.	
6.		6.		6.	
7.		7.		7.	
8.		8.		8.	
9.		9.		9.	
10.		10.		10.	
STRENGTHS-S		ST STRATEGIES		WT STRATEGIES	
1.	List threats	1.	Use strengths to avoid threats	1.	Minimize weaknesses and avoid threats
2.		2.		2.	
3.		3.		3.	
4.		4.		4.	
5.		5.		5.	
6.		6.		6.	
7.		7.		7.	
8.		8.		8.	
9.		9.		9.	
10.		10.		10.	

Exhibit 10.5: The TOWS Matrix

1. List the firm's key external opportunities.
2. List the firm's key external threats.
3. List the firm's key internal strengths
4. List the firm's key internal weaknesses.
5. Match internal strengths with external opportunities and record the resultant SO Strategies in the appropriate cell.
6. Match internal weaknesses with external opportunities and record the resultant WO strategies.

7. Match internal strengths with external threats and record the resultant ST Strategies.
8. Match internal weaknesses with external threats and record the resultant WT Strategies.

Some other example of SO, WO, ST, and WT Strategies are given as follows:

1. A strong financial position (internal strength) coupled with unsaturated foreign markets (external opportunity) could suggest market development to be an appropriate SO Strategy.
2. A lack of technical expertise (internal weakness) coupled with a strong demand for computer services (external opportunity) could suggest the WO Strategy of acquiring a high-tech computer company.
3. A strong distribution system (internal strength) coupled with intense government deregulation (external threat) could suggest concentric diversification to be a desirable ST Strategy.
4. Poor product quality (internal weakness) coupled with unreliable suppliers (external threat) could suggest backward integration to be a feasible WT Strategy.

The purpose of each Stage 2 matching tool is to generate feasible alternative strategies, not to select or determine which strategies are best! Not all of the strategies developed in the TOWS Matrix therefore will be selected for implementation.

The strategy-formulation guidelines can enhance the process of matching key external and internal factors. For example, when an organization has both the capital and human resources needed to distribute its own products (internal strength) and distributors are unreliable, costly, or incapable of meeting the firm's needs (external threat), then forward integration can be an attractive ST Strategy. When a firm has excess production capacity (internal weakness) and its basic industry is experiencing declining annual sales and profits (external threat), then concentric diversification can be an effective WT Strategy. It is important to use specific, rather than generic, strategy terms when developing a TOWS Matrix. Also it is important to include the "S1,02" type notation after each strategy in the TOWS Matrix. This notation reveals the rationale for each alternative strategy.

BCG Product Portfolio Matrix

A tool for strategic (product) planning and resource allocation, the Boston Consulting Group (BCG) product portfolio matrix analyses products on the basis of (a) relative market share and (b) industry growth rate.

- *Stars* Products which enjoy a high market share and a high growth rate are referred to as stars. Though they earn high profits, they require additional commitment of funds because of the need to make further investments for expanding their production and sales. Eventually, as growth declines and additional investment needs diminish, stars become cash cows.
- *Question marks* Production with high growth potential but low present market share are called question marks. Additional resources are required to improve their market share and potentially convert them into stars. Of course, there is no guarantee that this would happen—that is why they are called 'question marks'.
- *Cash cows* Products which enjoy a relatively high market share but low growth potential are called cash cows. They generate substantial profits and cash flows but their investment requirements are modest. The cash surpluses provided by them are available for use elsewhere in the business.
- *Dogs* Products with low market share and limited growth potential are referred to as dogs. Since the prospects for such products are bleak, it is advisable to phase them out rather than continue with them.

From the above description, it is broadly clear that cash cows generate funds and dogs, if divested, release funds. On

the other hand, stars and question marks require further commitment of funds. Hence, the suggested pattern of resource allocation should be as shown in Part A of Exhibit 10.6. Conscious efforts should be made to avoid the pattern of resource allocation depicted in Part B of Exhibit 10.6 some firms unwittingly adopt this pattern which leads to the neglect of stars and question marks and to the misdirection of surplus funds generated by cash cows into futile efforts to revive dogs.

General Electric's Stoplight Matrix

The general Electric Company of US is widely respect for the sophistication, maturity, and quality of its planning systems. The matrix developed by this company for guiding resource allocation is called the General Electric's stoplight matrix. It calls for analysing various products (or services) of the firm in terms of two key issues:

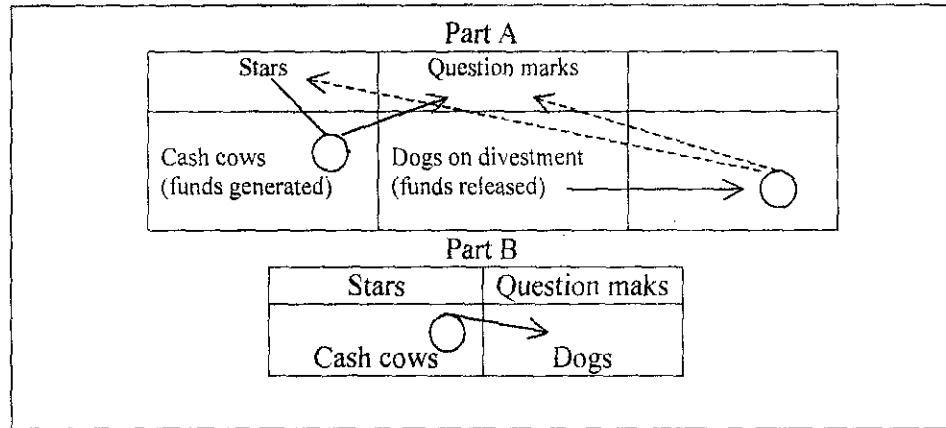


Exhibit 10.6: Pattern of Resource Allocation

Business strength How strong is the firm vis-à-vis its competitors?

Industry attractiveness What is the attractiveness or potential of the industry?

The commitment of funds to various products is guided by how they are rated in terms of the above two dimensions. As shown in Exhibit 10.7 products which are favourably placed justify substantial commitment of funds. Products which are unfavourably placed call for divestment, and products which are placed in between qualify for modes investment.

I n d u s t r y	A t t r a c t i v e n e s s	High Medium Low	Business Strength		
			Strong	Average	Weak
			Invest	Invest	Hold
			Invest	Hold	Divest
		Low	Divest	Divest	Divest

Exhibit 10.7: General Electric's Stoplight Matrix

Strategic Position and Action Evaluation (SPACE)

SPACE is an approach to hammer out an appropriate strategic posture for a firm and its individual business. An extension of the two-dimensional portfolio analysis, SPACE involves a consideration of four dimensions:

- Company's competitive advantage
- Company's financial strength
- Industry strength
- Environmental stability

The factors determining competitive advantage, financial strength, industry strength, and environmental stability are shown as follows:

Company's competitive advantage	Company's functional strength
Market share	Return on investment
Product quality	Leverage
Product life cycle	Liquidity
Product replacement cycle	Capital required/capital available
Customer loyalty	Cash flow
Competition's capacity utilisation	Ease of exit from market
Technological know-how	Risk involved in the business
Vertical integration	
Industry strength	Environmental stability
Growth potential	Technological changes
Profit potential	Rate of inflation
Financial stability	Demand variability
Technological know-how	Price range of competing products
Resource utilisation	Barriers to entry into market
Capacity intensity	Competitive pressure
Ease of entry into market	Price elasticity of demand
Productivity, capacity utilisation	

To apply the SPACE approach to a firm, the following procedure may be followed :

1. Numerically assess the firm on the factors which have a bearing on the four dimensions. The scale of assessment for the factors relating to the dimensions of *company's financial strength* and *industry strength* may be 0 to 7, with 0 reflecting the most unfavourable assessment and 7 the most favourable. However, the scale of assessment for the factors relating to the dimensions of *environmental stability* and *company's competitive advantage* may be 0 to -7, with 0 reflecting the most favourable assessment and -7 the most unfavourable.
2. Average the numerical values assigned for various factors relating to a given dimension to get the numerical score for the dimension.
3. Plot the scores for the four dimensions on the axes of the SPACE chart. The SPACE chart is shown in Exhibit 10.8.
4. Connect the scores to plotted to get a four-sided polygon, reflecting the size and direction of the assessment.

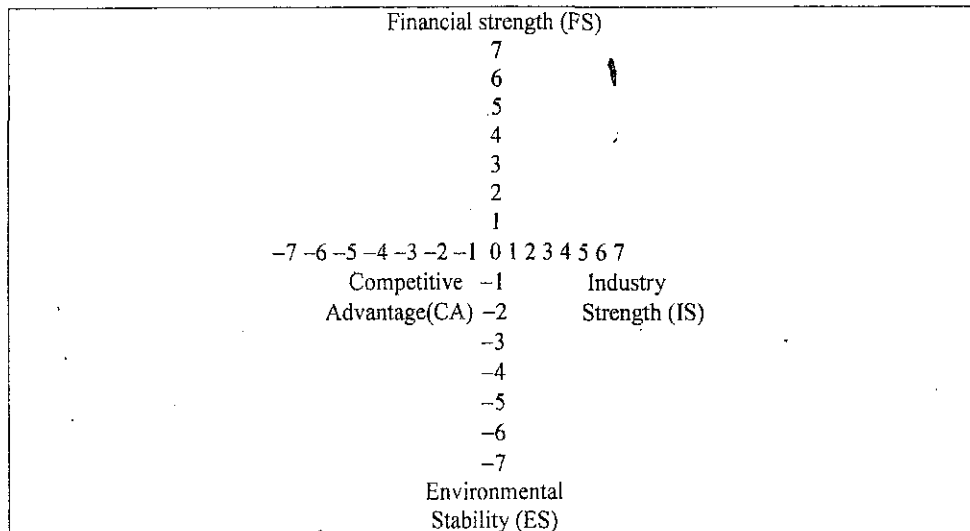


Exhibit 10.8: Space chart

Strategic Postures

The basic strategic postures associated with the SPACE approach, illustrated graphically in Exhibit 10.9 are as follows:

Aggressive Posture: This is appropriate for a company which (i) enjoys a competitive advantage and considerable financial strength and (ii) belongs to an attractive industry that operates in a relatively stable environment. An aggressive posture means that the firm must fully exploit opportunities available to it, seriously look for a acquisition possibilities in its own or related industries, concentrate resources to maintain its competitive edge, and enhance its market share. The aggressive posture is similar to the generic strategy of *overall cost leadership* suggested by Michael Porter.

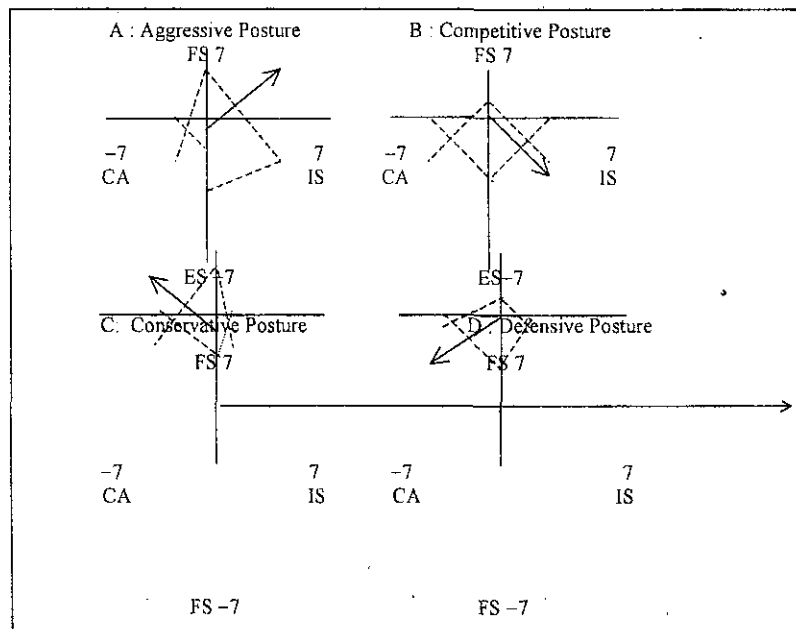


Exhibit 10.9: Basic Strategies Postures Associated with SPACE Approach

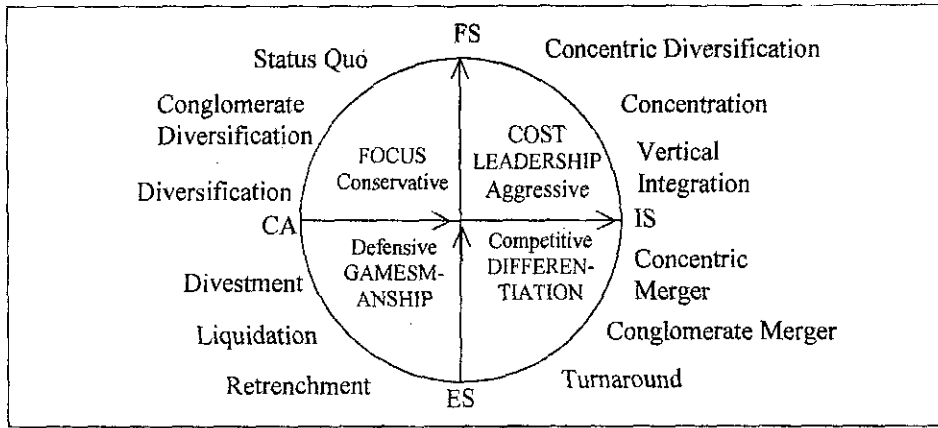


Exhibit 10.10: Generic Strategies and Key Options

Competitive Posture: This is suitable for a company which (i) enjoys a competitive advantage but has limited financial strength, and (ii) belongs to an attractive industry operating in a relatively unstable environment. The key planks of the competitive posture are as follows: maintain and enhance competitive advantage by product improvement and differentiation, widen the product line, improve marketing effectiveness, and augment financial resources. There is a great deal of *product differentiation* suggested by Michael Porter.

Conservation Posture: This is appropriate for a company which (i) enjoys financial strength but has limited competitive advantage, and (ii) belong to a not-so-attractive industry operating in a relatively stable environment. A conservative posture call for the following action: prune non-performing products, reduce costs, improve productivity, develop new products, and access more profitable markets. The conservation posture described here is somewhat similar to the generic strategy of *focus* suggested by Michael Porter.

Defensive Posture: This is suitable for a company which (i) lacks competitive advantage as well as financial strength, and (ii) belong to a not-so-attractive industry operating in an unstable environment. A defensive posture involves the following actions: discontinue unviable products, control costs aggressively, monitor cash flows strictly, reduce capacity, and postpone or limit investment. The defensive posture so defined may be likened to gamesmanship which calls for employing manoeuvres to keep the company afloat, check the onslaught of competition, and eventually facilitate withdrawal or exit

The generic strategies and the key options (which have important resource allocation implications) associated with them are shown in Exhibit 10.10. This is drawn from the book *Strategic Management - A Methodological Approach* by A.J. Rowe, R.O. Mason, and K.E. Dickel (Reading, Massachusetts, Addison-Wesley Publishing Company, 1986).

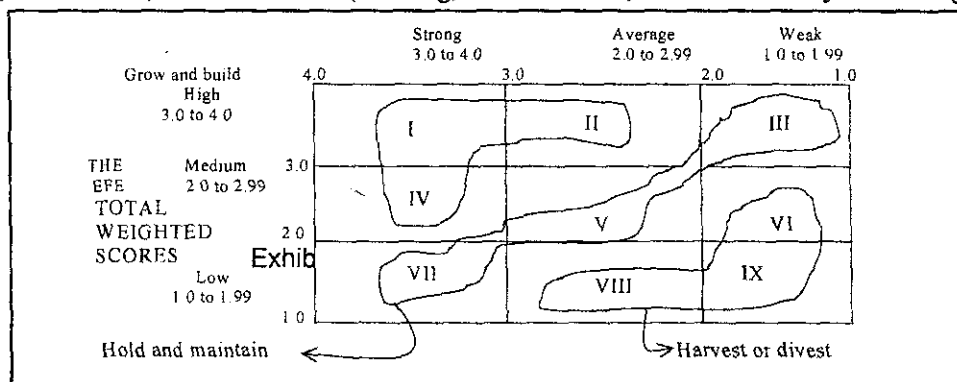


Exhibit 10.12: An Example IE Matrix : THE IFE TOTAL WEIGHTED SCORES

The Internal-External (IE) Matrix

The Internal-External (IE) Matrix positions an organization's various divisions in a nine-cell display Exhibit 10.11. The IE Matrix is similar to the BCG Matrix in that both tools involve plotting organization divisions in a schematic diagram; this is why they are both called portfolio matrices. Also, the size of each circle represents the percentage sales contribution of each division, and pie slices reveal the percentage profit contribution of each division in both the BCG and IE Matrix.

But there some important differences between the BCG Matrix and IE Matrix. The axes are different. Also, the IE Matrix requires more information about the divisions than the BCG Matrix. Further, the strategic implications of each matrix are different. For these reasons, strategists in multidivisional firms often develop both the BCG Matrix and the IE Matrix in formulating alternative strategies. A common practice is to develop a BCG Matrix and in IE Matrix for the present, and then develop projected matrices to reflect the future. This practice forecasts the expected effect of current strategic decisions on an organization's portfolio of divisions.

The IE Matrix is based on two key dimensions: the IFE total weighted scores on the x-axis and the EFE total weighted scores on the y-axis. Recall that each division of an organization should construct an IFE Matrix and an EFE Matrix for its part of the organization. The total weighted scores derived from the division allow construction of the corporate-level IE Matrix. On the x-axis of the IE Matrix, and 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. Similarly, 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 high.

The IE Matrix can be divided into three major regions that have different strategy implications. First, the prescription for divisions that fall into cells I, II, or IV can be described as "Grow and Build." Intensive (market penetration, market development, and product development) or integrative (backward integration, forward integration, and horizontal integration) strategies can be most appropriate for these divisions. Second, divisions that fall into cells III, V, or VII can best be managed with "Hold and Maintain" strategies; market penetration and product development are two commonly employed strategies for these types of divisions. Third, a common prescription for divisions that fall into cells VI, VIII, or IX is "Harvest or Divest." Successful organizations are able to achieve a portfolio of businesses positioned in or around cell I in the IE Matrix.

An example of a completed IE Matrix is given in Exhibit 10.12 which depicts an organization composed of four divisions. As indicated by the positioning of the circles, "Grow and Build" strategies are appropriate for Division 1, Division 2, and Division 3. Division 4 is a candidate for "Harvest or Divest." Division 2 contributes the greatest percentage of company sales and thus is represented by the largest circle. Division 1 contributes the greatest proportion of total profits, since it has the largest percentage pie slice.

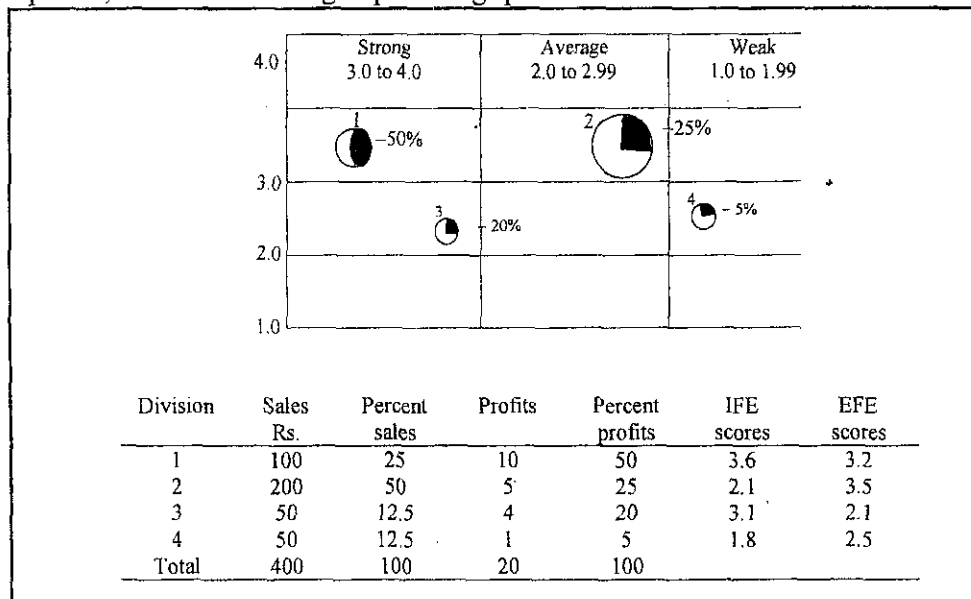


Exhibit 10.12: An Example IE Matrix : THE IFE TOTAL WEIGHTED SCORES

The Grand Strategy Matrix

In addition to the TOWS Matrix, SPACE Matrix, BCG Matrix, and IE Matrix, the Grand Strategy Matrix has become a popular tool for formulating alternative strategies. All organizations can be positioned in one of the Grand Strategy Matrix's four strategy quadrants. A firm's divisions could likewise be positioned. As illustrated in Exhibit 9.2 the Grand strategy Matrix is based on two evaluative dimensions: competitive position and market growth. Appropriate strategies for an organization to consider are listed in sequential order of attractiveness in each quadrant of the matrix.

Firms located in Quadrant I of the Grand Strategy matrix are in an excellent strategic position. For these firms, continued concentration on current markets (market penetration and market development) and products (product development) are appropriate strategies. It is unwise for a Quadrant I firm to shift notably from its established competitive advantages. When a Quadrant I organization has excessive resources, then backward forward, or horizontal integration may be effective strategies. When a Quadrant I firm is too heavily committed to a single product, then concentric diversification may reduce the risks associated with a narrow product line. Quadrant I firms can afford to take advantage of external opportunities in many areas; they can aggressively take risks when necessary.

		RAPID MARKET GROWTH	
		Quadrant II	Quadrant I
		<ol style="list-style-type: none"> 1. Market development 2. Market penetration 3. Product development 4. Horizontal integration 5. Divestiture 6. Liquidation 	<ol style="list-style-type: none"> 1. Market development 2. Market penetration 3. Product development 4. Forward integration 5. Backward integration 6. Horizontal integration 7. Concentric diversification
WEAK COMPETITIVE POSITION			STRONG COMPETITIVE POSITION
		Quadrant III	Quadrant IV
		<ol style="list-style-type: none"> 1. Retrenchment 2. Concentric diversification 3. Horizontal diversification 4. Conglomerate diversification 5. Divestiture 6. Liquidation 	<ol style="list-style-type: none"> 1. Concentric diversification 2. Horizontal diversification 3. Conglomerate diversification 4. Joint ventures
		SLOW MARKET GROWTH	

Exhibit 10.13: The Grand Strategy Matrix

Firms positioned in Quadrant II need to evaluate their present approach to the marketplace seriously. Although their industry is growing, they are unable to compete effectively, and they need to determine why the firm's current approach is ineffectual and how the company can best change to improve its competitiveness. Since Quadrant II firms are in a rapid-market-growth industry, an intensive strategy (as opposed to integrative or diversification) is usually the first option that should be considered. However, if the firm is lacking a distinctive competence or competitive advantage, then horizontal integration is often a desirable alternative. As a last result, divestiture or liquidation should be considered. Divestiture can provide funds needed to acquire other businesses or buy back shares of stock.

Quadrant III organizations compete in slow-growth industries and have weak competitive positions. These firms must make some drastic changes quickly to avoid further demise and possible liquidation. Extensive cost and asset reduction (retrenchment) should be pursued first. An alternative strategy is to shift resources away from the current business into divestiture or liquidation.

Finally, Quadrant IV businesses have a strong competitive position but are in a slow-growth industry. These firms have the strength to launch diversified programs into more promising growth areas. Quadrant IV firms have characteristically high cash flow levels and limited internal growth needs and can often pursue concentric, horizontal, or conglomerate diversification successfully. Quadrant IV firms may also pursue joint ventures.

The Decision Stage

Analysis and intuition provide a basis for making strategy formulation decisions. The matching techniques just discussed reveal feasible alternative strategies. Many of these strategies will likely have been proposed by managers and employees participating in the strategy analysis and choice activity. And additional strategies resulting from the matching analyses could be discussed and added to the list of feasible alternative options. As indicated earlier in this chapter, participants could rate these strategies on a 1 to 4 scale so that a prioritized list of the "best" strategies could be achieved.

The Quantitative Strategic Planning Matrix (QSPM)

Other than rating strategies to achieve the prioritized list, there is only one analytical technique in the literature designed for determining the relative attractiveness of feasible alternative actions. This technique is the *Quantitative Strategic Planning Matrix (QSPM)*, which comprises Stage 3 of the strategy-formulation analytical framework. 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. That is, the EEF Matrix, Competitive Profile SPACE Analysis, BCG Matrix, IE Matrix, and Grand Strategy Matrix that make up stage 2, provide the needed information for setting up the QSPM (Stage 3). The QSPM is a tool that allows strategists to evaluate alternative strategies objectively, based on previously identified external and internal critical success factors. Like other strategy-formulation analytical tools, the QSPM requires good intuitive judgement.

The basic format of the QSPM is illustrated in Exhibit 10.15. A column of a QSPM consists of key external and internal factors (from Stage 1), and the top row consists of feasible alternative strategies (from Stage 2). Specifically, the left column of QSPM consists of information obtained directly from the EFE Matrix and IFE Matrix. In a column adjacent to the critical success factors, the respective ratings received by each factor in the EFE Matrix and IFE Matrix are recorded. The top row of a QSPM consists of alternative strategies derived from the TOWS Matrix, SPACE Matrix, BCG Matrix, IE Matrix, and Grand Strategy Matrix. These matching tools usually generate similar feasible alternatives. However, not every strategy suggested by the matching techniques has to be evaluated in a QSPM. Strategists should use good intuitive judgement in selecting strategies to include in a QSPM.

Conceptually, the QSPM determines the relative attractiveness of various strategies based on the extent that key external and internal critical success factors are capitalized upon or improved. The relative attractiveness of each strategy within a set of alternatives is computed by determining the cumulative impact of each external and internal critical success factor. Any number of sets of alternative strategies can be included in the QSPM, and any number of strategies can comprise a given set. But only strategies within a given set are evaluated relative to each other. For example, one set of strategies may include concentric, horizontal, and conglomerate diversification, whereas another set may include issuing stock and selling a division to raise needed capital. These two sets of strategies are totally different, and the QSPM evaluates strategies only within sets. Note in Exhibit 10.14 that three strategies are included and they comprise just one set.

Key Factors	Ratings	STRATEGIC ALTERNATIVES		
		Strategy 1	Strategy 2	Strategy 3
Internal Factors				
Management				
Marketing				
Finance/Accounting				
Production/Operations				
Research and Development				
Information systems				
External Factors				
Economy				
Political/Legal/Government				
Social/Cultural/Demographic				
Technological				
Competitive				

Exhibit 10.14: The Quantitative Strategies Planning Matrix-QSPM

Internal Factors : 1 = major weakness; 2 = minor weakness; 3 = minor strength; 4 = major strength

External Factors: 1 = the firm's response is poor; 2 = the firm's response is average; 3 = the firm's response is above average; 4 = the firm's response is superior

A more detailed example of the QSPM is provided in Exhibit 10.15. This example illustrates all the components of the QSPM: Key Factors, Strategic Alternatives, Ratings, Attractiveness Scores, Total Attractiveness Scores, and Sum Total Attractiveness score. The three new terms just introduced -(1) Attractiveness Scores, (2) Total Attractiveness Scores, and (3) Sum Total Attractiveness Score-are defined and explained below as the six steps required to develop a QSPM are discussed.

Step 1 List the firm's key external opportunities/threats and internal strengths/ weaknesses in the left column of the QSPM. This information should be taken directly from the EFE Matrix and IFE Matrix. A minimum of ten external critical success factors and ten internal critical success factors should be included in the QSPM

Step 2 Assign Ratings to each external and internal critical success factor. These Ratings are identical to those in the EFE Matrix and the IFE Matrix. The Ratings are presented in a straight column just to the right of the external and internal critical success factors, as shown in Exhibit 10.15.

Step 3 Examine the State 2 (matching) matrices and identify alternative strategies that the organization should consider implementing. Record these strategies in the top row of the QSPM. Group the strategies into mutually exclusive sets if possible.

Step 4 Determine the Attractiveness Scores, defined as numerical values that indicate the relative attractiveness of each strategy in a given set of alternatives. Attractiveness Scores are determined by examining each external or internal critical success factor, one at a time, and asking the question "Does this factor affect the choice of the strategies being evaluated?" If the answer to this question is YES, then the strategies should be compared relative to that key factor. Specifically, Attractiveness Scores should be assigned to each strategy to indicate the relative attractiveness of one strategy over others, considering the particular factor. The range for Attractiveness Scores is 1 = not attractive, 2 = somewhat attractive, 3 = reasonably attractive, and 4 = highly attractive. If the answer to the above question is NO, indicating that the respective critical success factor has no effect upon the specific choice being made, then do not assign Attractiveness scores to the strategies in that set.

Note in Exhibit 10.15 that the "outstanding R & D Department" (an internal strength) has no significant effect upon the choice being made between acquiring the financial service versus the food company, so "blank" lines are placed in that row of the QSPM. "Two major foreign competitors are entering the industry" is a major external threat that results in an Attractiveness score of 1 for "Acquire Financial Service," compared to an Attractiveness score of 3 for the "Acquire Food services" strategy. These scores indicate that acquiring the Financial Services firm is "not attractive," whereas acquiring the Food services firm is "reasonably attractive," considering this single external critical success factor and the firm's current response to that strategy as indicated by the Rating.

Key factors	Ratings	Acquire Financial Services, Inc		Acquire Food Services, Inc		Rationals for Attractiveness Score
		AS*	TAS*	AS*	TAS*	
Internal Factors						
Top management team has fifteen years' experience.	3	4	12	2	6	Fifteen years' experience is in financial services
We have excess working capital of \$ 2 million.	4	2	8	3	12	Food services is valued at \$2 million.
All of our twenty plants are located in the Northeast United States.	1	2	2	4	4	Food Services is located in the Sunbelt.
Our R & D department is outstanding.	3	-	-	-	-	This items does not affect the strategy choice.
Our Return on Investment (ROI) ratio of .12 is lowest in the industry.						ROI at Food Services is higher than at Financial Services.
External Factors						
Interest rates are expected to rise to 15 percent in 1990.	2	3	6	4	8	Rising rates will hurt the financial services business
Population of the South is expected to grow by 15.3 million between 1992 and 2000.	3	4	12	2	6	Many new houses and apartments will be built and financed.
The financial services industry is expected to grow by 40 percent in 1992.	4	4	16	2	8	This 40 percent growth is in financial services.
Two major foreign	1	1	1	3	3	Food Services, Inc. is not affected by this entry.
President Bush is expected to deregulate the industry.	2	-	-	-	-	This item does not affect the strategy choice.
SUM TOTAL ATTRACTIVENESS SCORE			59		50	

Exhibit 10.15: A Sample Quantitative Strategies Planning Matrix

*AS = Attractiveness Score; TAS = Total Attractiveness Score

Attractiveness Score : 1 = not acceptable; 2 = possibly acceptable; 3 = probably acceptable; 4 = most acceptable

Internal Ratings: 1 = major weakness; 2 = minor weakness; 3 = minor strength; 4 = major strength

External Ratings: 1 = the firm's response is poor; 2 = the firm's response is average; 3 = the firm's response is above average; 4 the firm's response is superior

Note : Multiplying the Rating Times the Attractiveness Score is based upon the premise that to capitalize on strengths and take advantage of opportunities is more important for firms than improving weaknesses and avoiding threats. Some strategists do not agree with this premise and therefore do not compute the Total Attractiveness Scores. They simply sum the Attractiveness Scores to determine the relative attractiveness of strategies using the QSPM.

Step 5 Compute the Total Attractiveness Scores. Total Attractiveness Scores are defined as the product of multiplying the Ratings (Step 2) by the Attractiveness Scores (Step 4) in each row. The Total Attractiveness Scores indicate the relative attractiveness of each alternative strategy, considering only the impact of the adjacent external or internal critical success factor. Total Attractiveness Scores for each alternative are provided in Exhibit 3.26. The higher the Total Attractiveness Score, the more attractive the strategic alternative (considering only the adjacent critical success factor).

Step 6 Compute the Sum Total Attractiveness Score. It is the summation of the Total Attractiveness Scores in a strategy column of the QSPM. Sum Total Attractiveness Scores reveal which strategy is most attractive in each set of alternatives. Higher scores indicate more attractive strategies, considering all the relevant external and internal factors that could affect the strategic decisions. The magnitude of the difference between the Sum Total Attractiveness scores in a given set of strategic alternatives indicates the relative desirability of one strategy over another. (In the example, the Sum Total Attractiveness Score of 59, compared to 50, indicates that Financial Services, Inc. should be acquired.)

Positive Features and Limitations of the QSPM

A positive features of the QSPM is that sets of strategies can be examined sequentially or simultaneously. For example, corporate-level strategies could be evaluated first, followed by divisional-level strategies, and then functional-level strategies. There is no limit to the number of strategies that can be evaluated or the number of sets of strategies that can be examined at once using the QSPM.

Another positive feature of the QSPM is that it requires strategies to integrate pertinent internal and external factors into the decision process. Developing a QSPM makes it less likely that key factors will be overlooked or weighted inappropriately. A QSPM draws attention to important relationships that affect strategy decisions. Although developing a QSPM requires a number of subjective decisions, making small decisions along the way enhances the probability that the final strategic decisions will be best for the organization. A QSPM can be adapted for use by small and large, profit and nonprofit organizations and can be applied to virtually any type of organization. A QSPM can especially enhance strategic choice in multinational firms because many key factors and strategies can be considered at once. It also has been applied successfully by a number of small businesses.

The QSPM is not without some limitations. First, it always requires intuitive judgments and educated assumptions. The ratings and attractiveness scores requires judgments decisions, even though they should be based on objective information. Discussion among strategists, managers, and employees throughout the strategy-formulation process, including development of a QSPM, is constructive and improves strategic decisions. Constructive discussion during strategy analysis and choice may arise because of genuine differences of interpretation of information and varying opinions. Another limitation of the QSPM is that it can be only as good as the prerequisite information and matching analysis upon which it is based.

Subjective Factors in Strategic Choice

Strategic choice is a decision. At both the corporate and the business levels, this decision determines the future strategy of the firm.

After alternative strategies are examined, strategic choice is made. This is a decision to adopt one of the alternatives scrutinized. If the examination identified a clearly superior strategy, or if the current strategy will clearly meet future company objectives, then the decision is relatively simple. Such clarity is the exception, however, making the decision judgmental and difficult. Strategic decision makers, after comprehensive strategy examination, are often confronted with several viable alternatives rather than the luxury of a clear-cut, obvious choice. Under these circumstances, several factors influence the strategic choice decision. Some of the more important are:

1. Role of past strategy.
2. Degree of the firm's external dependence.
3. Attitudes toward risk.
4. Internal political considerations and the CEO.
5. Timing.
6. Competitive reaction.

Role of Past Strategy

A review of past strategy is the point at which the process of strategic choice begins.

As such, past strategy exerts considerable influence on the final strategic choice.

Current strategies are often the architects of past strategies. Because they have invested substantial time, resources, and interest in these strategies, the strategists would logically be more comfortable with a choice that closely parallels past strategy or represents only incremental alterations.

This familiarity and commitment to past strategy permeate the organization. Thus, lower-level management reinforces the top manager's inclination toward continuity with past strategy during the choice process. In one study, during the planning process, lower-level managers suggested strategic choice that were consistent with current strategy and

likely to be accepted while withholding suggestions with less probability of approval.

Research by Henry Mintzberg suggests that the past strategy strongly influences current strategic choice. The older and more successful a strategy has been, the harder it is to replace. Similarly, a strategy, once initiated, is very difficult to change because organizational momentum keeps it going.

Mintzberg's work and research by Berry Staw found that even as the strategy begins to fail due to changing conditions, strategists often increase their commitment to the past strategy. Firms may thus replace key executives when performance has been inadequate for an extended period because replacing top executives lessens the influence of unsuccessful past strategy on future strategic choice.

Degree of the Firm's External Dependence

A comprehensive strategy is meant to effectively guide a firm's performance in the larger external environment. Owners, suppliers, customers, government, competitors, and unions are a few of the elements in a firm's external environment. A major constraint on strategic choice is the power of environmental elements in supporting this decision. If a firm is highly dependent of one or more environmental factors, its strategic alternatives and ultimate choice must accommodate this dependence. The greater a firm's external dependence, the lower its range and flexibility in strategic choice.

Two examples highlight the influence of external dependence on strategic choice. For many years Whirlpool sold most of its major appliance output to one customer, Sears. With its massive retail coverage and access to alternate suppliers, Sears was a major external dependence for Whirlpool. Whirlpool's strategic alternatives and ultimate choice of strategy were limited and strongly influenced by Sears' demands. Whirlpool's grand strategy and important related decisions in areas such as research and development, pricing, distribution, and product design were carefully narrowed and chosen with the firm's critical dependence on Sears in mind. Chrysler Corporation's dependence on federal loan guarantees and financial concessions by labor considerably limited the strategic choice available in the early 1980s. The decision of Chrysler's Lee Iacocca to pay off several federal obligations before they were due was partially meant to increase Chrysler's flexibility by reducing one restrictive external dependence.

These examples show that a firm's flexibility in strategic choice is lessened when environmental dependence increases. If external dependence is critical, firms may include representatives of the external factor (government, union, supplier, bank) in the strategic choice process. In 1980, Chrysler, for example, took the unprecedented action of including Leonard Woodcock, President of the United Auto Workers, on its board of directors.

Attitudes toward Risk

Attitudes toward risk exert considerable influence on strategic choice. These attitudes may vary from eager risk taking to strong aversion to risk, and they influence the range of available strategic choice. Where attitudes favor risk, the range and diversity of strategic choices expand. High-risk strategies are acceptable and desirable. Where management is risk averse, the diversity of choices is limited; and risky alternatives are eliminated before strategic choice are made. Risk-oriented managers prefer offensive, opportunistic strategies. Risk-averse managers prefer defensive, safe strategies. Past strategy is quite influential in the strategic choice made by risk-averse managers, but it is less of a factor for risk-oriented managers. Exhibit 10.16 illustrates the relationship between attitudes toward risk and strategic choice.

Risk averse	Risk prone
Decrease choices	Expand choices
Defensive strategies	Offensive strategies
Stability	Growth
Incremental	Innovation
Minimize company weaknesses	Maximize company strengths
Strong ties to past strategy	Fewer ties to past strategy
Stable industry	Volatile industry
Maturing product/market evolution	Early product/market evolution

Exhibit 10.16: Managerial Risk Propensity and Strategic Choices

Industry volatility influences managerial propensity toward risk. In highly volatile industries, top managers must absorb and operate with greater amounts of risk than their counterparts in stable industries. Therefore, managers in volatile industries consider a broader, more diverse range of strategies in the strategic choice process.

Product/market evolution is another determinant of managerial risk propensity. If a firm is in the early stages of product/market evolution, it must operate with considerably greater risk than a firm later in the product/market evolution cycle.

In making a strategic choice, risk-oriented managers lean toward opportunistic strategies with higher payoffs. They are drawn to offensive strategies based on innovation, company strengths, and operating potential. Risk-averse managers lean toward safe, conservative strategies with reasonable, highly probable returns. The latter are drawn to defensive strategies to minimize a firm's weaknesses and external threats, as well as the uncertainty associated with innovation-based strategies.

A recent study examined the relationship between the willingness of strategic business unit (SBU) managers to take risks and SBU performance. The study found a link between risk taking and strategic choice. Looking first at SBUs assigned build or star strategic missions within a corporate portfolio, researchers found that the general managers of higher-performing SBUs had *greater willingness to take risks* than did their counterparts in lower-performing build or star SBUs. Looking next at SBUs assigned harvest strategies, successful units had general managers *less willing to take risks* than general managers in lower-performing harvest SBUs.

This study supports the idea that managers make different decisions depending on their willingness to take risks. Perhaps most important, the study suggests that being either risk prone or risk averse is not inherently good or bad. Rather, SBUs performance is more effective when the risk orientation of the general manager is consistent with the SBU's strategic mission (build or harvest). While this is only one study and not final determination of the influence of risk orientation on the process of making and implementing strategic decisions.

Internal Political Considerations

Power/political factors influence strategic choice. The existence and use of power to further individual or group interests is common in organizational life. An early study by Ross Stagner found that strategic decisions in business organizations were frequently settled by power rather than by analytical maximization procedures.

A major source of power in most organizations is the chief executive officer (CEO). In smaller enterprises, the CEO is consistently the dominant force in strategic choice, and this is also often true in large firms, particularly those with a strong or dominant CEO. When CEO begins to favor a particular choice, it is often unanimously selected.

Cyert and March identified another power source that influences strategic choice, particularly in larger firms. They called this the *coalition* phenomenon. In large organizations, subunits and individuals (particularly key managers)

have reason to support some alternatives and oppose others. Mutual interest often draws certain groups together in coalitions to enhance their position on major strategic issues. These coalitions, particularly the more powerful ones (often called dominant coalitions), exert considerable influence in the strategic choice process. Numerous studies confirm the use of power and coalitions on a frequent basis in strategic decision making. Interestingly, one study found that managers occasionally try to hide the fact that they prefer judgmental/political bargaining over systematic analysis and that when politics was a factor, it slowed decision-making.

Exhibit 10.17 illustrates the focus of political activity across phases of strategic decision making. It illustrates how the content of strategic decisions and the process of arriving at such decisions are politically intertwined. Each phase in the process of strategic choice presents a real opportunity for political action intended to influence the outcome. The challenge to strategists is in recognizing and managing this political influence. If such processes are not carefully overseen, various managers can bias the content of strategic decisions in the direction of their own interests. For example, selecting the criteria used to compare alternative strategies or collecting and appraising information regarding these criteria may be particularly susceptible to political influence. This must be recognized and, where critical, "managed" to avoid dysfunctional political bias. Reliance on different sources for obtaining and appraising information might be effective in this context.

Rather than simply being denoted as "bad" or inefficient, organizational politics must be viewed as an inevitable dimension of organizational decision making that must be accommodated in strategic management. Some authors argue that politics are a key ingredient in the "glue" that holds an organization together. Formal and informal negotiating and bargaining between individuals, subunits, and coalitions are indispensable mechanisms

Phases of strategic decision making	Focus of political action	Examples of political activity
Identification and diagnosis of strategic issues	Control of : Issues to be discussed Cause-and-effect relationships to be examined	Control of agenda Interpretation of past events and future trends
Narrowing the alternative strategies for serious consideration	Control of alternatives	Mobilization Coalition formation Resource commitment for information search
Examining and choosing the strategy	Control of choice	Selective advocacy of criteria Search and representation of information to justify choice
Initiating implementation of the strategy	Interaction between winners and losers	Winners attempt to "sell" or co-opt losers Losers attempt to thwart decisions and trigger fresh strategic issues
Designing procedures for evaluation of result	Representing oneself as successful	Selective advocacy of criteria

Exhibit 10.17: Political Activities in Phases of Strategic Decision Making

for organizational coordination. Recognizing and accommodating this in choosing future strategy will result in greater commitment and more realistic strategy. The costs are likely to be increased time spent on decision making and incremental (as opposed to drastic) change.

Timing Considerations

The time element can have considerable influence on strategic choice. Consider the case of Mech-Tran, a small manufacturer of fiberglass piping that found itself in financial difficulty. At the same time it was seeking a loan guarantee through the Small Business Administration (SBA), it was approached by KOCH industries (a Kansas

City-based supplier of oil field suppliers) with a merger offer. The offer involved 100 percent sale of Mech-Tran stock and a two-week response deadline, while the SBA loan procedure could take three months. Obviously, management's strategic decision was heavily influenced by external Wright indicates that under such a time constraint, managers put greater weight on negative than on positive information and prefer defensive strategies. The Mech-Tran owner decided to accept the OCH offer rather than risk losing the opportunity and subsequently being turned down by the SBA. Thus, faced with time constraints, management opted for a defensive strategy consistent with Wright's findings.

There is another side to the time issue – the timing of a strategic decision. A good strategy may be disastrous if it is undertaken at the wrong time. Winnebago was the darling of Wall Street in 1970, with its stock rising from Rs. 3 to Rs. 44 per share in one year. Winnebago's 1972 strategic choice, focusing on increasing its large, centralized production facility, was a continuation of the strategy that had successfully differentiated Winnebago in the recreational vehicle industry. The 1973 Arab oil embargo with subsequent rises in gasoline prices and overall transportation costs had dismal effects on Winnebago. The strategy was good, but the timing proved disastrous. On the other hand, IBM's decision to hold off entering the rapidly growing personal computer market until 1982 appeared to be perfectly timed. Welcomed by Apple with a full-page advertisement in *The Wall Street Journal*, IBM assumed the market share lead by early 1983.

A final aspect of the time dimension involves the lead time required for alternative choices and the time horizon management is contemplating. Management's primary attention may be on the short or long run, depending on current circumstances. Logically, strategic choice will be strongly influenced by the match between management's current time horizon and the lead time (or payoff time) associated with different choices. As a move towards vertical integration, Du Pont went heavily into debt to acquire Conoco in a 1982 bidding war. By 1983, the worldwide oil glut meant that Du Pont could have bought raw materials on more favourable terms in the open market. This short-term perspective was not of great concern to Du Pont management, however, because the acquisition was part of a strategy to stabilize Du Pont's long-term position as a producer of numerous petroleum-based products.

Competitive Reaction

In weighing strategic choices, top management frequently incorporates perceptions of likely competitor reactions to different options. For example, if management chooses an aggressive strategy that directly challenges a key competitor, that competitor can be expected to mount an aggressive counterstrategy. Management of the initiating firm must consider such reactions, the capacity, of the competitor to react, and the probable impact on the chosen strategy's success.

The beer industry provides a good illustration. In the early 1970s, Anheuser-Busch dominated the industry. Miller Brewing Company, recently acquired by Philip Morris, was a weak and declining competitor. Miller's management, contemplating alternative strategies, made the decision to adopt an expensive, advertising-oriented strategy. While this strategy challenged the big three (Anheuser-Busch, Pabst, and Schlitz) head-on, Miller anticipated that the reaction of the other brewers would be delayed due to Miller's current declining status in the industry. Miller proved correct and was able to reverse its trend in market share before Anheuser-Busch countered with an equally intense advertising strategy.

Miller's management took another approach in their next major strategic decision. In the mid-1970s they introduced (and heavily advertised) a low-calorie beer-Miller Lite. Other industry members had introduced such products without much success. Miller chose a strategy that did not directly challenge key competitors and, Miller anticipated, would not elicit immediate and strong counterattacks. This choice proved highly successful, because Miller was able to establish a dominant share of the low-calorie market before major competitors decided to react. In both cases, Miller's expectation of competitor reaction was key determinant of strategic choice.

Contingency Strategy

Ultimate strategic choices often depend on various assumptions about future conditions. The success of the strategy chosen is contingent, to varying degrees, on future conditions. And changes in the industry and environment may differ from forecasts and assumptions.

For example, Winnebago's strategy of centralized, economy-of-scale production and extensive inventories of large recreational vehicles (RVs) was contingent on a continued supply of plentiful, inexpensive gasoline for future customer use. With the Arab oil embargo, this contingency changed dramatically. Winnebago was left with extensive inventories of large RVs and high-break-even-oriented production facilities for large RVs. As a result, Winnebago was still trying to recover a decade later.

To improve their ability to cope in similar circumstances, an increasing number of firms have adopted a contingency approach to strategic choice. The critical assumptions on which success of the chosen strategy depends are identified. Conditions that may turn out to be different from the basic forecast or assumptions for these critical contingencies are identified, particularly negative ones. A downturn in the economy, a labor strike, an increase in the prime rate, a technological breakthrough, or a shortage of critical material are examples of such contingencies. Once these scenarios are identified, managers develop alternative, contingency strategies for the firm. Such contingency strategies can be short and/or long term and are appropriate at the corporate-, business-, and/or functional levels. Firms using this contingency approach often identify trigger points to alert management that a contingency strategy should be considered. The trigger points are specific deviations in key forecasts of industry or environmental conditions (like the supply and price of gasoline) and are set to alert management to the need to consider the alternative strategy and allow sufficient lead time for implementation of the contingency response. Strategic choice is made on the basis of certain conditions, assumptions, and premises. When there is a change of condition, a shift in assumptions, and when premises do not turn out to be wholly valid, then the strategy chosen becomes partly irrelevant. If such changes are drastic, the chosen strategies may have to be modified. Often, the shift in assumptions is sudden, leaving very little time for the strategists to reorient strategies. Contingency strategies are formulated in advance to deal with uncertainties that are a natural part of the business.

Most changes occur in a company's environment. Certain components of the environment, such as the social environment, alter gradually and such changes can be anticipated well in advance. Then there are other types of environment: for instance, market, regulatory or international environment, where changes could be sudden and leave little time for strategists to readjust to the situation.

The environment for different types of industries differs. Certain industries face a turbulent environment while others face a relatively placid environment. Businesses that exist in industries which face a turbulent environment feel a greater need for contingency strategies than those which exist in a relatively tranquil environment.

At present, there are many industries in India which operate in an environment characterised by fast-moving developments. The FMCG, power, telecommunications, information technology, and insurance sectors are illustrations of industries which have had to formulate contingency strategies to respond to the environmental situations as they occurred. Indian companies which follow a formal, structured approach to corporate planning take care to formulate contingency strategies in order to cope with environmental changes and the uncertainties associated with environmental forecasting.

Strategists at L&T developed three scenarios or models - pessimistic, most likely, and optimistic-based on different assumptions in relation to key variables. Another company which needed a reorientation of its strategies in the light of changes in government policy is Indal. The company, which was not doing well initially, tried for a merger with Mahindra & Mahindra unsuccessfully. In March 1988, the government allowed decontrol in pricing and distribution of aluminum, which was the main business of the company. This policy change caused the company to drop its plan to invest in other areas and instead focus on its aluminium business. Accordingly, expansion and diversification strategies were then formulated to capitalise on the new opportunities then available.

There are a few approaches to help companies develop and implement contingency strategies. One such approach is based on the model of contingency planning process. The model consists of three steps: identifying the contingent events; establishing the trigger points; and developing strategies and tactics. Essentially, the requirements of the model are to list events that may occur in the future which are critical to a company's strategy formulation process. Trigger points are established in the form of indicators which signal the impending occurrence of these events, after which strategies or tactics are employed to deal with the changed situation. This matter of reorienting the current strategies in the light of emerging environmental situations would be an issue to be discussed in the last phase of strategic management, namely, strategic evaluation and control. Contingency strategies have received a fair amount of attention from policy researchers as they are of immense value to strategists who have to deal with a transient phenomenon like the business environment.

Strategic Plan

A strategic plan (also called a corporate, group, or perspective plan), is a document which provides information regarding the different elements of strategic management and the manner in which an organisation and its strategists propose to put the strategies into action.

A comprehensive strategic plan document could contain the following information:

1. A clear statement of strategic intent covering the vision, mission, business definition, goals and objectives
2. Results of environmental appraisal, major opportunities and threats, and critical success factors
3. Results of organisational appraisal, major strengths and weaknesses, and core competencies
4. Strategies chosen and the assumptions under which the strategies would be relevant. Contingent strategies to be used under different conditions
5. Strategic budget for the purpose of resource allocation for implementing strategies and the schedule for implementation
6. Proposal organisational structure and the major organisational systems for strategy implementation, including the top functionaries and their role and responsibility
7. Functional strategies and the mode of their implementation
8. Measures to be used to evaluate performance and assess the success of strategy implementation

Typically, a strategic plan document could run into several pages and be treated as a formal report. Another possibility is that a brief document of three to five pages could briefly cover the points mentioned above. Much would depend on the nature and size of the company and the management policies regarding the preparation of the strategic plan document. It must be remembered, however, that when approved and accepted, a strategic plan document has to be communicated down the line to middle-level managers who will be responsible for its implementation.

Most large-size companies in India formulate strategic plans. Medium-sized and small-scale companies also perform the exercise though not necessarily in a formal and structured manner. The AIMA commissioned a nationwide study to find out what management techniques and tools companies are likely to employ. The study was conducted between April and June 1997. *Business Today* reported that 56 per cent of the total 160 companies surveyed had a published business strategy. Among these, 77 per cent were giant companies, 69 per cent were large, 53 per cent were medium-sized, and 45 per cent were small companies. The time period covered in the strategic plan was less than three years for 44 per cent of the companies; 40 per cent planned for three to five years time horizon, while 16 per cent did it for a period of more than five years. In terms of company size, 45 per cent of the giant companies

planned for more than five years, while 70 per cent of the small companies planned for a period of less than three years.

A special feature of strategic plans is that many companies consciously formulated their plans keeping in view the timeframe adopted for national-level planning. Thus, companies normally have a five-year planning period which is synchronized with that of the National Five-Year Plans. In fact, core public enterprises have to link their corporate plans with the national Five-Year Plans. Many public sector enterprises such as SAIL, BHEL, HMT and others have formulated corporate plans of varying duration. SAIL had drawn up an ambitious 15-year corporate plan till 2000_{AD}, while planning at BHEL has taken shape in the form of the first corporate plan which started in 1974.

Like public sector enterprises, private sector companies too formulate strategic plans. Multinational company (MNC) subsidiaries often have to prepare and plan the documents to be submitted to their parent companies for approval. Often, the MNC subsidiaries draw their strategic plans on the basis of guidelines provided by their parent institutions. Professional private sector companies may have executive committees consisting of senior level managers who formulate strategic plans. Family groups often draft group strategic plans to provide strategic directions to the different companies in the group.

The formulation of a strategic plan document provides a means not only to formalise the effort that goes into strategic planning but also for communicating to insiders and outsiders what the company stands for, and what it plans to do in a given future time period. A strategic plan is not always publicised. Rather, companies prefer to treat it as confidential, primarily for protecting their competitive interests. But the main features of the plan are often spelt out for communication to outsiders and for public relations purposes.

Chapter 11

Strategy Implementation – Aspects, Structures, Design and Change

The task of strategic management is far from complete after strategies have been formulated and a concrete strategic plan has been prepared. Then it is the job of strategists to put the plan into action. It is important to consider the interrelationship between the formulation and implementation of strategies. It is to be noted that the division of strategic management into different phases is only for the purpose of orderly study. In real life, the formulation and implementation processes are intertwined. Two types of linkages exist between these two phases of strategic management. The forward linkages deal with the impact of the formulation on implementation while the backward linkages are concerned with the impact in the opposite direction.

Forward Linkages

The different elements in strategy starting with the various constituents of strategic intent through environmental and organisational appraisal, strategic alternatives, strategic analysis and choice and ending with the strategic plan, determine the course that an organisation adopts for itself. With the formulation of new strategies, or reformulation leading to modified strategies, many changes have to be effected within the organisation. For instance, the organisational structure has to undergo a change in light of the requirements of a modified or new strategy. The style of leadership has to be adapted to the formulation of strategies. A whole lot of changes have to be undertaken in operationalising the formulated strategies. Clearly, the strategies formulated provide the direction to implementation. In this way, the formulation of strategies has forward linkages with their implementation.

Backward Linkages

Just as implementation is determined by the formulation of strategies, the formulation process is also affected by factors related with implementation. Recall that in the previous chapter, while dealing with strategic choice we observed that past strategic actions also determine the choice of strategy. Organisations tend to adopt those strategies which can be implemented with the help of the present structure of resources combined with some additional efforts. Such incremental changes, over a period of time, take the organisation from where it is to where it wishes to be.

It is to be noted that while strategy formulation is primarily an entrepreneurial activity, based on strategic decision-making, the implementation of strategy is mainly an administrative task based on strategic as well as operational decision-making. Looked at from another angle, formulation is a managerial task requiring analysis and thinking, implementation primarily rests on action and doing. The next section focuses on the various issues involved in the implementation of strategies.

Aspects of Strategy Implementation

The different aspects involved in strategy implementation cover practically every-thing that is included in the discipline of management studies. A strategist, therefore, has to bring to his or her task a wide range of knowledge, skills, attitudes, and abilities. The implementation tasks put to test the strategists' abilities to allocate resources, design structures and systems, formulate functional policies, take into account the leadership style required, and plan for operational effectiveness, besides, dealing with various other issues.

The Strategic plan devised by the organisation proposes the manner in which the strategies could be put into action. Strategies, by themselves, do not lead to action. There are, in a sense, a statement of intent: implementation tasks are meant to realise the intent. Strategies, therefore, have to be activated through implementation.

Strategies lead to several plans Each plan leads to several programmes. Each programme results in several projects. Projects are supported by funds through budgets. The administrative mechanisms of policies, procedures, rules and regulations support the working of the organisation while it implements the projects, programmes, plans, and strategies. In this manner, strategy sits at the top of a pyramid that has projects as its base as shown in Exhibit 11.1.

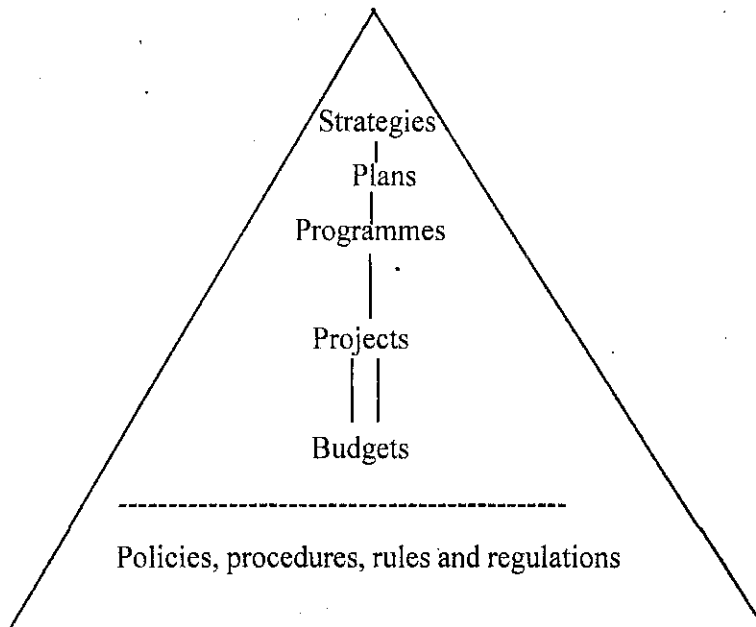


Exhibit 11.1: The Pyramid of Strategy Implementation

First of all, strategies should lead to plans. For instance, if stability strategies have been formulated, they may lead to the formulation of various plans. One such plan could be a modernisation plan. If expansion strategies have been adopted, various types of expansion plans will have to be formulated. An expansion plan could be designed to set up an additional plant to manufacture the same products. Similarly, diversification strategies could lead to new product development plans.

Plans result in different kinds of programmes. A programme is a broad term which includes goals, policies, procedures, rules and steps to be taken in putting a plan into action. Programmes are usually supported by funds allocated for plan implementation. An example of a programme is an R & D programme for the development of a new product.

Programmes lead to the formulation of projects. A project is a highly specific programme for which the time schedule and costs are predetermined. It requires the allocation of funds based on capital budgeting by organisations. Thus, R & D programmes may consist of several projects, each of which is intended to achieve specific and limited objectives, requires separate allocation of funds, and is to be completed within a set time schedule.

Projects create the needed infrastructure for the day-to-day operations in an organisation. They may be used for setting up new or additional plans, modernising the existing facilities, installation of newer systems, and for several other activities that are needed for the implementation strategies. A note of caution here: In practice companies may not make such a fine distinction among plans, programmes, and projects as we have done here. But as students of management we have to understand the difference and learn to distinguish between the different terms used in strategic management.

Implementation of strategies is not limited to the formulation of plans, programmes, and projects.

For the purpose of discussion and orderly presentation, we deal with the different aspects of implementation in the sequence indicated below. But it should be noted that the sequence does not mean that activities under each of the aspects are necessarily performed one after another. Many activities can be performed simultaneously, certain other activities may be repeated over time, and then there activities which are performed only once.

1. Project implementation
2. Procedural implementation
3. Resource allocation
4. Structural implementation
5. Behavioural implementation
6. Functional and operational implementation

While dealing with the several aspects given above, we have to cover a lot of ground in terms of concepts, methods, techniques and approaches. In practice a strategist would have to draw upon diverse specialisations available within the organisation. Experts from different areas such as project management, corporate management, legal affairs, finance, marketing, operations, and personnel, and economists, planners, technologists and others contribute in some or the other way in the implementation of strategies. It would be futile here to go into details of each and every aspect of implementation as the readers of this book will be aware of the different specialisation and functional areas. However, emphasis will be laid on how strategy affects the different implementation aspects and how they are adapted to suit the needs of a particular strategy. We move ahead on the assumption that a strategy creates its own requirements of the various aspects of implementation. As the strategy is modified or replaced with a new one, each of the aspects of implementation have to undergo a change. No wonder, strategy implementation is also - and rightly so-called by some as change management.

The strategy-implementation stage of strategic management is represented by the shaded portion of Exhibit 11.2. 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)!

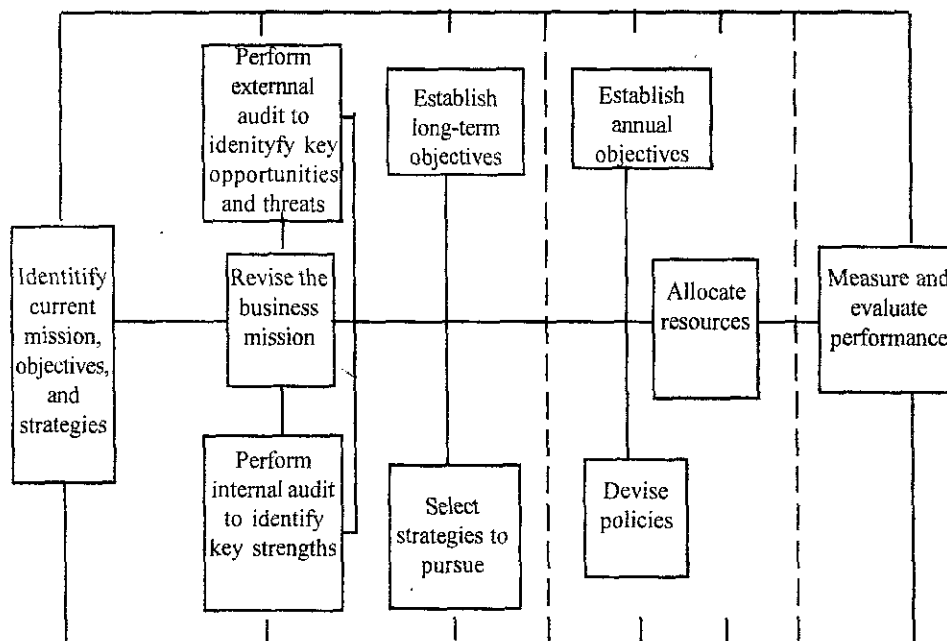


Exhibit 11.2: A Comprehensive Strategic Management Model

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 persons.

Strategy-formulation concepts and tools do not differ greatly for small, large, profit, or nonprofit organizations. However, strategy implementation varies substantially among different types and sizes of organizations. Implementing strategies requires such actions as altering sales territories, adding new departments, closing facilities, hiring new employees, changing an organization's pricing strategy, developing financial budgets, developing new employee benefits, establishing cost-control procedures, changing advertising strategies, building new facilities, training new employees, transferring managers among divisions, and building a better information system. These type of activities obviously differ greatly between manufacturing, service, and governmental organizations.

In all but the smallest organizations, the transition from strategy formulation to strategy implementation requires a shift in responsibility from strategies 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, revising reward and incentive plans, minimizing resistance to change, matching managers with strategy, developing a strategy-supportive culture, adapting production/operations processes, and developing an effective human resource function. 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.

Hamel and Prahalad emphasize the need for firms to develop a competitor focus at all hierarchical levels by gathering and widely distributing competitive intelligence; every employee should be able to benchmark her to his efforts against best-in-class competitors so that the challenge becomes personal. This is a challenge for strategies of the firm. Firms should provide training for both managers and employees to insure they have and maintain the skills necessary to be world-class performers.

Even after the grand strategies are determined and long-term objectives tentatively set, the strategic management process is far from complete. The tasks of operationlizing, institutionalizing, and controlling the strategy still remain. These tasks signal a critical new phase in the strategic management process: translating strategic thought into strategic action. Shifting from formulation to implementation gives rise to three interrelated concerns:

1. Identification of measurable, mutually determined annual objectives.
2. Development of specific functional strategies.
3. Communication of concise policies to guide decisions.

Annual objectives translate long-range aspirations into this year's budget. If annual objectives are well developed, they provide clarity, which is a powerful, motivating facilitator of effective strategy implementation.

Functional Strategies translate grand strategy at the business level into action plans for subunits of the company. Operating managers assist in developing these strategies, which, in turn, helps clarify what the manager's units are expected to do in implementing the grand strategy.

Policies are specific guides for operating managers and their subordinates. Policies, often misunderstood and misused, can provide a powerful tool for strategy implementation if they are clearly linked to operating strategies and long-term objectives.

Such measures as market share, ROI, return on equity (ROE), stock price, and new market penetration provide guidance in assessing the ultimate effectiveness of a chosen strategy. While such objectives clarify the long-range purpose of a grand strategy and the basis for judging its success, they are less useful in guiding the operating strategies and immediate actions necessary to implement a grand strategy.

A critical step in successful implementation of grand strategy is the identification and communication of annual operating objectives that relate logically to the strategy's long-term objectives. Accomplishment of these annual objectives adds up to successful execution of the business's overall long-term plan. A comprehensive set of annual objectives also provides a specific basis for monitoring and controlling organizational performance. Such objectives can aid in the development of "trigger points" that alert top management to variations in key performance areas that might have serious ramifications for the ultimate success of a strategy.

Annual objectives are specific, measurable statements of what an organization subunit is expected to achieve in contributing to the accomplishment of the business's grand strategy. Although this seems rather obvious, problems in strategy implementation often stem from poorly conceived or stated annual objectives. To maximize these objectives' contribution, certain basic qualities must be incorporated in developing and communicating them.

An annual objective must be clearly linked to one or more long-term objectives of the business's grand strategy. However, to accomplish this, it is essential to understand how the two types of objectives differ. Four basic dimensions distinguish annual and long-term objectives:

1. *Time frame.* Long-term objectives are focused usually five years or more into the future. Annual objectives are more immediate, usually involving one year.

2. *Focus.* Long-term objectives focus on the future position of the firm in its competitive environment. Annual objectives identify specific accomplishments for the company, functional areas, or other subunits over the next year.
3. *Specificity.* Long-term objectives are broadly stated. Annual objectives are very specific and directly linked to the company, a functional area, or other subunit.
4. *Measurement.* While both long-term and annual objectives are quantifiable, long-term objectives are measured in broad, relative terms; for example, 20 percent market share. Annual objectives are stated in absolute terms, such as a 15 percent increase in sales in the next year.

Annual objectives add breadth and specificity in identifying what must be accomplished in order to achieve the long-term objective. For example, the long-term objective "to obtain 20 percent market share in five years" Clarifies where the business wants to be. But achieving that objective can be greatly enhanced if a series of specific annual objectives identify what must be accomplished each year to achieve that objective. If market share is now 10 percent, then one likely annual objective would be "to achieve a minimum 2 percent increase in relative market share in the next year."

Specific annual objectives should provide targets for performance of operating areas if the long-term objective is to be achieved.

The link between short-term and long-term objectives should resemble cascades through the business from basic long-term objectives to numerous specific annual objectives in key operating areas. Thus, long-term objectives are segmented and reduced to short-term (annual) objectives. The cascading effect has the added advantage of providing a clear reference for vertical communication and negotiation, which may be necessary to ensure integrated objectives and plans at the operating level.

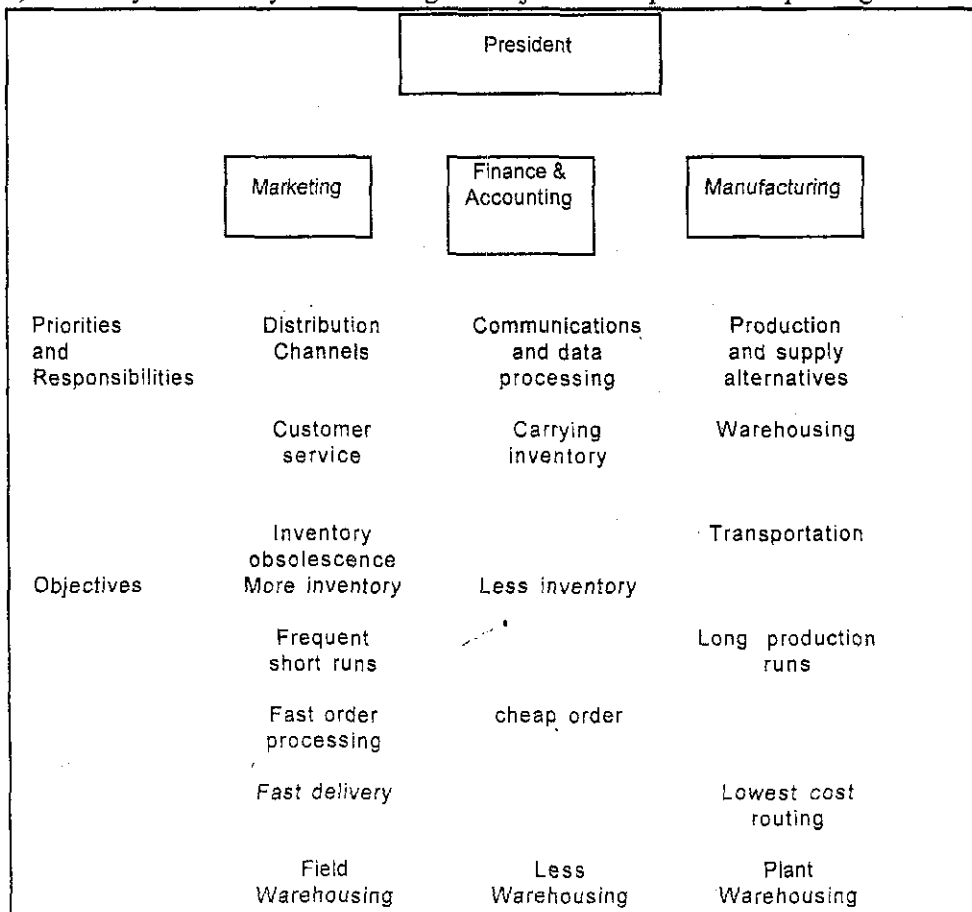


Exhibit 11.3: Logistic Priorities in a Manufacturing Firm

Implementation of grand strategies requires objectives that are integrated and coordinated. However, subunit managers (e.g., vice president of finance vice president of marketing, vice president of production) may not consider such a “superordinate” purpose in setting annual objectives. Consider the example in Exhibit 4.3. As can be seen, priorities of the marketing function can easily conflict with those of manufacturing or finance/accounting. For example, manufacturing might logically prefer long-production runs and plant warehousing to maximize efficiency. On the other hand, marketing might be better-served by frequent, short production runs and field warehousing to maximize customer convenience. Other functional conflicts are evident in Exhibit 11.3. Without concerted effort to integrate and coordinate annual objectives, these natural conflicts can contribute to the failure of long-term objectives (and the grand strategy), even though the separate annual objectives are well designed.

Successful implementation of strategy depends on coordination and integration of operating units. This is encouraged through the development of short-term (annual) objectives. Expressed another way, annual objectives provide a focal point for raising and resolving conflicts between organizational subunits that might otherwise impede strategic performance.

Managers should be involved at key points in the planning process so that annual objectives are integrated and coordinated. These managers are brought together to discuss important data, assumptions, and performance requirements. This promotes discussion of key interdependencies and a clearer, possibly negotiated determination of annual objectives in key performance areas. Particularly if major strategic change is involved, participation is essential both to establish the relationship of short-term operating activities and long-term strategy and to integrate and coordinate operating plans and programs.

Consistency in Annual Objectives

Experience indicates that managers in the same organization will have different ways of developing objectives. For example, managers in different functions, departments, or other subunits will often emphasize different criteria. Due to this lack of consistency, unit may not be comparable, commitment to objectives may differ, and the interdependence of units may be dysfunctional. For example, if the marketing area of the firm in Exhibit 11.3 had very clear, specific objectives regarding delivery time to customers while the manufacturing area’s objectives in this regard were ill defined, conflict might be frequent and counterproductive to the strategic success of the firm.

Annual objectives are more consistent when each objective clearly states what is to be accomplished, when it will be done, and how accomplishment will be measured. Objectives can then be used to monitor both the effectiveness of an operating unit and, collectively, progress toward the business’s long-term objectives. Exhibit 11.4 illustrates several effective and ineffective annual objectives. If objectives are measurable and state what is to be done and when it will be achieved in a clear, understandable manner, misunderstanding is less likely to occur among the interdependent operating managers who must implement the grand strategy.

Measurable. *Measurability* cannot be overemphasized as a key quality of annual objectives. Unfortunately, some key results are easier to measure than other. Line units (e.g., production) may easily be assessed by clear, quantifiable measures, while criteria for certain staff areas (e.g., personnel) are more difficult to measure. However, successful implementation requires setting measurable annual objectives in these difficult areas, as well. This is usually accomplished by initially focusing on *measurable activity*, followed by the identification of acceptable, measurable *outcomes*.

Examples of deficient annual objectives	Examples of annual objectives with measurable criteria for performance
To improve morale in the divisions (plant, department, etc.)	To reduce turnover (absenteeism, number of rejects, etc.) among sales managers by 10 percent by January 1, 1989. Assumption: Morale is related to measurable outcomes (i.e., high and low morale are associated with different results).
To improve support of the sales	To reduce the time lapse between order data and effort. delivery by 8 percent (two days) by June 1, 1989. To reduce that cost of goods produced by 6 percent to support a product price decrease of 2 percent by December 1, 1989.
To develop a terminal version of the SAP computer program.	to increase the rate of before- or on -schedule delivery by 5 percent by June 1, 1989. To develop a terminal version of SAP capable of processing X bits of information in time Y at cost not to exceed Z per 1000 bits by December 1, 1989. Assumption: There is virtually an infinite number of "terminal" or operational versions. Greater detail or specificity defines the objective more precisely.
To enhance or improve the training	To increase the number of individuals capable of performing X operation in manufacturing by 2 percent by April 15, 1989.
by July 15, 1989.	To increase the number of functional heads capable of assuming general management responsibility at the division level by 10 percent
training session.	To provide sales training to X number of individuals, resulting in an average increase in sales of 4 percent within six months after the
To improve the business's image	To conduct a public opinion poll using random samples in the five largest U.S. metropolitan markets and determine average scores on 10
dimensions of corporate responsibility by May 15, 1989.	To increase our score on those 10 items by an average of 7.5 percent by May 1, 1990.

Exhibit 11.4: Operationalizing Measurable Annual Objectives

Other qualities of good objectives acceptable, flexible, suitable, motivating, understandable, and achievable—also apply to annual objectives.

Another critical quality of annual objectives involves the need to prioritize short-term objectives. Due to timing considerations and relative impact on strategic success, annual objectives often have relative priorities. Timing considerations often necessitate initiating or completing one activity before another is started.

While all annual objectives are important, some deserve additional attention because of their particular impact on the success of a strategy. If such priorities are not discussed and indicated, conflicting assumptions about the relative importance of annual objectives might inhibit progress toward strategic effectiveness. Facing the real possibility of bankruptcy in 1983, Eastern Air Lines formulated a retrenchment strategy with several important annual objectives in labor relations, routes, fleet, and financial condition. But its highest priority involved maintaining the integrity of selected debt-related measures that would satisfy key creditors who could otherwise move to force bankruptcy.

Priorities are usually established in one of several ways. A simple ranking may be based on discussion and negotiation during the planning process. However, this does not necessarily communicate the real difference in the importance of objectives, so terms such as primary, top, or secondary may be used to indicate priority. Some businesses assign weights (for example, 0-100 percent) to establish and communicate the relative priority of each objective. Whatever the method, recognizing the priorities of annual objectives is an important dimension in implementing the strategy.

Systematic development of annual objectives provides a tangible, meaningful focus through which managers can translate long-term objectives and grand strategies into specific action. Annual objectives give operating managers and personnel a better understanding of their role in business's mission. This clarity of purpose can be a major force in effectively mobilizing the "people assets" of a business.

A second benefit involves the process required to derive annual objectives. If these objectives have been developed through the participation of managers responsible for their accomplishment, they provide an "objective" basis for addressing and accommodating conflicting political concerns that might interfere with strategic effectiveness. Effective annual objectives become the essential link between strategic intentions and operating reality.

Well-developed annual objectives provide another major benefit: a basis for strategic control. It is important to recognize here the simple yet powerful benefit of annual objectives in developing budgets, schedules, trigger points, and other mechanisms for controlling strategy implementation.

Annual objectives can provide motivational payoffs in strategy implementation. If objectives clarify personal and group roles in a business's strategies and are also measurable, realistic, and challenging, they can be powerful motivators of managerial performance-particularly when they are linked to the business's reward structure.

While annual objectives provide a powerful tool in operationalizing business strategy, they aren't sufficient in themselves. Functional strategies, the means to accomplish these objectives, must be clearly identified to encourage successful implementation. Changes in a firm's strategic direction do not occur automatically. On a day-to-day basis, policies are needed to make a strategy work. Policies facilitate solving repetitive or 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 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. About 80 percent of all corporations in the United States have instituted "No Smoking" policies.

Policies can apply to all divisions and departments (for example, "We are an equal opportunity employer") Some policies apply to a single department ("Employees in this department must take at least one training and development course each year"). Whatever their scope and form, policies serve as a mechanism for implementing strategies and obtaining objectives. Policies should be stated in writing whenever possible. They represent the means for carrying out strategic decisions.

Some example issues that may require a management policy are as follows:

- To offer extensive or limited management-development workshops and seminars
- To centralize or decentralize employee-training activities
- To recruit through employment agencies, college campuses, and/or newspapers
- To promote from within or hire from the outside
- To promote on the basis of merit or on the basis of seniority
- To tie executive compensation to long-term and/or annual objectives

- To offer numerous or few employee benefits
- To negotiate directly or indirectly with labor unions
- To delegate authority for large expenditures or to retain this authority centrally
- To allow much, some, or no overtime work
- To establish a high or low-safety stock of inventory
- To use one or more suppliers
- To buy, lease, or rent new production equipment
- To stress quality control greatly or not
- To establish many or only a few production standards
- To operate one, two, or three shifts
- To discourage using insider information for personal gain
- To discourage sexual harassment
- To discourage smoking at work
- To discourage insider trading
- To discourage moonlighting

Project Implementation

Strategies lead to plans, programmes, and project. Knowledge related to project formulation and implementation is covered under the discipline of project management. The Project Management Institute of the US defines a project as "a one-shot, time-limited, goal-directed, major undertaking, requiring the commitment of varied skills and resources". The goals or objectives for a project are derived from the plans and programmes, which are based on the strategies adopted. A project passes through various phases before a set of tasks can be accomplished.

Phases of Project

A project through different phases, not necessarily in the order listed below.

1. **Conception phase:** This phase is an extension of the strategy formulation phase of strategic management. Ideas generated during the process of strategic alternatives and choice consideration from the core of the future projects that may be undertaken by the organisation. The project ideas that are conceived have to be allocated priorities on the basis of which they will be chosen for further development.
2. **Definition phase:** After a set of projects have been identified and arranged according to the priority, they have to be subjected to a preliminary project analysis which examines the marketing, technical, financial, economic and ecological aspects. This analysis is done to find out whether it would stand the scrutiny of the financial institutions, banks and investors. After this screening, the viable projects are taken up and feasibility studies conducted. Feasibility studies are done for in-depth, detailed project analysis and result in an adequately formulated project. The results are documented in the form of a project feasibility report.

(Exhibit 11.5 provides an idea of what a project feasibility report may contain)

Project reports are prepared for internal as well as external purposes. Internally, the reports may be presented to the top management committees or Board of Directors for approval and sanction. Externally, the reports are submitted to financial institutions which evaluate the project proposals for the purpose of granting financial assistance.

Currently, the central financial institutions (IDBI, ICIC, IFCI, etc.) seek the following information for the purpose of financial assistance

1. General information, such as, name, form of organisation, location, nature of project (new, expansion, modernisation/diversification), nature of industry and products, and so on.
2. Information regarding project promoters
3. Particulars of the industrial concern seeking financial assistance
4. Particulars of the project (details regarding capacity, process, technical arrangements, management, location and land, buildings, plants and machinery, raw materials, utilities, effluents, labour, housing for labour, schedule of implementation, etc.)
5. Cost of the project including land and site development, buildings, plant and machinery, technical know-how fee, and so on
6. Means of financing (share capital, rupee loans, foreign currency loans, debentures, internal cash accruals, etc.)
7. Marketing and selling arrangements
8. Profitability and cash flow
9. Economic considerations (prices of competing products, economic benefits to the country and region, development of industrially backward areas, development of ancillary industries, etc.)
10. Environment considerations (water and air pollution, effluent disposal, and energy conservation)
11. Government consents including letter of intent, industrial license, capital goods clearance, import license, foreign exchange permission, approval of technical/financial collaboration, clearance by regulatory authorities, and so on.

Exhibit 11.5: The Contents of a Typical Feasibility Report

After the project definition phase, the project is cleared for implementation: But before being implemented, the project has to be further planned.

3. **Planning and organising phase:** Detailed planning, related to different aspects of the projects, such as, infrastructure, engineering designs, schedules and budgets, finance, and so on, has to be completed. A project structure which would deal with the organisation and manpower, systems and procedures, and so on, has also to be created which would enable the project manager to implement the project.
4. **Implementation phase:** The detailed engineering, order placement for equipments and material awarding contracts, civil and other types of construction, and so on, have to be undertaken during the implementation phase leading to the testing, trial, and commissioning of the plant.
5. **Clean-up-phase:** The final phase in project implementation deals with disbanding the project infrastructure and handing over the plant to the operating personnel.

It is to be noted that the above phases in projects are more relevant to new plants that are being set up to implement expansion and diversification strategies. But for other minor projects like a relocation of facilities, modernisation and upgradation of technology, and so on, a similar, though less detailed process, may be followed.

Procedural Implementation

Any organisation which is planning to implement strategies must be aware of the procedural framework within which the plans, programmes, and projects have to be approved by the government at the central, state and local levels. The procedural framework consists of a number of legislative enactments and administrative orders, besides the policy guidelines issued by the Government of India from time to time.

The regulatory mechanisms for trade, commerce, and industry span the whole range of legal structure from the Constitution of India, the Directive Principles, Central laws, State laws, general laws, sector-specific laws, industry-specific laws, and the rules and procedures imposed by the implementing authorities at the local level. The laws lay down elaborate rules and procedures to be followed.

Following the procedures laid down for project implementation constitutes an important component of strategy implementation in the Indian context. The Government has an elaborate set of procedures depending on the type of project to be implemented. Government agencies at the central and state levels play a major role while some procedures require the involvement of the local governmental agencies. All the subjects having a bearing on industrial development are handled by different ministries and departments at the central government level. There are apex level committees such as the Cabinet Committee on Economic Affairs. Apart from these agencies, the regulatory agencies, such as, Central Electricity Regulatory Commission (CERC), Telecom Regulatory Authority of India (TRAI), Insurance Regulatory and Development Authority (IRDA), also play a significant role. At the State level, the Directorate of Industries is the pivot around which the entire industrial activity in the State revolves.

Government policies, laws, rules and regulations and procedures are constantly under change specially under conditions where India is fast adapting to the international environment and incorporating liberalisation and globalisation measures in its policies.

Our purpose here is to only briefly refer to the procedural aspects of strategy implementation. The matter here is not meant to be a presentation of a comprehensive manual or guidelines for setting up projects in India. For that to take place, readers would have to refer to specialised subjects such as business and law, and the entrepreneurs would have to take recourse to specialised advice from chartered accountants, company secretaries, industry experts and consultants. You are advised to find out the latest available position regarding these regulatory mechanisms and procedures from the business press.

The regulatory elements to be reviewed are as below.

- Formation of a company
- Licensing procedures
- Securities and Exchange Board of India (SEBI) requirements
- Foreign collaboration procedures
- Foreign Exchange Management Act (FEMA) requirements
- Import and export requirements
- Patenting and trademarks requirements
- Labour legislation requirements
- Environmental protection and pollution control requirements
- Consumer protection requirements
- Incentives and facilities benefits

Formation of a Company

The formation of a company is governed by the provisions of the Companies Act, 1956 and consists of promotion, registration, and flotation. Promotion denotes the preliminary steps taken for the purpose of registration and flotation. Registration involves registering the memorandum of the company, articles of association, and the agreements with the Registrar of Companies, who issues a certificate of incorporation. Flotation means raising the capital to commence business.

Licensing Procedures

They system of planning (or planned development) rests on three policy documents consisting of Industrial Policy Resolution, 1956, Industries (Development and Regulation) Act (IDRI), 1951, and the statements of 1978, 1980, 1982, and 1991. The Policy Resolutions classify the industries into three categories. The first category industries are those that are directly under the government. The second category consists of industries which are promoted by the government and where the private sector supplements the efforts. The third category industries are left for the private sector. The IDRA, 1951 provided for a licensing system for the development and regulation of scheduled industries-those industries listed in the Schedule of the Act.

A license is a written permission from the government an industrial undertaking to manufacture specified articles included in the Schedule. If the license is to be given subject to the fulfillment of certain conditions (say, foreign collaborations or capital goods import) then a letter of intent conveying the intention of the government to grant a license, subject to the fulfillment of those conditions, is issued. Section 30 of the IDRA deals with the Registration and Licensing of Industrial Undertaking Rules. Under this Act, a license was necessary for establishign a new unit, manufacturing a 'new article' (any item related to a scheduled industry other than those specified in the license), substantial expansion of capacity in an existing business, and changing location.

One of the significant liberalisation measures in the post-1991 period has been to abolish industrial licensing, irrespective of the level of investment, for all industries except a few. These industries relate to security, defence, or environmental concerns and certain items of conspicuous consumption that have a high proportion of important inpts.

The licensing procedure requires the applicant to approach the Secretariat for Industrial Assistance (SIA), which is a common secretariat for receiving and processing all types of applications related to industrial project.

SEBI Requirements

The SEBI Act, 1992, replaced the Capital Issues Control Act, 1956, to deal with the capital markets. It had already been in existence since 1988 and became a statutory body in 1992. According to the SEBI Act, the SEBI has three objectives: to protect the interests of investors in securities, to promote the developmnt of the securities market, and to regulate the securities market. It is a quasi-judicial body, under the Securities Laws Ordinance, 1995, to deal with issue of capital, transfer of shares, and other related aspects. Its jurisdiction covers the primary market, secondary market, mutual funds, foreign institutional investors, and foreign brokers.

Though certain provisionss of the Companies Act, 1956 cover the issue of capital control, the SEBI enjoys comprehensive power of the significant aspects of the Indian capital market. It issues guidelines from time to time to oversee matters under its control. These guidelines are of relevance to companies accessing the capital market for funds for projects emanating as offshoot of their corporate and business strategies. For the purpose of stratey implementation, this Act is relevant so far as the provision of financial resources is concerned. Apart from this, this Act also affects mergers and amalgamations as they regulate the capital reorganisation plans for mergers.

Foreign Collaboration Procedures

Many strategic alternatives (for instance, expansion/diversification into high technology industries) call for foreign collaboration and investment. The government policy, in general, allows foreign investment and collaboration in a selective basis in priority areas, export-oriented or high-technology industries; and permitting existing foreign investment in non-priority areas.

All proposals to set up projects with foreign collaboration require prior government approval. The regulatory framework deals with the need for foreign technology, royalty payments, terms and conditions for collaboration agreements, and foreign investment.

Foreign investments are of two types: foreign direct investment (FDI), and foreign institutional investment (FII)

portfolio investment. FDI can take place through wholly-owned subsidiaries, joint ventures, or acquisition. Portfolio investment takes place through investment by the foreign institutional investors and investments in instruments such as global depository receipts (GDRs) and foreign currency convertible bonds (FCCBs). Special treatment is accorded to non-resident Indians (NRIs) and overseas corporate bodies (OCBs), predominantly owned by NRIs, in matters of foreign investments.

Joint ventures have been considered an important route for channelising foreign investments into and outside India. Apart from regulations concerning joint ventures in India, government policy is encouraging the setting up of joint ventures abroad. The RBI, Foreign Investment Promotion Board (FIPB), and Project Approval Board are the major regulatory agencies for joint ventures abroad.

The procedural aspects of foreign collaboration include preliminary evaluation by the promoter, obtaining industrial license (if necessary), applying for foreign collaboration to the concerned agency, applying for import of capital goods (if required), finalisation of agreement, and clearance from the RBI.

Foreign Exchange Management Act (FEMA) Requirements

The Foreign Exchange Management Act (FEMA) replaced the Foreign Exchange Regulation Act (FERA), 1973 in June 2000. The FEMA, 2000 has substantially liberalised provisions and rules related to the maintenance of dollar accounts by exporters, remittance of foreign exchange for visits abroad, agency commission, export claims reduction in export value, reimbursement of expenses incurred on dishonoured export bills, consular fee, and so on.

Foreign exchange transactions are classified as current account and capital account transactions. Several sets of rules have been made to facilitate foreign exchange transactions for the purpose of augmenting export activities from India. Exports of goods and services are governed under the Foreign Exchange Management (Export of Goods and Services) Regulations, 2000. The opening, holding, and maintaining of foreign currency accounts is governed by the Foreign Exchange Management (Foreign Currency Account by a Person Resident in India) Regulations, 2000. In keeping with the imperatives of globalisation, foreign exchange remittances for maintaining overseas branches and offices by Indian companies have been considerably liberalised.

Import and Export Requirements

Strategy implementation in areas such as modernisation, expansion, and diversification requires the consideration of import and export requirements. Imports are vital for capital goods and raw materials provision for new and existing projects. The high priority accorded to import substitution by the government often offers a viable alternative to companies for setting up new projects or for introducing new products or services. Export considerations by the companies by companies usually arise in the form of statutory stipulation in lieu of foreign collaboration and investments, and imports. In certain cases, exports offer an expansion opportunity for companies which operate in markets which are highly competitive or saturated. Thus, imports and exports requirements constitute an important part of any strategy implementation scheme.

The Export-Import Policy (Exim Policy) enunciates the foreign trade policy of the country. It is generally announced for a period of five years corresponding to the five-year planning period. The policy implementation and the legal framework for imports and exports in India is largely based on the Foreign Trade Development and Regulation Act (FTDRA), 1992, that replaced the Import and Export (Control) Act, 1947. The objective of the Act is to provide for the development and regulation of foreign trade by facilitating imports into, and augmenting exports from India.

The Department of Commerce in Ministry of Commerce is responsible for the country's external trade and all matters connected with commercial trade relations with other countries. There are several autonomous bodies, such as, commodity boards, export inspection council, export promotion councils, public sector undertakings such as the State Trading Corporation of India, among others under the administrative control of the Ministry of Commerce.

The FTDR Act provides for the appointment of the Director General of Foreign Trade who is responsible for advising on the formulation and implementation of the Exim Policy. Besides the Directorate General of Foreign Trade, there is Directorate General of Commercial Intelligence and Statistics for collection, analysis, and dissemination of commercial information related to foreign trade.

It is important for strategists to understand the rationale for the development and regulation of imports and exports. The government is interested in imports regulation because it apportions the available foreign exchange among different types of users, aims at import substitution progressively so that the balance of payments (bop) position is not affected adversely, and for the protection of domestic industries. Exports are considered obligatory in many cases, including those of FEMA companies. Fiscal measures are adopted by the government to discourage imports and exports of certain products. The matter of exports and imports has a substantial number of procedural aspects and associated documentation work. Other important matters are related to customs, financing of imports, foreign exchange, and incentives and support for export activities. The supportive measures for exports will be referred to in a later section which deals with incentives and other facilities. Most companies have to rely on exports and imports in the course of their strategy implementation. Specialised knowledge and advice is required to follow the procedures which are quite detailed and comprehensive.

Patenting and Trademarks Requirements

Patents, trademarks, copyrights, designs, and so on, are assuming greater significance in the Indian industry owing to international environmental changes. The major impact on these issues is of the WTO requirements related to the Trade Related Aspects of Intellectual Property Rights (TRIPs). The increasing competitiveness means that it is necessary to know the rights and privileges, and the legal procedures for protecting products and ideas. Familiarity with the law related to these is use has, therefore, become essential for strategy implementation. These laws are of special significance to industries, such as, chemicals, computer software, entertainment, food, and pharmaceuticals, where patents are a major competitive tool.

India is in the process of adapting its law related to patents and trademarks in line with the international requirements. Indian Patents Act, 1970 governs patenting in India, and it has been amended in the form of Indian Patents (Amendment) Act, 1995 to incorporate the intellectual property rights requirements. The Trade and Merchandise Marks Act, 1958 provides for the registration and better protection of trademarks and for the prevention of the use of fraudulent marks on merchandise. The Copyrights Act, 1957 relates to copyrights. These Acts define the terms, prescribe the procedures for registration, and mention the rights and duties of the entities holding the patents, trade marks, and copyrights.

Labour Legislation Requirements

An essential part of procedural implementation in any project as well as in a going concern is that of labour legislation. For the companies, labour constitutes a significant resource for the purposes of strategy implementation. For the government, the protection of labour interest has long been held to be a major responsibility of the State.

Labour legislation consists of several laws related to different aspects. A classification of these laws is as below:

1. Labour laws related to the weaker sections such as women and children
2. Labour laws related to specific industries such as mines and minerals, plantation, transport, construction, contract labour, and others.
3. Labour laws related to specific matters such as wages, social security, bonus, and so on.
4. Labour laws related to trade unions, industrial relations and worker's participation in management

According to the Indian Constitution, labour is a common subject among the Central and the State governments. Work

the Central government enacts, amends and repeals most of the legislation, the major administrative authority to adopt and implement the laws rests with the state governments. Besides the Central and State ministries of labour, there are a host of commissions, standing committees, statutory agencies, labour courts and tribunals, boards, and so on, to implement the labour legislation.

An aspect related to labour is the issue of exit policy. It refers to the policy concerned with the action to be taken regarding surplus manpower in companies, owing to a variety of reasons, such as, restructuring, retrenchment, closure, or technological developments. Voluntary retirement schemes and golden handshake schemes are quite popular in the Indian industry, particularly, in the public sector enterprises, banks, large private companies, and other overmanned organisations. There is no specific policy or law dealing with exit, and the actions are governed under the existing laws and regulations as and where they are applicable. However, the exit policy is gradually coming under formation and informed opinion is that a time may come when there will be adequate political will to enact and implement it. Exit policy, and the resultant rules and procedures have relevance to strategy implementation in cases of retrenchment grand strategies and the formulation and implementation of functional strategies related to human resource management.

The matter of procedural implementation regarding labour legislation has a significant bearing on the implementation of strategies in the areas of objective-setting, strategic choice, social responsibility, formulation and implementation of human resource management, and operational strategies.

Environmental Protection and Pollution Control Requirements

The issue of physical environment has attained global and national importance owing to a variety of reasons. Overuse and misuse of the basic life support systems and natural resources like air, land, water, flora and fauna, and non-renewable sources, such as, oil and natural gas, are cited as major factors leading to environmental and ecological degradation. The Indian public's awareness has also heightened considerably with controversies regarding disasters, such as, the Bhopal Gas Tragedy of 1984 and, more recently, the Sardar Sarovar and Narmada Sagar dam projects, and the relocation of polluting industrial units outside the urban periphery occupying the headlines. "Environmental aspects of nuclear power, the disappearance of plant and animal genetic resources, the limitations of existing pollution control technologies in industry, the destruction of wetlands and other special habitats and other issues" now engage the popular attention in India. Industrial activity contributes to environmental degradation in the form of air, water, land, and noise pollution affect the biodiversity of a region.

There are a host of Central and State laws dealing with the prevention and control of pollution and environmental protection. Some of these are: The Environment (Protection) Act, 1986; The Water (Prevention and Control of Pollution) Act, 1974; The Air (Prevention and Control of Pollution) Act, 1981; The Wildlife (Protection) Act, 1972; and The Forest (Conservation) Act, 1980. Besides there are elaborate procedures laid down under rules such as the Hazardous wastes (Management and Handling) Rules, 1989 and the Manufacture, Storage and Import of Hazardous Chemicals Rules, 1989.

The major responsibility to deal with environmental issues lies with the State Pollution Control Boards. The boards implement the pollution control laws. Any new project has to seek a no-objection certificate from the board, which then regulates and monitors the emission and discharge of hazardous wastes. Such monitoring takes place on the basis of standards, including ambient air quality standards for discharge of effluents and emission of smoke and vapour, and noise.

Project implementation, particularly in the case of process-based and chemical industries, requires adherence to the procedures laid down for environmental protection and pollution control.

Consumer Protection Requirements

In the course of strategy implementation, companies are increasingly required to conform to legislative measures to protect the consumers. The very fact that 'consumer protection' is an accepted term denotes that there is apprehension that consumers may be subjected to unethical and unfair acts of companies and they need to be protected through the law. The growth of consumerism and consumer awareness, coupled with growing competition, makes it imperative that companies conform to the procedures laid down in the law regarding consumer protection. Besides the law, there is also the social requirement of being perceived as a consumer-friendly organisation.

In India, consumer protection is ensured through a plethora of legislation. Some of these are: Essential Commodities Act, Trademarks and Merchandise Act, Sale of Goods Act, Standard Weights and Measures Act, and the IDR Act. However, the central legislation is the Consumer Protection Act, 1986, amended through the Consumer Protection (Amendment) Ordinance, 1993. This Act provides for the protection of consumer rights and the redressal of consumer disputes.

The Consumer Protection Act provides for the establishment of a Central Consumer Protection Council and State Consumer Protection Council in each State. The Department of Food and Civil Supplies is the nodal ministerial agency for the enforcement of the Act. The Act also provides for a three-tier consumer disputes redressal system at the District, State, and Central levels. At the district level, there is a District Forum, a State Commission at the State level, and a National Commission at the central level. These fora are primarily for the purposes of consumer disputes redressal and remedial action by the companies.

According to the Competition Act referred to above, consumer courts will be the sole guardians of consumer interests since the Competition Commission of India shall not deal with these matters.

The issue of consumer protection is highlighted in the procedural implementation at the level of business and operational strategies, and in the implementation of functional policies related to operations, quality, and marketing.

Procedures for Availing Benefits from Incentives and Facilities

Project implementation to put a strategy into action requires a consideration of various incentives, subsidies, and facilities. It is beneficial for entrepreneurs to be aware of these so that due advantage can be taken of these.

In providing incentives, and so on, the government does not play a regulatory but a promotional role. This role is manifested in various forms. In line with the objectives laid out in the Industrial Policy resolution, the government attempts to achieve employment generation, correction of regional imbalances, promotion of export-oriented industries and utilisation of installed capacity through higher production levels and productivity.

The primary instrument for achieving national plan objectives is regulation. Promotional activities, however, do play an important role. The fiscal, monetary, and budgetary policies of the government are aimed at the stimulation of activity in the priority industrial sectors. Discretionary control over money supply and banks and financial institutions' lending rates are used to affect industrial activity. Budget pronouncements may result in the reduction of excise duties, corporate and personal taxation rates, and so on, which increase the availability of finance for expansion activities.

The government also plays a promotional role in terms of purchasing, pricing, distribution, availability of raw materials, and provision of infrastructural facilities. A number of industries are critically dependent on government purchases. The Directorate General of Supplies and Disposal is the largest purchasing agency in the country. The system of administered pricing has a far-reaching impact on many industries, such as, steel, cement, fertilizers, and others. The distribution of many goods, such as, steel, cement, fuel (commonly known as essential commodities) affects industries such as, sugar, vanaspati, edible oils, common cloth, and several others. The government also undertakes the supply of essential raw materials or scarce imported raw materials (e.g. newsprint) which affects the supplier environment in many industries. In many industries, the CSFs include the regular availability of vital raw material in sufficient quantities.

Through the provision of infrastructural facilities, such as, power, water, skilled manpower, banking and financial services, health services, public utilities like transportation, and industrial sites and sheds, the government seeks to ensure balanced regional development through a dispersal of industries.

Various state governments and Union Territory administrations offer additional schemes. The schemes are administered through the central and state level ministries and departments by involving financial institutions. Expansion strategies can be implemented profitably if the various incentives can be availed of under the different government schemes. In the special case of small-scale industries wishing to implement their strategies, many benefits can be availed of under the comprehensive of Small-Scale Industries and its numerous agencies situated at various places in India. Export promotion efforts by the government take the form of several incentives like liberal import facilities, priority in financing and transportation, and so on. 100 per cent export-oriented units and units in free-trade zones enjoy special incentives and facilities.

From the point of view of strategic management, all the above measures undertaken by the government are highly relevant for business organisations. Strategic decision-making has to take these factors into account in objective-setting, strategic choice, and strategy implementation.

Overview of Procedural Implementation

In the preceding section, we have attempted to provide information related to a broad range of elements in the regulatory framework within which Indian organisations have to operate. It is to be observed that the role of the government is quite comprehensive and affects practically each and every aspect of an organisation's management, especially activities related to strategic management. While there are differing viewpoints regarding the extent the manner in which the regulatory framework should operate, an 'existentialist' view for strategists is to continually look for opportunities within the business environment, as such an environment is primarily the creation of government plans, priorities, policies and actions. Strategy formulation and implementation within organisations have to follow the ground rules laid by the government closely. We have indicated the major regulatory and promotional aspects that have to be considered by strategists. Many areas remain, for instance, the matter of direct and indirect taxation to be dealt with the relevant laws and procedures, or industrial sickness to be dealt with under the Sick Industrial Companies (Special Provisions) Act, 1985. These are areas that deal with special situations. Strategists would have to be aware of the details of procedural implementation relevant to the industry to which their companies belong.

Several organisations—usually large ones and ironically, even public enterprises—have to maintain a close liaison with various governmental agencies in order to get approvals, sanctions, permissions, and statutory benefits. This liaison is usually exercised through formal as well as informal means. Formally, companies maintain liaison offices in New Delhi and the state capitals, or employ advisors and consultants who assist and guide the organisation regarding procedural matters. Companies going in for expansion strategies, particularly diversification, usually look for industry experts and consultants who can advise them on all the aspects of the establishment of a project and guide them through the maze of governmental regulations. Most companies retain, commission or contract out the services of chartered accountants, company secretaries, legal experts and lawyers to advise them on procedural and legal matters. Informally, organisations seek to coordinate the influence governmental action through unconventional means, such as, political donations and lobbying.

Project and procedural implementation results in the necessary infrastructure and the required permission for an organisation to proceed with other aspects of strategy implementation. The first issue that a strategist is called upon to deal with is resource allocation and this is the subject matter of the next section.

Resource Allocation

Strategists have the power to decide which divisions, departments, or SBUs are to receive how much money, which facilities, and which executives. This is what we mean by resource allocation.

The resource allocation decisions are very similar in that they set the operative strategy for the firm. Assume, for example, that resources are allocated to existing units on some formula basis (e.g., 10 percent above last year's budget). The implicit operative strategy is pace expansion. If the official strategy is expansion in some lines of business with stability in others, then greater resource flows to areas targeted for expansion are necessary to give force to the strategy. The formula approach (such as 10 percent above last year's budget for all lines of business) would not reinforce such a strategy. What is important to understand is that once the strategic choice is made, resources must follow the strategy, or we haven't put our "money where our mouth is." SBU and lower managers are smart. If a firm's strategists describe a strategy in words but do not shift money and executive talent and other resources to support it, the strategy will be considered a paper strategy. As with objectives, there can be a difference between "official" and "actual" strategy. So resource allocation decisions about how much to invest in which areas of the business reinforce strategy and commit the organization to its chosen strategy.

Let's consider how resource allocation is important to several strategic options. If new-product development is seen as the key to an active offensive strategy, more funds and personnel will be needed in research and development, with the possibility of longer-term capital expenditures for a new plant or new equipment. If the strategy calls for expansion in new markets, greater flows of funds for advertising, sales personnel, and/or market research will be required. If retrenchment is under way, resource allocation is of particular significance. Care must be taken to protect units which provide long-term competitive advantages. Unfortunately, the "easy way out" is often used -everyone is cut back equally, or resource flows are reduced for units which have a longer-term payout but are short-term users of resources without commensurate revenue generation. The usual example is to cut R. & D or maintenance-the very places where long-term developments may be most critical for future competitive advantage. Thus shortsighted resource allocation decisions may come at the expense of the ability to pursue a long-term strategy.

Of course, resource allocation decisions are linked to objectives through the strategies being implemented. Decisions about dividend policies, for instance, are important in relation to objectives and the long-term ability to attract sources of capital. Thus how to share expected profits among investors, management, the labor and whether to reinvest in the business are important resource allocation choices with long-term strategy implications. External parties play a major role. For instance, government regulations may require a firm to invest large amounts of capital in "nonproductive" assets such as pollution-control equipment. Influential stockholders may force the firm to make greater dividend payouts. Thus the strategic agenda is partially set by the factors influencing the setting of objectives, since they will limit the resources available for implementing strategy as expressed in the allocation decisions. Finally, resource allocation is linked to the development of competitive advantage.

It is presumed that those approaches were considered during strategy formulation. The key here is to make sure that preferential distribution of capital goes to the most critical units-the units where the strategy is directed at creating competitive advantages.

This is one tool that strategists can use to link resource allocation decisions to choice of strategy. If you recall, several prescriptions for investment and cash flow decisions were made depending on the type of SBU identified in the matrix. Thus "cash cows" are SBUs from which resources can be obtained for allocation to "question marks" or "stars." Of course, we suggested that there are several problems with this approach for strategic choice, and they apply here as well. For instance, resource allocation for new SBUs with initially low market shares might be overlooked

But for multiple SBU firms this is one tool to aid thinking about how to allocate resources.

The primary approach to resource allocation in the implementation process is through the budgeting system. One system for budgeting resources within one firm is the product life cycle budgeting system used by Lear Siegler. This firm believes that the product life cycle of the product lines should influence its budgeting of resources. It believes that cash flow, departmental expenses, revenues, and capital expenditures should vary during the cycle. Therefore the balance sheets and income statements should look different at different stages of the cycle. The firm suggests adjusting resources accordingly. Thus to the extent that the product life cycle influences strategy, budgets tied to such a cycle will affect the product strategy. Others agree with this approach and suggest that zero-based budgeting is particularly useful when retrenchment strategies are being used.

From a long-term perspective, the capital budget is very critical. Here, plans for securing and distributing capital for large-scale investments are needed to accomplish strategy. Mergers, introductions of major new product lines, an increase in plant capacity and vertical integrations are key mission changes which will require long-term capital investment decisions.

The more routine year-to-year allocation decisions are made within this context. But they are also important for making sure that the strategic direction of the firm is being followed, and they serve as a guide to future strategy. So let's look at this budget process in more detail.

Remember that resource allocation as expressed in the budget needs to be carefully linked to strategy. Exhibit 11.6 shows one explanation of how these can be linked in a multiple-SBU firm. Note that the process will involve planning at various levels in a back-and-forth fashion over time. In a series of negotiations among managers at the SBU and corporate levels, the strategy and plans to implement it are worked out. The final output is a set of budgets which give force to the overall plan. Let's look at these stages of the budgeting process in a bit more detail.

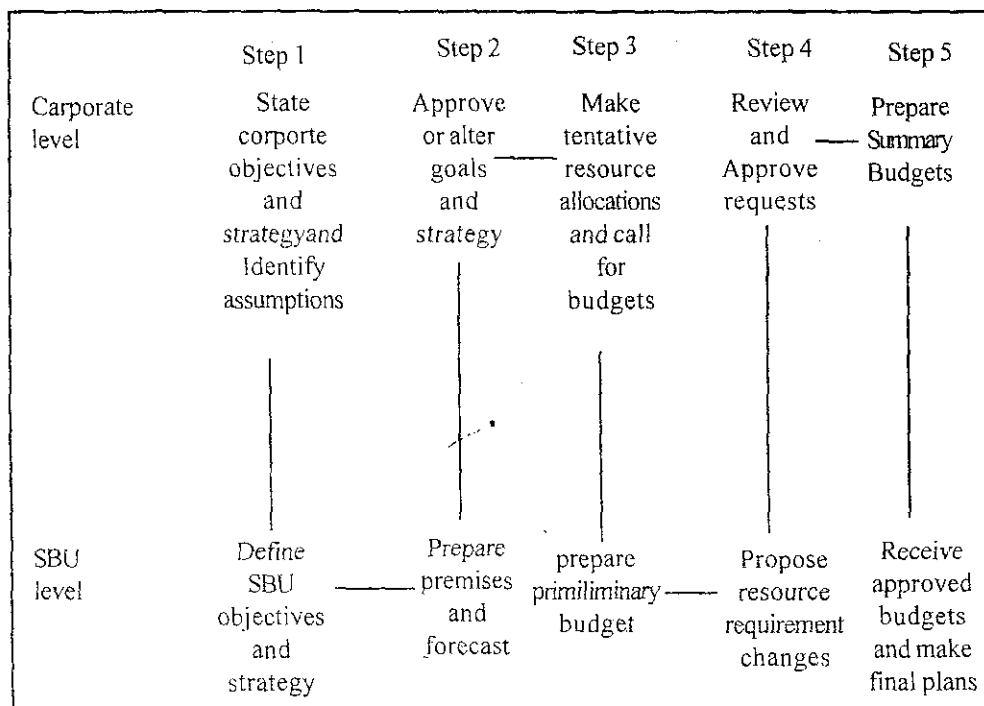


Exhibit 11.6: A Frame Work for the Strategic Budgeting Process

Step 1

Top management initiates the budgeting process. It does this by communicating the objectives of the firm for the period. It also announces the assumptions it uses the predicted economic and competitive conditions, for instance to set these objectives.

Of the various internal planning premises and assumptions which must be formulated, the sales forecast is clearly the most fundamental. Indeed, since anticipated product demand must be determined before budgets and plans for resource inputs are made, the sales forecast is typically cited as the basis or “key” for all internal planning. Among other things, the sales forecast is the basis for production planning, materials planning, capital planning. Moreover, projected sales, in whatever form tax revenues for a city, dollar output for a company, or donations for a charity constitute the revenue side of an organization’s income statement. Thus on the basis of forecasted sales, an organization is able to project production requirements, establish what materials need to be purchased, determine the number of personnel to be recruited, estimate the level and timing of required financial resources, and decide what it can afford in the way of operating expenses (such as those for advertising and sales promotion) for the purpose of exacting a certain profit level.

Step 2

The budget department (in large firms) or administrator communicates information and offer advice to the units preparing the budgets. This unit prepares the forms and procedures for developing a budget. It helps those preparing budgets with technical problems and in the actual preparation. If there are budget specialists at the division level, it trains these persons and coordinates their work.

Step 3

Each unit prepares a preliminary budget for the next period. Normally the unit begins with the previous period’s budget and performance against this budget. Next the unit states how the next period will differ from the current period. So the next year’s budget that the unit proposes is based on the past budget plus or minus expected changes. This shows how the units management expects to achieve its objectives. This is a critical stage if strategic change is taking place. The unit must specify what resources it will need to accomplish the strategy.

Step 4

The preliminary budgets developed in step 3 are reviewed and approved. The budget department analyzes and reviews each unit’s past performance and determines whether its projection are realistic given likely future conditions. After comparing the budgets of the various units, the budget department submits them to top management along with recommendations for approval or adjustment. Top management examines the budgets and approves them if they are consistent with past performance, anticipated revenues, and the firm’s strategy.

This is the stage at which the resource allocation choice will be made. Who gets the money to hire more people, buy new furniture or machinery, or build a new building? In most enterprises resources are scarce, and not every unit can be given what it wants (and says it needs). The allocation of funds can be crucial to the success of a unit (and to the career of its manager). Loss of marketing funds for TV spots at a strategic time, for example, can wreck a unit’s results. Because the decisions involved are so difficult, they are often made by a budget committee or a number of managers.

Step 5

At this stage summary budgets are usually prepared. Projected receipts and expenses are put together, and subsidiary budgets are developed for example, the operating budget, financial budgets, the capital budget, and expense budgets. The operating budget specifies materials, labor, overhead, and other costs. Financial budgets project cash receipts and

disbursements; the capital budget project major additions or new construction. The expense budgets project expenses not covered in other budgets, such as marketing costs. Finally, in the summary budget (profit and loss or income statement), the total obtained by combining the subsidiary budgets is subtracted from the projected receipts. The remainder is a profit or loss. If the budgets meet objectives, approvals are made, and the budgets are enacted. If changes are needed, negotiations will take place.

The mechanics of preparing capital and operating budgets are beyond our purview. But this process is important, as it relates to the formation and implementation of strategy. Through the entire process, a variety of real problems of relevance to strategists often emerge. Estimating both revenues and costs is very difficult. In the case of an automaker, for example, how many new cars will the company sell? This depends on a number of factors, such as the economy, competitors' products, and how consumers evaluate its product in comparison with competing products. The company's pricing policy and marketing image affect this estimate, as do product quality, engineering, and the aggressiveness and reliability of dealers. Managers often handle this problem by making their best guesses- "ball-park" estimates. Sometimes they miss. The point is, the issues we addressed earlier affect budget preparation.

Moreover, the question of who gets the most money from the budget has a major effect on the work environment as well as on the careers of managers. If, as a manager, you "lose the budget battle," your employees will have to do more work with fewer helpers and less desirable equipment. They will feel that you have failed them, and they will treat you accordingly. This is one of the problems with using the product portfolio approach. Few managers want to have their units known as dogs or cash cows. It is also a problem affecting retrenchment strategies. Negotiations to protect a unit in the budget battle may come at the expense of pursuing a strategy in the best interests of the overall organization. Indeed, gamesmanship, overstatement of real budget needs, and even secrecy can lead to highly political budget battles across departments.

Another problem is that the usual budget process tends to be designed for allocating resources to existing departments or various investment proposals. These may or may not be tied to strategic changes desired by the organization; if they are not, then the budget process reinforces existing resource allocation patterns.

The budget process itself can lead to problems if it is not tied to the strategic direction of the firm. In fact, the process sets the operative strategy as we suggested earlier. So if lower levels are unaware of shifts in strategic direction and if top managers fail to communicate strategic change or are weak negotiators, any intended strategy change is unlikely to take place.

Finally, you should note that the budget process is tied to the way units and divisions are arranged organizationally. New SBUs can be at a disadvantage if they are unaware of the "ins and outs" of the budget procedures used in their organization. And if truly major strategic shifts are occurring, the structure is likely to change along with the way resources are allocated. So let's turn to the second aspect of implementation structuring for strategy implementation.

The major difficulty arises due to a scarcity of resources. Financial, physical, and human resources are hard to find. Firms will usually face difficulties in procuring finance. Even if finance is available, the cost of capital is a constraint. Those firms that enjoy investor confidence and high creditworthiness possess a competitive advantage as it increases their resource-generation capability. Physical resources would consist of assets, such as, land, machinery, and equipment. In a developing country like India, many capital goods have to be imported. The government may no longer impose many conditions but it does place a burden on the firm's finances and this places a restriction on firms wishing to procure physical resources. Human resources are seemingly in abundance in India but the problem arises due to the non-availability of skills that are specially required. Information technology and computer professionals, advertising personnel, and telecom, power and insurance experts are scarce in India. This places severe restrictions on firms wishing to attract and retain personnel. In sum, the availability of scarce resources is a very real problem faced in

resource allocation.

Within organisations, there are several difficulties encountered in resource allocation. The usual budgeting for existing SBUs, divisions, and departments places restrictions on generating resources for newer units and those with a greater potential for growth.

Overstatement of needs is another frequent problem in a bottom-up approach to resource allocation. The budgeting and corporate planning departments may have to face the ire of those executives who do not get resources according to their expectations. Such negative reactions may hamper the process of strategic planning itself. When strategic budgeting is used for resource allocation, powerful units may be divested of resources for reallocation to potential units. 'Budget battles' may ensue if resource allocation affects vested interests.

It must be pointed out, however, that the CEO has a major role to play in managing the process of resource allocation. Strategic management, based on a participative mode, and the communication of the strategic plan to all executives creates a congenial environment where the resource allocation decisions may be taken amicably.

Structural Considerations

We usually conceive of organisation structure as a chart consisting of boxes in which the names of positions or designations of personnel (and sometimes the name of the person occupying the position) are written in a hierarchical order along with the depiction of the relationship that exists between various positions. To a strategist, an organisation structure is not only a chart but much more.

An organisation structure is the way in which the tasks and subtasks required to implement a strategy are arranged. The diagrammatical representation of structure could be an organisation chart but a chart shows only the 'skeleton'. The 'flesh and blood' that bring to life an organisation are the several mechanisms that support the structure. All these cannot be depicted on a chart. But a strategist has to grapple with the complexities of creating the structure, making it work, redesigning when required, and implementing changes that will keep the structure relevant to the needs of the strategies that have to be implemented.

To find out what the structural mechanisms are, it is useful to consider the case of a new organisation which has decided to achieve a set of objectives through the implementation of certain strategies. In the next two paragraphs we shall relate the 'story' of how structural mechanisms evolve.

The implementation of strategies would require the performance of tasks. Some of these tasks are related to the formulation and implementation of programmes and projects. We dealt with these tasks in the previous chapter which was on activating strategies. Having laid the foundations of an organisation, the strategists now have to devote their attention to the tasks, that would have to be performed on a continuing basis for the implementation of strategies. It would be practically impossible to list all such tasks, so the strategists would attempt to enumerate the major tasks. These major tasks would have to be grouped on the basis of the commonality of the skills required to perform them. Having grouped the major tasks, each category of such tasks will have to be again segregated on the basis of the ability of an individual to perform a unit of tasks. This is the process by which organisational units, such as, departments, are created and hierarchies defined.

The total responsibility to implement strategies has to be subdivided and distributed to different organisational units. The authority to discharge the responsibilities will also have to be delegated if the tasks have to be performed. To ensure that different organisational units do not work at cross-purpose, coordination will have to be ensured through communication. The performance will have to be appraised and controlled so that the tasks are performed in sequence and according to a schedule. Desirable behaviour to perform these tasks will have to be encouraged and undesirable behaviour curbed. For this, rewards and penalties will have to be used. Since the performance of tasks

cannot be left to chance, the creation of motivation will have to be facilitated so that organisational effort is directed towards a common purpose. Further, individuals will have to be trained so that objective-achieving capability is created and sustained.

The new organisation that has been exemplified will come into being and start functioning in the manner described above. All the activities mentioned will now have to be performed on a continuing basis.

We can not derive the different mechanisms on the basis of the above example. These are summarised as follows:

1. Defining the major tasks required to implement a strategy
2. Grouping tasks on the basis of common skill requirements
3. Subdivision of responsibility and delegation of authority to perform tasks
4. Coordination of divided responsibility
5. Design and administration of the information system.
6. Design and administration of the control system
7. Design and administration of the appraisal system
8. Design and administration of the motivation system
9. Design and administration of the development system
10. Design and administration of the planning system

The first four of these mechanisms will lead to the creation of the structure. The other six mechanisms are devised to hold and sustain the structure. Collectively, we could refer to the last six mechanisms as organisational systems.

Note that structural mechanism alone will not fulfill the requirements of strategy implementation. Structure is the 'hardware' while the other aspects constitute the 'software' of structure implementation. The other major aspects of implementation relate to the leadership styles, corporate culture, and other related issues. These will be dealt with in subsequent chapter. Here, we focus our attention on the structural mechanism required for the implementation of strategies.

The prescription for consciously matching an organisation's structure to the particular needs and requirements of strategy has arisen out of research done by Chandler. Child has further extended the thinking to include environment and effectiveness in the sequence to pinpoint the nature of choices that strategists make. He says that managerial choice occurs at the interface of environment and strategy, which then determines the structure. Though Chandler's thesis that strategy changes require structural changes to achieve economic efficiency is logically powerful, subsequent researches have not conclusively proved the relationship that structure follows strategy.

But often, structural consideration also affect-if not determine strategy, which is a case of backward linkage. Theorists in Business policy, therefore, are more concerned with the match that should exist between strategy and structure. In other words, a particular strategy creates special requirements that should be fulfilled by the structure. If it does not, then the structure will have to be redesigned. What shape the structure should take if a particular strategy is to be implemented successfully is difficult to answer. But here again, theory offer alternatives. One such alternative is to link structure to the stage of development that an organisation exists in at a given point of time.

Besides Chandler, Salter, Thain, and Scott have contributed to the thinking that any organisation, as it grows in size and diversity, moves from a simple to a complex organisational form. This concept is analogous of that of the product life cycle. Organisations too follow a life cycle consisting of the introduction, growth, maturity, and decline phases. The

life cycle of organisations could be divided into four states that are not distinct and may overlap.

Stage I organisations are small-scale enterprises usually managed by a single person who is the entrepreneur-owner-manager. These organisations are characterised by the simplicity of objectives, operations, and management. The form of the organisation is also simple and could be termed as entrepreneurial. The strategies adopted are generally of the expansion type.

Stage II organisations are bigger than Stage I organisations in terms of size and have a wider scope of operations. They are characterised by functional specialisation or process orientation. The organisational form is simple functional (typically divided into the finance, marketing, operations, and personnel departments) or process-oriented (divided into process-based departments arranged in a particular sequence according to the technology employed). The strategies adopted may range from stability to expansion.

Stage III organisations are large and widely scattered organisations generally having units or plants at different places. Each division is semi-autonomous and linked to the headquarters but functionally independent. The divisions may have a simple functional form depending on their particular needs. The strategies adopted may be either stability or expansion.

Stage IV organisations are the most complex. They are generally large multiplant, multiproduct organisations that result from the adoption of related and unrelated diversification strategies. The organisational form is divisional. The corporate headquarters assume the responsibility of providing strategic direction and policy guidelines through the formulation of corporate-level strategies. The divisions (which may be companies, profit centres or SBUs) formulate their business-level strategies and may adopt Stage I, II or III types of structures.

The stage of development theories present a convenient way to understand the way the structure may evolve as the organisation moves from one stage to the next. But, in practice, many variations may occur. It is not necessary that all organisations should pass through every stage of development. Nor does every organisation exhibit the characteristics of exclusively one stage.

A look at the different organisations will show that they do seem to follow the different stages mentioned above. Most companies have started as one-or two-person units in an entrepreneurial mode. Through expansion and in time, the companies have become bigger, creating the need for a subdivision of task which usually takes place along functional lines. Further, expansion creates the need for setting up additional plants, and if diversification strategies are adopted, then the organisational forms may ultimately become divisional. Exhibit 4.7 presents an interesting analysis of how organisational structures have evolved in the Indian context.

Business Today makes an interesting analysis of the chronological evolution of the organisational structure within Indian firms. The structures analysed show the firms responding to the environmental situation prevailing during a particular time period. Here is an account of how structures have evolved from the pre-1940s to the post 1990s.

One-man organisation (Pre-1940): The CEO is the hub around which there are workers.

The classic triangle (1940-50): The functions of sales, finance, and production are designed below the direct control of the CEO.

The managing agency (1950-60): The foreign company provides the licence to the local partner who acts as the managing agent. The functional areas are directly looked after by the managing agent who acts as the CEO.

The functional structure (1960-70): The traditional and popular structure of various functional areas directly under the control of the CEO.

The cross-holding structure (1970-80): The promoter (most often a family group or a powerful industrialist) has equity holding in several companies and exercises organisational control in the same proportion.

The conglomerate (1980-90): The business/family group emerges as the focal point managing a clutch of business vested in different companies. Each company manages one or more businesses.

The streamlined group (Post-1990): The group emerges as the focal point of structure with businesses vested in subsidiaries, joint ventures, and equity alliances. The organisational control is exercised through a flagship company.

Exhibit 11.7: The Evolution of the Organisation Structure in Corporate India

Structures for Strategies

Implementation is necessary to spell out more precisely how the strategic choice will come to be. Structural and administrative mechanisms which are compatible and workable need to be established to reinforce the strategic direction chosen and provide guides for action. A good strategy without effective implementation is not likely to succeed. Closing the gap between ideal and expected outcomes requires more than making a strategic choice.

Exhibit 11.8 is one consulting group's representation of the fact that strategy formation is but one component of a network of organization activities which must be integrated to accomplish objectives. The McKinsey framework suggests that the following components must fit together to make a strategy work effectively.

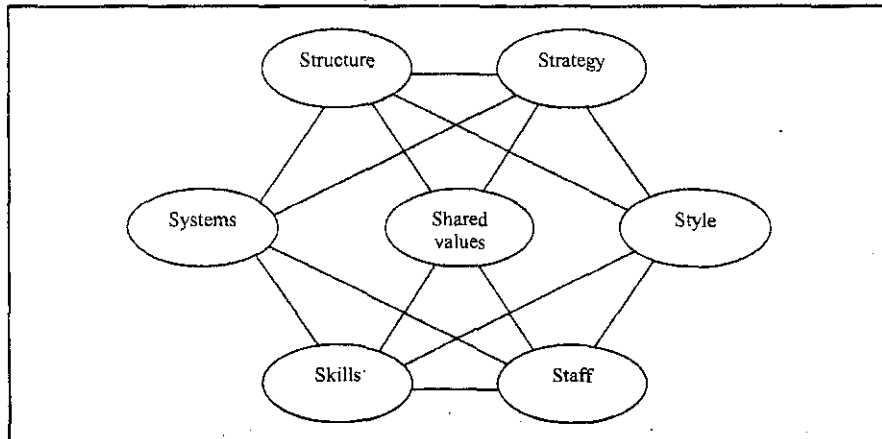


Exhibit 11.8: McKinsey 7-S Framework

1. *Strategy*. A coherent set of action aimed at gaining a sustainable advantage over competition, improving position vis-a-vis customers, or allocating resources.
2. *Structure*. The organization chart and accompanying baggage that show who reports to whom and how tasks are both divided up and integrated.
3. *Systems*. The process and flows that show how an organization gets things done from day to day (information system, capital budgeting systems, manufacturing process, quality control systems, and performance measurement systems all would be good examples).
4. *Style*. Tangible evidence of what management considers important by the way it collectively spends time and attention and uses symbolic behavior. It is not what management says is important; it is the way management behaves.
5. *Staff*. The people in an organization. Here it is very useful to think not about individual personalities but about corporate demographics.
6. *Shared values* (or superordinate goals). The values that go beyond, but might well include, simple, goal statements in determining corporate destiny. To fit the concept, these values must be shared by most people in an organization.
7. *Skills*. A derivative of the rest. Skills are those capabilities that are possessed by an organization as a whole as opposed to the people in it.

An organization is necessary if strategic purpose is to be accomplished. Thus, organizational structure is a major priority in implementing a carefully formulated strategy. If activities, responsibilities, and interrelationships are not organized in a manner that is consistent with the strategy chosen, the structure is left to evolve on its own. If structure and strategy are not coordinated, the result will probably be inefficiencies, misdirection, and fragmented efforts.

The need for structure becomes apparent as a business evolves. In a small firms where one person manages current operations and plans for the future, organizational structure is relatively simple. Owner-managers have no organizational problem until their hurried trips to the plant, late-night sessions assimilating financial information for their CPA, and pressed calls on potential customers are inadequate to meet the demands of a business's increasing volume. As the magnitude of business activity increases, the need to subdivide activities, assign responsibilities, and provide for the integration and coordination of the new organizational parts becomes imperative. Thus, how to structure the organization to effectively execute the business's strategy has become a major concern.

What is structure? A basically simple concept: the division of tasks for efficiency and clarity of purpose, and coordination between the interdependent parts of the organization to ensure organizational effectiveness. Structure balances the need for specialization with the need for integration. It provides a formal means of decentralizing and centralizing consistent with the organizational and control needs of the strategy.

Structure is not the only means for getting "organized" to implement the strategy. Reward systems, planning procedures, and information and budgetary systems are other examples that should be employed. In the day-to-day implementation of strategy, these elements operate interdependently with the formal organizational structure to shape how things are done. These other means may also be important, but it is through structure that strategists attempt to balance internal efficiency and overall effectiveness within a broader environment.

What are the structural choices? Five basic types are currently used by most business firms.

1. Simple.
2. Functional.
3. Divisional.
4. Strategic business unit.
5. Matrix.

Diversity and size create unique structural needs for each firm, but these five structural choices involve basic underlying features common to most business organizations.

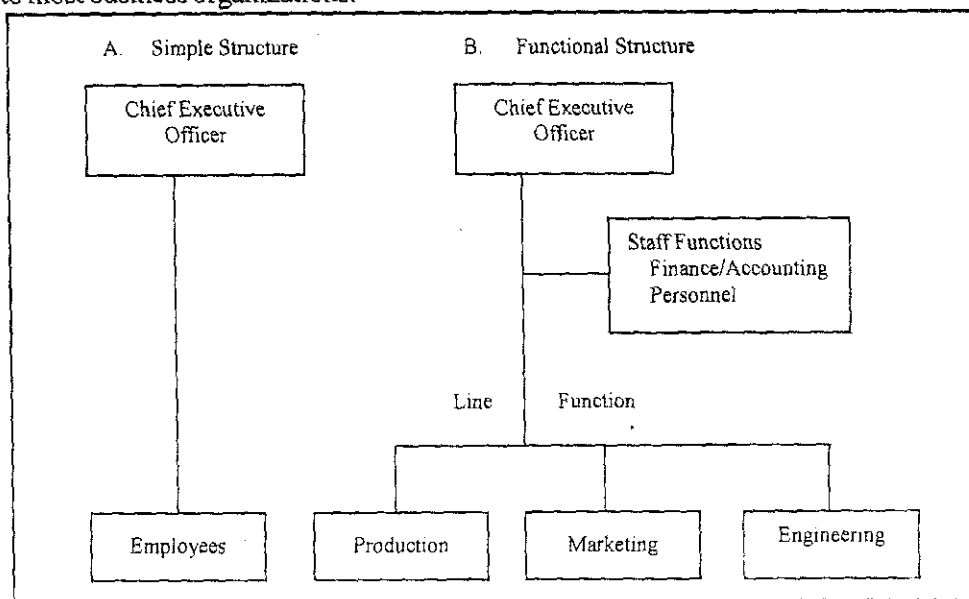


Exhibit 11.9: Simple and Functional Organisation Structures

Advantages	Advantages
<ol style="list-style-type: none"> 1. Facilitates control of all business's activities. 2. Rapid decision making ability to change with market signals. 3. Simple and informal motivation /reward/control systems. 	<ol style="list-style-type: none"> 1. Efficiency through specialization 2. Improved development of functional expertise. 3. Differentiates and delegates day-to-day operating decisions. 4. Retains centralized control of strategic decisions.
Disadvantages	Disadvantages
<ol style="list-style-type: none"> 1. Very demanding on the owner-manager. 2. Increasingly inadequate as volume expands. 3. Does not facilitate development of future managers 4. Tends to focus owner manager on day to day matters and not on future strategy. 	<ol style="list-style-type: none"> 1. Promotes narrow specialization and potential functional rivalry or conflict. 2. Difficulty in functional coordination and interfunctional decision making. 3. Staff-line conflict 4. Limits internal development of general managers.

Structure is not an end in itself but rather a means to an end. It is a tool for managing the size and diversity of a business to enhance the success of its strategy. This section identifies structural options and examines the role of structure in strategy implementation.

Exhibit 11.9 is a model of simple and functional organizational structures. In the smallest business enterprise, the simple structure prevails. All strategic and operating decisions are centralized in the owner-manager's domain. With the strategic concern primarily survival, and the likelihood that one bad decision could seriously threaten continued existence, this structure maximizes that owner's control. It also allows rapid response to product market shifts and the ability to accommodate unique customer demands without coordination difficulties. Simple structures encourage employee involvement in more than one activity and are efficacious in businesses that serve a localized, simple product/market. This structure can be very demanding on the owner-manager and, as volume increases, can pressure the owner-manager to give increased attention to day-to-day concerns at the expense of time invested in strategic management activities.

Functional structure predominates in firms that concentrate on one or a few related products/markets. Functional structures group similar tasks and activities (usually production/operations, marketing, finance/accounting, research and development, personnel) as separate functional units within the organization. This specialization encourages greater efficiency and refinement of particular expertise and allows the firm to seek and foster distinct competencies in one or more functional areas. Expertise is critical to single-product/market companies and to firms that are vertically integrated.

The strategic challenge in the functional structures is effective coordination of the separate functional units. The narrow technical expertise sought through specialization can lead to limited perspectives and different priorities across different functional units. Specialists may not understand problems in other functional areas and may begin to see the firm's strategic issues primarily as "marketing" problems or "production" problems. This potential conflict makes the coordinating role of the chief executive critical if a strategy is to be effectively implemented using the functional structure. Integrating devices (such as project team or planning committees) are frequently used in functionally organized businesses to enhance coordination and to facilitate understanding across functional areas.

When a firm diversifies its products/service lines, covers broad geographic areas, utilizes unrelated market channels, or begins to serve distinctly different customer groups, a functional structure rapidly becomes inadequate. For example,

functional managers may wind up overseeing the production or marketing or numerous and different products or services. And coordination demands on top management are beyond the capacity of a functional structure. Some form of divisional structure is necessary to meet the coordination and decision-making requirements resulting from increased diversity and size. Such a structure is illustrated in Exhibit 11.10 & 11.11.

A divisional structure allows corporate management to delegate authority for the strategic management of a distinct business entity. This can expedite critical decision making within each division in response to varied competitive environments, and it forces corporate management to concentrate on corporate level strategic decisions. The semiautonomous divisions are usually given profit responsibility. The divisional structure thus seeks to facilitate accurate assessment of profit and loss.

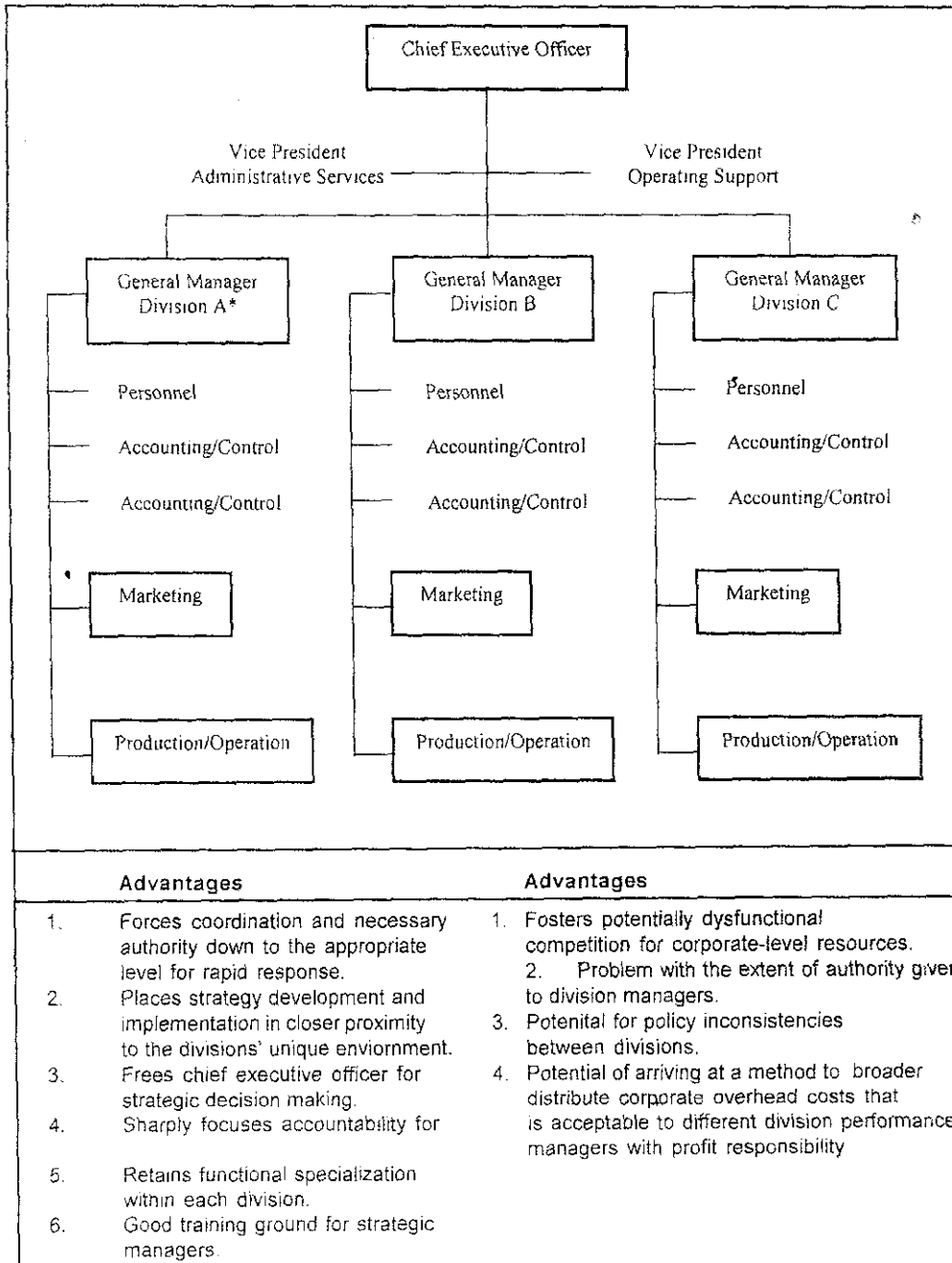


Exhibit 11.10: Divisional Organization Structure

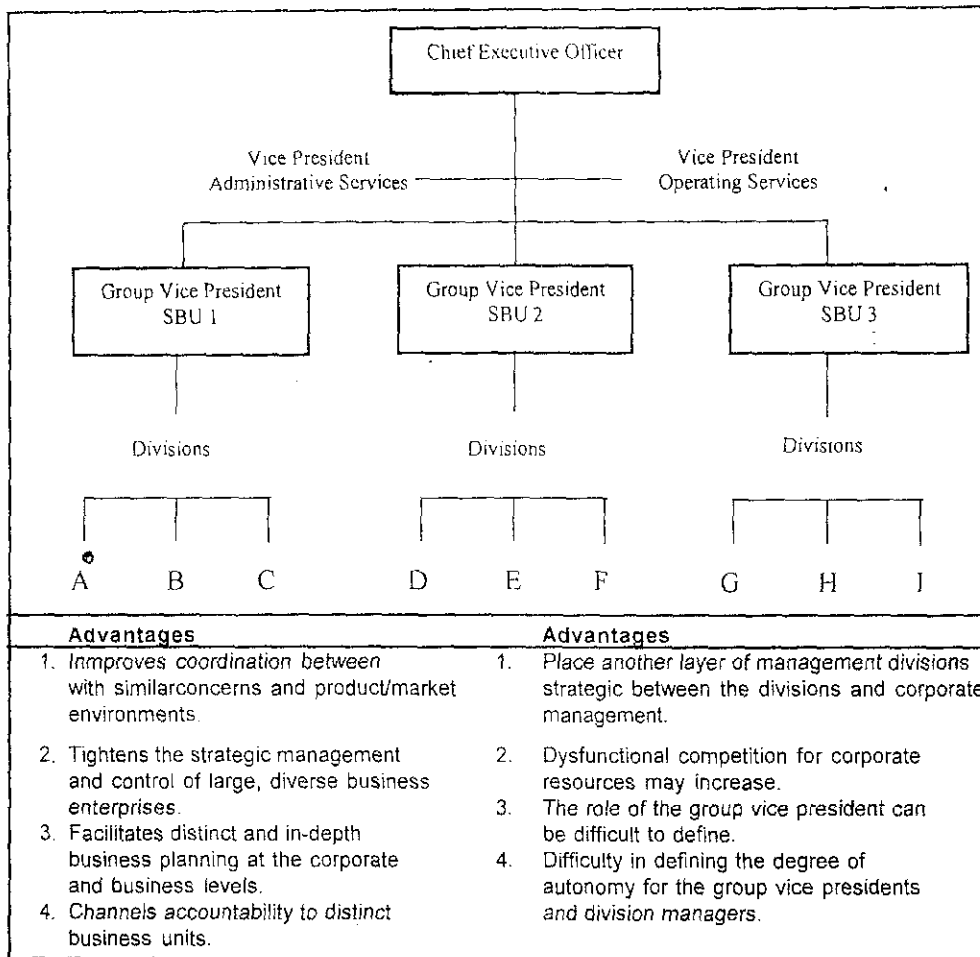


Exhibit 11.11: Strategic Business Unit Organizational Structure

Strategic Business Units

Some firms encounter difficulty in controlling their divisional operations as the diversity, size, and number of these units continues to increase. And corporate management may encounter difficulty in evaluating and controlling its numerous, often multi-industry divisions. Under these conditions, it may become necessary to add another layer of management to improve strategy implementation, promote synergy, and gain greater control over the diverse business interests. This can be accomplished by grouping various divisions (or parts of some divisions) in terms of common strategic elements. These groups, (sector) SBUs. For example, three separate divisions making food preparation appliances were merged into a single SBU serving the housewares market.¹ General Foods, after originally defining SBUs along product lines (which serve overlapping markets), restructured along menu lines.

In large companies, increased diversity leads to numerous product and project efforts, all with major strategic significance. The results is a need for an organizational form that provides and controls skills and resources where and when they are most useful. The matrix organization, pioneered by firms like defense contractors, construction companies has increasingly been used to meet this need. The list of companies now using some form of matrix organization includes Citicorp, Digital Equipment, General Electric, Shell Oil, Dow Chemical, and Texas Instruments.

The matrix organization provides for dual channels of authority, performance responsibility, evaluation and control, as shown in Exhibit 11.12. Essentially, subordinates are assigned to both a basic functional area and a project or product manager. The matrix form is included to combine the advantages of functional specialization and product/project

specialization. In theory, the matrix is a conflict resolution system through which strategic and operating priorities are negotiated, power is shared, and resources are allocated internally on a “strongest case for what is best overall for the unit” basis.

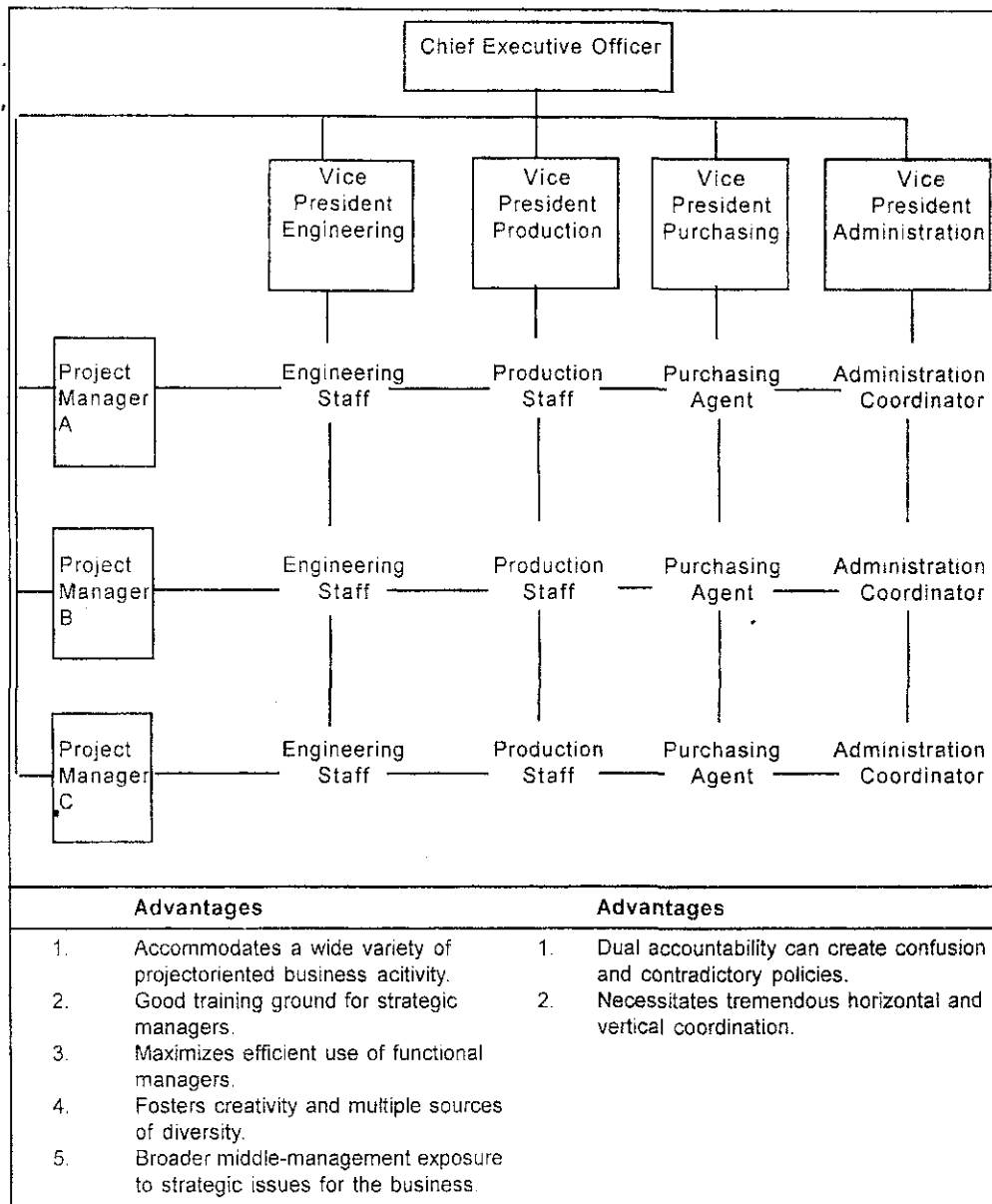


Exhibit 11.11: Strategic Business Unit Organizational Structure

The matrix structure increases the number of middle managers exercising general management responsibilities and broadens their exposure to organizationwide strategic concerns. Thus, it can accommodate a varied and changing project, product/market, or technology focus and can increase the efficient use of functional specialists who otherwise might be idle.

Citicorp used the matrix organization to implement an international expansion strategy focusing on both geographically different financial service requirements and at the same time targeting the multinational corporation market segment. The change was designed to increase the priority given to large, international organizations. The strategy ultimately gave Citicorp a better understanding of the worldwide financial officers of these corporation had. Matrix structure

was a strategic tool that allowed Citicorp to gain a competitive advantage with this important segment.

While the matrix structure is easy to design, it is difficult to implement. Dual chains of command challenge fundamental organizational orientations. Negotiating shared responsibilities, use of resources, and priorities can create misunderstanding or confusion among subordinates.

To overcome the deficiencies that might be associated with a permanent matrix structure some firms are using a "temporary" or "flexible" overlay structure to accomplish a particular strategic task. This approach, used recently by firm like General Motors, IBM, and Texas Instruments, is meant to take temporary advantage of a matrix-type team while preserving the shape and spirit of the underlying divisional structure. Thus, the basic idea of the matrix structure, to simplify and amplify the focus of resources on a narrow but strategically important product, project, or market, appears to be an important structural alternative within large, diverse organizations.

Which structure is best? Considerable research has been done on this question, and the collective answer is that it depends on the strategy of the firm. The structural design ties together key activities and resources of the firm. Therefore, it must be closely aligned with the needs/demands of the firm's strategy.

Alfred Chandler provided a landmark study in understanding the choice of structure as a function of strategy. Chandler studied 70 large corporations over an extended time period and found a common strategy-structure sequence:

1. Choice of a new strategy.
2. Emergence of administrative problems; decline in performance.
3. A shift to an organizational structure more in line with the strategy's needs.
4. Improved profitability and strategy execution.

General Electric's recent history supports Chandler's thesis. Operating with a simple divisional structure in the late 1950s, GE embarked on a broad diversification strategy. In the 1960s, GE experienced impressive sales growth. However, GE also experienced administrative difficulties in trying to control and improve the corresponding lack of increase in profitability. In the early 1970s, GE executives redesigned its organizational structure to accommodate the administrative needs of strategy (ultimately choosing the strategic business unit structure), subsequently improving profitability of and control over the diversification strategy.

Chandler's research and the GE example allow us to make four important observations. First, all forms of organizational structure are not equally effective in implementing a strategy. Second, structures seem to have a life of their own, particularly in larger organizations. As a result, the need for immediate and radical changes in structure is not immediately perceived. Once the need is perceived, lagging performance may be necessary before politically sensitive structure is changed or organizational power redistributed. Third, sheer growth can make restructuring necessary. Finally, as firms diversify into numerous related or unrelated products and markets, structural change appears to be essential if the firm is to perform effectively.

Research on corporate stages of development provides further understanding of the structures-strategy relationship. After studying numerous business firms, these researchers concluded that companies move through several stages as size and diversity increase.

Stage	Characteristics of the firm	Typical structure
I	Simple, small business. Offering one product/ service or one lines of products/services to small, distinct local or regionalized market.	Simple to functional
II	Singular or closely related line of products/ services but to a larger and sometimes more diverse market (geography, channels, or customers).	Functional to divisional
III	Expanded but related lines of product/services to diverse, large markets.	Divisional to matrix
IV	Diverse, unrelated lines of products/services to large, diverse markets.	Divisional to SBUs

Exhibit 11.13: Corporate Stages of Development

Exhibit 11.13 is a synthesis of these stage-of-development theories. The figure shows that a firm moves through each stage, size, diversity, and competitive environment change.

To complete effectively at different stages requires, among other things, different structures. Again, the choice of structure appears contingent on the strategy of the firm in terms of size, diversity of the product/services offered, and markets served. Two firms in the metal container industry help illustrate this point. Continental Can, the industry leader, employs a divisional structure. This is used to implement a diversification strategy intended to serve virtually every user of metal containers, as well as to compete in unrelated markets like forest products. Crown, Cork and Seal, the industry's fourth largest company, employs a modified functional structure to serve a limited domestic and international market of users with specialized container needs. Both firms are successful. Both derive their greatest revenues from the same industry. But each employs a different organizational structure because their strategies (narrow versus broad product/market scope) are different.

The choice of structure must be determined by the firm's strategy. And the structure must segment key activities and/or strategic operating units to improve efficiency through specialization, response to a competitive environment, and freedom to act. At the same time, the structure must effectively integrate and coordinate these activities and units to accommodate interdependence of activities and overall control. The choice of structure reflects strategy in terms of the firm's (1) size, (2) product/service diversity, (3) competitive environment and volatility, (4) internal political considerations, and (5) information/coordination needs for each component.

Even a change in strategy, with its accompanying alteration of administrative needs, does not lead to an immediate change in structure. The research of Chandler and others suggests that commitment to a structure lingers even when it's become inappropriate for a current strategy. Whether this is due to inertia, organizational politics, or a realistic assessment of the relative costs of immediate structural change, historical evidence suggests that the existing structure will be maintained and not radically redesigned until a strategy's profitability is increasingly disproportionate with increasing sales.

Organisational Design and Change

It is an extremely difficult proposition to decide which type of structure would satisfy the requirements of a particular strategy. In general; strategists have to ask themselves: 'What is required to implement the strategic plan and how best can it be done?' This entails what we indicated in organisation structure has to be based on those functions and activities that are critical from the viewpoint of strategy.

There is no clear answer to the question: "Which structure is best suited to a particular strategy?" Frequently, structures evolve as the organisation moves from one stage of growth to the next. The external and the internal

environments affect structural design in different ways. For instance, an organisation which faces a stable environment may use a functional structure since there is less need for interdepartmental coordination and communication, and innovation. On the other hand, a volatile environment demands a rapid-response capability, flexibility and quick decision-making. Such demands can be better met by the creation of a divisional or a matrix type of structure. The internal environment may also affect the structure in a similar fashion. A bureaucratic, slow-moving organisation may work better with a functional structure. In sum, it could be said that there is no one absolutely correct way to organise and the organisational design has to be based on the particular needs of the organisation at a given time.

The needs of an organisation can be derived from its mission and objectives. These needs are the key activities which have to be performed to achieve objectives and realise the mission. Organisational design, therefore, starts with the identification of such key activities. The sequence of steps followed in organisational design could be described as below.

1. Identification of key activities necessary to be performed for the achievement of objectives and the realisation of the mission through the formulated strategy
2. Grouping of activities that are similar in nature and which need a common set of skills to be performed
3. Choice of structure that could accommodate the different groups of activities
4. Creation of departments, divisions, and so on to which the groups of activities could be assigned
5. Establishing an interrelationship between different departments for the purpose of coordination and communication.

These five steps lead to the development of an organisational design but the process of organisation is not complete yet. There are various other issues to be tackled to see that the organisation becomes an effective medium for the implementation of strategy. For instance, it was mentioned in the previous sections that the basic units for structuring are the departments, based on functional specialisations. But this thinking is changing as organisations are attempting to create a more responsive structure in terms of processes based on cross-functional teams. Strategists have to grapple with a number of issues before the task of organisational design is over. The major issues are the span of management, basic departmentation, line and staff relationships, and the use of committees and group decision-making.

The span of management refers to the ways in which activities can be grouped. The different structures, as described in the previous section, consist of various departments, each of which deals with a distinct group of activities. The activities could also be organised on the basis of the processes leading to the manufacture of a product or provision of a service. These structures form the core of basic departmentation.

Line and staff relationships describe the way in which authority is dispersed within the organisation structure. Where a higher-level manager exercises direct supervision over a subordinate, authority is delegated in a direct line or steps. Staff positions are advisory in nature. Within the staff departments, however, authority may again be delegated on the basis of line relationships.

The use of committees and group decision-making is often done as an organisational device though it is not per se a part of the organisational structure. Still, committees are considered an inseparable part of structure. When they are constituted formally on a permanent basis, the committees work on the basis of specially delegated authority and responsibility. Other similar forms of group decision-making as well as group functioning are the teams, task forces, project units, liaison groups, etc.

It is to be pointed out that significant changes in thought related to organisation structural design have been taking place worldwide and are impacting Indian companies too. The major ideas in this context are: restructuring, reorganisation,

reengineering, deallyering, flatter structures, and so on. Restructuring and reorganisation refer to changing the organisation structure in line with the changes in the environment and strategies. Renigineering (or business process reengineering) is the fundamental rethinking and radical redesign of business processes to achive dramatic gains in areas such as cost, quality, service, and speed. Dealyering is reducing the number of levels in the organisational hierarchy with a view to facilitate better control and communication within the organisation. Flatter structures result due to dealyering. In this manner, organisations are attempting to adapt their organisational structures. Some of the changing structural characteristics of organisations are encapsulated in Exhibit 11.14.

Macy and Izumi highlights the comparative changing characteristics of the traditional organisational design and the emerging thinking in organisational design.

Their comparative analysis is given below.

Traditional organisation design	Emerging organisational design
Characteristic	Characteristics
One large firm	Small business units having cooperative relationships
Vertical communication patterns	Horizontal communication patterns
Centralised top-down decision-making	Decentralised participative decision making
Vertical integration	Outsourcing and virtual organisations
Work-/quality-based teams	Autonomous work teams
Functional work teams	Cross-functional work teams
Minimum training	Extensive training
Individual-focussed specialised job design	Value-chain team-focussed job design

Exhibit 11.14: Changes in Contemporary Organisation Design

The above description of the five essential steps, four related issues, and the emerging thought in organisational design are, in fact, a theoretical baiss for the creation of structure. It is up to the strategists to use this theoretical foundation and the emerging thought to design an organisational structure that would suit the requirements of a particular strategy. The skills of strategists are put to test when they design an appropriate organisational structure. Agin, a more rigorous test is faced when the existing structure has to be changed to suit the requirements of a modified or new strategy. We take up this issue in the following subsecion.

Right at the outset, it must be pointed out that organisation change takes place along two broad dimensions: the structural changes and the accompanying behavioural changes. The first type of change is related to modifications in structural relationships and may entail the creation or disbandment of departments or managerial positions. The second type of change relates to the concomittant behavioural modifications that are essential to absorb the impact of organisation changes. Students of management are quite familiar with the concepts of formal and informal organisations. What we are referring to then in the first and second cases are the formal and informal organisations respectively. While formal organisational changes are mainly administrative in nature and can be brought about the by the means of organisational planning and implementation the informal organisation changes are more complex and evolve as a response to formal organisational changes.

An example will serve to illustrate the nature of structural and behavioural changes. An organisation which follows a corporate-level strategy of stability has a simple functional structure in existence. This firm now plans to diversity into a related area and this strateigc shift as to be reflected in organisational changes. The choice of structure leads to divisional form of structure where a new division with a few departments is created to support the related product lines. Some of the functions like personnel and finance are retained at the corporate level as centralised department . Again, for instance, taking the case of business strategies it can be seen that a firm pursuing a low-cost strategy in a

mature, stable business can do with a simple functional structure. If there are some changes required then these can be planned in advance. But if a firm operates in a volatile environment and decides to adopt a differentiation business strategy then a divisional structure could serve its needs better. Like this, the firm can hope to cater to changing customer needs more effectively.

Keeping in mind the type of environment faced by a firm at a given time and the strategy that it adopts at the corporate-and business-level, the structural change can be envisaged. But organisational changes go beyond mere structural modifications and encompass the issues of how people would react to the changed situation, how the new relationships would be managed, and in what manner would the cohesiveness of the organisation be maintained.

Organisational change "is the movement of an organisation away from its present state and towards some desired future state to increase its effectiveness. Even in most stable organisations, change is necessary just to keep the level of given stability. The economic, social and technological environment is so dynamic that without the change that would be adaptive to the changed environment, even the most successful organisations will be left behind, unable to survive in the changed environment. Rapid change is not confined to high technology industries such as computers, software, biotechnology, robotics and so on. Many organisations which were once considered stable such as publishing, retailing, and even hospitals now face the need to adapt to change quickly. Accordingly, management must continuously monitor the outside environment and be sufficiently innovative and creative to find new and better utilisation of organisational resources so that the organisation always maintains its competitive edge.

Whether the change involves creativity and innovation within the organisation or simply a response to outside forces which may require organisational realignment, management must be aware of the forces and the need for change. Typically, organisations have little choice but to change. According to Barney and Griffin, the primary reason cited for organisational problems is the failure by managers to properly anticipate or respond to forces for change.

Recent surveys of some major organisations around the world have shown that all successful organisations are continuously interacting with the environment and making necessary changes in their structural design or philosophy or policies or strategies as the need be. The survey found that 44 percent of Japanese firms, 59 percent of American firms, 60 percent of German firms and 71 percent of South Korean firms so surveyed had significantly changed their organisational structure between 1989 to 1991.

Adapting to change would mean that the organisations have to learn new technologies, new markets and new ways of managing. In the future, the only truly sustainable source of competitive advantage will be the organisation's ability to change and learn new skills.

Learning organisations are firms that view change as a positive opportunity to learn and create new sources of competitive advantage. Bringing about organisational change that facilitates learning is not an easy task. Since, "man follows the path of least resistance", it is easier to employ known methods than to change to new methods where the outcomes may not be as certain. Hence, a change will be easier to make and adjust to, if the potential rewards after the change are sufficiently attractive. Accordingly, senior managers must be sensitive to any such resistance to change from the subordinates and take steps to encourage all constituencies of the organisation to join in and facilitate the needed changes. It must be noted, however, that what the employees resist is not the technical changes which they are generally willing to adopt, but the social changes which are the changes in the human relationships that most often accompany technical changes.

As a result, the emphasis must be on reducing the strain that might develop due to changes in these relationships.

Some organisations possess characteristics that greatly enhance their capabilities to adapt to rapid change. Pitts and

Lei have listed six such characteristics as shown below in Exhibit 11.15.

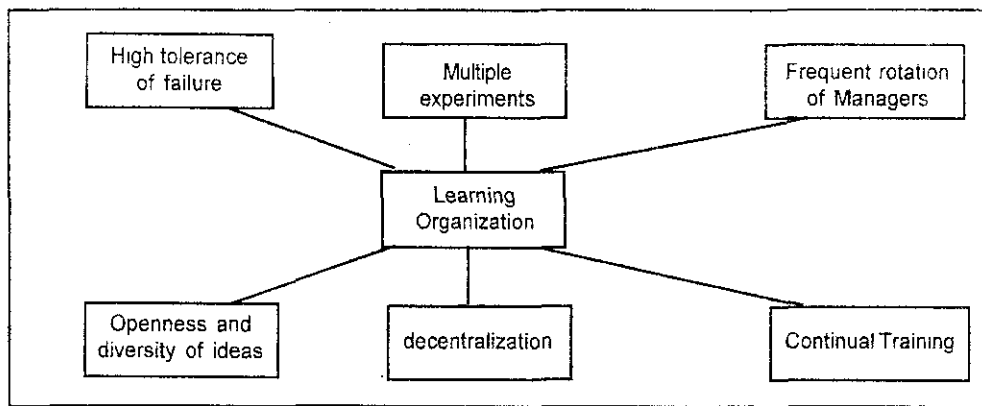


Exhibit 11.15: Characteristics Enhancing Capabilities to Adaptation to Rapid Change

1. Frequent Rotation of Managers

Managers usually become emotionally attached to their jobs, specially when they have been on the job for a long time. They become familiar with their work and their environment and they feel comfortable with their strategies and the way they do things. Over time, they develop a tendency to become less accepting of changes such as new strategies, approaches and way of doing things. One way to overcome this hesitation to change on the part of managers is their periodic rotation throughout the firm. This would give them exposure to various activities and experiences and they can appreciate the need for keeping an open mind and not be overly attached to just one activity. Such rotation also promotes the building of interrelationships across divisional and possibly functional lines.

General Motors practices such managerial rotation at their Saturn automobile manufacturing operations. Even employees are rotated through various activities so that not only do they acquire new and different skills in this process, but they also contribute towards an environment of informality and harmony. This results in improvements in the quality of the output.

2. Continual Learning

One reason why employees resist changes is the level of their comfort with their own skills and fear about the outcome of any change. If the organisations have inhouse facilities for regular and continuous training and development through which managers and their subordinates can learn new skills, then such resistance to change can be eliminated. Japanese companies put a high premium on internal training programmes and they encourage all employees to learn new skills and technologies. Sony, for example, views these training and development programmes as an ongoing investment for overall continuous improvement in all operations and functions.

3. Decentralisation

Decentralisation requires that the decision making authority be dispersed by extension and delegation through all levels of management. It tends to create a climate where by taking additional responsibilities and challenges, the organisational members receive executive training for growth and development. This freedom to make decisions gives the workers a feeling of status and recognition and this results in a feeling of dedication, commitment and belonging. This decentralisation of authority is also practical because the lower level subordinates are much closer to the points of operations and are in a position to know the problems more quickly and more accurately and hence are more likely to make the right decisions. Such authority encourages innovation, learning and creativity. For example, Johnson and Johnson, a conglomerate of 50 operating divisions, has decentralised all divisions so that each division

has the authority to do whatever is needed to succeed in its market. This high degree of decentralisation has enabled all business units to become some of the most successful innovators in their products and in their marketing techniques.

4. Openness and Diversity

Management must keep two-way channels of communication open and must be responsive to the diversity of viewpoints. This is a critical point for the learning process because learning generally comes from outside sources and closing the door to new and diverse ideas will be a hindrance to learning. Managers must be able to appreciate other people's viewpoints, values and experiences as sources of input for learning and decision making and must be willing to listen to their ideas and perspectives. For example, when Sony Corporation, which is primarily in electronics business acquired Columbia's film producers and studio managers to share their viewpoints with Sony managers so that they can learn about the specific film making problems. This openness has resulted in solving many problems that their film division faced.

5. High Tolerance of Failure

If managers are punished for their failures, then they will shy away from some good but risky adventures, even if the rewards of success are very high. All innovative projects have always some chances of failure. Fear of failure should not keep innovation under check. Accordingly, senior management must encourage their subordinates if their projects and efforts are meaningful and reasonable. In successful companies, failures are defined as experiments to learn from and an acceptable part of the learning process and personal growth. A case in point is Sony's development of digital cameras during the 1980s. The buying public was not ready for it and the project failed. Sony did not penalise their managers who were responsible for developing this product, but instead encouraged them to learn from this experience and apply their expertise in designing new products and technologies. Even with this failed product, Sony gained many insights into digital technology which was used into the new versions of many electronic devices such as CDs, VCRs and so on.

6. Multiple Experiments

The dynamics of technological advancements has made the development of new products, in keeping up with technology, much more complex task and process. Some times, a number of alternatives need to be pursued simultaneously to determine which one is better. It also makes it unlikely that a superior approach will be overlooked. The cost of running multiple projects should also be taken into consideration. The potential benefits must outweigh any costs involved. Looking at a problem from different angles and viewpoints might result in better solutions. Multiple approach also encourages people to look at situations differently and exposes them to different ways of thinking about and doing things. Sony Company's success with Walkman was a result of experimentation by several project teams which looked into the type of format which would be most desirable by consumers and would also be relatively easy to manufacture.

Many organisations have fully incorporated the characteristics discussed above. These organisations can adapt quickly to environmental changes and continuously create new sources of competitive advantage.

The learning process is undertaken at two different levels. These are lower level learning and higher level learning. The lower level learning is characterised by refinements in existing beliefs, understandings and organisational processes. On the other hand, the higher level learning involves developing new beliefs, understandings and organisational processes. Both types of learning are critical to organisational success. Lower level learning is described by one management scholar as "exploitation of the known" and higher level learning as "exploration of the new". Without lower level learning, it will be difficult for organisations to maintain a competitive edge in the existing market. Without higher level learning, the organisations will be so set with their routines that they become vulnerable to competitive forces created by new technologies and new products and services.

Research conducted by Cohen and Levinthal suggests two factors which contribute to the extent of higher level learning. First is the result of “problematic search”. In other words, if the established procedures and methodologies fail to deal with problems or crisis effectively, then managers search for new ways to solve such problems and this lead to higher level learning. Similarly, if the activities and operations are not consistent with the aspirations and vision of upper level managers, then they will initiate a problematic search to look for areas which can be further improved.

The second factor that influences higher level learning is known as “absorptive capacity”, which has been defined as the ability of the organisations to recognise and understand the value of new developments and absorb these developments in their system and use it for organisational benefit. Thus, the organisations monitor their external environments for any developments in emerging technologies and adopt these technologies in the organisation’s internal environment.

Some changes are deliberate, initiated by central management, carefully planned and goals oriented. The objectives of the planned change are two-fold. First, it seeks to improve the ability of the organisation to adapt to changes in its environment. Second, it seeks to change employee behaviour.

Once the need for change and the targets for change have been identified, the following general steps can be taken to implement such changes.

- *Develop New Goals and Objectives.* The managers must identify as to what new outcomes they wish to achieve. This may be a modification of previous goals due to change in internal and external environment or it may be a new set of goals and objectives.
- *Select an Agent for Change.* The management must decide as to how this change will be brought about. The decision may include inviting outside consultants and specialists who could suggest the various methods to bring in the change and monitor the change process.
- *Diagnose the Problem.* It is important to gather all pertinent data regarding the area where change is needed. This data should be critically analysed to pinpoint the key issues. Then the solutions can be focused on those key issues.
- *Select Methodology.* Because of natural resistance to change, it is very important to chart out a methodology for change which would be correct and acceptable to all. Members emotions must be taken into consideration when devising such methodology.
- *Develop a Plan.* This step involves putting together a plan as to what is to be done. For example, if a company wants to develop and implement flexitime policy, as to making the hours of work flexible to workers, it must decide as to what type of workers will be affected by it or whether flexitime should be given to all members or only to some designated members.
- *Select a strategy for implementation of the plan.* In this stage, the management must decide on the “when”, “where” and “how” of the plan. This includes the right timing of putting the plan to work, how the plan will be communicated to the workers in order to have the least resistance and how the implementation will be monitored.
- *Implement the Plan.* Once the right timing and the right channels of communication have been established, the plan is put into action. It may require briefing sessions or in-house seminars so as to gain acceptance of all the members and specially those who are going to be directly affected by the change.
- *Receive and Evaluate Feedback.* Evaluation consists of comparing actual results to the set goals. Feedback will confirm if these goals are being met so that if there is any deviation between the goals and the actual performance outcomes, the corrective measures can be taken.

According to Plunkett and Attner, managers can help create a climate that could be more conducive to change. The following three elements can be taken into account when developing a philosophy towards change.

1. Mutual Trust

Research studies have shown that trust is the most important factor in creating an effective and successful organisation. Mutual trust is a strong bond in friendship, in marriage as well as in organisational relationships. It gives great security in times of adversity and in an atmosphere of trust, employees will feel comfortable as the organisation moves through change.

2. Organisational Change

Organisational learning refers to the ability of the management to integrate new ideas into established systems so that a change for the better can be continuously in effect. There are many ways of doing things, and as such ways are adopted that encourage employees to share ideas and participate as change agents, all members learn to find the best ideas and put these ideas to work.

3. Adaptability

Adaptability means flexibility rather than rigidity. It means being open to new and different ways of doing things. If the managers are open-minded, responsive to any feasible ideas and recognise that change is beneficial and not threatening, then the organisation can be moulded to accept and promote change.

The Change Agents

The change agents are those elements which are responsible for bringing about the change, specially in the individual behaviour patterns. This is the most important type of change since other types of changes such as in strategy, structure or process can always be introduced simply by the management. However, behaviour patterns may have to be modified so that such management induced changes are accepted by the workers. Also, because behaviour is a highly complex phenomenon, it may require a number of strategies to make desirable changes in human behaviour. These change agents may either be the initiators of change or serve as catalysts for such change. Four types of change agents have been identified.

1. Outside Pressures

These are pressures from the external environment and are directed towards change in the entire organisation. These pressures may be in the form of government intervention, if there are serious quality or safety defects. The government may also get involved if there are labour strikes for long periods of time or mass demonstrations against the organisation. For example, in America, the government has ordered a recall of many types of automobiles when some safety defects have been discovered. Similarly, health inspectors have closed down many restaurants where health and safety violations were discovered in food and cleanliness.

2. Internal Organisational Development

This can come slowly through and within the organisation itself. This may include redefinition of goals as well as participative goal setting. Such development can be achieved through management by objectives (MBO), work redesign, team development and so on.

3. Individual Change

This change is the modification of behaviour within the individual where personal goals may be better served in the changed environment of the organisation. For example, in a government job, a person who is habitually late coming to work without any obvious repercussions or reprimands, might change his behaviour if the organisation starts taking notice of such tardiness in a negative way.

4. Changes from Central Management

The organisational changes may come from the top management, who may be convinced about its necessity and may direct and structural, strategic or technological changes that would be beneficial to the organisation and its members.

There have been a number of change agents that have been at work in changing the organisational processes and structures in response to environmental challenges. In America, for example, Ralph Nader, a consumer advocate, has been responsible for many changes in the areas of quality and safety of many products and especially in the automobile industry. In addition, such forces as women's liberation movement, strong labour unions and specific federal and state laws and regulations have brought about numerous changes that have affected the work ethics of the organisations and work roles of their members. Similarly, in India, where the bureaucratic structure is deeply embedded in the organisational system, pressures to give more freedom to the workers, to bring about equal opportunity for employment for all, irrespective of religion or gender and to keep pace with the changing world in technological development and processes.

Managing Resistance to Change

If the changes are to be implemented successfully, they need full acceptance from the employees. The easiest way to get this accepted is the participation of employees in the change effort. Research conducted by Coch and French in a clothing factory indicated that the total participation in the change process resulted in increased productivity. Some of the specific strategies employed in reducing resistance to change are as follows:

- *Shape Political Dynamics.* Accepting and implementing change becomes easier if the management can win the support of the most powerful and influential individuals in the organisation. Doing so builds a critical internal mass of support for change. These influential people could be informal leaders who can influence their followers and these can also be formal leaders such as managers and supervisors. Such endorsement for change by the leaders is an effective way to get others to go along.
- *Participation and Involvement.* A person who is involved in the process of change from the very beginning is more strongly committed to the change than someone who did not participate. Management must recognise this fact. The participation of employees in the process of change should be genuinely wanted by the employees so that they are enthusiastic about it. It should not simply be a mechanical act of calling upon many employees to "participate". Participation should be a part of and a result of total treatment of the employees. Thus, once they understand the need for change, they would be less likely to resist it.
- *Communication and Education.* If the employees do not have adequate information or if the information they have is inaccurate, then it is necessary to educate them about the change, its process, its working and its results. This education can be carried out through training classes, meetings and conferences. The reasons for the change must be communicated very clearly and without ambiguity at these meetings and the top management must show considerable emotional sensitivity towards workers. This will help persuade employees about the necessity for change and once persuaded they may even actively seek the change.
- *Reward Constructive Behaviours.* Once successful mechanism to facilitate organisational change is rewarding people for behaving in the desired fashion. This is especially critical during the transition period. For example employees who are required to learn new skills due to technological changes and learn them well should be praised for their successful efforts and they may also be offered financial incentives.
- *Leadership.* The greater the prestige and the credibility of the manager who is acting as a change agent, the greater will be his influence upon the employees who will be involved in the change process. Accordingly, it is important for the manager to win the confidence of the employees so that they become enthusiastic partners in the process of change.

- *Negotiation and Agreement.* Negotiation and agreement technique is used when costs and benefits must be balanced for the benefit of all concerned parties. This is often used in bargaining with labour unions. It is specially important in situations where the individuals or groups will end up as losers as a result of the change and where such individuals or groups have considerable power to resist.
- *Willingness for the Sake of the Group.* Some individuals may be willing to accept change, even if they are not totally satisfied with it, if the group that they belong to is willing to accept such change. This is specially true about the individuals who have a continuous psychological relationship with the group so that there is sufficient group cohesiveness or group togetherness. Accordingly, management must isolate such groups who have considerable influence upon its members and try to induce the group to involve itself in the change process and accept the necessary change.

These measures can assist considerably in reducing resistance to change. The management must understand that while unilateral use of authority and the power vested with them can sometimes bring change, and it may be necessary to use this power under certain situations, such a change would be highly resented and may be short-lived. For long-term stability of the change process, the management must invite active and willing participation from the employees and share with them the benefits derived from the change.

The Change Process

Once the resistance to change has been overcome and the need for change and the objective of such change are established and accepted, management must introduce the change process in such a manner that such change is more or less permanent and the management does not shift back to the original and more familiar ways of doing things. To make the change more lasting, Kurt Lewin proposed three phases of the change process for moving the organisation from the present to the future. These stages are: unfreezing, changing and refreezing.

1. Unfreezing the Situation

The process of unfreezing simply makes the individuals or organisations aware of the necessity for change and prepares them for such a change. Lewin proposes that the change should not come as a surprise to the members of the organisation. Sudden and unannounced change would be socially destructive and morale lowering. The management must pave the way for the change by first "unfreezing the situation", so that members would be willing and ready to accept the change. This way, if there is any resistance to change, it can be neutralised. According to Schein, unfreezing is the process of breaking down the old attitudes and behaviours, customs and traditions so that they start with a clean slate. This can be achieved by making announcements, holding meetings and promoting the ideas throughout the organisation via bulletin boards, personal contacts and group conferences. One type of message to the members of the organisation, suggested by Kreitner is as follows:

"We can all improve the effectiveness of our organisation while increasing our personal satisfaction, if we all cooperate in a comprehensive program of finding out where we are, where we want to go and how we can get there."

The unfreezing process basically cleans the slate so that it can accept new writings on it which can then become the operational style.

2. Changing to New situation

Once the unfreezing process has been completed and the members of the organisation recognise the need for change and have been fully prepared to accept such change, their behaviour patterns need to be redefined. H.C.Kellman has proposed three methods for reassigning new patterns of behaviour. These are:

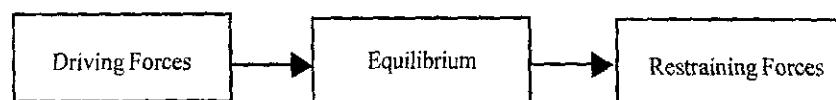
- *Compliance.* Compliance is achieved by strictly enforcing the reward and punishment strategy for good or bad behaviour. Fear of punishment, actual punishment or actual reward seem to change behaviour for the better. For example, many people have stopped smoking because of the warning given by the Surgeon General of the United States that smoking causes cancer of the lungs.
- *Identification.* Identification occurs when members are psychologically impressed upon to identify themselves with some given role models whose behaviour they would like to adopt and try to become like them. Many public organisations use celebrities as role models in advising young people not to use drugs.
- *Internalisation.* Internalisation involves some internal changing of the individual's thought processes in order to adjust to a new environment. Members are left alone to look within themselves and they are given freedom to learn and adopt new behaviour in order to succeed in the new set of circumstances. Sometimes, such soul searching bring about a new dimension to the philosophy of existence and thus bring about changes in such behavioural patterns that are not considered socially, morally or professionally redeeming.

3. Refreezing

Refreezing occurs when the new behaviour becomes a normal way of life. The new behaviour must replace the former behaviour completely for successful and permanent change to take place. Accordingly, in order for the new behaviour to become permanent, it must be continuously reinforced so that this new acquired behaviour does not diminish or extinguish.

This must be clearly understood that the change process is not a one time application but a continuous process due to dynamism and ever changing environment. Accordingly, the process of unfreezing, changing and refreezing is a cyclical one and remains continuously in action.

The implementation of this three step change model can be seen in the case of kidnapping victims or prisoners of war or deprogramming of some religious cultists. The prisoners of war, for example, may be brainwashed into believing that they are fighting a losing and immoral war and that their perceived enemy is really their friend. This can be done by certain shock treatments which involve these three steps of unfreezing, changing and refreezing process as explained earlier. If these prisoners return back to their own country, the process can be repeated to bring them back to their original behaviour. Another methodology to induce, implement and manage change was also proposed by Kurt Lewin, who named it "force-field analysis". This analysis is based upon the assumption that we are in a state of equilibrium where there is a balance between forces that induce change and forces that resist change. To achieve change we must overcome this status quo. The change forces are known as "driving forces" and the forces that resist change are known as "restraining forces" as shown below:



Managers who are trying to implement changes must analyse this balance of driving and restraining forces and then strengthen the driving forces or weaken the restraining forces sufficiently so that the change can take place.

Some of the other strategies pursued by strategic managers to bring about changes are: *reengineering*, *restructuring* and *innovation*. In order to achieve the goal of competitive edge, the organisations may adopt one or more of these strategies.

- (i) **Reengineering:** Reengineering is the "fundamental and radical redesign of business processes to achieve

dramatic improvements in critical, contemporary measures of performance such as cost, quality, service and speed. Reengineering involves complete overhaul of the organisation and strategic managers must completely rethink about the operations and activities of the organisation and focus on business processes rather than on business functions. A business process is any activity that promotes efficiency. It is not the responsibility of any one function but cuts across functions. The primary emphasis of reengineering is on customer satisfaction. The question that strategic managers always keep in focus is "how can we reorganise the way we do our work and our business processes in order to provide the best quality and the lowest-cost goods and services to the customer?" The proper response to this question results in fundamental changes in the business processes. The next question that requires attention is, "how can we now continue to improve our processes and find better ways of managing task and role relationships?"

- (ii) **Restructuring:** Restructuring involves making changes in the structure of the organisation so that some relationships in the organisation can be combined to make a flat structure and this should improve communication and thus efficiency. This requires eliminating unproductive division as well as some layers of corporate hierarchy. The process of making a flat organisation by reducing the number of managerial levels and divisions is known as downsizing. There are a number of reasons why downsizing becomes necessary. It is possible that the company has grown to be too tall over the years so that the human resources are not optimally utilised. Also a change in economic environment may reduce business activity thus necessitating structural changes. When Jack Smith became the Chief Executive Officer (CEO) of General Motors (GM) in 1992, the company had 22 levels in hierarchy and more than 20,000 corporate managers. Smith quickly moved to restructure the company so that it resulted in 12 hierarchical levels and 10,000 corporate managers.
- (iii) **Innovation:** Innovation is a process by which organisations use their skills and resource to create new innovative technologies or new products or new services so that they can better serve the needs of the customers. Without such innovation, organisations will be left behind. The new more powerful laptop computers are the result of technological innovation. Innovation can result in spectacular success for an organisation. For example, Apple Computer brought in a revolution in computer industry when it introduced a personal computer (PC). Similarly Honda made inroads in American economy by introducing a 50-cc motor cycle and at one time it controlled 80 percent of the market. Mary Kay Cosmetics developed a new way of serving customers by going to customers rather than customers coming to the cosmetic outlets.

Of all the strategies employed by strategic managers to bring about change, innovation is the most involved, and has the prospects for the greatest long-term success. Not all innovations are successful and hence a cost and benefit study should be conducted before commercialising the innovation.

Resistance to change can be considered the single greatest threat to successful strategy implementation. Resistance in the form of sabotaging production machines, absenteeism, filing unfounded grievances, and an unwillingness to cooperate regularly occurs in organizations. People often resist strategy implementation because they do not understand what is happening or why changes are taking place. In that case employees may simply need accurate information. Successful strategy implementation hinges upon managers ability to develop an organizational climate conducive to change. Change must be viewed as an opportunity rather as a threat by managers and employees.

Resistance to change can emerge at any stage or level of the strategy-implementation process. Although there are various approaches for implementing changes, three commonly used strategies are a force change strategy, an educative change strategy, and a rational or self-interest change strategy. A force change strategy involves giving orders and enforcing those orders; this strategy has the advantage of being fast, but it is plagued by low commitment and high resistance. The educative change strategy is one that presents information to convince people of the need for change; the disadvantage of an educative change strategy is that implementation becomes slow and difficult.

However, this type of strategy evokes greater commitment and less resistance than does the force strategy. Finally, a rational or self-interest change strategy is one that attempts to convince individuals that the change is to their personal advantage. When this appeal is successful, strategy implementation can be relatively easy. However, implementation changes are seldom to everyone's advantage.

The rational change strategy is the most desirable, so this approach is examined a bit further. Managers can improve the likelihood of successfully implementing change by carefully designing change efforts. Jack Duncan describes a rational or self-interest change strategy as consisting of four steps. First, employees are invited to participate in the process of change and the details of transition; participation allows everyone to give opinions, to feel a part of the change process, and to identify their own self-interests regarding the recommended change. Second, some motivation or incentive to change is required; self-interest can be the most important motivator. Third, communication is needed so that people can understand the purpose for the changes. Giving and receiving feedback is the fourth step; everyone enjoys knowing how things are going and how much progress is being made.

Igor Ansoff summarizes the need for strategists to manage resistance to change as follows:

Observation of the historical transitions from one orientation to another shows that, if left unmanaged, the process becomes conflict-laden, prolonged, and costly in both human and financial terms. Management of resistance involves anticipating the focus of resistance and its intensity. Second, it involves eliminating unnecessary resistance caused by misperceptions and insecurities. Third, it involves planning the process of change. Finally, it involves monitoring and controlling resistance during the process of change.

Due to diverse external and internal forces, change is a fact of life in organizations. The rate, speed, magnitude, and direction of changes vary over time by industry and organization. Strategists should strive to create a work environment in which change is recognized as necessary and beneficial so that individuals can adapt to change more easily. Adopting a strategic-management approach to decision making can itself require major changes in the philosophy and operations of a firm.

Strategists can take a number of positive actions to minimize managers and employees' resistance to change. For example, individuals who will be affected by a change should be involved in the decision to make the change and in decisions about how to implement change. Strategists should anticipate changes and develop and offer training and development workshops so managers and employees can adapt to those changes. They also need to communicate the need for changes effectively. The strategic-management process can be described as a process of managing change. Robert Waterman describes how successful (renewal) organizations involve individuals to facilitate change:

Implementation starts with, not after, the decision. When Ford Motor Company embarked on the program to build the highly successful Taurus, management gave up the usual, sequential design process. Instead they showed the tentative design to the work force and asked their help in devising a car that would be easy to build. Team Taurus came up with no less than 1,401 items suggested by Ford employees. What a contrast from the secrecy that characterized the industry before! When people are treated as the main engine rather than interchangeable parts, motivation, creativity, quality, and commitment to implementation go up.

Chapter 12

Behavioural Implementation Leadership, Culture, Politics, Power, Values and Ethics

Objectives to large extent reflect the expectations of stakeholders. To be successful, however, a company has to prioritize its objectives. Achievement of the objectives with emphasis on priorities is the basic aim of corporate strategic decisions.

It is important to emphasize that culture, value, and leadership, jointly and severally, significantly influence the shaping of corporate strategies. The culture of an organization is reflected in the way that people in the organization perform tasks, set objectives, and administer resources to achieve them, and is in its turn strongly influenced, if not moulded by the values originating largely from national history, tradition, and ethos. A third element in the threesome is leadership. It is universally recognized that the more successful organizations are those that are well led rather than those that are only well managed. Perhaps the most essential quality of a leader is his vision reflected in the mission of the organization. A successful leader is however, endowed with the capacity to convert that vision into the mission and goal of the organization and lead the organization to the achievement of its goals. For *sustained* success of the organization, however, this vision needs to be transmitted to become the abiding core values and culture of organization.

Objectives tend to emerge as the wishes of the most dominant coalition, usually the management of the organization, although there are notable exceptions. However, in pursuing these objectives the dominant group is very strongly influenced by its reading of the political situation (i.e. the perception of the power structure). For example, they are likely to set aside some of the expectations in order to improve the opportunities of achieving others.

Special reference must be made to the power of shareholders. Some of them have a short-term viewpoint being basically interested in quick return. Others have a longer-term view and also look for growth in the value of the shares. With the evolution and development of a professional managerial class the direct intervention of shareholders has become much less frequent. They tend to remain quiescent so long as their expectations are at least moderately met. If, however, they perceive or are made to perceive any threat to these prospects or are reasonably convinced of a better return under an alternative management, their intervention is immediate and decisive.

General Influence on Individuals and Groups

These are perhaps best encapsulated as in Exhibit 12.1. When analysing the significance of these factors on the strategic development of any organization, it is useful to ask the following questions:

- i. Which factors within and outside the organization have the most influence on the expectations of groups and individuals within it?
- ii. To what extent do the current strategies reflect the influence of any one of a combination of these factors?
- iii. How far would these factors help or hinder changes that would be necessary to pursue new strategic? External Influences

Values of Society

Attitudes to work, authority, equality, and a whole range of other important issues are constantly shaped and changed by society at large. From the point of view of corporate strategy it is important to understand this process for two reasons:

- a. The values of society change over time and corporate strategies need to be adapted accordingly.

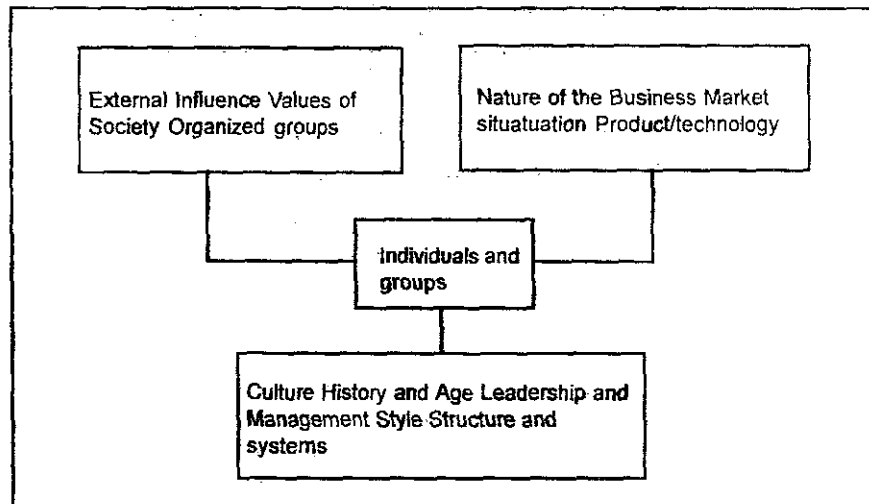


Exhibit 12.1: Influence on Individuals and Groups

- b. Companies that operate internationally would have the added problem of having to cope with very different standards and expectations across countries.

Two examples are interesting.

- i. Hofstede has undertaken extensive research into how national culture influences employee motivation, management styles, and organizational structures. He concludes that individual countries are markedly different from one another.
- ii. Terry, in his study of influence of British culture on the performance of managers concludes that the biggest single advantage of the British is that they do not pame when things get rough. On the other hand, their identifiable traits are insularity, chauvinism, and a low regard for professionalism in business.

Organized Groups

Individuals often owe allegiance to other groups such as trade association and professional bodies, which greatly influence their attitudes. Consequently, very often this professional staff has a strong 'professional' view of its role which may not accord with the managerial view of how it can best be used as a resource. At the corporate level, the entire organizational ethos of the company may be influenced by its membership of a trade association or similar body. These bodies may exert influence informally, but often seek to impose norms of behaviour on member companies through the development of 'codes of conduct'. At the international level, the Organisation of Petroleum Exporting Countries (OPEC) is an example.

Nature of the Business

In the case of business, issues such as market situation and the nature of product/technology within the company influence attitudes to company policy.

Market Situation

Different companies face quite different market conditions and any one company will face different conditions over time. Consequently, the attitude of people within the company will also change, often quite markedly, as external conditions change. Policy decisions that can be made in companies facing a highly competitive and depressed market will meet with considerable resistance in other companies facing less stringent conditions.

People are also influenced by the position of the company in relation to the life cycle of its products and market. People who have only known a company during a period of rapid growth may have developed expectations that are inappropriate when its product enter the stage of maturity.

Leadership Implementation

The role of appropriate leadership in strategic success is highly significant. It has repeatedly been observed that leadership plays a critical role in the success and failure of an enterprise and "it has been considered one of the most important elements affecting organisational performance. For the manager, leadership is the focus of activity through which the goals and objectives of the organisation are accomplished". While dealing with the role of strategists we learnt about the roles that different strategists play in strategic management. In particular, the role of chief executives as organisational leaders was discussed with a view to highlight the importance that is accorded to them since they are the most important of all strategists. Here, we discuss the leadership role that is assigned to strategists in general. We start with a review of the leadership theories and what lessons can be drawn from them for the purpose of strategy implementation.

Theoretical underpinning of Leadership

Leadership has been studied and researched for a number of years, resulting in numerous theories and models. No universally accepted theoretical framework has as yet been developed. However, enough is already known to be able to understand the various factors that affect the content and process of leadership. Exhibit 12.2 presents an overview of leadership theory through the different evolutionary eras and the emphasis placed on it in each era. It should, however, be noted that the eras are not chronological but have been set in terms of the similarity of approach adopted by several theorists. Thus, an era represents a group of leadership theories all of which adopt a similar approach. King points out that the future development of leadership theory may be based on an integrated approach.

Alber S King traces the historical development of leadership theories and identifies nine evolutionary eras, each focussing on a specific theme of leadership.

Era	Focus on
1. Personality	Traits and qualities, and great personalities
2. Influence	Relationship between individuals
3. Behaviour	Actions of leaders
4. Situation	Situation in which the leader operates
5. Contingency	Dependence on behaviour, personality, influence exerted by the leader on subordinates, and situation
6. Transactional	Role-differentiation and social interaction between the leader and subordinates
7. Anti-leadership	Absence of a real concept of leadership
8. Culture	Culture of the entire organisation
9. Transformational	Use of influence to create intrinsic motivation

Exhibit 12.2 Theory and Practice of Leadership

The tenth era, which King terms as the integrative era, may probably focus on an integration of the different approaches.

The evolutionary eras, as classified by King, bring into clear focus the changing emphasis of different theories of leadership. A greater understanding of the phenomenon of leadership may come through the integration of the different approaches in future.

Sziglayi and Wallace have proposed an integrative model of leadership based on three different theoretical approaches of leadership: trait (or personality), behavioural, and situational theories. Their integrative model of leadership includes four factors on the basis of which behavioural scientists and practicing managers can attempt to understand the phenomenon of leadership. These four factors are: the leader (individual characteristics, leadership style, dimension and reinforcing power); the subordinate (individual characteristics, and perception), the situation (nature of task, nature of group, organisational factors, sources of influence other than the leader), and the performance outcomes.

From the above, it can be seen that leadership has proved to be an elusive concept. Yet, the different attempts at explaining the phenomenon of leadership have increased our understanding of the issue and provided significant insights into its complexities.

Several conclusions can be drawn from theory regarding the manner in which leadership could be implemented by strategists. On the basis of its present state of knowledge, it can be said that the leader must.

- develop new qualities to perform effectively
- be a visionary, willing to take risks, and be highly adaptable to change
- exemplify the values, goals, and culture of the organisation, and be aware of the environmental factors affecting the organisation
- pay attention to strategic thinking and intellectual activities
- adopt a collective view of leadership in which the leaders influence is dispersed across all levels of the organisation.
- lead by empowering others and place an increasing emphasis on statesmanship
- adopt a new perspective on power to build subordinates' skills and confidence to make them agents of change
- create leadership at lower levels and facilitate the transformation of followers into leaders
- delegate authority and place emphasis on innovation

It is useful to shortlist the qualities and skills for effective leadership. These are:

- A vision, articulated through the culture and value systems.
- The ability to build and control an effective team of managers.
- The ability to recognize and synthesize important developments, both within and outside the organization. Requires strategic awareness, the ability to judge the significance of an observed event, and conceptualization skills.
- Effective decentralization, delegation and motivation.
- Credibility and competence: knowing what you are doing and having this recognized. Requires the ability to exercise power and influence and to create change.
- Implementation skills: getting things done, requires drive, decisiveness, and dynamism.
- Perseverance and persistence in pursuing the mission or vision, plus mental and physical stamina.

- Entrepreneurial qualities

This perhaps requires some elaboration, and takes the form of

- i. expansion of the concept of vision.
- ii. differentiation between leadership and management.
- iii. expansion on certain other requirements of leadership.

Vision

The leader's vision which gives point to the work of others should have the following attributes. The vision must be different.

A plan or a strategy which is a projection of the present or a replica of what everyone else is doing is not vision. A vision should

- reform the known scene.
- reconceptualize the obvious,
- connect previously unconnected dreams.

The vision must make sense to others.

The vision must be comprehensible

The leader must live the vision.

He or she must only believe in it but must be seen to believe in it.

The leader must remember that the vision remains a dream without the work of others

Differentiating between Leadership and Management

- Management is all about coping with complexity. Its practices and procedures are largely a response to the emergence of large organizations. Without good management, complex enterprises tend to become chaotic in ways that threaten their very existence.
- Leadership, by contrast, is about coping with change and determining directions.
- Companies manage complexity first by planning and budgeting: setting targets or goals for the (near) future (typically for the next month or year), establishing detailed steps for achieving these targets, and then allocating resources to accomplish them. By contrast, leading an organization to constructive change begins by setting a direction: developing a vision of the future (often the distant future) along with strategies to initiate the changes needed to achieve that vision.
- Management develops the capacity to achieve its plan by organizing and staffing, and in effect aligning people.
- Finally, management ensures plan accomplishment by controlling and problem solving: monitoring results in relation to the plan in some detail, both formally and informally, by means of reports, meetings, and other tools; identifying deviations. For leadership, however, achieving a vision involves motivation and inspiration, and thereby keeping people moving in the right direction, despite major obstacles to change, by appealing to basic but often untapped human needs, values and emotions.

Certain Other Requirements of Leadership

For leadership to flower, some things are necessary:

Essential requirements for discovery of one's leadership quality include:

- * Early responsibility.
- * Readiness to forgive oneself and be forgiven for mistakes made in the process of decision-making.
- * A belief in oneself
- * An awareness of other worlds
- * A company for lonelines

One of the major attributes of leadership is an attitude biased in favour of risk taking when oriented towards growth and success. This is particularly important as it implies a clear distinction between a first generation entrepreneurial strategic leader and a professional manager as chief executive. A first generation entrepreneurial strategic leader usually has personal values biased towards growth-oriented risk taking, and an ability to imprint his personal values and motivations on the organization. As the company grows older, its strategic leadership is taken over by professional managers whose culture and values are oriented towards managerial bureaucracy and its characteristic, comparatively negative attitude towards risk and innovation. This is amply evident in the recent history of Ford and General Motors. Chrysler, in comparison, demonstrates entrepreneurship and dynamism as it was 're-born' and, in consequence, has a 'younger' top management.

As a company grows older and takes on the role of a historical firm rather than an emerging one, however, the role of providing strategic leadership shifts to the general management and shareholders and, the 'founder' entrepreneur often finds his personal vision and goals at variance with those of the organization and finds himself pushed by the wayside.

This also marks a clear distinction between Japanese strategic leadership and that of the West, in particular the USA. Most Japanese industrial organizations still have their first generation entrepreneurs as CEOs who have successfully imprinted their personal values and attitudes on the organizations concerned and been able to impart sustained dynamism to them.

The significant difference between Japanese and Western leadership is, however, elsewhere. Generally speaking, Japanese firms do not have individual leadership but group leadership. What is very important is how individual 'followership' is transformed into group leadership and through this organizational process individual passiveness is transformed into collective dynamism. We cannot induce a dynamic and innovative set of organizational decision sets from a simple aggregation of a set of non-innovative and reserved individual decision codes. What is required is some form of quality transformation process, in turn requiring an organizational device to effect it, so that the passive decision codes of individual members can be changed into active codes of the firm. (Exhibit 12.3).

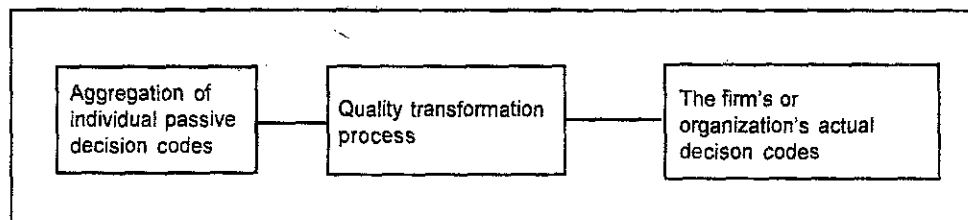


Exhibit 12.3: The Transformation of Decision Codes

The most significant aspect of Japanese strategic leadership is the development and use of this transformation device.

This is reflected in a chain of leadership based on merit in apparent contradiction to the concept of seniority embedded in the Japanese management system. The Japanese reward system has two distinct characteristics. While respect for seniority remains undisturbed as does lifetime employment as the backbone, there is a bifurcation at senior levels. Those with requisite merit are promoted within the organization and those lacking it are diverted out of the organization into subsidiaries or supplier organizations under the firm's umbrella.

Summarizing, Japanese culture and value are reflected in:

- Consensus in decision-making;
- respect for seniority;
- individual suggestions converted to group recommendations;
- meritocracy;
- entrepreneurial and innovative leadership;
- discipline.

Lastly, the cultural trait of quest for quality (as reflected in Buddhist teaching) has led Japanese industries from copying Western design improvement to innovation. This again stems from the concept of *wa kan yoh sai* (Japanese spirit and Western technology).

What about the Future?

Tattwajnananda infers that the Japanese concept of ethics, values, management style is only a transient phenomenon and is likely to go the Western way.

A few symptoms tend to confirm this inference. For instance:

- In a survey Exhibit 12.4 labour mobility reflected a shift from a strong tendency for labour to by and large remain content with the same employer throughout life. This shift, although comparatively minor, is still significant. It is a reflection of the seniority system supporting lifetime employment from inside and the wage system based on seniority forming the "closed" systems found in Japanese firms.
- Japanese youth have also started changing towards greater meritocracy (Exhibit 12.5).

	Percentage
Never	71.5
Once	14.8
Twice	5.4
Three times	2.2
Four or more times	1.3
No answer	4.9

Exhibit 12.4: Japanese Youth (1)
How many times have you changed jobs?

	Percentage
Only by seniority	10.2
Mainly by seniority but performance also considered	36.0
Mainly by performance but seniority also considered	25.8
Only by performance	6.5

Exhibit 12.5: Japanese Youth (2)
How would you like promotions and salary increases to be decided?

The following quotation and case histories are useful indicators:

Professor Kazuo Noda of St. Paul's University:

The young Japanese should really be regarded as foreigner-and foreigners from underdeveloped countries. They do not know old values, they do not conform to the established Japanese way of life and they do not know how to behave....In reality these young men are offshoots of a Japan that is itself changing

During the recent recessions, many companies offered employees voluntary redundancy. Much to the chagrin of the management, they found that young employees in their twenties and thirties who are most needed by the company are always the first to take advantage of such an offer. Employees in their forties and fifties, who command much higher salaries, and who the company really wished to retire, were always the last to leave.

While the permanent employment system has fostered a sense of security amongst older personnel, young employees are getting increasingly restless and do not appear to care for it over much. The personnel director of a large manufacturing company which was going to relocate one of its plants in the country had a rather serious problem on hand. Relocation of most of the workers and managers was to a distant plant several hours away from Tokyo, and many young engineers rather than change their workplace, preferred to change jobs, and were leaving the company wholesale.

Corporate Culture

The phenomenon which often distinguishes good organisations from bad ones could be summed up as 'corporate culture'. The well-managed organisations apparently have distinctive cultures that are, in some way, responsible for their ability to successfully implement strategies. "It has been clearly demonstrated that every corporation has a culture (which often includes several subcultures) that exerts powerful influences on the behaviour of managers." We shall see below what corporate culture is, how it influences corporate life, and how it can be managed so that it becomes strategy-supportive.

"Organisational (or corporate) culture is the set of important assumptions-often unstated-that members of an organisation share in common". There are two major assumptions in common: beliefs and values. Beliefs are assumptions about reality and are derived and reinforced by experience values are assumptions about ideals that are derived and worth striving for. When beliefs and values are shared in an organisation, they create a corporate culture.

The manifestation of corporate culture in an organisation is evident in:

- shared things (e.g. the way people dress)
- shared sayings (e.g. "let's get down to work")
- shared actions (e.g. a service-oriented approach)
- shared feelings (e.g. 'hard work is not rewarded here')

These shared assumptions can help to decipher the composition of the corporate culture of any organisation.

Impact of Culture of Corporate Life

The fact that organisations may have a strong or weak culture affects their ability to perform strategic management. "Culture affects not only the way managers behave within an organisation but also the decisions they make about the organisation's relationships with its environment and its strategy". "Culture is a strength that can also be a weakness". As a strength, culture can facilitate communication, decision-making and control, and create cooperation and commitment. As a weakness, culture may obstruct the smooth implementation of strategy by creating resistance to change.

An organisation's culture could be characterised as weak when many subcultures exist, few values and behavioural norms are shared, and traditions are rare. In such organisations, employees do not have a sense of commitment, loyalty, and a sense of identity. Rather than being members of organisation these are wage-earners. There are several traits exhibited by organisations that have a weak or unhealthy culture. Some of these are: politicised organisational

environment, hostility to change, promoting bureaucracy in preference to creativity and entrepreneurship, and unwillingness to look outside the organisation for best practices.

An organisation's culture could be strong and cohesive when it conducts its business according to a clear and explicit set of principles and values, which the management devotes considerable time to communicating to employees, and which values are shared widely across the organisation.

There are three factors that seem to contribute to the building up of a strong culture. These are: (a) a founder or an influential leader who established desirable values, (b) a sincere and dedicated commitment to operate the business of the organisation according to these desirable values, and (c) a genuine concern for the well-being of the organisation's stakeholders.

Exhibit 12.6 illustrates how corporate culture in two different groups—multinational subsidiaries and professionally-managed companies versus family businesses and non-resident Indians' companies—may create a different impact on an organisation. While the views expressed in this exhibit are decidedly in favour of family business and non-resident Indian's companies, there is no doubt that "in each sector of industry, the management style and corporate culture is distinctive". What is more appropriate to say is that Indian organisations, particularly family businesses, "seem to be in a ferment now", and that companies "known for their conservatism and traditional orientation have to now shift over to a more open and participative corporate culture if they have to maintain progress."

Having discussed that constitutes corporate culture and how it affects corporate life, it is important to understand its relationship with strategy. Since each strategy creates its own unique set of managerial tasks, strategy implementation has to consider the behavioural aspects and ensure that these tasks are performed in an efficient and effective manner. Managerial behaviour arising out of corporate culture, can either facilitate or obstruct the smooth implementation of strategy. The basic question before strategists, therefore, is how to create a strategy-supportive corporate culture. In other words a major role of the leadership within an organisation is to create an appropriate strategy-culture fit.

S K Bhattacharya has analysed the major difference in multinational subsidiaries and professionally-managed companies on the one hand, compared to family business and non-resident Indian's companies on the other, with regard to corporate culture.		
Dimensions of Corporate Culture	Multinational subsidiaries and professionally managed companies	Family business and NRI'S companies
1. Nature of desired managerial skills and capabilities	Emphasis on professional qualification and rank	Emphasis on demonstrated skills, depth, and quality of knowledge
2. Actual performance or results achieved	Emphasis on seniority, conformity to organisational values, loyalty, and a relative fit between desired managerial behaviour and position in hierarchy	Emphasis on originality of action and thinking, innovation, and upgradation of knowledge and skills by personal efforts
3. Managerial style of planning and decision making	Emphasis on Information gathering, bureaucratic mode of functioning, risk-aversion, and non-entrepreneurial decision-making	Emphasis on selective information usage, and intuitive and qualitative decision-making of an entrepreneurial nature
4. Management systems adopted	Emphasis on the use of elegant, sophisticated and rational systems which degenerate due to low usage	Emphasis on reliance on business sense and 'no-frills' systems geared to quick action
5. Nature of management control.	Emphasis on comprehensive, formal, and written reporting, and rationalisation of failures rather than resolution of problems.	Emphasis on primary use of verbal reporting and remedial action

Exhibit 12.6: Impact of Culture on Two Different Groups of Organisations

The strategists have four approaches to create a strategy supportive culture:

1. *To ignore corporate culture.* The first approach may be followed when it is nearly impossible to change culture. This is advisable because it is really difficult to change a nebulous phenomenon such as corporate culture. Besides, cultural changes, when enforced in a short duration, may be traumatic for members of an organisation.
2. *To adapt strategy implementation to suit corporate culture.* It is easier to change implementation to suit the requirements of corporate culture. This is possible because the behavioural aspects of implementation offer a range of flexible alternatives to strategists in terms of structure, systems of corporate culture. However, each situation in the organisation would call for an innovative solution and would test the capabilities of managers as strategists.
3. *To change the corporate culture to suit strategic requirements.* As said earlier, it is extremely difficult to change corporate culture. But in some cases it may be imperative. For instance, the post-liberalisation spate of takeovers and acquisitions in the Indian industry led to a situation where many erstwhile multinational subsidiaries were taken over by family business groups. This led to a process-often prolonged and painful-of cultural transition. But such a transition may be brought about by a careful understanding of existing culture, making strategic risks explicit, assessing risks of cultural change, enhancing managerial capability to imbibe changes, and, most importantly, exhibiting a strong, assertive leadership.
4. *To change the strategy to fit the corporate culture.* Rather than changing culture to suit strategy, it is better and more economical to consider the cultural dimension while formulating strategy in the first place. One of the important factors is commitment to past strategic actions which should take care that strategic changes are not drastic but incremental, allowing the cultural ripple effects to settle down to create a more conducive environment for strategy implementation. However, if an impregnable cultural barrier is faced after strategy implementation, it may be better to abandon the strategy or use a combination of the above three approaches.

It is important to realize that an understanding of the process of policy-making in an organization cannot be achieved without paying attention to the issue of organizational culture. It is equally important when analysing the strategic position of an organization to assess how this culture has influenced the development of the organization and the strategies it has pursued.

A useful analysis of culture can be achieved by examining the cultural web of factors within an organization that preserve and sustain commonly held core beliefs: the 'recipe'. An examination of the recipe is important for two reasons.

- i. It provides a background against which an assessment of future strategic choices can be made, both in relation to options that may be open within the current recipe and for those requiring more significant change.
- ii. Where the recipe would need to be changed to provide a background against which to assess how change might be achieved.

While different facets of the cultural web will be discussed in order to build up an analysis of the influence of culture on strategy, it must be remembered that it is the subtle interrelationship between these various facets that is of greatest importance. The impact of the cultural web on an organization can be analysed by looking at the issues depicted in Exhibit 12.7.

Stories, rituals, and symbolic behaviour in organizations provide valuable insight into the organization's core beliefs. These factors are a product of the history and age of the organization since they come into being and develop over time through the experiences of individuals and groups undertaking the day-to-day tasks. The stories and myths detail the essence of the company's past strategies, legitimize the behavioural pattern of individuals and groups currently within the organization and the attitude of outsiders towards it.

It is an oft-repeated and confirmed observation that the way companies are organized and managed has a strong relationship with the era in which that particular industry had its origins. History and tradition can be a considerable problem where culture has developed in a way that threatens the survival of the organization in the light of a changing environment—such as new technologies or competitors. This is of particular significance to India and other developing countries.

Aspects of the cultural web	Some useful questions
Stories and myths	<ol style="list-style-type: none"> 1. What core beliefs do the stories reflect? 2. How strongly held are these beliefs with power holders? 3. How pervasive are the beliefs (through the levels)? 4. How do beliefs relate to strengths and weaknesses? 5. How are the heroes? 6. Do the heroes conform to, or challenge the beliefs?
Rituals and symbols	<ol style="list-style-type: none"> 1. What behaviour is expected and rewarded (e.g. risk taking)? 2. What language is used to describe the organization and its activities? 3. What is the dominant attitude towards each stakeholder group?
Leadership and management style	<ol style="list-style-type: none"> 1. What are the core beliefs of the leadership? 2. Which aspects are stressed in public (e.g. annual reports)? 3. How do they regard structures (e.g. centralists or devolutionists)? 4. What type of strategy is favoured (e.g. defensive or speculative)? 5. What attributes are sought in new recruits?
Structure and systems	<ol style="list-style-type: none"> 1. Do structures/systems encourage collaboration or competition? 2. Which aspects of strategy are most closely monitored and controlled? 3. What kind of training is given?

Exhibit 12.7: Analysing the Impact of the Cultural Web on Strategy: A Checklist

Miles and snow categorize organizations into three basic types in terms of how they behave strategically, namely (i) defenders, (ii) prospectors, and (iii) analysers. Their characteristics of policy-making are summarized in Exhibit 12.8. When undertaking strategic analysis, grouping provides a means of assessing the dominant culture of the organization. By reviewing the type of systems and the historical choices of strategies, the analyst can distinguish between a defender and a prospector organization, and hence judge the extent to which new strategies might fit the current core beliefs of the organization (the recipes). In the context of the current discussion on leadership, the central dilemma for organizations should now be clear. A cohesive culture also demands,

Organization type	Dominant objectives	Preferred strategies	Planning and control systems
Defenders	Desire for a secure and stable niche in market	Specialization: cost-efficient production, marketing emphasis on price and service to defend current business; tendency towards vertical integration.	Centralized, detailed control Emphasis on cost efficiency Extensive use of formal planning.
Prospectors	Location and exploitation of new product and market opportunities	Growth through product and market development (often in spurts). Constant monitoring of environmental change. Multiple technologies.	Emphasis on flexibility, decentralized control, use of ad hoc measurements.
Analysers	Desire to match new ventures to present shape of business	Steady growth through market penetration. Exploitation of applied research Followers in the market.	Very complicated coordinating roles between functions (e.g. product managers) Intensive planning.

Exhibit 12.8: Different Types of Organization Cultures and their Influence on Policy Making

and often produces, 'cloning' within the organization, with more and more like minded individuals being selected for key leadership roles or becoming 'socialized' into the organization's dominant beliefs and approaches. There are, however, dangers of blindly following this 'recipe'.

Strategy Formulation as a Cultural Process

In the context of the role of the cultural web, it is perhaps useful and necessary to discuss strategy formulation as a cultural process in some detail. It is too simplistic to think of strategy as a response to the environment, for it is evident that faced with similar environments, organizations will respond differently. This response is likely to be influenced by the past experience of managers and by the wider social and political processes in the organization. It is this social and cultural process that needs to be clearly understood and appreciated. By 'organizational culture' we mean the deeper level of basic assumptions and beliefs that are shared by members of an organization, that operate unconsciously and define in a basic taken for granted way an organization's view of itself and its environment. Often it manifests itself through organizational 'symbols', such as logos, organization charts, status symbols, policies, rewards and incentive, and the like-in short 'the way we do things here'.

The Recipe and The Cultural Web

The set of beliefs and assumptions which forms part of the culture of an organization has variously been called interpretative schemes, paradigms, and recipes. Here use the name 'recipe'. The recipe is a set of beliefs and assumptions held relatively commonly throughout the organization that is taken for granted within that organization but is discernible to the external observer. The recipe makes sense of the situation in which managers find themselves and provides a basis for formulation of strategy. This process is sketched in Exhibit 12.9.

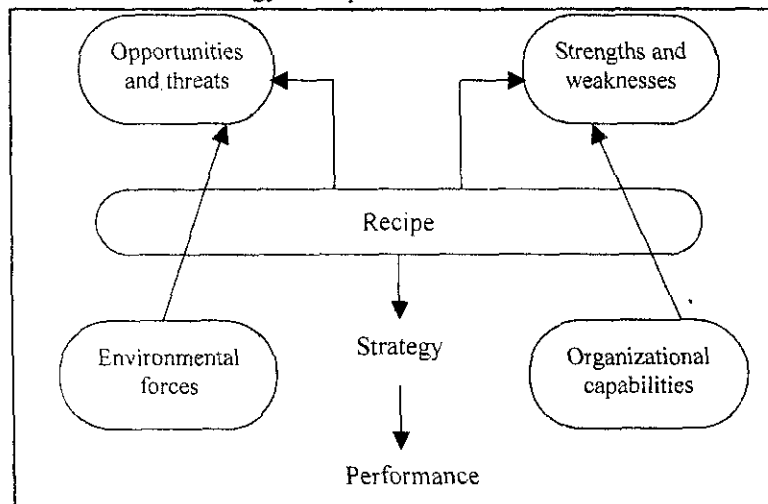


Exhibit 12.9: The Role of the Recipe in Strategy Formulation

The relationship and distinction between the recipe and organizational strategy need to be clarified. Environmental forces and organizational capabilities do not in themselves create organizational strategy: it is people who create strategy. The mechanism by which this is done is the recipe. The forces at work in the environment, and the organization's capabilities in coping with these, are made sense of through the assumptions and beliefs called the recipe and on the basis of this strategy is formulated. The strategies that managers advocate and those that emerge through the social and political processes are then typically configured within the bounds of this recipe. However, environmental forces and organizational capabilities, whilst having this direct influence on strategy formulations, nevertheless do impact much more directly on organizational performance. It is, however, necessary to distinguish between actual influence and managerial perception of influence on the organization. Lack of attention to this difference can give rise to significant problems.

The recipe may, thus be a very conservative influence on strategy, and particularly since the links between the recipe itself and the way things are done in the organization are likely to be close. This is illustrated Exhibit. 12.10.

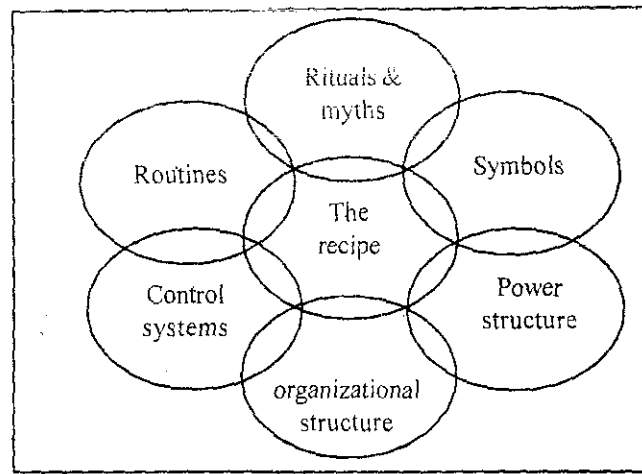


Exhibit 12.10: The Cultural Web of an Organization

Thus, for example, the links between the power structure in the organization and the core set of beliefs held by managers in that organisation are likely to be strong. The recipe represents the 'formula for success' which is taken for granted in the business and likely to have grown up over years; the most powerful groupings within the business are likely to have derived their very power from association with this set of beliefs and their ability to put them into operation. One implication of this is that it is likely that a purely analytical questioning of the recipe will not only be taken as evidence of the analyst's lack of understanding of the problems of the business but may actually be perceived as a political threat, rather than objective analysis, for it will very likely be perceived as an attack on those most associated with such core beliefs. Even if managers 'intellectually' accept such analysis, they may be more influenced by the recipe and its cultural underpinnings in formulating, persisting with, and adjusting strategy. The recipe is also likely to be associated with control systems, routines, and rituals of the organization that will tend to preserve the status quo. The point is that the recipe is not just a set of beliefs and assumptions; rather it is embedded in a organization-specific cultural web that legitimizes and preserves the assumptions and beliefs in the organization. Such a cultural web for an imaginary company is shown in Exhibit 12.11.

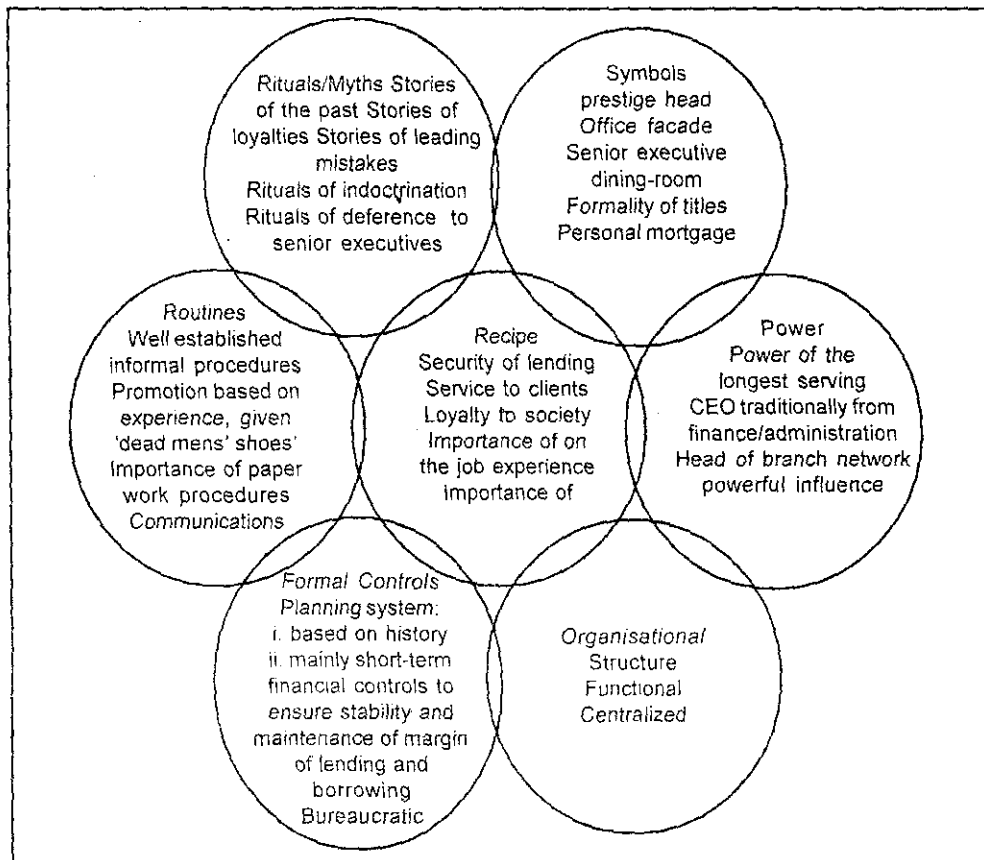


Exhibit 12.11: The Cultural Web: An Illustrative Example

A Cultural View of Patterns of Strategic Change

Faced with pressures for change, consequent upon buffeting through environmental changes, managers will be likely to deal with the situation in ways that protect the recipe from challenge. This raises difficulties when managing strategic change, particularly when the action required falls outside the ambit of the current recipe and the constraints of the cultural web: that is managers would have to change their core beliefs substantially.

When necessary, such drastic changes may be desirable, but do not occur easily. Managers are more likely to attempt to deal with the situation by searching for what they understand and deal with in terms of the existing recipe. Faced with stimulus for action, say declining performance, managers first seek for means of improving the implementation of existing strategy. This could be through a tightening of controls. If this is not effective, then a change of strategy may occur, but still a change which is in line with the existing recipe. Thus, for instance, managers may seek to extend the market for their product but retain the same views about the range of products, the principal virtues of the product, the nature of what remain as their main markets, and how they should go about operating in these markets. There is still no change in recipe and such changes are unlikely until this attempt at reconstructing the strategy keeping the recipe intact also fails. A change of recipe is usually a last resort and perhaps is automatically accompanied by changes in strategy and methods of control.

This is but an alternative picture of incrementalism and an almost certain consequence is the strategic drift occurring where strategy lags environmental change to lesser or greater degree. Under usual conditions of evolutionary strategic change, this drift may not be disastrous and can usually be made up. In cases of environmental discontinuity, however, as has been already discussed and we appear to be currently facing such drift may be akin to disaster and incrementalism is simply inadequate. This chapter argues that managers would have to accept the need for urgent change in recipe if necessary, entailing a tremendous cultural shift. This is perhaps the greatest challenge facing management today. Exhibit 12.12 illustrates the dynamics of recipe change discussed earlier.

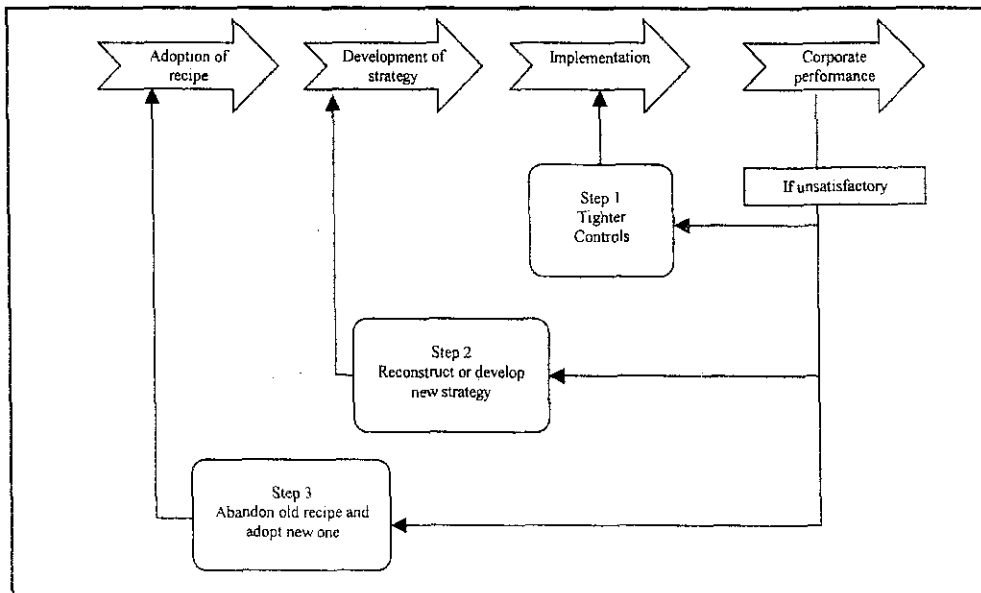


Exhibit 12.12: Dynamics of Recipe Change

Strategists should strive to preserve, emphasize, and build upon aspects of an existing culture that support proposed new strategies. Aspects of an existing culture that are antagonistic to a proposed strategy should be identified and changed when implementing new strategies. Substantial research indicates that new strategies are often market driven and dictated by competitive forces. For this reason, changing a firm's culture to fit a new strategy is usually

more effective than changing a strategy to fit an existing culture. Numerous techniques are available to alter an organization's culture, including recruitment, training, transfer, promotion, restructure of an organization's design, role modeling, and positive reinforcement.

In a recent article, Jack Duncan described "triangulation" as an effective, multimethod technique for studying and altering a firm's culture. Triangulation includes the combined use of obtrusive observation, self-administered questionnaires, and personal interviews to determine the nature of a firm's culture. The process of triangulation reveals needed changes in a firm's culture that could benefit strategy. Schwartz and Davis suggest four specific guidelines for changing an existing culture to effectively match a new strategy:

1. Identify the relevant culture and subcultures in the organization through individual and small-group meetings. Develop a list of simply stated beliefs about "the way it is" in the organization and of current imperatives for how to behave. Review these until there is a consensus about the central norms in the culture.
2. Organise these statement about the firm's culture in terms of managers tasks and key relationships.
3. Assess the risk that the organisation's culture presents to the realization of the planned strategic effort. This is done by first determining the importance of the culture products and then determining their compatibility with the intended strategy.
4. identify and focus on those specific aspects of the organization's culture that are highly important to successful strategy fomulation, implementation, and evaluation. It may then be possible to develop alternative organizational approaches that better fit the existing culture, as well as to design planned programs to change those aspects of culture that are the source of the problem.

Schein indicates that the following elements are most useful in linking culture to stategy:

1. Formal statements of organizational philosophy, charters, creeds, materials used for recruitment and selection, and socialization.
2. Designing of physical spaces, facades, buildings.
3. Deliberate role modeling, teaching, and coaching by leaders.
4. Explicit reward and status system, promotion criteria.
5. Stories, legends, myths, and parables about key people and events.
6. What leaders pay attention to, measure, and control.
7. Leader reactions to critical incidents and organizational crises.
8. How the organization is designed and structured.
9. organizational systems and procedures.
10. Criteria used for recruitment, selection, promotion, leveling off, retirement, and "ex-communication" of people.

In the personal and religious side of life, the impact of loss and change is easy to see. Memories of loss and change often haunt individuals and organizations for years. Ibsen says, "Rob the average man of his life illusion and you rob him of his happiness at the same stroke." When attachments to a culture are severed in an organization's attempt to change direction, employees and managers often experience deep feelings of grief. This phenomena commonly occurs when environmental conditions dictate the need for a new strategy. Managers and employees often struggle to find meaning in a situation that changed many years past. Some people find comfort in memories; others find solace in the present. Weak linkages between strategic management and organizational culture can jeopardize performance and success. Deal and Kennedy emphasize that making strategic changes in an organization always threatens a culture:

...people form strong attachments to heroes, legends, the rituals of daily life, the hoopla of extravaganza and ceremonies, and all the symbols of the workplace. Change strips relationships and leaves employees confused, insecure, and often angry. Unless something can be done to provide support for transitions from old to new, the force of a culture can neutralize and emasculate strategy changes.

Any strategic plan must be consistent with the organization's culture. A strategic plan for a bank had been prepared by a group of external consultants. Although the plan was excellent, its probability of success was low. It would have required the bank's officers to become aggressive and engage in cut-throat practices with the bank's competitors, something the officers were neither able nor willing to do.

Corporate Politics and use of Power

All corporate cultures include a political component and, therefore, all organisations are political in nature. Strategists should understand the organisations are a microcosm of the society in which they exist. Organisational members bring with them their likes and dislikes, views and opinions, prejudices and inclinations when they enter organisations. Managerial behaviour cannot be purely rational and, therefore, an understanding is to be acquired of how politics work and the use of power is to be made.

Power is defined as "the ability to influence others" and corporate politics is "the carrying out of activities not prescribed by policies for the purpose of influencing the distribution of advantages within the organisation". Politics is related to the use of power but it is not similar to it. Usually, we tend to view politics and power negatively as means for domination, manipulation, and subjugation. But these can be viewed in a positive way also. In this sense, politics and power may be thought of as a means for the achievement of organisational objectives.

Henry Mintzberg is of also of the view that corporate politics is neither inherently good nor bad. Though most of the time corporate politics lead to divisiveness that is not good for an organisation, yet there are times when it needs to be shaken up in order to bring about changes. These are occasions when the organisation is emerging from a phase of stability and entering into a period requiring some fundamental changes. Strategy implementation is basically about change management. Therefore, corporate politics has a definite role to play in strategy implementation. Recommending the need for creating political tension and apolitical harmony. Mintzberg says that "The organizations must ... pull apart before it can pull together again". It can be said that strategists need to know when to use politics and power to get things done and when to shun politics and encourage harmony.

Power within an organisation is derived from five types of sources:

1. Reward power arise from the ability of managers to reward positive outcomes.
2. Coercive power arises from the ability of managers to penalise negative outcomes
3. Legitimate power arises from the ability of managers to use position to influence behaviour
4. Referent power arise from the ability of managers to create a liking among subordinates due to charisma or personality
5. Expert power arises from the manager's competence, knowledge, and expertise that is acknowledged by others

Strategists use one or more of these power base to influence the behaviour of organisational members.

Power is the potential ability to influence behaviour and change the course of events by overcoming resistance and convincing people to do things they would not otherwise do. Power and influence are subjects often approached critically with disdain and apprehension. It is considered more socially correct to be critical of power than to speak of

how to get more of it and use it to your advantage. And yet power is essential to change, progress, and improvement. As Warren Bennis and Burt Nanus, noted authorities on the subject of leadership, have explained, "Power is at once the most necessary and the most distrusted element exigent to human progress."

The application of too much power is to be reviled, but the absence of power is to be lamented. While power has been and continues to be abused. It is hard to imagine that the best response to this problem is to do away with it. We may be uncomfortable with the idea of using power to achieve our own ends, but we must also be dismayed when crises arise because of its absence. Jeffrey Pfeffer, author of *Managing with Power*, contends that "one of the major problems facing organizations today is not that too many people exercise too much power, but rather the opposite: too few people exercise enough power." Bennis and Nanus reach a similar conclusion: "These days, power is conspicuous by its absence.... There is something missing POWER, the basic energy to initiate and sustain action translating intentions into reality, the quality without which leaders cannot lead."

As these quotes suggest, power is an essential part of implementation. If an organization is to see its strategies implemented, it must rely on leaders who understand the sources and uses of power and act accordingly. The primary reason that power carries so many negative connotations is that it is usually defined too narrowly. Power carries so many negative connotations is that it is usually defined too narrowly. Power and influence can take many forms, and, to be effective in using them, you need to move beyond overly simplistic negative stereotypes. We can classify the alternate forms power takes by considering its sources and its uses, as shown in Exhibit 12.13, both the institution and the individual have been identified as sources of power. Institutional power is based on formal authority granted by the organization that allows one to govern the actions of others. The amount of institutional power is typically a function of one's position in an organization: the higher one's position, the greater the power granted by the institution. This relationship between hierarchical level and this type of power explains why we often speak of someone's having "power over" something or someone.

but there are many influential people whose power does not come from their institutional positions. A classic example is the computer "whiz kid" who holds greater power than organizational ranking would suggest because he or she is the only one who really understands how the company's computers work. This is a form of influence known as expert power. Or there may be someone to whom others regularly defer out of respect and admiration, even though this person is not in a formal position to exercise such influence, an example of referent power:

In example such as these, the source of the power is not the institution but the individual. Power that stems from within an individual is usually formed over time as a result of many actions and through various interactions with others. Power that comes from within an individual rather than from an institution is considered more appropriately as "power through," rather than "power over." The types of power derived through negotiation, political maneuvering, and communication stem from what an individual does personally rather than what an institution grants.

Again referring to Exhibit 12.13, we see that, regardless of its source, power can be used in a fashion that ranges from the explicit (overt or blatant) to the implicit (unobtrusive or subtle). When a supervisor gives workers an order, this is an explicit use of the power; those being influenced are aware of it. But not all uses of power are nearly so obvious. When a leader consistently identifies goals in the same order, an implicit message is being sent that the first goal is the highest priority. Over time, this will influence the thoughts and actions of others without the leader's ever having explicitly stated that the first goals should be given priority. By combining the two sources and the two uses of power we are able to identify four types of power or influence: *commanding, shaping, persuading, and inducing.*

		Use of Power	
		Explicit	Implicit
Source of Power	Institution	Power and influence through COMMANDING manifests itself through: Orders Given Structures Changed System Changed	Power and influence through SHAPING manifests itself through: Culture Change "Rewired" Networks Modified Agendas
	Individual	Power and influence through PERSUADING manifests itself through: Expertise Negotiation Communication	Power and influence through INDUCING manifests itself through: Charisma Politics Role Modeling

Exhibit 12.13: Sources and Uses of Power and Influence

Commanding

Much of what people find most unattractive about power is found in the north west corner of Exhibit 12.13, where influence comes in the form of commands. Here, power derive from institutional sources is used explicitly: based on formal authority a manager gives orders and uses rewards or punishments to enforce them. We call this combination of source and use of power commanding. This type of power is readily abused; when abused, it manifest itself in ways that range from petty favoritism to fascism. Naturally, such misuse of power is disliked and discouraged. However, it would be a gross overstatement to say that explicit use of institutionally derived power is always bad. There are may circumstances in which such power is very appropriate the classic example being military action. Military operations depend on a command and control form of power in which the source of authority is specified by the institution and the use of authority is often necessarily explicit.

But the use of commands is not limited to military applications. The command-and-control approach to implementing a plan of action is neither inherently right nor inherently wrong for business organizations. Its use depends on the situation at hand. In the simple and/or stable situations in which strategic programming is feasible, a command-and-control approach to implementation may be not only reasonable but desirable. In such a situation, institutionally derived power used in an overt manner may be very effective in keeping an organization on track and moving.

However, as we have also discussed, the number of organizations that are able to rely exclusively on strategic programming is shrinking. This suggests that, for most leaders to be as effective as possible, they will need to use forms of influence well beyond formal authority.

Those who are higher in an organization can have a much greater impact on the organization's structure (both macro and micro), as well as its resourcing and control systems. Controlling these organizational elements is not as blatant as issuing commands, but it can have an even greater impact. Commands usually apply to a fairly small subset of the organization, while altering the context and systems of an organization may have a much farther-reaching effect. By using institutionally granted authority to alter these elements of the organisation, managers can escert tremendous amount of power to help bring about desirable changes. Though less obtrusive than commands, changes in the formal

elements of organization structure and systems are still fairly explicit and obvious uses of institutionally derived power.

Research has shown that these explicit uses of institutionally granted power are often less effective than other approaches that are less heavy-handed and more implicit. For instance, one study found that of seven forms of power surveyed, coercive power (the one close to our "commanding" category) was the least effective. Research findings such as these suggest that most managers need to take actions that entail the use of power in other ways. We advocate that managers develop and employ all the different combinations of sources and uses of power. Moving away from the northwest corner and drawing on other forms of power from throughout this exhibit is what we call using a "full-portfolio" approach to power. By developing a full portfolio, one can become less reliant on commanding and other uses of obtrusive formal authority. You should recognize that we are not decrying the use of power altogether. While we stress the need for decreased reliance on commanding, at the same time we stress the increased use of other forms of power. For example, we will argue that one of the most effective uses of institutional power is "shaping" instead of commanding.

Shaping

An organization's networks and culture are the elements of its context that provide the backdrop against which everyday behavior plays out. We are often unaware of precisely how these elements of context affect us, although when we do stop and think about it, most of us will agree that their impact is immense. This being the case, there is an opportunity for leaders who can shape networks and culture to have a more important, if less obvious, impact on their organizations than they might have by relying on their formal authority. For example, research has shown that in today's flatter organizations networks are emerging as particularly important sources of power. One study concluded that one of the most important differences between influential managers and less successful manager was their connection to and use of a network of resource persons—a balanced web of relationships with superiors, subordinates, peers, and other key players. Another concluded that "the ability of managers to get things done depends more the numbers of networks in which they're centrally involved than on their height in a hierarchy."

Beyond shaping elements of the organization's networks and cultures, those granted power by the institution can use it to shape agendas, both literally and figuratively. Though this use of power is not often discussed, we find it to be among the strongest uses of formal authority. For example, we know of several cases in which CEOs have used their position in an organization's hierarchy to shape the entire organization's agenda. In one such case, the COE, having become convinced the organization needed to become more involved in international competition, made it a practice of putting any issues dealing with international affairs at the top of the agenda for all his weekly meetings with the VPs. This ensured that adequate time was available to discuss them, but often there was no time left to discuss other items the CEO considered less important. Thus, over several months, the organization made progress on international issues while other concerns were left on the back burner.

This was a case of shaping a literal agenda, but there are many examples of leader's figuratively shaping their organizations agendas by moving certain topics to the forefront of people's minds and keeping them there. Consider the CEO of one hospital who explained that his most important job was to "get the concept of competition on the radar screens of everyone in [the] organization." While hospitals once themselves genteel organizations with more important things to worry about than competition, changes in the industry have now brought hospitals into competition only with one another but with doctors and insurance companies as well. Unless this CEO could get this concept internalized by people throughout his organization there was little hope the hospital would prosper in the new environment. Therefore, he used his position to frame issues in terms of competition, to ask questions that required those around him in the organization to think about competition, and to establish competition as a frequent topic of conversation and thought throughout the organization.

Without formal authority from the institution, the CEO would not have been nearly as successful as he was in bringing about the change. But while he used formal authority, he used this power in a manner that was less obtrusive than issuing orders. In fact, to those caught up in the day-to-day operation of the hospital, it was not always clear why competition kept coming up as a topic of discussion, and many of them saw their insights into competition and its importance as being something they had discovered on their own as a result of personal initiative. Lao Tsu, the sixth century B.C. Chinese philosopher, made a similar point when he wrote:

The wicked leader is he who people despise.

The good leader is he who the people revere.

The great leader is he who the people say, "We did it ourselves."

This proverb recognizes unobtrusive forms of power as more effective than command-and-control tactics. For instance, we are convinced that if the hospital CEO in our example had simply issued a decree insisting that people change their attitudes to think more competitively, he would have failed miserably. There is much merit in attempting to supplement explicit forms of institutional power with subtle efforts to influence others in less obtrusive ways.

Persuading and Inducing

So far, we have been focusing on the upper half of Exhibit 12.13, which may have given you the mistaken impression that power depends on organizational position and other sources of institutional authority, while it is an undeniable fact of life that "rank has its privileges," not all forms of power are derived from institutional sources. In fact, researchers have found that personal power (found in the lower half of Exhibit 12.13) is generally more effective than position power (the upper half of the exhibit).

In the lower half of the exhibit, you can see other forms of power that stem from within the individual. These forms of power are available to individual at all levels of the organization, regardless of their rank or formal authority. When used explicitly, individual power tends to manifest itself through acts of expertise, negotiation, and communication. When used in a less overt manner, individual power is seen through acts of charisma, politics, and providing a role model that others aspire to follow.

Politics is concerned with the use of power and relates to managing coalitions, consensus-building, and the creation of commitment to organisational purpose and mission. The nature of organisation itself creates the conditions for corporate politics to manifest itself. Through the creation of an organisation structure, not only are the hierarchy, position, and relationships created, but structure leads ultimately to conflicts, coalitions, drives, and ambitions among the people who constitute an organisation. Most managers are aware that the higher they move, the pyramid of the organisational structure narrows down progressively, there are fewer top position available as one moves higher. This causes jockeying for power resulting an political play. Since material rewards, promotions, prestige and ego are involved, each organisation, more or less, is affected by corporate politics. For every one manager that consider corporate politics and the use of power as bad, there could be another manager who feels that it is good. So, despite some well-meaning managers shunning it, politics remains a part of the organisation. Political considerations and use of power, therefore, are a part of behavioural implementation by strategists.

Politics and power affect the way a strategy is formulated and implemented. "A manager cannot effectively formulate and implement strategy without being perceptive about company politics and being adept at political maneuvering." The different elements in the hierarchy of objectives, i.e. logic intent, vision, mission, and objectives are affected by the formation of groups and coalitions which influence the direction that the organisation has to take. Political considerations affect which type of objectives take precedence over others and what strategy the firm has to choose.

Generally there is even more politics in implementing strategy than in formulating it. In implementation, politics and power affect a number of elements. The nature of strategy implementation requires consensus-building, managing coalitions, and creating commitments. It also requires conflict resolution and balancing of interests. To take a few examples: resource allocation is ultimately a rational-political decision which results in the distribution of authority and responsibility and decides how power will be exercised, and corporate culture is itself the outcome of the use of politics and power.

Experience has repeatedly shown that by having an understanding of the use of politics and power, strategists can perform the tasks of strategic management better. "Indeed, having astute political skills is a definite, and even a necessary, asset for a general manager (or strategist) to have in orchestrating the whole strategic process".

A strategic use of politics and power becomes even more critical where strategy changes are to be made. In reality, most strategic decisions and most strategic thrusts in large enterprises emerge as part of an evolving continuous political consensus building with no precise beginning or end."

Therefore, it is imperative to make strategy changes with a judicious use of politics and power.

The typical approaches to a strategic use of politics and power may involve one or more of these actions:

- First of all, to accept the inevitability of politics being there in the organisation
- To understand how an organisation's power structure works, who wields real power and influence, and who are the individuals and groups whose opinions carry weight and cannot be disregarded
- To be sensitive and alert to political signals emanating from different parts of the organisation
- To know when to treat softly and real on coalition management and consensus building, and when to push through decisions and actions by a selective and judicious use of "Machiavellian" methods
- To lead strategy and not to dictate it, being patient till a consensus emerges
- To let most negative decisions emerge as a group consensus rather than as a directive from the top
- To gather support for acceptable proposals and to let the unacceptable ideas die a natural death
- To reward organisational commitment and penalise negative or indifferent attitudes
- To practice principled politics and use openness and honesty to counter unprincipled politics

In the Indian context, the presence of politics and use of power and, perhaps, more visible than in other cultures. This may be due to the pervasive enviousness exhibited in Indian organisations. Managers have not only to deal with and be affected by intracorporate politics, but also intercorporate politics, between rival companies. At a higher level, Indian industry is plagued with politics between associations and federations of business, public versus private sector, small versus large sector, multinational versus local firms, and technocrats versus bureaucrats. In such a milieu, strategists have to be aware of not only internal political considerations but also the politics and power play present in other organisations, particularly government departments and ministries, with whom they have to deal.

Talking about corporate politics and use of power, we have been walking a tightrope between moral and amoral uses of politics and power. It is easy for strategists to often forget the distinction between use of politics and power for the benefit of self, organisation, or the society. What blurs the distinction is a lack of personal values and a sense of business ethics.

More than 30 years ago, esteemed political scientist Norton Long wrote, "People readily admit that governments are organizations. The converse—that organizations are governments—is equally true but rarely considered." Like it or not, organizations have many of the same characteristics as governments do, chief among these being politics. As Jeffrey

offer puts it. Organizations, particularly large ones, are like governments in that they are fundamentally political entities. To understand them, one needs to understand organizational politics, just as to understand governments, one needs to understand government politics. Experienced managers agree with these theorists, but they are not necessarily happy about it, as shown by the reported in Exhibit. 12.14.

Organizations are political entities:	Agree
The existence of workplace politics is common to most organizations.	93%
The higher you go in organizations, the more political the climate becomes.	76%
Politics are important to individual success.	72%
Successful executives must be good politicians.	89%
Powerful executives don't act politically.	15%
You have to be political to get ahead in organizations.	69%
People are divided regarding the desirability of organizational politics:	
Organizations free of politics are happier than those where there are a lot of politics.	59%
Politics in organizations are detrimental to efficiency.	56%
Politics help organization function effectively.	42%
Top management should try to get rid of politics within the organization.	48%

Exhibit 12.14: Experienced Managers Have Mixed Opinions on Organisational Politics

These data show that experienced managers recognize organizations as power entities and that successful or powerful executives must behave politically. However about half the respondents believe politics are detrimental to organizational efficiency and a happy organizational life and think management should try to rid organization of their politics. While we may empathize with this desire, it is not realistic. For thing, while half the people may want to be rid of politics, half do not. As long there is such a large number of managers who "believe in" politics, organizations be political entities. But beyond such simplistic arguments, there are more common force at work that sustain politics in organizations. Note that 42 percent of managers surveyed believe that politics help organizations function effectively-as many as those who believe that politics are detrimental. Who is right? both.

Henry Mintzberg, whose theories of management we have drawn from here throughout this text, also agrees that politics are neither inherently good nor bad sees a definite place for politics in bringing about needed organizational change argues that, most of the time, organizations benefit from avoiding the divisive that politics foster. However, he also argues that this is not always the case and sometimes an organization needs to be shaken up by its politics in order to about needed changes. He writes, "Most of the time, the cooperative pulling together... is to be preferred, so that the organization can pursue its established strategy perspective. But, occasionally, when fundamental change becomes necessary, the organization has to be able to pull apart through the competitive force of politics. The librium, "when an organization hopes to adhere to what Mintzberg calls "its established strategic perspective," the absence of politics is beneficial, as it fosters the cooperation and efficiency that facilitate the incremental changes that are dominant during these periods. That is why Mintzberg writes, "Politics often impedes necessary [incremental] changes and wastes valuable resources." However, the paradigm shifts that form the "punctuation" part of the model are so difficult to bring about that only powerful political forces may be strong enough to cause a break with past thinking and allow a new order to emerge. In describing the disruptive nature of such paradigm shifts, Mintzberg concludes that "political challenge may also be the only means to promote really fundamental change." Summarizing the alternating need for political tension and apolitical harmony, he concludes, "The organization must, in other words, pull apart before it can pull together again."

This suggests that managers need to be very sophisticated in their use of politics, knowing not only how to use politics to get things done but when to downplay politics and encourage harmony. With the need for such political sophistication

in mind, we offer the following advice to those who seek to harness political forces.

- *Admit that politics are inevitable.* Politics exist whenever different groups have different ideas that they want to see implemented and the individuals in the groups work to see their shared ideas moved forward. Can you imagine an organization in which this did not happen? In which no one shared ideas about what should happen and/or no one was willing to work to see their ideas advanced? Surely such a lethargic organization would not long survive. Most of the organizations we know are filled with politics but carefully controlling how you engage in politics and how they are allowed to affect your organization.
- *Resolve to practice principled politics.* What many people find most abhorrent and politics is their being used for personal gain. Recall from Exhibit 4.29 that 70 percent of the respondents agreed the “you have to be political to get ahead organizations.” While it is true that political behavior is often directed at furthering one’s personal advantage, this is not politics’ only role. As we discuss above, politics can be a constructive force for bringing about desirable organizational change. The concept of “principled politics” is premised on the notion that the primary role of politics should be strengthening the organization, not the politician.
- *Recognize that, when you want to get something done, it will be considered both politically and objectively.* Since politics are inevitable, plan for them. Recognize that, as you advance your ideas, they will meet with resistance from others who have different ideas they are trying to advance. Some of the resistance your ideas meet will be based on concern about their merits as assessed from an objective standpoint. Other resistance will be more political in nature. Either form of insistance can stop your progress, and it is myopic to focus exclusively on one or the other.
- *Be clear up front about what you will and won’t do.* The politically heated moment in which your adrenaline is following and events are unfolding rapidly is not the place or time to wonder whether you will regret a particular course of action later on. Think things over beforehand, and come to some clear personal guide lines about how you will behave under a broad set of varying scenarios. Use the forethought to keep yourself in check and avoid doing anything under presume that you would normally not do.
- *Use openness and honesty to undermine unprincipled politics.* Unprincipled politics are a mold that cannot stand the light of public scrutiny. Let others know what you will and won’t do. Openly talk about your motives and why you want to advance the ideas you are pushing. Ask others not to share opinions about others with you unless they are comfortable with those statements being repeated publicly. When you disagree with others, be willing to share your reasons for disagreeing. Deal with people face-to-face, and whenever possible, avoid the kind of behind-the-scenes, “smoke-filled-rooms” politics that can be so carrying and destructive.

Personal Values and Busines Ethics

Only personal values and a sense of business ethics can help a strategist to distinguish between moral and amoral use of politics and power as a means to attain organisatioñal goals. We attempt to answer these questions: what are personal values and business ethics? Why and how are they important? and what is the relation of values and ethics to strategy?

Personal values refer to a conception of what an individual or groups regards as desirable. A value is a view of life and a judgement of what is desirable which is very much a part of a person’s personality and a group’s morale. Thus, a benign attitue to labour welfare is a value which may prompt an industrialist to do much more for wokers than the labour laws stipulate. Service-mindedness is a value, which when cherished in an organisation, manifests in better customer satisfaction. Personal values are imbibed from parents, teachers, and elders, and as an individual grows, values are adapted and refined in the light of new knowledge and experiences. Within organisations, values are imparted by the founder-entrepreneur or a dominant chief executive, and these remain in some form a long time after

that person is not there. J. R. D Tata, the previous chairman of the Tata group, when asked to define the House of Tata and what links the different Tata companies together said: "I would call it a group of individually-managed companies united by two factors. First, a feeling that they are part of a larger group which carries the name and prestige of Tatas, and public recognition of honesty, reliability and trustworthiness. The other reason is more metaphysical. There is an innate loyalty, a sharing of certain beliefs. We all feel a certain pride that we are somewhat different from others". The several values that J R D Tata refers to have been derived from the ideals of J N Tata, the founder of the Tata group.

In the discipline of management studies business ethics is "the study of how personal moral norms apply to activities and goals of a commercial enterprise. It is not a separate moral standard, but the study of how the business context poses its own unique problems for the moral person who acts as the agent of this system". Practically, business ethics operates as a system of values and "is concerned primarily with the relationship of business goals and techniques to specifically human ends." 'Specifically human ends' means viewing the needs and aspirations of individuals not merely as individuals but as a part of society. It also means realization of the personal dignity of human beings.

A major task of leadership is to inculcate personal values and impart a sense of business ethics to the organisational members. At one end, values and ethics shape the corporate culture and dictate the way how politics and power will be used and, at the other end, clarify the social responsibility of the organisation.

The twin issues of personal values and business ethics have come to occupy centre stage in management. There is an increasing awareness around the world about ethical practices in business. International organisations such as the World Bank and IMF are concerned about whether the aid provided by them is used for the intended purposes and not frittered away by corrupt government officials. 'Transparency International' brings out an annual rating of countries on an index of corruption that serves as a guideline for foreign investors and international donor agencies.

Within India, there are significant social, cultural, political, technological, and economic factors affecting the state of personal values and business ethics within industry. Corporate governance has attracted worldwide attention as a means to induce ethical behaviour in business.

A typical dilemma faced by strategists is to somehow reconcile the pragmatic demands of work (which often degenerate to a distortion of values and unethical business practices to the call of the 'inner voice' which somehow prevents them from using unethical means for achieving organisational goals. This dilemma stems from the fact that apparently the value system of the organisation has already been contaminated beyond redemption. Some analysts attribute this to the acceptable transition of a developing society where social mechanisms have become obsolete.

Corruption in industry, which is a major by-product of the degradation of value and ethics, is also related to the inability of industry to stand up to the discretionary powers of a regulatory system designed and administered by an unholy alliance of bureaucrats and politicians. But repeated observations have shown that excellent organisations that have an explicit belief in, and recognition of, besides other values-the importance of economic growth and profits, are driven by values rather than avarice. It has been possible for Indian companies such as Asian Paints, Bajaj Auto, ICICI, Infosys, and Amul to excel on the basis of superordinate goals-a set of values and aspirations and corporate culture. Strategists, therefore, have to provide the right values and ethical sense to the organisations they manage. Exhibit 12.15 provides material on which to determine the 'rightness' of values and ethics based on Indian psycho-philosophical thought.

Personal values and ethics are important for all human beings. They are specially important for strategists as they are custodian of immense economic power vested in business organisations by society. The possession of personal values by strategists is good, but the important issue is whether it is right to let them affect the considerations for strategy formulation and implementation. Rather a more relevant question could be: Can strategists prevent their personal values from affecting strategy formulation and implementation? To seek answer, witness what Christensen and

others say: "Executives in charge of company destinies do not look exclusively to what a company might do or can do. In apparent disregard of the second of these considerations, they sometimes seem heavily influenced by what they personally want to do." If we now look at the last proposition in Exhibit 12.15, we find that it is indeed true. The intentions of individuals, that is, their 'purity of mind' as decision-makers within an organisation matter a lot in strategic management. There has to be a right connection between values, ethics, and

Prof S K Chakraborty of IIM, Calcutta has done extensive pioneering work on Indian psycho-philosophical thought, contained in ancient texts, to derive insights for the purpose of developing managerial effectiveness. His basic idea is to rely on education versus training, values versus skills, principles versus policies, and wisdom versus knowledge to develop managerial effectiveness. His model of managerial effectiveness is based on seven Indian thoughts: the concept of self and reality, disidentification, theory of Gunas, theory of Samskaras, the doctrine of Karma, theory and method of work, and a 'giving' model of motivation.

With regard to values and ethics rooted in Indian thought, several ideas have been proposed:

1. The concept of self in man has to embrace the spiritual dimension beyond the physical, social and economic dimensions.
2. The creative energies of human beings are derived from, and rooted in, the Supreme Creative Intelligence.
3. Managerial decision-making requires the interplay of both analytic and holistic faculties.
4. The final resolution of managerial conflicts lies in the de-egoisation of the self.
5. The key to cooperation and teamwork lies in realising that the same 'atman' dwells in all.
6. The quality of managerial decision-making and skills can be improved through an understanding and internalisation of the doctrine of karma.
7. Motivational strategies need to be based on a 'giving' model rather than a 'needing' model of man.
8. Ability for developing effective leadership style requires an understanding of three qualities of man: sattwa (righteousness), rajas (selfishness), and tamas (laziness).
9. All managerial decisions are subjective in the ultimate analysis and the effectiveness of such decisions depends critically on the purity of the mind of the decision-maker.

Exhibit 12.15: Values and Ethics in the Context of Indian Psycho-Philosophical Thought

strategy. It is imperative that strategists take strategic decisions not only on the basis of purely economic reasons but also consider values and ethics.

Business ethics has traditionally been considered to integrate core values, such as, honesty, trust, respect, and fairness into strategic management, policy-making, practising management, and decision-making. It has been perceived as a set of legally driven codes, in the form of a list of do's and don'ts for the company executives, that have to be complied with. A significant change is occurring in considering business ethics as central to managing organisations. Companies are formulating value-based, globally-consistent codes for ethical understanding and appropriate decision-making at all levels even as they face immense external challenges.

Business ethics is being identified as a major source of competitive advantage. In 1999 a study by the DePaul University of 300 companies found that firms making an explicit commitment to follow an ethic code provided more than twice the shareholder value than those that did not. An earlier study of 1997 had found that companies with a defined commitment to ethical principles outperformed others. What this means is good ethics is also good business. Companies recognised as ethical organisations are able to attract investment and human capital, retain talent, differentiate themselves in the markets, and create a perception of being customer-friendly. As the chairman of a successful company in India says: "Value-based organisations have demonstrated that even so-called soft concepts can be extremely powerful. Money can't buy reputation and integrity; both have to be earned. Organisations based on strongly-held

shared values amongst their customers and employees (and in that order) have been able to professionalise and develop their market potential through strong brand loyalty and relationship building with their constituents”.

Recognising the immense significance of business values and ethics in the context of good business, there have been attempts at describing how ethics can be imbibed as a part of managerial activities through the adoption of a practical framework.

At this point, it is necessary to differentiate between values and ethics. Values are personal in nature (e.g. a belief in providing customer satisfaction and being a good paymaster) while ethics is a generalised value system (e.g. avoiding discrimination in recruitment and adopting fair business practices). Business ethics can provide the general guidelines within which strategic management can operate. Values, however, offer alternatives to choose from. For example, philanthropy as a business policy is optional. A strategist may or may not possess this value and still remain within the limits of business ethics. It is values, therefore, that vary among the strategists in an organisation, and such a variance may be a source of conflict at the time of strategy formulation and implementation. A major set of tasks in strategy implementation is to create consistency among the business values and ethics and the proposed strategy. This is done through inculcating the right set of values, reconciling divergent values, and modifying values that are not consistent with the strategy.

Organisations derive values and ethics from their corporate culture. Corporate culture, as we have seen earlier, is the outcome of the shared assumptions that individual members of the organisation have. The right set of values and a code of ethics have to be formulated by an organisation on the basis of its founding philosophy, cherished traditions, norms of ethical behaviour, and social requirements. Several organisations have formulated such codes for their members.

Inculcating values and ethics: Once the values and ethical codes are formulated, strategists have to set about inculcating them. Several actions could be taken for this to be accomplished. A representative list of such actions is given below.

- Considering values and ethics in recruitment and selection to ensure compatibility of the character traits of potential employees to the ethical system of the organisation.
- Incorporating the statement of values and code of ethics into employee training and educational programmes.
- Example-setting by top management in terms of actions and behaviour that reinforce the values.
- Communication of the value and code of ethics through wide publicity and explanation of compliance procedures.
- Constant monitoring of compliance by superior staff and top management.
- Consistent nurturing of values within the organisation through their integration into policies practices, and actions.
- Paying special attention to those parts of the organisation that are susceptible to ethically-sensitive activities, such as, purchase and procurement, dealing with government and other external agencies.

Reconciling divergent values: Strategists have to reconcile divergent values and modify values, if necessary. A typical situation of value divergence may arise while setting objectives and determining the precedence of different objectives. One group of strategists (may be, a coalition) is interested in production-oriented objectives such as standardisation and mass production while another group may stress marketing related objectives, like product quality, a variety, and small-lot production. These interests may be legitimate in the sense that they arise from their functional bias. It is for the chief executive now to reconcile the divergent values. Obviously, this can be done best in the light of strategic requirements and environmental considerations.

Modifying values to create consistency: Modification of values is frequently required for strategy implementation. A particular strategy, say of expansion, may be suboptimal if existing values do not conform to these requirements. In

such cases, modification of values is necessary. But what was said of corporate culture is true for values too: they are difficult, if not impossible, to change. A judicious use of politics and power, redesigning of corporate culture, and making systematic changes in organisation can help to modify values gradually.

Of late this absence of a uniform national ethos and sense of value based on ethical considerations is being increasingly noticed by management philosophers and sundry models are being advanced that will, hopefully lead to the development of value-based ethical standards in Indian industries. Below we discuss some of them.

The Chakraborty Model

Chakraborty bases his model on Vedantic principles and considers them as the long-lived national ethos of India. His model of ethical morality is briefly structured on the following:

- The basic concept is to harness secular complexity to the guiding hand of sacred simplicity. This is achieved by referring to the four goals of the human system:
- Dharma (rectitude and righteousness)
- Artha (money and wealth)
- Kama (desires and needs)
- Moksha (liberation of the spiritual core).

The secular goals of artha and karma are integrated into the model within the bounds of dharma or ethicomoral propriety and moksha or liberation of the inner spirit core.

- To make Vedantic spirinomics a reality, the following correctives may be sought from sacred simplicity.
- To aim and strive for a 'pure-mind', meaning emotions, feelings, impulses; the matter of the heart, so to say, should take precedence over intellect/sharpening.
- Emphatically follow the law 'the subject is the cause, the object is the effect'. Indeed, in any management system, the crux lies in human beings, not in the system or its structural dimensions.
- Work must be done without personal claims to egocentric results (i.e. rewards) as the primary driving force. This in effect means desireless work (nishkam karma).
- Transition from this concept of 'egoless' work to the ethico-moral concept of 'ego-led' work as enshrined in the doctrine of karma, as explained in essence by Toynbee.

The ethical level of a society at a particular moment depends on the state of karma-account of each of the participants in society. The most important objective for a human being, both for his own sake and for the sake of society is to improve his karma.

- Human personality comprises (a) an outer active, involved all dynamic self called prakriti, and (b) an inner, quiescent witness and silent self called purusha. Even when one works in the midst of turbulent or hectic external circumstances, the inner purusha exists all the time as a permanent background of stillness. The practice of this depth awareness is a crucial process for effective self-management.
- The exchange theory of generating the means of human sustenance and economic wealth is obtained through a systemic framework linking the human and the cosmic. This is expressed by the concept of yagnartha karma, i.e. work done is a sacrifice. In consequence, care and concern flow in this theory not merely from an awakened moral conscience, but from a more all-embracing cosmic and spiritual conscience.

- Creativity in future must, on the whole, be directed towards serving the 'simple living high thinking' goal for humanity in conformity with the Vedantic transformational goal of unfolding the higher self or core self within which is poorna or that which is autonomously whole and self-sufficient.
- The credibility of a leader rests ultimately on the attribute of 'impersonal love' springing from the higher self. Consequently, human development should be based on the following concept:

Consciousness of personality begins with the feeling of separateness from all, but has its culmination in the feeling of unity with all. The life in which the consciousness of unity is primary and separateness the secondary factor, and therefore the personality is large and bright in truth-this is the soul of life.

This consciousness of unity is ekatmanubhuti

These ethical considerations lead to the concept of a business ashram as a credible Indian concept of an ethical view of business. Some possible tangible outcomes of widespread adoption of this 'business ashram' vision would be the following.

- i. There should be a growing tendency towards products with longer life cycles as against the ever shorter ones today.
- ii. Organizations should tend to contract rather than expand, as is the current tendency.
- iii. Localized, decentralized economic activities should increase faster than centralized ones. Production and distribution should be more space-specific.
- iv. The need for high speed, long distance, continuous travel should gradually decline. Bicycles should once again come into their own at the expense of cars and aeroplanes.
- v. Employee relations are likely to become more cooperative and less adversarial, as a consequence of greater identification with smaller sized enterprises and the spirit of trusteeship implied amongst owners/top managers.
- vi. Competitive advertising, preying upon gullible customers, is likely to decline.
- vii. Usiness growth fuelled by greed and achieved through manipulation, financial mergers, and heavy debt financing are likely to be less and less favoured.
- viii. Local resources for local markets to meet local needs being once again the principal thrust, the frenzied search for strategic advantage, strategic intent, strategic response, and so on for global markets should slow down.
- ix. Mental illnesses due to overconsumption outside and undernourishment within should fall.
- x. Living in society is likely to become simpler and less energy intensive. Change for the sake of change will appear to be less justifiable.
- xi. Loyalty and gratitude to organizations and colleagues may once again become important features of professionalism.
- xii. Reduction in greed and interpersonal rivalry should give basic human values like sharing and humility a better chance of coming into their own.
- xiii. Networking, interpersonal or inter-organizational, may rest on something more dignified and genuine than the self-centred instrumental motives of the present.
- xiv. More and more decisions are likely to be subjected to the test of whether their effects are likely to be spiritually ethically, and ecologically positive or negative.
- xv. With the gradual replacement of the slogan of external consumption by the gospel of inner living, creativity will

tend to be channelled more into arts such as music, literature, and painting rather than into the ever-increasing proliferation of superfluous goods and products.

- xvi. In education, realization and idealism should regain their lost importance, as against the current primary of information and careeism.
- xvii. The human being is likely to be less compelled to fit or mould himself/herself to technological imperatives. Rather, technology will be accepted or rejected by the standards of the respiritualized human being.
- xviii. Alignment and empowerment of the individual will/energy with the ultimate Divine Will will gradually become a widespread 'experiment-based' reality. This process will lead to progressively error-free, morally correct decisions.
- xix. Leaders of organizations/institutions should move towards blending the principles of secular 'king-ship with those of sacred rishihood'. They will thus tend to manifest the rajarshi or philosopher king model
- xx. The workplace will tend to be transformed into a 'spiritual/moral gymnasium'. Here, income, profit, and the like will be treated as a means of serving the basic physico-economic needs of employees and society. The end to be served would tend to be the flowering of the spiritual essence in human beings by ensuring a wholesome physical existence.

The Four Core (Cardinal) Virtues Model

The 'Occupational Hazard' of Business Life

In sum, this hazard may be described as teleopathy, the unbalanced pursuit of purpose, and consists of three basic elements.

Fixation: This is a state where, in a sense, the goal owns the person. Management by objectives is in effect replaced by being managed by one's objectives; investing in goals beyond our capacity for critical judgement, thus treating the self as a means not an end.

Rationalization: Two types of rationalization dominate the landscape in the context of business and work life: Loyalty (appealing to fiduciary obligations to shareholders in the face of market competition) and legality (appealing to the permissibility of a behaviour or policy within the constraints of the law). Each provides an excuse for questionable business behaviour, though not always plausibly.

Detachment: Repeating the fixation-rationalization 'loop' becomes a self-reinforcing habit. This habit leads eventually to a kind of callousness, which some observers have called a separation of the head from the heart. Competitiveness and goal seeking eventually drive out compassion and generosity, making more serious compromises easier as time passes. The detached organization, like the detached individual, loses the ability to connect its behaviour to the larger human picture. The division of labour becomes the division of responsibility, and the division of responsibility becomes the fragmentation or dilution of responsibility beyond recognition.

Teleopathy then is a moral condition in which the unbalanced pursuit of purpose manifests itself in three symptoms: fixation, rationalization, and detachment. It is the principal occupational hazard of business leadership in a market economy, and its consequences for the lives of individuals, companies, and society at large can be devastating: alienation, stress, unreasonable demands on work time, loss of creativity, and loss of community.

Avoiding teleopathy as an occupational hazard requires a new outlook on the part of management. In particular, in an increasingly global market place, convictions about core human values and virtues acutely need to be clarified and strengthened.

The foundation for such clarity and strengthening can be found by considering four core (cardinal) virtues that have for two thousand years serve as a foundation for moral theory and practice: prudence, temperance, courage, and justice. Each relates fairly directly to current challenges in business ethics.

In the current industrial and business context, Exhibit 12.16 shows the role each of them might play in organizational decision-making balancing the pursuit of purpose and increasing corporate awareness.

Business leaders who understand the importance of these organization virtues will take their companies social consciences in hand, avoiding tempting appeals to competitive dilemmas and other familiar excuses.

The essence of responsible management perhaps lies in appreciating the art of orchestration affirming multiple values in a compatible and healthy way.

That the principles enunciated above go beyond religious boundaries will be realized if it is remembered that Shakers, Quakers, and Masonic lodge members abide broadly by the same concepts. Whether they can be realistically extended to the industries today is, however, moot question.

Cardinal virtue of habit	Prevention of teleopathy	Sallent stakeholders	Illustrative applications	Managerial implementation
<i>Prudence</i>				
Attention to a long term comprehensive decision perspective	Avoids fixation on 'us', here and now	Wide-ranging primarily owners or investors, employees and communities.	Environmental awareness, bribery, temptations, leadership succession	Planning structures uncentive systems
<i>Temperance</i>				
Attention to spiritual and higher order goods and service	Avoids fixation on maturity and detachment from being fully human	Customers and employees primarily, but also competitors amogn others.	Fair competition, responsible marketing to needs not just wants	Control systems, employees, consumer audits.
<i>Courage</i>				
Rising above sole reliance on market pressures and legal compliance; need for responsible risk.	Avoids denials and rationalization in the name of strength for concience and 'others do it'	Again wide-ranging but primarily owners, investors, employees, and community.	Strong board membership, diverse staff composition, internal whistle-blower protection.	Readership development programmers: reward for initiative, individual spirit.
<i>Justice</i>				
Attention to distributive as well as aggregative productive results to process as well as to overcome.	Avoids fixation on self-serving ends: rationalization at the cost of the weak.	Employees customers, and communities primarily, but also shareholders and competitors.	Fair compensation of employees job security, consumer product safety and quality, tax honesty.	Regular audits of affected stakeholders: representative voices.

Exhibit 12.16: Role of Cardinal Virtues

The TattwaJnanananda Model

The model depends heavily on the Upanishads, namely mukti (freedom) and purnatva (fullness), arising from bodhi (complete enlightenment).

The nature of atman (real man) is sat, cit, ananda (existence, knowledge, and bliss).

Ethics in India is based on dharma and karma.

The moral values and Purusarthas

1.	Dama	----	Self-control
2.	Shraddha	----	Self-respect
3.	Svadhya	----	Self effort
4.	Satya	----	Truth
5.	Asteya	----	Non-seeking
6.	Vidya	----	knowledge
7.	Dhi	----	Wisdom
8.	Brahmacarya	----	Sexual purity
9.	Ahimsa	----	Non-injury
10.	Sauca	----	Cleanliness
11.	Akrodha	----	Freedom from anger
12.	Seva	----	Service to all beings

The two secular ideals that man pursues are artha (wealth) and kama (pleasure). They lead to spiritual freedom (moksha) if they are subordinated to dharma (moral conduct).

Ego Management Through :

- **Self-control:** A ruler's self conquest is the foundation of his kingdom. He who controls his self, controls all. only then will regionalism, linguistic bias, caste conflicts, and religious tensions cease.

- **Self-respect:**

Sarve yasya vinetarch

Sarve panditamaninach

Sarve mathattvamicehanti

Kulani tadavisate

That race in which every one considers himself the leader, everyone regards himself to be wise, and everyone hankers for recognition, goes to ruin.

A man of self-respect has confidence in his own abilities and respects those in others. He helps others to help themselves. He does not feel that his talents are going unnoticed and that he deserves much more than he is getting.

- **Self effort:** Udyuginam purusasim hamupati kaksmih darivam iti kapurushah vadanti. Daivan abhatya guru purusamatmasakhya yatma krte yadi na sidhyati kuta dosha.

The goddess of wealth becomes propitious to the industrious lionhearted person. Only cowards say 'Atas fate, fate!' But dismissing fate, act boldly on your own strength. If something fails, after putting in effort, what is the harm?

Self-effort at the right time can change the future. One who listens well, decides on a goal with proper deliberation and then lets go the goals and concentrates on the means succeeds. His very presence inspires his co-workers.

- **Excellence in work:**

Yoga karmasu kausalam

Gita

Yoga is skill in work

- **Progressive attitude:** The manager should have a habit of studying (sravana), the power to think deeply (manana) and to meditate (nididhasana)

Yad yad acarati srestach

tatadevetaro janah

Gita

Truth at any cost

Practice what you preach

Whatever the superior person does, others follow that. Intensity and pervasiveness of concern: A mother's tyaga (renunciation), not exploitation earns her the unshakeable position of commander in the house

- **Character building**

a. Habit formation

b. Concentration and meditation

The Astangayogo of Patanjali speaks of yama, niyama, asana, pranayama, pratyahara, dharma, dhayana, and samadhi, the moral training and exercise by which meditation or dhyana, quite a high state of concentration, absorption, and composure, is attained.

- **Prayers:**

Om saha navavatu

Saha nau bhunaktu

Saha viryam karavavhai

Tejasvi navadhitam astu

Ma vidvisavahai

Sama Veda

Om may he, (the divine being) protect and murish us; may we grow in strength together. May our study be invigorating. May there be no hatred or ill feeling between us.

● Also,

Om, asato ma sadgamaya

Tamasu ma jyotirgamaya

Mrtymamritamgamaya

Yajur Veda and Brihaduranyaka Upanishad

Om, from the unreal lead me to real,

From darkness to light

From death to immortality

Indian ethics mean every individual acquiring a capacity for independent thinking and having and utilizing the freedom to take the right moral decisions after gathering all the relevant facts and weighing the pros and cons of alternatives.

A somewhat different approach is found in the Gita:

Janami, dharman na cha me, pravriti,

Jamamyadharman na cha me nivriti,

Taya hrishiksha hridi sthitena,

Jatha nijuktohsmi thatha karomi

I know what is right but do not have the will to follow it. I know what is wrong but do not have the will to desist from it. Hence, oh Lord! I shall do whatever you guide me to do residing in my heart.

- i. Although the models discussed above are rooted in Hindu philosophical scriptures, their idealistic nature would, in all probability, make them unacceptable across the religious divide existing in India.
- ii. Neither bears any relation to the historical tradition and reality existent in India.
- iii. Both are totally utopian in nature, do not consider the current realities and the reasons for their evolution.
- iv. Both are highly individualistic, concentrating on how one should improve the 'self' and do not indicate how this can be extended to group thinking.
- v. Both indicate the direction for achievement of ethical goals individually through self-realization (nishkam karma in the Chakraborty model and the subordination of the secular ideals of artha [wealth] and karma [pleasure] to dharma [moral conduct] to achieve freedom [moksha] in the Tattwajnanananda model) and are silent about the linkage of self-realization to leadership.
- vi. The future (or rather, desirable future) of Indian industry under Chakraborty's ethico-moral concepts has been briefly delineated earlier. It is a moot question whether Indian industries will, by following those ethico-moral concepts, survive in the existing competitive atmosphere.

The Caux Principles

The gradual decimation of organization culture and values systems in Western industries is, however, reality. Its likely harmful consequences have startled industrial leaders and management philosophers alike. Attempts are being made, therefore, to develop value and cultural norms that industries can adopt irrespective of product or type or country. They are also considered significant and important enough to become an integral part of the syllabus of management schools, to enable their widespread dissemination. The Caux principles is one such model.

The Caux principles are a set of moral guidelines developed by an international group of business leaders, incorporating the Minnesota principles earlier documented by the Minnesota Centre for Corporate Responsibility at the University of St. Thomas in Minneapolis. The Caux principles do not pretend to mirror everyday reality, but they are a means of expressing a world standard against which corporate performances can be held accountable. In the end members seek to begin a process that identifies shared values and reconciles differing values. Their goal is to articulate a perspective on business behaviour that is acceptable to and honoured by all countries.

The Caux principles are rooted in two fundamental ethical ideas: The Japanese concept of 'kyosei' and the more Western concept of human dignity. 'Kyosei' means living and working together for the common good in a way that enables cooperation and mutual prosperity to coexist with healthy and fair competition. 'Human dignity', refers to the sacredness or value of each human person as an end, not simply as a means to others' purposes or even, in the case of basic human rights, to majority prescriptions.

The motivation for the formulation of the Caux principles is enshrined in the preamble itself.

The mobility of employment and capital is making business increasingly global in its transactions and its effects. Laws and market forces in such a context are necessary but insufficient guides for conduct. Responsibility for a corporation's actions and policies, and respect for the dignity and interests of its stakeholders are fundamental, and shared values, including a commitment to shared prosperity, are as important for a global community as for communities of smaller scale.

It is possible to identify certain norms around which ethics can be discussed. These ethical norms often overlap but nevertheless act as useful points of reference.

- i. **Self-Interest:** The concept of self-interest has been held as one of the most important elements in career planning and formulation of management control systems. Personal goals are often at variance with corporate objectives, and if the two can be made to converge, both individual and organizational effectiveness and efficiency are known to increase.

It is also now accepted that it is in the interest of organizations to be seen as acting ethically.

Even this is, however, influenced and vitiated by the viewpoint of the viewer. Thus Marxist scholars speak of alienation, exploitation, and private accumulation of public wealth, placing a label of immorality squarely at the doorstep of the corporate body. Liberal scholars place the same themes within the framework of reasonable business sense.

- ii. **Utilitarianism:** In its original sense, utility is the want satisfying power of a good or a commodity. Utilitarianism states that human beings maximize their pleasures and minimize their pain. In doing so they act rationally and consistently, choosing between alternatives.

It is, however, a contra-change, contra-progress argument quite commonly used.

- iii. **The Categorical Imperative:** In the business world the term means that there should be an 'honour code' for corporations just as for the armed forces. The constant endeavour to put the ethical and other interests of the organization and nation above all other interests must prevail throughout the business world at all levels.
- iv. **Duty:** Duty assumes a hierarchy, a set of obligations, and range of stated or unstated expectations regarding modes of behaviour. This is interpreted by many in terms of 'managerial prerogatives'.

Three thought-provoking questions arise.

- How can organizations protect themselves from employees who behave unethically?

- Are unethical actions usually the work of an unscrupulous few or does management inadvertently corrupt employees who are ordinarily honest?
- Do reward systems and disciplinary procedures, or even ethical codes themselves, induce honest employees to do dishonest things?

A further question in this connection is: 'To whom does one owe one's duty?' To the self, to the cause, to the profession, to the community or to the employer?

Tied closely to the question of 'duty' is the issue of 'loyalty'. The question is loyalty to whom, for whom and by whom? Can unethical behaviour be excused in the name of loyalty?

Duty is thus, to say the least, a nebulous term and is usually defined by the personal preference of the actors concerned.

- v. **Justice:** Every decision a manager makes must be based on a strict code of ethics to ensure fairness to all. For this, managers must ask themselves and honestly answer specific questions. Once again, the answers are subjective. It, therefore, is only through self-discipline alongside a general rise in social consciousness that this kind of policy can succeed.

David Vogel opines that much of the public interest in ethics stems from the media depiction of the present times as an era of greed. Indeed, it can be demonstrated how ethical perceptions vary with the perceiver's politico-economic position and with the contingency of the situation. Indeed, social justice is mostly used as an excuse to distort facts and mystify reality by the key players in the market.

- vi. **Neutralization:** Manifestations of neutralization may be of the following forms.

- Being cruel in order to be kind.
- Personnel managers playing off one union against another to maintain peace.
- To gain social legitimacy, managers denying any ulterior motives to their actions and refusing to accept that harm to others might have resulted as a consequence.

These are manifestations of ethical dilemma being contrary to the concept of integrity, but nevertheless pursued to maximize personal advantage:

- vii. **Legality:** Hannah Arendt's 'action philosophy' developed in connection with the Nuremberg trials is a fit manifestation of this. Under pressure from the organization and the solidarity demanded by their peer group, managers tend to discard their conscience and obey orders. This can either be in the form of condoning and cooperating with harmful behaviour for personal gain or cooperating with harmful behaviour for what the manager considers to be a greater mission for the organization.

To elaborate on 'action philosophy', it is useful for five reasons:

- It helps us to appreciate and understand the pressures that managers are subject to, and that these pressures are not a new phenomenon, being different in form rather than in content from the problems of the past.
- It helps us, given the mutable nature of objective social reality, to understand the range of ideal types of neutralization and denial.
- It allows a guide to decision-making when an ethical dilemma is involved.
- It is free from all accepted ideologies, and as such serves as an ideal type of framework for decision-

diminishing bank deposit of Christian belief. It has now come to a position where the basis of belief on which the ethics was constructed has all but disappeared.

At one time opponents of Christianity were confident that an alternative source of civic morality would evolve. That theory has not proved successful. Neither has the belief that the urge to do good is so deep-rooted that no commonly agreed morality is required to control private and corporate activity.

Reactions are logically expected. Thus Sir Geoffrey Chandler says:

The trouble is that too many businesses leaders proclaim simplistically that they are in business 'to make money'. But so are burglars and brothel keepers. . . You cannot tack on 'ethics' or 'social responsibility' to business behaviour like an unrelated musical cadenza. They must be inherent in all that a business does.

A survey of a large number of businesses evinces surprising unanimity in the identification of issues that all involve ethical considerations for business. These problems generally fall into four basic categories and are shown in Exhibit 12.17.

Perhaps the categories require some elaboration:

- i. Equity is generally used to mean basic fairness, apart from any established legal or human right. For example, executive salary scales are sometimes the subject of controversy when critics say that it is inequitable for certain employees to receive annually thirty or forty times more than the lowest paid worker in the firm. Some arguments for comparable worth are also rooted in an ethical appeal to greater fairness in determining the material rewards for work.

Equity issues are, however, not limited to salary and pay considerations. They can also arise in the pricing discretion companies are permitted under the applicable law. As in the case of compensation practices, ethical questions can be raised with regard to either results or the means used to attain them.

Equity	Rights	Honesty	Exercise of corporate power
Executive salaries	Corporate due process,	Employee conflict of interest.	Political action committees
Comparable worth	Employer health screening	Security of company records	Workplace safety
Product pricing	Employee privacy	Inappropriate gifts	Environmental issues
	Sexual harassment	Unauthorized payments to foreign officials	Disinvestment
	Affirmative action	Advertising content	Corporate contribution
	Equal employment opportunity.	Government contract issues	Social issues raised by religious organizations
	Shareholders interest	Financial and cash management procedures	Plant/Facility closures and down sizing
	Employment at will	Conflict between corporation's ethical system and business practices in foreign countries	
	Whistle blowing		

Exhibit 12.17: Ethical Categories of Current Corporate Issues

- ii. Rights are treatments to which a person has just claim. The origin of the claim may be legislation, legal precedent or community notions of dignity. Modern views or rights are generally protective in nature. They seek to defend individual autonomy from encroachment by powerful institutions or the community at large.

Societies accept the concept of rights to varying degrees. The Japanese, for example, rely heavily on their traditional concept of reciprocal obligation, which mandates discussion, conciliation, and adjustment of differences

instead of an appeal to abstract concepts of justification. Rather than filing lawsuits, Japanese who allege discrimination usually form a 'victim group' that negotiates with company representatives. The resulting accommodation does not set a precedent, but establishes a basis for ongoing dialogue.

Dignity is a subcategory of rights, where protection is rooted in the community's sense of elemental decency rather than regulated by specific constitutional, judicial or legislative mandates. For example, employee privacy and sexual harassment are issues subject to increasing legislative and judicial activity, but the legislative and judicial systems have yet to find an absolute formula for extending these rights to employees.

- iii. Honesty in corporate ethics relates to the integrity and truthfulness of a company's actions or politics. Issues of honesty arise both in connection with corporate behaviour and with employees acting under the company's nominal supervision. Misleading advertising, questionable financial and cash management procedures, 'gifts' for foreign officials and waste or fraud in the performance of government contracts are examples of corporate behaviour that may be labelled dishonest.

Other honesty issues arise in connection with the company's responsibility for supervision of those who act in its name, and the reciprocal obligation of employees to observe company and community standards in their business dealings. The misappropriation of proprietary information for personal enrichment, or to help a competitor, is an abuse of trust. Acceptance of inappropriate gifts can corrupt the purchasing process. Conflicts of interest between employee activities outside the workplace and company interests can create situations of divided loyalty. In all these circumstances it is the employee who has an ethical responsibility, but a company cannot escape the consequences of lack of proper supervision.

- iv. Exercise of corporate power: Corporations recognize a responsibility to contribute to community enterprises that are consistent with their mission and with their commitments to the various constituencies they serve.

Corporate financial and executive assistance and efforts to generate public support for programmes are believed to be an important element of the company's ethical profit. Business organizations also acknowledge the ethical component of adhering to standards for workplace, product, and environmental safety.

Beyond generally accepted responsibilities, more controversial positions advocated by religious or political groups may raise ethical questions that have an impact on corporate policy and practices. For instance, in recent years companies faced external pressures to disinvest from South Africa. In consequence, while some companies withdrew from South Africa, several others argued that the ethical position was to remain in South Africa, because they believed foreign investment was a critical level for social change in that country.

Ethics and Leadership of the Future

Certain common and distinct features portend the future quite decisively. Among these are the following:

- Emergence of the information society resulting from developments in micro-electronics, making information across the world easily and readily available to every citizen, leading gradually but inexorably to the emergence of a borderless world.
- Geostategic changes resulting in the emergence of three gigantic trading and industrial economic groups, NAFTA, the EEC, and Japan and ASEAN, and the consequent serious concern on the part of other regions of the world finding themselves hemmed in and buffeted.
- The awakening of minorities, nationalism, and regionalism
- Development, growth, and cultural awakening of the developing countries of the world, with the consequent impact on their national ethos.

making under conditions of relative uncertainty.

- Philosophy, the mother of all sciences, provides a theoretical foundation for decision-making on holistic planes.

The question here is, are duty, loyalty, justice, and legality discrete ideas? The codes of conduct of extra corporate, as also professional bodies (medicine, law), philanthropic bodies (Lions, Rotarians), socio-cultural bodies (Theosophists, Freemasons) comprise quasi-legal concepts that enjoin members to adhere to certain ethical behavioural norms and cover them with the umbrella of 'legality'.

We have seen that in real life, violations of these norms are too numerous to be treated as exceptions - to mention a few:

- The Hippocratic oath is too frequently violated.
- In spite enjoining to the contrary, advertisements for liquors abound.
- Against the intent of legal provisions, cigarette manufacturers blithely continue to advertise their cigarettes, satisfying the legal provision by always citing the statutory warning against smoking in their advertisements as discreetly as is feasible.

The questions to be asked here, however, are different:

- Do these codes of conduct innovative behaviour and prevent people from taking a stand based on their convictions?
- Are people being forced to conform?
- If so, is it healthy for society and its continued progress and evolution?
- Is order not the antithesis of 'freedom'?
- Should order, therefore, be pursued by any organization or by society?

- viii. **Ideological Conviction:** It is clear that the answers we get to social issues depend on the questions we ask. The questions we ask depend on the values we hold, and the values we hold are born out of our ideology. Hence ideology is germane to all thought and all action, yet it is frequently seen that megalomania overtakes common sense, self-interest and ideology. Above all, the precept most at work is 'nothing succeeds like success'.

But this brings us to an examination of public good versus private gain, a question that has always troubled moral philosophers. The often conflicting views are illustrated by the following comments:

- Capitalism is the first social system in which the wealthy could claim they received their wealth as a 'just' reward for performing a socially useful function.
- 'Property is theft' (Pierre Proudhon).
- Capitalists can be likened to race of wolves: he who gets there does so at the cost of others (Che Guevara).
- 'Morality lay on the side of the heavier artillery' (Voltaire).
- Capitalism begins not with material self interest but by "giving". Because the inventor has no guarantee of return on his investment; his investment constitutes a gift to the community (George Gilder in *Wealth and Poverty*).

- ix. ***The Light of Day:*** This is manifested in the statement 'If you cannot discuss your decision freely and openly, it is not ethical.' In this the metaphysics of 'reason', the realism of 'dialectic', the pragmatism of 'phenomenology' and simple home truths regarding human behaviour have been neatly encapsulated. At the same time 'categorical imperative' has been emasculated, 'utilitarianism' has been rendered impotent.

A review of these nine aspects of ethical dilemma amply shows that each of them is open to differing interpretations and hence they together fail to provide a general basis for formulating ethical norms.

Ethics, Values, Culture, and Leadership

A significant change has become evident in corporate attitude to business ethics since the eighties. Prior to the eighties business ethics tended to be reflected in the desire to do 'good work'. i.e. showing benevolent intentions cost effectively. This form of corporate paternalism was no longer considered sufficient in the eighties. Rather, the attitude on business ethics centred on the personal behaviour of the individual rather than just the image of the organization. It implied not only that relationships between organizations are governed by implicit or explicit codes of behaviour but that the constituents of business extend beyond customers and shareholders to encompass all those who work for the organizations, communities and, in effect, everyone directly affected by the organization's activities.

But what would these codes of ethics, that in effect are a quantification of business ethics, contain? This is where differences arise.

The cause for this difference is not difficult to locate. To quote Michael Hoffman, a respected professor of philosophy and business ethics:

"Our present century has been weaned away on relativism (denial of ethical absolutes), on pragmatism (the belief that something is right if it works), on positivism (equating knowledge with observable experience), and on behaviourism (interpreting human actions as totally determined and predicatable). The unifying thread of all this is the reduction of everything considered true and meaningful to material reality or physical experience. Science and materialism have flourished and ethics and values have been relegated to matters of emotion, attitude and feeling.

Such ideology permits no significant development of the non-material non-measurable aspects of our lives, such as freedom, morality and divinity: However, there is something about the human spirit which resists this sterile picture and cries out for a different ideology, which will preserve our humanity and provide our life with a value system."

Expressed differently, Morgan McCall points out that creative (and thus effective) leaders are often inconsistent, devious, and two-faced. His implication is that the direction of commerce has little to do with social morality. This view is shared by F.G. Bailey (*Humbuggery and Manipulation: The Art of Leadership*). After considering the role of leaders in society, he concludes:

"Leaders are often Villains and ... it is very difficult to be an effective leader and at the same time a good person. . . one does better to look dispassionately at the institution (of leadership) itself and admit that it has no place for those who practice nothing but the right and the good."

The logic behind this attitude is not hard to seek when one looks at the historical perspective. Although the Christian belief amongst some intellectuals in the last century was replaced by doubt, these great Victorian agnostics believed that all people of goodwill wished to maintain a framework of Christian ethics, governing both individual and public actions. They thought it would be possible to retain Christian ethics while sidelining or even rejecting Christian doctrine.

For a time the agnostic lobby appeared to be successful although now, with hindsight, the record appears rather different. For a considerable time commonly shared Christian ethic survived on what can be described as an ever-

- The population explosion.
 - The environment, with global warming as an immediate, visible source of anxiety.
 - The advance of high technology
 - The loss of values: a general loss loosening the bonds that had previously ensured the coherence of society and confined individuals to its norms.
- Exponential growth in sundry categories of crime, violence, and coercion, organized for monetary gain or political power. Some such manifestations are:
 - The Mafia
 - The drug network
 - Likely limitation of energy resources
 - Increasing impact of the globalization of industrial and business activities with MNCs expanding and proliferating, pushing the world and various countries towards increasing liberalization and withdrawal or easing of restrictions and border controls.

In the context of the above and the need for multinationals to be able to avoid loss of face and likely nationalistic backlash in the developing countries around the world, it would be necessary for these international companies to develop new codes of ethics.

In short, it is necessary to carefully distinguish between values at the individual and the collective level. In many cases they are compatible. The fight against pollution provides a good example of this. Indeed, the interdependence of nationals and the globalization of a number of problems entail an increase in universal awareness and need for a new international code of ethics at the collective level. A number of new ethics dictated by the pressure of new facts are:

The ethics of nature	Imposed by global environmental issues.
The ethics of life about genetic engineering	Discussed increasingly because of the controversy
The ethics of development	Resulting from the increasingly unbearable gap between the rich and the poor
The ethics of money	Because it is divorced from economic realities and dominates the ambitions of too many individuals
The ethics of images	Who should rule over the media and modulate the excessive dramatization of the image on television?
The ethics of solidarity	Dictated by the fact that the dimension of the problems posed to humanity today requires cooperation between a condition of their survival.

human beings as

It is necessary for multinationals if they are to survive and thrive that the personal ethical convictions of their employees and the company's culture are compatible with the code of ethics described above.

Leadership of the Future

In considering this question we again sharply underline two major aspects of development in the future.

- The proliferation and growth of MNCs (or, rather, internationalization of companies) consequent to the increasing trend towards globalization.
- Development, growth, and cultural awakening of the developing countries of the world with the consequent impact on their national ethos.

Against this backdrop, a typical leader of the future would be the CEO of an international company. Certain requirements of such a leader perhaps merit consideration, but before that the nature of the likely developments may be shortlisted.

- The pace of change will be felt in several areas. Globalization will no longer be an objective but an imperative, as markets open and geographic barriers become increasingly blurred and perhaps even irrelevant. Corporate alliances, joint ventures, and acquisition will increasingly be driven by competitive pressures and strategic rather than financial structuring. Technological innovation and the translation of that innovation into market place advantage will accelerate further.
- There are going to be increasing demands for sensitivity to the environment. Only total commitment of everyone in the company will provide the level of responsibility that will be acceptable to employees, governments, and customers.

This change in environment must bring in a change in the culture of successful companies. The essence of business in the twenty-first century is going to be tapping talent. What really matters is not so much where to locate the plants, it is how to locate the best people and motivate them. In all this, the key word is partnership. Partnership will be of all kinds: increasingly strategic interdependence between companies, governments and people. Setting up in new countries will be different from what it used to be. Once, you dropped an American off in Venezuela or Thailand with a boatload of toothpaste and had him build a business. Now it will be necessary to establish a partnership with local business people or local government. Simultaneously, the top-down approach to decision-making, previously in practice, will no longer be valid. The fundamental difficulty will be how to execute a global strategy and still allow those leading the local entity to feel that they are controlling their own destiny. They need to be encouraged to be entrepreneurial so that they can feel responsible for the results.

As already mentioned, this involves a shift in culture. To move towards a winning culture it will be necessary to create what might be called a 'boundaryless company'. The barriers between functions such as engineering and marketing, between people based on salaries, and geographic barriers between locations must disappear. The lines between the company and its vendors and customers must be blurred into a smooth, fluid process, and with no objective other than satisfying the customer and winning in the market place.

When it comes to managing people, business will need to move away from the authoritarian approach towards a shared decision-making approach. The radical change in employee involvement will give workers responsibility in the total business process, and a consequence will be a flattening of the organizational pyramid.

Global companies simply cannot prosper in a diverse, multicultural world unless they reflect the diversity to some degree. It is like the Darwinian ideal that diversity in the gene pool creates strength in and survivability of the species. A corporation that successfully draws on the talents and abilities of all its employees as individuals will be best positioned for success.

As companies reflect more cultural diversity, they will become more tolerant, more willing to use differences, rather than similarities, as criteria for individual success within the organization. Any business climate in which broadly different individuals may succeed will be one in which the organization as a whole prospers.

In this context, the general features of a future leader may be sketched:

a. Areas of Expertise.

- Strategy formulation
- Marketing/sales
- Foreign languages and computer literacy
- Human resource management
- Negotiation/conflict resolution

bi. Personal Characteristics

- Creative
- Open minded
- Inspiring
- Encouraging
- Enthusiastic
- Intelligent
- Energetic

bii. Also Desirable but Rated Somewhat Lower

- Analytic
- Physically fit
- Risk-taking
- Intuitive
- Loyal
- Organized
- Diplomatic
- Collaborative

biii. Desirable Characteristic Rated Lowest

- Tough
- Patient
- Conservative
- Personable
- Dignified

c. Management Style

- Visionary
- Delegate authority; readily reassign or terminate individuals not meeting targets
- Maintain a lean staff and set a personal example of cost consciousness
- Superb communicator

Power

Another, widely pervasive element, influencing the decision-making process in an organization is the exercise of power. For the purpose of strategic analysis, power is best understood as the extent to which individuals or group are able to persuade, induce or coerce others into following certain courses of action. This is the mechanism by which one set of expectations will dominate policy-making or seek compromise with others.

Sources of power within organizations

The normally recognized sources of power are summarized in Exhibit 12.18

Within Organization	For External Stakeholders
1. Hierarchy (formal Power), e.g. autocratic decision-making	1. Control of strategic resources, e.g. materials, labour, money
2. Influence (informal power), e.g. charismatic leadership	2. Involvement in strategic implementation, e.g. distribution outlets, agents.
3. Control of strategic resources, e.g. strategic products (steel, oil).	3. Possession of knowledge (skills), e.g. subcontractors
4. Possession of knowledge/skills, e.g. computer specialists	4. Through internal links, e.g. informal influences.
5. Control of environments, e.g. negotiating skills.	
6. Involvement in strategic implementation, e.g. by exercising discretion.	

Exhibit 12.18: Sources of Power

Hierarchy provides people with formal power over others and is one method by which senior managers influence policy. It is, however, important to remember that this type of power has very limited effect if used in isolation.

Influence can be an important source of power and may arise from personal qualities (the charismatic leader) or because a high level of consensus exists within the group or company (i.e. people are willing to support the prevailing viewpoint). Indeed, there is strong support for the view that the most important task of managers is to shape the culture of the organization to suit its strategy. However, the extent to which an individual or group can use his/its influence is determined by a number of other factors. In many situations, prior commitments to principles may be quite central to the organization's mission. Thus a 'no redundancy' policy may be interpreted to counter actions proposed by senior management (such as productivity levels).

Control of strategic resources is a major source of power within companies. However, the relative importance of different resources will change over time and power derived in this way can show dramatic changes. Within any one company, the extent to which various departments are seen as powerful will vary with the company's circumstances. Design or R & D departments may be powerful in companies developing new products or processes. Whereas marketing people may dominate those that are primarily concerned with developing new markets.

Knowledge/skills: Individuals can derive power from their specialist knowledge or skills. Certain individuals may be viewed as irreplaceable to the company, and some would jealously guard this privileged position by creating a mystique around their jobs. This can be a risky personal strategy, since others within the organization may be either spurred to acquire the skills or to devise methods of bypassing them. The powers of many organizations' computer specialists were threatened by the advent of minicomputers which provided others the means of bypassing those specialists.

Control of the environment: It is well known that events in the company's environment are likely to influence its performance. Hence, the more uncertain the environment, the more likely the company to be dependent upon individuals within the organization with specialist knowledge of that aspect of the environment. This is particularly true when the environment is hostile. That is probably why more than anything else, financial and marketing managers are seen as dominant in the policy determination of a company.

Exercising discretion: This is a most significant source of power within an organization and is often overlooked. Whatever the strategic decision taken, its execution cannot be controlled in all its minutest details, and even the dynamics of the situation change between the time a decision is taken and its implementation. It is therefore up to the implementers to interpret and execute the particular parts of that policy, and in doing so, use their own personal discretion. This is a major source of power for middle management in organizations.

Sources of Power for External Stakeholders

Resource dependence is the most common source of power. Thus major suppliers, banks, and shareholders all derive power from this source.

Involvement in implementation through linkages between value chains can be an important source of power for supplier channels, and buyers. One of the major changes since the sixties in many industries has been the extent to which power shifted from the manufacturing sector to the distribution sector. The greater the knowledge distribution companies have of trends in consumer tastes the greater their ability to dictate terms to manufacturers rather than simply function as outlets for goods designed and planned by manufacturing companies.

Knowledge and skills critical to the success of the company may be a source of power. This is the source of power for many subcontractors.

Internal links can provide a route for external stakeholders to influence company strategy. This, of course, is highly influenced by the nature of the organization. Thus a highly authoritarian organization is likely to be hostile to any attempts by outside stakeholders to formally involve themselves in formulation of strategy and any influence on policy by an external stakeholder must be derived in other ways. In contrast, organizations believing in industrial democracy would actively seek to involve a wide variety of stakeholders in strategic decision-making.

Methods of Assessing Power

It is useful to analyse and arrive at some simple guidelines on how to assess power in an organization. Following Pfeffer, it is suggested that the best way to cope with this complex situation is to step back from the details and look for the indicators of power. There are four major indicators each for the internal and the external sources of power.

Internal Sources

The status of the individual or group, as indicated by position within the hierarchy, individual salaries, and job grades of the group, reputation of the individual or group.

The claim on resources as measured by the department's budget, or the number of employees within the group, in particular, tends in the proportion of resources claimed by the group. The less powerful group would invariably find its resources eroded by the more powerful.

Representation in a powerful position, such as on the Board of Directors or the various decision-making committees.

Symbols of power, such as size and location of individual's office, whether s/he has a secretary, carpets, and a private telephone.

External Sources

The status of an external party, such as a supplier. This is often indicated by the way such a party is discussed among company employees and whether they respond quickly to its demands.

Resource dependence can be measured directly. For example, the proportion of the company's business tied up with any one customer or supplier and the ease with which the supplier, financier, or customer can be replaced at short notice.

Negotiating arrangements: Whether external parties are dealt with at arm's length or are actively involved in negotiations with the company. Thus a customer who is invited to negotiate over the price of a contract is in a more powerful position than a similar party that is given a fixed price on a take it or leave it basis.

Symbols are equally valuable clues, i.e. whether the management team wines and dines some customer or supplier, or the level of person in the company who deals with the particular supplier. The care and attention paid to correspondence with outsiders will tend to differ from one party to another.

Social Responsibility

In the past twenty-five years or so there has been increasing awareness and acceptance by management of the diversity of stakeholder interests and expectations to be accommodated. This has given rise to the notion of social responsibility, by which is meant the acceptance by management of organization responsibilities of a social nature wider than the legal minimum that it is bound to fulfill. There are a wide variety of issues that can be considered to fall under this broad heading. These are summarized in Exhibit 12.19.

How organizations respond to these issues varies considerably and may be summarized in Exhibit 12.19.

Internal Aspects	External Aspects
<p><i>Employee welfare</i> Providing medical care, assistance with mortgages, extended sickness leave, assistance for dependent, etc.?</p> <p><i>Working conditions</i> Enhanced working surroundings, social and sporting clubs, above minimum safety standards, etc.?</p> <p><i>Job design</i> Designing jobs to the increased satisfaction of workers rather than efficiency, etc.</p>	<p><i>Pollution control</i> Reducing pollution below legal standards even if competitors are not doing so, etc.?</p> <p><i>Product safety</i> Danger arising from the careless use of products by consumers, etc.?</p> <p><i>Marketing practices</i> Curtailing advertising that promotes products which harm health (e.g. tobacco and sweets), etc.?</p> <p><i>Employment</i> Positive discrimination in favour of minorities?</p> <p><i>Community activity</i> Sponsoring local events and supporting local good causes etc.?</p>

Exhibit 12.19: Some Questions of Social Responsibility

Behaviour and Attitude			
Role	Economic	Social	Political
Profit maximizer	Profit dominates	Regarded as an impediment to profit	Actively avoids involvement with political system
Profit satisfier	Growth business	Reacts against societal and social pressures as incursions	Avoids interaction with political system
Defender of the enterprise	The business of business is business	Reacts against the societal component as not being within the firm's proper ambit	Stands up for 'free enterprise'
The lone wolf	Prime emphasis on profit	Voluntarily but unilaterally assumes responsibility	Avoids involvement unless cornered
Socially engaged	Prime emphasis on profit	Interactively engaged	Engaged only in negotiation of the rules of the game
Socially progressive	Prime emphasis on profit	Interactively engaged	Positively involved in formulation of national industrial policies
Global Actor	Prime emphasis on profit	Interactively engaged	Assumes a responsibility to foster a balance between national and international economic policies
Developer of society	Financial self sufficiency	Produces changes in the lives of mankind through innovation.	Positively involved with emphasis on planned development of social infrastructures
Social servant	Secondary to social obligations	Provides essential but non economic goods and services	Positively involved in formation of national industrial policies with emphasis on social matters
Employment provider	Subsidized operation	Provides jobs	Subsidized and supported by government

Exhibit 12.20: Social Responsibility: Roles of the Firm

Within the eight categories listed above (Exhibit 12.19) four groups of responses may be discussed. Each of them may give rise to conflicts of objective and policy. We briefly discuss these.

- i. The first group is at one extreme, and its 'only business is the business'. Its only social responsibility is to increase profit. It would, in consequence, treat the legal requirements regarding social responsibilities as unavoidable hindrances. The first three categories fall in this group.
- ii. The next group is categories 4 to 7. here social responsibility is exercised in a carefully, selective way, an usually justified in terms of economic common sense. Sponsorship or welfare provision would be rationalized as sensible expenditure akin to any other form of investment or promotion expenditure, being considered to be in the long-term interest of the company. The companies falling in this group would argue that management ignores social influences at its peril and the 'smarter' companies are those that recognize and cope with these issues in policy-making. The conflicts of responsibility that arise here are for example, between pollution control and job position control and job provision. Extra costs in pollution control mean uncompetitive costs and thus threaten plant closure and job loss.
- iii. The next group would be in category 8. It considers a wide variety of social responsibility issues as important influences on policy-making. The companies falling in this group would retain uneconomic units to preserve jobs, avoid manufacture of anti-social' products, and would be prepared to bear reduction in profitability for the social good. Conflict will naturally come when this reduced profitability threatens survival.
- iv. Lastly, there would be organizations in categories 9 to 10 that are run specifically in response to community needs. Here societal needs are paramount and profit is secondary- often a constraint. Conflict would arise in keeping the organization efficient and commercial, thus minimizing the subsidy requirements.

Chapter 13

Functional Implementation – Plans and Policies

A functional strategy is the short-term game plan for a key functional area within a company. Such strategies clarify grand strategy by providing more specific details about how key functional areas are to be managed in the near future.

Functional strategies must be developed in the key areas of marketing, finance, production/ operations, R&D, and personnel. They must be consistent with long-term objectives and grand strategy. Functional strategies help in implementation of grand strategy by organizing and activating specific subunits of the company (marketing, finance, production, etc.) to pursue the business strategy in daily activities. In a sense, functional strategies translate thought (grand strategy) into action designed to accomplish specific annual objectives. For every major subunit of a company, functional strategies identify and coordinate actions that support the grand strategy and improve the likelihood of accomplishing annual objectives.

To better understand the role of functional strategies within the strategic management process, they must be differentiated from grand strategies. Three basic characteristics differentiate functional and grand strategies :

1. Time horizon covered.
2. Specificity.
3. Participation in the development

Time Horizon

The time horizon of a functional strategy is usually comparatively short. Functional strategies identify and coordinate short-term actions, usually undertaken in a year or less. Sears, for example, might implement a marketing strategy of increasing price discounts and sales bonuses in its appliance division to reduce excess appliance inventory over the next year. This functional strategy would be designed to achieve a short-range (annual) objective that ultimately contributes to the goal of Sears' grand strategy in its retail division over the next five years. This shorter time horizon is critical to successfully implementing a grand strategy for two reasons. First, it focuses functional managers' attention on what needs to be done now to make the grand strategy work. Second, the short-time horizon allows functional managers to recognize current conditions and adjust to changing conditions in developing functional strategies.

Specificity

A functional strategy is more specific than a grand strategy. Functional strategies guide functional actions taken in key parts of the company to implement grand strategy. The grand strategy provides general direction. Functional strategies give specific guidance to managers responsible for accomplishing annual objectives. Such strategies are meant to ensure that managers know how to meet annual objectives. It is not enough to identify a general grand strategy at the business level. There must also be strategies outlining what should be done in each functional area if the annual (and ultimately long-term) objectives of the company are to be achieved. Specific functional strategies improve the willingness (and ability) of operating managers to implement strategic decisions, particularly when those decisions represent major changes in the current strategy of the firm.

Specificity in functional strategies contributes to successful implementation for several reasons. First, it adds substance, completeness, and meaning to what a specific subunit of the business must do. The existence of numerous functional

strategies helps ensure that managers know what needs to be done and can focus on accomplishing results. Second, specific functional strategies clarify for top management how functional managers intend to accomplish the grand strategy. This increases top management's confidence in and sense of control over the grand strategy. Third, specific functional strategies facilitate coordination between operating units within the company by clarifying areas of interdependence and potential conflict.

Participants

Different people participate in strategy development at the functional and business levels. Business strategy is the responsibility of the general manager of a business unit. Development of functional strategy is typically delegated by the business-level manager to principal subordinates charged with running the operating areas of the business. The business manager must establish long-term objectives and a strategy that corporate management feels contributes to corporate-level goals. Key operating managers similarly establish annual objectives and operating strategies that help accomplish business objectives and strategies. Just as business strategies and objectives are approved through negotiation between corporate managers and business managers, the business managers typically ratifies the annual objectives and functional strategies developed by operating managers.

The involvement of operating managers in developing functional strategies contributes to successful implementation because understanding of what needs to be done to achieve annual objectives is thereby improved. And perhaps most critical, active involvement increase commitment to the strategies developed.

It is difficult to generalize about the development of strategies across functional areas. For example, key variables in marketing, finance, and production are different. Furthermore, within each functional area, the importance of key variables varies across business situations.

A key task of strategy implementation is to align or fit the activities and capabilities of an organisation with its strategies. Strategies operate at different levels and there has to be congruence and coordination among these strategies. Such a congruence is the vertical fit. Then, there has to be congruence and coordination among the different activities taking place at the same level. This is the horizontal fit.

When a lower-level strategy, such as a functional strategy, is aligned with a higher level strategy, in this case the business strategy, then a vertical fit takes place. The vertical fit alone is not sufficient to integrate the strategic network. It is also essential to create a horizontal fit at the level of individual functional strategies. What this means is that the different functional areas of marketing, finance, operations, personnel, and information management and all the operation activities performed in these areas should not work at cross-purpose. There has to be an alignment among them which is the horizontal fit. In this manner, the vertical fit leads to functional strategies and their implementation, and the horizontal fit leads to operational implementation.

The consideration of vertical fit leads us to define functional strategies in terms of their capability to contribute to the creation of a strategic advantage for the organisation. Looked at this way, we have primarily be a function of the R & D department, but an organisation may structure it in such a way, we have the following types of functional strategies.

Strategic marketing management means focussing on the alignment of marketing management within an organisation with its corporate and business strategies to gain a strategic advantage.

Strategic financial management means focussing on the alignments of financial management within an organisation with its corporate and business strategies to a gain a strategic advantage.

Strategic operations management implies focussing on the alignment of operations management within organisation

with its corporate and business strategies to gain a strategic advantage.

Strategic human resource management means focussing on the alignment of human resource management within an organisation with its corporate and business strategies to gain a strategic advantage.

Strategic information management means focussing on the alignment of information management within an organisation with its corporate and business strategies to gain a strategic advantage.

It should be noted that these are emergent areas in the discipline of management. The literature and texts in each of these functional areas assign a definite meaning to these terms. You might have noted that managers in the industry and business magazines and newspapers frequently use terms, such as, marketing strategy, advertising strategy or purchasing strategy. Several terms are also prefixed with the term 'strategic', for instance, strategic procurement or strategic recruitment. You should be cautious while using these two terms since the terms 'strategy' and 'strategic' are often used without much discretion. In strategic management there is a definite meaning conveyed by these terms, but in practice the usage tends to trivialise the real meaning. So, when you wish to prefix a term such as 'strategic' before, say, procurement, then make sure that strategic procurement is carried out while keeping in view the objectives and strategies of an organisation, and it is seen as something which has a vital long-term significance to the future of the organisation.

The consideration the horizontal fit means that there has to be an integration of the operational activities undertaken to provide a product or service to a customer. These have to take place in the course of operational implementation.

Operational implementation is the approach adopted by an organisation to achieve operational effectiveness. When an organisation performs value-creating activities optimally and in a way which is better than its competitors, it results in operational effectiveness.

A value chain is a set of interlinked value-creating activities performed by an organisation. These activities may begin with the activity of procurement of basic raw materials and include the act of processing in its various stages, right upto the obtainment of end products which may be marketed to the ultimate consumer.

To reiterate this, the value chain of a manufacturing organisation is divided into primary and support activities. Primary activities are directly related to the flow of products to the customer and include five subactivities: inbound logistics (receiving, storing, etc.), operations (transformation of raw materials to finished products), outbound logistics (order processing, physical distribution, etc.), marketing and sales (pricing, promotion, etc.), and service (installation, repairs, etc.). Support activities are provided to sustain the primary activities. These consist of the firm's infrastructure (including, finance, accounting, general management, etc.), human resource management, technology development, and procurement.

In most organisations, the value-chain activities are dispersed among the different functional areas to be performed by organisational units one of which is a department. For instance, a marketing department is typically responsible for three of the five primary value-chain activities, namely, outbound activities logistics, marketing and sales, and service. The operations department usually performs the two other activities: inbound logistics and operations. The support value-chain activities involve several other departments. For example, procurement is generally placed with the operations department, but all the departments may also be procuring items regularly. Technology development may primarily be a function of the R & D department, but an organisation may structure it in such a way that it may be placed under the operations department. All departments deal with the finance and human resource management functions, but specialised departments of finance, accounting and human resource management usually exist to deal with these activities. So, a value-chain classification and departmental segregation do match to an extent.

The considerations of vertical fit and horizontal fit help to explain why integration is necessary for the different subsets of functional activities.

Functional strategies are not implemented directly. They have to be defined in terms of plans and policies. So, functional implementation takes place through functional plans and policies.

Functional Plans and Policies

For effective implementation, strategists have to provide directions to functional managers regarding the plans and policies to be adopted. In fact, the effectiveness of strategic management depends critically on the manner in which strategies are implemented. In this section, we look at the nature of functional plans and policies, why they are needed, and how they are developed.

As we already know that functional strategies operate on a level below the business strategies. There might be several subfunctional areas within functional strategies. For instance, a company might have a textile division among its several business areas. Within the textile division there might be functional areas, such as, marketing, operations, R & D, and so on. Further, a functional area of marketing may have subfunctions such as, product development, advertising and sales promotion, market research and so on.

Functional strategies, defined in terms of functional plans and policies-plans or tactics to implement business strategies, are made within the guidelines which have been set at higher levels. Plans are formulated to select a course of action, while policies are required to act as guidelines to those actions. Functional plans and policies, are therefore, in the nature of the tactics which make a strategy work.

Functional managers need guidance from the corporate and business strategies in order to make decisions. In simple terms, functional plans tell the functional managers what has to be done, while functional policies state how the plans are to be implemented.

Glueck has suggested five reasons to show why functional plans and policies are needed.

Functional plans and policies are developed to ensure that :

1. The strategic decisions are implemented by all the parts of an organisation.
2. There is a basis available for controlling activities in the different functional areas of a business.
3. The time spent by functional managers on decision-making may be reduced as the plans laydown clearly what has to be done and the policies provide the discretion framework within which decisions need to be taken.
4. Similar situations occurring in different functional areas are handled by the functional managers in a consistent manner.
5. Coordination across the different functions takes place where necessary.

The development of functional plans and policies is aimed at making the strategies formulated at the top management level practically feasible at the functional level. Strategies need to be segregated into viable functional plans and policies that are compatible with each other, thereby augmenting the horizontal fit. In this way, strategies can be implemented by the functional managers.

The process of development of functional plans and policies may range from the formal to the informal. Larger and more complex organisations may have several hundred policies related to every major aspect. Many of these policies could have been formulated through a formal process and published in many manuals and documents. Smaller organisations with simpler businesses may operate with fewer policies, most of which could be informal and understood rather than written down.

The process of developing functional plans and policies-formal or informal is similar to that of strategy formulation.

Environmental factors relevant to each functional area will have an impact on the choice of plans and policies. Organisational plans and policies shall affect the choice of functional plans and policies. Finally, the actual process of choice will be influenced by objective as well as subjective factors. Then functional plans and policies will affect, and are affected by, the resource allocation decisions.

But before we move on the next section, two points have to be noted. First, functional areas have been traditionally segregated into finance, marketing, production and personnel. Information management has emerged as a significant function within organisations. But not all organisations divide functional areas traditionally—they do it on the basis of what they actually need. For instance, service organisations will have a different of functional areas. Second, the discussion of functional plans and policies that follows is only indicative and not exhaustive. This is understandable because functional managers in each area would formulate plans and policies in much greater detail than we can possibly do here. Creating plans and policies leads to conditions where subordinate managers will know what they are supposed to do and willingly implement the decision.

Managers create plans and policies to make the strategies work. Policies provide the means for carrying out plans and strategic decisions. The critical element is the ability to factor the grand strategy into plans and policies that are compatible, workable, and not just “theoretically sound.” It is not enough for managers to decide to change the strategy. What comes next is at least as important. How do we get there? When? And How efficiently? A manager answers these questions by preparing plans and policies to implement the grand strategy. For example, let us say that the strategic choice was to diversify. Now the executive must decide what to diversify into, where to diversify, how much money will be needed, where the money will come from, and what changes are needed in marketing, production, and other functions to make diversification work.

The amount of planning and policymaking in the formal sense will vary with the size and complexity of the firm. If the firm is small, or if it is a simple business, a few policies and plans will suffice. The plans and policies are generally understood and verbal. Larger and more complex firms find that policies and plans on every major aspect of the firm – marketing, finance production and operations, personnel, and so forth—are necessary, for the competitive advantage of the large firm is its power, not its speed. That is where the smaller firm or decentralized division excels.

The processes involved in establishing plans and policies are quite similar to those influencing strategy formation and choice. That is, environmental factors can influence the choices : internal policies and the power of subunits jockeying for position play a role etc. Hence, resistance to change, conflict resolution techniques, and coalition building will all be at play in the development of plans and policies.

Without good plans and policies managers would make the same decisions over and over again. And different managers might choose different directions, and this could create problems. On the other hand, plans and policies should never be so inflexible as to prevent exceptions for good reasons. So criteria for judging the adequacy of plans and policies developed would include the following :

- Do they reflect present or desired company practices and behaviour?
- Are they practical, given existing or expected situations?
- Do they exist in areas critical to the firm’s success?
- Are they consistent with one another, and do they reflect the timing needed to accomplish goals?

As a result, policies and plans will :

- I. Specify more precisely how the strategic choice will come to be – what is to be done, who is to do it, how it is to be done, and when it should be finished.

2. Establish a follow-up mechanism to make sure the strategic choice, plans, and policy decisions will take place.
3. Lead to new strengths which can be used for strategy in the future.

One example of a set of plans for several strategies is given in Exhibit 13.1. For each of these plans, a set of policies will have to be established for the appropriate area of the business. The policies will ensure that the plans are carried out as intended and that the different areas are working toward the same ends. Companies have plans and policies that cover nearly every major aspect of the firm. The example in Exhibit 13.1 illustrates only a few areas. The minimal plans and policies which must be developed are the key functional decisions for each area of the business.

Strategy	Marketing product line plans	Manufacturing plans	Human resources plans	Financial plans	Timing
Retrenchment	Identify product lines for divestment—those with low sales or margins.	Identify plants to close on the basis of capacity utilisation.	Reduce personnel on the basis of skills needed in the future and seniority.	Eliminate or reduce dividends, and manage cash flows.	Sell plants and reduce personnel in 1 year out dividends now.
Stability	Push the high-margin products in the line.	Defer plant and equipment investments over \$ 200,000.	Invest in training programs to improve management skills.	Develop good bank relations, maintain steady dividends, and strengthen the balance sheet.	Continue for three years unless trends show high opportunity.
Expansion	Extend and improve product lines; volume is more critical than margins.	Expand plant capacity to support new products as necessary.	Hire additional sales, R&D, and production workers and managers.	Increase the debt-equity ratio by one-third. Consider the impact of dividend policy on cashflow needs.	Evaluate market share position and financial condition after 2 years.

Exhibit 13.1: Alternative Business Strategies and Plans

Then we will return to some questions about how these are to be integrated, since our criteria suggest that plans and policies need to be consistent, provide for coordination, and deal with timing issues.

Specialists in each area develop plans and policies in much more breadth and depth than we can cover here. But the list indicates the types of major questions which need to be addressed if strategy is to be implemented effectively.

Functional Strategies in Marketing Area

The role of the marketing function is to profitably bring about the role of products/service in target markets for the purpose of achieving the business' goals. Functional strategies in the marketing area should guide this endeavour in a manner consistent with the grand strategy and other functional strategies. Effective marketing strategies guide marketing managers in determining who will sell what, where, when, to whom, in what quantity, and how. Marketing strategies must therefore entail four components: product, price, place and promotion. Exhibit 13.2 illustrates the types of questions that operating strategies must address in terms of these four components.

Key functional strategies	Typical questions that should be answered by the functional strategy
Products (or service)	<p>Which products do we emphasize?</p> <p>Which products/services contribute most to profitability?</p> <p>What is the product/service image we seek to project?</p> <p>What changes should be influencing our customer orientation?</p>
Price	<p>Are we primarily competing on price?</p> <p>Can we offer discounts or other pricing modifications?</p> <p>Are pricing policies standard nationally or is there regional control?</p> <p>What price segment are we targeting (high, medium, low, etc.)?</p> <p>What is the gross profit margin?</p> <p>Do we emphasize cost/demand or competition oriented pricing?</p>
Place	<p>What level of market coverage is necessary?</p> <p>Are there priority geographic areas?</p> <p>What channels of distribution are key?</p> <p>What are the channel objectives, structure, and management?</p> <p>Should the marketing managers change their degree of reliance on distributors, sales reps, and direct selling?</p> <p>What sales organization do we want?</p> <p>Is the sales force organized around territory, market or product?</p>
Promotion	<p>What are key promotion priorities and approaches?</p> <p>Which advertising/communication priorities and approaches are linked to different products, markets and territories?</p> <p>Which media would be most consistent with the total marketing strategy?</p>

Exhibit 13.2: Functional Strategies in Marketing

A functional strategy for the product component of the marketing function should clearly identify the customer needs the firm seeks to meet with its product and/or service. An effective functional strategy for this component should guide marketing managers in decisions regarding features, product lines, packaging, accessories, warranty, quality, and new product development. This strategy should provide a comprehensive statement of the product/service concept and the target market(s) the firm is seeking to serve. This, in turn, fosters consistency and continuity in the daily activity of the marketing area.

A product or service is not much good to a customer if it is not available when and where it is wanted. So, the functional strategy for the place component identifies where, when, and by whom the product/services are to be offered for sale. The primary concern here is the channel(s) of distribution—the combination of marketing institutions through which the products/services flow to the final user. This component of a marketing strategy guides decisions regarding channels (for example, single versus multiple channels) to ensure consistency with the total marketing effort.

The promotion component of marketing strategy defines how the firm will communicate with the target market. Functional strategy for the promotion component should provide marketing managers with basic guides for the use and mix of advertising, personal selling, sales promotion, and media selection. It must be consistent with other

marketing strategy components and, due to cost requirements, closely integrated with financial strategy.

Functional strategy regarding the price component is perhaps the single most important consideration in marketing. It directly influences demand and supply, profitability, consumer perception, and regulatory response. The approach to pricing strategy may be cost oriented, market oriented, or competition (industry) oriented. With a cost-oriented approach, pricing decisions center on total cost and usually involve an acceptable markup or target price ranges. Pricing is based on consumer demand (e.g., gasoline pricing in a deregulated oil industry) when the approach is market oriented. With the third approach, pricing decisions centre around those of the firm’s competitors.

Pricing and other marketing policies become particularly critical at various stages of product development and the firm’s strategy. Price has become a primary weapon in tactical battles to secure a market share. For example, if rapid expansion is desired early in the development of a product, pricing may be below cost. (Of course, a desire to attract customers through loss leaders may be another reason for selling below cost.) Being a price leader or follower is a policy which managers need to address. Here in particular you can see how the development of plans can be affected by managerial values. Offensive versus defensive strategists will view a particular pricing question differently. During periods of stable demand we would expect prices to remain relatively fixed (perhaps adjusted for inflation). If the strategy is retrenchment, price increases and a reduction in promotion and distribution costs would be expected if not outright abandonment. If the firm is retrenching out of certain areas as opposed to liquidating, an orderly withdrawal through various “demarketing” mechanisms would be necessary.

Packaging can be an alternative competitive weapon in the strategy of the firm. If product stability is the strategy, packing changes (e.g., toothpaste in a pump, or shaving cream in a brush) can help expand the pace of market penetration.

Policies and plans must be made which interrelate several aspects of the strategy. For instance, a policy of different prices for different customers (or a one-price policy) is one which can have an impact on the product and market strategy. As you will see later, plans and policies must also be set in relation to other aspects of the business—for instance, price is particularly critical in relation to volume-cost-profit conditions, which affect production and the financial condition.

Functional Strategies in Finance/Accounting

While most operating strategies guide implementation in the immediate future, the time frame for financial functional strategies varies because strategies in this area direct the use of financial resource in support of the business strategy, long-term goals, and annual objectives. Financial operating strategies with longer time perspectives guide financial managers in long-term capital.

Key functional strategies	Typical questions that should be answered by the functional strategy
Capital Acquisition	What is an acceptable cost of capital? What is the desired proportion of short-and long-term debt, preferred and common equity? What balance is between internal and external funding? What risk and ownership restrictions are appropriate? What level and forms of leasing should be used in providing assets?
Capital allocation	What are the priorities for capital allocation projects? On what basis is final selection of projects to be made? What level of capital allocation can be made by operating managers without higher approval?
Dividend and working capital management	What portion of earnings should be paid out as dividends? How important is dividend stability? Are things other than cash appropriate as dividends? What are the cash flow requirements; minimum and maximum cash balances? How liberal/conservative should credit policies be? What limits, payment terms, and collection procedures are necessary? What payment timing and procedure should be followed?

Exhibit 13.3: Functional Strategies in Finance

Investment, use of debt financing, dividend allocation, and the firm's leveraging posture. Operating strategies designed to manage working capital and short-term assets have a more immediate focus. Exhibit 13.3 highlights some key questions financial strategies must answer for successful implementation.

Long-term financial strategies usually guide capital acquisition in the sense that priorities change infrequently over time. The desired level of debt versus equity versus internal long-term financing of business activities is a common issue in capital acquisition strategy. For example, Delta Airline has a long standing operating strategy that seeks to minimize the level of debt in proportion to equity and internal funding of capital needs. General Cinema Corporation has a long-standing strategy of long-term leasing to expand its theatre and soft-drink bottling facilities. The debt-to-equity ratios for these two firms are approximately 0.50 to 2.0, respectively. Both have similar records of steady profitable growth over the last 20 years and represent two different yet equally effective operating strategies for capital acquisition.

Another financial strategy of major importance is capital allocation. Growth-oriented grand strategies generally require numerous major investments in facilities, projects, acquisitions, and/or people. These investments cannot generally be made immediately, nor are they desired to be. Rather, a capital allocation strategy sets priorities and timing for these investments. This also helps manage conflicting priorities among operating managers competing for capital resources.

Retrenchment or stability often require a financial strategy that focuses on the reallocation of existing capital resources. This could necessitate pruning product lines, production facilities, or personnel to be reallocated elsewhere in the firm. The overlapping careers and aspirations of key operating managers clearly create an emotional setting. Even with retrenchment (perhaps even more so!), a clear operating strategy that delineates capital allocation priorities is important for effective implementation in a politically charged organizational setting.

Capital allocation strategy frequently includes one additional dimension-level of capital expenditure delegated to operating managers. If a business is pursuing rapid growth, flexibility in making capital expenditures at the operating level may enable timely resources to an evolving market. On the other hand, capital expenditures may be carefully controlled if retrenchment is the strategy.

Dividend management is an integral part of a firm's internal financing. Because dividends are paid on earnings, lower dividends increase the internal funds available for growth, and internal financing reduces the need for external, often debt, financing. However, stability of earnings and dividends often makes a positive contribution to the market price of a firm's stock. Therefore, a strategy guiding dividend management must support the business's posture toward equity markets.

Working capital is critical to the daily operation of the firm, and capital requirements are directly influenced by seasonal and cyclical fluctuations, firm size, and the pattern of receipts and disbursements. The working capital component of financial strategy is built on an accurate projection of cash flow and must provide cash management guidelines for conserving and rebuilding the cash balances required for daily operation.

Sources of capital are related to uses of capital. A prime example is leasing versus buying fixed assets. A policy to lease classes of assets will change the nature of the need for funds over time and the nature of the balance sheet. Thus owning a building (say, the Pan Am building in Manhattan) versus leasing such space has an impact on working capital needs and the ability to finance other types of activities. Hence a strategy of rapid expansion, if funds are limited in the short term, might be accomplished through leasing rather than buying. Sale- and-leaseback arrangements became quite popular in the early 1980s because of the favourable tax benefits associated with such policies.

Other financial policies concern the evaluation of proposals for investing in certain projects. For instance, a "hurdle

rate of return" may be specified as a policy guide before some strategic option will be considered. Hurdle rates may differ, depending on how risk is assessed. Another method for assessing potential investment alternatives includes a risk-adjusted discount rate in the net present value approach. A policy of a mix of investment risks is as useful as marketing-mix policies or planning a mix of basic and applied research. The investment risk mix is related to strategic choice, of course. If expansion is the desired strategy, greater risks are acceptable. A mix of low-risk projects only may be an indication that retrenchment is on the horizon. In the mid-1980s, corporate treasurers made increasing use of "swap transactions" which allowed firms to trade interest rate payments and limit some exposure to risk of interest rate fluctuation. In addition, more and more firms sought to hedge foreign currencies as part of their financial plans.

The other area in which risk plans are needed is in the area of insurance. Corporate liability insurance in the mid-1980s was becoming very expensive, and in some instances difficult to get at all. Some firms were forced out of business because they did not believe they could expose themselves to the risk of doing business without insurance. Other firms chose a plan of in-house protection, but such plans require a large resource base. Still others joined consortia to pool resources as an alternative to traditional insurers. Another possibility is to change the nature of coverage for catastrophic risks and at the same time reduce or eliminate coverage for more common risks. Choices here can affect the strategy in terms of costs of doing business, or even lead to ultimate retrenchment (liquidation or sale).

Specific targets for current assets and cash flows are also needed for items such as inventories (finished goods and raw materials) and accounts receivable and payable. Policies for the desired proportion of funds tied up in these accounts and the accounting treatment (e.g., LIFO or FIFO, or book or market value) are relevant here, as are rules for financial disclosure based on historical or "inflation-related" reporting. Some of these policies are mandated by SEC or other government bodies, but managers should decide which approach provides them with the most useful information for decision making (as opposed to which treatment makes the books "look better"). Alternative treatments of accounting data can lead to significant differences in the data upon which managers base their decisions.

Policies governing asset use have a direct impact on other components of strategy and cannot be made in isolation. For example, a policy with respect to maintaining a particular monetary value of safety stock of finished goods relates to marketing policy regarding customer relations and the ability to deliver outputs, as well as to production policy regarding lead times and the size of production runs. Or if an airline is trying to enhance relations with travel agents in a new territory, then extending the time for accounts receivable on the payment for tickets may be an important decision affecting marketing and finance.

Financial plans also become important in particular strategic actions such as mergers or liquidations or bankruptcies. In some cases, legal factors restrain choices. But there are usually several options which require a financial decision as to how to best implement the strategy. Such an option would require a policy decision or would be made in relation to other plans associated with the desired financial structure of the business.

If a firm is divesting or liquidating, financial policies as well as other plans will need to be specified. For instance: How urgent is it? What will the cash flow look like? What will creditors get? Who are the potential buyers? What will the price be? How will we lay off people? In the early 1980s, many firms began to alter their plans to focus on debt reduction and increasing the cash flow due to stability strategies taken in response to disinflation.

Finally, some financial policies can have an indirect effect on strategy through the executive compensation system. For instance, firms which use stock options as a form of compensation may ultimately change the nature of control of the business or influence risk choices made by the executives involved. The implications could be positive or negative, and so such outcomes should be considered as these plans and policies are established.

Hence, some of the crucial financial questions needing implementation include :

- Where will get additional funds to expand, either internally or externally?
- If external expansion is desired, how and where will it be accomplished?
- What will be strategy do to our cash flow?
- What accounting systems and policies do we use (for example, LIFO and FIFO)?
- What capital structure policy do we pursue? No debt or a heavily leveraged structure?
- How much should we pay out in dividends.
- How much cash and how many other assets do we keep on hand?
- Should we hedge our foreign currency exchange risk?

It is crucial that financial plans and policies are such that the funds needed are available at the right time and at the lowest cost.

Functional Strategies in Research and Development

With the increasing rate of technological change in most competitive industries, research and development (R&D) has assumed a key functional role in many organizations. In the technology-intense computer and pharmaceutical industries, for example, firms typically spend between 4 and 6 per cent of their sales dollars on R&D. In other industries, such as the hotel/motel and construction industries, R&D spending is less than 1 per cent of sales. Thus, R&D may be a vital function—a key instrument of business strategy—although in stable, less innovative industries, R&D is less critical as a functional strategy than is marketing or finance.

Exhibit 13.4. illustrates the types of questions addressed by an R&D operating strategy. First, R&D strategy should clarify whether basic research or product development research will be emphasized. Several major oil companies now have solar energy subsidiaries with R&D strategy emphasis on basic research, while smaller competitors emphasize product development research.

R&D decision area	Typical questions that should be answered by the functional strategy
Basic research versus commercial development	To what extent should innovation and break-through research be emphasized? In relation to the emphasis on product development, refinement, and modification? What new projects are necessary to support growth?
Time horizon	Is the emphasis short term or long term? Which orientation best supports the business strategy? Marketing and production strategy?
Organizational fit	Should R&D be done in-house or contracted out? Should it be centralized or decentralized? What should be the relationship between the R&D unit(s) and product managers? Marketing Managers? Production Managers?
Basic R&D posture	Should the firm maintain an offensive posture, seeking to lead innovation and development in the industry? Should the firm adopt a defensive posture, responding quickly to competitors developments?

Exhibit 13.4: Functional Strategies in R&D

Directly related to the choice of emphasis between basic research and product development is the time orientation for these efforts mandated by R&D strategy. Should efforts be focused on the near or the long term? The solar subsidiaries of the major oil companies have long-term perspectives, while their smaller competitors appear to be focusing on the immediate future. These orientations are consistent with each business' strategy if the major oil companies want to ensure their long-term position in the energy field, while the smaller companies want to establish a competitive niche in the growing solar industry.

R&D strategy should also guide organization of the R&D function. For example, should R&D efforts be conducted solely within the firm or should portions of the work be contracted outside? A closely related issue is whether R&D should be a centralized or decentralized function.

The basic R&D posture of the firm influences each of these decisions because strategy in this area can be offensive, defensive, or a combination of these. If the R&D strategy is offensive, technological innovation and new product development are emphasized as the basis for the firm's future success, as is true for small, high-technology firms. However, this orientation entails high risk (and high payoff) and demands considerable technological skill, forecasting expertise, and the ability to quickly transform basic innovations into commercial products. Guidelines are needed to encourage the types of R&D efforts required for the strategy. For example, if new-product development is the basic strategic direction of the firm, then the research effort will be geared to focus on this activity. Of course, stability strategies which may call for product improvements would require a greater emphasis on modification to the existing line. If a turnaround strategy is desirable, R&D efforts may be focused on improving production processes to reduce costs. Unfortunately, retrenchment strategies often are implemented by cutting R&D activities which may be needed for long-term improvements in the business. Such short-sighted policies provide an example of how the implementation of the current strategy may limit long-term strategy development.

The strategy of vertical integration (e.g. backward or forward expansion in function) is another area where R&D policy becomes particularly relevant. The technologies involved in providing inputs or subsequent processing of outputs associated with changing functions would normally require policies to provide for resources and expertise in the new areas of activity.

Another area would include the relative focus of effort on performing basic or applied research. Few companies will authorize the research department to study anything its scientists may be interested in. But the extent of concern with short-term commercialization versus theoretical knowledge which may lead to major breakthroughs is an issue of some importance. If a firm is going to undertake basic research, it must be prepared to accept certain financial outcomes and commitments: longer-term risk with potentially no payout or long payback periods, and enough capital to exploit discoveries if and when they are made. Of course, the firm may need to engage in some basic research if the nature of its business requires it (e.g., most pharmaceutical firms depend on basic research).

Some R&D options are available which reflect whether the strategy is offensive or defensive. That is, as with policies such as pricing, strategists can choose to be leaders or followers. If leadership is endorsed, greater emphasis will be placed on R&D in order to be "first to market." Of course, the costs and risk can be high. Others prefer to be fast seconds or followers who take basic research done by others and pursue product modification. In the follower approach, another option is to buy the R&D efforts of others (such as university, government, or independent research labs). Buying patents or paying license or royalty fees may be another option for firms which do not have strengths in the R&D area or for firms which do not wish to make a commitment to or take the risks of building technological leadership. Another option is the joint-venture strategy, which combines internal and external approaches. Such strategies require policies for negotiating contracts and agreements using outputs from research efforts, and deciding how the firm's own R&D departments will be involved in the joint efforts.

Policies as to the amount of financial commitment in R&D can be based on the following guidelines:

- Maximum range –5 to 2 per cent gross profit, depending on the industry
- Minimum range – competitor actions.

However these figures provide a potentially wide range of discretion within which managers must subjectively determine how the R&D activity fits as a component of overall strategy. Perhaps more importantly, questions of how these funds will be used need to be addressed. Exhibit 13.6 suggests that changing policies on how R&D personnel use their resources can impact a firm's strategy.

Functional Strategies in Production/Operations

Production/operations management (POM) is the core function in the business firm. POM is the process of converting input (raw material, supplies, people, and machines) into value-enhanced output. This function is most easily associated with manufacturing firms. However, it applies equally to all other types of business (including service and retail firms, for example).

Functional strategies in POM must guide decisions regarding : (1) the basic nature of the firm's POM system, seeking an optimum balance between investment input and production/operations out put and (2) location, facilities design, and process planning on a short-term basis. Exhibit 13.5 illustrates these concerns by highlighting key decision areas in which the POM strategies should provide guidance.

The facilities and equipment component of POM strategy involves decisions regarding plant location, size, equipment replacement, and facilities utilization that should be consistent with grand strategy and other operating strategies.

The purchasing function is another area that should be addressed in the POM strategy. From a cost perspective, area a new suppliers an advantage or risky because of over dependence? What criteria (for example, payment requirements) should be used in selection vendors? How should purchases be made in terms of volume and delivery requirements to support operations? If such questions are critical to the success of a grand strategy, functional strategy guidelines improve implementation.

Functional strategies for the planning and control component of POM provide guidelines for ongoing production operations. They are meant to encourage efficient organization of production / operations resources to match long-range, overall demand. Often this component dictates whether production / operations will be demand oriented, inventory oriented, or subcontracting oriented. If demand is cyclical or seasonal, then POM strategy must ensure that production / operations processes are efficiently geared to this pattern. A bathing suit manufacturer would prefer

Key operating strategies	Typical questions that should be answered by the functional strategy
Facilities and equipment	How centralized should the facilities be? (One big facility or several small facilities?) How integrated should the separate processes be? To what extent will further mechanization or automation be pursued? Should size and capacity be oriented toward peak or normal operating levels?
Purchasing	How many sources are needed? How do we select suppliers and manage relationships over time? What level of forward buying (hedging) is appropriate ?
Operations planning and control	Should work be scheduled to order or to stock? What level of inventory is appropriate? How should inventory be used (FIFO/LIFO). controlled, and replenished? What are the key foci for control efforts (quality, labor cost, downtime, product usage, other)? Should maintenance efforts be preventive or breakdown oriented? What emphasis should be placed on job specialization? Plant safety? use of standards?

Exhibit 13.5: Functional Strategies in POM

inventories to be at their highest in the early spring, for example, not the early fall. If demand is less cyclical, a firm might emphasize producing to inventory, wanting a steady level of production and inventories. When demand fluctuations

are less predictable, many firms subcontract to handle sudden increases in demand while avoiding idle capacity and excess capital investment.

Plans must be made for the levels of production or operations desired to fit the strategy. If rapid expansion is desired through internal means, does the firm have sufficient capacity to accommodate such expansion? Is the plant being used on overtime, double, or triple shifts? If retrenchment is under way, do we want to cut back production volume or keep the plant going and build inventories?

These questions may call for a plan for long-term production vis-à-vis marketing plans. Generally, three options exist for scheduling capacity usage: demand matching, operations smoothing, and subcontracting. If demand is seasonal, for example, demand matching calls for producing output with the season. Operations smoothing calls for continuous production to meet average demand levels. Subcontracting allows a firm to maintain steady minimal levels of output while meeting peak periods with output from subcontractors. Each of these approaches, of course, implies some tradeoffs with respect to the costs of equipment, overtime, inventories, labor, maintenance, and subcontracting. When demand downturns occur, a plan to build inventory instead of retrenching becomes a major strategic decision.

As the plan is determined, there may remain a need or desire for longer-term capacity buildup. Here the options may include adding capacity, merging with another producer, or joint ventures. In any case, questions concerning the types of equipment, the amount of capacity, and the interface with existing units need to be addressed. Naturally, the overall size of a plant is of importance here and involves questions of economies of scale. This is partly determined by the technology employed but is also influenced by production scheduling and the basic marketing strategy. A large, "efficient" plant may not be effective if it is not producing the kinds of outputs called for by the strategy. Capacity planning is also related to the policy question regarding scheduling. If demand matching is used, then plant size is geared to the production of peak output; otherwise, capacity can be smaller.

Assuming that a strategy of expansion is under way, another question of importance is where to locate plants or operations facilities. For instance, a major component in airline operations is the location of facilities for aircraft maintenance.

Of course, the critical elements of the firm's marketing and financial plans are relevant to the location decision. For instance, if new distribution approaches are a part of the strategy, locating plants near potential markets may outweigh factors such as the availability or cost of raw material inputs. The financial trade-offs of locating facilities near sources of labor or energy versus customers also need to be examined. Naturally, the type of product and logistics costs of inputs versus outputs become relevant considerations.

Another factor of some importance is the degree of certainty associated with a new strategy. For instance, in the selection of a site for a new plant, the availability of land for further expansion later may be important if the decision is to plan for anticipated sales increases in the long run. And if the decision involves a move to foreign countries, social stability and tax conditions may play a role.

Finally, plants may be located near existing facilities to take advantage of economies of organization, purchasing, and the like. In some cases, the decision is to replace existing facilities (or equipment) with new ones to take advantage of new technologies that are replacing obsolete ones. In other cases, the decision is to add on to an existing plant or build nearby. In still others, the firm seeks to take advantage of lower-cost foreign labor by locating plants outside its home country. Again, factors such as labor, transportation, market location, and technologies play key roles in these determinations.

The types of processes to use are largely determined by the technology needed to produce given outputs. Still, some discretion or options may exist, particularly with respect to issues like the quality of processing equipment and allowable tolerances. Many Japanese firms have gained significant competitive advantages by pursuing a policy

high-quality statistical control for their processing systems.

Policies regarding investment to maintain or replace a plant and equipment can be important to the long-term ability of a firm to compete successfully and achieve objectives such as profits. Of course, the need for the maintenance of facilities varies from firm to firm. Maintenance at nuclear power plants or of aircraft is an absolute necessity. But there are often choices about whether to follow routine schedules (e.g., preventive maintenance) or whether to defer maintenance until there is a breakdown or replacement becomes necessary. Of course, keeping up-to-date, cost-effective equipment is a question of importance in creating a competitive advantage.

The overall quality component of a firm's strategy may determine the type of policy established for maintenance. But the criticality of prompt delivery of outputs may also play a role, and once again trade-offs with regard to inventory policies, the use of overtime, production schedules, and the like, become relevant.

Another key area in the operations of the firm involves sources of inputs or services important to the strategy. Choices about whom to purchase from involve more than a simple question of cost or availability. For instance, options may exist for shipping outputs by various forms of transportation (e.g., rail, airplane, ship). The speed of delivery versus costs may be important in the selection of the mode as well as the vendor. Further, whether to use one or more vendors or several sources for inputs and services is a question of some significance. Increasing dependence on one or a few sources may increase favourable treatment and cost savings but could come at the expense of flexibility.

Perhaps the key strategic issue involving sourcing is the make or buy question. In many instances, the decision is made by purchasing departments largely on the basis of the price to buy versus the cost to make. Yet such a policy is, in effect, a strategic decision regarding the development of competitive advantages. For instance, different financial needs are involved in making versus buying, and these can affect the capital structure. If quick delivery is important to the strategy, consideration must be given to the varying reliability of suppliers versus the control over components or supplies made in-house. If expansion strategies for new products are desired, a firm may opt for buying specialty products to round out a line or making these itself. Of course, plant capacity, personnel skills, and the financial condition all play a role in such a decision. Similarly, if retrenchment is the strategic choice, cost trade-offs of making versus buying can play a role here. Network firms have gone to extreme vertical *disintegration* by choosing to eliminate control over internal production. Many use foreign suppliers as sources. In essence, the question of vertical integration as a strategy is implicit in make-or-buy decisions. Hence, internal and external factors as well as objectives involved in strategy formulation should guide the establishment of policies in this area: strategic choice should not be left to the purchasing department by default.

Here, policies such as relying on supplies within 60 miles of a plant, or shipping finished goods immediately (instead of producing for inventory) can implement a just-in-time approach to accomplishing aggregate manufacturing flexibility. Similarly, personnel policies allowing the hiring of temporary or part-time workers for operations as necessary increase flexibility and can reduce costs. Allen-Bredley Company found that its highly automated assembly line increased flexibility, albeit at a cost of lower output. Yet the flexibility was seen as a higher-order priority than output, one that was essential to Allen-Bradley's future competitive ability.

POM is a crucial functional area in implementing strategies. Traditionally, marketing and POM have been rivals. But they must coexist and work together, and their tasks must be coordinated through appropriate policies and plans, if any strategy is to work.

POM operating strategies must be coordinated with marketing strategy if the firm is to succeed. Careful integration with financial strategy components (such as capital budgeting and investment decisions) and the personnel function are also necessary. Exhibit 13.6 helps illustrate the importance of such coordination by showing the different POM concerns that arise when different marketing/financial/personnel strategies are required as elements of the grand strategy.

Possible elements of strategy	Concomitant conditions that may affect or place demands on the operations function
1. Compete as low-cost provider of goods or services	Broadens market. Requires longer production runs and fewer product changes. Requires special purpose equipment and facilities.
2. Compete as high-quality provider	Often possible to obtain more profit per unit, and perhaps more total profit from a smaller volume of sales. Requires more quality-assurance effort and higher operating cost. Requires more precise equipment, which is more expensive. Requires highly skilled workers, necessitating higher wages and greater training efforts.
3. Stress customer service	Requires broader development of service people and service parts and equipment. Requires rapid response to customer needs or changes in customer tastes, rapid and accurate information system, careful coordination. Requires a higher inventory investment.
4. Provide rapid and frequent introduction of new products	Requires versatile equipment and people. Has higher research and development costs. Has high retraining costs and high tooling and changeover in manufacturing. Provides lower volumes for each product and fewer opportunities for improvements due to the learning curve.
5. Strive for absolute growth	Requires accepting some projects or products with lower marginal value, which reduces ROI. Diverts talents to areas of weakness instead of concentrating on strengths.
6. Seek vertical integration	Enables company to control more of the process. May not have economies of scale at some stages of process. May require high capital investment as well as technology and skill's beyond those currently available within the organization.
7. Maintain reserve capacity for flexibility	Provides ability to meet peak demands and quickly implement some contingency plans if forecasts are too low. Requires capital investment in idle capacity. Provides capability to grow during the lead time normally required for expansion.
8. Consolidate processing (centralize)	Can result in economies of scale. Can locate near one major customer or supplier. Vulnerability : one strike, fire, or flood can halt the entire operation.
9. Disperse processing of service (decentralize)	Can be near several market territories. Requires more complex coordination network : perhaps expensive data transmission and duplication of some personnel and equipment at each location. If each location produces one product in the line, then other products still must be transported to be available at all locations. If each location specializes in a type of component for all products, the company is vulnerable to strike, fire flood, etc. If each location provides total product line, then economies of scale may not be realized.
10. Stress the use of mechanization, automation, robots	Requires high capital investment. Reduces flexibility. May affect labor relations. Makes maintenance more crucial.
11. Stress stability of employment	Serves the security needs of employees and may develop employee loyalty. Helps to attract and retain highly skilled employees. May require revision of make-or-buy decisions, use of ideal time, inventory, and subcontractors as demand fluctuates.

Exhibit 13.6: Operations Management Concerns Associated with Different Elements of a Strategy.

Functional Strategies in Personnel

The strategic importance of functional strategies in the personnel area has become more widely accepted in recent years. Personnel management aids in accomplishing grand strategy by ensuring the development of managerial talent, the presence of systems to manage compensation and regulatory concerns, and the development of competent, well-motivated employees. Functional strategies in personnel should guide the effective utilization of human resources to achieve both the annual objectives of the firm and the satisfaction and development of employees. These strategies involve the following areas:

Employee recruitment, selection, and orientation.

Career development and counseling, performance evaluation, and training and development.

Compensation.

Labor/union relations and Equal Employment Opportunity Commission (EEOC) requirements.

Discipline; control, and evaluation.

Operating strategy for recruitment, selection, and orientation guides personnel management decisions for attracting and retaining motivated, productive employees. This involves such questions as : What are the key human resource needs to support a chosen strategy? How do we recruit for these needs? How sophisticated should the selection process be? How should new employees be introduced to the organisation? The recruitment, selection, and orientation component of personnel strategy should provide basic parameters for answering these questions.

The development and training component should guide personnel actions taken to meet future human resource needs of the grand strategy. Merrill Lynch, a major brokerage firm, has a long-term corporate strategy of becoming a diversified financial service institution. In addition to handling stock transactions, Merrill Lynch is actively moving into such areas as investment banking, consumer credit, and venture capital. In support of these far-reaching, long-term objectives, Merrill Lynch has incorporated extensive early-career training and ongoing career development programs to meet its expanding need for personnel with multiple competencies.

Functional strategies in the personnel area are needed to guide decisions regarding compensation, labor relations, EEOC requirements, discipline, and control to enhance the productivity and motivation of the work force. Involved are such concerns as; What are the standards for promotion? How should payment, incentive plans benefits, and seniority policies be interpreted? Should there be hiring preference? What are appropriate disciplinary steps? These are specific personnel decisions that operating managers frequently encounter. Functional strategies in the personnel area should guide such decisions in a way that is compatible with business strategy, strategies for other functional areas, and the achievement of annual objectives..

Perhaps one of the most difficult decisions regarding personnel occurs when a firm is pursuing a retrenchment strategy. At these times, questions usually include whether or not to lay off or terminate employees, how many, and who. Again, union contracts may establish some kind of policy here (resulting from earlier negotiations where a previous policy was laid down). But a firm may also attempt to protect labor and seek a shortened workweek or maintain the level of production for a time. Such policies relate to those in production and finance. A related matter is the relative proportion of managers and workers in the line and staff functions. Several writers have suggested that the policies of many firms have stressed placing the brightest and best people in staff functions at the expense of the line, which does the basic work. This has been blamed for declining productivity, inadequate plant investment, marginal quality standards, and the like. As a result, many firms have begun a streamlining program by cutting the corporate level and other staff levels. Their goal is to pare overhead costs and gain some control over unwieldy, top-heavy structures. Of course, such trade-offs must be made with other objectives and considerations in mind.

Some firms incorporate a long-term human resource plan as an integral component of the strategic plan. Human resources managers have become an integral component in the strategic management activity, particularly as firms engage in mergers or major retrenchments requiring significant changes in the work force. Thus requires forecasts of human resource needs (labor and management) in conjunction with other changes going on in the planning effort.

Doug Hall and Judith Richter emphasize that human resource managers need to foster more effective balancing of professional and private lives, since nearly 50 million people in the United states are now part of two-career families. A corporate objective to become more "lean and mean" must today include consideration for the fact that a good home life contributes immensely to a good work life.

"You can count on baby-boomers to force the issue of family versus work onto the corporate agenda. Fully 73 percent of all women age 25 to 34 now work for pay, as do half of all women with babies under a year old. For them and their husbands, child care, flexible hours, and job sharing are pressing concerns".

The work/family issue is no longer just a "women's problem." Some specific measures that firms are taking to address this issue are providing spouse relocation assistance as an employee benefit, providing company resources for family recreational and educational use, establishing employee country clubs, such as those at IBM and Bethlehem Steel, and creating family/work interaction opportunities.

Some organizations have developed "family days," when family members are invited into the workplace, taken on plant or office tours, dined by management, and given a chance to see exactly what other family members do each day. "Family days" are inexpensive and increase the employee's pride in working for the organization. *Flexible working hours* during the week is another human resource response to the need for individuals to balance work life and home life. The work/family topic is being made part of the agenda at meetings and thus is becoming "discussable" in many organizations.

Research indicates that employees who are *dissatisfied with childcare arrangements* are most likely to be absent or unproductive. Lack of adequate childcare in a community can be a deterrent in recruiting and retaining good managers and employees. Some benefits of on site childcare facilities are improved employee relations, reduced absenteeism and turnover, increased productivity, enhanced recruitment, and improved community relations.

A recent survey of women managers revealed that one-third would have their present employer for another employer offering childcare assistance. The conference Board in 1989 reported that over 500 firms in the United States had created on-site or near-site childcare centres for their employees, including Merck, Campbell Soup, Hoffmann-La Roche, Stride-Rite, Johnson Wax, CIGNA, Champion International, Walt Disney World, and Playboy Resorts.

Other common childcare service arrangements include employer-sponsored day care, childcare information, and referral services. IBM, Steelcase, Honeywell, Citibank, 3M, and Southland have established contracts with third-party childcare information and referral services.

The nation's largest employer sponsored day-care center is operated by Intermedics, a Texas-based medical instruments firm. Employee turnover declined 23 percent the first year Intermedics instituted the centre. In Virginia, twenty-two companies recently pooled \$100,000 to establish a parent-run childcare cooperative. Other companies that effectively address childcare concerns of managers and employees include Clorox, American Express, and Nyloncraft.

At least 10,000 U.S. employers now offer programs to improve or maintain their employees' health, such as programs to stop smoking, reduce cholesterol, promote regular exercise, and control high blood pressure. Another 1,000 American firms offer on-site, fully equipped fitness centres to promote good employee health. Perhaps the leader in this area is Johnson & Johnson, which provides an 11,000-square-foot fitness center, aerobics and other exercise classes, seminars on AIDS and alcohol abuse, and an indoor track. J & J's program is called "Live for Life."

Policies and plans with respect to all the functions of a firm normally involve some questions of legality. For instance, a merger strategy to be implemented through the purchase of a competitor involves legal questions. A marketing policy to give exclusive territories to distributors may involve legal issues. Securing favorable price breaks on large purchases of materials or hiring certain classes of employees for the executive ranks also involves legal issues, and so on. Some firms may pursue a policy for the purpose of testing a legal issue, as Sears did when it challenged the Equal Employment Opportunity Commission. Other executives may delay implementing plans until "advice of counsel" is sought as to the legal ramifications of pursuing a given strategy in a certain way. Of course, implementing a strategy by moving into international territories compounds the difficulties and introduces the question of whether policies need to be established that are common to all SBUs or whether autonomy is to be granted to suit local conditions. The legal ramifications may have a great deal to do with a firm's policy on organizing such units. More firms appear to be increasing the size of in-house legal departments as problems connected with product liability, employee health and safety, employment practices, pollution problems, and so on have grown.

Once the legal issues are explored, there are still policy issues involved. In essence, a firm may have a policy of "let's follow the letter of the law," "let's follow the spirit of the law," or "let's test the law (if we're willing to pay the possible consequences)." Depending on the importance of the issue, the risks involved, and the values of management, these options are more or less likely for a given situation. The role of the legal staff is to lay out the implications so that managers can make a decision. Unfortunately, some manager let their lawyers determine policies them selves, and this can lead to the "tail wagging the dog."

Somewhat related to policies concerning legal issues is the whole area of social responsibility. Policies in this area remain quite nebulous. A whole variety of issues can be involved, including advertising ethics, bribing government officials (foreign or domestic), and corporate philanthropy. Like legal policies relations policies can cut across all the functional areas. There may be ethical questions in developing certain areas of research (such as research on DNA) or in selling products that are unsafe to certain types of consumers (such as infant formula in Africa). Of course, some production processes may be designed to use state-of-the-art technology to prevent pollution, or there may be an option to continue the legal dumping of dangerous chemical wastes. The list of issues seems to be endless. As a result, the public affairs-government relations function has grown increasingly important, more staff members and resources are being allocated to this office, and more authority to make policies had been granted.

Policies here have an impact on the image the organization wishes to present. But some can also be seen as necessary to protect long-term economic interests. For example, many firms operating in South Africa under conditions of apartheid face critical policy questions. Thus some firms may choose to encourage employee participation in community activities, involve themselves in political action committees (PACs), or provide financial support for community development projects. In many instances, these policies may be a way to 'manage the environment.' Remember, strategies can be active or passive. More firms these days appear to exercise active approaches to influencing their environment to create opportunity or avert threat. In addition to involvement with PACs the public relations staff or high-level executives will monitor the progress of pieces of legislation in federal or state capitals. This involves watching committee assignments for bills, noting hearing schedules for bills of interest, and determining the action to be taken on each bill (testimony at hearings, speaking with committee members, attending the hearing, briefing key legislators regarding the issues, etc.).

Of course, the degree to which a firm attempts to exercise "influence" requires a policy on how far legal limits are to be stretched (e.g., should bribery be overlooked). This is a particularly difficult problem for the international firm. Should it behave as a change agent, or adapt to local customs? Should it follow the adage "When in Rome do like the Home Office"? The usual prescription is to strike a balance of constructive interaction, but this is often easier said than done.

When all line and staff functions have developed plans and policies to aid implementation of the strategic choice, implementation is not necessarily complete. There is a need to be sure that there is internal consistency in the policies and plans developed for the line and staff. And these need to be related to the assessment of the role of strengths and weaknesses as they relate to the development of competitive advantage. Let's consider an example to illustrate this key point.

Suppose that a furniture manufacturer pursues marketing plans calling for a narrow product line, a low price, and broad distribution. Various policies would probably include decentralized storage of finished goods, large-lot-size production, a low-or medium-skilled work force, and a limited number of large-scale plants.

On the other hand, a manufacturer of high-priced, high-style furniture sold through exclusive distributors might call for production to order, many model and style changes, well-trained and highly paid workers and supervisors, etc. While the operations and labor costs and policies in the second case might be seen as less efficient and a relative weakness, nonetheless they are consistent with and effective for the chosen strategy. If the manufacturer attempted to follow the usual prescriptions for "efficient" production (large-scale mass production of items), it probably would not be effective in carrying out its strategy.

As we discussed each area earlier, you may have noted that effective decisions cannot be made without regard to their impact on other areas of the business. Otherwise, suboptimization is likely to result. Trade-offs are generally required in this process. A policy of minimizing the inventory may come at the expense of satisfying customers. Exhibit 13.7 shows some of the common trade-offs occur across areas as well.

Hence, top executives must be involved with negotiations and policy formulation to assure that the plans that are developed are working together to accomplish the key tasks needed to carry out a given strategy. The extent of involvement needed relates to the strategy itself. Consider, for instance, the need to link R& D, production, and marketing departments. If the strategy is to develop and produce products for specific customer needs, there will be a greater need to coordinate the activities of the three departments than if a “push” strategy in marketing is in use (selling whatever products are developed and produced). An example of this is Ford’s “Team Taurus.” Normally, the 5-years process of creating a new automobile is sequential—product planners define a concept, the design team takes over, and then engineering develops specifications that are passed on to manufacturing and suppliers. Such an approach was creating problems at Ford. The Team Taurus approach put together a group from planning, design, engineering, and manufacturing at the beginning of the process. The group asked assembly-line workers and suppliers for their ideas, at the same time doing extensive market research and back engineering on competitors’ products to identify customer-desired features. Such integration was seen as necessary if Ford was to compete with foreign automakers.

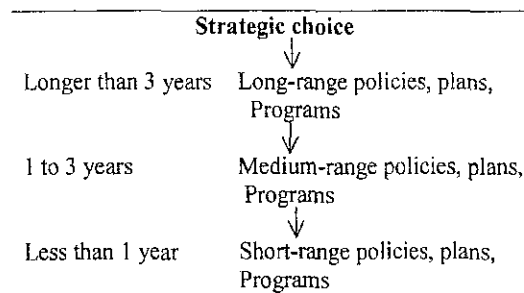
Policy area	Decision	Alternatives
Plant and equipment	Span of process Plant size Plant location Investment decisions Choice of equipment Kind of tooling	Make or buy One big plant or several smaller ones Locate near markets or locate near materials Invest mainly in buildings or equipment or inventories or research General-purpose or special-purpose equipment Temporary, minimum tooling or “production tooling”
Production planning and control	Frequency of inventory taking inventory size Degree of inventory control What to control Quality control Use of standards.	Few or many breaks in production for buffer stocks High inventory or a lower inventory Control in great detail or in lesser detail Controls designed to minimize machine downtime or labor cost or time in process, or to maximize output of particular products or material usage High reliability and quality or low costs Formal or informal or none at all
Labor and staffing	Job specialization Supervision Wage system Supervision style Industrial engineers	Highly specialized or not highly specialized Technically trained first-line supervisors on non technically trained supervisors Many job grades or few job grades; incentive wages or hourly wages Close supervision or loose supervision Many or few
Product design/engineering	Size of product line Design Stability Technological risk Engineering Use of manufacturing engineering	Many customer specials or few specials or none at all Frozen design or many engineering change orders. Use of new processes unproved by competitors or follow-the-leader policy Complete packaged design or design-as-you-go approach Few or many manufacturing engineers
Organization and management	Kind of organization Executive use of time Degree of risk assumed Use of staff Executive style	Functional or product focus or geographical or other High involvement in investment or production planning or cost control or quality control or other activities Decision based on much or little information Large or small staff group Much or little involvement in detail; authoritarian or nondirective style, much or little contract with organization

Exhibit 13.7: Some Important Trade-off Decisions in Various Policy Areas

If the business is highly capital-intensive with high manufacturing costs, then a stronger linkage between R&D and manufacturing is likely to be helpful for developing cost-saving process improvements. The idea is that policies can be developed to encourage the organization to maintain a desired liaison across units to effect the communication and coordination needed. In some instances, specialized formal units (e.g., expeditors) may be set up in the organization to facilitate this coordination. The management information system may be used here for coordination and control.

The timing of these plans and policies must be designed so that they mesh correctly. For instance, a number of computer companies attempted to rush into new products with marketing programs promising more than could be delivered. Customers were anxiously awaiting the arrival of their new machines before production was capable of providing the necessary output. So lead times within each area of the business need to be considered in relation to one another before plans are implemented. Further, some policy decisions can be made and implemented immediately (e.g., change from LIFO to FIFO, hire unskilled workers). Others take long lead times to come to fruition (e.g., research and development, building new plants). For example, Genentech had a plant whereby it would hire sales force personnel contingent on approval of a new drug by the FDA, which takes some time.

Thus, in effect, firms create a cascade of plans and policies, with the long-range choices affecting medium- and short-range decisions.



Policies also vary over time, shifting with strategic needs. One interesting perspective sheds some light on what may be one way to determine how plans need to change with certain strategies. Fox has shown how implementation will vary depending on where the firm's main product or service is in the product-service life cycle. Exhibit 13.8 presents his framework. Of course, a multiple-SBU firm may have a number of products, each of which is in a different stage of development. Hence specific guidelines are subject to some question as to their overall usefulness. Nonetheless, the exhibit does illustrate how policies can be meshed with different demands imposed by a strategy change.

Finally, it should be remembered that if contingency planning or second-generation planning is being used, alternative functional policies for each contingency plan must be developed.

These and many other functional plans and policies are needed to implement the grand strategy. Your ability to formulate these will be a good indication of your practical ability to make the strategy work. Research suggests that the success of a firm's strategy is dependent on proper implementation and balancing of resources, plans, and policies.

	Functional focus	R & D	Production	Marketing	Physical distribution
Precommercialization	Coordination of R&D and other functions	Reliability tests Release blueprints	Production design Process planning Purchasing department lines up vendors and subcontractors	Test marketing Detailed marketing plan	Plan shipping schedules, mixed carloads Rent warehouse space, trucks
Introduction	Engineering; debugging in R&D production, and field	Technical corrections (engineering changes)	Subcontracting Centralize pilot plants; test various processes; develop standards	Induce trial; fit pipelines; sales agents or commissioned salespeople; publicity	Plan a logistics system
Growth	Production	Start successor product	Centralize production Phase out subcontractors Expedite vendors' output; long runs	Channel commitment Brand emphasis Salaried sales force Reduce price if necessary	Expedite deliveries Shift to owned facilities
Maturity	Marketing and logistics	Develop minor variants Reduce costs through value analysis Originate major adaptations to start new cycle	Many short runs Decentralize Import parts, low-priced models Routinization Cost reduction	Short-term promotions Salaried salespeople Cooperative advertising Forward integration Routine marketing research; panels, audits	Reduce costs and raise customer service level Control finished-goods inventory
Decline	Finance	Withdraw all R&D from initial version	Revert to subcontracting; simplify production line Careful inventory control; buy foreign or competitive goods; stock spare parts	Revert to commission basis; withdraw most promotional support Raise price Selective distribution Careful phase out, considering entire channel	

Personnel	Finance	Management accounting	Other	Customers	Competition
Recruit for new activities Negotiate operational changes with unions	Life-cycle plan for cash flows profits, investments, subsidiaries	Payout planning full costs/revenues Determine optimum lengths of life-cycle stages through present-value method	Final legal clearances (regulatory hurdles, patents) Appoint life-cycle coordinator	Panels and other test respondents	Neglects opportunity or is working on similar idea
Staff and train middle management Stock options for executives	Accounting deficit; high net cash outflow Authorize large production facilities	Help develop production and distribution standards Prepare sales aids, sales management portfolio		Innovators and some early adopters	(Monopoly) Disparagement of innovation Legal and extra-legal interference
Add suitable personnel for plants Many grievances Heavy overtime	Very high profits, net cash outflow still rising Sell equities	Short-term analyses based on return per scarce resource		Early adopters and early majority	(Oligopoly) A few imitate, improve, or cut prices
Transfers, advancements, incentives for efficiency, safety, and so on Suggestion system	Declining profit rate but increasing net cash inflow	Analyze different costs/revenue Spearhead cost reduction, value analysis, and efficiency drives	Pressure for resale price maintenance Price cuts bring price wars; possible price collusion	Early adopters, early and late majority, some laggards; first discontinued by late majority	(Monopoly competition) first shakeout, yet many rivals
Find new slots Encourage early retirement	Administer system; retrenchment Sell unneeded equipment Export the machinery	Analyze escapable costs Pinpoint remaining outlays	Accurate sales forecast very important	Mainly laggards	(Oligopoly) after second shakeout, only few rivals

Exhibit 13.8: Relationship of Implementation to the Product Life Cycle

Operational Implementation

Operation implementation is the approach adopted by an organisation to achieve operational effectiveness. This is the final aspect of strategy implementation. Operation implementation deals with the nitty-gritties of strategy. This is time for action as this is the stage at which the most tangible work gets done. Obviously, the scope of operation implementation would be very wide. It would cover practically everything that is done in an organisation. It is the major task of line managers. Just like a war is won ultimately on the basis of ammunition and supplies rather than grand strategies alone, the success of corporate and business strategies crucially depends on how operational implementation is done and in what way operational effectiveness is achieved.

Porter considers operational effectiveness as necessary but not sufficient to the success of strategy. He explains the term as "performing similar activities better than rivals perform them. Operational effectiveness includes but is not limited to efficiency. It refers to any number of practices that allows a company to better utilize its inputs by, for example, reducing defects in products or developing better products faster".

One of the fundamental objects of the discipline of management has been to show organisations ways to improve their operational effectiveness. While doing so, a number of practices have developed over a period of time. These practices or techniques or methods are derived from concepts, theories, and models, which, in turn, have been sourced from management thoughts and philosophies. There has been a virtual explosion of management philosophies, theories, and practices in the second half of the twentieth century, and the trend continues in the twenty-first century. A majority of these developments relate to the basic issue of improving operational effectiveness. Managers have desperately looked for new philosophies, theories, and practices that can help them in improving operational effectiveness. Often this search has led them to tangible results. Sometimes, though, it has resulted in disappointment.

The scope of operational implementation and operational effectiveness is very wide. Most of you, the readers of this text, are likely to be either students – the (aspiring executives), or middle-level managers. You have learnt about several management practices in the area of strategic management, and in other courses as well. The functional area courses (such as, marketing or finance) and core courses (like, economics or quantitative methods) deal primarily with the techniques, methods, and practices- all meant to help organisations improve operational effectiveness. All these come to the fore during the course of operational implementation. This section would, therefore, not attempt to achieve the impossible, that is, to discuss all the practices in operational implementation. Rather it would attempt to draw your attention to the critical areas of operational implementation and point out some representative practices. For discussing operational implementation, we propose to deal with operational effectiveness in terms of 4-P's: productivity, processes, people, and pace.

The four areas of operational effectiveness that we shall deal with here are of productivity, process, people, and pace. By considering these we hope to cover all the major aspects of operational implementation. All these terms are familiar to you but we reiterate their meaning here to set the tone for further discussion.

Productivity is the measure of the relative amount of input needed to secure a given amount of output. It is frequently expressed mathematically as the ratio of the quantity of output to the quantity of input. Inputs are resources (such as finance, raw materials, machinery and equipments, information, time or management). Outputs are the products and services.

Processes are courses of action used for operational implementation. Processes are often implemented through methods. These methods are systematic and orderly procedures, and consist of sequential steps implemented in a chronological order. The purpose of all processes is to achieve optimum utilization of resources.

People are the stakeholders in the organisation. The significant people are the investors, employees, suppliers, customers. Among these, employees play a direct and central role in operational implementation.

Pace is the speed of operational implementation and is measured in terms of time. Efficiency is the parameter often used to express the pace of operational implementation. Efficiency is the amount of work done (or performance) per unit time.

Observe that these areas of operational effectiveness are not mutually exclusive. A practice that is chosen to achieve productivity adopts a process that is followed by people and is executed at defined pace. What is important is the overall effects achieved, that is, operational effectiveness. This is the reason why horizontal fits is so important to operational implementation.

Next, we shall take up the four areas of operational effectiveness for discussion. But let us clarify two points before we discuss these four areas.

Firstly, we said above that by taking up these four areas we hope to cover the major aspects of operational implementation. Yet the scope of operational implementation is so wide that other aspects may have to be included in practice. For instance, profitability may be an aspect that matter at the level of operational implementation. The several small activities that make up operational implementation contribute to profitability. So some of you might feel that profitability should also be included as an area of operational implementation.

Secondly, within one area we include practices that primarily relate to that area. To some of you it may seem that practice we place in one area should really belong to another area. This is understandable since the integrated nature of operational implementation makes it possible that one practice contributes to more than one area. For instance, a productivity practice may also contribute to better process and it usually leads to faster pace.

The discussion that follows will primarily be in terms of the practices, techniques, and methods used in a particular area. These practices have been proposed from time to time by management theorists, practitioners, and consultants. Each practice is based on a set of concepts, theories and models. And these, in turn, are derived from management thoughts and philosophies. Different thoughts and philosophies have dominated the practice of management at different times. Environmental factors, to a large extent, have been the stimuli for these practices. So, if scientific management held sway over managements practice in the beginning of the twentieth century then the application of information technology assumed greater importance by the close of the millennium. Along the way, we have seen the rise and fall of management practices. We will close this section by referring to this issue. But before we do that let us have an overview of the management practices in the four areas of operational effectiveness. More emphasis shall be laid on the modern practices so that you are able to relate to the role that they play in operational implementation.

Productivity

One of the earliest practices to be adopted for operational effectiveness was that of scientific management, propounded by Frederick Taylor in the beginning of the twentieth century. It focused on the optimum utilisation of resources such as workers, machine, and time. It led to the development of work-study techniques of time and motion study, that are still used extensively in industrial engineering. Operations research techniques came to be used during and after the Second World War. Linear and non-linear programming helped in the development of techniques aimed at optimum utilisation of resources. The 1970s saw computer applications in manufacturing substantially enhancing the productivity of operations. Computer-aided design (CAD) and computer-aided manufacturing (CAM) permitted the resolution of problems that would otherwise not be possible owing to the vast amount of computations involved. The 1980s witnessed the spread of quality and productivity techniques popularized by Japanese firms. The 1990s saw a virtual explosion in terms of techniques and method for productivity improvement. In a large measure, these were motivated by the pressure of Japanese competitive superiority in manufacturing and quality over the American and European firms.

The modern practices of productivity enhancement are an amalgam of the traditional methods, variations made upon the traditional methods, and new methods. Automated assembly lines, for instance, can be seen as an extension of the

scientific management philosophy, aided by computerized manufacturing by computerized numerical control (CNC) machines, and implemented through flexible manufacturing system incorporating cellular manufacturing layout and robotics technology.

The significant modern practices observed here are of just-in-time manufacturing, cycle time reduction, group technology, mass customisation, concurrent engineering and processing, optimized production technology, flexible manufacturing systems, cellular manufacturing, total productive maintenance, and lean manufacturing.

Just-in-time manufacturing (1970s) is a Japanese productivity technique designed to tackle cost reduction from a system wide perspective. It is a comprehensive approach and includes simpler product designs, fewer parts requirements, streamlining of process flows, fewer changes, and reduction of production set-up times. Such a production system requires fewer suppliers who supply small quantities in a perfectly-timed arrangement, resulting in practically no inventory.

Cycle time reduction (1980s) though the concept of cycle time is much older this technique aims at minimising the time taken for the allocated work to be done at each workstation on an assembly line.

Group technology (1980s) is a way of organising and using data for components that make up a number of products that have similar properties and manufacturing requirements. Assimilation of data helps in avoiding duplication of design and manufacturing a variety of products.

Mass customisation (early 1990s) attempts to blend the desirable attributes of mass production and customized production.

Concurrent engineering and processing (early 1990s) involves integrated, simultaneous design of products or services and their related processes, including manufacturing and support. It is intended to involve designer and engineers from time the customer requirements and product concept are defined.

Optimized production technology (1980s) is a computer-based system for planning production, materials requirements, and resource utilisation through focusing on the bottleneck work centers and careful management of materials and resources related to those centers, so that the output is maximised and inventories are reduced.

Flexible manufacturing system (1980s) is a computer-controlled process technology suitable for producing batches of a variety of high quality products quickly. It falls between the traditional high-volume mass production and job-shop type of production systems and retains the advantages of both.

Cellular manufacturing (1980s) is a system where the arrangement of production facility is done in such a manner that the equipment used to make similar parts, or families of parts, are grouped together. This idea seems to be quite close to the traditional concept of process layout-based production system.

Total productive maintenance of Seiichi Nakajima (1984) challenged the traditional concept of maintenance as reactive problem-fixing by a comprehensive system of managing productivity through organisation wide autonomous maintenance done by everyone rather than a department alone.

Lean manufacturing (1990) is based on the thinking that all the stages of manufacturing between sourcing to marketing should be so integrated that a variety of products are produced with minimum resources and at the exact time that they are required.

As a practice for operational implementation, productivity is significant for all types of strategies but is specially relevant for business strategies of cost-leadership, differentiation, and focus. Productivity improvements have a tremendous potential for exercising cost control and effecting cost reduction, resulting in the implementation of cost-leadership strategies. The disaggregation of process, possible through say, flexible manufacturing systems, makes it possible to reap the advantages of mass production, and batch manufacturing makes it possible for the firms to

implement differentiation strategies. Similarly, focus, based either on low-cost or differentiation, is also possible. As you must have noted, most modern productivity improvement techniques attempt to retain the advantages of mass production, that is low cost, with customized production, that is necessary for differentiation to be created.

Processes

Processes have an overwhelming presence in management. The term 'management' is defined in terms of the managerial processes of planning, organising, leading, and controlling. Decision-making in management and strategic management are processes too. The functional areas of marketing, finance, operations, human resource management, and information management operate on the basis of well-established processes. These functional areas have myriad processes, such as, selling, marketing research, budgeting, inventory control, maintenance management, staffing, management development, and informing processing.

The history of management is replete with examples of processes designed to make human work systematic and meaningful. From Henri Fayol's (1916) processing of managerial activities of planning, organising, command, coordination, and control, through Peter Drucker's (1973) enunciation of the practices of management, to the process of knowledge management formalised by Tom Davenport (1998), the quest for processes has been rewarding though tortuous at times.

The modern practices related to processes are several. Among these the major comprehensive processes are business process reengineering, enterprise-wide resources planning, quality management processes, benchmarking, value chain, and supply-chain management.

Quality-management systems (such as total quality management, based on W E Deming's [1986] theory, and total quality control, an empirical Japanese administrative system) aid in the operational implementation of quality management processes. Motorola's six-sigma system (announced in 1994, though its use was made much earlier by the company) of measuring, analyzing, improving, and controlling quality rigorously in processes and subprocesses so that the defect rate is just 3.4 per million units.

Michael Porter's (1980) value-chain analysis- which deals with the set of interlinked value-creating activities performed by an organisation-helps in examining all the activities that a firm performs and how they interact. This could result in process improvements. The concept of value-chain led to the development of several concepts in the 1980s and 1990s.

Business process reengineering, propounded by the Michael Hammer and James Champy (1993), aims at transforming or reinventing organisation for greater efficiency and deals with the fundamental rethinking and redesigning of business processes to achieve dramatic improvements in cost, quality, service, and speed.

Enterprisewide resource planning (ERP of the early 1990s) are software packages that link the isolated information centers into an integrated Enterprisewide structure of functional and activity database. These systems are successors to the material requirement planning (MRP-I) and manufacturing resources planning (MRP-II) systems, long used for planning and scheduling the time-phased material requirements for operations.

Benchmarking (1990s) is the process aimed at finding the best practices within and outside the industry to which an organisation belongs. The purpose of benchmarking is to find the best performance in an area so that one could match one's own performance with them, and even surpass them.

Supply-chain management (1990s) traverse the whole value-chain to manage the procurement of a whole range of inputs that are required to produce a product or service so that the process can be performed in an integrated and optimum manner. Vendors, transporters, and buyers become a part of the firm's value-chain, and the benefits of process improvements and operational effectiveness are shared by all.

Outsourcing (1990s) is a variation of the traditional make-or-buy concept where portions of value-chain activities are commissioned to external suppliers on the basis of economic analysis, so that the firm's own focus remains on its core competence. A related concept is of the modular organisation where the value-stream, down to its components, is broken down and a decision taken to focus on core activities and to outsource rest of the activities to outside agencies who can perform them more efficiently. Here too, the vendors and suppliers are a part of the firm's processing system and the benefits from optimization and operational effectiveness are shared by all.

Processes, as practices for operational implementation, are significant for all types of strategies. Since process improvement is the basic purpose of all new processes, there are several benefits of lower cost, better quality, lesser wastage, lower production time, and higher productivity. So processes are relevant for operational implementation of all types of business strategies. For instance, strategic advantage results from the ability of a company to manage its value-chain in a way that enables it to offer better customer value, thereby making it more competitive. Also, deconstructing value-chains by using supply-chain management and outsourcing makes it possible to offer higher differentiation, as the firm's own facilities are not tied down to mass manufacturing.

People

Nineteenth century management considered people as just a unit of productive labour within and a member of the buying community outside. Operational implementation was all about taking maximum work out of wage-earners and paying them as little as possible. The worker management relation was the master-servant type or, at best, a paternalistic mai-baap connection. The emergence of human relations, industrial sociology, industrial psychology, and the ideas of human behaviour and motivation during the period 1930 through 1960 caused a drastic change in the perception of people as a critical resource. The transformation of labour relations to personnel management and then to human resource management and strategic human resource management is an indication of the change that has taken place with regard to people management.

Operational implementation with regard to people management assumes a wider scope when strategies have to address an extended body of stakeholders. The coverage includes not only the people-the employees- within but also outside, such as, the customer, suppliers, and the society at large. The content of operational implementation, therefore, must take into account activities related to all these stakeholders.

That people factor become a critical contributor to operational effectiveness is indicated by a plethora of terms such as job-enrichment, empowerment, team-building, multiskilling, knowledge-worker, human capital, intellectual capital, organizational learning, and knowledge management related to employees. The focus of competitive strategies and marketing has decidedly shifted in the favour of the customers. Integrative processes, such as supply-chain management, include suppliers as a part of the organizational system. And issues, such as, corporate governance, ethics and values, and social responsibility, widen the concerns of people management to adopt operational measures to address a wider audience of stakeholders.

Here we focus on some of the major practices related to people management in the contemporary context.

Strategic recruitment and selection encompasses manpower planning aligned with strategic, scientific selection processes designed on the basis of psychometry to have the right match between employee and job requirements, campus recruitment and internet-based recruitment through job and career websites.

Performance management includes aspects, such as, psychometry testing for placement, carefully designed orientation programmes, flexibility in working hours, application of behavioral sciences in designing motivational systems, building up self-directly teams, empowerment through flatter structures, decentralization and involvement, effective communication skills, negotiation techniques, and career planning and development.

Training and development is done through an increasing emphasis on creativity and innovation, multiskilling, cross-cultural training, and using the principles of organizational learning and knowledge management processes.

Performance appraisal and retention management is done through design and application of formal performance

appraisal, pay-for-performance systems that clearly link performance with rewards, feedback systems, non-monetary incentives, and employee stock option schemes.

Separation management is no longer considered just as retrenchment and paying the dues stipulated under the law. Exit interviews, early retirement schemes, sabbaticals, voluntary retirement schemes, and outplacement services are becoming the norm as many companies are downsizing.

Besides the people within, companies are also focusing on customers through customer survey and feedback, market research, relationship marketing, and customer relationship management. Investors are provided with better information through transparent disclosures and aesthetically-designed corporate annual reports. They are also treated to special discount schemes for the company's product and services. Companies are becoming more socially responsive to the ultimate stakeholder-the society-by engaging in innovative social development programmes. Emphasis is placed on building up reputation and there is more openness and transparency in providing better service and more information.

As can be seen, people management offers a wide scope for enhancing operational effectiveness.

Pace

The final area that we take up for discussion is the pace. By this is meant the speed of operational implementation. The area is important since time is now recognized as being of essence to strategy implementation. In terms of value-chain, pace can be seen as performing every activity faster than the rivals so that strategic advantage results. Operational implementation makes it possible to speed up activities.

Time study was proposed by Taylor and his associates as early as 1900 in order to analyse the sequence of production work to identify wastage and to build up more efficient process. For most part of the early twentieth century, the traditional techniques prevailed and several of them are still in use.

The nature of managerial work was studied by Mintzberg (1973). While researching on how managers actually spend their time he found that they engage in bursts of activities interspersed by interruptions. This led to a greater understanding of how sub optimal utilisation of times takes place within organisations.

Network analysis and activity charts (1970s), successors to Gantt charts of 1901, have been popular technique to optimize time and resource allocation by focussing on the critical path. Timely project execution is seen as a source of saving on cost overruns.

Time-based management (late 1980s), including time-based competition (1990s), are ideas that have been advanced to illustrate the point that time can be used as a strategic weapon. First-movers in competitive markets are assumed to gain advantages not available to late-movers.

Time management (1980s) has emerged as a significant practice to increase productivity and efficiency. Most productivity and process related practices also result in time-saving. Organizational mechanisms such as delegation are preferred as they enable managers to focus on critical activities through 'management by exception' or the 80-20 principle. Technology support has made it possible to use time-saving devices. But, by far, the most significant technology that quickens the pace of operational implementation is IT. What is remarkable about computers and IT is that almost all the developments have taken place in the second half of the twentieth century prompting some people to call this period as the information age and the economy as the knowledge economy. Workers are now knowledge-workers, since most people within an organisation are involved in some aspect of information management.

Information management is the branch of management that deals with the collection, processing, storing, and disseminating of information for the purpose of managerial decision making.

Information system is a system in which data flow takes place between people and organisational unit, such as, departments and functions. From simple transaction processing system, the developments in information system have led to management reporting system, decision support system, group support system, executive support system, and export support system.

Information technology constitutes the hardware and software that is used in information systems. Embedded information technology is IT that is integrated with the other components, such as, products and services. Knowledge based products or services are called as such because their function and performance are embedded within them.

The first-order information systems are the single-user systems in applications, such as, electronic spreadsheets for automation and analysis of record-keeping, database management systems for managing data productivity, multimedia presentation for integration of data formats of text, sound, image, animation, and video. The second-order information systems are the multiuser and network systems that use telecommunications technology with IT resulting in applications such as electronic mail (e-mail), voice mail, video-conferencing, work-group conferencing, electronic bulletin boards, electronic funds transfer, electronic data interchange and electronic commerce. The potential of convergence of IT, telecommunication, and consumer electronics technology is being realised in the form of greater interactivity.

The implications of the developments in information management are mind-boggling and exciting for operational implementation. IT is augmenting immensely the capability of organisations to enhance their operational effectiveness. The most significant benefit is in terms of the speed of processing and dissemination of data, an aspect of what we refer to as pace here. Several of practices that we refer to in this section- such as, flexible manufacturing systems, ERP or knowledge management-have been possible through the application of IT. It is obvious, therefore, that pace is of immense practical values for all types of strategies.

Given such a wide array of practices, methods, and techniques for enhancing operational effectiveness in the areas of productivity, processes, people, and pace, the managers have a difficulty in choosing which of these to pick up to use in operational implementation. The choice is made even more difficult owing to factors, like the credibility of the originators of these practices, who are often high-profile management consultancy firms or respected academician-consultants. And many of these are global consultancy firms and global management gurus. They make presentations so effectively in conjunction with a blitzkrieg of publicity in the business media that the power of their technique seems to be overwhelming. Managers in firms often fall for techniques and choose those indiscriminately. Disappointment results and soon the technique is termed as a fad not worth using. Several management techniques have risen like a phoenix and then have bitten the dust. Managers, possibly in their desperate search for a panacea for organisational ills, opt for the latest technique and then find that it does not work. This is not a correct approach. The malady often does not lie with the technique but in the way it is chosen and applied.

Managers need to derive the areas of improvements from the requirements of the strategy that they are implementing. Organisational analysis can serve as a starting point for identifying the areas where functioning needs to be improved. Having done that, the technique can then be chosen and applied. After all, continuous improvement is the ultimate goal of all implementation as encapsulated in the Japanese concept of kaizen.

It is important to remember that any technique has a history, background, context, and requirements. A technique cannot be applied blindly. There are essential prerequisites to applying a technique and then there are the consequences. A proper understanding of all these aspects is necessary in applying a technique. For instance, supply-chain management cannot be applied if the supplier-company relationship is not congenial, the cost of implementation is prohibitive, the quality of products needs improvement, the speed of work within the organisation is suboptimal, and there is no flexibility of operations. Then support systems, such as, an information system with adequate inputs of IT, are required for the application of supply-chain management to be feasible.

There is enough information available regarding the management principles, theory, concepts, and models working behind a technique. On the one hand, managers need to be aware of these to enhance their understanding and gain a comprehensive assessment of the usage of a technique. On the other, managers need to have an in-depth understanding of their organisation. A match of what the organisation needs and what the technique has to offer has to be made.

The application of techniques is facilitated with the help of books and journals, manuals, in-house experts, and consultants related to the management techniques. A dedicated and patient approach can help managers in applying the practices, methods, and techniques for enhancing operational effectiveness and effective operational implementation.

Chapter 14

Strategic Evaluation and Control

There are three primary types of organizational control: strategic control, management control, and the operational control. Strategic control, the process of evaluating strategy, is practiced both after strategy is formulated and after it is implemented. The organization's strategists evaluate strategy once it has been formulated to ascertain whether it is appropriate to mission accomplishment and again once it has been implemented to determine if the strategy is accomplishing its objectives.

Management control is the process of assuring that major subsystems progress towards the accomplishment of strategic objectives is satisfactory. For example, is SBU/Product Division A's ROI performance acceptable? Or, is the production Department meeting its quality control objectives? Operational control is the process of ascertaining whether individual and work group role behaviors (performance) are congruent with individual and work group role prescriptions. For example, is Rama reaching his sales quota?

Like the phase of planning, the types of control are not distinct entities. Rather, in various organizations, one type of control may be almost indistinguishable from another. Furthermore, the devices used in one type of control may also be employed in another. For example, management control devices such as ROI may be used to measure not only the performance of organizational components but the total organization as well. Finally, while most operational and many management control systems may possess automatic correction activities. The evaluation of strategy requires executive judgment.

Strategic, management, and operational control systems perform an important integrative function. The measurement of performance as related to objective accomplishment coordinates activity. Experience and research have revealed that any number of variables may cause performance to be incongruent with strategy. For example, the assumptions under which strategy was formulated may change. Or, strategy, plans, and policies may not be adhered to. Deviations from either assumptions or guidance lead to unsatisfactory results. Therefore, the successful strategy must have control as one of its dimensions.

What is controlled varies from level to level in the organization. The organization strategists are responsible for strategic control, as are the stockholders, theoretically. Management control is principally the function of top management, especially the CEO. Operational control is primarily the concern lower-level managers. Strategic control and management control are concerned with perspectives broader than the details dealt with in operational control. Note, however, that "war" rooms and strategic information systems allow top management to view the details of operations if necessary. While much of what follows is related to formal control systems, informal control systems may suffice in a smaller organization, especially for operational control where personal observation is possible.

Control may be depicted as a six-step feedback model as follows:

1. **The establishment of standards of performing:** Standards are specific points against which actual performance will be judged. As such they are more detailed expressions of Strategic objectives and are the bases of role prescriptions. Establishing standards for organizational subcomponents is the first step in management control and establishing them for individuals is the first step in operational control.

2. **The statement of acceptable tolerances:** The standard is a single point on a continuum of possible behaviors, but it is not always necessary to perform exactly to that point. Normally, deviation from standards will be tolerated within certain control limits.
3. **Measurement of actual performance:** Measurement is the third step in management or operational control. It involves the identification of role behavior either for components of individuals. Measurement techniques vary from situation to situation and are often imprecise.
4. **Comparison of standards and performance:** While comparing standards and performance might appear to be a simple task, it is quite complex in the more qualitative performance areas because of the inability to quantify either standards or performance.

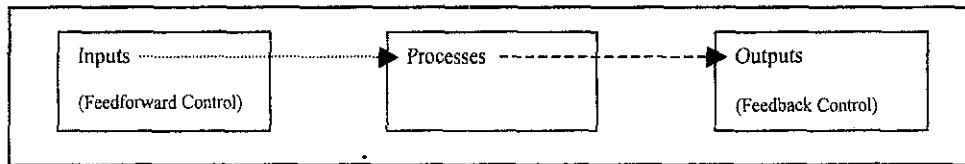


Exhibit 14.1: The Organization as a Processing System

5. **Action:** Where performance is satisfactory- that is, congruent with standards- no action is necessary. But where it is not, corrective action must be taken.
6. **Preventive action:** As Bill Greenwood has observed, it is insufficient simply to correct problems. Rather, action must be taken to assure these problems do not occur again.

This model focuses on results (output). In fact, most control systems- strategic, management, or operational- focus on results. Often, the consequence of utilizing these feedback control systems is that the unsatisfactory performance continues until the malfunctioning is discovered. One technique for reducing the problems associated with feedback control system is "feedforward control". First suggested by Harold Koontz and Robert W. Bradspies, feedforward control focuses on the inputs to the system and attempts to anticipate problems with outputs (see exhibit 14.1)

With respect to strategy and planning, feedforward control has wide applicability. For example, the feedforward principle underlies the concept of simulation modeling. "What if" question are, after all, examinations of hypothesized inputs to determine resultant effects on system outputs. Simulations of performance can be made in any number of Strategic situations to test for changes in basic assumptions. In fact, any situation with identifiable inputs which can be modeled can and should utilize the feedforward approach.

Once strategy has been formulated, it should be evaluated. Several criteria for evaluation have been suggested. The best known of these, the Tilles model, can be summarized as follows :

1. Is the strategy internally consistent- for example, is it consistent with mission and consistent among its own plans?
2. Is it consistent with the environment?
3. Is it consistent with internal resources?
4. Does it have an appropriate amount of risk?
5. Does it have a proper time horizon?
6. Is it workable?

E.P. Learned and others, building on the Tilles model, suggest that the following are also proper evaluative questions:

7. Is it identifiable? Has it been clearly and consistently identified and are people aware of it?
8. Is it appropriate to the personal values and aspirations of key managers?
9. Does it constitute a clear stimulus to organizational efforts and commitment?
10. Is it socially responsible?
11. Are there early indications of the responsiveness of market segments to the strategy?

J. Argenti adds:

12. Does it rely on weaknesses or do anything to reduce them?
13. Does it exploit major opportunities?
14. Does it avoid, reduce, or mitigate the major threats? If not, are there adequate contingency plans?

Intuitively, these questions seem sound. More importantly, they relate directly to the strategic management process model. In fact, these questions, when considered in total, comprise a checklist to determine if the strategic management process model has been properly followed. All these questions can be applied as the strategy progresses through its various stages, including implementation. Progress and changes can thus be observed. Specific standards of performance are established by the strategic objectives of the master strategy and subsequent component objectives.

Once implement occurs, measurements will be taken to determine if the objectives have been reached. The tolerances established in Step 2 of the six-step feed back model vary from firm to firm. Tolerances are primarily judgmental—they tell how much deviation from the standard management can live with. Corrective and preventive action may require that strategy be changed.

Management control becomes a distinct concern when decentralization occurs. Where management control is imposed, it functions within the framework established by the strategy. Management control focuses on the accomplishment of the objectives of the various substrategies comprising the master strategy and the accomplishment of the objectives of the intermediate plans. Normally these objectives (standards) are established for major subsystems within the organization. Such as SBUs, projects, products, functions, and responsibility centers. Allowable tolerances vary from organization to organization. Typical management control measures include ROI, residual income, cost, product quality, efficiency measures, and so forth. These control measures are essentially summations of operational control measures. When corrective or preventive action is taken, it may involve very minor or very major changes in the strategy. Often, top management strategists may be removed from their positions as the consequence of poor performing as indicated by these control measures. One large firm has a policy for its European operating division managers: "Two consecutive quarters of declining ROI and you're fired!" Often, critical decisions for a company's future result from rather imperfect control information.

Operational control systems are designed to ensure that day-to-day actions are consistent with established plans and objectives. Operational control is concerned with individual and group role performance as compared with the individual and group role prescriptions required by organizational plans. Such control systems are normally concerned with the past (unless feedforward systems are being utilized). Operational control focuses on events in a recent period. Operations control systems are derived from the requirements of the management control system. Specific standards for performance are derived from the objectives of the operating plans, which are based on intermediate plans, which are based on strategy. Performance is compared against objectives at the individual and group levels. Corrective or preventive action is taken where performance does not meet standards. This action may involve training, motivation,

leadership, discipline, or termination.

It is important to know who the participants are and what role they will play in strategic evaluation and control. This will answer the question: who evaluates the strategy and how do they do it? Going beyond the role of evaluators, we are also interested in knowing who the appraisers are and how they help in strategic evaluation.

The various participants in strategic evaluation and control and their respective roles are described below.

Theoretically, every organisation is ultimately responsible to its shareholders-lenders and the public in the case of private companies, and the government in the public sector companies. The role of shareholders, in practice, however, is limited. This is specially true of the general public where the individual holding is too small to be of any effective value in strategic evaluation. Lenders such as financial institutions and banks which have an equity stake are typically concerned about the security and returns on their shareholding rather than in the long-term assessment of strategic success. The government, through its different agencies, does play a significant role in the strategic evaluation and control of public sector companies.

The Board of Directors enacts the formal role of reviewing and screening executive decision in the light of their environmental, business and organisational implications. In this way, the board is required to perform the functions of strategic evaluation in more generalized terms. But there is a lot of variation among Indian companies in the way in which the Board may perform its control functions. In some companies, the Board may have the real authority to oversee strategic evaluation, while in other companies its authority may be usurped by other like chief executive or a higher de facto authority, such as the family council, in the case of family-owned companies, the headquarters in the case of MNC subsidiaries, or the controlling ministry in the case of public sector companies.

Chief executives are ultimately responsible for all the administrative aspects of strategic evaluation and control. Ideally, a chief executive should not sit in judgement over the performance of the organisation under his or her control. Rather, the chief executive should be evaluated on the basis of his/her performance. This leads to the question that who should evaluate the chief executive. Normally, the evaluation of a person should be done by an individual or a group to whom he reports. In cases where the chief executive is accountable to no one in particular (this is possible in the case of an entrepreneurial organisation), it is difficult to allocate this responsibility apart from relying on self-evaluation. But in the other cases, the ownership pattern can determine who should evaluate the chief executive. Thus, the family council in family-owned companies and majority shareholders in other cases could evaluate a chief executive's performance.

The SBU or profit-centre heads may be involved in performance evaluation at their levels and may facilitate evaluation by corporate-level executives.

Financial controllers, company secretaries, and external and internal auditors form the group of persons who are primarily responsible for operational control based on financial analysis, budgeting, and reporting.

Audit and executive committees, setup by the Board of the chief executive, may be charged with responsibility of continuous screening of performance. The corporate planning staff or department may also be involved in strategic evaluation.

Middle-level managers may participate in strategic evaluations and control as providers of information and feedback, and as the recipients of directions from above, to take corrective actions. While evaluating organisational units one cannot avoid relying on the performance evaluation of individuals. This creates certain barriers in strategic evaluation and control. We would point out **five major types** of barriers in evaluation: the limits of control, difficulties in measurement, resistance to evaluation, tendency to rely on short-term assessment, and relying on efficiency versus effectiveness.

Limits of control: By its very nature, any control mechanism presents the dilemma of too much versus too little control. It is never an easy task for strategists to decide the limits of control. Too much control may impair the ability of managers, adversely affect initiative and creativity, and create unnecessary impediments to efficient performance. On the other hand, too less control may make the strategic evaluation process ineffective and redundant.

Difficulties in measurement: The process of evaluation is fraught with the danger of difficulties in measurement. These mainly relate to the reliability and validity of the measurement techniques used for evaluation, lack of quantifiable objectives or performance standards, and the inability of the information system to provide timely and valid information. The control system may be distorted and may not evaluate uniformly or may measure attributes which are not intended to be evaluated.

Resistance to evaluation: The evaluation process involves controlling the behavior of individuals and, like any other similar organisational mechanism, is likely to be resisted by managers.

Short-termism: Managers often tend to rely on short-term implications of activities and try to measure the immediate results. Often, the long-term impact of performance on strategy and the extended effects of strategy on performance is ignored. This is so as immediate assessment seems to be the easy way out and taking the long-term implications into account may be seen as too tedious.

Relying on efficiency versus effectiveness: It is instructive to remember that efficiency is 'doing the things rightly' while effectiveness is 'doing the right things'. There is often a genuine confusion among managers as to what constitutes effective performance. Measuring the wrong parameters may lead to a situation where the right type of performance does not get rewarded. In fact, sometimes performance that does not really contribute to the achievements of objectives may be rewarded if assessed on the basis of efficiency alone.

How can these barriers be avoided? In this context, it is apt to quote Andrews when he says: "the true function of measurement (or evaluation) is to increase perceptions of the problems limiting achievement". This is indeed a profound statement. In Andrew's opinion, it is the attitude towards evaluation that is more important than the process of evaluation itself. For instance, bureaucratic control often ends up being control just for the sake of control and not for the real purpose of finding out what is obstructing effective performance. The real worth of evaluation lies in its ability to throw up the problems that are constraining achievement and then doing something about them so that performance can be made effective.

The basic issue in all evaluation should be that control should be dictated by strategy. There needs to be a vertical fit between the strategy requirements, and the evaluation and control exercised over the performance. The guidelines below are suggested in order to make controls effective.

- Control should involve only the minimum amount of information as too much information tends to clutter up the control system and creates confusion.
- Control should monitor only managerial activities and results even if the evaluation is difficult to perform.
- Controls should be timely so that corrective action can be taken quickly.
- Long-term and short-term controls should be used so that a balanced approach to evaluation can be adopted.
- Controls should aim at pinpointing exceptions as nitpicking does not result in effective evaluation. The 80:20 principle, where 20 percent of the activities result in 80 percent of achievement, needs to be emphasized. Getting bogged down with the activities that do not really count for achievement makes the evaluation ineffective.
- Reward for meeting or exceeding standards should be emphasized so that managers are motivated to perform. Unnecessary emphasis on penalties tend to pressurise the managers to rely on efficiency rather than effectiveness.

Strategic Controls

Control of strategy can be characterized as a form of "steering control". Ordinarily, a significant time span occurs between initial implementation of a strategy and achievements of its intended results. During that time, numerous projects are undertaken, investments are made, and actions are undertaken to implement the new strategy. Also during that time, both the environmental situation and the firm's internal situation are developing and evolving. Strategic controls are necessary to steer the firm through these events. They must provide the basis for correcting the actions and directions of the firm in implementing its strategy as developments and changes in its environmental and internal situations take place.

Prudential Insurance Company provides a useful example of the proactive, steering nature of strategic control. Several years ago, Prudential committed to a long-term market development strategy wherein it would seek to attain the top position in the life insurance industry by differentiating its level of service from other competitors in the industry. Prudential decided to establish regional home offices, thus achieving a differential service advantage. Exercising strategic control, prudential managers used the experience at the first regional offices to reproject overall expenses and income associated with this strategy. In fact, the predicted expenses were so high that the location and original schedule for converting other regions had to be modified. Conversion of corporate headquarters was sharply revised on the basis of the other early feedback. Thus the steering control (strategic control) exercised by Prudential managers significantly altered the strategy long before the total plan was in place. In this case, major objectives remained in place while changes were made in the strategy; in other cases, strategic controls may initiate changes in objectives as well.

The four basic types of strategic controls are:

1. Premise control
2. Implementation control
3. Strategic surveillance
4. Special alert control.

The nature of these four strategic controls is summarized in exhibit 14.2.

Premise Control

Every strategy is based on assumed or predicted conditions. These assumptions or predictions are planning premises; a firm's strategy is designed around these predicted conditions. Premise control is designed to check systematically and continuously whether or not the premises set during the planning and implementation process are still valid. If a vital premise is no longer valid, then the strategy may have to be changed. The sooner an invalid premise can be recognized and revised, the better the chances that an acceptable shift in the strategy can be devised.

Premises are primarily concerned with two types of factors: environmental and industry. They are described below.

A company has little or no control over environmental factors, but these factors exercised considerable influence over the success of the strategy. Inflation, technology, interest rates, regulation, and demographic/social changes are examples of such factors. Strategies are usually based on key premises about these factors.

These factors affect the performance of companies in a given industry. They differ among industries, and a company should be aware of the factors that influence success in its particular industry. Competitors, suppliers, substitutes, and barriers to entry are a few such factors about which strategies assumptions are made.

Premises, some major and some minor, are often made about numerous environmental and industry variables. To

attempt to track every premise may be unnecessarily expensive and time-consuming. Therefore, managers must select those premises and variables that (a) are likely to change and (b) would have a major impact on the company and its strategy if they did.

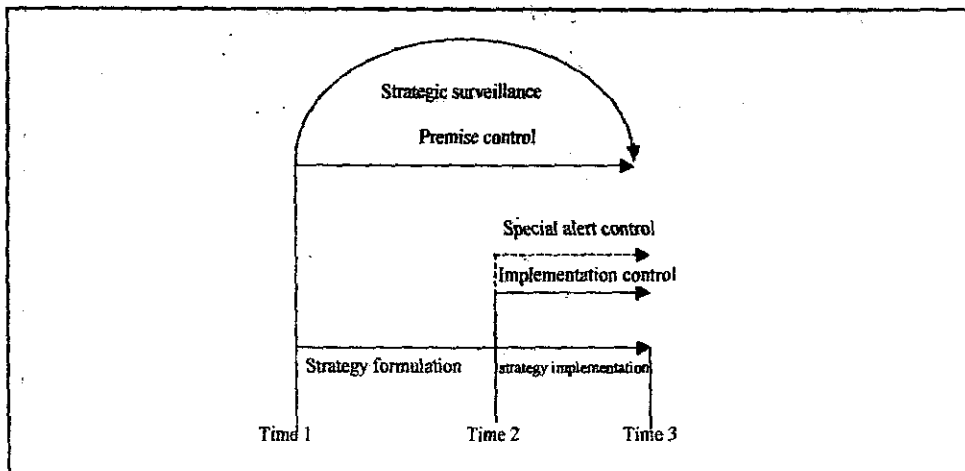


Exhibit 14.2: Four Types of Strategic Control

The key premises should be identified during the planning process. The premises should be recorded, and responsibility for monitoring them should be assigned to the persons or departments who are qualified sources of information. For example, the sales force may be a valuable source for monitoring the expected price policy of major competitors, while the finance department might monitor interest rate trends. All premises should be placed on key success premise so as to avoid information overload. Premises should be update (new predictions) based on update information. Finally, key areas within the company or key aspects of the strategy that the predicted changes may significant impact should be pre-identified so that adjustments necessitated by a revised premise can be determined and initiated. For example, senior marketing executives should be alerted about changes in competitors' pricing policies in order to determine if revised pricing, product repositioning or other strategy adjustments are necessary.

Implementation Control

The action phase of strategic management is located in the series of steps, programs, investments, and moves undertaken over a period of time to implement the strategy. Special programs are undertaken. Functional areas initiate several strategy-related activities. Key people are added or reassigned. Resources are mobilized. In other words, managers convert broad strategic plans into concrete actions and results for specific units and individuals as they go about implementing strategy. And these actions take place incrementally over an extended period of time designed ultimately to enact the planned strategy and achieve long-term objectives.

Strategic control can be undertaken within this context. We refer to this type of strategic control as implementation control. Implementation control is designed to assess whether the overall strategy should be changed in light of unfolding events and results associated with incremental steps and actions that implement the overall strategy. The earlier example of Prudential Insurance Company updating cost and revenue projections based on early experiences with regional home offices is an illustration of an implementation control. The two basic types of implementation control are: (1) monitoring strategic thrusts (new or key strategic programs) and (2) milestone reviews.

Implementing broad strategies often involves undertaking several new strategic projects-specific narrow undertakings that represent part of what needs to be done if the overall strategy is to be accomplished. These projects or thrusts provide a source of information from which managers can obtain feedback that helps determine whether the overall strategy is progressing as planned and whether it needs to be adjusted or changed.

While strategic thrusts seem a readily apparent type of control, using them as control sources is not always easy to do. Early experience may be difficult to interpret. Clearly identifying and measuring early steps and promptly evaluating the overall strategy in light of this early, isolated experience can be difficult.

Two approaches are useful in enacting implementation controls focused on monitoring strategic thrusts. One way is to agree early in the planning process on which thrusts, or phases of those thrusts, are *critical factors in the success of the strategy or of the thrust*. Managers responsible for these implementation controls single these out from other activities and observe them frequently.

The second approach for monitoring strategic thrusts is to use stop/go assessments linked to a series of meaningful thresholds (time, costs, research and development, success, etc.) associated with particular thrusts. Days Inn's nationwide market development strategy in the early 1980s included a strategic thrust of regional development via company-owned inns in the Rocky Mountain area. Time problems in meeting development targets led company executives to reconsider the overall strategy, ultimately deciding to totally change it and sell the company.

Managers often attempt to identify critical milestones that will occur the time period the strategy is being implemented. These milestones may be critical events, major resource allocations, or simply the passage of a certain amount of time. In each case, a *milestone review usually involves a full-scale reassessment of the strategy and the advisability of continuing or refocusing the direction of the company*.

A useful example of strategic implementation control based on milestone review can be found in Boeing's product development strategy to enter the supersonic transport (SST) airplane market. Competition from the joint British/French Concord effort was intense. Boeing had invested millions of dollars and years of scarce engineering talent through phase I of its SST venture. The market was believed large, but the next phase represented a billion-dollar decision for Boeing. This phase was established as a milestone review by Boeing management. Cost estimates were greatly increased; relatively few passengers and predictions of rising fuel costs raised estimated operating costs; the Concord had massive government subsidy, while Boeing did not. All factors led Boeing management to withdraw, in spite of high sunk costs, pride, and patriotism. Only an objective, full-scale strategy reassessment could have led to such a decision. In this example, a major resource allocation decision point provided the appropriate point for a milestone review. Milestone reviews might also occur concurrent with the timing of a new major step in the strategy's implementation or when a key uncertainty is resolved. Sometimes managers may even set an arbitrary time period, say, two years, as a milestone review point. Whatever the basis for selecting the milestone point, the critical purpose of a milestone review is to undertake a thorough review of the firm's strategy so as to control the company's future.

Strategic Surveillance

By their nature, premise control and implementation control are focused control. The third type of strategic control, strategic surveillance, is designed to monitor a broad range of events inside and outside the company that are likely to threaten the course of the firm's strategy. The basic idea behind strategic surveillance is that some form of general monitoring of multiple information sources should be encouraged, with the specific intent being the opportunity to uncover important yet unanticipated information.

Strategic surveillance must be kept unfocused as much as possible and should be designed as a loose "environmental-scanning" activity. Trade magazines, *The Wall Street Journal*, trade conferences, conversations, and intended and unintended observations are all sources of strategic surveillance. While strategic surveillance is loose, its important purpose is to provide an ongoing, broad-based vigilance in all daily operations so as to uncover information that may prove relevant to firm's strategy.

Special Alert Control

Another type of strategic control, really a subset of the other three, is special alert control. A special alert control is the need to thoroughly, and often rapidly, reconsider the firm's basic strategy based on a sudden, unexpected event. A political coup in the Middle East, an outside firm suddenly acquiring a leading competitor, an unexpected product difficulty like Tylenol's experience with poisoned capsules—all of these represent sudden changes that can drastically alter the company's strategy.

Such an occurrence should trigger an immediate and intense reassessment of the company's strategy and its current strategic situation. Many firms have developed crisis teams to handle initial response and coordination when faced with unforeseen occurrences that may have an immediate effect on the firm's strategy. Increasingly, companies are developing contingency plans along with crisis teams to respond to such circumstances.

Exhibit 14.3—summarizes the major characteristics of the four types of strategic controls. While each type of strategic control is different, they share a common purpose: to assess whether the strategic direction should be altered in light of unfolding events. Unlike operational control, strategic controls are designed to continuously and proactively question the basic direction of the strategy.

Operations controls are concerned with providing action control. Strategic controls are concerned with "steering" the company's future direction. Both are needed to manage the strategic process effectively.

Strategic controls are useful to top management in monitoring and steering the basic strategic direction of the company. But operating managers also need control methods appropriate to their level of strategy implementation. The primary concern at the operating level is allocation of the company's resources.

Basic characteristics	Types of strategic control			
	Premise control	Implementation control	Strategic surveillance	Special alerts
Objects of control	Planning premises and projections	Key strategic thrusts and milestones	Potential threats and opportunities related to the strategy	Occurrence of recognizable but unlikely events
Degree of focusing	High	High	Low	High
Data acquisition:				
Formalization	Medium	High	Low	High
Centralization	Low	Medium	Low	High
Use with:				
Environmental factors	Yes	Seldom	Yes	Yes
Industry factors	Yes	Seldom	Yes	Yes
Strategy-specific factors	No	Yes	Seldom	Yes
Company-specific factors	No	Yes	Seldom	Seldom

Exhibit 14.3: Summary Characteristics of the Four Types of Strategic Control

Evaluation Techniques for Strategic Control

The essence of strategic control is to continually assess the changing environment to uncover events that may significantly affect the course of an organisation's strategy. Techniques for strategic control could be classified into two groups on the basis of the type of environment faced by the organisations. The organisations that operate in a relatively stable environment may use strategic momentum control, while those which face a relatively turbulent environment may find strategic leap control more appropriate.

Strategic momentum control: These types of evaluation techniques are aimed at assuring that the assumptions on whose basis strategies were formulated are still valid, and finding out what needs to be done in order to allow the organisation to maintain its existing strategic momentum. There are three techniques which could be used to achieve these aims: responsibility control centres, underlying success factors, and generic strategies.

1. Responsibility control centres form the core of management control systems and are of four types: revenue, expense, profit, and investment centres. Each of these centres is designed on the basis of the measurement of inputs and outputs. The study and application of responsibility centres is done under the discipline of management control systems.
2. The underlying success factors enable organisations to focus on the CSFs in order to examine the factors that contribute to the success of strategies. By managing on the basis of the CSFs, the strategists can continually evaluate the strategies to assess whether or not these are helping the organisation to achieve its objectives.
3. The generic strategies approach to strategic control is based on the assumption that the strategies adopted by a firm similar to another firm are comparable. Based on such a comparison, a firm can study why and how other firms are implementing strategies and assess whether or not its own strategy is following a similar path. In this context, the concept of strategic group is also relevant. A strategic group is a group of firms that adopts similar strategies with similar resources. Firms within a strategic group, often within the same industry, and sometimes in other industries too, tend to adopt similar strategies.

Strategic leap control: Where the environment is relatively unstable, organisations are required to make strategic leaps in order to make significant changes. Strategic leap control can assist such organisations by helping to define the new strategic requirements and to cope with emerging environmental realities. There are four techniques or evaluation used to exercise strategic leap control: *strategic issue management, strategic field analysis, systems modelling and scenarios*.

1. *Strategic issue management* is aimed at identifying one or more strategic issues and assessing their impact on the organisation. A strategic issue is a forthcoming development, either inside or the organisation, which is likely to have an important impact on the ability of the enterprise to meet its objectives. By managing on the basis of strategic issues, the strategists can avoid being overtaken by surprising environmental changes and design contingency plans to shift strategies whenever required.
2. *Strategic field analysis* is a way of examining the nature and extent of synergies that exist or are lacking between the components of an organisation. Whenever synergies exist the strategists can assess the ability of the firm to take advantage of them. Alternatively, the strategists can evaluate the firm's ability to generate synergies where they do not exist.
3. *Systems modelling* is based on computer-based models that simulate the essential features of the organisation and its environment. Through systems modelling, organisations may exercise pre-action control by assessing the impact of the environment on organisation because of the adoption of a particular strategy.
4. *Scenarios* are perceptions about the likely environment a firm would face in the future. Its use could be extended to evaluation by enabling organisations to focus strategies on the basis of forthcoming developments in the environment.

Several of the above techniques for strategic control—with the possible exception of responsibility centres—are of a relatively recent origin. The development of these techniques is an evidence of the expanding body of knowledge in strategic management. As the use and application of strategic management gains approval, it is quite likely that organisations would start using such techniques. Operational control, however, uses more familiar techniques which have traditionally been used by strategists. In the next part of this section, we look at techniques for operational control.

Evaluation Techniques for Operational Control

The classification of evaluation techniques in the three parts: internal analysis, comparative *analysis*, and comprehensive analysis.

Internal analysis: Internal analysis, which consists of value-chain analysis, quantitative (financial and non-financial) analysis, and qualitative analysis, deals with the identification of the strengths and weaknesses of a firm in absolute terms.

1. *Value chain analysis* focusses on a set of inter-related activities performed in a value-chain analysis for the purpose of operational evaluation lies in its ability to segregate the total tasks of a firm into identifiable activities which can then be evaluated for effectiveness.
2. *Quantitative analysis* takes up the financial parameters and the non-financial quantitative parameters, such as, physical units or time, in order to assess performance. The obvious benefit of using quantitative factors (either financial or physical parameters) is the ease of evaluation and the verifiability of the assessment done. These are probably the most-used methods for evaluation for operational control. Among the scores of financial techniques described in all standard texts in the area of finance are traditional techniques, such as, ratio analysis, or newer techniques, such as, economic value-added (EVA) and its variations, and activity-based costing (ABC). These are proven methods so far as their efficacy for evaluating operational effectiveness is concerned. Apart from the financial quantitative techniques, there are several non-financial quantitative techniques available for the evaluation for operational control, such as: computation of absenteeism, market ranking, rate of advertising recall, total cycle time of production, service call rate, or number of patents registered per period. Many more techniques can be evolved by firms to suit their specific requirement.
3. *Qualitative analysis* supplements the quantitative analysis by including those aspects which is not feasible to measure on the basis of figures and numbers. The methods that could be used for qualitative analysis are based on intuition, judgement, and informed opinion. Techniques like surveys and experimentation can be used for the evaluation of performance for exercising operational control.

Comparative analysis: This consists of historical analysis, industry norms, and benchmarking. It compares the performance of a firm with its own past performance, or with other firms.

1. *Historical analysis* is a frequently used method for comparing the performance of a firm over a given period of time. This method has the added benefit of enabling a firm to note how the performance has taken place over a period of time and to analyse the trend or pattern. Such an analysis can offer the firm a better perception of its performance as compared to an absolute assessment.
2. *Industry norms* is a comparative method for analysing performance that has the advantage of making a firm competitive in comparison to its peers in the same industry. Being a comparative assessment, evaluation on the basis of industry norms enables a firm to bring its performance at least up to the level of other firms and then attempt to surpass it.
3. *Benchmarking* is a comparative method where a firm finds practices in an area and then attempts to bring its own performance in that area in line with the best practice. Best practices are the benchmarks that should be adopted by a firm as the standards to exercise operational control. Through this method, performance can be evaluated continually till it reaches the best practice level. In order to excel, a firm shall have to exceed the benchmarks. In this manner, benchmarking offers firms a tangible method to evaluate performance.

Comprehensive analysis: This includes balanced scorecard and key factor rating. His analysis adopts a total approach rather than focussing on one area of activity, or a function or department.

1. *Balanced scorecard* method is based on the identification of four key performance measures of customer perspective, internal business perspective, innovation and learning perspective, and the financial perspective. This method is a balanced approach to performance measurement as a range of parameters are taken into account for evaluation.
2. *Key factor rating* is a method that takes into account the key factors in several areas and then sets out to evaluate performance on the basis of these. This is quite a comprehensive method as it takes a wholistic view of the performance areas in an organisation

Besides the several techniques referred to above, we could mention four other techniques that are used by some companies to assess performance. These are the network techniques, parta system, management by objectives, and the memorandum of understanding.

1. The *parta* system is an indigenous system adopted usually by *Marwari* firms to keep track of daily cash generation. Parta is the pre-determined budget of the net cash inflows from operation before tax and dividend. The parta is decided in between the family group and company head, and actual performance is compared to this budgeted parta on a daily basis, thus making parta an effective operational control device.
2. *Network techniques* such as programme evaluation and review technique (PERT), critical path method (CPM), and their variants, are used extensively for the operational controls of scheduling and resource allocation in projects. When network techniques are modified for use as a cost accounting system, they become highly effective operational controls for project costs and performance.
3. Management by Objectives (MBO) is a system, proposed by Drucker, which is based on a regular evaluation of performance against objectives which are decided upon mutually by the superior and the subordinate. By the process of consultation, objective-setting leads to the establishment of a control system that operates on the basis of commitment and self-control. Thus, the scope of MBO to be used as an operational control is quite extensive.
4. *Memorandum of understanding* Just like MBO is a commitment to objectives between individuals, a memorandum of understanding (MoU) is an agreement between a public enterprise and the Government, represented by the administrative ministry in which both parties clearly specify their commitments and responsibilities. Having done that, the enterprises are evaluated on the basis of the MoU. Though an MoU is usually thought of as a technique used solely in the context of public enterprises, its use can be extended to any situation where an external agency is required to evaluate a firm's performance. Thus, a multinational company can set an MoU with its subsidiary and a family business group council can use an MoU to evaluate its constituent companies. With the greater professionalisation of private firms, especially in the family business sector, the use of MoUs can be helpful. But in India the usage of MoU is traditionally confined to the evaluation of performance in a public enterprise.

Operational control systems guide, monitor, and evaluate progress in meeting annual objectives. While strategic controls attempt to steer the company over an extended time period (usually five years or more), operational controls provide post-action evaluation and control over short time periods—usually from one month to one year. To be effective, operational control systems must take four steps common to all post-action controls:

1. Set standards of performance.
2. Measure actual performance.
3. Identify deviations from standards.
4. Initiate corrective action or adjustment.

Budgeting Systems

The budgetary process was the forerunner of strategic planning. Capital budgeting in particular provided the means for strategic resource allocations. With the growing use of strategic management, such allocations are now based on strategic assessment and priorities, not solely on capital budgeting. Yet capital and expenditure budgeting, as well as sales budgeting, remain important control mechanisms in strategy implementation.

A budget is simply a resource allocation plan that helps managers coordinate operations and facilitates managerial control of performance. Budgets themselves do not control anything. Rather, they set standards against which action can be measured. They also provide a basis for negotiating short-term resource requirements to implement strategy at the operating level.

Most firms employ a budgeting system, not a singular budget, in controlling strategy implementation. Exhibit 14.4 represents a typical budgeting system for a manufacturing business. A budgeting system incorporates a series of different budgets fitting the organisation's unique characteristics. Because organizations differ, so do their budgets. Yet most firms include three general types of budgets—revenue, capital, and expenditure—in their budgetary control system.

Revenue Budgets: Most firms employ some form of revenue budget to monitor their sales projections (or expectations), because this reflects a key objective of the chosen strategy. The revenue budget provides important information for the daily management of financial resources and key feedback as to whether the strategy is working. For evaluative purposes, the revenue budget may be derived from revenue forecasts arrived at in the planning process, or it may be linked to past revenue patterns. For example, most hotel/motel operators emphasize daily revenue compared to revenue for the same day in the previous year as a monitor of sales effectiveness.

A revenue budget is particularly important as a tool for control of strategy implementation. Revenue budgets provide an early warning system about the effectiveness of the firm's strategy. And if the deviation is considerably below or above expectations, this budgetary tool should initiate managerial action to reevaluate and possibly adjust the firm's operational or strategic posture.

Capital Budgets: Capital budgets outline specific expenditures for plant, equipment, machinery, inventories, and other capital items needed during the budget period.

To support their strategies, many firms require capital investment or divestiture. A firm committed to a strong growth strategy may need additional capacity or facilities to support increased sales. On the other hand, a firm intent on retrenchment may have to divest major parts of its current operations to generate additional resources. In both cases, the firm is concerned with management of significant financial resources, probably over an extended time period.

For effective control, a capital budget that carefully plans the acquisition and expenditure of funds, as well as the timing, is essential.

Two additional budgets are often developed to control the use of capital resources. A *cash budget* forecasts receipts and disbursements of cash—cash flow—during the budget period. And a *balance sheet budget* is usually developed to forecast the status of assets, liabilities, and net worth at the end of the budget period.

Expenditure Budgets. Numerous expense/cost budgets will be necessary for budgetary control in implementation of strategy in various operating units of the firm. An expenditure budget for each functional unit and for sub-functional activities can guide and control unit/individual execution of strategy, thus increasing the likelihood of profitable performance. For example, a firm might have an expenditure budget for the marketing department and another for advertising activities.

In such budgets, Rs./dollar variables will be the predominant measure, although nondollar/Rs. measures of physical activity levels may occasionally be used as a supplement. For example, a production budget might include standards for expenditures as well as standards for output level or productivity. These non-dollar/Rs. variables might also include targets or milestones that provide evidence of necessary progress in particular strategic programs.

An expenditure or operating budget is meant to provide concrete standards against which operational costs and activities can be measured and, if necessary, adjusted to maintain effective strategy execution. The expenditure budget is perhaps the most common budgetary tool in strategy implementation. If its standards are soundly linked to strategic objectives, then it can provide an effective communication link between top management and operating managers about what is necessary for a strategy to succeed. It provides another warning system alerting management to problems in the implementation of the firm's strategy.

The budgeting system Exhibit 14.4 provides an integrated picture of the firm's operation as a whole. The effect on overall performance of a production decision to alter the level of work-in-process inventories or of a marketing decision to change sales organisation procedures can be traced through the entire budget system. Thus, coordinating these decisions becomes an important consideration for the control of strategy implementation.

Exhibit 14.4 provides an illustration of how budgets can be coordinated to aid in coordinating operations. In this chart, production, raw material purchases, and direct labor requirements are coordinated with anticipated sales. In more comprehensive systems, other budgets may be included : manufacturing expense, inventories, building services, advertising, maintenance, cash flow administrative overhead, and so on,

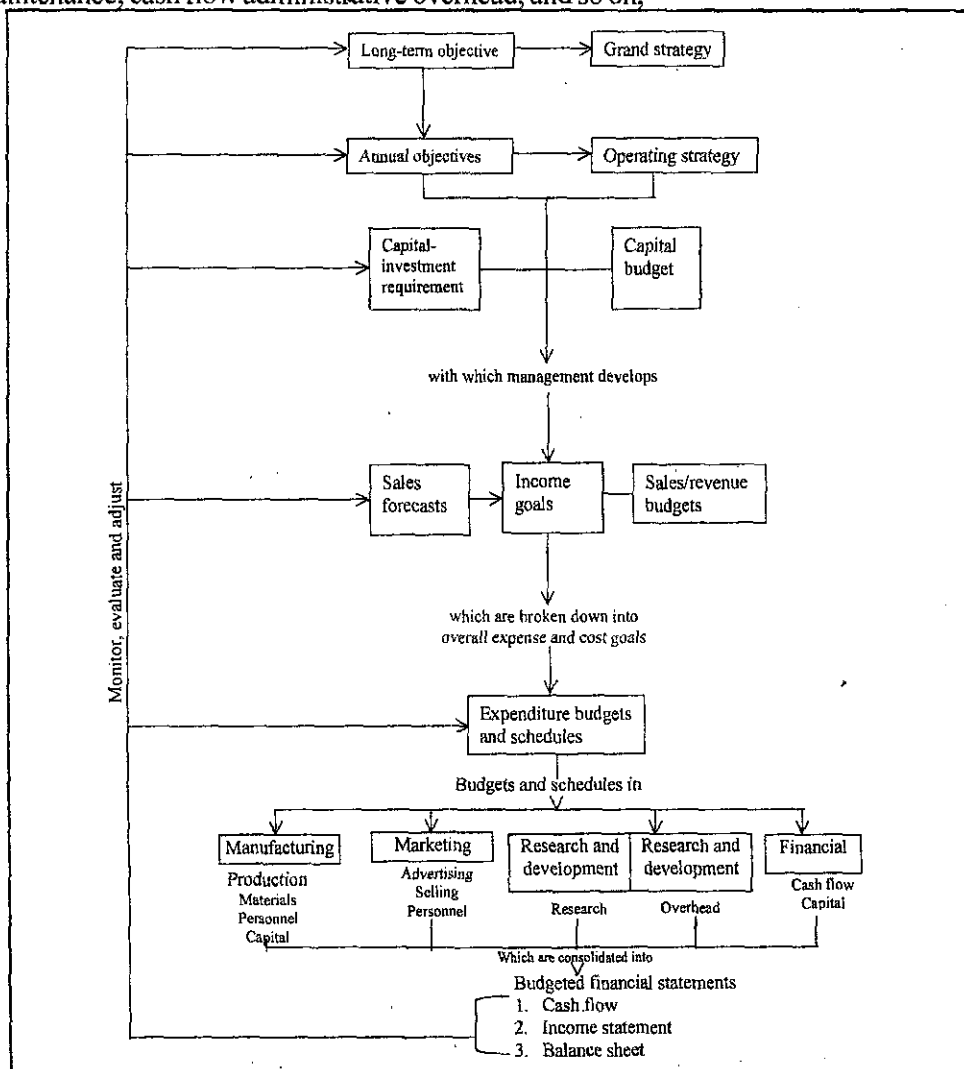


Exhibit 14.4: A Typical Budgeting System for Controlling Strategy Implementation

Scheduling

Timing is often a key factor in the success of a strategy. Schedule is simply a planning tool for allocating the use of a time-constrained resource or arranging the sequence of interdependent activities. The success of strategy implementation is quite dependent on both. So scheduling offers a mechanism with which to plan for, monitor, and control these dependencies. For example, a firm committed to a vertical integration strategy must carefully absorb expanded operations into its existing core. Such expansion, whether involving forward or backward integration, will require numerous changes in the operational practices of some of the firm's organizational units. A good illustration of this is Coors Brewery, which recently made the decision to integrate backward by producing its own beer cans. A comprehensive, two-year schedule of actions and targets for incorporating manufacture of beer cans and bottles into the product chain contributed to the success of this strategy. Major changes in purchasing, production scheduling, machinery, and production systems were but a few of the critical operating areas that Coors' scheduling efforts were meant to accommodate and control.

Key Success Factors

One useful way to effect operational control is to focus on "key success factors." Key success factors identify performance areas that must receive continuous management attention. These are the factors that are of greatest importance in implementing the company's strategies. Examples of key success factors focused on internal performance include: (1) improved productivity, (2) high employee morale, (3) improved product/service quality, (4) increased earnings per share, (5) growth in market share, and (6) completion of new facilities.

Each key success factor must have measurable performance indicators. Management of 1-2-3 from Lotus for example, identified product quality, customer service, employee morale, and competition as the four key determinants of the success of their strategy to rapidly expand Lotus's software offerings. They identified three measures to monitor and control each key success factor as follows:

For product quality:

- Performance data versus specifications.
- Percentage of product returns.
- Number of customer complaints.

For customer service:

- Delivery cycle in days.
- Percentage of orders shipped complete.
- Field service delays

For employee morale:

- Trends in employee attitude survey.
- Absenteeism versus plan.
- Employee turnover trends.

For competition:

- Number of firms competing directly.
- Number of new products introduced.

Percentage of bids awarded versus standard.

Key success factors succinctly communicate the critical elements for which operational managers must be responsible in making the strategy successful. Because their achievement requires the successful performance of several key individuals, these factors can be a foundation for teamwork among managers in meeting the company's strategic objectives.

Budgeting, scheduling, and monitoring key success factors are important means to control the implementation of strategy at the operational level of the company. Common to each operational control system is the need to establish measurable standard and to monitor performance against these standards.

Monitoring Performance and Evaluating Deviations

Operating control system require the establishment of performance standards. In addition, progress must be monitored and deviations from standards evaluated as the strategy is implemented. Timely information must be obtained so that deviations can be identified, the underlying cause determined, and actions taken to correct or exploit them.

Exhibit 14.5 illustrates a simplified report on the current status of key performance indicators linked to the firm's strategy. These performance indicators represent progress after two years of a five-years plan intended to differentiate the firm as a customer-service-oriented provider of high-quality products.

Key success factors	Objective, assumption or budget	Forecast performance at this time	Current performance	Current deviation	Analysis
Cost control : Ratio of indirect overhead to direct field and labor costs	10%	15%	12%	+3 (ahead)	Are we moving too fast or is there more unnecessary overhead than originally thought?
Gross profit	39%	40%	40%	0%	
Customer service:					
Installation cycle in days	2.5 days	3.2 days	2.7 days	0.5 (ahead)	Can this progress be maintained?
Ratio of service to sales personnel	3.2	2.7	2.1	-0.6 (behind)	Why are we behind here? How can we maintain the installation cycle progress?
Product quality: Percentage of products returned	1.0%	2.0%	2.1%	-0.1% (behind)	Why are we behind here? Ramifications for other operations?
Product performance versus specification	100%	92%	80%	-12% (behind)	
Marketing: Sales per employee monthly	Rs. 12,500	Rs. 1,500	Rs. 12,100	+ Rs 600 (ahead)	Good progress. is it creating any problems to support?
Expansion of product line	6	3	5	+2 product (ahead)	Are the products ready? Are the perfect standards met?
Employee morale in service area : Absenteeism rate	2.5%	3.0%	3.0%	(on target)	
Turnover rate	5%	0%	15%	-8% (behind)	Looks like a problem! Why are we so far behind?
Competition: New product introductions (average number)	6	3	6	-3 (behind)	Did we underestimate timing? Implications for our basic assumptions?

Exhibit 14.5: Monitoring and Evaluating Performance Deviations

Management's concern is comparing *progress to date* with expected progress at this point in the plan. Of particular

interest is the current deviation because it provides a basis for examining suggested actions (usually from subordinate managers) and for finalizing decisions on any necessary changes or adjustments in the company's operations.

In Exhibit 14.5, the company appears to be maintaining control of its cost structure. Indeed, it is ahead of schedule in reducing overhead. The company is well ahead of its delivery cycle target, while slightly below its service/sales personnel ratio objective. Product returns look OK, although product performance against specification is below standard. Sales per employee and expansion of the product line are ahead of schedule. Absenteeism in the service area is meeting projections, but turnover is higher than planned. Competitors appear to be introducing products more rapidly than expected.

After deviations and the underlying reasons for them are identified, the implications of these deviations for the ultimate success of the strategy must be seriously considered. For example, the rapid product line expansion indicated in Exhibit 14.5 may be in response to competitors' increased rate of product expansion. At the same time, product performance is still low and, while the installation cycle is slightly above standard (improving customer service), the ratio of service to sales personnel is below its target. Contributing to this substandard ratio (and perhaps reflecting a lack of organizational commitment to customer service) is the exceptionally high turnover in customer service personnel. The rapid reduction in indirect overhead costs might mean that administrative integration of customer service and product development requirements had been reduced too quickly.

As a result of this information, operations managers face several options. The deviations observed may be attributed primarily to internal factors or discrepancies. In this case, priorities can be scaled up or down. For example, greater emphasis might be placed on retaining customer service personnel while de-emphasizing overhead reduction and new product development. On the other hand, the management team could decide to continue as planned in the face of increasing competition and decide to accept or gradually improve the customer service situation. Another possibility is reformulating the strategy or a component of the strategy in the face of rapidly increasing competition. For example, the firm might decide to shift emphasis toward more standardized or lower-priced products to overcome customer service problems and take advantage of an apparently ambitious sales force.

This interpretation of Exhibit 14.5 is but one of many possible explanations. The important point is the critical need to monitor progress against standards and give serious, in-depth attention to both the reasons underlying observed deviations and the most appropriate responses to them.

Evaluations such as this are appropriate for organizational subunits, product groups, and operating units in a firm. Budgets, schedules, and other operating control systems with performance targets and standards linked to the strategic plan deserve this type of attention in detecting and evaluating deviations. The time frame is more compressed—usually quarterly or even monthly during the budgeted year. The operating manager typically reviews year-to-date progress against budgeted figures. After deviations are evaluated, slight adjustments may be necessary to keep progress, expenditures, or other factors in line with programmed needs of the strategy. In the unusual event that deviations are extreme—usually because of unforeseen change—management is alerted to the possible need for revising the budget, reconsidering certain functional plans related to budgeted expenditures, or examining the units and effectiveness of the managers responsible.

An acceptable level of deviation should be allowed before action is taken; if not, the control process will become an administrative overload. Standards should not be regarded as absolute because the estimates used to formulate them are typically based on historical data, which, by definition, are "after the fact." Furthermore, absolute standards (keep equipment busy 100 percent of the time, or meet 100 percent of quota) are often used with no provision for variability. Standards are also often derived from averages, which, by definition, ignore variability. These difficulties suggest the need for defining acceptable *ranges* of deviation in budgetary figures or key indicators of strategic success. This

approach helps in avoiding administrative difficulties, recognizing measurement variability, delegating more realistic authority to operating managers in making short-term decisions, and hopefully improves motivation.

Some companies use trigger point for clarification of standards, particularly in monitoring key success factors. A *trigger point* is a level of deviation of a key indicator or figure (such as a competitor's actions or a critical cost category) that management identifies in the planning process as representing either a major threat or an unusual opportunity. When that point is "hit," management is immediately alerted ("triggered") to consider necessary adjustments in the firm's strategy. Some companies take this idea a major step forward and develop one or more *contingency plans* to be implemented once predetermined trigger points are reached. These contingency plans redirect priorities and actions rapidly so that valuable reaction time is not "wasted" on administrative assessment and deliberation of the extreme deviation.

Correcting deviations in performance brings the entire management task into focus. Managers can correct performance by changing measures. Perhaps deviations can be resolved by changing plans. Management can eliminate poor performance by changing how things are done, by hiring new people, by retaining present workers, by changing job assignments, and so on. Correcting deviations from plans, therefore, can involve all of the functions, tasks, and responsibilities of operations managers. Operational control systems are intended to provide essential feedback so that company managers can make the necessary decisions and adjustments to implement the current strategy.

Ratio Analysis

Ratios of financial statement items (here, balance sheets and income statements) are widely used to measure strategic and management performance. With the exception of the current and quick ratios, few generally acceptable and appropriate ratio values exist. The exact number of ratios to use (Exhibit 14.6) the circumstances in which to use them, their components, and their exact meanings are often not agreed upon. Every financial analyst seems to have a preferred system.

The major problem with using these sources is finding the exact industry or group of firms against which to compare the subject firm. While data on large organization is abundant, the multiplicity and diversity of products among firms makes comparisons suspect. Data on intermediate-sized firms is virtually nonexistent. Even where comparative ratios are available, they must be used with caution. Financial statement information is subject to varying accounting practices which hamper comparisons. Footnotes to these statements often make significant differences as to the true value of certain items.

Return on Investment (ROI)

As a result of the positive aspects of decentralization, it has become a popular organizational design technique. The need arises to control the resulting subsystems. Two primary types of control systems exist to exert financial control over these decentralized units: those that control projects and those that control responsibility centres. Anthony, Dearden, and Vaneil describe five types of responsibility centres.

1. Standard cost centers are those for which standard costs can be computed. By multiplying this cost times units, an output measure is devised.
2. Revenue centers are those for which revenues can be determined.
3. Discretionary expense centers are organizational units, normally staff units, whose output is not commonly measured in financial terms.

4. Profit centers are subsystems for which both costs and revenues can be measured and where responsibility for the difference—profit—has been assigned.
5. Investment centers are profit centers for which the assets employed in obtaining profit are identified. (These are SBUs or major project divisions.)

ROI (net income divided by total assets) is the performance measure most frequently used for the last of these responsibility centers – the investment center. ROI is a critical issue in large organizations. Inappropriate division control systems reduce executive motivation. This can and usually does result in reduced profits. Indeed, while ROI analysis has several advantages, it also has several limitations.

Advantages of ROI analysis include the following :

Ratio	Formula for Calculation	Calculation	Industry Average	Evaluation
<u>Liquidity:</u> Current	$\frac{\text{Current assets}}{\text{Current liabilities}}$	Rs $\frac{700,000}{300,00} = 2.3$ times	2.5 times	Satisfactory
Quick, or acid test	$\frac{\text{Current assets} - \text{Inventory}}{\text{Current Liabilities}}$	$\frac{400,000}{300,00} = 1.3$ times	1.0 times	Good
<u>Leverage:</u> Debt to total assets	$\frac{\text{Total debt}}{\text{Total assets}}$	$\frac{1,000,000}{2,000,000} = 50$ percent	33 per cent	Poor
Times interest earned	$\frac{\text{Profit before taxes plus interest charges}}{\text{Interest charges}}$	$\frac{245,000}{45,000} = 5.4$ times	8.0 times	Fair
Fixed charge coverage	$\frac{\text{Income available for meeting fixed charges}}{\text{Fixed charges}}$	$\frac{273,000}{73,000} = 3.7$ times	5.5 times	Poor
<u>Activity:</u> Inventory turnover	$\frac{\text{Sales}}{\text{Inventory}}$	$\frac{3,000,000}{300,000} = 10$ times	9 times	Satisfactory
Average collection period	$\frac{\text{Receivables}}{\text{Sales per day}}$	$\frac{200,000}{8,333} = 24$ days	20 days	Satisfactory
Fixed assets turnover	$\frac{\text{Sales}}{\text{Fixed assets}}$	$\frac{3,000,000}{1,300,000} = 2.3$ times	5.0 times	Poor
Total assets turnover	$\frac{\text{Sales}}{\text{Total assets}}$	$\frac{3,000,000}{2,000,000} = 1.5$ times	2 times	Poor
<u>Profitability</u> Profit margin or sales	$\frac{\text{Net profit after taxes}}{\text{Sales}}$	$\frac{120,000}{3,000,000} = 4$ percent	5 percent	Poor
Return on total assets	$\frac{\text{Net profit after taxes}}{\text{Total assets}}$	$\frac{120,000}{2,000,000} = 6.0$ percent	10 percent	Poor
Return on net worth	$\frac{\text{Net profit after taxes}}{\text{Net worth}}$	$\frac{120,000}{1,000,000} = 12.0$ percent	15 percent	Poor

Exhibit 14.6: Summary of Financial Ratio Analysis

1. ROI is a single comprehensive figure influenced by everything that happens.
2. It measures how well the division manager uses the property of the company to generate profits. It is also a good way to check on accuracy of capital investment proposals.
3. It is a common denominator which can be used to compare many entities.
4. It provides an incentive to use existing assets efficiently.
5. It provides an incentive to acquire new assets only when such acquisition would increase the return

Limitations of ROI analysis include the following:

1. ROI is very sensitive to depreciation policy. Depreciation write-off variances among divisions affect ROI performance. Accelerated depreciation techniques reduce ROI, conflicting with capital budgeting discounted cash flow analysis.

2. ROI is sensitive to book value. Older plants with more depreciated assets and lower initial costs have relatively lower investment bases than newer plants (note also the effect of inflation on raising costs of newer plants and on the distortion of replacement costs), thus causing ROI to be increased. Asset investment may be held down or assets disposed of in order to increase ROI performance.
3. In many firms that use ROI, one division sells to another. As a result, transfer pricing must occur. Expenses incurred affect profit. Since in theory the transfer price should be based on total impact on firm profit, some investment center managers are bound to suffer, Equitable transfer prices are difficult to determine.
4. If one division operates in an industry with favourable conditions and another in an industry with unfavourable conditions, one will automatically "look" better than the other.

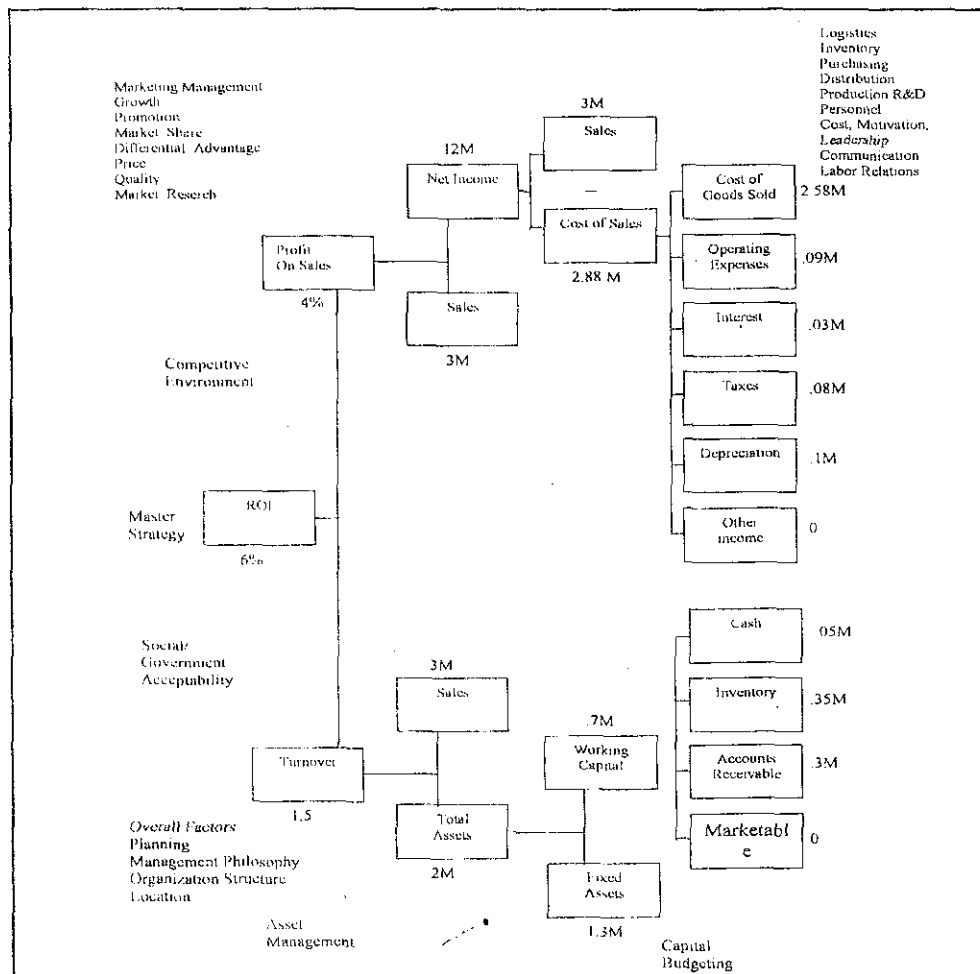


Exhibit 14.7 Financial Analysis Using ROI

5. The time span of concern is short range. The performance of division managers should be measured in the long run. This is top management's time span capacity--how long it takes for their performance to realize results.
6. The business cycle strongly affects ROI performance, often despite managerial performance.

Despite these criticisms, ROI will likely continue as the leading index of management performance if for no other reason than its simplicity. Importantly, though, ROI must be supplemented with other decision information.

ROI is an important concept in terms of both total organizational control and subsystem control. As noted, it is the

most widely used measure of a firm's operating efficiency. While ROI represents net income as a percentage of total assets, it is a function of many variables. ROI results from two key factors, profit margin on sales and assets turnover.

Management Audits

One of the major questions confronting organization today is how to evaluate the performance of the top management team. In order for this end to be achieved, several factors must be considered:

1. Did top management accomplish the objectives it established?
2. How good were the objective it established? How good were the strategies it employed to accomplish these objectives?
3. What factors beyond the control of top management affected its performance?
4. How well has it responded to and how well has it anticipated these factors?

These questions are operational control criteria for top management. Note, it is strategy that is at issue.

Several systems have attempted to measure top management's performance. One of the more promising is the management audit which examines all facets of organizational activity.

The audit has been widely used in many of the largest corporations and in smaller firms as well. Importantly, the audit can be adapted to organizations with missions other than profit, such as commonweal, service, and mutual benefit organizations.

Although management audit activity has seemed to decline in recent years, several additional approaches to the management audit have been suggested. Of interest is Greenwood's management audit. He suggests that a management audit should examine.

1. Strategy and strategy determinants, especially environmental factors.
2. The major functional activities of a firm—marketing, operations (production), personnel, and accounting and finance.
3. Whether managers are performing the major functions of management—planning, organizing, staffing, directing, and controlling.

Finally, Greenwood recognizes the need for an annual organization policy audit. In this audit Greenwood has followed a management theory approach more traditional than Martindell's.

Management audits may also follow a format parallel to the content of the master strategy. Such an analysis is divided into four major parts: those for enterprise, corporate, business, and functional strategies. This approach includes recognition of product divisions but examines strategy on the basis of functional activities within divisions if they exist.

In observing any technique, it is important to note its weaknesses. While the strength of the management audit is that it often has been able to successfully predict corporate performance, it is not always accurate. Such audits have predicted success for some companies that failed miserably. Why? First, and probably most important at this time, the environment may change drastically.

Regardless of its weaknesses, the audit serves an important function in its comprehensive examination of the organization

While examination of the "bottom line" indicates problems, the auditing of other areas is vital in explaining the causes of these problems. The audit is primarily effective because it looks beyond financial information and systematically appraises the performance of top management.

Human Resource Accounting (HRA)

The evaluation of human assets offers great promise, but to date this promise has been largely unfulfilled. The relevance of human resource accounting to strategic management is connected principally to evaluating the worth of the abilities, skills, knowledge, aspirations, and so forth of the strategic decision makers. But, in addition, the evaluation of corporate strengths and weaknesses requires an assessment of all employees and their potentials related to threats and opportunities.

To date, much of the implementation of HRA has involved calculations of the historical cost of human "assets" to the organization. A typical cost model observes the cost of recruiting and acquisition, formal training, orientation, development, familiarization, and related human resource expenses. Other HRA cost models exist. One might calculate opportunity cost—for example, and replacement cost—based on historical cost with operation costs added. In addition to cost models of HRA, one other major model—the economic value approach—exists in aggregate or on an individual basis. Ultimately, this latter is the information sought, but the difficulties, and even impossibilities of estimation, in this author's opinion, severely limit the applicability of the approach. The main problem with the economic value approach is one of validity. Such approaches require estimation of the worth of individuals to the organization. The question is, how can one be sure these estimations are meaningful?

The Social Audit

In recent years, business's critics have demanded that social audits of corporations be conducted. The term *social audit* refers to any device which attempts to evaluate an organization's social performance. Areas which might be audited include environmental protection, equal employment opportunity, consumer satisfaction, governmental relationships, energy usage, and employee job satisfaction.

Ultimately the aim is to determine the social impact of the firm on its stakeholders. While some social areas are readily definable, a quantitative measure of both requirements and performance for many of these areas is extremely difficult, if not impossible, to obtain. Furthermore, it is difficult to obtain agreement as to exactly what business should accomplish. Each pressure group seems to have its own set of demands. Obviously, business cannot respond to all of them. Many corporations have audited their activities in several of the social responsibility areas, and the scoring systems which have been used are becoming more quantitatively oriented. The process of strategic evaluation and control does not operate in isolation; it works on the basis of the different organisational systems that are used to implement strategies. Here, we shall briefly review the role of organisational systems in evaluation.

Information System

Evaluation is done by comparing actual performance with standards. The measurement of performance is done on the basis of reports generated through the information system. In fact that purpose of information management system is to enable managers to keep track of performance through control reports. Several of the techniques described in the previous section, whether for strategic surveillance or financial analysis, are based on the use of an information system to provide relevant and timely data to managers to allow them to evaluate performance and strategy, and initiate corrective action. In fact, with the increasing sophistication of the information management systems and the use of IT it is possible to devise elaborate methods for evaluation. Techniques such as data warehousing and datamining enable organisations to delve deeper into their internal systems and come up with information that can be useful for

evaluation and control purposes.

Control System

The control system, of course, is at the heart of the any evaluation process, and is used for setting standards, measuring performance, analysing variances, and taking corrective action.

Appraisal System

The appraisal system actually evaluates performance and so is a part of the wide control system. However its significant role in evaluation, is yet to be acknowledged. When the performance of managers is appraised, it is their contribution to the organisational objectives which is sought to be measured. In practice, it is difficult to differentiate strictly between the performance of individuals and that of the organisational units they belong to. Thus, the achievement of a department or a profit centre is the sum total, or even more, synergistically, of the individual performance of managers and employees in the department or profit centre. The evaluation process, through the appraisal system, measures the actual performance and provides the basis for the control system to work.

Motivation System

The central role of the motivation system is to induce strategically desirable behaviour so that managers are encouraged to work towards the achievement of organisational objectives. Now, if we look at the way the evaluation process works, we will observe that its efficacy depends on the extent to which it is able to bring actual performance to the level of the standards. In other words, the lesser the deviation of actual performance from standards, the higher is the efficacy of the evaluation process. The motivation system plays a significant role in ensuring that deviations do not occur, or if they do, then they are corrected by the means of rewards and penalties. Incentive systems are directly related to the amount of deviation. Performance checks, which are a feedback in the evaluation process are done through the motivation system.

Development System

The development system prepares the managers for performing strategic and operational tasks. Among the several aims of development, the most important is to match a person with the job to be performed. This, in other words, is matching actual performance with standards. This matching can be done provided it is known what a manager is required to do, and what is deficient in terms of knowledge, skills, and attitude. Such a deficiency is located through the appraisal system. In reality, what we term as corrective action in the evaluation process is, in reality, the taking of steps that would lead to the development of individuals who are enabled to perform as required. The role of the development system in evaluation is, therefore, to help strategists to initiate and implement corrective action.

Planning System

In the planning system (which is more concerned with the formulation of strategies), we deal with the issue of 'planning for evaluation'. Since the evaluation process is a part of strategic management it has to be planned for. Questions such as these are to be dealt with: who will perform evaluation? How will the information generated be used? How much resource will be required? To what extent will control be exercised so that it is cost-effective? And what administrative systems will be required to support the evaluation system? Further, the evaluation processes also provides feedback to the planning system for the reformulation of strategies, plans, and objectives. Thus, the planning system closely interacts with the evaluation process on a continual basis. Several additional factors should be considered with respect to control.

Control Policies

Just as organizations establish strategic and implementation policies, they must also establish policies which guide control of the organization. Control policies naturally evolve from the objectives and standards established for performance. The organization must simply indicate to its managers and other employees, what the specific objectives are, how performance against these will be measured, what comparisons will ensure, and how differences between expectations and performance will be handled. Rewards must naturally be tied to results.

The organization needs policies establishing total performance measurements, intermediate organizational level performance measurements, and work group and individual performance measurements. Of principal concern is that the 'what' and 'how' of control is sufficiently definitive to motivate employees to perform.

Characteristics of information	Operational Control	Management Control	Strategic Control
Source	Largely internal	Internal, partly environmental	Internal and environmental
Scope	Well defined, narrow	Moderately broad	Broad in scope
Level of aggregation	Detailed	Aggregated	Aggregated
Time horizon	Historical	Historical	Future and historical
Frequency of use	Very frequent, continuous	Periodic	Occasional, but with increasing frequency

Exhibit 14.8: Information Requirements by Type of Control

A Note on the Role of Information in Control

A decision can be only as good as the information upon which it is based. In strategic control, management control, and operational control situations, for both feedforward and feedback control systems, comparison and adjustment occur as information is received. The absence of information, such as is the rule in management-by-exception control systems, is also important. There are differences in the characteristics of the information required in strategic control, management control, and operational control. These differences are portrayed in Exhibit 14.8. Mass of information at operational levels must be meaningfully reduced before top management reports are prepared.

Integrated Planning and Control Systems

In a previous text, the importance of integrated planning and control was stressed from a planning perspective—objectives provide direction and motivation. Objectives are anticipated results. As such, for control purposes, they provide standards against which to compare performance. PERT, CPM, MBO, PPBS, budgets, and other planning and control systems can and should be applied to ensure successful mission accomplishment. It is essential that implementation be controlled if it is to be effective.

Execution and control of strategy ultimately depend on individual organizational members, particularly key managers. And motivating and rewarding good performance by individuals and organizational units are key ingredients in effective strategy implementation. While positive reinforcements are given primary emphasis, sanctions or negative reinforcements are important tools for controlling and adjusting poor performance. Motivating and controlling individuals efforts, particularly those of managerial personnel, in execution of strategy is accomplished through a firm's reward-sanction mechanisms—compensation, raises, bonuses, stock option, incentives, benefits, promotions, demotions, recognition, praise, criticism, more (or less) responsibility, group norms, performance appraisal, tension, and fear. These mechanisms are positive and negative, short run and long run.

Control mechanisms align personal and subunit actions and objectives with the objectives and needs of the firm's strategy. This is not easy, and reward-sanction structures controlling strategy execution vary greatly across different

firms. For example, Harold Geneen, former CEO of ITT, purportedly used an interesting combination of money (compensation and incentives), tension (strict accountability for results), and fear to control individual managers' efforts toward strategy implementation. According to one author.

Geneen provides his managers with enough incentives to make them tolerate the system. Salaries all the way through ITT are higher than average—Geneen reckons 10 percent higher—so that few people can leave without taking a drop. As one employee put it: "We're all paid just a bit more than we think we're worth." At the very top, where the demands are greatest, the salaries and stock options are sufficient to compensate for the rigors. As someone said, "He's got them by their limousines."

Having bound his men to him with chains of gold, Geneen can induce the tension that drives the machine. "The key to the system," one of his men explained, "is the profit forecast. Once the forecast has been gone over, revised, and agreed on, the managing director has a personal commitment to Geneen to carry it out. That's how he produces the tension on which the success depends." The tension goes through the company, inducing ambition, perhaps exhilaration, but always with some sense of fear: what happens if the target is missed?

Financial incentives are important reward mechanisms. They are particularly useful in controlling performance when they are directly linked to specific activities and results. Intrinsic, non financial rewards, such as flexibility and autonomy in the job and visible control over performance, are important managerial motivators. And negative sanctions, such as withholding financial and intrinsic rewards or the tensions emanating from possible consequences of substandard performance, are necessary ingredients in directing and controlling managers' efforts.

The time horizon on which rewards are based is a major consideration in linking rewards and sanctions to strategically important activities and results. Numerous authors and business leaders have expressed concern with incentive systems based on short-term (typically annual) performance. They fear short-term reward structures can result in actions and decisions that undermine the long-term position of a firm. A marketing director who is rewarded based on the cost effectiveness and sales generated by the marketing staff might place significantly greater emphasis on established distribution channels than on "inefficient" nurturing and development of channels that the firm has not previously used. A reward system based on maximizing current profitability can potentially shortchange the future in terms of current investments (time, people, and money) from which the primary return will be in the future. If the firm's grand strategy is growth through, among other means, horizontal integration of current products into new channels and markets, the reward structure could be directing the manager's efforts in a way that penalizes the ultimate success of the strategy. And the marketing director, having performed notably within the current reward structure, may have moved on to other responsibilities before the shortcoming emerge.

Short-term executive incentive schemes typically focus on last year's (or last quarter's) profits. This exclusive concentration on the bottom line has four weaknesses in terms of promoting a new strategy:

1. It is backward looking. Reported results reflect past events and, to some extent, past strategy.
2. The focus is short term, even though many of the recorded transactions have effects over longer periods.
3. Strategic gains or losses are not considered due to, among other things, basic accounting methods.
4. Investment of time and money in future strategy can have a negative impact. Since such outlays and effort are usually intermingled with other expenses, a manager can improve his or her bonus by not preparing for the future.

While there are clear dangers in incentive systems that encourage decidedly short-run thinking and neglect the longer term, there is real danger in hastily condemning short-term measures. Arguing that managers must be concerned with long-run performance is easy; it also may be too easy to make the mistake of concluding that short-term

concerns are not important or that they are necessarily counterproductive to the strategic needs of the organization. Such a simplistic and quick conclusion can be dangerous. In an effectively implemented strategy, short-term objectives or aims support, and are critical to, the achievement of long-term strategic goals. The real problem is not the short-versus long-term concerns of management; it is the lack of integration of and consistency between long-and short-term plans and objectives in the control system that is vital to the successful implementation of strategy. The critical ingredients for the achievement of this consistency are appropriate rewards and incentives.

To integrate long-and short-term concerns, reward systems must be based on the assessment and control of both the short-run and long-run (strategic) contributions of key managers. An effective reward system should provide payoffs that control and evaluate the creation of *potential* future performances as well as last year's results. Exhibit 14.9 illustrates a management reward system tied to a five-year cycle of strategy implementation. Review and evaluation in a specific year include both an assessment of performance during that year and an evaluation of progress toward the five-year strategic objectives. The annual objectives and incentives in each year can reflect adjustments.

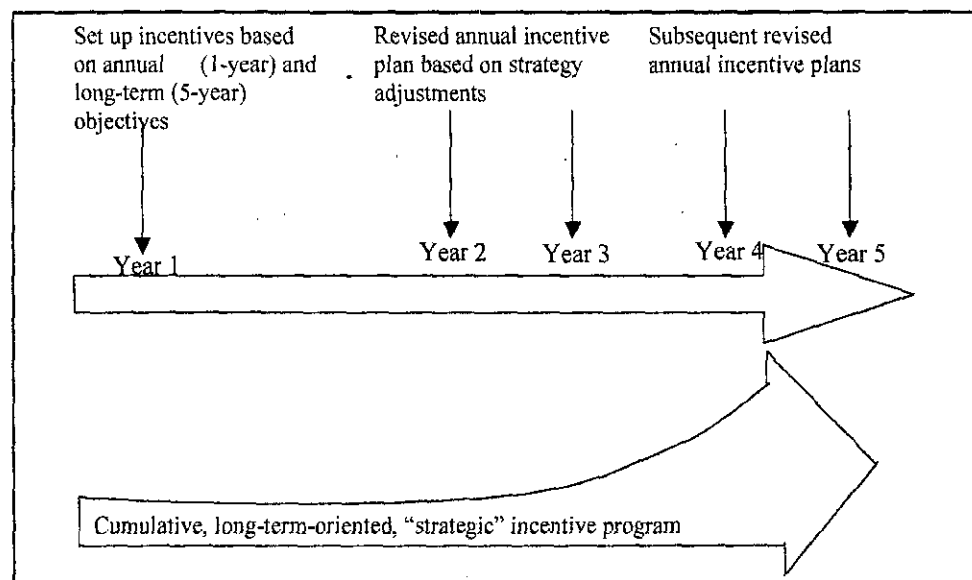


Exhibit 14.9: Annual Incentive System with Long-term Perspective

necessary for successful implementation of the strategy. This helps integrate short-and long-term considerations in strategy implementation by linking adjustments necessary in supporting revised, long-term considerations to next year's reward structure. The second component in the management reward system in Exhibit 14.9 is an incentive based on cumulative progress towards strategic objectives. It is shown as increasing in size or amount over time, which reinforces a long-term, strategic perspective. Incentives such as stock option, deferred bonuses, or cumulative compensation indexed to future performance indicators are ways this reward component could be structured. The key ingredient is an incentive system linked to longer-term progress toward strategic goals. This approach reinforces the interdependence or performance over the five-year period rather than the importance of any one year.

These incentive priorities (long-term versus short-term) should vary depending on the basic nature of the strategy. Exhibit 14.10 provides the results of a recent study illustrating this point. Comparing the importance of 11 criteria used in determining bonuses for SBU managers, the researchers found that long-term criteria were more important determinants of bonuses in SBUs with "build-oriented" strategies than in SBUs with "harvest-oriented" strategies. Short-term criteria were important in both types of SBUs, although these criteria were much more important than long-term criteria for determining incentive structures in harvest-oriented SBUs.

Another refinement suggested in constructing incentives systems that reward long-term (strategic) as well as short-

term thinking is the use of strategic budgets. In this approach, strategic budgets are employed simultaneously with operating budgets, but the objectives and plans associated with each budget vary a great deal. The focus of the operating budget is control and evaluation of business as usual. The strategic budget specifies resources (and targets) for key programs or activities linked to major initiatives that are integral to the long-term strategy. Concerned that executive incentive plans can and should give more explicit weight to strategic activities, proponents of a strategic budget approach suggest three basic steps:

1. Measure progress toward strategic targets separately from results of established operations.
2. Determine incentive awards separately for established operations and for progress towards strategic targets.

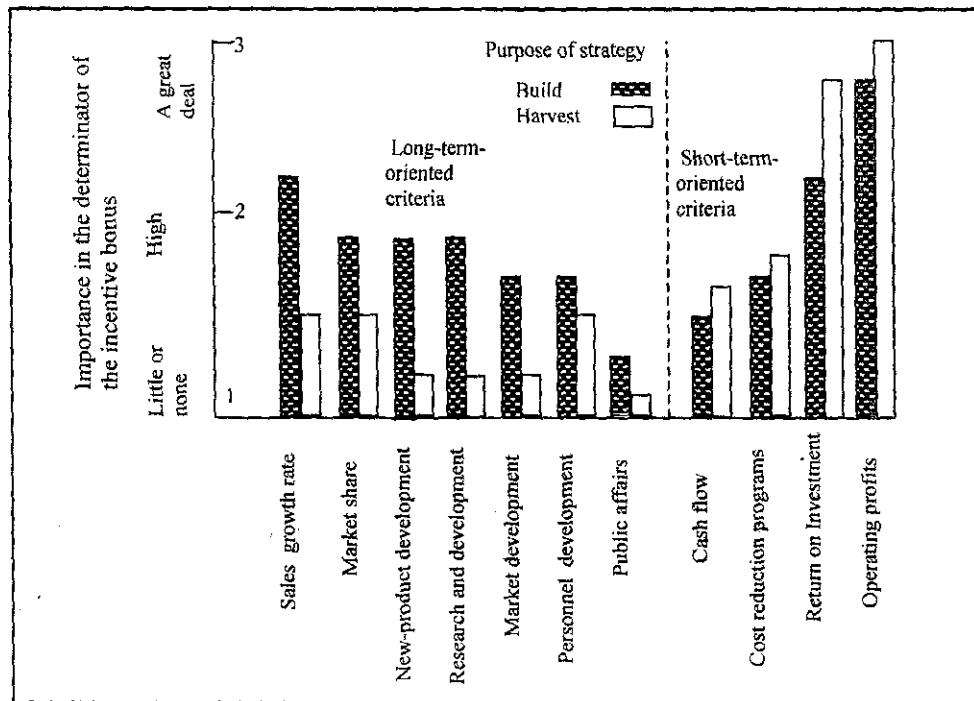


Exhibit 14.10: Perceived Importance of Various Performance Dimensions in Determination of SBU General Manager's Incentive Bonus

3. Devise a long-term, stock option equivalent to encourage revisions of strategy and entrepreneurial risk taking.

Common to each of these reward and sanction approaches is growing recognition of the need for a two-tiered incentive system linked to short-run and long-term considerations. The relative emphasis in terms of reward linkages should be determined by the focus of the strategy. For businesses with growth-oriented strategies, for example, incentive systems weighted towards long-term payoffs are more appropriate.

Incentive emphasizes long-term value based on either stock appreciation, length of the option, or a combination of both. While this emphasis is appropriate, short-term operating objectives deserve attention so that short-term performance is geared towards long-term objectives. For businesses pursuing more immediate strategic goals, the incentive emphasis should shift accordingly. In harvest business units of large firms, for example, greater emphasis on short-term, easily quantified performance indicators appears to be the basis for reward systems designed to evaluate strategic results.