Business Strategy

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Detailed Curriculum

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Long-term Objective and Strategy Formulation: Defining Objectives – The Need for Objectives – The Nature of Objectives – Levels of Objectives: Strategic to Operating – The Hierarchy of Objectives – Grand Strategies – Setting Long-term Objectives and Strategy Sets.

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Business Strategy: The Road Ahead: Defining Value Chain – Value Chain and Buyer Value – Competitive Scope and the Value Chain – Value Chain and Industry Structure – Value Chain and Organization Structure – Change of Strategy and Organizational Change – Forces and Types of Change – Resistance to Change Strategies for Implementation and Change – Role of the Strategist – Global Competitiveness.

Chapter I

Introduction to Strategic Management

After reading this chapter, you will be conversant with:

- Evolution of the Concept of Strategic Management
- Importance of Strategic Management
- Components of Strategic Management
- Levels of Strategy Planning
- Making Strategic Decisions

Introduction

Gary Hamel estimated that American senior managers generally spend about 3 percent of their time thinking and planning for the future. While 3 percent may be enough for a start-up Internet company, whose leader's mission is an Initial Public Offering (IPO), cash in and early exit, it is not good enough if the senior management's principal aim is to build an enduring company.

The best way to predict the future is to create it. Sony, since its inception, has tried to determine its own future. Sony's goal has always been to create something out of nothing. An example is the Sony Walkman. A strategic plan is the first step in bringing out a new product. A well-crafted strategic plan gives one control over the vagaries of the marketplace. Since the mid-1980s, a lot of attention has been given to operational efficiency and nobody can deny its importance. But too much concentration on the present and disregard for the future does not augur well for an organization. Hence, an organization operating in an intensely competitive global environment must have strategies that provide the framework for a long-term future plan.

Strategic management can be defined as the set of decisions and actions resulting in formulation and implementation of strategies designed to achieve the objectives of an organization. It involves taking decisions about products, location, and the organization's structure – these determine the survival of the organization in the short- and long-term. Strategic management is a comprehensive procedure and starts with a strategic diagnosis. It continues with a series of additional steps, culminating in new products, markets, technologies and capabilities. The strategist's work is to challenge the prevailing setup with a single question: "Why?", and to ask the same question as many times as necessary to make the future as clear as the present for managers at all levels.

EVOLUTION OF THE CONCEPT OF STRATEGIC MANAGEMENT

The word *Strategy* comes from the Greek word *Strategia,* which means a *General* or *Military Commander.* War and strategy are inseparable. Wherever there has been war, there has been a strategy to wage it. War and strategy are not new concepts; what is new is the increased emphasis of strategy in the business context. Every business strategy that is hammered out in the boardrooms of an Asian, American or European company can be traced back to a battlefield of a war past as shown in Box 1.

Igor Ansoff pioneered the concept of strategy. Later, Henry Mintzberg, and Michael E Porter enriched the concept of strategic management with their original insights.

Box 1: Impact of War on Business Strategies

Business wars are some times as fierce as the wars fought in the actual battlefield. Today's successful business strategies can be traced back to military strategies that have been used effectively from ancient Greece to Desert Storm. Strategic principles remain unchanged through time and context. The strategies can be identified as:

i. **'Attack Strength' Strategy:** Attacking the enemy in his stronghold is the aim here. The Japanese attack on Pearl Harbor is an example of this strategy. Similarly, a decade ago, Lexus (Toyota) fought Cadillac (GM) and Lincoln (Ford) in the US luxury car market that was a comfortable duopoly for its rivals. In 1999, Lexus surpassed both Cadillac and Lincoln in sales.

ii. **'Attack Weakness' Strategy:** The American attack against Germany in Morocco during the Second World War, is an example of this strategy. The Nazis ignored the impending US attack on Morocco, thinking that Morocco was hardly worth defending. The successful American attack on Morocco opened up the way for the ultimate defeat of Hitler in the Second World War. Sam Walton, the founder of Wal-Mart, executed this strategy in the early 1960s by opening retail stores in small towns ignored by the then giant – Sears.

iii. **Bringing Change to a Failing Company:** When Moses freed the Hebrews from slavery under Rameses II, he did not hesitate to strike down those who were recalcitrant. This was part of the change he needed to bring about, for the construction of a new Israel. In the corporate world, when Jack Welch took over as CEO of GE in 1981, he foresaw the potential problems that lay ahead for GE and instituted an aggressive strategy aimed at a complete overhaul. His detractors called him "Neutron Jack" for his ruthless change strategies. Welch continued with the implementation of his plans. The result – when Jack Welch left the company in 2001, GE was the company with the highest profits in the world.

iv. **Concentration of Forces:** This strategy is most relevant in today's business scenario. Organizations should coordinate their resources and concentrate on the areas where the competition is most intense. Using this strategy, in ancient times, generals like Caesar and Genghis Khan overwhelmed rivals with much bigger armies. Companies like Nike, Nokia and FedEx excel because of their concentration strategy.

v. **Forging a Strategic Alliance:** The alliance among the US, the UK and the USSR overcame Nazi Germany in the Second World War. This underlines the importance of strategic alliances. Similarly, in today's highly competitive business environment, organizations are increasingly entering into alliances to take advantage of various synergistic benefits.

vi. **Patience and Time:** When the rival is blundering, a well-run organization should not attack it but wait patiently for the rival's self destruction. Napoleon's failed invasion of Russia is a classic illustration of this strategy. Companies such as Yahoo and Boeing practice this strategy.

vii. **Control the Choke Point:** The Spartans, with an army of three hundred soldiers blocked the Persian army with 4,00,000 soldiers at a narrow pass in Northern Greece called Thermopyle. At this geographic choke point, the Spartans killed 15,000 Persians, before themselves being overrun and killed. The blocking of the Persian army gave other Greek states the time to prepare for war and to defeat the Persians ultimately. At one time, the AOL portal with its 26 million – person service that links the customer and the Internet was a perfect example of the strategy used at Thermopyle. Any organization that hoped to reach potential customers online was forced to use the AOL portal.

viii. **Containment is Good Enough:** The Cold War between the US and the erstwhile USSR during the later half of the 20th century is an example of containment strategy. In business, when there is competition between two organizations of equal size, if one organization tries to eliminate the other, then both firms will end up with shattered profit margins and mountains of debt, and, in the end, bankruptcy. So, containment is often preferred.

ix. **A Combat-ready Company:** Netscape was an early entrant on the Internet. However, Microsoft took only six months to develop a competitive product. Cisco, which went on an acquisition spree in order to strengthen its technology, displays impressive battle-readiness too. These companies learnt from the example of the American defense forces, in always being ready to face attack.

Source: Dennis Laurie, from Battlefield to Boardroom.

Ansoff's Strategic Success Paradigm

The systematic study of strategic management was pioneered by Ansoff. Igor Ansoff conducted extensive research on acquisitions by American companies between 1948 and 1968. He found that acquisitions based on a rational strategy fared far better than those that were based on opportunistic decisions.

Ansoff's strategic success paradigm identifies the conditions that optimize profitability. The key elements of this paradigm are as follows:

i. There is no universal success formula for all firms.

ii. The level of turbulence in the environment determines the strategy required for the success of a firm.

iii. The aggressiveness of the strategy should be aligned with the turbulence in the environment to optimize the firm's success.

iv. The management's capabilities should be aligned with the environment to optimize the firm's success.

v. Internal capability variables i.e., cognitive, psychological, political, anthropological and sociological variables, all jointly determine the firm's success.

After 11 years of testing his paradigm empirically, Ansoff translated it into a diagnostic instrument called "Strategic Readiness Diagnosis". His book "Corporate Strategy", (1965), played a key role in the development of strategic planning. In another book, "An Analytical Approach to Business Policy for Growth and Expectation," Ansoff elaborated upon a highly complex "cascade of decisions." He introduced "gap analysis" (the gap between where you are today and where you want to be) and the concept of synergy to a wide audience for the first time. Thus, he left an indelible mark on the practice of strategic management.

Mintzberg: Strategy as Craft

The next most influential thinker in the field of strategic management after Ansoff was Henry Mintzberg. Mintzberg added a new dimension to strategic management by bringing the personal side of the manager into the picture. He proposed an *intuitive* view of strategic management, and attacked the *rationalism* of his contemporaries with regard to the subject. In his first book, *The Nature of Managerial Work,* (1973)*,* he advocated a more humane approach to strategy formulation and implementation, and coined the term "crafting strategy". He saw strategy formulation as a deliberate, delicate and dangerous process. Mintzberg also identified five types of "ideal" organizational structures: simple structure, machine bureaucracy, professional bureaucracy, divisionalized form and 'ad hoc' racy.

Peter Drucker's Contribution

After World War II, the use of formal strategic thinking to guide management decisions was encouraged. Peter Drucker argued that "management is not just passive, adaptive behavior; it means taking action to make the desired results come to pass." According to Drucker, though economic theory had treated markets for long as impersonal forces which were beyond the control of individual entrepreneurs and organizations, in the age of multidivisional organizations, managing "implies responsibility for attempting to shape the economic environment, for planning, initiating and carrying through changes in that economic environment, for constantly pushing back the limitations of economic circumstances on the enterprise's freedom of action." According to Pankaj Ghemawat, Drucker's observation that by consciously using formal planning a company could exert some positive control over market forces became the rationale for business strategy.

Drucker's biggest contribution to business strategy was the introduction of the concept of Management by Objectives (MBO). When Drucker introduced the concept in 1954, most managers were concerned with processes rather than goals. With MBO, the focus shifted from processes to goals. According to Drucker, MBO is more than a technique of management, it is a philosophy of managing. MBO transforms the basic assumptions of managing from exercising control to self-control.

Michael Porter: Strategy and Competitive Advantage

Michael Porter introduced generic strategies like focus, cost leadership, cost differentiation to reduce the uncertainties of the competitive environment. He also suggested the study of different components of strategic management such as the environment, in which the company operates, through his 'five forces' theory.

Porter in his "*Competitive Strategy",* (1980), addressed the issue of how companies sustain their competitive advantage. Another book by Porter, "*The Competitive Advantage of Nations",* (1990), is a major body of work on competitiveness and economic development. The ideas in "*The Competitive Advantage of Nations"* and a series of other publications continue to guide economic policy throughout the world.

Porter's important contributions to strategic management include the "Five forces model", the "value chain", and the concept of "generic strategies". According to his "five forces model", the nature and degree of competition in an industry depends on five forces: the threat of new entrants, the bargaining power of customers, the bargaining power of suppliers, the threat of substitute products, and the rivalry between existing players. To determine a strategic plan for growth in such a volatile business environment, an organization must understand how these forces operate in the industry and affect the company-specific situation.

Porter proposed measuring every activity of the company in terms of its overall competitiveness. Further, he proposed the use of value chain analysis of an organization's internal processes, and the interactions between different functions, to determine how and where value could be added. He also advocated three generic strategies: cost, differentiation and focus, which help the organization to compete effectively in the market place. These strategies determine the basis of competition. One can sum up Porter's work in three words, "vigorous domestic rivalry", which means that firms that engage in intense competition tend to survive and prosper.

IMPORTANCE OF STRATEGIC MANAGEMENT

As the above discussion indicates, strategy refers to the plans made and actions taken to enable an organization fulfill its intended objectives. When we speak of strategy as plans for the future, we refer to an intended strategy. When we speak of strategy as actions taken; we refer to a realized strategy. In both cases, we are considering the efforts directed towards fulfilling an organization's purposes. In fact, strategy comprises the most fundamental ends and means of an organization.

The Hierarchy of Strategic Intent

The term strategic intent refers to the purpose(s) an organization strives to achieve. The strategic ends pursued by a typical business could be either generic, like the vision and mission of the organization, or more focused, like the goals and objectives of the firm. Every organization needs to be careful to align the broad and narrow scenarios. Otherwise, money may be invested, time spent, energy dissipated and resources utilized to fulfill a narrow set of objectives that do not move in the direction of the broader vision of the firm. The focus of the set of narrow intentions should be consistent with the broader ones.

COMPONENTS OF STRATEGIC MANAGEMENT

Strategic planners should take into consideration different components of strategic management in finalizing their business strategy. A comprehensive understanding of these components helps in designing effective plans for the future of the organization. These components include: vision, company mission, company profile, external environment, strategic analysis and choice, long-term objectives, annual objectives, grand strategy, functional and operational strategies, policies, institutionalizing the strategy, and control and evaluation.

Vision

The company's vision is a description of what the organization is trying to do and become. It gives a view of an organization's future direction and course of business activity. It is often communicated through the mission statement. Above all, vision is a powerful motivator and keeps an organization moving forward in the intended direction.

Company Mission

The mission of a company sets apart one company from other companies in the same area of business. The mission identifies the scope of the company's operations, describes the company's product, market and technological areas of thrust, and reflects the values and priorities of its strategic decision makers. The mission of a business looks to an endless future as if the firm is immortal. Box 2 provides an illustration of company mission statement.

Box 2: Hewlett-Packard's Mission Statement
To let our growth be limited only by our profits and our ability to develop and produce technical products that satisfy real customer needs. We do not believe that large size is important for its own sake; however, for at least two basic reasons continuous growth is essential for us to achieve our other objectives. In the first place, we serve a rapidly growing and expanding segment of our technological society. To remain static would be to lose ground. We cannot maintain a position of strength and leadership in our field without growth. In the second place, growth is important in order to attract and hold high-caliber people. These individuals will align their future only with a company that offers them considerable opportunity for personal progress. Opportunities are greater and more challenging in a growing company.

Source: www.HP.com

Company Profile

The profile of a company depicts the quantity and quality of the company's financial, human and physical resources. The profile also assesses the strengths and weaknesses of the company's management and organizational structure. It also analyzes the company's past successes and traditional concerns in the context of the company's current capabilities, in an attempt to identify its future capabilities.

External Environment

The external environment consists of all the conditions and forces that affect an organization's strategic options and define its competitive situation. The external environment consists of three interactive segments. They are the operating environment, the industry environment and the remote environment.

Strategic Analysis and Choice

Strategic analysis enables a firm to identify a range of *possible* attractive investment opportunities. Opportunities that are compatible with the company's mission are identified as *desired* opportunities. Further weeding out from the list of *desired* opportunities, results in the identification of potential options or *strategic choices.* The entire process of strategic choice is meant to combine long-term objectives and generic and grand strategies, in order to place the firm in an optimal position in the external environment for achievement of the company mission.

Strategic analysis and strategic choice in a single or dominant product business involve the identification of strategies that are most effective at building a sustainable competitive advantage. Such a competitive advantage is based on key value chain activities and capabilities, i.e., the core competencies of a firm. Multi-business organizations focus on the best combination of businesses to maximize their shareholder value.

Annual Objectives

These are the objectives that the firm seeks to achieve in one year. Annual or short-term objectives relate to the same areas of business as do the long-term objectives. The major difference is that short-term objectives are more specific and are based on the long-term objectives. For instance, if the firm's long-term objective is to cut manufacturing costs by 20% in the next 4 years, then the annual objective might be to reduce its manufacturing costs by 5% every year. Hence, achieving short-term or annual objectives is crucial to attaining the long-term objectives.

Long-term Objectives

Long-term objectives refer to those results that an organization seeks to achieve over a number of years. Such objectives are typically set in terms of profitability, return on investment, competitive position, technological leadership, productivity, employee relations, public responsibility and employee development.

Grand Strategy

A grand strategy is a statement of means that indicates the methods to be used to achieve the company's objectives. This strategy is a unique package of long-term strategies. The grand strategy provides the framework for the entire business of the firm. Grand strategies focus on concentration, market development, product development, innovation, horizontal integration, vertical integration, joint venture, strategic alliance, consortia, concentric diversification, conglomerate diversification, turnarounds, divestiture, or liquidation.

Functional or Operational Strategies

The grand strategy is split into strategies for each business division or function. These strategies are referred as functional strategies. They are specific to the needs of each functional area and prescribe an integrated action plan for every function. In general, there will be one functional strategy for every functional area.

Operational strategies provide the means for achieving annual objectives. The company budget is coordinated with the needs of operating strategies to ensure specificity, practicality and accountability in the plans.

Policies

These are directives or guidelines given to managers and their subordinates as the framework to guide their thoughts, decisions and actions while implementing the organization's strategy. They help to make the operating processes consistent with the firm's strategic objectives, and are often referred to as standard operating procedures.

By standardizing routine decision-making and limiting the discretionary powers of managers and subordinates in implementing operations strategies, they increase managerial effectiveness.

A few examples of company policies or standard operating procedures are:

- The head office should authorize every purchase activity.
- The annual performance review of every employee should be undertaken on the individual's date of joining.

Institutionalizing the Strategy

The annual objectives, functional strategies, and policies are valuable channels for communicating what needs to be done to implement the overall strategy. The translation of long-term objectives into short-term goals will make the strategy operational. Implementation of strategy must be institutionalized. i.e., it must become part of the day-to-day activities of the company, if it is to be effectively implemented.

Three organizational elements: structure, leadership and culture help institutionalize a firm's strategy. Structure of the organization can influence the strategy when a particular function holds control over senior management. Similarly, a manager's perception of the business situation is influenced by various factors. His background and experience have a large bearing on the way he perceives the opportunities as well as threats. All these elements have to be integrated to ensure that strategy is successfully institutionalized and implemented.

Control and Evaluation

After a strategy is implemented, it should be monitored to determine the extent of success, i.e., the number of objectives achieved. Strategy formulation is largely subjective, and the first test of reality for a strategy is in its implementation. Strategic managers should employ early monitoring and control methods, to ensure that the strategic plan is followed. Early review and evaluation is also helpful for making modifications to the plan. The ultimate test of the strategy is its ability to achieve the ends – annual objectives, long-term objectives, and the company's mission. The firm is successful only to the extent that the strategy used achieves the designated objectives.

LEVELS OF STRATEGY PLANNING

There are three levels in the hierarchy of strategy planning. They are the corporate level, the business level and the functional level. Corporate level managers give direction to the organization. They steer the organization in the turbulence of the dynamic business environment. Business level managers give shape to the vision of the corporate managers. Functional level managers make the strategy a reality. Though their roles are clearly different the contribution of the managers at all three levels are equally important.

In a single business scenario, the corporate and business level responsibilities are clubbed together and undertaken by a single group, i.e., the top management, whereas in a multi business scenario, there are three fully operative levels.

Corporate Level

At the corporate level, strategies are devised in an attempt to exploit the firm's distinctive competencies by developing long-term plans for business operations. To a great extent, attitudes at the corporate level reflect the concerns of the stakeholders and society at large.

Corporate level strategy deals basically with the selection of the areas of business in which the company is going to operate. This strategy is concerned with the objectives of the organization, the ways in which business will be integrated and managed the development of synergies by coordinating and sharing different resources, and investment of financial resources across business units. Box 3 illustrates how strategy is implemented at corporate level.

Box 3: Ford's Revival
Henry Ford established the Ford Motor Company in 1903. Ford's first car, Model A, rolled out in the same year. The company introduced a number of expensive models, all of which eventually failed. Model T's introduction was a major turning point in the company's history. The car was initially sold for \$950, but the price was brought down to \$360 by the use of improved manufacturing techniques. By 1925, Ford was selling two million cars per year. But by the mid-1920s, GM's Chevrolet division began to increase its market share while Ford, basking in the success of Model T, lost touch with the market. GM introduced a variety of cars, and new models each year. GM also extended credit to customers, which Ford did not do. Not surprisingly, Ford began to lag behind GM. When Henry Ford II took over as the CEO in 1946, Ford began to change. He established "profit centers", closed obsolete plants and retrained workers. The company went public in 1956, and integrated companies in Europe. These corporate level strategies helped revive Ford.

Source: Ford, Global Strategic Management Case Studies on Fortune 500 Companies. (Volume IV, Transworld University, January 2000), 1.

Business Level

Business level strategy involves making decisions about the competitive position of a single business unit. The managers at this level translate the general statements of corporate strategic planners into exact, concrete, functional objectives and strategies for individual business divisions. Business level managers determine what the company's competitive advantage is to be based upon, in a specific product-market area. The goal of business level managers is to select, enter and grow in the most profitable market segment with the highest potential for growth. In short, this strategy is concerned with using generic strategies such as cost leadership, differentiation and focus to create competitive advantage. Box 4 shows how strategy is implemented at business level.

Box 4: ABB Minimizes Costs
Asea Brown Boveri (ABB) is a $30 billion global engineering group, and has business interests in electric power transmission, generation and distribution; automation; oil and gas; petrochemicals; industrial products and contracting; and financial services. The power transmission division provides products and solutions related to the transmission of power. The company's main operations are in various countries in Europe and the Americas, where deregulation has increased the demand for turnkey system solutions. ABB identified and chose cost management as the critical factor in the power transmission segment. Hence, the company chose to compete for market share on the basis of cost. The company chose to develop economies of scale to reduce costs. ABB standardized designs, products and manufacturing processes at 27 power transformer production plants worldwide. The result – the operating revenues of the company increased to $374 million in 1998 from $316 million in 1997.

Source: ABB, Global Strategic Management Case Studies on Fortune 500 Companies. (Volume III, Transworld University, January 2000), 6.

Functional Level

This level consists of managers from geographic, product and functional areas. These managers design short-term strategies and fix annual objectives in different areas such as research and development, finance and accounting, marketing, production, operations, and human relations. Functional level managers address problems related to the efficiency and effectiveness of production, success of particular products and services in increasing their market share, and quality of customer service. The functional objectives are quantifiable and are operational in nature. These objectives relate to a particular period. Hence, they can be modified from one period to another based on the requirements and functioning of the business. Moreover, the cost of failure of these strategies is relatively small and hence the risk perception is marginal. Box 5 illustrates how a strategy is implemented at functional level.

Box 5: Methods of Manufacturing at Canon
Canon's manufacturing activities are spread across 26 countries. To maintain uniformity in the quality of its products and to utilize manufacturing capacity to the fullest, Canon focuses on process innovations. Canon's manufacturing facilities are based on the concept of "any product on any line", and thus, the company has great flexibility. Canon also employs a "stop and fix it" system. Any worker can stop the line whenever a problem is noticed. A trouble-shooter on each assembly line helps the worker solve the problems on the spot when a problem occurs. This system not only gives the workers control over the assembly line but also makes sure that mistakes made at one stage are not

carried forward to the next stage of assembly. Approximately 3,000 parts are required for the different models of 'new process' copiers. Canon uses a computerized scheduling system to fix the numbers and types of copiers that are made each day. This system helps Canon to prevent mismatch of parts. This functional strategy also helps the company to cut down on both space requirements and inventory.

Source: Canon. Global Strategic Management Case Studies on Fortune 500 Companies. (Volume IV, Transworld University, January 2000), 15

MAKING STRATEGIC DECISIONS

Strategic management is defined as the set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company's objectives. Strategic management comprises nine critical tasks:

i. Formulating the company's mission, including broad statements about its purpose, philosophy and goals.

ii. Developing a company profile that reflects its internal conditions and capabilities.

iii. Assessing the company's external environment, including both the competitive and general contextual factors.

iv. Analyzing the company's options by matching its resources with the external environment.

v. Identifying the most desirable options by evaluating each option in light of the company's mission.

vi. Selecting a set of long-term objectives and grand strategies that will achieve the most desirable options.

vii. Developing annual objectives and short-term strategies that is compatible with the selected set of long-term objectives and grand strategies.

viii. Implementing the strategic choices by means of budgeted resource allocations in which the matching of tasks, people, structures, technologies and reward systems is emphasized.

ix. Evaluating the success of the strategic process as an input for future decision-making.

Characteristics of Strategic Decisions

There are several important differences between strategic management and various management functions like operations, human resources, marketing, accounting, finance, research and development, etc. The characteristics of strategic decisions are listed below:

Strategic Management Integrates Various Functions

Excellence in a wide range of functional specialties is considered an essential prerequisite for success in a competitive marketplace. There needs to be a guiding force that integrates the efforts of these specialists throughout the organization. Strategic management is central to capitalizing on functional expertise and integrating all functions to a suitably broad strategy for the organization.

Strategic Management Considers a Broad Range of Stakeholders

Organizations must meet the needs of various stakeholders such as customers, suppliers, employees, owners, managers, the government and the public at large. Corporate level managers must understand that their decisions affect the various stakeholders involved. Functional managers are expected to focus on individual stakeholders, rather than balancing the needs of all the stakeholders in the organization. For instance, a sales manager concentrates on the customers while the human resources manager pays more attention to the employees. The purchasing manager may have to think only about suppliers, and the production manager about product output and quality. This leads to the flow of effort in different directions. However, optimum results can be obtained only when all the resources of the different functions of the organization are integrated and utilized. Hence, the top management should have a strategic perspective and necessarily take account of all stakeholder groups when outlining strategies.

Strategic Management Entails Multiple Time Horizons

The top management cannot be oblivious to the long-run viability of the organization. It should have clear idea as to where the organization stands today and where it is expected to reach in the near future. In addition, it should be conscious of the short run and long run ramifications of different organizational activities. Functional managers tend to focus on short run issues alone. But as strategic planners, they can broaden their perspective to make a better contribution to the organization in the short run as well as in the long run.

Strategic Management is Concerned with Both Efficiency and Effectiveness

The difference between being efficient and being effective is the difference between *doing things right* and *doing the right things.* In their efforts to focus on doing things right, functional managers often neglect to do the right things that can lead their organization toward its ultimate objectives. Strategic management encourages a balanced emphasis on both these dimensions of managerial work.

Developing a Strategic Perspective

Developing a right strategic perspective contributes to effective implementation of strategy. However, organizations often fail to develop sound strategic management perspective for a variety of reasons. Some of these reasons are:

i. Lack of awareness within the top management team about the organization's real operating situation. This happens when information systems fail to provide the information that the top management needs to determine the organization's position relative to competitors, consumption trends, relative costs, etc.

ii. "Kidding themselves" syndrome: This happens when senior managers are collectively deluding themselves about the organization's condition. Usually this occurs when the senior management team acts as a tightly-knit group. As there is no flow of either fresh information or new perspectives, the top managers tend to hold the same stereotyped views of the business environment. They reject or ignore or reinterpret the unpleasant information that does not tally with their own preferred views of the operating environment.

iii. Vested interests of the managers also play havoc with strategic planning. Managers prefer to maintain their existing position and power. This personal interest results in continuation of the same strategies even in a changed business environment.

iv. Excessive involvement in everyday operational problems also leads to inefficient strategic plans. This over-emphasis on regular activities leaves no time to study emerging trends and to think about future plans.

v. The top management in many organizations gets complacent after some initial successes. This blinds the managers to difficult situations the company faces. This is another reason why managements often continue with tried and trusted strategies that may be inappropriate in the present and future scenarios.

vi. A change in direction is often misinterpreted as an admission that what was done in the past was a mistake. This makes managers who were closely associated with decisions taken in the past, reluctant to see the organization move in a new direction.

vii. Inability on the part of the top management to locate its competitive edge may also lead to its ignoring strategy planning altogether.

In general, organizations, like individuals, abhor change and resist it tenaciously. A crisis is necessary to make the top management pay more than lip service to strategic management. Perhaps the biggest hindrance to strategy formulation is the manager's involvement in day-to-day business. Everyday events drive away the best strategic intentions. The solution is to make strategy development process *a formal* activity.

SUMMARY

- Strategic management refers to a set of decisions and actions that result in the formulation and implementation of plans designed to achieve a company's objectives. Strategies used today in corporate wars have their origins in the battles of the past.
- The systematic study of strategic management was pioneered by Ansoff. Mintzberg added a new dimension to strategic management by bringing the personal side of the manager into the picture. Drucker introduced the concept of Management by Objectives (MBO). Later, Porter introduced the concept of competitive advantage and generic strategies like focus, cost leadership, cost differentiation to reduce the uncertainties of the competitive environment. He also suggested the study of different components of strategic management such as the environment, in which the company operates, through his 'five forces' theory.
- Strategic planners should take into consideration different components of strategic management in finalizing their business strategy. A comprehensive understanding of these components helps in designing effective plans for the future of the organization. These components include: vision, company mission, company profile, external environment, strategic analysis and choice, long-term objectives, annual objectives, grand strategy, functional and operating strategies, policies, institutionalizing the strategy and control and evaluation.
- The process of strategy formulation requires an understanding of the characteristics and value of strategic management. This exercise needs a clear strategic perspective and an understanding of the different levels in the hierarchy of strategy planning in an organization.
- Corporate level strategy deals with the challenges that arise from the changing external environment at the level of the organization as a whole. This level of strategy aims to make the organization proactive in facing the turbulence of the marketplace. Business level strategy is formulated with the perspective of changes that might be necessary in the future at the level of business divisions or strategic business units. Functional level strategy addresses the need for short-term objectives concerned with various functional departments like production, operations, R&D, financial accounting, marketing, and human relations.

Chapter II

Strategic Management Process

After reading this chapter, you will be conversant with:

- The Process of Strategic Management
- Strategic Decision-making
- Practical Limitations of the Strategic Management Model

Introduction

Strategic management involves the study of an organization's internal and external environments in order for the organization to discover and take advantage of available opportunities. It also involves deciding upon identifying and building competitive advantages to attain the desired objectives. Effective integration of the different stages in the process of strategic management is necessary to achieve the desired outcome of competitiveness. Through proper integration, organizations can leverage their resources, core competencies and capabilities, to compete effectively in the global market.

In Chapter I, we looked at the components of strategic management. In this chapter, we study how strategic management is undertaken, using each of its components. In other words, we look at the process of strategic management.

A company's mission reflects the strategic intent of the organization, the products it plans to manufacture and the markets it plans to serve. The mission influences the formulation and implementation of strategies. Objectives are outlined in order to translate managerial statements of strategic vision and business mission into clearly defined performance targets. Corporate managers get valuable feedback by measuring the actual results against the targets set.

A company's objectives and methods of implementing strategy are not fixed for all time. Periodic reviews of strategies and the incorporation of new elements in line with changes in the environment are essential in strategic management.

THE PROCESS OF STRATEGIC MANAGEMENT

A process in management is defined as a perceptible flow of information through interrelated stages of analysis directed towards the achievement of an aim. There are four basic elements in the process of strategic management:

- Environmental scanning,
- Strategy formulation,
- Strategy implementation, and
- Evaluation and control.

Box 1 demonstrates the benefits of environmental scanning, strategy formulation, and strategy implementation in a firm.

Box 1: Sears Reinvents Itself

Not long back Sears was the largest retailer in the United States. Its legendary 'Big Book' catalog was considered the primary (and sometimes the only) source for items ranging from wrenches to bathtubs. In the 1980s, Sears entered other businesses such as banking, investment and real estate service, in addition to selling appliances, hardware, clothes and other goods.

Sears moved away from its main business, retail sales, with this new development. The company steadily lost ground in retailing, falling from the Number 1 position to Number 3 behind Wal-Mart Stores, Inc. and Kmart Corporation. Sears could not keep up with discounters such as Wal-Mart and Kmart, and with specialty retailers such as Toys R Us, Home Depot, Inc. and Circuit City Stores, Inc. that focused on a wide selection of low-price merchandise in a single category. Neither could Sears compete with trend-setting department stores. In the 1990s, Sears came to a stage where it was neither sure of its customers nor its competitive basis. This was a lacuna in the company's strategy.

Arthur C Martinez, the then CEO of Sears, went in for a major strategic overhaul. Under the new strategy, the company decided to concentrate on its core businesses. It disposed off its non-retail assets, upgraded the section on women's apparel, renovated dowdy stores and launched an advertising campaign to effect a turnaround at Sears. Through extensive customer research, Sears found that its hardware lines enjoyed a very high level of brand loyalty. Moreover, research suggested that customers preferred convenience to breadth of category in its hardware stores.

After its hardware store idea was successfully tested, the company drew up a plan to set up 1,000 freestanding, 20,000-square-foot hardware stores by 2006 at a cost of $1.25 million per outlet. After this exercise in strategic management, the company was confident of doing well in the future.

Source: John A, Byrne, Strategic Planning, Bureau reports. 2001.

Environmental Scanning

Environmental scanning involves monitoring the environment, and evaluating and disseminating information obtained from the internal and external environments. The aim of environmental scanning is to identify the strategic factors that may determine the future of the firm. An organization can derive several benefits from environmental scanning including the development of a common perception, identification of strengths and weaknesses, an understanding of trends and conditions, and the optimum utilization of internal and external information. Tools such as surveys, questionnaires, focus groups, and open forums can be employed in environmental scanning.

SWOT analysis is the most commonly used technique for environmental scanning. SWOT is an acronym for the strengths, weaknesses, opportunities and threats faced by a firm. Strengths and weaknesses are within the control of the top management in the long run. Opportunities and threats are external factors that are outside the control of the organization. The key strengths of the firm become the core competencies that the organization can use to gain competitive advantage.

Strategy Formulation

Strategy formulation refers to the development of long-term plans for managing opportunities and threats in the external environment, and for utilizing the strengths and overcoming the weaknesses within the organization. A strategist takes into consideration components of strategic management such as company mission, company profile, external environment, strategic analysis and choice, long-term objectives, annual objectives, grand strategy while formulating a strategy.

Strategy formulation helps an organization to:

- Capitalize on available opportunities.
- Address the challenges faced by the organization.
- Provide leadership that understands and masters change.
- Incorporate an in-depth planning model that involves the community.

Strategy Implementation

The process by which strategies are put into action is called strategy implementation. Programs, budgets and procedures are developed for this purpose. This process may call for changes in overall culture, organizational structure, and/or the management system. The implementation of strategy is typically handled by middle and lower level managers, except when drastic company-wide changes are needed. However, implementation is reviewed by the top management from time to time.

Requirements for Strategy Implementation

STRUCTURE

The firm's structure plays a vital role in achieving firm's objectives. A proper structure is essential for strategy to be operational. Structure serves as a vehicle for managers to exploit the skills and capabilities of their employees. They can further use the structure in motivating their employees through providing incentives to ensure superior efficiency, quality, innovation or customer responsiveness.

BUDGET

This is a statement of the programs to be implemented in monetary terms and is used for planning and control. The budget details the investments to be made and the returns expected from the investments. The budget is also a proforma financial statement.

Evaluation and Control

Evaluation and control refer to the processes in which corporate activities and performance results are compared with the desired performance. This information is used to take corrective action and resolve problems. It also pinpoints the weaknesses of strategic plans implemented earlier. Thus, this exercise provides a valuable opportunity for organizational learning.

For effective evaluation and control, the management must obtain clear, prompt and unbiased information from the people who actually execute the strategies. Unbiased information is essential as this information is used for corrective action and to minimize the mistakes the organization might commit in the future.

Feedback is a very important part of the evaluation process as it provides an opportunity to revise or correct decisions made in the earlier stages. Poor performance indicates that something has gone wrong with either strategy formulation or implementation. It could also mean that a variable was ignored in the environmental analysis.

Implications for Managers

Looking at strategic management as a process, helps to highlight certain aspects of the model:

- A change in any component will have an influence on several other components.
- In the two-way impact at various levels of the strategic management model, the flow of information or impact is reciprocal. For instance, the mission has an effect on the environmental variables, and vice versa.
- The process of strategic management should be kept flexible. If the strategic plan has to be reevaluated because of factors like the entry of new competitors or appointment of a new CEO for the firm, then the process should start once again with environmental analysis. However, equal attention should not be given to all the components of the process; instead, attention paid to different components should be based on need. The mission statement may remain the same for a longtime, whereas objectives and strategies may have to be updated annually in tune with the achievements of the firm.
- This perspective implies that feedback from institutionalization, review, and evaluation will loop back into the early stages of planning. Feedback is defined as the post-implementation results, collected as inputs for future decision-making. Thus, plans for the future should reflect changes brought about by previous strategic actions. The management also needs to study, measure and analyze the impact of strategies for possible modifications in the company mission.

STRATEGIC DECISION-MAKING

Strategic management places a heavy emphasis on strategic decision-making. As organizations grow larger and environments become more uncertain, decisions become increasingly complex and difficult to make. Before we study strategic decision-making in detail, we should have an idea of why some decisions are called strategic.

For a decision to be called strategic, it should have the following characteristics:

- It deals with the long run future of the entire organization.
- It commits substantial resources and demands a great deal of commitment from people at all levels.
- It acts as a directive. It sets a precedent for lower level decisions and future actions, and has implications for the entire organization.

Modes of Strategic Decision-making

Henry Mintzberg has classified strategic decision-making into three different modes:

- Entrepreneurial mode
- Adaptive mode
- Planning mode.

ENTREPRENEURIAL MODE

In this mode, strategies are framed by one powerful individual. The entrepreneurial mode focuses solely on the organization's opportunities. Problems associated with strategy are given secondary importance. Strategy is formulated based on the founder's own vision of direction and is exemplified by bold decisions. The dominant goal is the growth of the organization. Apple Computers provides an example of this mode of strategic decision-making. The disadvantage of this mode is that it does not consider problems that may arise during strategy implementation. The advantage is the speed with which a strategy can be formulated and implemented. Box 2 gives an example of entrepreneurial mode of decision-making.

Box 2: Decision-making at Apple
Steve Jobs, the founder of Apple Computers is considered a brilliant man in Silicon Valley. His innovative ideas of user-friendly software for the Macintosh changed the design and functionality of software interfaces created for computers. But Jobs ignored the advice of experts who advised him to keep in touch with intended customers and avoid the pitfall of anaerobic isolation; not to assume that customers would pay any price to secure the latest computer technology; and, to ease the way for customers to adopt a new standard by providing software and hardware bridges that would help in connecting older machines to new ones. He introduced the first personal computer controlled by a mouse – Lisa, which had a user-friendly interface, but had an un-friendly price of $10,000. The product failed miserably in the market place. The company's products also lacked coherence. Each of Apple's three computers used a separate operating system. This approach cost Apple millions of dollars in lost sales.

Source: www.Apple.com

ADAPTIVE MODE

This mode is characterized by reactive solutions to existing problems. This mode of decision-making results in a fragmented strategy with incremental improvement. Companies such as Barnes and Noble, and Coke employ this type of decision-making.

PLANNING MODE

In this mode, appropriate information for situational analysis is gathered systematically. A few feasible alternative strategies are developed and the most appropriate strategy is selected. The planning mode encompasses both a proactive search for opportunities and a reactive solution to existing problems. The planning mode helps the company to be better prepared for environmental uncertainties.

There is a fourth approach that might be followed by a company – logical incrementalism. It is a synthesis of the above three approaches. When developing strategies, organizations choose an interactive process for probing the future, experimenting, and learning from a series of incremental commitments. This approach is useful when the environment is changing rapidly and it is important to build a consensus before committing the entire company to a specific strategy.

Strategic Decision-making Process

Though every mode of strategy can be used in one situation or the other, the planning mode, which includes the basic elements of the strategic management process, is a more rational and better method of strategic decision-making. It is more appropriate for dealing with complex and changing environments. An eight-step strategic decision-making process has been advanced by Hunger and Wheelen for improving strategic decision-making.

PRACTICAL LIMITATIONS OF THE STRATEGIC MANAGEMENT MODEL

The limitations of the strategic management model must be recognized to understand how the model can be used properly. An awareness of its limitations will help to ensure effective strategic management. All models have three important practical limitations: the models are holistic, analytical, and non-political.

Holistic vs. Tactical

Strategic planning should be initiated by the company's top management. Because of the broad perspective of executives at a high level, the strategy evolves from the general to the specific. The business is first studied as a whole, then from the standpoint of individual divisions or functions, and in the end the specific operational activities of the firm.

Some researchers argue that the holistic approach is inferior to the tactical approach (which is the exact opposite of the holistic approach). Since strategic managers work high up in a firm, they should start by obtaining an operational view of the firm's strengths and weaknesses, and then end with the firm's compatibility with the external environment.

The risk of using a holistic model is the tendency to overlook difficulties in implementation. It may sometimes lead to managers glossing over details that may eventually prove critical. However, the tactical approach poses greater risks as it is not flexible. Using the tactical approach, managers may put more than necessary emphasis on narrow operational issues, thus making it difficult to envisage new opportunities. Another disadvantage of the tactical approach is that it is difficult to integrate with planning activities. The initial phases of planning in the tactical approach are disjointed in nature. The tactical approach also concentrates more on the present than on the future. Strategic planning, however, is intended to be future-oriented. The tactical approach also concentrates more on improving current capabilities rather than on satisfying anticipated needs.

In conclusion, it appears that the holistic approach is superior to the tactical alternative. However, users must be alert to the data-gathering and implementation problems of the holistic approach.

Analytical vs. Prescriptive

Another major issue to be aware of when using the strategic management model is that it is analytical rather than prescriptive or procedural. The model generally describes the logical or analytical steps that many businesses actually use in their strategic activities. However, it does not prescribe the procedures required for each step. The model gives a general approach towards strategic planning and not a sure way to success. The model is only a dependable outline on which individualized planning systems can be constructed.

Non-Political

The third limitation is that it is non-political. The model appears to be devoid of subjective assessments, intuitive decision-making, favoritism, human error and other forms of political activity. However, strategic management being a behavioral activity is as prone to these pitfalls as other people processes.

It is truly a management process. The people involved in the process must be skillfully led, organized, planned for, and controlled. Therefore, people-related concerns have to be skillfully managed by effective strategic managers. The limitation with this strategic management model is that it presumes that strategic planners are skilled managers, and does not incorporate the political elements explicitly.

The strategic management process goes through continual assessment and updating. While elements do not change, the relative emphasis each element receives varies with decision makers and the environments in which the company operates. The negative consequences of instituting a strategic management process such as inability to react and adapt to current happenings can be overcome as firms gain knowledge, experience and skill in designing and managing planning activities.

SUMMARY

- The process of strategic management consists essentially of environmental scanning, strategy formulation, strategy implementation, and evaluation and control. Environmental scanning is a study of the external environment, focusing on both the remote and the operating environments. Comprehending the external environment is a prerequisite for strategic management because it influences the organization and also gets influenced by the company's activities.
- Strategy formulation involves setting up long-term and short-term objectives. This process also involves choosing a mix of strategies and designing policies that guide the execution of strategy. As policies determine the extent of success of any strategy, they should be designed carefully. The top management also wields influence over the formulation and implementation of strategies through framing policies.
- Strategic decisions can be undertaken in the entrepreneurial mode, the planning mode or the adaptive mode. The process by which strategies and policies are put into action is called strategy implementation. Programs, budgets, and procedures are developed for this purpose. This process may call for changes in the company's culture, the organizational structure, and/or the management system. The implementation of strategy is typically handled by middle and lower level managers, except when drastic company-wide changes are needed. But implementation is reviewed by the top management from time to time.
- The evaluation phase marks the beginning and the end of the strategic management process. It includes a thorough review of the results of the strategy in terms of its contributions in financial and operational terms, and in terms of social goals.
- The careful use of strategic management can assure better returns for shareholders and help develop the potential of the organization. Nevertheless, there are some practical limitations. The strategic management model is criticized as being too holistic, excessively analytical and non-political.

Chapter III

Company Mission and Vision

After reading this chapter, you will be conversant with:

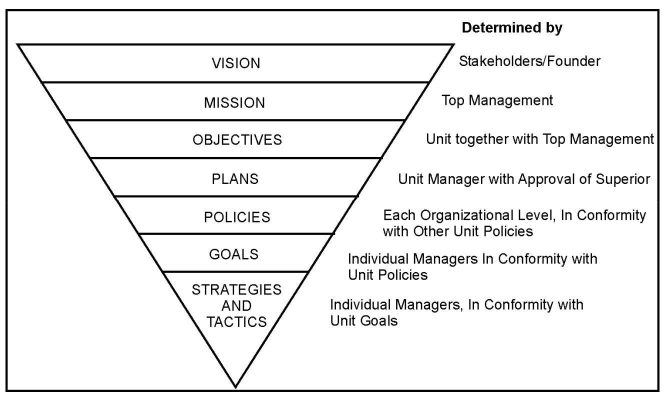
- Vision
- Mission Statements
- Social Responsibility
- Stakeholders Approach to Social Responsibility
- Guidelines for a Socially Responsible Firm

Introduction

An organization's vision and mission act as guidelines for strategy formulation. The process of strategy formulation involves articulating a vision for the organization, translating the vision into a mission that defines the organization's purpose, converting the mission into performance objectives, detailing each objective into specific goals, and formulating tactics and strategies for accomplishing the goals (Refer Figure 1).

The vision of a company provides managers with unity of direction that transcends individual, parochial and transitory needs. It projects a sense of worth and intent that can be identified and assimilated by those inside and outside the company. A vision becomes tangible when it is expressed in the form of a mission statement. Such a statement verbalizes the beliefs of the manager and the directions in which the manager seeks to lead the organization. A company's mission embodies the business philosophy of strategic decision-makers, reflects the firm's self-concept (how the firm perceives itself), and indicates the principal product or service areas, and identifies the primary customer needs that the company attempts to satisfy. It describes the market, product and technological areas of the business and in doing so, reflects the values and priorities of strategic decisions-makers and guides future executive action. A well designed mission statement talks about customer needs (what needs of the customer are satisfied?), customer groups (who is served?), the company's activities, technologies, and competencies (how does the enterprise create and deliver value?).

Figure 1: Organizational Direction



Source: P Subba Rao, Business Policy and Strategic Management, (Himalaya Publishing House) 91.

VISION

A well-conceived vision comprises two main components. First component is core ideology. The second component is an envisioned future. A good vision builds upon the play between these two complementary forces. A good vision defines core ideology, "what we stand for and why we exist" that never changes and sets forth envisioned future, "what we aspire to become, to achieve, to create" that demands significant change and progress.

The vision needs to be specific so that scope for different interpretations is minimized. The vision needs to be communicated effectively as a first step to its actual implementation. Both effective communication and effective implementation require substantial effort and deployment of resources.

The vision of an organization is what insiders of the organization create or perceive. However, vision should also reflect the concerns of other stakeholders such as shareholders, customers, the local community and society in order to be effective. The support of shareholders is necessary to bring about any major change in the organization. The vision of the company should also try to streamline and correlate the personal goals of employees with organizational goals to the extent possible.

MISSION STATEMENTS

A company's mission plays a critical role in its survival. The absence of a mission often results in the failure of a firm since its short run actions can be counterproductive to the firm's long run purpose. Firms without a mission identify the scope of their operations in product and market terms only. A mission statement, on the other hand, describes the product, the market and the technological areas of emphasis for the business, and forms its overriding *raison d'etre*.

The term 'mission' is defined as "the fundamental and enduring purpose of an organization that sets it apart from other organizations of a similar nature". The mission statement is an enduring statement of purpose for an organization; it refers to the philosophy of the business and serves to build the image of the company in terms of activities currently pursued by the organization, and its future plans. This philosophy establishes the values, beliefs and guidelines for business plans and business operations. Mission statements come in various forms but the most effective are those that are direct, precise and memorable. Most corporate mission statements are built around three main elements:

- **History of the organization:** The critical characteristics and events of the past must be considered while formulating and developing a mission statement.
- **Distinct competencies of the organization:** The articulation of key goals that reflect the distinct competencies of the organization where it offers an advantage over other organizations.
- **The environment of the organization:** The management should identify the opportunities provided and threats or challenges posed by the environment before formulating a mission statement.

The characteristics of a good mission statement are:

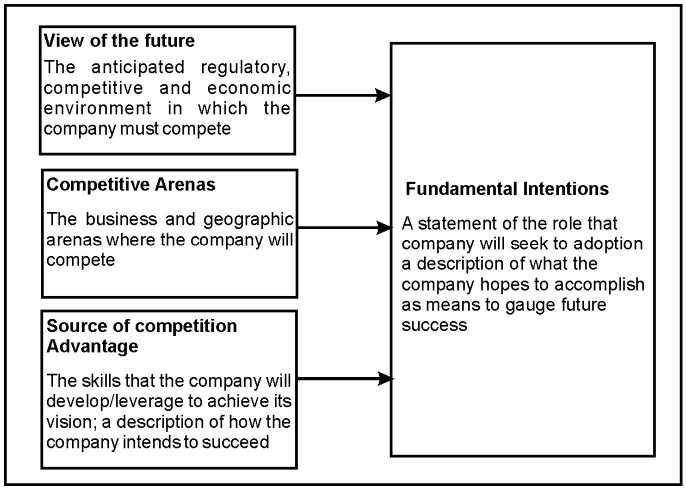
- It differentiates the company from its competitors.
- It defines the business (es) that the company wants to be in, not necessarily the one(s) it is in.
- It is inspiring.
- It is relevant to all the stakeholders in the firm, not just shareholders and managers.
- It attempts to ensure that the organization behaves in the way that it promises it will by defining the purpose for which the firm exists.
- It seeks to clarify the purpose of the organization – why it exists.

A mission statement usually attempts to answer the following questions:

- What is our reason for being? What is our basic purpose?
- What is unique or distinctive about our organization?
- Who are, or should be, our principal customers, clients?
- What are, or should be, our principal economic concerns?
- What is likely to be different (from its existing state) about our business three to five years in the future?
- What are our principal products at present and what will they be in the future?
- What are the basic beliefs, values, aspirations and philosophical priorities of the firm?

The key elements of a mission statement are explained in Figure 2.

Figure 2: Key Elements of a Mission Statement



Source: James Balloun and Richard Gridley, "Post Merger Managementa: Understanding the Challenges," Mickey quarterly, Fall 1990.

Formulating a Mission Statement

The process of formulating a mission is best understood by considering a firm at its inception. A typical business organization begins with the aspirations and beliefs of a single entrepreneur. The mission is then based on the following fundamental assumptions:

i. The product or service can provide benefits at least equal to its price.

ii. The technology to be used in production will provide a product/service that is competitive in cost and quality.

iii. The product or service can satisfy a customer need currently felt by specific market segments.

iv. The management philosophy of the business will result in a favorable public image.

v. The business will provide financial rewards for those willing to invest their labor and money in the firm.

vi. With hardwork and the support of others, the business can grow and be profitable in the long run.

vii. The entrepreneur's concept of the business can be communicated to and adopted by employees and stockholders.

As the business grows, the company may redefine its mission statement. The revised mission statement generally reflects the same set of elements as the original. It will state:

- The basic type of product or service to be offered.
- The primary markets or customer groups to be served.
- The technology to be used in production or delivery.
- The fundamental concern for survival through growth and profitability.
- The public image sought.
- The managerial philosophy of the firm.
- The firm's self-concept.

Basic Product, Primary Market and Principal Technology

The three indispensable components of a mission statement are the basic product, the primary market and the principal technology used in production or delivery. These three components describe the business activity of the company. The business plan of ITT Barton, a division of ITT, covers these three mission components in its statement. The company presents the following information under the heading of "Business Mission and Area Served."

"The unit's mission is to serve the industry and government with quality instruments used for the primary measurement, analysis and local control of fluid flow, level, pressure, temperature and other fluid properties. The instruments produced by the unit include: flow meters, electronic readouts, indicators, recorders, switches, liquid level systems, analytical instruments such as titrators, integrators, controllers, transmitters and various instruments for the measurement of fluid properties (density, viscosity, gravity) used for process variable sensing, data collection, control and transmission.

Markets served include instrumentation for oil and gas production, gas transportation, chemical and petrochemical processing, cryogenics, power generation, aerospace, and government as well as other instrument and equipment manufacturers."

The mission statement stated above clearly indicates to all readers the firm's basic products, primary markets and principal technologies.

Company Goals

A mission statement has to be more specific than the company's vision. Nevertheless, a mission statement hardly ever gives concrete directions for action. Hence, the need for more specific company goals. Just as the mission statement tries to make a company's vision more specific, company goals attempt to make a mission statement more concrete. Profitability is one of the important goals of any business organization. Profit can be measured or defined in different ways. In the long run, profit is accepted as "the clearest indication of a firm's ability to satisfy the principal claims and desires of employees and stockholders." However, there is a danger that decisions aimed at short-term profitability will lead to strategic myopia. Hence, the need for a long-term perspective. If a firm overlooks the concerns of customers, suppliers, creditors, and regulatory agents, the short run results might be profitable, but in the long run, the financial consequences are likely to be detrimental.

Goals indicate a desired future state that a company attempts to realize. To be meaningful, goals should have three main characteristics:

- **They should be precise and measurable:** If a goal cannot be stated precisely and measured accurately, the company will face difficulties in assessing its progress in attaining that goal.
- **They should address important issues:** To maintain its focus, an organization should operate with a limited number of major goals. This implies that only important goals should be selected.
- **They should specify a time period in which they should be achieved:** Deadlines can inject a sense of urgency into goal attainment and act as motivators.

The features of the strategic goals of an organization are:

- **They address both financial and non-financial issues:** The financial goals aim at profitability. Whereas non-financial goals aim at abstract elements which cannot be quantified in money terms. For example, the financial goal of Boeing is "Profitability as measured against our ability to achieve and then maintain a 20% average annual return on stockholder's equity." But, the non-financial goal of Boeing is "Integrity, in the broadest sense, must pervade our actions in all relationships, including those with our customers, suppliers and each other. This is a commitment to uncompromising values and conduct. It includes compliance with all laws and regulations."

- **They facilitate reasonable trade-offs:** Most businesses have a range of goals, all of which are not consistent with one another. For example, a firm may aim at low-cost leadership and good employee relations simultaneously. If a recession occurs, managers may face a dilemma. On the one hand, maintaining the workforce will lead to losses (as it might destroy the firm's cost competitiveness); on the other hand, laying off workers will result in poor employee relations. Goals guide the firm in deciding about the alternative (whether to choose low cost position or buy peace with workers). Thus, the management's task in such situations is to make the trade-offs required and establish goals that help to resolve such difficult situations.
- **They can be reached through "stretch":** Appropriate goals force the organization to "stretch" itself beyond these limitations in order to reach the projected goals. By constantly setting goals that demand more and more effort, an organization is more likely to reach its fullest potential. However, the goals should not be set arbitrarily as this might harm the organization instead of motivating its employees.
- **They cut across financial areas:** In order to facilitate supervision and efficiency, organizations are classified into various departments or functions. However, goals cut across the organization and operate as an integrating force. Without well-understood goals, departments are likely to act independently, and this will hamper the progress of the organization.

The mission statement should explicitly acknowledge the importance of long-run survival, profitability and economic growth. The mission statement of Hoover Universal identifies the concern for survival. It states, "In this respect, the company will conduct its operations prudently, and will provide the profits and growth which will assure Hoover's ultimate success."

Defining a company's mission, bearing in mind the need for growth, is a difficult task. This is because an organization has to plan as well as keep its options open for the future, in terms of the products the firm will manufacture, the markets the firm will enter, and the technology it will choose. This process is a delicate one as overemphasis on planning might lead to the firm's inability to respond spontaneously. Hence, the firm should make clear when it is going to deviate from its plans. Thus, one can safely conclude that goals are the most specific form of strategic intent. Setting and pursuing goals is an essential process as goals give a general sense of direction and provide specific benchmarks for evaluating the company's progress in achieving its aims.

Company Philosophy

Company philosophy and values give a framework/boundary for individual actions aimed at achieving corporate goals. A company's philosophy is also known as its creed, and usually forms a part of the company's mission. It reflects or states the basic beliefs, values, aspirations, guiding principles and philosophical priorities that the strategic decision-makers are committed to emphasize in their management of the firm.

Box 1: The Company Philosophy of Sun Microsystems
"We believe human development to be the worthiest of the goals of civilization for nurturing growth in the capabilities of people."

Source: www.sunmicrosystems.com

Public Image

Public agitation often stimulates a heightened corporate response, but an organization is generally concerned about its image even in the absence of expressed public concern. Customers associate certain qualities with certain companies. For example, Johnson & Johnson products are regarded as “safe” products and Sony’s products as “quality” products. Companies influence this process of association through various public relation exercises. A company sets out to create a particular public image from the start. The mission statement should reflect the public image. Thus, Johnson & Johnson’s mission should not leave scope for diversification into handful pesticides. The issue of public image is more important to a growing firm that is involved in redefining its markets, products, and its mission.

Company Self-concept

A major determinant of any company’s continued success is its continuous interaction with the external environment. In a competitive environment, a firm should realistically evaluate its own strengths and weaknesses. The idea that the organization/firm must “know itself” is the essence of the term ‘company self-concept’. A firm’s ability to survive in a dynamic and highly competitive environment would be severely limited if it did not understand the impact that it has or could have on the environment. A company’s mission reveals its self-concept. The strategic decision-makers should see the firm as a socially responsive, prudent and independent entity. The mission statement of Hoover Universal reflects its self-concept, stating that: “Hoover Universal is a diversified, multi-industry corporation with strong manufacturing capabilities, entrepreneurial policies and individual business unit autonomy”.

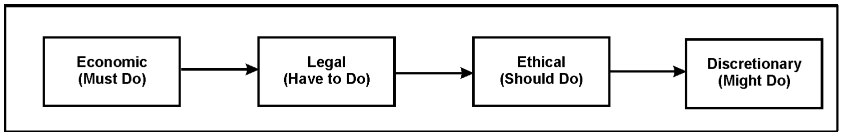
SOCIAL RESPONSIBILITY

Corporate social responsibility is a public movement that has gained momentum over the past few decades. Citizens have started demanding that corporations be accountable for their actions. This movement has resulted in business managers becoming more transparent and socially responsible in their actions. Organizations are being pressurized to improve their performance not only in financial but also in non-financial areas. As a result, organizations have started building social criteria into their strategic decision-making. Human rights issues and healthy environmental practices are no longer seen as compromising on profitability. The firms with a good reputation in these areas are regarded highly by the public and are often able to sustain profits even under adverse circumstances.

Managers of business organizations have four social responsibilities:

- **Economic:** This responsibility deals with producing goods and services of value to society so that the firm may repay its creditors and shareholders.
- **Legal:** Legal responsibilities are laid down by governments. They are set out as laws that organizations have to obey. For example, environmental pollution norms have to be adhered to by all factories under the purview of the Pollution Control Board (PCB). To this effect, the PCB issues compliance certificates to these factories and inspects them periodically to check facilities.
- **Ethical:** Ethical responsibilities involve the widely-held beliefs about behavior in a society. Society expects companies to adhere to its ethical norms and reacts negatively to what are seen as unethical practices.
- **Discretionary:** Discretionary responsibilities refer to the purely voluntary obligations that a corporation assumes, such as philanthropic contributions and training the unemployed. Ethical responsibilities are obligatory whereas discretionary responsibilities are purely voluntary. The four responsibilities are shown according to the priority attached to them in Figure 3.

Figure 3: Responsibilities of Business



Source: AB Caroll, "A Three Dimensional Conceptual Model of Corporate Performance," Academic of Management Review, October 1979, p 499.

A firm can behave responsibly in the interests of society in a number of ways. Social responsibility is not a one-way process; the organizations themselves benefit considerably by undertaking greater social responsibility. To whom are organizations responsible? The answer to this question is: all who come under the category of 'corporate stakeholders'. The stakeholders are those who affect, or get affected by, the business activities of corporations. The category of stakeholders comprises the following groups:

Shareholders: Shareholders provide the capital that is necessary for firms to survive and grow. In turn, they expect the management to operate in ways that bring them the highest possible return on their investment. Shareholders and managements sometimes hold different perspectives on business opportunities. These different perspectives occasionally lead to conflict.

Employees: Although, managers speak of their organization's employees as "members of the family", their actual treatment of employees may not always conform to this ideal. One area of concern is the treatment of employees during plant closures. Plant closures should be accompanied by a degree of managerial concern for employees.

Customers: Several decades ago, words like *caveat emptor* (let the buyer beware) were used to indicate that the firm had little responsibility towards its customers. However, this is no longer acceptable as customers punish firms with this attitude by turning away from their products. Social concerns such as health, safety and quality are also gaining greater prominence.

Local Community: The community in which an organization operates is its local area of influence. While communities usually want businesses in their areas, businesses in turn expect various forms of infrastructure facilities like adequate transportation systems, gas, electricity services, etc. Organizations provide goods and services the community needs. They also provide employment opportunities to its constituents. Thus, organizations cater to the needs of the local community and benefit.

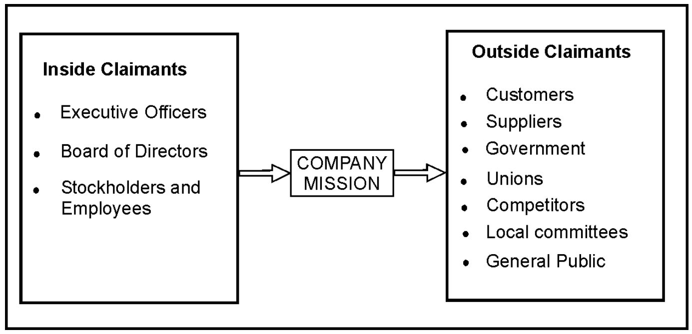
Society: Social responsibility at the societal level encompasses issues that are regional and national in scope. Some organizations provide training in basic skills to help workers meet the requirements of available jobs. Organizations also take on environmental responsibilities such as recycling, waste disposal, protecting the ozone layer and energy efficiency.

An interesting question that arises is whether companies that are socially responsible are more successful financially. It is difficult to arrive at an answer because it is not easy to measure the social responsibility of one firm against that of another. Research suggests that a firm's financial performance influences its ability to undertake socially responsible activities. Firms engaged in socially responsible activities build stable relationships with their major stakeholders. This helps them to reduce the risk of lawsuits and governmental fines that threaten organizational well-being.

STAKEHOLDERS APPROACH TO SOCIAL RESPONSIBILITY

Strategic managers must recognize and acknowledge the legitimate role of stakeholders of the firm in defining or redefining the company mission. The stakeholders of a firm can be divided into two categories: insiders and outsiders. This is graphically represented in Figure 4.

Figure 4: Claimants to a Company Mission



Source: Daniel J McCarthy, Robert J Minichiello and Joseph R Curran, Business Policy and Strategy – Concepts and Readings (Delhi: AITBS, 1996, 4th Edition) 133.

The insiders are the groups and individuals who are stockholders and persons employed by the firm. The outsiders are groups and individuals who are not insiders, but are affected by firm's production and marketing of goods. The outsiders commonly include customers, suppliers, the government, competitors, the local community and the general public. The insider and outsider groups expect the organization to act in a responsible manner towards the satisfaction of their claims. The claims of various groups of stakeholders on the organization include:

- The stockholders' claim to appropriate returns on their investments.
- The employees' claims for job satisfaction and compensation leading to certain standard of living.
- The customers' desire for value for their money.
- The suppliers' requirement of dependable buyers.
- The Governments' desire for adherence to legislated roles, regulatory roles, regulations, laws and taxes.
- Competitors' unwillingness to face unfair competition.
- The Unions' wish for benefits for members in proportion to their contribution to company success.
- The claim of local communities, which expect companies to be responsible "citizens."
- The assurance sought by the general public that the quality of life will be improved as a result of the firm's existence.

When an organization attempts to define its mission, it incorporates the interests of various claimant groups. This process involves four steps.

Identification of Claimants

Every business deals with a different set of stakeholder groups, which might vary in number, size, influence and importance. Consequently, while defining the mission statement, the strategic managers must identify all the stakeholder groups and weigh their relative rights and their relative abilities to affect the firm's success.

Understanding Claimants' Demands vis-a-vis the Company

The strategic managers should understand the specific demands of each group of stakeholders. By doing so, they would be in a better position to appreciate and respond to the concerns of claimants. The outsider group considers issues like the wastage of resources, contamination of air and water, and depletion of natural resources the key considerations in the strategic decision-making of the firm. The insider group, on the other hand, believes only in the progress of the organization. Hence, the need arises for balance between the internal and external forces.

Recognition and Prioritization of Claims

The concerns of various stakeholder groups are often in conflict. For example, the claims of the government and the general public tend to concentrate on the aspect of quality of service. This could limit profitability, which is the central concern of the shareholders and the creditors. Thus, in a mission statement, claims must be reconciled in order to resolve the competing, conflicting and contradictory claims of stakeholders. The mission statement should have internally consistent and precisely focused objectives and strategies that display unity of purpose, while taking account of the multiple claims on the business.

Coordination of Claims and Mission Components

The demands of stakeholder groups constitute only one set of inputs to the company mission. Other principal determinants are the managerial operating philosophy and the factors related to product – market or offer in the market. A question that arises is: How can the company simultaneously satisfy claimants and optimize its success in the marketplace? The answer one can get is that the issues related to the claims of stakeholders are as complex and situational as to defy clearly defined rules of conduct. Thus, each organization must decide on its own approach to fulfill its perceived social responsibility. Different approaches reflect the various situational factors and differing priorities of the claims on the company. Companies discuss their efforts and achievements in acting in a socially responsible fashion primarily through their annual reports.

GUIDELINES FOR A SOCIALLY RESPONSIBLE FIRM

Even after decades of public debate on the social responsibility of business, the individual firm has to struggle to determine its own orientation. The guidelines for a socially responsible firm are listed below:

- The main purpose of a business is to make profit. Strategic managers should strive for the optimal profit that can be achieved over the long run.
- Profits cannot be claimed until business costs are paid. These costs include all the costs determined by a detailed analysis of the social balance between the firm and society.
- If there are social costs in areas where no objective standards for correction exist, managers should generate a corrective standard. The corrective standards should be based on the manager's judgment of what ought to exist and should encourage the individual involvement of stakeholders in developing the necessary social standards.
- When competitive pressure precludes socially responsible action, the business should recognize that its operation in depleting social capital represents a loss. It should attempt to restore profitable operation through either better management (if the problem is internal) or corrective legislation (if society is suffering as a result of the way that the rules of competition have been made).

Since social issues are numerous and complex, each business must select its own approach for meeting its social responsibility. Today, as philanthropic activities become more and more of a key success factor, companies are assuming more positive roles regarding social issues. Businesses must therefore be socially responsible while preparing their mission statement.

Strategy and Business Ethics

Ethics is defined as "the discipline dealing with what is good and bad, and right and wrong, or with moral duty and obligation." Business ethics encompasses the morality of issues in business. The purpose of business ethics is not to teach the difference between right and wrong, but to give people the tools for dealing with moral complexity. Moral values are instilled into every human being at an early age through formal and informal socialization. Although strategic managers adhere to such moral principles in their private lives, some fail to apply them in their professional lives.

Business ethics is important and worthy of serious attention. The behavior of strategic leaders and their awareness of the behavior of employees at all level throughout the organization influence this aspect of corporate culture. These strategic leaders determine the business ethics practiced in an organization.

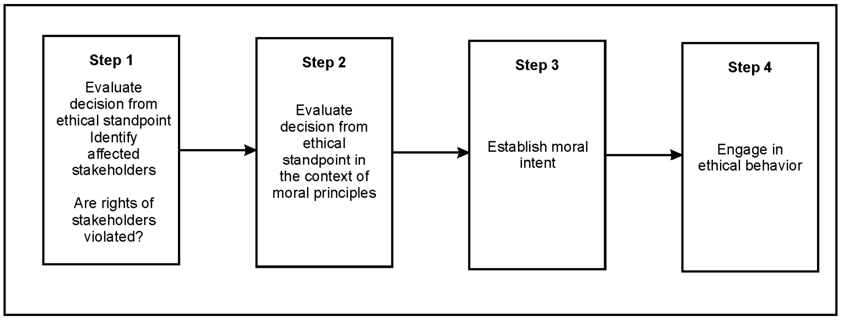
Sometimes, individual managers or employees adopt certain practices that senior managers regard as unethical. These need to be identified and stopped. If they remain unchecked, they are likely to continue, with the argument that "everyone does it." Issues such as insider dealing, salary increments for chief executives, etc., often come to the notice of the public through the media. Such issues affect people's perceptions of businesses in general and at the level of the individual firm. The response of different members of the public varies markedly in the sense that some people feel disgruntled and do nothing while others take more strong action through protests and boycotts.

Potential ethical issues must be considered when making strategic decisions. Objectives and strategies should be realistic and achievable rather than over-ambitious and impossible. If the objectives are over-ambitious, the employees may behave unethically.

Ethical Decision-making

There is no worldwide standard of conduct for business people. Cultural norms and values vary from country to country, and ethnic groups within a country. For example, what is considered to be a bribe in one country may be considered a normal business practice in some another country. What is legal/illegal has to be clear and definite? Differences in values also lead to differing notions of ethical behavior between business people and key stakeholders. For example, managers believe that profit maximization is the key goal of the firm, whereas concerned interest groups may have other priorities. This difference in values can make it difficult for one group of people to understand another group's actions. For example, socially progressive people may contend that business people working in tobacco, alcoholic beverages and gambling industries are acting unethically by making and advertising products with potentially dangerous side-effects such as cancer, addiction, etc. People working in these industries could respond by asking if it is ethical for people who do not smoke, drink or gamble, to reject another person's right to do so. These are also ultimately decided by the state, and the corporate entities have to conform to the legal decisions. An ethical decision-making process is shown in Figure 5.

Figure 5: A Model of Ethical Decision-making



Source: Charles WL Hill and Gareth R Jones, Strategic Management – An Integrated Approach, Text and Case, 4th Ed, 2002, P. 62.

In step 1, the managers must *identify* the stakeholders who will be affected by the decision and in what ways. The managers need to determine whether the proposed decision would violate the fundamental entitlements of any stakeholders. For example, the right to information about health risks in the workplace is a fundamental right of employees. Step 2 involves *judging* the ethics of the proposed strategic decision. The judgment should be guided by the principles articulated in the mission statement and the moral principles that the company has adopted as a member of society. In Step 3, the company has to *establish moral intent,* i.e., the company must resolve to place moral concerns ahead of other concerns in cases in which either the rights of stakeholders or key moral principles have been violated. At this stage, inputs from the top management are valuable. Without the pro-active encouragement of top managers, middle level managers might tend to place the narrow economic interests of the company before the interests of stakeholders. Step 4 requires the company to *engage in ethical behavior.* Developing a code of ethics can help in doing this. Codes of ethics specify how an organization expects its employees to behave while on the job.

Thus, strategic leaders should be objective about how society views their company and its products, and, wherever possible, should avoid actions that can damage its image. If an action that is viewed as unethical by certain stakeholders is unavoidable (such as the closure of a plant), it is important to use public relations to explain fully why the decision was taken. Thus, the need for a good corporate image should not be underestimated.

SUMMARY

- The process of strategy formulation begins with the firm's vision. Vision describes the broad thinking that goes into determining the future of the organization. The company mission is a set of intentions the company hopes to realize in the future. Vision is vague, personal and unwritten, whereas, the mission is clearly expressed. While formulating a mission, managers need to take into consideration various factors such as the basic product, primary market, principal technology, company goals, company philosophy, public image, and the company's self-concept. The company's mission, though more specific than the vision, gives few concrete directions for action. The mission statement also reflects social responsibility. It should address the different concerns of various stakeholders such as shareholders, customers, employees, society, and the local community. Ethical norms held important in the society and in business institutions also influence the company mission to a large extent.
- A company's mission plays a crucial role in its long-term and short-term success. Moreover, the mission statement ensures uniformity of purpose. Therefore, due attention should be paid to the process of laying out the company's mission. Company goals express its mission in specific terms. The company philosophy is an important part of the company mission. The mission should also take into consideration the public image of the company.

Chapter IV

Analysis of Business Environment

After reading this chapter, you will be conversant with:

- Remote Environment
- Planning Environment
- Social Environment
- Political Environment
- Economic Environment
- Legal Environment
- Operating Environment
- Environmental Scanning
- Five Forces Model
- Structural Analysis and Competitive Strategy
- Structural Analysis and Industry Definition
- Designing Opportunistic Strategics
- Formulation of Strategy

Introduction

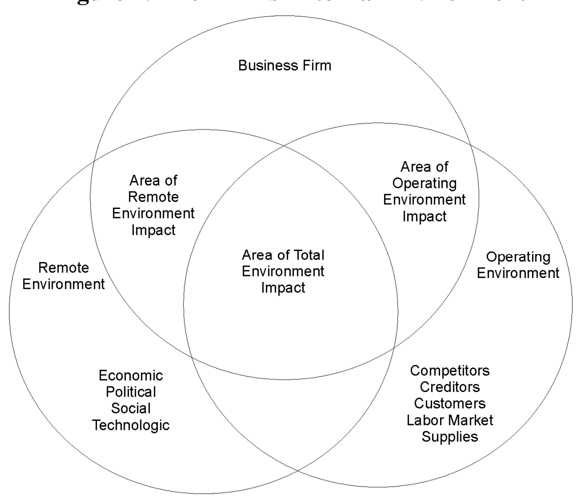
The main purpose of any business firm is to earn profits, which obviously come from the products they produce and services they render to the customers. The products once manufactured have to be dispatched out to the external environment, that is, the market. The external environment consists of many factors that govern the product's sale. These factors are uncontrollable by nature. Some of the factors such as competition and political, economical, legal, government rules and regulations, etc., influence the firm's choice of direction and action and also affect the internal environment of the organization. We can broadly categorize this environment into two types: remote environment and operating environment.

REMOTE ENVIRONMENT

The remote environment consists of a set of forces that originate beyond a firm's operating situation. These comprise political, economic, social, technological and industrial forces which create opportunities, threats and constraints to the firm. For example, if there is a recession in the construction industry then every individual contractor will face a decline in his business due to the decrease of construction activity in the entire industry. On the other hand, when there was a trade agreement between the United States and China in the 1970s, it provided an opportunity for US electronics manufacturers to widen their scope of operation.

An organization's external environment is shown in Figure 1. The figure depicts the firm's business area, remote environment and the operating environment cutting into an area of total external environmental impact on the firm. Let us examine each component in detail to have a holistic view of external environmental forces.

Figure 1: The Firm's External Environment



Source: John A Pearce II and Richard B Robinson Jr., Strategic Management – Formulation, Implementation and Control, (Delhi: AITBS, 3rd Edition) 100.

PLANNING ENVIRONMENT

In the present competitive scenario, environmental stability is not guaranteed. Changes in the environment are rapidly taking place in the environment due to various usually uncontrollable factors. The external environment consists of two parts viz., remote environment, and operating environment. Factors such as social, political, economic and technical come under remote environment, whereas customers, creditors, suppliers, labor markets and competitors comprise the operating environment. Apart from these, there are five competitive forces (threat from entrants, potential competition, bargaining power of buyers, and bargaining power of suppliers and threat from substitute products) that must be considered as part of the planning environment. Every firm should ponder these factors and formulate its strategies through effective planning. Since, customers choice varies from time to time based on individual requirements, the company must be in a position to meet their interests. At the same time, the company has to face many constraints imposed by the government and other legal bodies. Effective environmental planning is therefore a difficult task for firms. Efficient strategies designed must be designed in such a way that they are understandable, suitable, flexible, etc. So, a company can be successful if it routinely monitors the environment and modifies or develops new strategies as and when they are required.

SOCIAL ENVIRONMENT

The social environment is an important factor as changes in the values, beliefs, attitudes, opinions and lifestyles in society create potential opportunities for an organization. For a company to grow, it is necessary to take advantage of societal changes. The cultural, demographic, religious, educational and ethnic conditioning of individuals in society affects the social environment.

Since the middle of the twentieth century, a large number of women have started working outside their homes. Women in the workforce have decisively affected the hiring and compensation policies and resource capabilities of firms that employ them. They have also created a demand for a wide range of products and services necessitated by their absence from home. A whole range of products and services such as convenience foods, microwave ovens and day-care centers, have entered the market on account of this social development.

Demographic change (change in population) has implications for several businesses, for example, producers of goods targeted at the youth. Such businesses will have to make a shift in their long-range marketing strategies. Many producers of hair and skin care products have changed their products to fit the changed customer base. P&G has diversified its products in order to make its products appeal to the older generation as well as the youth. Thus, changes in the composition of the population and in the attitudes exhibited by consumers lead to changes in the products themselves.

POLITICAL ENVIRONMENT

Political forces influence the legislations and government rules and regulations under which the firm operates. Every company faces political constraints in the form of antitrust laws, fair trade decisions, tax programs, minimum usage legislation, pollution and pricing policies, administrative activities and many other actions, aimed at protecting the consumers and the local environment. These laws, rules and regulations affect a company's profits. However, there are other political actions such as patent laws, government subsidies and product research grants that support business activities. Thus, political forces influence the organization both positively and negatively. Political activity also influences three additional functions, viz., the supplier function, the customer function and the competitor function.

The supplier function is influenced by political activity when any private business is dependent on government-owned resources and national stockpiles of agricultural products. This dependence undoubtedly affects the firm's strategies.

As regards the customer function, government demand for products and services can create, sustain, enhance or eliminate many market opportunities. For example, the development of synthetic fuel during the Carter administration created a demand for new skills, technologies and products in the US. Likewise, the development of some advanced laser technologies was the outcome of the star wars defense program.

Similarly, when the government takes precautions to protect consumers and local industries, its decisions greatly affect businesses. So, the government's actions are of great concern to every firm. Firms analyze the government's strategies and develop complementary plans that can help them in exploiting the opportunities.

ECONOMIC ENVIRONMENT

Economic factors clearly indicate the nature and direction of the economy in which a firm operates. Every market is unique and consumption patterns change along with the wealth of the consumers in various market segments. For strategic planning all the economic trends at national and international levels have to be considered. Prime interest rates, inflation rates and trends in the growth of the Gross National Product (GNP), general availability of credit, the level of disposable income and the propensity of people to spend are the economic trends that have to be analyzed.

The potential economic impact of international forces appeared to be severely restricted and was largely discounted until recently. The focus of economic environmental forecasting was changed by the new international power brokers. The European Economic Community (EEC), the Organization of Petroleum Exporting Countries (OPEC) and coalitions of Lesser-Developed Countries (LDC) are three well known examples of influential international power brokers.

In 1957, the Treaty of Rome led to the establishment of EEC or the European common market, with Western European countries as it members. The elimination of quotas and industrial products was their objectives. So, to compete more effectively in international markets, the member countries were helped by the Intra-European cooperation.

Countries such as the United States, Canada, Japan, the EEC and other countries negotiated on multilateral trade activities in the year 1979, regarding the establishment of rules for international trade. Almost every aspect of business activity in the United States was affected by these negotiations.

The OPEC is constituted of countries that export enormous amounts of oil to other countries. It is one of the most powerful international economic forces in existence today. When the major world suppliers of oil and gas, who are a part of OPEC, drastically increased prices in the early 1970s, the economies of the US and other countries of the world went into recession. The automobile industry of US was affected by the rules imposed by the government to redesign engine sizes and performance standards. It was also affected by increased user costs because people were willing to spend more for a well featured, advanced, technological automobile.

Third World and Fourth World countries recently got a chance to be involved in international commerce due to the threats and opportunities they faced because of globalization or liberalization.

The less developed countries got motivated by the success of OPEC and found that it would be economically beneficial to form organizations to face the established powers, i.e., the multinational enterprises which established their stay in those countries. Since 1974, the producers of primary commodities in the less developed countries strengthened their trade organizations by fixing high prices on their products and achieving larger real income or profits. On the other hand, huge new markets were offered by the developing countries to US firms in foodstuffs and capital machinery. The business community's economic well being can be affected by each of these international forces, either for better or for worse. So, companies should perpetually monitor the market and examine the changes that are taking place and formulate a suitable strategy. A strategy based on the international arena is a critical part of the management process.

LEGAL ENVIRONMENT

Legal factors also have to be considered by the firms before stepping into another country. In recent years, the move toward deregulation, which involves the elimination of many legal restrictions, is a significant trend. Due to this, entry barriers are minimized leading to enormous competition among the firms in an industry. In 1979, the airline industry faced problems due to deregulation. There were fare-wars that lasted for many years. Many companies entered the airline industry and created intense competition by providing low fares. This ultimately resulted in turmoil in the last decade. Presently, the United States telecommunications is on the verge of experiencing turmoil, following deregulation in 1996.

Another legal problem pertains to the depletion of the ozone layer, acid rain and global warming. These problems are caused due to air pollution by chloroflouro carbons and other pollutants that are out in the atmosphere become hazardous to the environment. As a result governments will implement environmental regulations to minimize this pollution.

In a similar manner, many laws can be imposed by the government. So, every firm should adjust itself to the environmental policies of the concerned country where its operations are located.

OPERATING ENVIRONMENT

The operating environment includes factors in the immediate competitive situation regarding the procurement of resources, profitability for the company from their products and services, etc. The operating environment consists of factors like competitive position, customer profile, reputation among suppliers and creditors, and an accessible labor market. This environment is also called as the competitive or task environment.

Competitive Position

By assessing its competitor's position in the market, a firm can improve or formulate strategies to optimize its environmental opportunities. The firm must develop competitor profiles to forecast their short-term as well as their long-term growth and profit potential. During the construction of the competitor's profile, the factors that are to be considered are:

i. Market share

ii. Breadth of product line

iii. Effectiveness of sales distribution

iv. Proprietary and key account advantages

v. Price competitiveness

vi. Advertising and promotion effectiveness

vii. Location and age of facility

viii. Capacity and productivity

ix. Experience

x. Raw material costs

xi. Financial position

xii. Relative product quality

xiii. R&D advantages/position

xiv. Caliber of personnel

xv. General image.

These factors are weighed and suitable rating is given to them in accordance with the competitor that is to be evaluated. The weighed values and the rankings are multiplied by each other and the resulting weighed scores are added to yield a numerical profile of the competing business.

The rating scale suggested is as follows:

- Very strong competitive position (5 points)
- Strong competitive position (4 points)
- Average competitive position (3 points)
- Weak competitive position (2 points)
- Very weak competitive position (1 point).

Customer Profile

In the present competitive world customers are considered to be kings, because they are the ones who generate profits for the manufacturer. So, it is essential for managers to understand their customers properly and make them loyal towards the firm. In order to achieve this loyalty, the managers should constantly monitor their customer's psychology and cater to their requirements whenever necessary by developing a suitable customer profile and making it a part of the strategy. While developing a customer profile, managers should properly plan for the strategic operations, expect changes in the size of markets, forecast demand fluctuations, and appropriate allocation of the resources. The construction of the customer profile includes information pertaining to geographic, demographic, psychographic and buyer behavior.

It is important to define the geographic area from which customers do or could come. Almost every product or service posses some quality to attract the buyer, which comes from some specific or significant location. For example, take the case of Sony, its origin is from Japan; IBM from US; Hyundai from Korea and SAP from Germany.

Demographic variables are used to differentiate the customers. These variables include age, sex, marital status, income and occupation. This information can be easily collected, quantified and can be used for strategic forecasting.

The purchasing power of the customers can be better determined by their personality and lifestyles than demographic and geographic variables. A psychographic study is considered to be an important component of the total profile.

Buyer behavior gives an idea of the customer's purchasing behavioral patterns with regard to a product or service. Variables such as usage rates, benefits and brand loyalty constitute the buyer's behavior and significantly assist in designing a more accurate and profitable target-strategy. So, information pertaining to all these factors is essential for developing an effective Customer profile.

Suppliers and Creditors

A business firm should maintain dependable relationships with its suppliers and creditors for its long-term survival. A firm relies on its suppliers for financial support, services, materials and equipment. In addition, it may request its suppliers and creditors for quick delivery, liberal credit terms, or broken lot orders. So, it is imperative for a firm to develop good relations with suppliers and creditors. In addition to strong ties with suppliers and creditors, several other related factors should also be considered. With regard to its competitive position with suppliers, a firm should address the following questions:

i. Are suppliers price competitive? Do suppliers offer attractive quantity discounts? How costly are their shipping charges?

ii. Are vendors competitive in terms of production standards and in terms of deficiency rates?

iii. Are supplier's abilities, reputation and products and services competitive?

iv. Are suppliers reciprocally dependent on the firm?

With regard to its position with its creditors, the following questions are to be considered.

i. Is the stock fairly valued and willingly accepted as collateral?

ii. Do potential creditors perceive the firm as having an acceptable record of past payment? A strong working capital position? Little or no leverage?

iii. Are creditors' current loan terms compatible with the firm's profitability objectives?

iv. Are creditors able to extend the necessary line of credit?

Based on these questions, competitive strategies can be formulated and efficiently implemented.

Personnel: Nature of Labor Market

A firm must possess the ability to retain its capable employees in order to achieve success. A suitable strategy must be formulated to make experienced and knowledgeable employees dedicate themselves to the organization. This strategy can involve incentives, promotions, training, transfers as per employees' requests etc. The personnel department must take care in recruiting people that meet industry specifications. However, personnel recruitment and selection alternatives are influenced by the nature of business in the operating environment. When recruiting employees, three factors that have to be considered: reputation as an employer, local employment rates, and ready availability of personnel with the necessary knowledge and skills.

A firm should possess a good reputation in the minds of employees and the community. It should provide a competitive compensation package, be concerned with the employee's welfare, and also provide superior quality products and services (better than its rival firms). This helps the firm retain its valuable employees.

The availability of skilled and experienced employees varies considerably. Moreover, it is difficult for a firm to attract skilled people to a plant that is situated in an economically depressed area.

Some people possess very high qualifications, thus making it necessary for a firm to pay a high compensation package and also create a suitable post for them in the organization. If rival firms are unable to meet the requirements of these professionals (technical experts, industry executives, oil drillers, etc.), then it gives a business firm leverage over its rival firms for attracting qualified professionals.

ENVIRONMENTAL SCANNING

During the past two decades, companies and researchers have sought to determine how the environmental scanning task should be accomplished. In the mid-1960s, Francis J Aguilar conducted a research study which revealed that the commonest sources of data about the external environment were personal experiences, journals, reports, books, professional meetings, industrial conferences, colleagues, board members, friends and employees.

In the mid-1970s, formal environmental appraisal units or positions were established by some companies. Out of these companies, General Electric Co., is considered to have pioneered a business environmental studies staff in May 1967. Such units were also created by Coca-Cola, Gillette, Wayer Haeuser, Whirlpool and AT&T. These units utilized names such as futures research, commercial research, social forecasting and environmental scanning. Monsanto Company even appointed a director of future research. Issue managers were employed by other companies who were responsible for considering the immediate future and the next one to five years, and charged with not only identifying issues but also setting forth specifically how the firm might deal with them.

In the early 1970s, the failure of conventional corporate planning departments to foresee such developments as the sudden eruption of the energy crisis, food and material shortages, the rise of environmental groups, and the imposition of price controls was believed to be the impetus for the creation of the formal environmental appraisal function.

A study in some organizations found that what the environmental appraisal function was not linked to strategic plans and decisions. This situation was due to:

i. Improper attitudes of managers toward the process.

ii. Short-term orientation of managers.

iii. Complexity of the entire process.

iv. Inability to gather information and use it.

v. Lack of confidence in the information and/or the people who developed it.

By the mid-1980s, a number of different approaches to environmental appraisal were being utilized. Some companies possessed in-house units (which involved direct reporting to the top management) as parts of planning departments. To undertake scanning tasks some firms joined together. For the publication of a quarterly trend analysis report more than 200 insurance firms had co-operated. Continuous monitoring of the report is essential to expose changes in society that seem to be relevant to the insurance industry. Still other information is supposed to rely on specialized consultants.

A major study of 10 large companies, specifically identified as "leading edge" firms in the environmental analysis field, reported that the function is harder and complex to perform in the competitive world. The experiences of these companies led to the identification of four basic principles regarding the effective implementation of the environmental analysis function.

i. Environmental analysis must be linked, conceptually and practically, to current planning and operations.

ii. Environmental analysis serves a number of separate purposes, and different analytic structures and systems may be required in order to achieve those different purposes.

iii. Systems for environmental analysis must fit the culture and decision-making styles of the organizations and areas they serve.

iv. Continuing support from internal changes is required to sustain environmental analysis in an organization over time.

FIVE FORCES MODEL

The effective formulation of strategy needs a clear understanding of competition. Competition in an industry is determined not only by existing competitors but also by other market forces such as customers, suppliers, potential entrants, and the existence of substitute products. Understanding the level of competition is important because the level of profits depends to a large extent upon the level of competition. The strategist's goal then is to position the firm in such a way that it is not vulnerable to the attacks of competitors. The position should give the firm enough space to defend itself confidently. Given this, the need to study the underlying sources of competitive pressure is obvious. Understanding the sources of competition can help the firm to gauge its own strengths and weaknesses, and to perceive the trends in the industry so that it can position itself optimally for the best returns. Michael E Porter of the Harvard Business School has developed a framework known as the "Five Forces Model" to help managers to analyze the business environment. According to Porter, the five forces, namely, the threat of new entrants, the bargaining power of buyers, the bargaining power of suppliers, the rivalry among existing players, and the threat of substitute products, play a vital role in shaping the company's future.

Threat of New Entrants

New entrants to an industry bring in new capacity, and capture market share from the existing players. The result is more players and more competition. This situation can lead to price wars, which can result in falling returns. This decline in profitability becomes a problem for the new entrants too. That is why new entrants to an industry often take the 'acquisitions' route. The willingness and ability of firms to enter a particular industry depends on the barriers to entry. There are six such barriers: economies of scale, product differentiation, capital requirements, cost disadvantages independent of size, access to distribution channels, and government policy. These influence the decision to enter a new industry.

ECONOMIES OF SCALE

Firms realize economies of scale as the output of manufacturing units increases. They manufacture goods at a lower average cost compared to other manufacturers with lower levels of output. These economies of scale act as a barrier against firms which consider entering an industry with a smaller manufacturing capacity. Economies of scale realized in several functions can act as barriers. For example, Xerox and GE were unable to enter the mainframe computer industry mainly due to their lack of scale economies in production, marketing, research and service. Similarly, economies of scale create barriers in distribution, utilization of the sales force, and financing for the business.

PRODUCT DIFFERENTIATION

Firms differentiate their products by establishing brand identification and customer loyalty. Brand identification and customer loyalty can be built through advertising, customer service, product differences, or first mover advantage. Product differentiation thus forces the new entrant to spend huge amounts to overcome this cost disadvantage. In soft drinks, over-the-counter drugs, cosmetics, investment banking, and public accounting, differentiation is the most important barrier protecting existing firms. Brewing companies employ differentiation along with economies of scale, distribution, production, and marketing to create barriers which are almost impenetrable.

CAPITAL REQUIREMENTS

A firm needs capital not only for advertising and R&D, and but also for customer credit, inventories, and to absorb start-up losses. Huge capital requirements limit the number of players in industries such as computer manufacturing and mineral extraction. For example, Xerox created a major capital barrier to entry in copiers when it chose to rent out copiers rather than selling them outright. This business strategy greatly increased the need for working capital for all the players in the copier market.

COST DISADVANTAGES INDEPENDENT OF SIZE

Existing firms in an industry sometimes enjoy advantages that are not available to new entrants. These advantages spring from the effects of the learning curve and the experience curve. Similarly, proprietary technology, access to the best sources of raw materials, assets purchased at lower prices, government subsidies and favorable locations can give competitive advantages to existing firms in an industry.

ACCESS TO DISTRIBUTION CHANNELS

The product of a new entrant must replace the products of existing firms and occupy shelf space. New entrant tries to ensure this replacement through price breaks, promotions, intense salesmanship or other means. However, if there is a limited number of a distribution channel, it will be more difficult for the new entrant to gain selling space. This is because the existing players may have already entered into exclusive agreements to promote their products. To overcome this problem, the new entrant may be forced to create its own distribution channels. Timex, for example, had to create its own distribution channels to sell its watches in the marketplace.

GOVERNMENT POLICY

The government can use its discretion to influence the competition in an industry by imposing controls, mandating license requirements, and limiting access to raw materials. Trucking, railroads, liquor retailing and freight are regulated industries. Barriers to entry are also created when the government imposes regulations pertaining to air and water pollution standards, product safety and efficacy. For example, pollution control requirements can increase the capital needed for the installation of sophisticated equipment. Standards for product testing, common in industries like food and health related products, can lead to substantial lead times and raise the capital cost of entry.

Intensity of Rivalry among Existing Competitors

Rivalry in an industry occurs when one or more firms make an effort to increase their market share. This can lead to price wars, advertising battles, launches of new products and increased customer services and warranties. Some firms gain the upper hand through intense rivalry, while their competitors suffer a fall in market share. The intensity of rivalry depends upon many factors. Rivalry is usually intense when there are many competitors of similar size. Slowdowns in industrial growth also make firms keen to grab each other's market share. A lack of differentiation among the products of the players in the industry also leads to intense competition. The absence of switching costs can also lead to an unstable marketplace. In the paper and aluminum industries, manufacturers often resort to underpricing to avoid spoilage of the goods. It is difficult for firms to move out of certain industries, because of their fixed investments. In the vinyl and chlorine industries, which are characterized by large increments in capacity, the firms often cut prices disrupting the supply-demand balance to avoid excess capacity problems. Thus, a variety of factors, ranging from exit barriers to the loyalty of old players to the industry despite low returns, increase the intensity of competition in an industry.

The Bargaining Power of Buyers

Customers are the ones who buy products from the firm. But they are not always the final users of the product. For example, for Unilever, the direct buyers of its detergents are wholesalers and retailers. Bulk buyers such as supermarkets often have greater bargaining power, i.e., they can ask for lower prices from the supplier company, than single customers or small retailers. If buyers are in a weaker bargaining position than the supplier, the supplying company can hike prices and make high profits on that basis. Thus, the bargaining power of buyers is one of the factors in industry-level strategic analysis. Porter says that buyers are powerful under the following circumstances:

- When the suppliers are many and the buyers are a few and large.
- When the buyers purchase in large quantities.
- When the supplier's industry depends on the buyers for a large percentage of its total orders.
- When the buyers can switch orders between supply companies at a low cost thereby playing companies off against each other to force down prices.
- When it is economically feasible for the buyers to purchase the input from several companies at a time.
- When the buyers can use the threat to provide for their own needs through vertical integration as a device for forcing down prices.

For example, the buyers of auto components are powerful. In the US, the buyers are General Motors, Ford and Chrysler. There are numerous suppliers of auto components. So, to keep the buyers loyal to them, auto components suppliers must provide quality products to their buyers.

The Bargaining Power of Suppliers

The bargaining power of suppliers determines the company's profitability when the suppliers are able to force the price that the buyer must pay for the product. Suppliers are powerful under the following circumstances:

- When the product that they sell has few substitutes and is important to the purchasing company or buyer.
- When no single industry is a major customer for the suppliers.
- When products in the industry are differentiated to such an extent that they are not easily substitutable and it is costly for a buyer to switch from one supplier to another.

- To raise prices, the supplier can use the threat of vertically integrating forward into the industry and competing directly with the buying company.
- The buying companies cannot use the threat of vetically integrating backward and supplying their own needs as a means to reduce input prices.

An example of a powerful supplier is Intel, the world's largest manufacturer of microprocessors. Manufacturers of personal computers are dependent on this single powerful supplier of computer chips. Most standard personal computers run on Intel's microprocessors. So, PC manufacturers have little choice but to use an Intel microprocessor as the brains for their machines. As a result, Intel has become the most powerful supplier in the industry.

The Threat of Substitute Products

Substitute products can match the needs of the customer in the same way as the original product. Coffee, tea and soft drinks, all serve the consumer's need for refreshment. Due to the existence of substitutes such as tea and soft drinks, the prices charged by companies in the coffee industry are restricted. If coffee prices are hiked, customers have the option of switching over to tea or soft drinks, which are its substitutes.

A close substitute is a potential threat to the company's product. The existence of a substitute limits the price which can be charged for a product and therefore the profitability of the company.

STRUCTURAL ANALYSIS AND COMPETITIVE STRATEGY

Once the forces affecting competition in an industry and their underlying causes are diagnosed, the firm is in a position to analyze its strengths and weaknesses. The crucial strengths and weaknesses are a firm's posture vis-à-vis the underlying causes of each competitive force. Where does the firm stand against substitutes, against the causes of entry barriers and in coping with rivalry from established competitors?

In order to create a defendable position against the five competitive forces, an effective competitive strategy takes offensive or defensive action. Broadly, this involves a number of possible approaches.

- Positioning the firm so that its capabilities provide the best defense against the existing array of competitive forces.
- Influencing the balance of forces through strategic moves, thereby improving the firm's relative position.
- Anticipating shifts in the factors underlying the forces and responding to them, thereby exploiting change by choosing a strategy appropriate to the next competitive balance before rivals recognize it.

Positioning

In the first approach, the structure of industry is taken into consideration and is matched with the company's strengths and weaknesses. To defend, a competitive forces strategy is developed. Based on knowledge of the company, it is analyzed whether the company is in a position to face the competition, especially in the areas where the competitive forces are weak. If the competitive forces are too strong in particular areas, then it will be better for a firm to avoid that marketplace. So, accordingly the firms should position themselves in the market.

Influencing the Balance

A strategy that takes the offensive can be devised by the company. Innovation in marketing can raise brand identification or the differentiation of products can be achieved. In order to overcome the entry barriers, capital investments in large-scale facilities or vertical integration are essential. The balance of forces is partly a result of external factors and partly within a company's control. To identify the key factors driving competition in the particular industry, structural analysis is used.

Exploiting Change

Industrial evolution is important strategically, because evolution, of course, brings changes in the structural sources of competition. The pattern of industry development, in the familiar product life cycle, for example, growth rate is said to decline as the business becomes more mature and the companies tend to integrate vertically. The critical part that is to be considered is whether the structural sources of competition are affected by the above mentioned factors. Consider vertical integration broadly and these may be strong benefits to compete in groups of related industries. The firm wants to go for eliminating needless confusion in drawing industry boundaries by decoupling industry definition and that of the businesses.

STRUCTURAL ANALYSIS AND INDUSTRY DEFINITION

In competitive strategy formulation, a great deal of attention has been directed at the need for defining the relevant industry. When defining a business beyond national boundaries to potential international competition and beyond the ranks of one's competitors today to those that may become competitors tomorrow, numerous writers have stressed the need to look beyond product to function. The proper definition of a company's industry has become an endlessly debated subject. The fear of overlooking latent sources of competition that may some day threaten the industry is an important motive in this debate. The need for debates on where to draw industry boundaries should be reduced by structural analysis by focusing broadly on competition well beyond the existing rivals. Any definition of an industry is a choice of where to draw the line between established competitors and substitute products, between existing firms and suppliers and buyers. The matter of degree has little to do with the choice of strategy.

The industry's definition is not the same as the definition of where the firm wants to compete. Just because the industry is broadly defined, it does not mean that the firm can or should compete in the extensive vertical integration that is taking place in the maturing mini computer industry, both in manufacturing and in software development. The greatly increasing economies of scale as well as the amount of capital necessary to compete in the industry, is a significant trend. By this, the barriers to entry are raised and may drive some smaller competitors out of the industry once growth levels off. The most important sources of competition in the industry are affected by those trends which hold the highest priority from a strategic stand point. The final profitability can also be predicted with the help of structural analysis.

Diversification Strategy

For determining the diversification strategy, the framework for analyzing industry competition can be used. It provides a guide for answering the extremely difficult question inherent in diversification decisions: What is the potential of this business? The framework may allow a company to spot an industry with a good future before this good structure is reflected in the prices of acquisition candidates. The valuable types of relatedness in diversification can be identified with the help of this framework.

Potential Competitors

Potential competitors are the companies that are not currently competing in the industry but are creating a tremendous competition for other companies through their capabilities. American Telephone and Telegraph, for example, was considered a potential competitor in the personal computer industry in the early 1980s for it had the technology, sales force and capital necessary to manufacture and sell PCs. In 1985, AT&T entered the industry but failed to secure a strong market position. Potential competitors usually get discouraged by the incumbent companies from entering the industry because the entry of more companies will create problems for the established companies (in holding their share in the market and in generating profits). So, entry of potential competitors is a threat to the established company's profitability. On the other hand, if the new entry is low then it can be advantageous for the incumbent companies to raise prices and earn greater returns.

The strength of the competitive force of a potential rival depends upon the height of barriers to entry. If the barriers to entry are more, then it becomes very expensive for a company to enter an industry, and vice versa. High barriers of entry keep the potential competitors out of the industry. The main sources of barriers of entry are brand loyalty, absolute cost advantages, economies of scale and government regulations.

Rivalry among Established Companies

The rivalry among the established companies is the second of Porter's competitive forces. If the rivalry is weak, then the companies raise the prices and can earn great profits, and if it is strong, then there will be a price war or price competition. Thus, a strong threat takes the form of intense rivalry among the established companies within an industry. The extent of rivalry among the established companies within an industry is the function of three factors.

i. Industry's competitive structure.

ii. Demand conditions.

iii. Height of exit barriers in the industry.

COMPETITIVE STRUCTURE

The number and size distribution of companies in an industry is referred to as the competitive structure. Structures differ from fragmented to consolidated and have varied implications for rivalry. A large number of small or medium sized companies are contained in a fragmented industry; so, none of them can dominate the industry. But large companies in small numbers constitute a consolidated industry, or in extreme cases, a monopoly. Agriculture, video rental and health clubs to real estate brokers and sun tanning parlors come under fragmented industries, whereas aerospace, automobiles and pharmaceuticals constitute consolidated industries.

Many fragmented industries possess low barriers of entry and have commodity products that are very hard to differentiate. Generally, the profits rise and fall depending on the situation. Low barriers of entry during strong demand and high profits will lead to more new entrants hoping for profitability. This situation is exemplified by the explosion in video stores, health clubs and sun tanning parlors during the 1980s. Excess capacity is created due to the flood of new entrants into a booming, fragmented industry. In order to utilize the spare capacity, a company cuts down its prices. While differentiating its products from the competitor's products, companies face the difficulty. This results in price competition which brings down the industry's profits and forces some companies out of business. For example, after a decade of expansion and booming profits, health clubs are now facing problems in maintaining their profit margins due to excessive competition. To maintain their membership in the industry, they are forced to offer large discounts to their customers. A fragmented industry constitutes a threat rather than an opportunity.

It is very difficult to predict the nature and intensity of rivalry in the consolidated industries. The companies are interdependent in consolidated industries; this means that competitive actions of one company directly affect the profitability of the others in the industry. The market share of the companies gets affected by the competitive action taken by any other company in the industry. This will lead to undercutting of prices and reduction in profit margins, thus, pushing the industry profits down in the process. For example, in the early 1990s, fare wars wracked the airline industry. When the demand for airline travel fell during 1990 (US economy was in a recession), airlines started decreasing their prices for maintaining their passenger loads. When one airline serving a particular route cut its prices, then others soon followed, resulting in severe decline in prices. Due to this, some companies like Pan American went bankrupt. So, high rivalry in consolidated industries will lead to price wars and constitute a threat to the companies. The strategy for the companies is to fix suitable prices that are competitive to others.

DEMAND CONDITIONS

The intensity of rivalry among the established companies is also based on the demand conditions. Growing demand from either new customers or additional purchases by existing customers tends to reduce rivalry among the companies because increased requirement for the products (by the customers) creates opportunities for companies to expand. Rivalry reduces due to growing demand because companies have a chance of selling more products without affecting profit margins and market share of other companies. A good example of this phenomenon is the open case which profiled demand cycles in the DRAM industry. The DRAM industry is quite fragmented, with no company accounting for more than 10 percent of the market. The product is sold primarily on price because it is difficult to be determined. Because of these two factors, there is a vigorous price competition and low industry profit.

Conversely, more rivalry is as a result of decline in demand. Companies fight to maintain revenues and market shares. When consumers start buying less, or leave the marketplace, then the demand decreases. So, for a company to grow under these conditions it should take away the market share of other companies.

EXIT BARRIERS

To keep the companies in an industry during low returns, exit barriers are used. These are economic, strategic and emotional factors. If exit barriers are high, companies can become locked into an unprofitable industry in which overall demand is static or declining. This can result in excess production capacity. Intensified price competition is due to excess capacity with companies cutting prices in an attempt to obtain the orders needed to utilize their idle capacity. Common exit barriers include the following:

i. Investments in plant and equipment that have no alternative uses and cannot be sold off. If the company wishes to leave the industry, it has to write off the book value of these assets.

ii. High fixed costs of exit, such as severance pay to workers who are being made redundant.

iii. Emotional attachment to an industry: a company is unwilling to exit from its original industry for sentimental reasons.

iv Economic dependence on the industry: when a company is not diversified and so relies on the industry for its income.

How Competitive Forces Shape Strategy?

The competitive forces which include threat to entry, potential competition rivalry, bargaining powers of buyers, bargaining powers of suppliers, and threat from substitute products play a vital role in affecting the industry's environment. These forces can create threats and opportunities for the firm. Based on the information gathered, the firm should identify its strengths and weaknesses and mould itself accordingly to exploit the opportunities created by these forces by formulating suitable strategies.

DESIGNING OPPORTUNISTIC STRATEGIES

The designing of business strategies involves a systematic approach which is multifaceted, complex and requires assessment in-depth. This process is multifaceted because it involves the interactive influences of both remote and operating environments. The strategic decision which is to be prepared must be systematic and comprehensive. The process is complex because the environmental forces are very difficult to be controlled, especially external factors. These can fluctuate at any time and hence become uncontrollable in nature. Finally, most of the strategies are developed by gathering relevant information on the environment and assessing it in-depth. Limited objectivity will not help the management accurately predict future events in the competitive external environments. Designing a strategy to optimize opportunities is a very complicated task. When developing the firm's plans, strategic managers should emphasize four major design recommendations based on the multifaceted, complex and subjective nature of corporate strategy formulation. These include issue selection, data collection, conducting environmental impact studies and planning for flexibility.

Issue Selection

The issues that are most likely to be critical to the success of the strategy have to be determined initially. This issue identification will help to focus and prioritize data collection efforts. In a recent study that involved more than 200 company executives, these respondents were asked to identify key planning issues in terms of their increasing importance to strategic success. The issues that were selected were competitive domestic trends, customer or end user preferences and technological trends. These three factors were considered to be most important for effective strategy formulation. By knowing the competitors trends the firm can modify its strategy. Since the customer preferences change repeatedly, they should be monitored by the management constantly to enable it to meet them. Technology also plays a major role in providing a product of superior quality to the customers in time. So, all these factors play a vital role in the formulation of an effective strategy.

Data Selection

It is imperative for managers to gather more information through forecasting to design appropriate strategies. The information can be gathered from government publications, discussing competitive conditions with sales managers and clients, reading business magazines, and serving on community councils and committees.

The data collected in this manner may not be valid and is often difficult to document and verify. Therefore, public sources would be beneficial for collecting systematic data which is pertinent in nature. Such data are readily available, inexpensive and comparatively reliable. The sources of public data include annual reports, business literature indexes, business periodicals and reference services, government publications, trade publications, stock broker reports and many others. All these sources will be useful for examining the general environmental trends. Managers must carefully select data from this information source when constructing a strategic data base. When selecting or generating data for managerial base, factors such as manageability, accessibility, variability, relevance, importance and cost must be considered.

Impact Studies

After the data is collected, managers should undertake impact studies to determine the overall consequences of implementing available alternative strategies. In the process, the environmental data gets transformed by the firm into situation specific environmental information. The impact study must involve the assessment of probable effects on the firm's strengths and weaknesses, operating environment, competitive position and likelihood of achieving corporate objectives, grand strategies and mission. Businesses attempt to develop objective estimates, whenever they find it possible, along with the impact studies (which are generally considered to be subjective and intuitive). In order to increase the objectivity of the data analysis, firms increasingly employ techniques like exponential smoothing, time trends and adaptive forecasting.

Flexibility

Incorporation of flexibility is the next important consideration when designing strategies. Since it is difficult to forecast environmental conditions (because they are uncertain), decision makers strive for the optimal level of flexibility to enhance their chances of profitability.

Several approaches can be suggested to increase such flexibility.

i. The strategy must be stated in general terms so that those implementing it will have some discretion in terms of their unique situations.

ii. The strategies must be treated as rules with exceptions so that an aspect of a strategy can be violated if such action can be justified.

iii. The options must be kept open.

While flexibility in a strategic plan will lessen the plan's benefits by increasing costs, shortening planning and action horizons, and increasing internal uncertainty, an overly rigid stance in support of a particular strategy can be devastating to a firm faced with unexpected environmental turbulence.

FORMULATION OF STRATEGY

The risks involved in a nation's market should be identified by the companies before entering the market. Risks can arise from shifting borders, unstable governments, foreign exchange problems, corruption and technological pirating. So based upon these factors the company should adjust itself to sustain in the competitive environment. Some companies opt to enter a number of countries, whereas some others enter fewer countries, but with deeper commitment. Ayal and Zif have suggested that a company should enter fewer markets when:

i. Market entry and market control costs are high,

ii. Product and communication adoption costs are high,

iii. Population and income size and growth are high in the initial countries chosen, and

iv. Dominant foreign firms can establish high barriers to entry.

Before entering the market, the firms expect to have high market attractiveness, high competitive advantage and low risk.

Entering to the Market

After selecting a country to enter, the company has to decide the best mode of entry. There are nine common modes of entry.

i. Indirect Exporting

ii. Direct Exporting

iii. Licensing

iv. Joint Ventures

v. Direct Investment

vi. Acquisitions

vii. Production Sharing

viii. Management Contracts

ix. Turnkey Operations.

INDIRECT EXPORTING

Exporting through independent intermediaries to various countries is indirect exporting. There are four types of intermediaries. They are:

Domestic exporter: Who exports the products of the manufacturer to various countries.

Domestic based exporting agent: The agent negotiates with domestic producers and foreign purchaser for exports. Coordination between the domestic producers and foreign purchasers are through such agents. Commission is charged for the services rendered.

Cooperative organization: Cooperative organization is the organization set up by a number of producers manufacturing similar products. On behalf of these producers, the cooperative organization gets involved in export dealings. This type of arrangement is used by the producers of agricultural products.

Export management company: This intermediary manages exports for a fee.

The costs involved in indirect exporting are low, leaving the producers free to concentrate on their manufacturing activities or some other internal activities. Marketing these products on their own would involve high operating expenses.

DIRECT EXPORTING

In the earlier stages, companies depended on indirect exporting, but slowly they started exporting by themselves to gain benefits and economies of scale. The investment and risk of direct exporting is greater than that of indirect exports. The methods of direct exports are as follows:

Domestic based export department or division: A domestic based export department or division is nothing but an export division within the marketing department of a company. This division will perform all the functions pertaining to exports.

Overseas sales branch or subsidiary: Overseas sales branch or subsidiary is the branch established in one or more foreign countries to perform the functions of export marketing. These branches perform customer service activities in addition to marketing functions.

Traveling export sales representatives: Traveling export sales representatives involve sending of sales personnel to various foreign countries to explore and execute business.

Foreign based distributors or agents: Foreign based distributors or agents are appointed by companies to deal with exports. These personnel belong to the relevant foreign country and are given exclusive rights to represent the company in their marketing programs.

Participation of companies in international exhibitions and trade fairs is essential to exhibit their products.

LICENSING

A license will be given by a licensor to the foreign company to use its production process, trademark, patent, trade secret or other item of value for a fee or royalty. The entry of a manufacturer in the foreign market will be of little risk. The advantages of production expertise or technology of a well known product without having to start from scratch is gained by the foreign company. By licensing bottlers around the globe, Coca-Cola enters different markets. It supplies them syrup and trains the personnel of the foreign companies to produce and sell their product. There are different forms of licensing, one of which is management contract. Under this, the company sells the management contract to the owners of a foreign hotel, airport, hospital or other organization to manage these businesses for a fee. Management expertise is provided by the firm.

The second one is contract manufacturing, where the product is manufactured by local manufacturers. The third form is franchising. A complete brand concept is offered by the franchiser to tile franchisee. Along with tile brand concept, the franchiser also offers an operating system. The fees are paid by the franchisee to the franchiser.

JOINT VENTURES

Foreign investors and local manufacturers join together to form joint ventures. Technological transfer, market sharing and investment sharing are involved in a joint venture. The ownership and control is shared by the foreign investor and local producer. The domestic manufacturer's participation in ownership and control is essential for some governments when permitting the entry of foreign firms into domestic market. The resources, skills and expertise are substituted by the two firms forming a joint venture. Some joint ventures are successful and run for many years. Some foreign investors, after gaining knowledge of marketing conditions, consumer behavior and the culture of the people, may divorce the local investor and start their independent companies. The reverse can also happen. The other problems of joint ventures include cultural variations of the two companies, variations in the policies of reinvestment of profits, competition between the two firms for critical managerial positions, and the like. A joint ownership may hamper specific manufacturing and marketing policies for a multinational company. This problem is usually faced while competing in the world market.

DIRECT INVESTMENT

This is the ultimate way of going international. The involvement of a company in ownership and control of foreign-based assembly or manufacturing or service facilities is included in direct investment. The foreign company can buy part of the local manufacturing facilities or can buy full interest in the local company, or can build its own facilities on its own. Customer needs can be met and exports to other countries can be efficient if the company starts producing in the foreign country. This strategy helps the company widen the market and get distinct advantages.

ACQUISITIONS

It is better for a foreign company to acquire an already established company in the host country rather than start from scratch. The established company can be purchased by the foreign company in its entirety rather than on a piece meal basis.

Synergistic benefits can be enjoyed by the foreign company if it acquires a firm with strong complementary product lines and an efficient distribution network. It becomes difficult for a foreign company to acquire local companies if information about the potential companies is not available. Restrictions imposed by the government on ownership and control are also a limiting factor for acquisition.

PRODUCTION SHARING

The higher labor skills and technology available in developed countries with the lower cost labor available in developing countries is combined by production sharing. This is the precise reason why many offshore development centers have sprung up in the software industry in India.

MANAGEMENT CONTRACTS

A large amount of management talent is available at large MNCs. Management contracts offer a means through which an MNC may use part profits and personnel to assist a firm in a host country for a specified fee and period of time. Until the local management is trained and developed, the MNC can continue its operations by earning some income from its investment. These arrangements help developing economies that have the capital but do not have the skilled manpower and managerial skills.

TURNKEY OPERATIONS

For the construction of operating facilities in exchange for a fee, turnkey operations come into the picture. After completion, the facilities are transferred to the host country. Normally, the government department or agency is the customer in many turnkey projects. The foreign company supplies some of its own equipment for the project. For example, L&T operates many turnkey projects in several countries for governments and large organizations.

SUMMARY

- In this chapter, we discussed the external environment in-depth. We considered all the major factors that affect the company's environment. For any firm to make an entry, it has to decide on many factors that become obstacles for these new firms to enter and compete. Even for the existing firms, strategy formulation must be efficient and flexible to face their competitors, new as well as old.
- The environment can be divided into the remote environment and the operating environment. The remote environment consists of political, social, economic factors, etc., whereas the operating environment consists of creditors, customers, suppliers, competitors, etc.
- Apart from these, the five competitive forces (threat to entry, rivalry in industry, bargaining power of suppliers, bargaining power of buyers, and threat from substitute products) make it difficult for firms to sustain themselves in the competitive market. So, for a company to establish itself in the competitive environment, it should be in a position to formulate effective strategies. In order to do this, a firm should undertake environmental scanning and monitor the environment constantly.

Chapter V

Analysis of Internal Environment

After reading this chapter, you will be conversant with:

- Value of Systematic Internal Assessment
- Strategy and Internal Analysis
- Analyzing Departments and Functions
- Analyzing Management
- The Human Side of Enterprise
- Quantitative Approach for Evaluating Internal Factors

Introduction

Strategic success depends on a realistic analysis of the firm's internal capabilities. The internal analysis of an organization is basic to the study of business policy and strategy. For a strategy to succeed, it should have realistic assessment of the firm's internal resources and capabilities. An internal analysis provides the means to identify the strengths to build on and the weaknesses to overcome when formulating strategies. An analysis of internal resources will reveal what the organization is capable of doing in view of the resources profile.

Internal analysis needs facts, opinions, statements and observations to be assembled and analyzed by the analyst. From such an analysis, a profile of the resources, strengths and weaknesses can be prepared. Judgments are then made, based on the profile, about the organization, its subunits, its people, and the way it has been managed. In this chapter, we will examine how a firm assesses its internal strengths and weaknesses and aspects to be considered. We begin the chapter by discussing the value of systematic internal assessment.

VALUE OF SYSTEMATIC INTERNAL ASSESSMENT

The process of internal analysis in most firms is not systematic, but it remains a critical ingredient in strategy development. Based on the match between the strengths and the projected market opportunities, a firm ultimately charts its strategic course. The internal analysis of a firm reveals what it is doing, what it wishes to do and what it might do. An internal analysis that leads to a realistic company profile involves:

- Trade-offs,
- Value judgments, and
- Informed and educated guesses.

A value chain is a linked set of value – creating activities that begins with the purchase of basic raw materials from suppliers, and ends with distribution of a product or service. A value chain analysis evaluates the organization in the context of its value-creating activities.

Defining the Value Chain

A clear understanding of the value chain helps the firm identify its competitive advantage. As a part of the defining process, individual value activities in the firm are identified. A value chain segregates a firm into strategically relevant activities to understand the cost behavior of each activity. By performing these activities economically and efficiently, a firm can gain competitive advantage. For example, identifying low cost suppliers and gaining access to their value chain can improve the performance of the firm in the short-term as well as in long-term.

Expanding or narrowing the extent of operations also affects the competitive advantage of a firm. Likewise, a firm operating in related industries can create a competitive advantage by exploiting inter-relationships among the industries.

A firm might choose to provide an activity internally or externally based on how one activity influences other activity is in the value chain. The Whirlpool Corporation prefers to serve its customer internally. Thus, it seeks to gather valuable information through its service representatives. This feedback helps the organization in rectifying problems in the service and design new products.

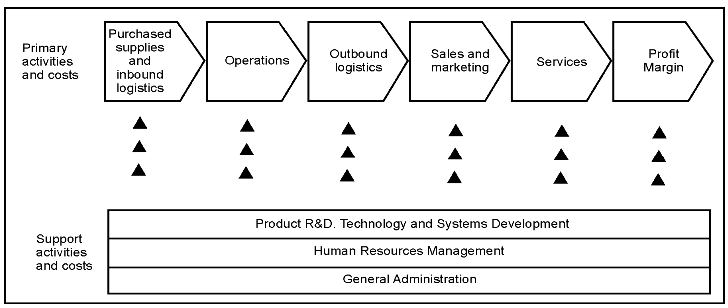
Mergers help in benefiting from the synergies in the value chain linkages. These linkages provide access to global markets and offer a larger range of products to the customers.

Value Chain Analysis

Value chain analysis is based on the assumption that a business's basic purpose is to create value for its users and its products or services. In this method of analysis, strengths and weaknesses are assessed by dividing a business into a number of linked activities, each of which may produce value for the customer. In value chain analysis, managers divide the activities of their firms into sets of separate activities that add value. To do so, the activities of the organization (such as raw material procurement. logistics, operations, sales, marketing, technology development, firm infrastructure, etc.) have to be identified and examined by managers. Managers thus acquire an in-depth understanding of their firm's capabilities, its cost structure, and how these create competitive advantage or disadvantage.

Value chain analysis divides a firm's activities into two major categories, i.e., primary and support activities as illustrated in Figure 1. Primary activities are those activities that are involved in the physical creation of the product, marketing and after-sales support. Support activities assist the primary activities by providing infrastructure that allows them to take place on an ongoing basis. The value chain includes a profit margin, creating value that exceeds cost so as to generate a return for the effort. Each of the primary and support activities can be further divided for a thorough internal analysis.

Figure 1: The Value Chain



Source: Pearce and Robinson, Strategic Management.

Conducting a Value Chain Analysis

In the initial step of a value chain analysis, a company's operations are divided into specific activities or business processes as shown in Figure 1. The next step is to attempt to attach costs to each discrete activity (Activity-based costing). If managers assign costs and assets to each and every activity, managing internal strengths and weaknesses would be much easier and simpler. Once the company's value chain has been documented and costs determined, managers need to identify the activities that are crucial to customer satisfaction and market success. The following considerations are essential at this stage:

- The manager's choice of activities has to be influenced by the company's basic mission.
- The manager must take into consideration the nature of value chains and the relative importance of the activities since they vary by industry.

Value chain analysis also requires a meaningful comparison to use for evaluating the role of an activity as a strength or weakness.

The framework of the value chain analysis has certain strengths. Firstly, it clearly highlights the importance of customer value. Secondly, it provides a sense of direction to managers by offering a generic checklist of what to analyze when assessing a firm. Lastly, it indicates that everything an organization does can be managed to improve the firm's overall ability to create value. Thus, the value chain framework is useful for organizations in general and to managers in particular. However, the framework suffers from certain limitations. It does not provide a sense of how various activities interact or relate to one another.

STRATEGY AND INTERNAL ANALYSIS

When evaluating or developing a strategy, the starting point is the organization's present strategy and the resources it has or may be able to acquire. The internal analysis process considers the firm's resources, the business the firm is in, its objectives, policies and plans, and how well they were achieved. The important questions that are answered by the process of internal analysis are:

- Is this strategy consistent with the various resources of the enterprise?
- Are the available resources appropriate for any changes in strategy or new strategies?

The results and conclusions of the analysis are crucial ingredients in determining what the future strategy might be or can be. The internal analysis not only indicates what the firm's resources are but also judges how well these assets have been used by the management. Although the internal analysis is a very important element of the strategy formulation and evaluation process, it is one element and only a part of the overall analysis of the organization. It initiates the analysis by clarifying what an organization is capable of doing in light of the resources available. Thus, internal analysis requires the analyst to appraise the management's utilization of resources, formation and implementation of strategy, and performance by the various functions required by the strategy.

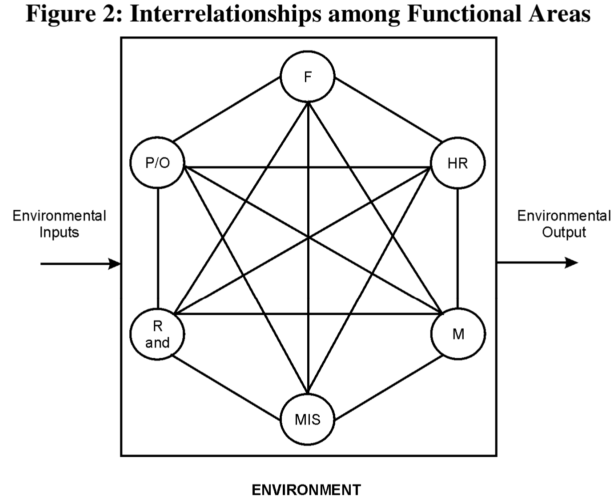
The Analysis Process

The first part of the analysis process is gathering the data, information and facts. This is because proper analysis requires conclusions and/or judgments based on facts, opinions, observation and other evidence available. Once relevant information has been selected, analyzed and conclusions have been reached, it is necessary to consider alternative solutions and actions. The decisions finally arrived at must be made in the context of overall organizational strategy.

ANALYZING DEPARTMENTS AND FUNCTIONS

All organizations irrespective of their size, nature and scope of business must perform the functions of finance, production, marketing, human resource and research and development. For efficient strategic planning, implementation, and control, careful planning, execution and coordination of these functions are highly essential. The different departments of a firm are like the different organs of the human body. Needless to say, managers should understand the interrelationships among these functions to formulate effective strategies. Figure 2 shows that the activities of all the functional areas are interwoven to attain their objectives as well as those of the entire firm. The various departments and functions of a firm are described below.

Figure 2: Interrelationships among Functional Areas



F= Finance; HR = Human Resources; M = Marketing; MIS = Management Information Systems; R and MD = Research and Marketing Development; P/O = Production/Operations.

Production/Operations/Technical

The basic objective of the production function is to ensure that the outputs produced have a value that exceeds the combined costs of the inputs and the transformation process. The production strategies of small business units would be different from those of large business units. These two strategies are therefore discussed separately.

Strategies for Small Business Units

- Small business units go for low initial investment in their plant, equipment, and long-term advertising, etc., because they compete in niche markets on price.
- The units that adopt the niche-differentiation strategy select an approach that yields quality. Sometimes, they may opt for handcrafting processes and produce according to the customer's preferences.
- These units also make low investments in semi-variable and variable costs.

Thus, small business units generally adopt differentiation strategies that lower costs and increase differentiation. This strategy may involve higher costs initially, but eventually it will result in cost savings and quality improvement.

Strategies for Large Business Units

The major advantage of large business units is the reduction in cost per unit of output due to economies of scale. As a firm gains experience in producing a product, production/manufacturing costs can be systematically reduced. Moreover, three variables are generally present in these units. They are:

i. *Capital-labor substitution*: Substituting capital for labor and vice-versa.

ii. *Economies of scale*: Reductions in cost per unit of output as volume of output increases.

iii. *Learning*: Understanding the role of specialization and its advantages.

These three variables, when put together, will result in decrease in cost per unit as the business gains greater market share. But large business units have to bear the risk of technological innovations. That is to say, when plant and machinery become obsolete, the investment will have to be written off.

A firm's (whether large or small) production groups must communicate and interact with other functional areas such as marketing and research and development on a continuous/periodic basis. This is because consumers demand value added products, thus pressurizing the production department to maintain quality and reliability at the lowest possible cost. Moreover, the effects that production and related areas have on financial statements must also be taken into consideration. This is because, ultimately, the managers will be evaluated in light of what they have done or not done to enhance the company's financial position.

Finance and Accounting

Insight into the financial situation of a company will quickly place its condition in perspective. The critical areas in any profit or non-profit organization can be summed up as follows:

- Scanning and using funds,
- Planning for securing and using funds,
- Controlling expenditure, and
- Reporting all transactions and results to appropriate parties.

Facts can be gathered and tentative conclusions can be drawn in the initial scanning of operations. Later, analyzing can provide information and understanding in considerable depth.

The financial statements of a firm offer abundant information about the present position and also reveal the results of operations over time. The details of cash, receivables, inventories and corresponding liabilities are provided by the balance sheet. The job of the internal analyst is to "make the figures talk." Suitable explanations and notes have to be given at the end of every financial statement so that the reader can get an idea of it in an instant. However, a common tendency is to state conclusions rather than facts when analyzing financial statements. The response of the internal analyst to information from the financial statements should be factual and substantially quantitative. For example, an analyst after calculating ratios concludes that the company has too much debt and is heavily leveraged. But the study of the company's return on equity indicates that excellent financial practices are being employed. The balance sheet and income statements then provide factual information within the limitations of accounting principles. Thus, inferences and conclusions are better made after considering other information in addition to the statements.

Financial Analysis

One of the most important tools for assessing the strength of an organization within its industry is financial analysis. A financial analysis measures how a company is doing in comparison with past years and its competitors in the industry. There are four basic groups of financial ratios:

- Liquidity ratio
- Leverage ratio
- Activity ratio
- Profitability ratio.

Liquidity ratio

A company's ability to meet its imminent financial obligation is known as liquidity. Liquidity ratios are used as indicators of a firm's ability to meet its short-term obligations. Two widely used liquidity ratios are:

The quick ratio recognizes that inventory is usually less liquid than other current assets. In the case of long production processes, inventory may not provide much liquidity because it cannot be turned into cash.

Leverage ratio

Leverage ratios identify the source of a firm's capital, i.e., owners or outside creditors.

Activity ratio

In general activity ratios measure a firm's efficiency in generating sales and making collections. The various activity ratios are: inventory turnover, average collection period, fixed asset turnover, total asset turnover etc.

Other things being equal, a low inventory is more efficient because it indicates that the firm does not have many assets tied-up in inventory. Total asset turnover and fixed asset turnover measures the company's ability to generate sales for a given level of assets. A higher ratio indicates a more efficient firm.

Profitability ratio

Profits are the net result of a large number of policies and decisions chosen by a company's management. Profitability ratios indicate how effectively a firm is being managed.

For profit margin and return on assets, high ratios are superior to low ratios; but with return on equity, a high value may indicate a higher level of financial leverage than of managerial efficiency. Also, a high degree of financial risk may accompany a high return on equity.

Financial analysis is not a standardized or mechanical process. It is the means for analysis and must always be directed towards the needs of a specific situation. Financial analysis, if approached in a proper manner, can be a productive starting point for assessing financial strengths and weaknesses and other attributes of a firm, based on past performance.

Information in financial statements is historical and often derived from a relatively distant past. The data shows what has happened and what the situation was in the past. Future trends can be drawn but the basic assumption that conditions will remain similar enough to extrapolate data seldom proves accurate. Financial data can provide insight into the future when analyzed properly in a strategic context. Regardless of the type of institution, the finance function must be examined in order to gain some insight into its health. Even non-profit institutions must pay their bills in time to continue operations. Even though profit is not an objective of non-profit organizations, an excess of income over expenses allows them to grow larger and stronger to accomplish their service objectives.

A review of the financial conditions provides information about the organization and the management. It also reveals whether revenues have been increasing profitability. A financial analysis identifies the financial resources of the firm and how well they have been and are being utilized. All of this is important when considering the appropriateness and implementation of past, present and future strategies.

Marketing

An analysis of the marketing function requires the inclusion of the product-market strategy. Marketing brings together the organization and the external environments crucial to its existence. In the marketing function, the various activities undertaken are:

- Market Research
- Market Analysis
- Market Forecasting
- Sales Forecasting
- Advertising
- Direct Selling.

In the marketing function, information is brought to the organization and forwarded to its customers. Thus, marketing is a vital communication link between the organization and the outside world. Internal relationships exist between the marketing group and the research and development, production and planning areas. The product managers, project managers and information coordinators of various kinds strive to accomplish effective communication between marketing and other departments, and thus between the outside world and the internal organization. For other departments to perform well, sometimes, vital information has to be provided by the marketing department. For example, sales forecast forms a basis for budget and financial/planning and market research forms a basis for product development. In certain organizations, the marketing function is so essential that they are looked upon as “marketing” companies. For example, Coca-Cola is known the world over for its marketing function. An analysis of the marketing function ultimately leads to strategy changes at the corporate or individual business unit level. Thus, analyzing the marketing function leads to recommendations about both marketing and marketing management in the organization.

Research and Development

A major functional area of any organization is often research and development. The importance of R&D varies with the nature of organization. In certain circumstances, the R&D function is of minor importance (For example, retailing operations). The research and development function either supplements a product-oriented effort or improves the production processes. Although many firms develop new products, those with technically oriented products are most involved in R&D. In such organizations, research and development is accomplished at great expense, but it is a vital necessity if the firm is to prosper or even survive. Many non-profit organizations such as hospitals and universities also engage in R&D. Such organizations spend large sums to support medical education, staff and equipment to improve their products, services and contributions to society.

The two areas of research and development are product R&D and process R&D. Product R&D is concerned with innovations/implementations in the firm’s products. Process R&D attempts to reduce the costs of operations and seeks constant improvement in quality through more efficient processes. Business units that adopt low-cost strategies emphasize on process R&D, whereas businesses that adopt differentiation strategies emphasize product R&D.

If the organization has strengths in R&D or if the external environment demands it, the company should commit itself to a strong R&D effort. Companies with less technical strength must develop a “fast follower” strategy that recognizes an ability to lead in R&D. Like the other areas, in this area also, the analyst needs to gather facts, draw conclusions and make recommendations for change.

Integrating the Functional Areas

All the functional areas must work in perfect coordination to implement the generic strategy successfully. The perfect inter-working of one functional area with all other functional areas is required.

SUPERIOR PRODUCT DESIGN

Designing a superior product involves not only the contributions of production department, but also the contribution of finance, marketing and costing departments. Superior service when combined with superior design gains an advantage over its competitors. Thus, product design includes features like designing a product for easy manufacturing, improving the product’s quality and functionality.

SUPERIOR CUSTOMER SERVICE

Developing and maintaining qualitative customer service is more challenging than improving product quality. Companies that provide premium services can command premium prices of their product. An important method for providing superior quality service is giving personal attention to the customers. All functional areas must work together like a team to provide qualitative service to the customer, before and after sales.

SUPERIOR SPEED

Speed in developing, producing, distributing products and providing services will give the organization and the business a significant competitive advantage.

SUPERIOR GUARANTEE

Less than acceptable products are produced due to problems of functioning, quality, etc. Companies give guarantees in order to avoid customer grievances. Guarantees are provided to gain a competitive advantage over the competitors. A service guarantee is more challenging to provide than a product guarantee.

Thus, overall strategic success depends on the tight integration of all the functional areas. And business organizations can achieve competitive advantage by accomplishing full functional integration.

Box 1 lists the typical internal factors that would be the focus of internal analysis in most firms. The list is segregated along functional lines because firms organize their operations through functional lines to get their products sold, delivered, financed and accounted. A close scrutiny of each of these functions serves as a compelling, strategically relevant focus for internal analysis. Organizations are not likely to evaluate all factors listed in Box 1 as potential strengths and weaknesses. For example, the strategic factors of firms in the oil industry will be quite different from those of firms in the hospitality or construction industry.

Strategists examine a firm’s past performance to isolate key internal contributions to favorable (or unfavorable) results. Analysis of past trends in a firm’s sales, costs and profitability is very important for identifying its strategic internal factors. The identification of strategic internal factors requires an external focus. Strategists’ efforts to isolate key internal factors are assisted by the analysis of industry conditions and trends and by comparisons with competitors. Thus, by adopting the functional approach, managers focus on basic business functions, thus leading to a more objective, relevant internal analysis that enhances strategic decision-making. Whether looking at attributes of marketing, production, finance or research and development, the functional approach structures managers’ thinking in a focused and potentially objective manner.

Box 1: Strategic Internal Factors

The typical factors that would be the focus of internal analysis in most business firms are as follows:

Marketing

- Firm's product; breadth of product line
- Concentration of sales in a few products or to few customers
- Ability to gather needed information about markets
- Market shares or submarket shares
- Channels of distribution, number, coverage and control
- Effective sales organization and knowledge of customer needs
- Pricing strategy and pricing flexibility
- After sales service and follow-up.

Finance and Accounting

- Ability to raise short-term capital
- Ability to raise long-term capital, debt/equity
- Tax considerations
- Cost of capital relative to industry and competitors
- Relations with owners investors and stockholders
- Cost of entry and barriers to entry
- Price-earning ratio
- Working capital: flexibility of capital structure
- Effective cost control; ability to reduce costs.

Productivity/Operation/Technical

- Raw materials cost and availability; supplier relationships
- Inventory control system, inventory turnover
- Location of facilities layout and utilization of facilities
- Economies of scale
- Effective use of subcontracting
- Efficiency and cost/benefit of equipment
- Research and development of technology/innovation
- Patents, trademarks, and similar legal protection.

Personnel

- Management personnel
- Employees skills and morale
- Labor relations cost compared to industry and competition
- Efficient and effective personnel policies
- Employee turnover and absenteeism
- Specialized skills
- Effective use of incentives to motivate performance.

Organization of General Management

- Organizational structure
- Firm's image and prestige
- Firm's record for achieving objectives
- Organization of communication system
- Organization climate culture
- Strategic planning system.

Source: ICFAI Center for Management Research.

ANALYZING MANAGEMENT

Within a strategic framework, the internal analysis of an organization begins and ends with the management of the organization. Everything else is dependent on the actions of the firm's management group. The management can be evaluated on the basis of the organizational profile of strengths and weaknesses in light of what it has and has not done, or what it has or has not achieved. If more than one group of managers is involved, each group should be evaluated in view of its accomplishments during a particular time. Moreover, individuals and groups within the management may be evaluated separately. In diversified organizations, the management of each subunit is assessed individually.

Assessing Top Management

The assessment of the top management of the organization is a major reason for the internal analysis of an organization. Top management, in this context, refers to those primarily responsible for organizational strategy. These are the managers who guide the overall destiny and operations of the organization. The important questions to be asked here by the analyst are:

- How has the organization been managed in the past?
- How is it being managed now?
- How well is the company prepared to face the future?

Top management can be analyzed and evaluated in-depth by pulling together the separate areas into an overall profile or analysis of the entire organization. The analyst should make statements about the firm as a whole, its top management, and the strategies of the past, present and future. When formulating business strategy, conclusions and decisions should be based on information as comprehensive as can be obtained within a reasonable time and at a reasonable cost.

Using Results to Analyze Management

A variable input involved in the analysis of management is results. The various types of results could be:

- Production/Manufacturing
- Marketing
- Human Resources
- Research and Development
- Financial.

With respect to results, the most important questions are:

- Were objectives established and measures developed against which to compare with the results?
- Were planned results accomplished in all the important areas within the organization?
- How well did management assess its position, plan for change and carry out change?
- Was a strategy developed and implemented?
- Were objectives articulated, and understood by those responsible for implementing them?
- Have decisions been made by one person or by a group?
- Have the top level managers been open to and initiated change readily?

The answers to such questions tell much about the future possibilities of the organization as well as about its present condition. Thus, a thorough look at results in profits, sales, cost reduction, research and development, building of plants, morale, social contribution and other areas will reveal much about the quality of both the organization and its management. Generally, good performance in the functional areas will lead to good overall results.

Stockholders and Directors

The stockholders of a business organization have the basic rights of ownership, unless management overlaps heavily with ownership. The management should act in the best interests of the stockholders. It should take decisions that would clearly benefit the stockholders over the long run. If the directors do not consider the interests of stockholders, they fail in one of the basic responsibility of management, i.e., to protect and enhance the investment of the firm's owners. Regarding stockholders, the analyst should explore the following questions:

- How do stockholders collectively make themselves heard?
- What is the stockholders' representation on the board of directors?
- Is the board active or inactive?
- Does the board of directors have a voice in the determination of strategy?
- Is the composition of the board logical considering the nature of the organization and its business?
- Has the board of directors exercised its powers in setting the basic objectives of the organization?

THE HUMAN SIDE OF ENTERPRISE

The human element permeates all segments and units within an organization. Due to this, it should be considered independently. Although attention has been given to the human element in each functional area, an overall profile of the organization should view this aspect as an area in itself. The human resource management function includes major activities like:

- Designing and analyzing jobs based on the future needs of the organization.
- Planning for future human resource needs. .
- Recruiting, selecting and employing people based on the organization's needs.
- Training the employees to develop the organization's human resources.
- Appraising the performance of the employees and moving them among different levels based on organizational needs.
- Fixing and maintaining compensation package for employees.
- Maintaining conducive human relations.
- Creating and maintaining a high quality of work life in the organization.
- Adopting growth strategies for human resource development.
- Creating and maintaining a harmonious organizational climate.
- Team building.
- Managing the diversified culture among the employees.

Companies adopting stability as a strategy do not bring significant changes in human resource management. In the process of internal analysis, the analyst must judge whether the human element is actually a resource and strength for the organization or a weakness that may impede management efforts to employ other resources successfully.

The development and sustenance of human resources function is a major task. This has to be taken care of not only by top management but also by all the executives in the organization. If management has succeeded here, high morale is likely to follow. Thus, strengths in the human resource side of the organization are crucial during the implementation of strategy.

QUANTITATIVE APPROACHES FOR EVALUATING INTERNAL FACTORS

There are various quantitative tools for evaluating the internal capabilities of a firm. For evaluating financial, marketing and operating factors, ratio analysis is a useful tool. The firm's balance sheet and income statement are important sources from which meaningful ratios can be derived. The process that helps in guiding internal analysis is described below.

i. In the first step, managers audit the key aspects of the business operation. In addition, the target key areas are assessed. Generally, the targeted areas are central to the firm's strategic decision and are called as "strategic internal factors".

ii. In the second step, managers evaluate the firms' status by comparing the current condition of the strategic internal factors with the past capabilities of the firm. Through this comparison, managers find out how much improvement has been achieved. They also find out whether each key factor presents a favorable or unfavorable situation.

iii. The third step is the most crucial one. In this step, managers seek some basis for comparison that is linked to key industry or product/market conditions. This comparison accurately determines whether the company's condition on a particular factor represents a potential strength or weakness. Managers use three perspectives when making such a comparison.

   - Requirements for success across different product/market stages of evolution,
   - What competitors are capable of doing,
   - Perceived key requirements for success in the market/industry segments in which they compete.

   The results of this step determine whether key strategic internal factors are:

   a. **Competitive Advantages:** If the key strategic internal factors lead to competitive advantages, then they provide an edge over competitors.

   b. **Basic Business Requirements:** If the key strategic internal factors are basic business requirements, then they are important capabilities for the firm. But these internal factors will also be typical for every viable competitor.

   c. **Key Vulnerabilities:** If the key strategic internal factors lead to vulnerabilities, then the company lacks the necessary skill, knowledge or resources to compete effectively.

iv. The final step in internal analysis is to provide the results. Sometimes, in this step, the company profile is used as input into the strategic management process.

The process of internal analysis, when matched with the results of management's environmental analysis and mission priorities, provides the critical foundation for strategy formulation. The managers are in a better position to formulate effective strategies when the internal analysis is accurate, thorough and timely.

SUMMARY

- When evaluating a corporation's functional and managerial resources, answers to numerous key questions reveal how the organization looks as a whole. The internal analysis and resulting profile is valuable for identifying the areas in which the organization has performed well in the past and the areas in which it is doing well at present. In this chapter, we discussed the meaning of internal analysis and the value of systematic internal analysis. Strategy and internal analysis were then discussed in the chapter. Then various departments and functions such as finance, marketing, production, etc., were also analyzed. It was concluded that all the functional areas must work in perfect coordination to implement a strategy successfully.
- Within a strategic framework, the internal analysis begins and ends with the organization's management. As a result, topics such as analyzing management, assessing top management and stockholders and directors are discussed. Then the human resource function was examined as it permeates all the segments and units within an organization. Lastly, a quantitative approach for evaluating internal factors was discussed. Thus, a complete internal assessment is necessary for strategy formulation.

Chapter VI

Organizational Culture

After reading this chapter, you will be conversant with:

- Meaning of Culture
- Culture and the Organization
- Culture and Strategy Creation
- Culture and Organizational Structure
- Culture and Style of Management
- Culture and Power
- Determinants of Culture
- Aspects and Levels of Culture
- Change of Culture
- Culture and Values
- Cultural Influences on Organizational Life

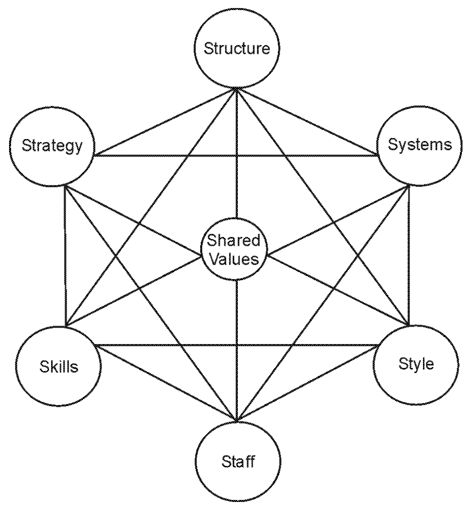
Introduction

In this chapter, we would discuss the meaning of culture and its linkage to the organization. The culture and its strategy relationship through structure, style of management and power are discussed in detail. We would also look into the aspects of culture, its determinants, levels and methods employed to change the culture. The implications of culture on values and value systems along with cultural influences on organizational life are discussed in detail.

MEANING OF CULTURE

Every organization has its own culture. An organization's culture is an equivalent to an individual's personality. It is an intangible, ever-present theme that provides meaning, direction, and the basis for action. As personality influences the behavior of an individual, the shared assumptions of beliefs and values among a firm's members influence opinions and actions within a firm. McKinsey 7-S framework as shown in Figure 1 highlights the importance of shared values leading to culture of the organization as a whole. It forms the nucleus of the framework.

Figure 1: The McKinsey 7-S Framework



Organizational Culture

Organizational culture is the set of important assumptions (often unstated) that members of an organization share in common.

An organizational member can simply be aware of the beliefs and values of the organization without sharing them personally. The beliefs and values have more personal meaning if the member views them as the guiding principles for appropriate behavior in the organization by complying with them. Fundamental commitment through internalization of the beliefs and values of the organization by members result in corresponding behavior that is intrinsically rewarding for the members. The members derive immense personal satisfaction from their actions in the organization since they are congruent with their personal beliefs and values. The assumptions become shared assumptions through internalization among an organization's individual members. Those shared internalized beliefs and values shape the content and account for major strength of an organization's culture.

CULTURE AND THE ORGANIZATION

Leaders typically attempt to manage and create a distinct culture within their organizations through a variety of ways. Some common methods are as follows:

Key Themes or Dominant Values Emphasized

Throughout the world, businesses build strategies around distinct competitive advantages they possess or seek. These competitive advantages are achieved through quality, differentiation, cost advantages, speed, etc. Insightful leaders nurture these key themes or dominant values within their organizations and reinforce competitive advantages that they seek to maintain or build.

The key themes or dominant values may center around some wordings in the organization's advertisements. They are also often found in internal company communications. For instance, Xerox's key themes include respect for the individual and services to the customer. P&G emphasize that its overarching value is product quality. Delta Airlines flies by the "family feeling" theme. These themes build team spirit and nurture each employee's cooperative attitude towards others, cheerful outlook towards life, and above all pride in a job well done. Safety orientation of Dupont states that a report of every accident must be on the chairman's desk within 24 hours. This strict adherence to the policy resulted in a safety record that was many times better than the chemical industry average and many more times better than the all manufacturing industry's average.

Encourage Dissemination of Stories and Legends about Core Values

Companies with strong cultures are enthusiastic collectors and tellers of stories, anecdotes and legends in support of basic beliefs. Some companies emphasize on customer service that they uphold the 99.5 percent service level to customers. Some others share stories and ideas with the entire organization by way of rallies designed around some major theme such as quality, cost reduction, ethical issues, etc. A few major global giants like 3M aiming at – innovation, P&G, Johnson & Johnson, IBM, that look for – *quality,* developed organizational cultures around those themes that members identify strongly and share those beliefs and values with others.

Institutionalization of Practices that Systematically Reinforce Desired Beliefs and Values

Companies with strong cultures are clear about their beliefs and values that keep them together and also take the process of shaping those beliefs and values very seriously. Many companies institutionalize yearly contests that reinforce the desired beliefs and values throughout the company.

Adopt Very Common Themes in their Own Unique Ways

The following are the most typical beliefs that shape organizational culture:

i. A belief in being the best.

ii. A belief that growth and profits are essential to a company's healthy financial position.

iii. A belief in superior quality and service.

iv. A belief in the importance of informal communication.

v. A belief in the importance of people as individuals and a faith in their ability to make a strong and effective contribution.

vi. A belief in inspiring people to do their best, whatever their ability.

vii. A belief in the importance of the details of execution – the nuts and bolts of doing the job well.

viii. A belief that customers should reign supreme.

Every organization implements these beliefs differently to fit a particular situation. Every organization's values are the handiwork of one or two legendary leaders. Therefore, every company has a distinct culture that it believes no other company can copy successfully. Hence, in companies with very strong cultures, employees either accept the norms laid out by such cultures or opt out from that cultural dictate leaving the company.

The stronger a company's culture becomes and the more that culture is directed towards the organizational stakeholders, the less the company uses policy manuals, organizational charts, and detailed rules. Procedures and regulations to enforce discipline and norms. The main reason is that the guiding values inherent in the culture convey in a clear fashion what every employee is supported to do in most situations.

Management of Organizational Culture in a Global Organization

Organizational culture must recognize cultural diversity – the reality of present global organizations. Social norms create differences across national boundaries that influence people's interaction, read personal cues and otherwise interrelate socially. Values and attitudes under similar circumstances also vary among countries. For instance, individualism forms the central core to the value structure of North American countries whereas group needs dominate the value structure of Japan. Similarly, family needs gain importance in the value structure of the Indian subcontinent. Religion also creates cultural differences. Hence, religious holidays, practices and beliefs differ structurally in very fundamental way that needs to be taken into account to shape organizational culture in a global setting. Education or ways people are accustomed to learning differ across national borders. The process of shaping an organizational culture often involves considerable "education" and the organizational leaders should be sensitive to global differences in approaches to education. This would make sure that the cultural education efforts are effective.

Therefore, cultural diversity, both domestically and internationally, is something that most managers will experience due to differing backgrounds from global acquisitions and mergers. Many managers face the situation in global companies located world over employing many people with different countries of origin having many languages and moreover find it all the more difficult to manage many cultures that these people represent. For instance, in India itself, there is wide variety of cultures with very rich heritage which differs from state to state and sometimes within the state itself.

CULTURE AND STRATEGY CREATION

The key components of a firm are the structure, staff, systems, style and people. These influence the ways of execution of key managerial tasks. They also influence the formation of critical management relationships. Strategy depends on these relationships between a firm's culture and the critical factors that form an organization. Implementation of a new strategy is largely concerned with minor to major adjustments in these organizational components to accommodate the perceived needs of the strategy. Culture and strategy creation revolves around the strategy and culture relationship that requires sensitivity to the interaction between the changes necessary to implement the new strategy and the compatibility between those changes and the firm's culture.

Table 1 provides a simple framework for managing the strategy and culture relationship that identifies four basic situations a firm might face.

Table 1: Managing the Strategy-Culture Relationship

<table>
<tr><td rowspan="2">Changes in key organizational factors that are necessary to implement the new strategy</td><td>Many</td><td>Link changes to basic mission and fundamental organizational norms
1</td><td>Reformulate strategy or prepare carefully for long-term, difficult change
4</td></tr>
<tr><td>Few</td><td>**2**
Synergic Focus on reinforcing culture</td><td>**3**
Manage around the culture</td></tr>
<tr><td></td><td></td><td>High</td><td>Low</td></tr>
<tr><td></td><td></td><td colspan="2">Potential compatibility of changes with existing culture</td></tr>
</table>

Linkage to Mission

A firm in situation 1 in the Table 1 faces a challenge in which implementing a new strategy requires several changes in structure, systems, managerial assignments, operating procedures or other fundamental aspects of the firm. However, most of the changes are potentially compatible with the existing organizational culture. Firms in such situation usually perform effectively and either seeks to take advantage of a major opportunity or attempt to redirect major product-market operations consistent with proven core capabilities. Such firms will be in a very promising position. They can pursue a strategy that requires major changes but still benefit from the power of cultural reinforcement.

The four basic considerations that are emphasized by firms managing a strategy culture relationship are:

i. *Key changes should be visibly linked to the basic company mission*: The company mission provides a broad official foundation for the organizational culture. Top management should make use of all available internal and external meetings to reinforce the message that the changes are inextricably linked to the company mission.

ii. *Emphasis should be placed on the use of existing personnel*: Wherever possible, existing personnel should fill positions created to implement the new strategy. Existing personnel embody the shared values and norms of the organization that will have influence to ensure cultural compatibility, since major changes are implemented by way of a new strategy.

iii. *Care should be taken if adjustments in the reward system are needed*: The adjustments should be consistent with the current reward system.

iv. *Key attention should be paid to the changes that are least compatible with the current culture*: The current norms should not get disrupted as far as possible. For instance, an organization may choose to subcontract an important step in a production process since that step might be incompatible with the current organizational culture.

Many global firms are entering the internet-based market. Serving such radically different market requires numerous organizational changes. To maintain maximum compatibility with the existing culture while doing so, these companies had to adopt considerable public and internal effort to link their Internet focus with the longstanding mission. Many messages relating to the new technology with the tradition of the organizational beliefs and values need to be communicated and every stakeholder has to be encouraged to adapt the new technology. For instance, the new technology in this case could be network-centric computing and going online in day-to-day management. Utmost care should be taken in filling the personnel for such new positions by making use of the existing staff to implement the strategy.

Maximize Synergy

A firm in cell 2 needs only a few organizational changes to implement the new strategy. Even those changes are potentially quite compatible with the current culture. A firm under such situation should emphasize two broad themes.

i. Take advantage of the situation to reinforce and maintain the current culture.

ii. Use the time of relative stability to remove various existing organizational road blocks to bring in the desired culture.

Manage Around the Culture

A firm in cell 3 needs to make a few major organizational changes to implement a new strategy. But, these changes are potentially inconsistent with the firm's current culture. The critical situation for a firm at this juncture is that, the changes it proposes to make should have reasonable chance of success.

A firm can manage around the culture in many ways –

- Create a separate firm or division
- Use new task forces, teams or program coordinators
- Sub-contract
- Bring in outside expertise
- Sell out a successful idea.

Even though the above ways are viewed as options, the key idea is to create a method or to achieve the change avoiding confrontation with the existing incompatible cultural norms. For the success, the organization should establish a diminishing resistance to change, whereby the new strategy may be absorbed into the firm gradually at an appropriate time.

Reformulate the Strategy or Culture

A firm in cell 4 faces the most difficult challenge. Such a firm must make organizational changes that are inconsistent with the current values and norms. Such an organization also faces complex, expensive incompatibilities that often require long-term challenge to change the current culture. Reformulation of strategy is appropriate to firms that require massive organizational change and such a strategy gives rise to massive cultural resistance. Such large-scale change management requires reshuffling of even the top management and to restrategize the existing. Usually, in such exercises, voluntary retirement schemes are implemented as part of a massive recreation of the culture to go along with major strategic changes. If such situations need to be avoided, the firm may opt to reformulate the strategic plans itself so that they are more consistent with the established organizational norms and practices.

CULTURE AND ORGANIZATIONAL STRUCTURE

Organizational structure is a major priority in implementing a carefully formulated strategy. If structure and strategy are not closely coordinated, then the result will probably be inefficiency, misdirection and fragmented efforts. All activities, responsibilities and interrelationships need to be organized in a manner that is consistent with the strategy chosen; else the structure is left to evolve on its own.

The need for an organizational structure becomes apparent as a business evolves. The organizational structure is relatively simple in a small firm where one person manages the current operations and plans for the future. As the magnitude of business activity increases, the essential need to subdivide activities, assign responsibilities and provision for the integration and coordination of the new organizational parameter arises. These organizational parameters provide a structure that provides a formal means of decentralizing and centralizing which is consistent with the organizational and control needs of the strategy.

Five basic types of structural choices that are currently used by most of the business firms are:

- Simple
- Functional
- Divisional
- Strategic Business Unit (SBU)
- Matrix.

Diversity and size create unique structural needs for a firm. However, structure is not the only means for getting ‘organized’ to implement a strategy. Reward systems, planning procedures, and information and budgetary systems also should be employed. These elements operate interdependently with the formal organizational culture to shape the way the things are done. But it is through structure that strategists attempt to balance internal efficiency and overall effectiveness within a broader environment. Therefore, structure is not an end in itself but rather a means to an end.

Figure 2: A Simple Organization

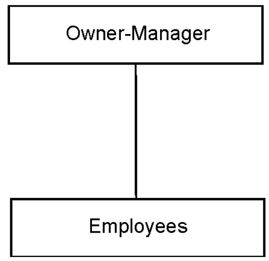


Figure 2 shows the simple organizational structure. In the smallest form of business enterprise, the simple structure prevails. All strategic and operating decisions are centralized with the Chief Executive Officer (CEO). The strategic concern primarily is survival; hence, one bad decision could seriously threaten the continued existence of the business. Therefore, this structure maximizes the CEO's control. This structure also allows rapid response to product/market shifts and has the ability to accommodate unique customer demands without any coordination difficulties. These structures also encourage employee involvement in more than one activity. These types of structures are efficient in businesses that serve a localized, simple product/market. .

Figure 3: Functional Organizational Structure

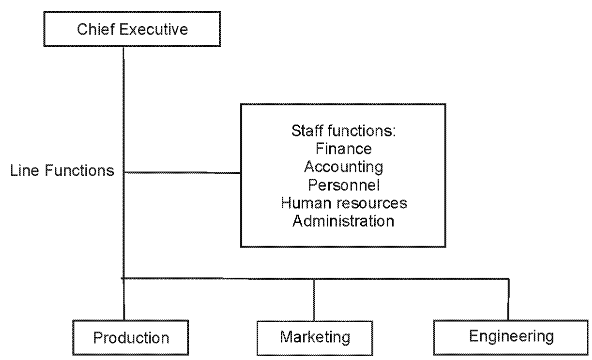


Figure 3 shows the functional organizational structure. These structures predominate in firms that concentrate on one or a few related products/markets. Functional structures group similar tasks and activities as separate functional units within the organization, like production, operations, marketing, sales, finance, accounting, research and development, personnel, industrial relations, human resources development etc. Thus, specialization encourages greater efficiency and refinement of a particular functional expertise. This structure also allows the firms to seek and foster distinct competencies in one or more functional areas leading to the firm's overall strength and core competency. Expertise is critical to single product/market companies and also to the firms that are vertically integrated. The challenges that this structure poses are:

- 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.
- Stakeholders see the firm's strategic issues primarily as functional problems.
- CEO's coordinating role becomes critical with the potential conflict if the strategy needs to be effectively implemented.

Therefore, integrating devices such as project teams or planning committees are frequently used in such structurally designed businesses to enhance coordination and to facilitate a thorough understanding across functional areas.

Figure 4: Divisional Organizational Structure

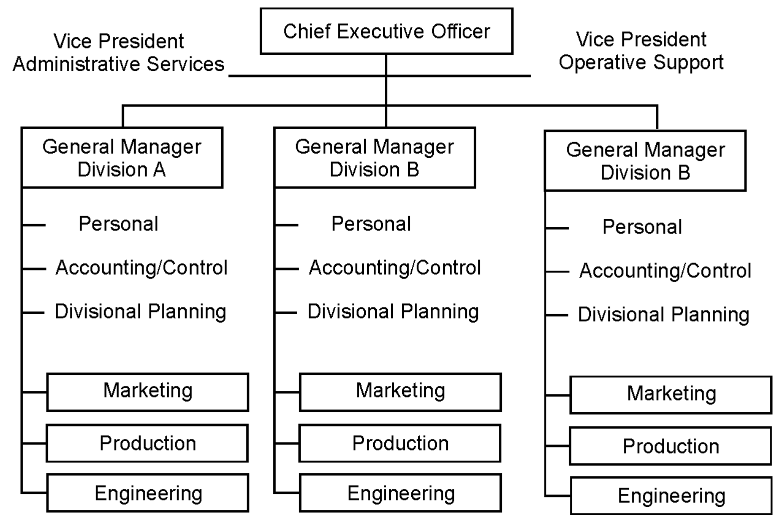


Figure 4 depicts the divisional form of organizational structure. This structure best suits such firms where there is diversity in product lines, covering broad geographic areas, utilizing unrelated market channels, serving distinctly different customer groups etc. A divisional structure allows corporate management to delegate authority for the strategic management of a distinct business entity. Critical decision-making is expedited within each division in response to a variety of competitive environmental pressures. This structure also has a distinct advantage i.e., it forces the corporate management to concentrate on corporate level strategic decisions.

Figure 5: Strategic Business Unit

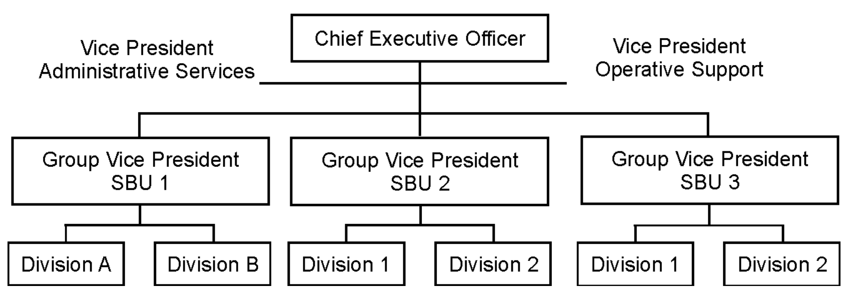


Figure 5 highlights the Strategic Business Units (SBU) in a figurative way. As the divisional operations overweigh, firms encounter difficulty in controlling the structure due to sheer diversity, size and increasing number of units. The evaluation and control of numerous multi-industry divisions may become difficult leading to formation of another layer of management to improve strategy implementation, promotion of synergy and to gain greater control over the diverse business portfolios. The grouping of various divisions or parts of some divisions in terms of common strategic elements is commonly called as formation of a Strategic Business Unit (SBU). These structures are usually centered around independent product/market segments served by the firm.

Figure 6: Matrix Organizational Structure

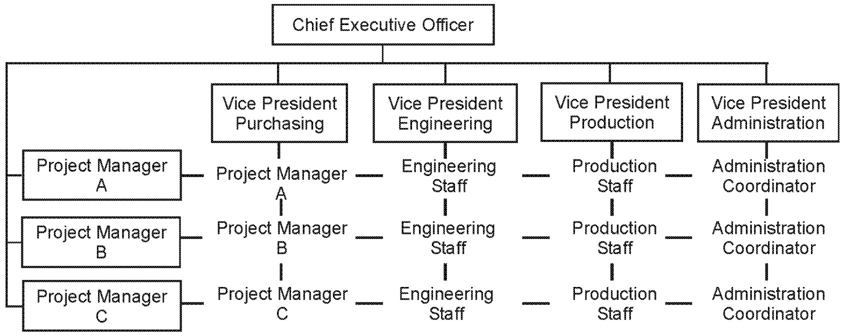


Figure 6 highlights the matrix organization structure. In large firms, increased diversity leads to numerous product and project efforts with major strategic significance. The organizational form that provides and controls skills and resources where and when they are required most is the matrix organization. Essentially, both the functional area and a project/product specialization is achieved. It combines the advantages of a functional organization and product/project specialization. This structure has a built-in conflict resolution system where strategic and operational priorities are negotiated, power is shared and resources are allocated internally on a thorough need basis. This structure increases number of middle managers exercising general management responsibilities that broadens their exposure to organization wide strategic concerns. Therefore, this structure can accommodate a varied and changing project, product/market technology focus and can increase the efficient use of functional specialists who otherwise might be idle.

There are certain associated difficulties in a matrix organizational structure.

- It is easy to design but 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 certain difficulties, some organizations have designed a temporary or flexible overlay structure. Thus, the basic idea of 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 and diverse firms. The following four important observations lead to linking an organizational structure to strategy and culture.

i. All forms of organizational structures are not equally effective in the implementation of a strategy due to many cultural diversifications.

ii. Structures seem to have a life of their own, particularly in large organizations. As a result, the need for immediate and radical changes is not immediately perceived. Even if the need is perceived, lagging performance may be necessary before culturally politicized sensitive structure is changed or organizational power redistributed.

iii. Sheer growth can make restructuring necessary leading to readjustment of all cultural forms to unify and coordinate with the current requirements.

iv. As firms diversify into numerous related or unrelated products and markets, structural and cultural change appears to be essential if the organization has to perform effectively.

CULTURE AND STYLE OF MANAGEMENT

In general, organizational culture is the product of strategic leadership.

The Influence of the Founder: First, organizational culture is created by the strategic leadership provided by an organization's founder and top managers. The organization's founder is particularly important in determining culture because the founder imprints his or her values and style of management on the organization.

Second, the leadership style established by the founder is transmitted to the company's managers, and as the company grows, it typically attracts new managers and employees who share the same values. Moreover, members of the organization typically recruit and select only those who do share their values. Therefore, an organization's culture becomes more and more unique as its members become more similar. The virtue of these shared values and common culture is that it increases integration, improves coordination and bonds a unique style of management among organizational members. For instance, the common cultural language that typically emerges in an organization is because people share the same beliefs and values that facilitate cooperation among managers. Similarly, rules and procedures, and supervision are less important when shared values and norms control behavior and motivate employees. When organizational members internalize the cultural norms and values that bond them to the organization and increase their commitment, they find new ways to help the organization succeed. That is, employees are more likely to commit themselves to organizational goals and work actively to develop new skills and competencies to help them achieve those goals.

CULTURE AND POWER

Power, from the viewpoint of strategic management and specifically organizational culture, is an extent to which individuals or a group is able to persuade, induce or coerce others into following certain courses of actions. It would be highly helpful to know the sources of power to understand and assess the importance of power in relation to culture within strategic management. A clear distinction should be made between the authority and power in assessing the impact of power on culture and in turn strategic management.

Sources of Power: The sources of power can be divided into two broad categories. They are: (i) internal sources and (ii) sources for external stakeholders.

Internal Sources

HIERARCHY

Hierarchical positions in the organizational structure provide formal authority to the managers at higher levels. The managers with more formal authority influence the policy formulation and implementation extensively. Managers should use this power along with other types of power to make their influence efficient.

INFLUENCE/CHARISMA

Influence is an importance source of power. This arises from personal qualities like charisma of the leader. Charisma is the leader's ability to influence others through personal magnetism, enthusiasm and strongly held convictions. Leaders communicate these convictions and their vision for the future through a dramatic, persuasive manner of speaking. Charismatic leaders create an image of competence and success. Their personal magnetism makes them role models for their employees, thus influencing the overall organizational culture. The more the followers admire their leaders, the more likely they are to accept their leader's values and beliefs. This acceptance makes the leaders to exert significant influence over their followers' behaviors. The charismatic leaders are more powerful during the periods of organizational crisis and transition.

CONTROL OF STRATEGIC RESOURCES

Control of strategic resources is an important source of power. The relative importances of different resources change depending upon the strategy and situation. The leader can gain power by possessing or controlling the strategic resources.

EXPERTISE OR KNOWLEDGE OR SKILL

Expertise or knowledge is a crucial source of power for top management. Managers acquire power through achievement and performance. The better the achievement and performance, the greater will be the power of the managers. Expertise refers to a manager's ability to influence the behavior of others. The subordinates follow the managers as they believe that their managers have command and knowledge of the situation. Thus, norms are informally established leading to a definite organizational culture.

CONTROL OF THE ENVIRONMENT

Usually, events internally in the company affect the external view of the company's performance. Some individuals or groups have more influence over events and company's internal environmental factors. This can be a source of power within the company. Normally, marketing and finance managers can control the important internal environmental factors. Therefore, they play a dominant role in cultural settings of strategic management whereas the human resources, production and operations managers take a back seat.

EXERCISING DISCRETION

Exercising discretion is a most significant source of power within an organization. Individuals or groups, due to the nature and levels of their jobs, derive power. Normally, strategy is to be implemented by a number of individuals across the organization. These individuals use the power so derived in the process of strategy implementation, thus, making the organization stand unique in its cultural transition.

Sources for External Stakeholders

RESOURCE DEPENDENCE

Almost all external stakeholders like banks, financial companies, suppliers of raw materials, etc., derive power as the company depends on them for resources. Usually, the short-term survival of a company is mostly dependent on anyone or more of these stakeholders.

INVOLVEMENT IN IMPLEMENTATION

Under the present day circumstances, all over the world, the importance now has been shifted from manufacturing to the distribution. The distribution agencies have the power of knowledge about consumer's tastes and preferences. In fact, distribution agencies determine or influence the type of product to be produced. Thus, the distribution agencies derive power by involving in the implementation process.

EXPERTISE

The agencies having specialized skills or expertise like the advertising agencies that is demanded by the company to perform a specific activity for remuneration derive the power for their expertise knowledge.

INTERNAL LINKS

Internal links can provide a way for external stakeholders to influence the company's strategy. Highly authoritarian organization normally does not provide internal links and give chance to external stakeholders to influence the strategic management process to a minimum.

Methods of Assessing Power

It is rather very difficult to assess power of internal individuals or groups and external stakeholders. However, suggested best way of assessing power is to depend on indicators of power. There are four basic indicators of power within organizations.

THE STATUS OF THE INDIVIDUAL OR GROUPS

The position of an individual in the organizational hierarchy, the job and the grade of work would indicate the assessment of the power. Similarly, the reputation of individual or group compared to others can also be used to assess the power held by them.

THE CLAIM ON RESOURCES

The claim of the individual or group for resources in terms of share in budget, number of employees, finances, etc., can be used to measure the power. Usually, resources of the least powerful group get eroded by more powerful group.

REPRESENTATION IN POWERFUL POSITIONS

The power of the individuals and groups can be assessed by their representation in boards, committees, groups, teams, etc.

SYMBOLS OF POWER

Power of individuals and groups can also be assessed through various symbols like the size and location of offices, facilities like secretary, telephones, carpets, meeting tables, etc.

The indicators to assess the power of external stakeholders are:

i. *The status:* The status of the external stakeholders like suppliers of raw materials, distributors, financial institutions, etc., can be assessed through the timeliness of response and the extent of demands that are met by the company.

ii. *Resource dependence:* Resource dependency can be measured by the proportion of the company's business with a single distributor, proposition of the raw material supplied by a supplier to the total raw materials required by the company, etc.

iii. *Negotiating arrangements:* The power of the external stakeholder can be assessed through whether the stakeholder invited for negotiation is allowed to interact closely or treated at arm's length.

iv. *Symbols:* Symbols are equally valuable clues. The symbols that are used to assess the power of external stakeholders include the level of manager that deals with the stakeholder, whether the management team wine or dine with the stakeholders, etc.

DETERMINANTS OF CULTURE

There are three basic determinants of organizational culture.

First, the influence of the business environment in general and the industry in particular. For instance, companies in industries are characterized by rapid technological change, such as software, electronic and computer companies normally have cultures that strongly value innovation.

Second, founders, leaders and managers bring a pattern of assumptions with them when they join the organization. These assumptions often depend on those individuals' own experiences in the culture of the national, regional, ethnic, religious, occupational and professional communities to which they belong.

Third, the actual experience people in the organization have had in working out solutions for coping with the basic problems the organization encounters molds shared assumptions. For instance, two companies may each value co-operation and internal competition, but one company may emphasize co-operation more in decision-making and resource allocation, while internal competition may predominate in the other. The cultures of these two companies consequently are quite different even though some of their basic assumptions about cooperation and internal competition are the same.

Taken together, these three principle sources suggest that the content of culture derive from a combination of prior assumptions and new learning experiences.

ASPECTS OF CULTURE

Not all cultures produce equally powerful effects. Some cultures are stronger than others.

Strength of Culture: The strength of a culture influences the intensity by which organizational members comply with it as they go about their daily activities. The three specific features of cultures that determine its strength are *thickness, extent of sharing* and *clarity of ordering.*

There are a number of important shared assumptions that vary from one organization to another.

Thick cultures have many shared assumptions whereas *thin* cultures have a few. Moreover, cultures with many layers of important shared beliefs and values have a stronger influence on organizational behavior. Generally, thinner cultures have a weaker influence on organizational life. For instance, many global corporations like IBM, GM, GE, Microsoft have a sense of thick cultures made-up of numerous shared beliefs and values, like respect for the individuals, encouragement of constructive rebellion and doing the right thing at all times. Let us look at the shared assumptions aspect a little deeper than it appears on the surface. Some important assumptions are more widely shared than others are. A few are completely shared in the sense that every member of the organization would have to internalize them. Cultures with more widely shared beliefs and values have a more pervasive impact since more people are guided by them.

One aspect of culture which assumes predominance over the others is that the shared beliefs and values in many organizational cultures are clearly ordered. Their relative importance and their relation to each other are fairly unambiguous. In less ordered cultures, relative priorities and interrelationships are not very clear. The cultures, where there is a clear order of shared assumptions, have a more pronounced effect on organizational behavior because members of the organization are sure of values that should prevail in cases of conflicting interest.

The content of a culture would determine the *direction* of influence of such culture on the organizational behavior. The *intensity* of a culture that affects the behavior depends on a culture's strength.

Strong cultures are also more resistant to change. This represents a major asset or liability depending on the culture's compatibility with the needs of the organization's chosen strategy.

LEVELS OF CULTURE

Organizations show three common value sets or levels of culture.

First, successful companies have cultures promoting a *bias for action.* The emphasis is on autonomy and entrepreneurship. Employees are encouraged to take risks. For instance, to create new products even though there is no assurance that these products will be the winners. In such organizational culture, managers are closely involved in the day-to-day operations of the company and do not simply make strategic decisions isolated in some ivory tower and employees have a "hands-on, value driven approach."

Second, the set of values stems from the *nature of the organization's mission.* The company sticks with what it does best and maintains control over its core activities. Generally, a company can easily get sidetracked into pursuing activities outside the area of its core expertise just because the opportunities seem to promise a quick return. Management cultivates culture to stick to knitting that shows that the company stays with the businesses it knows best. The company also establishes close relationships with customers as a way of improving its competitive position. The customers know about the company's performance since they use the company's products and services. Therefore, at this level, the organizations emphasize customer oriented values, learn customer's needs and improve abilities to develop products and services that the customers desire. For example, Toyota is sure of its mission and takes constant steps to maintain the desired culture as per its mission's requirements.

The third level *denotes operationalizing the organization.* The company establishes an organizational design that motivates each employee to do the best. The belief inherent in this level of culture is that productivity is obtained through people and that the respect for the individual is the primary means by which an organization can create the right atmosphere for productive behavior. For instance, Kodak and P&G pay this kind of attention to their employees. An emphasis on entrepreneurship and respect for the employee leads to the establishment of a structure that gives employees the latitude to make decisions and motivates them to succeed. A simple structure and a lean staff best fit this situation. The organizations are designed with only the number of managers and hierarchical levels that are necessary to get the job done. The organizations at this level of culture are sufficiently decentralized to permit employees' participation but centralized enough for management to make sure that the company pursues its strategic mission.

These three main levels of culture are at the heart of an organization's value system and management transmits and maintains them through strategic leadership. Strategic managers need to establish the values and norms that will help the organization to leap into the future. When the organization accomplishes this strong bonding between the three levels of culture, only those people who fit the values are recruited into the organization and through training they become a part of the organization's culture. Thus, the type of control systems chosen should reinforce and build on one another in a cohesive way. Organizational culture cannot by itself make the structure work. It must be backed by output and behavior controls and matched to a reward system so that all employees cultivate organizational norms and values and pursue organizational goals.

CHANGE OF CULTURE

Few environments are stable for any prolonged period of time. Thus, if an organization is to survive, managers must take actions that enable an organization to adapt to environmental changes. If they do not take such an action, they may find themselves faced with declining demand for their products. Two distinct cultural settings, namely *adaptive cultures* and *inert cultures,* are observed in many organizations. Adaptive cultures are those that are innovative and encourage and reward initiative taking by middle and lower level managers. On the other hand, inert cultures are those that are cautious and conservative, that do not value middle and lower level managers taking such action and indeed may actively discourage such behavior.

Managers in organizations with adaptive cultures are able to introduce changes in the way the organization operates, including changes in its strategy and structure that allow the organization to adapt to changes occurring in the external environment. This phenomenon does not occur at organizations with inert cultures. As a result, organizations with adaptive cultures are more likely to survive in a changing environment and have higher performance than organizations with inert cultures.

When an inert culture exists in an organization, strategic problems can result. For instance, if top managers accept the same set of norms and values, the danger arises that they will be unable to steer the organization in a new strategic direction if the environment change occurs and new competitors or technology demand such a change. Furthermore, having designed their structures, managers became used to the way they operate, and they rarely recognize the important effect structure has on cultural norms and values. Thus, organizational culture can promote inertia. For example, at IBM, managers were unable to see, until it was too late, that the development of powerful personal computers and interactive networking software would have long range implications for IBM's cash cow products like mainframe computers. This blindness resulted from the strong beliefs and values of IBM's culture that mainframes would always be the dominant product by its very design and personal computers would only be additions to mainframes. Moreover, IBM's tall and centralized structure slowed decision-making and encouraged the development of conservative norms and values that made managers averse to risk and reluctant to challenge the status quo position of the organization. Another issue that distorts the decision-making process is the cognitive biases. Over a period of time, the norms and values of an organization's culture can bias decision-making and cause managers to misperceive the reality of the situation facing their company. To prevent these strategic leadership problems, great care needs to be taken in composing the top management team.

CULTURE AND VALUES

Values are basic assumptions about which ideals are desirable or worth striving for. They derive from personal experience and identification with those who have had an important influence on one's personal development since early childhood. Values represent preferences for ultimate end-states, such as striving for success or avoiding debt at all costs.

It is important to note that these definitions do not refer to what people say are their beliefs and values but rather to the beliefs and values they actually hold, whether consciously or otherwise. For instance, an important professional assumption for a banker is client confidentiality. This value is taken for granted, and a banker may become conscious of it only if it is challenged or violated. For example, a client might question the banker about it or a fellow banker might violate it, either of which would draw attention to this important value. Even after drawing attention to it, this value remains present and potent. It is usually hard to change, as are other beliefs and values that the individual actually holds, consciously (openly) or otherwise.

With this classification of culture as assumptions involving personal beliefs and values, the meaning of *shared* in the definition of culture can be made more explicit with the discussion of value systems in organizations.

CULTURAL INFLUENCES ON ORGANIZATIONAL LIFE

Culture is strength as well as a weakness. It is strength since culture eases and economizes communications, facilitates organizational decision-making and control. It may generate higher levels or cooperation and commitment in the organization. The result is efficiency in that these activities are accomplished with a lower expenditure of resources such as time and money that would not be otherwise possible. The stronger the culture, the greater its efficiency.

Culture, on the other hand, becomes a weakness when important shared beliefs and values interfere with the needs of the business, its strategy, and the people working on the company's behalf. To the extent that the content of a company's culture leads its people to think and act in inappropriate ways, culture's efficiency will not help achieve effective results. This condition is usually a significant weakness because it is hard to change a culture's content.

The five basic processes that lie at the heart of any organization are cooperation, decision-making, control, communication and commitment.

Cooperation

True cooperation cannot ultimately be legislated. Managements can resort to carefully worded employment contracts, spell out detailed expectations, and devise clever incentive schemes to reward first the right behavior.

However, even well thought out formal procedures can never anticipate all contingencies. When something unforeseen occurs, the organization is at the mercy of the employee's willingness to act in the spirit of cooperation, which involves intent, goodwill, and mutual trust. The degree of true cooperation is influenced by the shared assumptions in this area usually, shared beliefs and values of informality and family spirit generates high levels of true cooperation within organizations.

Decision-making

Shared beliefs and values give organizational members a consistent set of basic assumptions and preferences. This leads to a more efficient decision-making process since fewer disagreements arise over which premises should prevail.

However, efficiency does not imply effectiveness. If the shared beliefs and values are not in keeping with the needs of the business, its strategy, and its members, dysfunctional consequences will be a result. For instance, the reliance on the people at the top management in crisis situation to guide in case of problems would be efficient but no longer effective in a complex, multiplant environment that the top managements face in today's complex business situations. These assumptions had to change for better.

Control

The essence of control is the ability to take action to achieve planned results. The basis for action is provided by two different control mechanisms – formal procedures and clans.

Formal procedures rely on adjusting rules, procedures, guidelines, budgets and directives. The clan mechanism relies on shared beliefs and values. In effect, shared beliefs and values constitute an organizational "compass" that members rely on to choose appropriate courses of action. Clan control derives itself from cultural settings. A strong culture facilitates the control process by enhancing the clan control. Clan control is highly efficient in selective environments. But again, efficiency and effectiveness should not be confused.

Communication

The major reasons people miscommunicate daily in organizational and every day life include the technical problem of distortion between the point where a communication starts out and the point where it is received. A second and more important hurdle in communication concerns difficulties in interpretation. No two people will interpret a statement the same way.

More complex are the communication problems of one organization member trying to communicate with someone located in a different unit or of the corporate senior executive trying to communicate with the entire work force.

Culture reduces these dangers of miscommunication in two ways. First, there is no need to communicate in matters for which shared assumptions already exist. Certain things go without saying. Second, shared assumptions provide guidelines and cues to help interpret messages that are received. Thus, a strong culture encourages efficient and effective communication. The advantage of this efficiency and effectiveness should not be underestimated – since communications are the lifeblood of organizations.

Culture's content affects the content of communication. Some organization's cultures value open communication. These cultures believe in "Bad news is bad, but withholding it is worse." Other cultures do not value open communication. In these cultures, withholding relevant information that has not been specifically requested, secrecy and outright distortion may prevail.

Commitment

A person feels committed to an organization when he or she identifies with it and experiences some emotional attachment to it. A variety of incentives – salary, prestige, personal sense of worth – tie the individual to the organization. Strong cultures foster strong identification and feelings through multiple beliefs and values that the individual can share with others.

In making decisions and taking actions, committed employees automatically evaluate the impact of alternatives on the organization. Committed people will put out the extra effort needed to get the organization out of a bind. For instance, shared values of highly responsive customer service lead the people to "move mountains" to meet intermittent and unexpected surges in the product demand, without being given special incentives to do so, people are thoroughly rigoured into the values of high quality customer service and expediting behavior that these had to become more than strategic or operational directions. That is to say that they were thoroughly internalized into the personal beliefs and value systems of individuals.

Culture has a pervasive influence on organizational life. But people working in an organization do not ordinarily recognize this because the basic assumptions and preferences guiding thought and action tend to operate at a preconscious level and remain outside their realm of awareness. Some of cultures, manifestations – the shared words, actions, doing and feelings – may be apparent, but the underlying beliefs and values are frequently unstated and not always obvious. Their subtle quality is easily taken for granted.

SUMMARY

- The strength of culture determines its efficiency. However, the content of culture determines its effectiveness because content determines the direction in which culture influences organizational behavior.
- If the content of the culture guides organizational thinking and action in ways that are out of keeping with the needs of the business and its strategy culture becomes ineffective and sometimes dysfunctional regardless of its efficiency.

Chapter VII

Mergers, Acquisitions and Joint Ventures

After reading this chapter, you will be conversant with:

- Rationale for Mergers and Acquisitions
- Mergers and Industry Life Cycle
- Reasons for International Mergers and Acquisitions
- Joint Ventures in Business Strategy
- Rationale for Joint Ventures
- Reasons for Failure of Joint Ventures

Introduction

Mergers can be defined as the integration of two or more firms on co-equal basis. In mergers, firms pool all their resources together to create a sustainable advantage. An acquisition refers to the process of gaining partial or complete control of one company by another for some strategic reasons. Unlike mergers, acquisitions can sometimes be unfriendly, i.e., when a firm tries to takeover another by adopting hostile measures which may not be in the interest of the acquired firm. Mergers and Acquisitions (M&As) have become a popular strategy in the last two decades. Some strategic thinkers feel that M&As have played a crucial role in the restructuring of the US companies during 1980s and 1990s.

RATIONALE FOR MERGERS AND ACQUISITIONS

Increased Market Power

The primary reason for firms going in for Mergers and Acquisitions (M&As) is their desire to increase their market power. A firm gains market power, when it is able to sell its goods or services at a price lower than its competitors or the cost of producing the product or service is much less as compared to its competitors. A firm may have core competencies but may lack the required resources and size to compete in the market. Thus, most M&As which take place with the intention of increasing market power target competitors, suppliers, distributors, or businesses in related industries. In order to expand the size of the firm, firms go for horizontal, vertical and conglomerate mergers. In the following paragraphs, we will discuss the different types of mergers.

Horizontal Mergers

If two firms are operating and competing in the same business activity merge, it is known as a horizontal merger. Combining two business entities, results in a larger firm and thus, greater economies of scale. But, it is not the only reason for the popularity of horizontal mergers. Though horizontal mergers benefit from large-scale operations, not all firms merge horizontally to achieve economies of scale. Firms may merge horizontally to share resources and skills and to derive synergy. Governments make efforts to regulate horizontal mergers as they can minimize competition. By decreasing the number of firms in an industry, a horizontal merger may create a monopoly market and the consumer suffers.

Vertical Mergers

When two firms in the same industry but in different stages of the value chain, merge, it is called a vertical merger. There are different reasons for companies entering into vertical mergers. They are: reducing costs of communication, coordinating production, better planning for inventory and production.

Conglomerate Mergers

When two firms from unrelated business activities merge, it is known as a conglomerate merger. Conglomerate mergers can be categorized into three different types: (i) product extension merger, (ii) geographic extension merger, and (iii) pure conglomerate merger. When two firms in a related business activity merge, it is called a product extension merger. It helps to broaden the product line of firms. When two firms operating in non-overlapping geographic areas merge it is known as geographic extension merger. When two firms from unrelated business activities merge, it is known as a pure conglomerate merger. Apart from increasing the market power there are many other reasons that have contributed in the increase of M&A activity, some of which are discussed below:

Overcoming Entry Barriers

When firms try to enter new markets they often face many problems, some of which may act as barriers to its entry. Well established firms in a market may sell their products and services in large volumes thereby gaining economies of scale. Economies of scale become a barrier to entry. Another barrier that a new entrant in the market faces is product loyalty. Creating enduring relationships with customers leads to product loyalty which may be difficult to overcome by a new entrant. Moreover, a new entrant has to spend huge amounts on advertising. The cost of advertising increases further when a new entrant in the market prefers differentiating its products from its competitors. Thus economies of scale, product loyalty and high advertising expenses act as barriers for a firm trying to enter a new market. The greater the barriers to entry, the more the likelihood that firms will take to M&As to overcome these barriers.

Cost of New Product Development

Developing new products and launching them successfully in the market requires commitment of the firm's resources and the return on investment may take a long time. Moreover, the market acceptance of the new product is also unpredictable. According to a research 88 percent of the new products fail to achieve expected results. And 60 percent of innovative products are copied within four years of being patented.

Firms prefer M&As to avoid the internal costs of developing new products. Moreover, M&As also reduce the risks associated with the launch of a new product, as the product is already tested in the market. If a company acquires a company that already has an established product in the market the acquiring company can enter the market more quickly.

Pharmaceutical companies use M&As to gain a quick entry into the market and overcome the high costs of product development. As patents on many key drugs expire after a certain period, firms which do not have a strong R&D center are likely to be left behind. Thus, M&As seem to be the preferred option for such companies.

Increased Speed to Market

M&As lead to faster market entry when compared to the time taken for new product development. Research has shown that M&As are the quickest route to new markets and new capabilities. The new capabilities can be used to introduce new products and enter markets and this can create an advantageous market position. However, how long the advantage may last depends upon the rivals' competitive responses.

Lower Risk Compared to Developing New Products

Developing a new product involves a lot of risk. Managers view M&As as risk-free method of getting entry into new markets. But one major drawback associated with increasing M&As activities is that they prevent investments in new product development. Research shows that M&As have become a means to avoid risky internal ventures. Many firms would not like to incur heavy expenses in developing new products, as acquisitions often seem to provide an economically more viable option.

Increased Diversification

Firms find it easy to develop and introduce new products in markets, in which they have some experience. On the contrary, if a firm launches a product that has no relation to its existing portfolio of the products, there are lower chances of its success. Thus, in order to diversify, firms would prefer M&A route. M&As can be used for both related as well as unrelated diversification. M&As are more common when firms want to diversify on a global level.

Before undertaking any M&A activity to diversify its product lines, a firm needs to study and evaluate the fit between the acquiring and the acquired firm. If the acquired firm and the acquiring firm are similar, there are greater chances of the acquisition being successful. Many multinational companies engaged in the production of household appliances used M&A excessively to diversify their product portfolio in India.

Reshaping the Firm's Competitive Scope

The intensity of competition affects the profitability of a firm. To reduce the negative effect of competition, and reduce their dependence on a single or a few products, firms acquire other firms. If a firm is dependent on a single product for all its revenues and profits, the competitive scope of the company is likely to be reduced. To avoid dependence on a single product, many firms venture into new industries through acquisitions.

MERGERS AND INDUSTRY LIFE CYCLE

There is a close link between the various stages in the industry life cycle and the level of M&A activity. All the four stages, i.e., introduction, exploitation, maturity and decline, have distinct role to play in M&A process. In the initial and growth stages of the industry life cycle, new or small firms are the targets for related or conglomerate mergers. The process of mergers is initiated by larger firms in mature or declining industries. The larger firms provide managerial and financial efficiencies through mergers. Horizontal mergers between smaller firms take place to acquire managerial and financial resources. The purpose behind horizontal and related mergers in the maturity stage is to match the low cost and price performance of other firms, both domestic and foreign by achieving economies of scale in research, marketing and production. Table 1 relates the various stages of industry cycle with the type of merger.

Table 1: Mergers and Industry Life Cycle

Stage of Industry Life Cycle	Type of Merger
Introduction Stage	Newly created firms may sell to outside larger firms in a mature or declining industry, thereby enabling larger firms to enter a new growth industry. These result in related or conglomerate mergers. The smaller firms may wish to sell because they want to convert personal income to capital gain and because they do not want to place large investments in the hands of managers that do not have a long record of success. Horizontal mergers between smaller firms may also occur, enabling such firms to pool management and capital resources.
Exploitation Stage	Mergers during the exploitation stage are similar to mergers during the introductory stage. The impetus for such mergers is reinforced by the more visible indications of prospective growth and profit and by the large capital requirements of a higher growth rate.
Maturity Stage	Mergers are undertaken to achieve economies of scale in research, production, and marketing in order to match the low cost and price performance of other firms, domestic or foreign. Some acquisition of smaller firms by larger firms takes place for the purposes of rounding out the management skills of the smaller firms and providing them with a broader financial base.
Decline Stage	Horizontal mergers are undertaken to ensure survival. Vertical mergers are carried out to increase efficiency and profit margins. Concentric mergers involving firms in related industries provide opportunities for synergy and carry-over. Conglomerate acquisitions of firms in growth industries are undertaken to utilize the accumulating cash position of mature firms in declining industries whose internal flow of funds exceeds the investment requirements of their traditional lines of business.

Source: Mergers, Restructuring and Corporate Control – Weston, Chung and Hoag.

Horizontal and related mergers may take place in the maturity stage to match the low cost and price performance of other firms (domestic or foreign) by achieving economies of scale in research, marketing and production. Some horizontal acquisitions may take place to provide management skills and a broader financial base.

In the decline stage, horizontal mergers take place to ensure survival, vertical mergers to increase efficiency and profit margins, concentric acquisitions to obtain opportunities for synergy and carry-over of managerial capabilities, and conglomerate acquisitions may be undertaken to utilize financial slack of mature firms in declining industries.

REASONS FOR INTERNATIONAL MERGERS AND ACQUISITIONS

There are various reasons for the growth of cross border mergers and acquisitions. Some of these reasons are growth, technology, government policy, differential labor costs, productivity, and source of raw materials.

Growth

Growth is one of the primary motivating factors for cross border M&As. M&As provide an opportunity for firms to grow fast. A firm making profits in an ailing economy would not like to make additional investments in the same country. It makes perfect business sense for the firm to invest in an economy which promises faster growth. Firms which have operations in one particular country may not have a cost advantage because of limited sales. If the operations are expanded to other countries, due to the economies of scale the firm can gain cost advantage.

TECHNOLOGY

A technologically superior firm may go in for M&As to exploit its technological advantage. On the other hand, a firm which lacks technological advantage may go for M&As to gain access to superior technology. By using advanced technology of the acquired firm, the acquirer can improve its competitive position and profitability both at home and abroad.

GOVERNMENT POLICY

Government policies and regulations relating to tariffs, quotas, can have a major impact on M&As. If a country imposes tariffs and quotas to protect its domestic industry, exports will suffer. The threat of such restrictions encourages cross border M&As. Environmental and other regulations can increase the time and cost required to build facilities abroad for entry. Thus, acquiring a company with facilities in place makes good business sense.

DIFFERENTIAL LABOR COSTS, PRODUCTIVITY

Labor costs comprise a significant portion of the cost of production. Many multinational companies go in for M&As to take advantage of the availability of cheap labor. It is because of this reason many multinational companies are heading towards developing countries like India and China to set-up their manufacturing bases. Higher productivity of labor also influences cross border M&As.

SOURCE OF RAW MATERIALS

This factor plays an important role in the growth of vertical mergers, more so for acquiring firms from resource-poor domestic economies. This approach may not be feasible in the case of strategic raw materials as many countries have restrictions on foreign ownership of such assets.

DIVESTURES

A divestiture is the sale of a part or a division of a company to a third party. The division may include assets, product lines, or subsidiaries. These are sold for cash or securities or a combination of both. There are various reasons for the growth of divestitures. Companies often claim that they divest businesses to raise working capital or to pay back the debts of the organization. This claim is questionable since financing needs can be fulfilled by methods other than divestiture. A study done by Linn and Rozeff in 1984, revealed two main reasons for divestitures:

i. The assets are worth more as part of the buyer's organization than as part of the seller's.

ii. The assets are actively interfering with other profitable operations of the seller.

The need to get rid of a loss making subsidiary is often cited as a reason for divestiture. However, divestiture will not yield any gains, unless the subsidiary is sold for more than its present value. In some cases, it is advisable to sell a subsidiary even if the sale fails to generate more than its present value. For example, subsidiaries that hinder the efficient functioning of other units should be sold even if the sale does not lead to any monetary gain.

Reasons Forcing Companies to Divest

EFFICIENCY GAINS AND REFOCUS

While M&As lead to synergy, divestures can result in reverse synergy. A particular business may be more valuable to someone for generating cash flows and that someone will be paying a higher price for the business than its present value. Divestiture is also used to enable a company to make certain strategic changes.

The competitive advantage that a company has, may change over time due to changing market conditions, and as a result, a company may have to divest a particular business. In some cases, the past diversification programs of a company may have lost value, making it necessary for a company to refocus its core competencies. A divestiture helps in bringing back a company onto its core competencies.

INFORMATION EFFECTS

The information that a divestiture conveys to investors is another reason for divestiture. If the information given by management is unknown to investors, the announcement of divestiture can be seen as a change in investment strategy or in operating efficiency. This may be taken in a positive sense and boost share price. However, if the divestiture announcement is perceived as the firm's attempt to dispose off a marketable subsidiary to deal with adversities in other businesses. it will send a wrong signal to investors. Whether the divestiture is seen as a good or bad signal depends on the circumstances.

WEALTH TRANSFERS

Divestiture results in the transfer of wealth from debt holders to stock holders. This transfer takes place when a company divests a particular division and distributes the resulting proceeds of the sale among stockholders. As a result of this transaction there is less likelihood of repayment of debt and it will have lesser value. If the total value of the firm remains unchanged, its equity value is expected to rise.

TAX REASONS

As in the case of mergers, divestitures also provide a considerable tax advantage. When a company is losing money and is unable to use a tax-loss carry forward, it is better to divest wholly or in part to realize a tax benefit. When there is increased leverage due to restructuring, a firm can have a tax shield advantage due to interest payments being tax deductible.

JOINT VENTURES

Joint ventures, as a strategy, are more complex and more formal than all other arrangements, such as licensing arrangement, etc. Joint ventures involve the creation of a third entity, representing the interests and capital of the partners involved. In a joint venture, both the partners contribute their own proportional amounts of capital, distinctive skills, managers, reporting systems, and technologies to the venture. The emphasis is on collaboration rather than mere exchange. While exchange simply involves obtaining something back for what you have put in, collaboration involves creation of new value.

A joint venture leads to the creation of a separate business enterprise. This, however, does not imply that the participants to the joint venture cease to exist. Joint venture participants continue to exist as separate firms. A joint venture may take the form of a partnership, a corporation, or any other form of business organization the participating firms might choose to select.

The following characteristics are taken into account while describing joint ventures:

i. Contribution of money, property, effort, knowledge, skill or other asset to a common undertaking, by the partners involved.
ii. Joint property interest in the subject matter of the venture.
iii. Right of mutual control or management of the enterprise.
iv. Expectation of profit, or presence of "adventure".
v. Right to share in the profit.
vi. Usual limitation of the objective to a single undertaking or ad hoc enterprise.

The scope and duration of joint ventures is, therefore, limited. Joint ventures involve only a small fraction of each participant's total activities. Each participant must contribute or offer something unique and of importance to the venture and, at the same time, provide a source of gain to the other participants to the venture.

FINANCIAL DEFENSIVE MEASURES

The factors that make a firm a desirable candidate for acquisition and vulnerable to a takeover include:

- A low stock price compared to asset replacement cost or their potential earning power.
- A highly liquid balance sheet with large amounts of excess cash, a valuable securities portfolio and a significantly unused debt capacity.
- Good cash flow relative to current stock prices.
- Subsidiaries or properties that can be sold off without significantly improving the cash flow.
- Relatively small stock holdings under the control of incumbent management.

These factors, in combination serve to simultaneously make a firm an attractive investment opportunity as well as facilitate its financing. The firm's assets provide collateral security for an acquirer's borrowings and the target's cash flows from operations and divestitures facilitates repayment of loans.

Financial defensive measures may include – adjustments in asset and ownership structure; leveraged recapitalizations; golden parachutes; and poison puts.

Adjustments in Asset and Ownership Structure

Adjustments in asset and ownership structure may either be brought about by acquisitions and divestitures of assets or through issuance and repurchases of voting securities. Acquisitions and divestitures of assets may involve sale to a third party of assets in the bidder's line of business, cash purchases or sale of assets unrelated to the bidder's line of business, etc. Issuance and repurchases of voting securities may involve repurchases from current public shareholders, issuance to dispersed group other than current holders, etc.

Leveraged Recapitalizations

Also known as recap, leveraged recapitalization is a relatively new technique of financial restructuring and was first developed by Goldman Sachs for Multimedia in 1985. A large one-time cash dividend is given to outside shareholders and insiders (managers) and employees are given new shares instead of a cash dividend in a typical recapitalization. Newly borrowed funds help finance the cash dividend. The firm's leverage is thus raised to an "abnormally" high level and this helps to discourage takeover attempts.

Golden Parachutes

These refer to separation of provisions of an employment contract that compensate managers for loss of jobs as a result of change of control. These provisions call for either a one-time payment or a payment spread over a specified period, at full or partial rates of normal compensation. Many companies adopt golden parachute features in their employment contracts for top managers. Golden parachutes are viewed as tools to reduce the conflict of interest between shareholders and managers in change of control situations.

Poison Puts

In this strategy, the target company issues bonds, which encourage holders to cash in at a high price. As a result of the cash drainage, the target becomes unattractive.

ANTI-TAKEOVER AMENDMENTS

Anti-takeover amendments are amendments to the firm's corporate charter, which are intended to make it more difficult for an unwanted acquirer to take over the firm. These are popularly called shark repellents. As is the case for all charter amendments, anti-takeover amendments must be voted on and approved by shareholders. There are various types of anti-takeover amendments:

Super Majority Amendments

Under such amendments, shareholder approval by at least a two-thirds vote and sometimes even 90 percent of the voting power of outstanding capital stock is required for change of control. In many cases, a board-out clause is introduced, which empowers the board to determine when and if the supermajority provisions will be in effect. The management's flexibility in takeover negotiations gets limited as a result of pure supermajority provisions.

Fair Price Amendments

The corporate charter may be amended to require supermajority provisions with a board-out clause and an additional clause, which waives the requirement of supermajority if a fair price is paid for all tile shares purchased. Fair price is defined as the highest price paid by the bidder during a specified period, and is sometimes required to exceed the book value of the target, or an amount determined relative to accounting earnings.

Classified Boards

Staggered or classified, boards of directors are another major type of anti-takeover initiative. The rationale behind proposing a staggered board or classified board is to ensure continuity of policy and experience. For example, if a board has nine members, it will be divided into three classes with only three members standing for election for a three-year term each year. A new shareholder would have to wait at least two annual general meetings to gain control of the board of directors.

Authorization of Preferred Stock

Boards of Directors have the discretion to create a new class of securities with special voting rights. In a control contest, these securities are offered to friendly parties. Though this method has been traditionally used as a tool to give the board of directors flexibility in financing under dynamic economic conditions. it is basically a defensive measure against hostile takeover bids.

POISON PILL DEFENSE

Poison pill defense is a popular but controversial defense mechanism against hostile takeover bids. The process involves creation of securities known as poison pills. These securities provide their holders with special rights to be exercised only some days after a takeover attempt. The takeover attempt could be either a tender offer for control or accumulation of a specified percentage of target shares. The exercise of the rights makes the takeover more difficult and / or costly for an acquirer.

Usually, shareholders' approval is not sought for adoption of poison pills by the board of directors. The rights provided by a poison pill plan can be quickly altered by the board or redeemed by the firm any time before their exercise, following the occurrence of the triggering event.

TARGETED SHARE REPURCHASE AND STANDSTILL AGREEMENTS

Targeted repurchase, also known as greenmail, is a process in which a target firm indulges in private negotiations and repurchases a large block of its stock from an individual shareholder or a subset of shareholders at a premium. The purpose of premium buy-back is to put an end to the threat of a hostile takeover by the large block holder or greenmailer. As greenmail is a type of blackmail, both the payers and buyers of greenmail are not seen with respect. According to opponents of greenmail, greenmailers are responsible for causing damage to shareholders. According to them, the large block investors are corporate "raiders" who snatch corporate assets, causing harm to other shareholders.

A standstill agreement is a voluntary contract in which the stockholder who is bought out, agrees to abstain from making further investments in the target company for a specified time period. If the standstill agreement is made without a repurchase, the large block holder agrees to refrain from increasing his or her ownership, as this may give him a controlling position in the company.

STRATEGIC REACTIONS BY TARGETS

Some of the preliminary takeover defenses, especially the poison pill defense, can also be erected after the fact. Target firms, however, are at a disadvantage with respect to timing, once an offer is on the table. There is ample time available to the raider to investigate potential targets, arrange for financing, and choose the moment when the market conditions are optimal for attack. In contrast, there are only 20 days available to the target firm in which to respond. The Securities and Exchange Commission (SEC) sets the 20 days time as the time period during which a tender offer remains open.

The target firms can succeed in gaining a little more time by making use of a relatively new service, called "shark watching", being offered by proxy solicitation firms for a fee. These firms claim to be able to detect and identify early accumulations of stock. As per SEC regulations, it is not necessary for buyers to reveal their identity until they have already acquired 5 percent of a firm's stock. Hence, early warning provided by the proxy solicitation firms obviously gives the target more time to tailor a defense against the particular purchaser to look for a more acceptable merger partner (a white knight), and so on. If it is evident that the individual or group buying the stock is not really a serious acquirer but only interested in repurchase of his / her stock at a premium, early detection can reduce the amount of greenmail required to be paid in order to eliminate the threat.

Almost always, the first response of the target is to maintain that the initial bid of the acquirer is woefully inadequate. Another early response could be accusing the would be acquirer of SEC violations or filing an antitrust or other lawsuit against the bidder. The judicial process involved can surely provide breathing room, irrespective of whether or not merit exists in the litigation. Once some time has been gained, the target firm can pursue other avenues, such as making an acquisition (thereby creating an anti-trust incompatibility with the bidder's operations), or acquiring a firm in a regulated industry (with the primary aim of subjecting the entire takeover transaction to closer government scrutiny). However, responses to threats, in many cases, are directed more towards delaying the ultimate takeover, with the goal of driving up the price, rather than defeating the purpose altogether.

JOINT VENTURES IN BUSINESS STRATEGY

More recently, joint ventures are being referred to as "strategic alliances". Joint ventures are stimulated by a number of motives as described below:

i. The primary motive for starting a joint venture is to share investment expenses or enable a large company rich in cash that it can invest to collaborate with a smaller company having a product or production idea but lacking in funds to pursue the opportunity. However, it has been observed that finance is usually forthcoming if the product idea is a good one. It is only when the outcome is highly uncertain (high risks involved) and payoff is not likely to ensure till several years into the future, that financing is likely to become a problem. Even though outside investors may be reluctant to finance the project even on an equity basis because of the high risks involved, a business firm may be interested because it possesses more information on the project or has other projects that may benefit from the learning experience that may be gained from the joint venture.

ii. The learning experience that may be obtained is the second strong motive for joint ventures.

iii. A joint venture serves as a method for reducing the investment outlay and sharing the risks, even for a large company. This is, of course, in addition to the learning experience that may be achieved.

iv. As reported in the *Los Angeles Times* in 1984, anti-trust authorities may be more willing to permit joint ventures rather than mergers. This is because joint ventures result in an increase in the number of firms while mergers lead to a decrease in the number of firms. In a joint venture, parent firms continue their operations even after a new firm is created. The likelihood of receiving endorsement from government agencies is particularly more in case of joint ventures in research and development areas.

Further, joint ventures may be used to acquire complementary or technological resources at lesser cost, or to derive benefits from economies of scale, critical mass, and learning experience, all of which are elements of strategic alliances.

Joint ventures may also be used as an element for long-range strategic planning by firms. Similar to a spider's web, a small firm in a highly concentrated industry acquires countervailing power among rivals in a product market and among rivals for a scarce resource by entering into joint ventures with several of the industry's dominant firms, thus forming around itself a self-protective network of counterbalancing forces. This strategy is feasible only when the small firm has something unique to offer the industry leaders.

RATIONALE FOR JOINT VENTURES

The basic motive for starting a joint venture is sharing investment. A company with adequate cash may enter into collaboration with a smaller company which has technical expertise but lacks funds. If a company has a good product idea then finance will not be a constraint. However, if the project involves high risk and the returns are expected only after a considerable period of time, securing funds becomes a problem for the company. While other investors may show reluctance to invest in the project even on an equity basis because of high risks involved, another business firm may be interested in the same. This could be because firm wants to utilize the knowledge it has on the project and or because it wants to gain some knowledge on the subject and utilize it for other projects as well. Thus, learning is the second biggest motive for joint ventures.

According to Berg, Duncan, and Friedman (1982), 50% of all joint ventures take place for the purpose of knowledge acquisition. The contractual relationship between the joint venture partners is determined on the basis of the complexity of knowledge to be transferred. When a complex and complicated set of knowledge has to be transferred, the most effective and appropriate means of transfer is Learning-by-doing and Teaching-by-doing (L/BD), as it is difficult to impart classroom training in such a situation. Simulation of the atmosphere (operations, machines. work group) may be essential to enable proper knowledge transfer. To achieve efficiency in the process being taught, successive adaptations to changing internal and external events also become necessary. Hence, job incumbents, however skilled, may be unable to describe job skills to trainees except in an operational context. L/TBD is therefore, the most appropriate vehicle for knowledge transfer, more so in joint ventures.

Companies can also enter into joint ventures to reduce the investment outlay and share risk. Another reason for the increasing number of joint ventures is to gain endorsement from government authorities. The possibility of joint ventures getting approval from anti-trust authorities is greater than mergers. This is primarily because joint ventures help in the creation of more firms (as compared to mergers) and reduce the chances of business being monopolized. Companies also enter into joint ventures to acquire complementary technological or management resources at lower cost, or to derive benefits from economies of scale, critical mass and learning experience.

Another rationale for joint ventures is to gain tax advantages. If an organization contributes a patent or licensable technology to a joint venture; the tax consequences may be less than on royalties earned through a licensing arrangement. If the joint venture is in the form of a corporation, only the assets of the corporation are at risk; the partners risk is limited only to the extent of their investment. The risk factor is more crucial in the industries where the risk of worker, product or environmental liability is very high. The use of joint ventures in many circumstances may be favored due to a number of other more technical tax advantages such as limitation on operating loss carry-over, benefits of multiple surtax exemptions, etc.

There are many other reasons for the growth of the joint ventures. These can be summarized as follows:

- To augment financial and technical ability to enter a particular line of business.
- To share technological knowledge and management skills
- To diversify the risk involved in the project
- To obtain distribution channels or raw materials supply
- To gain economies of scale
- To extend business by sharing investments
- To take advantage of tax treatment or political incentives.

REASONS FOR FAILURE OF JOINT VENTURES

Joint ventures, like any other long-term contracts are prone to difficulties. According to independent studies conducted by McKinsey & Co., and Coopers & Lybrand, 70 percent of joint ventures are either disbanded or fall short of expectations. Other studies suggest that on an average, joint ventures do not even last as long as one half the term of years stated in the joint venture agreement. Some of the reasons for the failure of joint ventures are:

- The contract may be too inflexible to permit required adjustments in the future.
- Lack of commitment and time in implementing the project.

- Inability or failure to develop the desired technology.
- Lack of adequate pre-planning for the joint ventures.
- Failure to reach an agreement on alternative approaches to achieve the basic objectives of the joint venture.
- Refusal by managers possessing expertise in one company to share knowledge with their counterparts in the joint venture.
- Inability of parent companies to share control or compromise on difficult issues.
- Critical issues of public policy and long-term strategies of individual business firms may arise in certain joint ventures.

SUMMARY

- The integration of two or more firms on co-equal basis is known as merger. The first and the foremost reason for M&As is the firms' desire to increase market power. In order to expand the size of the firm, firms go in for horizontal, vertical and conglomerate mergers. If two firms operating and competing in the same business activity merge, it is known as horizontal merger. When firms in the same industry but in different stages of the value chain merge, it is called a vertical merger. When two firms from unrelated types of business activities merge, it is known as conglomerate merger. Conglomerate mergers can be categorized into three different types: (i) product extension merger, (i) geographic extension merger and (iii) pure conglomerate merger.
- Other reasons for increasing use of M&A are overcoming entry barriers, high cost of new product development, increased speed to the market, lower risk involved in M&As compared to new product development, diversification to other activities, and reshaping the firms' competitive scope. Various stages of industry life cycle, i.e., introduction, exploitation, maturity, and decline also influence the different types of mergers. The reasons for cross border mergers and acquisition are growth, technology, product advantages and assured supply of raw material.
- Divestures are undertaken for two reasons: the assets are worth more as part of the buyer's organization than as part of the seller's; or the assets are actively interfering with other profitable operations of the seller. The reasons for the divestures are efficiency gains and refocus, information effects, wealth transfer and tax reasons.
- A combined undertaking or partnership by two or more persons to create a single business enterprise or profit is known as joint venture. The reasons for failure of joint ventures include – inflexibility of the contract, inadequate pre-planning, critical issues of public policy, and long-term strategies, etc., which create difficulties in successful operation of joint ventures causing them to break-up soon after initiation.

Chapter VIII

Analysis of Choice

After reading this chapter, you will be conversant with:

- Criteria for Evaluating Strategic Alternatives
- Strategic Analysis at Corporate Level
- Strategic Analysis at Business Unit Level
- Behavioral Considerations Affecting Strategic Choice
- Contingency Approach to Strategic Choice

Introduction

The search for alternative strategies is incremental and creative. The search begins by developing alternatives and then analyzing and selecting the most appropriate strategy from the alternatives developed. These strategies are usually incremental alternatives developed. The search for multiple alternatives depends on a systematic comparison of strengths, weaknesses, risks and trade-offs of each alternative. When evaluating alternatives, the focus is the future. The process of analysis is concerned with understanding what the future holds and how the company can sustain and grow. All types of strategies have to be analyzed in the process; the probable hurdles of strategy implementation also have to be identified. The firm's attitude towards risk plays an important role in the analysis and selection of a strategy.

In this chapter, the techniques used to aid strategic choice at the corporate and business level will be explored. We begin the chapter by discussing the criteria for evaluating strategic alternatives and the process of strategic analysis at the corporate level.

CRITERIA FOR EVALUATING STRATEGIC ALTERNATIVES

For evaluating strategic alternatives, a number of criteria are available. In order to make the evaluation practically possible, all the criteria can be classified into three groups, i.e., criteria of suitability, feasibility and acceptability.

Criteria of Suitability

The criteria for suitability attempts to measure the extent to which the proposed strategies fit the situation identified in the strategic analysis. The strategy to be selected should meet the following criteria:

- Can the strategy overcome the difficulties identified in the strategic analysis?
- To what extent can the strategy exploit the environmental opportunities by using the company's strengths?
- Do the company's objectives and values fit in with the strategy?

Criteria of Feasibility

The criteria of feasibility assess the practical implementation and working of strategy. In the evaluation stage, the following questions need to be assessed:

i. Does the company have sufficient financial resources to implement the strategy?
ii. Is the company capable of performing at the required level?
iii. Can the necessary market position be achieved?
iv. Is the company capable of coping with competition effectively?
v. Will the technology be available to compete effectively?
vi. Can the company ensure that the required managerial and operative skills will be available?
vii. Is the company capable of procuring the necessary materials and services?

Criteria of Acceptability

The acceptability of the strategy is the third measurement. Acceptability involves not only the consequences of the strategy, but also the personal considerations (for example, values) of the strategy decision maker, as he has to accept it. An analysis of the following factors will help in identifying the consequences of the strategy after its implementation:

- The financial position of the firm in terms of profitability.
- Financial problems like liquidity (how it will be solved?).
- Effect of capital structure.
- The level of acceptability of cultural changes within the organization.
- The nature of change in the company with outside stakeholders.
- The acceptability of the strategy by the company's environment (like the local community).
- The proposed strategy's fit with the existing system (or will the existing system require changes?)

STRATEGIC ANALYSIS AT THE CORPORATE LEVEL

In diversified, multi-industry companies, the fundamental method of corporate strategic analysis is the "business portfolio approach". For example, General Electric has many Strategic Business Units (SBUs) and the company has to decide how this portfolio of business should be managed to achieve corporate objectives. A corporate strategy is sought that sets the basic strategic thrust for each business unit in a manner consistent with the resource capabilities of the firm.

The matching stage of the analytical framework for strategy formulation is also called corporate portfolio analysis. This strategy has to be adaptable to multi-product market firms in which each product/market is managed as a separate business or profit center because the firm is not dominated by one product/market. Moreover, each business is a separate entity and a contributor to the corporation's total portfolio of business. In such companies, the corporate strategic considerations are not separate and distinct from business-level considerations. The portfolio approach provides a simple way of identifying and evaluating alternative strategies for the generation and allocation of corporate resources.

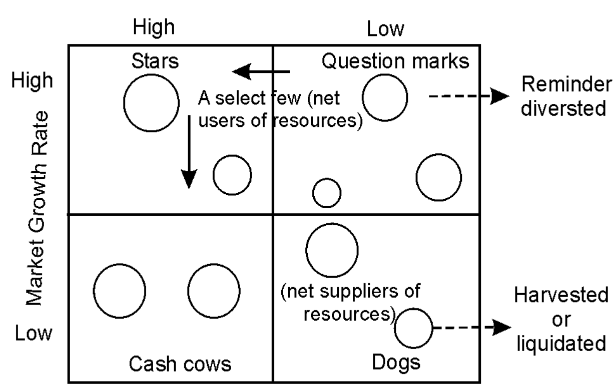
BCG Matrix

BCG Growth-Share matrix is widely used in corporate strategic analysis. This matrix helps in analyzing likely "generators" and optimum "users" of corporate resources. Organizations have to take decisions regarding the allocation of resources between competing business units. This task of allocation is complex in a constantly changing scenario. However, an organization is required to take decisions based on some fundamental criteria. In the early 1970s, the Boston Consulting Group developed a model for managing a portfolio of different business units (or major product lines). This matrix takes into consideration, the growth rate of the market and the relative market share of the business unit. The market growth rate demands attention because, it is an important factor that indicates whether the organization should stay in a particular industry or not. Rapid growth and maximum returns are possible for a firm only in booming industries. Hence, it is prudent for an organization to enter and continue to operate in a growing industry. High market share gives some special benefits to the organization such as economies of scale and bargaining power in relations with buyers and sellers. The BCG growth-share matrix displays the positions of business units on a graph of the market growth rate against their market share relative to competitors.

The Boston Consulting Group (BCG) matrix is illustrated in Figure 1.

Figure 1: BCG Growth/Shares Matrix

Relative Competitive Position (Market Share)



Source: John A Pearce II and Richard B Robinson Jr., Strategic Management (All India Traveller Booksellers, 2000) 2980.

Resources can be allocated to business units on the basis of their classification into categories. Business units are classified into four categories, namely, (i) Cash Cows, (ii) Stars, (iii) Question Marks, and (iv) Dogs.

Cash Cows – These business units hold a large market share in a mature and slow-growing industry. These businesses have a strong business position and negligible investment requirements and hence the returns from these businesses are often more than their investment requirements. Organizations often tap their cash cows' in order to draw out resources required elsewhere in the organization.

Stars – These business units have a large market share in fast growing markets or industries. Firms need to invest in stars as the industry is still emerging and market share is also growing. Often the investment requirements of stars are greater than the revenues they generate. But, once the industry reaches the stage of maturity, the stars hardly need any investment and become major sources of revenue for the firms.

Question Marks – These business units have a small market share in a high growth market. They demand significant investment because their cash needs are high, a norm in a growing industry. As the market is growing rapidly, acquiring market share is easier than in a mature market. However, the stage of growth in the industry is characterized by a lot of uncertainty that results from changes in technologies, distribution channels, and the players themselves. Hence, there are only a few question marks that are able to grow into stars.

Dogs – These business units have low market share in an intensely competitive mature industry characterized by low profits. A dog does not need much of investment, but it ties up capital that could be invested in industries with better returns. Hence, organizations concentrate on recovering as much as possible from these units in terms of returns on investment and often undertake ruthless cost cutting. Unless there is larger purpose in keeping such units, an organization should divest of dogs at the earliest.

However, recent research suggests that well-managed dogs can have a positive effect on the organization, and be highly reliable revenue generators. These well-managed dogs have a narrow business focus, concentrate on high product quality and moderate prices, have strong control over costs, and advertise only to a limited extent. Though these units can generate surplus returns, yet, the possibility of being transformed into a cash cow does not exist.

Though the BCG matrix provides a framework for allocating resources among different business units and allows one to compare many business units. it is criticized for over-simplification. For example, the relation between market share and profitability is questionable, and the emphasis on improving market share may lead the organization in a direction which does not meet the objectives of the organization. Figure 1 shows a four square BCG matrix. Each portion in the matrix has its own implications and importance.

Table 1: Process of Strategic Analysis

Corporate-level Strategy	Business-level Strategy
i. Analysis of the overall company portfolio of businesses in terms of relative business unit strength matched with relative industry attractiveness and stage of development.	i. Analysis of the match between the business's current strategic position (company profile) and the major strategic opportunities and threats (environmental analysis) that exist or will exist in the planning period in time.
ii. Identification of probable corporate performance if the current business unit portfolio is maintained with respective strategies.	ii. Examining the probable results of pursuing the current strategy in light of the new business-environment match.

iii. Comparison of this projected corporate performance with tentative corporate objectives to identify major performance gaps.	iii. Comparison of these results with tentative business objectives to identify major performance gaps and strategic concerns.
iv. Identification of alternative portfolios (including different strategy combinations at the business unit level) to close performance gaps.	iv. Identification of alternative strategies to close performance gaps and confront (or avoid) strategic concerns.
v. Evaluation of the alternatives and strategic choice.	v. Evaluation of the alternatives and strategic choice.

STRATEGIC ANALYSIS AT BUSINESS UNIT LEVEL

Once business units in a multi-industry firm have been identified, each business unit must identify and evaluate its strategy options. Strategic choices at the business level can be made through two different approaches: SWOT Analysis and Strategy Selection Matrix.

SWOT Analysis

The process of strategy formulation begins with situation analysis. i.e., the process of finding a strategic fit between external opportunities and internal weaknesses. SWOT is an acronym for strengths, weaknesses, opportunities and threats. It is a systematic study and identification of those aspects and strategies that best suit the individual company's position in a given situation. The strategy should improve an organization's business strengths and make use of opportunities and at the same time, reduce its weaknesses and stave off threats.

Strengths

Strengths are the resources, skills or other advantages the firm enjoys relative to its competitors. They are the distinctive competences that give the firm a comparative advantage in the marketplace. Some of the strengths that a company may possess are:

i. Distinct technical superiority with the best technical know-how.
ii. Financial resources.
iii. Skills of the people in the organization.
iv. Goodwill and image in the market for goods and services.
v. Access to the best distribution networks.
vi. The discipline, morale, attitude and manners of the employees.
vii. Market leadership.
viii. Good buyer/supplier relations.

Weaknesses

A weakness is a limitation or deficiency in resources, skills and capabilities that seriously impedes effective performance. It refers to a constraint that checks movement towards a distinct competitive advantage for the firm. Some sources of weakness could be limitations of:

- Facilities.
- Financial resources.
- Management capabilities.
- Marketing skills.
- Brand image.

Corporate strength and weakness are a matter of interpretation. Understanding the key strengths and weaknesses of a firm helps in narrowing down the choice of alternative strategies. The study of internal strengths and weaknesses provides a useful framework for making the best strategic choice.

Opportunities

An opportunity refers to a very favorable situation in the firm's environment. An environmental opportunity is a situation which makes it possible for a particular company to enjoy a competitive advantage. For example, changes in the Exim policy may bring opportunities to some export-oriented companies. Some opportunities for a firm may be:

- Identification of a new market segment;
- Changes in the regulatory environment;
- Technological changes; and
- Improved buyer or supplier relationships.

Threats

A threat refers to an extremely unfavorable situation in the firm's environment. It is a challenge posed by an unavoidable trend that could lead in the absence of purposeful action to the erosion of the company's position.

Some threats to a firm may be:

i. Slow market growth

ii. Entry of resourceful multinational companies/competitors

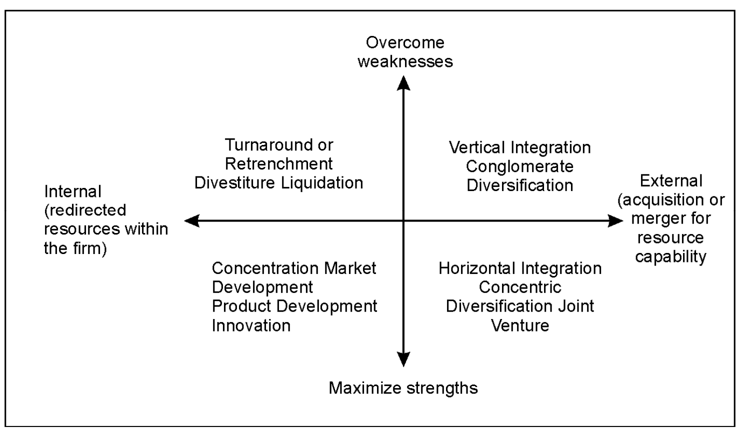
iii. Increased bargaining power of key buyers or suppliers

iv. Quick rate of obsolescence due to major technological change

v. Adverse changes in government policies, rules and regulations.

Opportunities and threats are the external factors and forces in the business environment, which change from time to time. These opportunities and threats affect organizations to a great extent because organizations operate in a business environment influenced by others. Understanding the key opportunities and threats to a firm helps its managers to identify realistic options from which to choose an appropriate strategy.

Figure 2: SWOT Analysis Diagram



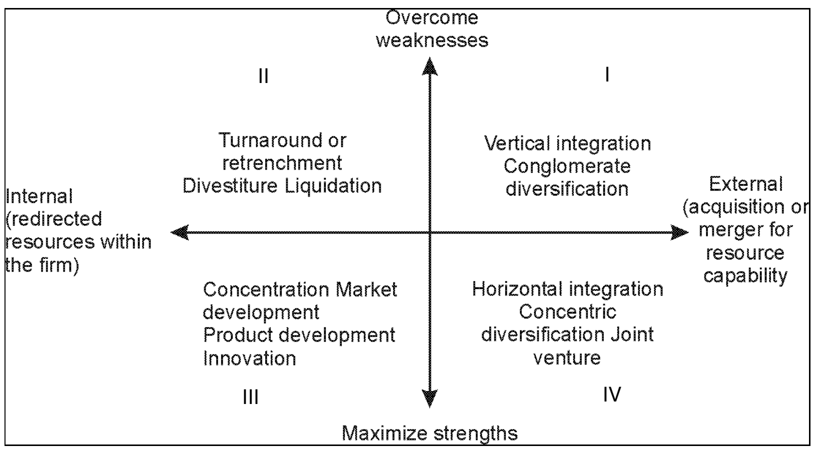
Source: John A Pearce II and Richard B Robinson, Jr., Strategic Management (All India Traveller Bookseller, 2000) 294.

An application of the SWOT analysis is illustrated in Figure 1. In the figure, the key external opportunities and threats are systematically compared to internal strengths and weaknesses. Cell 1 is the most favorable situation in which the firm faces several opportunities and has numerous strengths. This condition suggests growth-oriented strategies to exploit a favorable match. In cell 2, a firm with key strengths faces an unfavorable environment. In this situation, firms should use current strengths to build long-term opportunities. A business in cell 3 faces impressive market opportunity, but is constrained by internal weaknesses. The focus of strategy for such firms is eliminating internal weaknesses to effectively pursue market opportunity. In cell 4, the firm faces major threats from the environment and is constrained by critical internal weaknesses. Such firms should support defensive guiding alternative strategies. What one manager sees as an opportunity, another may see as a potential threat? Different assessments may reflect underlying considerations within the organization, as well as differing factual perspectives. A SWOT analysis covers all aspects of a firm's situation and provides a dynamic and useful framework for choosing a strategy.

Strategy Selection Matrix

The SWOT analysis identified the actual position of the business. But, there could be businesses that face major opportunities and some threats in its environment. Likewise, it may have numerous internal weaknesses, but it may also possess one or two major strengths. Therefore, in such situations, it becomes very difficult to place a company in a particular cell. A more specific tool for analyzing such situations is the strategy selection matrix. The matrix is shown in Figure 3. The key variables of central concern in the selection process are:

Figure 3: Grand Strategy Selection Matrix



Source: John A Pearce II "Selection among Alternative Grand Strategies," California Management Review 30, No.2 (Spring 1982), 29.

THE PRINCIPAL PURPOSE OF THE STRATEGY

The choice of an internal or external emphasis for growth and/or profitability. In the figure, the firm in Quadrant I views itself as overly committed to a particular business with limited growth opportunities. It can be said that the company has "all its eggs in one basket". Since the quadrant I companies face high risks, one solution could be vertical integration. Vertical integration would enable the firm to reduce risk by reducing uncertainty either about inputs or about access to customers. An alternative solution for the firm could be conglomerate diversification. This approach provides a profitable alternative for investment without diverting management's attention from the original business. The strategic managers considering these approaches must guard themselves against exchanging one set of weaknesses for another. Firms in Quadrant II choose to redirect resources from one business activity to another within the company. The various strategies that can be taken by firms in Quadrant II are:

i. Turnaround or Retrenchment,

ii. Divestiture, and

iii. Liquidation.

The least disruptive of the Quadrant II strategies is retrenchment, i.e., pruning of the current business's activities. Retrenchment can serve as a turnaround strategy if the weaknesses were from inefficiencies. In a turnaround strategy, the business gains new strength by streamlining its operations and eliminating waste. Divestiture offers a good possibility for recouping the company's investment. Also, liquidation can be an attractive option when the alternatives are an unwarranted drain on organizational resources.

If a firm believes in and prefers an internal emphasis for maximizing strengths, four alternative strategies hold considerable promise in Quadrant III. The strategies are:

i. Concentration.

ii. Market Development.

iii. Product Development.

iv. Innovation.

The business that selects concentration as its strategy is strongly committed to its current products and markets. It will strive to solidify its position by reinvesting resources for fortifying its strengths. With market and product development strategies, the business attempts to broaden its operations. Product development is preferred when existing customers have an interest in products related to the firm's current lines. Market development is chosen if it is felt that the products will be well received by the new customer group. Innovation is chosen as a strategy when the business's strengths are in creative product design or unique production technologies. When following a strategy of innovation, sales can be stimulated by accelerating perceived obsolescence.

The firms in Quadrant IV believe in maximizing a business's strength by aggressively expanding its basis of operations. Such firms prefer an external emphasis when selecting a strategy. The various strategies that can be undertaken by firms in this quadrant are:

i. Horizontal Integration;

ii. Concentric Diversification; and

iii. Joint Venture.

Horizontal integration enables a firm to quickly increase its output capability. Concentric diversification also facilitates a good choice. This is because the original and newly acquired businesses would be related and the distinctive competencies of the diversifying firm would facilitate a smooth, synergistic and profitable expansion. The final option for increasing resource capability through external emphasis is a joint venture. A joint venture allows a business to extend its strengths into competitive arenas that it would be hesitant to enter alone. Therefore, formidable ventures become attractive growth alternatives.

BEHAVIORAL CONSIDERATIONS AFFECTING STRATEGIC CHOICE

Strategic choice refers to the decision to adopt any of the alternative strategies. The decision process is relatively simple if the analysis clearly identifies a superior strategy or if the current strategy clearly meets the company objectives into the future. If there is an overwhelmingly superior strategy, then decision-making is easy. However, in reality this clarity is an exception. When different alternatives promise similar payoffs the decision-making process becomes judgmental and difficult. Because the strategic decision-makers are confronted with several viable alternatives rather than a clear-cut choice. Under such circumstances, various factors influence the choice. Some of these factors are:

Role of Past Strategy

The process of strategic choice begins with a review of past strategy. Often, the firm's strategists have also been the architects of strategies used earlier. Owing to their familiarity with and commitment to past strategy, both lower level managers and top level managers show an inclination towards continuity. This is probably the reason why firms sometimes replace key executives when performance of the firm has been inadequate for an extended period because replacing them lessens the influence of past strategies on options for the future. On the other hand, the more successful the strategy becomes, the harder it is to replace it with a new one, even under changed circumstances.

Attitude towards Risk

The firm's attitude towards risk influences the range of strategic choices available. Some organizations have a strong aversion to risk, while others are eager risk-takers. The range and diversity of strategic choices expands when these attitudes are adequately controlled before strategic choices are made. In risk-oriented organizations, high-risk strategies are acceptable and desirable.

Table 1, shows the relationship between attitudes toward risk and strategic choice. Another factor influencing managerial propensity towards risk is industry volatility. In highly volatile industries, top managers absorb and operate with greater amounts of risk than their counterparts. Such managers consider a broader and diverse range of strategies in the process of strategic choice. Another factor influencing the risk propensity of managers is product/market evolution. If a firm is in the early stages of product/market evolution, it has to operate with greater risk than a firm in the later stages of the product/market evolution cycle.

Table.1: Managerial Risk Propensity and Strategic Choices

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

Source: John A Pearce II Richard B Robinson Jr., Strategic Management – Strategy Formulation and Implementation. (3rd Edition, 1998) 305.

When making a strategic choice, risk oriented managers are attracted towards opportunistic strategies with higher pay-offs. They are drawn to offensive strategies based on innovation, company strengths and operating potential. On the other hand, risk averse managers lean toward safe, conservative strategies with reasonable, highly probable returns. They are drawn to defensive strategies to minimize the uncertainty associated with innovation based strategies. Thus, attitudes towards risk exert considerable influence on strategic choice.

Competitive Reaction

Organizations have to take into consideration the reactions of competitors while making strategic choices. If a firm chooses an aggressive strategy that directly challenges a key competitor, then that competitor will definitely launch a counterstrategy. Keeping this point in view, the management of the initiating firm must consider aspects such as the capacity of the competitor to react, and the probable impact of the reaction on the chosen strategy.

Degree of Firm's External Dependence

A comprehensive strategy is meant to ensure a high level of performance in the external environment. The various components of the external environment are:

- Suppliers
- Customers

- Government
- Competitors
- Unions.

A major constraint when making a strategic choice is the extent of influence of environmental elements on a firm's decision. The greater the firm's dependence on external factors, the lower will be the range and flexibility of its strategic choice.

Values and Preferences

An important basis of strategy choice lies in the background, needs, desires and values of the owners/managers. Managerial and owner attitude and its influence are seen and felt clearly in smaller companies. These factors also affect large organizations, depending on the amount of actual control in the hands of one or a few individuals. Although the amount of influence varies, the characteristics of owners and managers invariably play a part in the process of strategic choice.

CONTINGENCY APPROACH TO STRATEGIC CHOICE

The success of the strategy chosen is contingent to varying degrees, on future conditions. In order to overcome the embargoes imposed by the components of the external environment, firms adopt a contingency approach to strategic choice. In this approach, the critical assumptions on which the success of the chosen strategy depends are identified. The conditions (particularly negative ones) that may turn out to be different from the basic assumptions for these critical contingencies are also identified. Some examples of such contingencies are:

- A downturn in the economy;
- A labor strike;
- An increase in the prime rate;
- A technological breakthrough; and
- A shortage of critical materials.

Once the negative conditions in the scenarios have been identified, managers should develop alternative contingency strategies for the firm. The contingency strategies can either be short-term or long-term in nature. Moreover, these contingency strategies could be appropriate at the corporate, business, and/or functional levels. Firms using the contingency approach identify the trigger points so that the management can be alerted to consider a contingency strategy. The trigger points are specific deviations in key forecasts of industry and are set to alert management. In such, the management of the firm needs to consider alternative strategies and allow sufficient lead time for implementation of the contingency approach.

SUMMARY

- In this chapter, we discussed several considerations in strategic analysis and choice. We began the chapter by discussing the criteria for evaluating strategic alternatives, such as the criteria for suitability, feasibility and acceptability. For multi-industry firms, strategic analysis begins at the corporate level.
- The corporate strategy is concerned with the generation and allocation of corporate resources. The portfolio analysis method is a technique of strategy examination at the corporate level.
- Strategic analysis and choice do not end with corporate level strategy. The business level strategies must be examined in order to identify and evaluate the strategy options of each business. We discussed the SWOT analysis and the strategy selection matrix for making strategic choices at the business level. The factors that influence strategic choice such as the impact of past strategy, managerial attitudes toward risk, competitor's reaction, degree of firm's external dependence, time constraints, and values and preferences were discussed in the chapter. The contingency approach to strategic choice – by incorporating the flexibility to alter a chosen strategy if underlying assumptions change – also examined.

<u>**Chapter IX**</u>

Long-term Objective and Strategy Formulation

After reading this chapter, you will be conversant with:

- Defining Objectives
- The Need for Objectives
- The Nature of Objectives
- Levels of Objectives: Strategic to Operating
- The Hierarchy of Objectives
- Grand Strategies
- Setting Long-term Objectives and Strategy Sets

Introduction

No business or enterprise activity can begin unless there is a purpose, aim or objective to be reached. It is like a distant navigational aid that helps to keep the direction and renavigate in case the course changes. The activity of planning starts when the objectives are defined. Objectives are a vital prerequisite to successful operation of an organization. Objectives are a must in any organization if it has to utilize the resources relative to its opportunities and if the organization is to be well managed strategically. Once managers have determined their organization's mission, the next step is to establish how that mission is to be accomplished. The managers do this by formulating a set of objectives. Objectives are the concrete, specific aims that management seeks to achieve for the organization, often within a stated time period. The formulation of appropriate objectives is crucial to an organization's success in accomplishing its mission, since these objectives form the basis for planning, policymaking and setting performance standards.

DEFINING OBJECTIVES

Many authors have defined objectives and some of the definitions are illustrated below:

i. Mc Farland says that, "these are the goals, aims, and purposes that organization wishes to achieve over varying periods of time".

ii. Terry feels that "a managerial objective is the intended goal that prescribes definite scope and suggests direction of efforts of managers".

iii. Koontz O Donnel calls it a term commonly used to indicate, "the end point of a management program".

iv. Etzioni has said almost same thing but in a different way, "A desired state of affairs which the organization attempts to realize".

The planning process is considered as one of the prime functions of management. Also, the inseparability of objectives and planning has brought much attention to the setting of objectives as a major managerial taste. Several forces influence the selection of basic objectives. They include:

- The external environment
- The internal resources of the institution
- The personal values of major decision makers
- Management's perceptions of its societal obligations.

The factors stated above must be analyzed as part of the strategic planning process. Also, objectives specify the desired end results in addition to providing the original impetus and direction for coordinated action. Examples of objectives could be:

i. The company will ensure 35% rate of return on investment.

ii. The company will obtain 50% share for its products in the market.

iii. Company will ensure superior product with competitive price.

iv. Company will enter into foreign markets within 'x' years.

All these are overall objectives at the topmost level and will be time bound. All of these can belong to one company and it may even have a few more than listed. The establishment of objectives is necessary in the management of any enterprise, whether that enterprise is a profit making business or non-profit organization. To those who want to understand business strategy, understanding the many roles of objectives in organizations is critical.

THE NEED FOR OBJECTIVES

Organizations come into being for some purpose or purposes. The purpose/purposes of an organization's existence should be clarified, articulated and defined by the management. This is done through the establishment of objectives, which pervades the managerial process. An organization not guided by objectives is an organization not being managed properly. There are hardly any organizations with no purpose and no direction. Without objectives, an organization may continue to exist, but it cannot be considered to be under the control of management. The need of objectives can be emphasized from the following:

Objectives Provide Direction

As the beacon of a lighthouse guides ship captains to safety, objectives direct the efforts of managers into certain channels in the pursuit of these objectives. Therefore, clearly defined objectives specify an end result for the organization.

Objectives Serve as Standards

As a temperature of 70 degree Fahrenheit may reflect a homeowner's standard for a comfortable setting, objectives serve as standards for the manager. Without clearly defined objectives, managers possess no tools for evaluating performance. Without objectives, there are no means of deciding whether work is satisfactory or acceptable.

Objectives Serve as Motivators

Objectives encourage workers to put forth their best efforts to achieve the end goals. For example, employees who understand the objective of profitability and their role in generating profits may be motivated to work harder or more efficiently under a bonus or other profit sharing program.

Therefore, objectives improve the effectiveness of an organization by producing three major benefits: (i) providing direction, (ii) serving as standards for evaluating performance, and (iii) motivating members of the organization.

THE NATURE OF OBJECTIVES

The definitions of objectives stated earlier in the chapter gives us the clue as to what the nature of objectives should be.

i. Firstly, objectives are the goals set by the enterprise, which have to be reached.

ii. Objectives are the most essential part of a plan and relate to the future.

iii. They give direction to all functions and plans of an organization. They will have a bearing on policies, staffing, directing and of course, control.

iv. Objectives are not sacrosanct in the sense that a change in situation will have a bearing on these and they may be changed.

v. They come in various garbs viz. primary and secondary, general and specific, long-term and short-term, few to many in number.

vi. There is always a hierarchy of objectives. The objectives of the top management give direction to departmental ones that in turn give line to shop floor objectives.

vii. All objectives of the enterprise at all levels are inter-connected and inter-related because their original source is one. They form a network of objectives.

viii. Objectives are bound by restrictions of premises.

The strategic managers must ensure that objectives are communicated to all members of the organization. Each employee should understand how his/her individual work objectives relate to the overall organizational objectives. As the organization and the environment in which it operates change, objectives may require adjustments to reflect these changes.

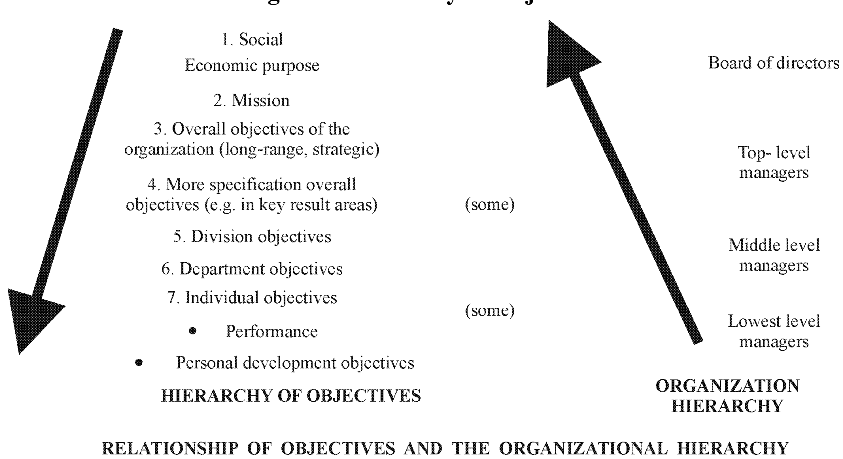
LEVELS OF OBJECTIVES: STRATEGIC TO OPERATING

Companies have specific planning goals in areas such as production, marketing, finance, etc but these derive from broader and more abstract, basic objectives. The functional objectives are based upon personal needs values and goals of individuals and groups that are within or that influence the organization. Also, the degree of abstraction is the key to understanding organizational objectives. Objectives vary by nature in the level of precision with which they are described, in the breadth of their coverage within an organization, and in periods during which they are applicable. Moreover, objectives deal with specific decisions, performance and expected results. They are needed because managers must be able to measure their progress towards achievements and attainments especially in areas critical to organizational survival and success. Specific objectives are dependent upon the establishment of broader objectives. This is because they state more clearly the short-term measurable goals that are to be achieved if attainment of broader strategic objectives is to become a reality for the organization. The process of business strategy requires that managers at all levels of an organization become involved in a process of formulating objectives that are consistently linked. Failure to achieve this consistency linkage results in sub-optimization.

THE HIERARCHY OF OBJECTIVES

Objectives state end results and overall objectives need to be supported by sub-objectives. Thus, objectives form a hierarchy. Figure 1 shows hierarchy of objectives, ranging from the broad aim to specific individual aims. At the zenith of the hierarchy are the socio economic objectives, such as requiring the organization to contribute to the welfare of the people by providing goods and services at reasonable cost. The next level consists of the mission of the organization. At the third level are the overall objectives and strategies (such as designing. producing and marketing reliable, low-cost products).

Figure 1: Hierarchy of Objectives



Source: H Weihrich and J Medleson, Management: An MBO Approach (Duuque, Iowa: WM, C Brown Co., 1987), P.xi. Used with permission.

The next level of the hierarchy contains more specific objectives called *Key Result Areas* (KRAs). These are the areas in which performance is essential for the success of the enterprise. The KRAs have to be watched very carefully. The objectives have to be further translated into division, department and unit objectives down to the lowest level of the organization. The accomplishment of each subsidiary objective should contribute to the achievement of its respective superior objective, thus providing a thorough integrated and harmonious pattern of objectives to all members of the units.

Descending the hierarchy, objectives become less abstract, less enduring and less encompassing in the total organizational context. The objectives at the lower level of hierarchy require fewer resources; involve commitment from fewer organizational members and are more readily measurable. Viewing the hierarchy of objectives, one can picture the roles of various levels of management.

Thus, the concept of hierarchy helps to clarify the nature of objectives, particularly strategic objectives. The concept not only shows that it is not useful to consider only a single objective for any institution, but it also demonstrates that a multiplicity of objectives must be articulated if organizational direction is to be clearly understood. Moreover, this concept places objectives into an orderly and logical framework. With this framework, the nature of objectives can be more readily described, analyzed and understood.

GRAND STRATEGIES

Grand strategies, often called master or business strategies provide basic direction for strategic actions. In other words, a grand strategy is a strategy that provides the basic strategic direction at the corporate level. They are the basis of coordinated and sustained efforts directed towards achieving long-term business objectives. Also, they indicate the time period over which objectives are to be achieved. Thus, a grand strategy can be defined as a comprehensive general approach that guides a firm's major actions. .

The grand strategies can be divided into growth strategies and retrenchment strategies.

Growth Strategies

The growth strategies are adopted when firms remarkably broaden the scope of their customer groups, customer functions and alternative technologies singly or in combination with each other. They involve a significant increase in performance objectives. Thus, growth strategies are those grand strategies that involve organizational expansion along some major dimension. In business organizations, growth typically means increasing sales and earnings. Though other criteria such as increase in number of geographic locations, clients served, etc may also be the criteria for growth. The major growth strategies are:

- Concentration
- Market Development
- Product Development
- Innovation
- Horizontal Integration
- Vertical Integration
- Joint Ventures
- Concentric Diversification
- Conglomerate Diversification

The various growth strategies are discussed taking one at a time.

CONCENTRATION

Firms pursue concentration strategies to grow while remaining relatively simple. Concentrated growth is the strategy of the firm that directs its resources to the profitable growth of a single product, in a single market with a single dominant technology. The main rationale for this approach is that the firm thoroughly develops and exploits its expertise in a delimited competitive arena.

The main advantage of concentrated growth strategy is that it leads to enhanced performance. The major characteristics of a concentrated growth strategy are the ability to assess market needs knowledge of buyer behavior, customer price sensitivity and effectiveness of promotion. These characteristics are a major determinant of competitive market success. Firms pursuing the concentration strategy identify new developments and trends within the industry and respond to them. Table 1 illustrates strategic alternatives available to the firms pursuing concentration strategies.

Table 1: Strategic Alternatives for Firms Pursuing Concentration Strategies

Focus on Customer:
Increase usage by present customers
Increase purchase size or frequency
Improve product location
Expand product line (sizes, options, styles)
Expand shelf space
Attract Competitors' Customers:
Increase promotional efforts
Initiate price cuts
Attract Non-users of the product:
Advertise new uses
Offer special prices and promotions
Increase product availability (new geographic uses)
Focus on Product:
Differentiate product from its competitors
Increase Rate of Product Obsolescence
Change styles
Change options
Change colors
Develop new uses for the product
Improve product servicing
Focus on Technology:
Develop new equipment to improve efficiency
Develop new products
Find uses for by-products
Improve quality.

Specific conditions in the firm's environment are favorable to the concentrated growth strategy. One such condition is that when the firm's target markets are not product saturated. Markets with competitive gaps leave the firm with alternatives for growth rather than taking market share away from competitors. Another favorable condition exists when the firm's inputs are stable in price and quantity and are available in the amounts and at the times needed. Also, a stable market – a market without the seasonal or cyclical swings that would encourage a firm to diversify, favors the pursuit of concentrated growth.

RISKS AND REWARDS OF CONCENTRATED GROWTH

Under stable conditions, concentration poses less risk than any other grand strategy. But in a changing environment, concentrating in a single product market makes a firm vulnerable to changes in that segment. Also, it is difficult for an organization to attempt sudden changes if its product is threatened by near-term obsolescence, changes in customer needs, new substitutes or changes in technology. In the case of concentration, over commitment to a specific technology and product market can hinder a firm's ability to enter a new or growing product market that offers more attractive cost-benefit trade-offs. Also, organizations following concentration strategy incur high opportunity costs that result from remaining in a specific product market and ignoring other options that could employ the firm's resources more profitably.

A major misconception about the concentrated growth strategy is that the firm practicing it will settle for little or no growth. A firm adopting this strategy grows by building on its competencies. By this, the firm achieves a competitive edge by concentrating in the product-market segment it knows best. The firm that chooses a concentrated growth strategy directs its resources to the profitable growth of a narrowly defined product and market, focusing on a dominant technology. Therefore, the success of a concentration strategy is founded on the firm's use of superior insights into its technology, product and customer to obtain a sustainable competitive advantage.

MARKET DEVELOPMENT

Market development ranks second only to concentration as the least costly and least risky of the grand strategies. The strategy of market development consists of marketing present products often with only minor modifications, to customers in related market areas by adding channels of distribution or by changing the content of promotion and so on. The specific approaches to market development are:

A. Opening additional geographic markets

- Regional expansion
- National expansion
- International expansion

B. Attracting other market segments

- Developing product versions to appeal to other segments
- Entering others channels of distribution
- Advertising in other media

Market development allows firms to practice a form of concentrated growth by identifying new uses for existing products and new demographically, psychographically and geographically defined markets. For example, firms are said to practice the strategy of market development if they switch from advertising in trade publications to advertising in newspapers or if they add jobbers to supplement their mail-order sales efforts. Therefore, changes in media selection, promotional appeals and distribution are used to initiate the approach of market development.

PRODUCT DEVELOPMENT

Product development involves the substantial modification of existing products or the creation of new but related products that can be marketed to current customers through established channels. The strategy of product development is adopted either to prolong the life cycle of current products or to take advantage of a good brand name. The idea of product development is to attract satisfied customers to new products as a result of their positive experience with the organization's initial offering. Some of the options available to firms undertaking product development are:

A. Developing new product features:

- Adapt (to other ideas, developments)
- Modify (change color, motion, sound, odor, form, shape)
- Miniaturize (smaller, shorter, lighter)
- Magnify (stronger, longer, thicker, of extra value)
- Rearrange (other patterns, layout. sequence, components)

- Reverse (inside out)
- Substitute (other ingredients, process, power)
- Combine (blend, alloy, assortment ensemble, combine units, appeals ideas)

B. Developing quality variations

C. Developing additional models and sizes (product proliferation)

Therefore, product development strategy is based on the penetration of existing markets by incorporating product modifications into existing items or by developing new products with a clear connection to the existing product life. For example, Nokia is developing video cameras that can even provide basic telephony and even Web Connectivity.

INNOVATION

Periodic changes and improvements in the products are expected by both the consumers and industrial markets. Due to this reason, organizations make innovation their grand strategy. The underlying rationale of the innovation strategy is to create a new product life cycle and thereby make similar existing products obsolete. Firms following this strategy reap the initial high profits associated with customer acceptance of a new or greatly improved product. While most growth oriented firms appreciate the need to innovate occasionally, a few firms use it as their fundamental way of relating to their markets.

Horizontal Integration

When a firm's long-term strategy is based on growth through the acquisition of one or more similar firms operating at the same stage of the production-marketing chain, its grand strategy is called as horizontal integration. The various reasons as to why firms take up the strategy of horizontal integration are:

- To increase the market share
- To reduce the cost of operations per unit of business through the large scale economies
- To have greater access to channels of distribution
- To get greater leverage to deal with the customers and suppliers
- To enjoy increased operational flexibility
- To promote the products and services more efficiently to a larger audience
- To take the advantage of the benefits of synergy.

Therefore, horizontal integration means the degree to which a firm operates in multiple geographic locations at the same point in an industry' value chain. The horizontal integration for a firm may range from full to partial ownership to long-term contracts. An example of horizontal integration could be the case of ICICI into many areas of the financial services sector.

Vertical Integration

Vertical Integration involves effecting growth through the production of inputs previously provided by suppliers or through the replacement of a customer role by disposing of one's own inputs. In other words, in vertical integration, new products and/or services, which are complementary to the existing product and/or service lines, are added. Vertical integration is characterized by the extension of the company's definition in two directions from the existing business viz. backward integration and forward integration.

Backward Integration

Backward integration takes place when a firm assumes a function previously provided by a supplier (going backward on an industry's value chain). For example, 7-Up, the soft drink manufacturer used this method to own the, lemon tree orchards that produced the lemon extract for the drink that was earlier supplied by many suppliers. The advantages of backward integration strategy are:

- Firms can have a regular and uninterrupted supply of raw materials, components and other inputs.
- Firms can enjoy economies of large-scale operations.
- Quality control of raw materials, components and parts is ensured.
- Firm can increase its power of negotiation with other suppliers in view of access to information on costs, facilities, earning potential, etc.
- There can be a minimization on direct taxes payable on purchases of inputs.

Though this strategy offers many advantages, it is not free from limitations. Certain drawbacks of this strategy are:

- Technological upgradation in one of the firms necessarily forces the management to upgrade the technology of the remaining firms. This process demands heavy financial investment that may not be feasible in short-term.
- Adverse economic conditions in the main firm also affect the firm supplying raw materials, etc.

Forward Integration

When organizational growth encompasses a role previously fulfilled by a customer, the process is known as forward integration (going forward on an industry's value chain). For example, a personal computer maker could own a chain of retail stores from which it sells its machines. Firms adopt the strategy of forward integration due to the advantages it offers, such as:

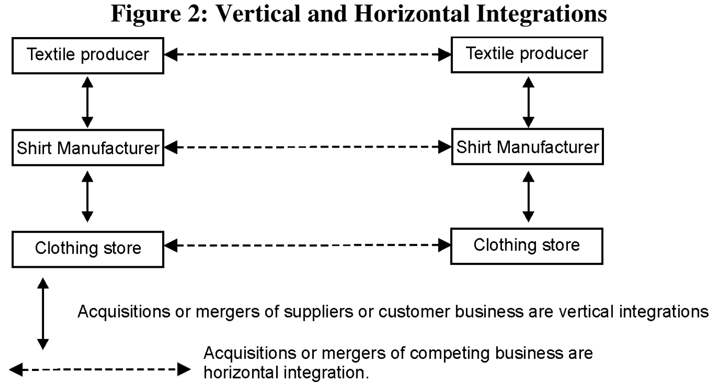
- Greater acquisition of control over sales prices and level of output.
- Firms can improve their competitive position.
- Firms can develop their own network for consumer feedback.
- Firms can have their own facilities for providing pre-sales and post-sales service.

In spite of the advantages, this strategy suffers from certain disadvantages such as:

- Since the firm produces final products with its own components and sells the final products as well as components, it competes with its own customers,
- Sometimes, firms face financial problems as thus strategy demands for large-scale operations at retail level.

Although backward integration is usually more profitable than forward integration, it can reduce a corporation's strategic flexibility in the long-run since exit from business would be a difficult proposition. Figure 2 depicts both horizontal and vertical integration.

Figure 2: Vertical and Horizontal Integrations



JOINT VENTURES

Joint ventures are partnerships in which two or more firms carry out a specific project in a selected area of business. Companies often form joint ventures to combine the resources and expertise needed to develop new products or technologies. It also enables a firm to enter a country that restricts foreign ownership. Joint ventures are formed when:

- An activity is uneconomical for an organization to do alone.
- The risk of business has to be shared.
- The distinctive competence of two or more organizations can be pooled together.
- Setting up of an organization requires surmounting hurdles such as tariffs, quotas, government interference, cultural roadblocks, etc.

There could be many reasons for the foundation of joint ventures. Firstly, in some countries, foreign firms are allowed to operate only if they enter into a joint venture with a local partner. Secondly, the size of the project may be so large that one company may not be in a position to accomplish it. Thirdly, some projects require multidimensional technology and firms with different technologies may join together. Also, one firm with technological competence and another firm with managerial competence may join together. Lastly, a foreign firm with technological competence can join with a domestic firm with marketing competence. Anyone or more than one reason could be tact for formation of joint ventures.

Joint ventures are commonly used because they offer certain advantages to the competencies. Some of them are:

- Joint ventures help in spreading development costs
- Joint ventures are useful as a form of 'trial marriage' to see if firms can work together before undertaking a merger.
- Joint ventures are adopted as a strategy by firms entering international markets.
- Partner in the host country assists in interpreting local customs and culture and translating technical language.
- Joint ventures provide the chance to combine the strength of two partners and utilize the opportunities provided by the environment.
- When the development costs and risks of opening in a foreign market are high, a company might gain by sharing these costs and risks with a local partner.
- Moreover, in many countries, political considerations make joint ventures the only feasible entry mode.
- They provide quick access to channels of distribution, thus reducing the marketing cost.

Despite of these advantages, joint ventures can be difficult to establish and run because of certain drawbacks.

- Problems of equity participation by the foreign and home partners.
- A company that enters into a joint venture risks losing control over its technology to its venture partner.
- Foreign exchange regulations imposed by both governments.
- Lack of proper coordination between/among partners.
- Differences of culture and customs between both the partners.
- Loss of control to the other firm.

Joint ventures are formed for specific and time bound objectives that, once achieved, leave little reason for the alliance to be continued. The most valuable contribution of joint venture is that both the companies share the strengths of each other participating firm and eliminate the weaknesses of both the firms by acquiring other's strengths.

CONCENTRIC DIVERSIFICATION

Diversification is an approach that entails affecting growth through the development of new areas that are clearly distinct from current businesses. In addition to diversifying for growth reasons, organizations often diversify to reduce the risk that can be associated with single product or industry operations.

Concentric diversification occurs when an organization diversifies into a related, but distinct business. In other words, it involves the acquisition of businesses that are related to the acquiring firm in terms of technology, markets or products. With concentric diversification, the selected businesses possess a high degree of compatibility with the firm's current businesses. For example, a snow ski manufacturer acquires a firm that makes water skis. This move would even out sales around the year and remove cyclicality of the business.

CONGLOMERATE DIVERSIFICATION

Conglomerate diversification is a diversification into a new business area that has no obvious connection with any of the company's existing areas. It is also called unrelated diversification. Organizations that adopt this diversification strategy are often referred to as conglomerates. For example, X Gas Ltd. creates another business unit, i.e., X Finance Company Ltd. The benefits of this strategy are:

- Reduction of risks, particularly for businesses that operate in industries subject to rapid technological change.
- Economies of large-scale operation.
- Financial stability and increased profits.

The principal difference between the two types of diversification is that concentric diversification emphasizes some commonality in markets, products or technology. And conglomerate diversification is based principally on profit considerations.

Retrenchment Strategies

A company pursues retrenchment strategies when it has a weak competitive position in some or all of its product lines, thus resulting in poor performance. Retrenchment strategies are adopted when the firm's survival is at stake. These strategies impose a great deal of pressure to improve performance. The specific reasons for adopting retrenchment strategies could be:

- Existence of poor economic conditions
- Operating and production inefficiencies
- Inability of the firm to implement latest technology
- The company has not met its objectives and there is pressure from shareholders or customers to improve performance
- Excessive competitive pressures
- When the strengths are insufficient to face the threats posed by the environment.

The retrenchment strategies that would be discussed are divestiture and liquidation.

DIVESTITURE

A divestiture strategy involves the sale of a firm or a major component of a firm. This strategy is adopted if the company is unable either to pull itself by its bootstraps or to find a customer to whom it can become a captive company. There are three approaches of divestiture. Firms can select any approach depending upon the need for adopting this strategy. They are:

i. Divestiture strategy can be pursued by spinning off a part of the business as an independent entity.

ii. Firms can sell a business unit to another firm. Mergers are the result of one firm selling a part of its operations to another firm.

iii. Another form of this strategy is simply closing down a portion of the firm's operations.

The causes for adopting divestment strategy could be:

- When a firm's market share is negligible or when the market size is small to earn desired profit.
- Often limited resources force firms to divest from less profitable business to more profitable business.
- Parts of businesses are divested when they do not fit in the original business of the firm.
- If cash outflows are more than cash inflows, in any unit, then the firm is forced to divest that unit.
- Firm's inability to meet the competition.
- The technological changes and the inability of the firm to invest additional financial resources.
- Divestment of unprofitable wings becomes necessary to allow the remaining business to survive.
- Sometimes, this strategy is necessary to abide by the provisions of the law.

Thus, divestiture strategy is used when the firm wants to increase the efficiency of a strategic business unit or major operating division or product line that has failed to achieve the desired results.

LIQUIDATION

The liquidation strategy involves closing down a business organization and selling its assets. This strategy is adopted when the industry is unattractive and the company is too weak to be sold as a going concern. In liquidation, management converts as many saleable assets as possible to cash, which is then distributed to the shareholders after all obligations are paid. This is the last alternative strategy, as its consequences are severe. The various reasons for adoption of liquidation strategy could be:

- Small businesses and partnership firms liquidate when one or more partners want to withdraw from the business.
- When a sole proprietor wants to retire or take up another job, he has to liquidate his business.
- The liquidation strategy is essential when one of the partners has to withdraw and all other partners express their inability to buy the withdrawing partner's share.
- Liquidation occurs when the value of assets of the firm are more worthwhile than the rate of return earned by the firm.
- Sometimes, owners adopt the liquidation strategy when they receive a highly attractive offer and they may feel that liquidating the business is more worthwhile.

The consequences of liquidation would include:

- Liquidation leads to a closure of an agency performing economic functions. Therefore, government does not encourage liquidation, unless it is warranted.
- Employees and trade unions do not welcome this strategy because the jobs of the employees will be terminated.

- The stakeholders (creditors, dealers, financial companies. Banks, customers, suppliers) do not prefer this strategy because the obligations of the firm towards them will be fully or partially unmet.
- It would be difficult to find a buyer, as it involves large amount of finance.

In view of the consequences stated above, firms should adopt this strategy in a planned way and very carefully. Liquidation strategy should be adopted when it enables the company to get maximum proceeds by selling the assets and meet the obligations of various stakeholders.

SETTING LONG-TERM OBJECTIVES AND STRATEGY SETS

Long-term objectives are statements of the results a firm seeks to achieve over a specified period. To achieve long-term prosperity, strategic planners commonly establish long-term objectives in seven areas. They are:

Profitability

The ability of any firm to operate in the long run depends on attaining an acceptable level of profits. The profit objective is generally expressed in earning per share or return on equity.

Public Responsibility

In the long run firms recognize their responsibilities to their customers and to society at large. Such firms work to establish themselves as responsible corporate citizens.

Productivity

Strategic managers constantly try to improve the productivity of their organization. Sometimes, the productivity objective is stated in terms of desired cost decreases. For example, objectives may be set for reducing defective items or for overtime, and so on.

Competitive Position

One measure of corporate success is relative dominance in the market place. Therefore, organizations formulate long-term objectives for improving their competitive position.

Employee Development

Employees value growth and career opportunities. Thus, strategic planners often include an employee development objective in their long-range plans.

Employee Relations

Organizations are bound by union contracts and they actively seek good employee relations. Strategic planners set objectives for safety programs, employee stock option plans for improving employee relations.

Technological Leadership

Another long-term objective that is often set by strategic planners is with regard to technological leadership.

The criteria that are to be used in preparing long-term objectives are:

- **Flexible:** The long-term objectives should be adaptable to unforeseen changes in the firm’s environment (internal and external).
- **Measurable:** Long-term objectives should be measurable over time i.e. they must clearly and concretely state what will be achieved and when it will be achieved.
- **Motivating:** Long-term objectives should be high enough to challenge but not so high to frustrate or so low as to be easily attained. Also, objectives should be tailored to specific groups so that they can be motivating.

- **Suitable:** The long-term objectives must be suited to the broad aims of the firm, which are expressed in its mission statement.
- **Understandable:** The long-term objectives must be so stated that they are understandable to the recipient as they are to the giver. The strategic managers at all levels must understand what is to be achieved.
- **Achievable:** Lastly, objectives must be possible to achieve. This means that the strategic managers while formulating long-term objectives must take all the limiting factors into consideration.

Therefore, when strategic planners study their opportunities, they try to determine which opportunities are most likely to result in achieving various long-range objectives. Simultaneously, they forecast whether an available grand strategy could take advantage of preferred opportunities. In essence, two distinct but highly interdependent choices are being made at one time i.e., formulating long-term objectives and determining grand strategy sets.

The selection of long range objectives and grand strategies involve simultaneous and sequential decisions. Also, objectives can be achieved only if strategies are implemented. In fact, long-term objectives and grand strategies are so interdependent that some business consultants do not distinguish between them. But there is some distinction between the two. Objectives indicate what strategic managers want but provide few insights on how they will be achieved. On the other hand, strategies indicate what type of actions will be taken, but do not define what ends will be pursued.

SUMMARY

- The place of objectives in strategy management is vital. Broad strategic objectives provide the direction for rational planning and policy making in an organization. This chapter provides an overview of objectives and strategies. We begin the chapter by discussing as to what are objectives and the need for objectives. Then the nature of objectives and the levels of objectives have been discussed, which notes the various levels of specificity among objectives set at the different levels in an organization.
- Grand strategies provide the basic directions for strategic actions at the corporate level. In the final part of the chapter, the grand strategies i.e. growth and retrenchment strategies have been discussed. The major growth strategies discussed are concentration market development, product development, innovation, horizontal integration, vertical integration, joint ventures, concentric diversification and conglomerate diversification. The major retrenchment strategies discussed are divestiture and liquidation. The chapter is concluded by giving a note on long-term objectives and selection of long-term objectives and strategy sets.

Chapter X

Strategy Implementation and Monitoring

After reading this chapter, you will be conversant with:

- Identification of Annual Objectives
- Developing Functional Strategies
- Structural Considerations
- Organizational Structure and Systems
- Corporate Resource Planning
- Functional Resource Planning
- Allocation or Resources
- Strategic Controls
- Operational Control Systems
- Reward Systems
- Crisis Management

Introduction

A firm that is moving from strategy formulation to strategy implementation has to give enough consideration to three interrelated concerns: identification of measurable, mutually determined annual objectives: development of specific functional strategies: communication of concise policies to guide decisions. It is also important that employees from all the levels in the organization are involved in strategy formulation.

Annual objectives express long-range goals in terms of yearly budget. These objectives if developed appropriately can provide clarity, which is a strong motivator, and effective facilitator of strategy implementation. Annual objectives act as a guide for implementation once long-term objectives are translated into specific short-term ones.

Functional strategies translate grand strategy at the business level into action plans for subunits of the company. Operating managers play a key role in developing these strategies, and these strategies make clear what the manager's units are supposed to do to ensure effective implementation of the grand strategy.

Policies are directives or guidelines given to managers and their subordinates as the framework to guide their thoughts, decisions and actions while implementing the organization's strategy. They are meant to bring consistency between operating processes and the firm's strategic objectives, and are often referred to as standard operating procedures. By standardizing routine decision-making and limiting the discretionary powers of managers and subordinates in implementing operations strategies, they increase managerial effectiveness.

IDENTIFICATION OF ANNUAL OBJECTIVES

Market share, return on investment, return on equity, stock price and expansion into new markets indicate the ultimate effectiveness of a chosen strategy. The long-term purpose of a grand strategy and the basis for judging its success should be reflected in annual objectives. The identification and communication of annual objectives that relate to the long-term objectives of a strategy is a crucial step in the successful implementation of a strategy. The successful execution of the business's overall long-term plan is based on the accomplishment of these annual objectives. Annual objectives also provide a specific basis for monitoring and controlling organizational performance. Such objectives can aid the development of "trigger points" that alert top management.

Qualities of Effective Annual Objectives

Annual objectives are specific, measurable statements of what an organization's subunit is expected to achieve in the next year as a part of the business's grand strategy. Although these objectives are achievable, organizations sometimes fail to accomplish them due to a poor understanding of the environment. Certain basic precepts must be incorporated into the development and communication of objectives for them to be useful.

Linkage to Long-term Objectives

An annual objective must be linked clearly to the long-term objectives of the organization. Before aligning these two types of objectives, managers must study the different ramifications of the grand strategy. At the same time, the management should be clear about the differences between these two types of objectives. These objectives differ basically in the following four aspects:

- **Time Frame:** Long-term objectives are fixed for 5 years or more, whereas the annual objectives are fixed for only one year.
- **Focus:** Long-term objectives focus on the future position of the firm in its competitive environment, while the emphasis of annual objectives is on specific goals for the company, functional areas, or other subunits.

- **Specificity:** Long-term objectives are broadly stated, whereas annual objectives are directly linked to the company. a functional area, or other subunit, and are very specific.
- **Measurement:** Both long-term and annual objectives are quantifiable. Long-term objectives are measured in broad relative terms: for example, 20 percent market share, whereas 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 completed successfully in order to achieve the long-term objectives. For example, if a company has a long-term objective of achieving 20 percent market share after 5 years, then a series of specific annual objectives must be fixed in order to meet the long-term objective. Specific annual objectives provide targets for achieving the long-term objectives. They clearly identify the performance requirements of the various operating areas. "Opening two regional distribution centers in the south in the year 2005" might be one annual objective of a marketing manager. "Concluding an arrangement for Rs.l0 million line of credit at one percent above prime lending rate in 2005" might be an annual objective of financial manager. These objectives will support the operations of new distribution centers and the additional purchases necessary to increase output in accordance with long-term objectives.

Integrated and Co-ordinated Objectives

Implementation of grand strategies requires integrated and co-ordinated objectives. However, the subunit manager, viz., vice-Presidents of finance, marketing and production may not recognize the importance of integration and co-ordination in setting annual objectives. The priorities of the marketing function may be totally different from those of finance/accounting or manufacturing. For example, in manufacturing, long production runs and plant warehousing are preferred in the interests of efficiency. On the other hand, marketing which usually aims at customer satisfaction can be made more efficient by frequent, short production runs and field warehousing. The annual objectives of different subunits should be integrated and co-ordinated. Without this, long-term objectives remain unfulfilled due to the conflicts between departments. Proper co-ordination and integration of operating units leads to successful implementation of the strategy. This is encouraged through the definition of short-term annual objectives.

Consistency in Annual Objectives

An organization must maintain consistency in setting its annual objectives. In an organization with many departments, the managers of the different departments may not think on the same lines. Due to their varied work backgrounds, managers might have different and inconsistent perceptions. For example, the marketing manager of the firm may prefer objectives regarding the delivery time to customers, that may be inconsistent with the operations manager's objectives, and this may eventually block the strategic success of the firm.

Annual objectives are said to be consistent when each objective clearly states what is to be accomplished, when it will be accomplished, and how each accomplishment will be measured. Annual objectives are used in order to monitor the effectiveness of an operating unit, and to progress collectively towards the business's long-term objectives. Similarly, recognizing the annual objectives is an important aspect in implementing strategies.

Benefits of Annual Objectives

Annual objectives also help operations managers and personnel to define their role in the business mission. This clarity of purpose is useful for mobilizing and motivating the people in the organization.

The objectives are drawn up by the managers who are responsible for their accomplishment. This makes the managers more accountable for planning and achieving targets. Well-set annual objectives also provide a basis for strategic control. Thus, the setting of annual objectives helps the organization in developing budgets, schedules, trigger points and other mechanisms for strategy implementation and control.

Annual objectives provide strong motivation for managers in strategy implementation. This is particularly true when they are linked to the business's reward structure. However, it should be ensured that the objectives clarify personal and group roles in a business's strategies, and are also measurable, realistic and challenging.

DEVELOPING FUNCTIONAL STRATEGIES

A functional strategy is a short-term game plan for a key functional area within a company. Functional strategies clarify the grand strategy, and provide specific details about the management of key functional areas in the near future.

Functional strategies must be consistent with long-term objectives and the grand strategy. They enable the grand strategy to be pursued in terms of daily activities. Functional strategies help in the implementation of the grand strategy by organizing and activating specific subunits (marketing. finance. production etc.) of the company.

Differences between Grand and Functional Strategies

There are three basic characteristics which differentiate functional strategies from grand strategies:

- Time horizon covered,
- Specificity, and
- Participation in their development.

TIME HORIZON

For a functional strategy the time horizon is usually short. For example, BPL Sanyo might prefer 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 is designed to achieve an annual objective but ultimately contributes to the goal of BPL Sanyo's grand strategy in its retail division over the next five years.

SPECIFICITY

A functional strategy is more specific than a grand strategy. Functional strategies are restricted to the company's subunits, carrying out certain functional activities in key areas, in order to implement the grand strategy. The general direction is provided by the grand strategy. Functional strategies give specific guidance to managers responsible for completing the objectives successfully. Such strategies are meant to ensure that managers meet their objectives in the best possible way. The willingness and ability of operating managers to implement strategic decisions can be improved by specific functional strategies, particularly when those decisions represent major changes in the current strategy of the firm.

For example, the grand strategy of a movie production firm, Usha Kiran Movies, indicates the direction that its movie theater division should follow in order to capture the market. Its marketing functional strategies give specific direction to managers on the type of movies (action, horror, comedy. family oriented etc.) they should show and the pricing strategy (competitive in the local area) they should follow.

Specificity in functional strategies contributes to the successful implementation of plans in several ways. First, it adds substance, completeness and meaning to what a specific subunit of the business must do. The functional strategies ensure that managers know what needs to be done and can focus on achieving the results. Second, specific functional strategies clarify for the top management how functional managers intend to complete the grand strategy successfully. This increases the top management's confidence in the grand strategy. Third, the co-ordination between operating units within the company is facilitated since areas of interdependence and potential conflict are clarified by specific functional strategies.

PARTICIPATION

Various people at the functional and business levels participate in both functional and business strategy formulation. Business strategy is the responsibility of the general manager of the business unit. Manager of each business unit relies on his subordinates for the design and implementation of the functional strategies. Functional managers establish annual objectives and operating strategies meant for his department.

It is difficult to generalize about the development of strategies across functional areas because of the difference in the key variables in marketing, finance and production. Further, within each functional area, the importance of key variables varies across business situations.

Functional Strategies

MARKETING

The role of the marketing function is to increase sales of the product and thus increase revenue generation for the company. Functional strategies in marketing should back up this effort in a manner consistent with the grand strategy and strategies relating to other business functions. Marketing managers develop marketing strategies which determine who will sell what, where, when, to whom, in what quantity and how. The four components, viz., product, price, place and promotion must be covered by marketing strategies.

A product or service must be available to a customer wherever and whenever he needs it. Marketing functional strategies identify the correct time, place and seller for the product. Decisions on the channels to be used (for example. single versus multiple channels) are also based on marketing strategy. The marketing manager's decisions regarding features, product lines, packaging, accessories, warranty, quality and new product development must also follow the recommendations of the marketing functional strategy. The strategy should include a comprehensive statement of the product/service concept and the target markets, the firm seeks to serve. This will promote consistency and continuity in the daily activities of the marketing unit.

Marketing strategy defines how a firm can communicate with the market efficiently in order to sell its products and services. Under marketing strategy, different options for selling such as personal selling, sales promotion, advertising and media selection are considered. The marketing strategy should be consistent with other strategies like financial strategy and operational strategy.

The single most important consideration in marketing is the functional strategy regarding price. Every customer expects to spend less and get more value from the product. So, when two products are of similar quality but differ in their price, the customer naturally prefers the product with a lower price. This decision of the customer affects the organization's revenue generation. Thus, the price influences demand and supply, profitability, consumer perception, and possibly a regulatory response (of the government). The approach to pricing strategy may be cost-oriented, market-oriented or competition-oriented. Pricing decisions are centered on total cost with an acceptable markup or target price ranges, under a cost-oriented approach. When the approach is market-oriented, pricing is based on consumer demand (for example, petrol pricing in a deregulated oil industry). With the competition-oriented approach, pricing decisions center around those of the firm's competitors.

FINANCE/ACCOUNTING

While most operating strategies guide implementation in the immediate future, financial strategies direct the use of resources in supporting long-term goals and annual objectives. The financial managers follow strategies with long time perspectives in investment, use of debt financing, dividend allocation and the firm's leveraging posture. Long-term financial strategies usually act as the basis for programs of capital acquisition.

Before embarking on acquisition of capital, decisions have to be taken on the desired level of debt and equity, and the internal long-term financing of business activities. For example, Delta Airlines seeks to minimize the level of debt in proportion to equity and to the internal funding of capital needs.

Capital allocation is another important aspect of financial strategy. A company has numerous alternative areas for investment for example, in facilities, projects acquisitions or in recruiting people. Proper planning is necessary to make the right investments. With appropriate planning, scarce capital can be used in the most productive way.

When the company is downsizing or trying to remain at a stable level, it requires a financial strategy that focuses on the reallocation of existing capital resources. The pruning of product lines, production facilities or personnel and their reallocation elsewhere in the firm may all be necessary in such a strategy.

The strategy relating to capital allocation should be carefully implemented. For example, when the business is growing, demand for the firm's product is high; capital expenditure strategy at the operating level should be flexible enough to respond adequately to an evolving market. .

RESEARCH AND DEVELOPMENT

Research and development is a critical function in many organizations because of the increasing importance of technology in most industries. The technology-intense computer and pharmaceutical industries reinvest between 4 to 6 percent of their total sales in R&D. R&D strategy determines the appropriateness of basic research or product development for the firm. Several major oil companies are currently concentrating on basic research in order to exploit alternative energy sources, while smaller companies are concentrating on product development.

R&D strategy should also guide the flow of the R&D efforts. Should R&D efforts be conducted solely within the firm or should portions of the work be contracted out? Whether R&D should be a centralized or a decentralized function? The R&D functional strategy should address these questions.

Strategy in the area of R&D can be either offensive or defensive. or a combination of both. An offensive strategy emphasizes technological innovations and new product development as the basis for the firm's future success. But this strategy has high risk inherent in it, because innovation and commercialization need a combination of considerable technological skill forecasting expertise and the ability to quickly transform basic developments into commercial products. A defensive strategy emphasizes the modification of the product and the ability to copy or acquire new technology to maintain a firm's position in the industry.

A firm with technological leadership employs a combination of offensive and defensive R&D strategies. DuPont in the chemical industry, GE in the electrical industry, and IBM in the computer industry, al1 have defensive and offensive R&D strategies for products in the market and products under long-term research

PRODUCTION/OPERATIONS

Production/Operations Management (POM) is a core function in the organization. The process of converting inputs (raw material. supplies. people and machines) into value enhanced output is important in all types of firms whether in manufacturing, services or retail business.

Functional strategies in production and operations management cover: (i) Basic input-output relationships and their optimization and (ii) Factors affecting production in the short-term such as, location, facilities, design and process planning. POM strategy is the basis for decisions regarding equipment replacement plant location, plant size and manner of utilization of facilities. These decisions should be in tune with the grand strategy and other operating strategies. For example, in the mobile home industry, Winnebago's plant and equipment strategy entailed one large, centralized production center (in Iowa) located near its raw materials with modernized equipment and a highly integrated production process. Fleetwood Inc opted for decentralized production facilities located near markets where it emphasizes maximum equipment life and less integrated labor intensive production process.

The POM strategy should also provide guidelines for the purchase function. From a cost perspective, the company should ensure that it does not depend on few suppliers for raw materials because these suppliers can take advantage of the situation to sell the raw materials at higher prices. What criteria and payment requirements should be used in selecting vendors? In what way and how should purchases be made in terms of volume and delivery requirements to support operations? Providing broad answers to these questions will help to draw up functional strategy guidelines. These guidelines improve the implementation process and contribute to the success of the grand strategy.

The POM strategy must ensure that production operation processes are geared up to meet demand efficiently. A bathing suit manufacturer should maintain a high level of inventory before the summer holiday season but not before the rainy season. A POM strategy addresses such issues by working out answers to the following questions:

- What is the appropriate inventory level? What purchasing procedure and level of quality control should be established?
- What is the trade-off in emphasizing cost versus quality in production/ operations?
- How far ahead should the firm schedule its production and lure personnel? How much time should it set aside for guaranteeing deliveries?
- What criteria should be followed in adding or reducing equipment, facilities, shifts and people?

If the demand is less cyclical, a firm might maintain a uniform level of production and inventories. Many firms subcontract production in order to handle sudden increases in demand without the problems of idle capacity in slack periods and high capital investment.

If the firm is to succeed, POM strategies must be co-ordinated with marketing strategy, financial strategy, and human resources strategy.

PERSONNEL/HUMAN RESOURCES

The strategic importance of functional strategies in the area of personnel management is now widely accepted. Personnel management contributes to the successful implementation of the grand strategy of the company by nurturing managerial talent, managing compensation and motivating employees. Functional strategies in the personnel department are aimed at the effective utilization of human resources in achieving the annual objectives of the firm and bringing satisfaction to employees. These strategies cover 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 requirements, and
- Discipline and control.

The operating strategy for recruitment, selection and orientation is the basis for personnel managers' decisions. It helps attract and retain motivated employees, who are productive for the organization. It covers the following questions:

- What are the key human resource requirements for the grand strategy chosen?
- How should the company recruit to meet these needs?
- How sophisticated should the selection process be?
- How should new employees be introduced to the organization?

The broad answers to these questions should be provided by the recruitment, selection and orientation component of personnel strategy.

The new recruits required to meet the future, human resource needs in accordance with the grand strategy should be provided for by developing appropriate training facilities. A major brokerage firm, Merrill Lynch, has a long-term corporate goal of becoming a diversified financial service institution in addition to handling stock transactions. For this purpose, the firm has devised extensive early career training and ongoing career development programs to meet its expanding needs for personnel with multiple competencies.

Functional strategies for personnel management are the basis for decisions pertaining to compensation, labor relations, discipline and control, to enhance the productivity and motivation of the workforce.

The following questions are relevant in achieving these objectives:

- What are the standards for promotion?
- How payment, incentive plans, benefits and seniority policies should be laid out? Should there be luring preferences?
- What are the appropriate disciplinary steps for various types of undesirable behavior?

These are the areas in which specific personnel decisions have to be taken by managers.

Thus, on the whole, functional strategies are considered to be important because they provide specific guidelines to enable each major sub-activity to contribute to the implementation and accomplishment of the grand strategy.

STRUCTURAL CONSIDERATIONS

An organization is essential, if strategic purpose is to be accomplished. Thus, in implementing a carefully formulated strategy, organizational structure is a major priority. The structure is left to evolve on its own activities and responsibilities, and interrelationships are not organized in a manner that is consistent with the strategy chosen. If there is no co-ordination between the structure and strategy then the result will probably be inefficiencies, misdirection and fragmented efforts.

As the business evolves, the need for structure becomes apparent. Organizational structure is relatively simple in small firms where one person manages current operations and plans for the future. Owner managers have no organizational problem until their hurried trips to the plant, late night sessions assimilating financial information from their accountants, and pressed calls on potential customers are inadequate to meet the demands of a business's increasing volume. As the magnitude of business activity raises, the need to subdivide activities, assign responsibilities and provide for the integration and co-ordination of the new organizational parts become very much essential.

A structure is basically a simple concept that means the division of tasks for efficiency and clarity of purpose and co-ordination between the interdependent parts of the organization to ensure organizational effectiveness. The need for specialization with the need for integration is balanced by the structure. The formal means of decentralizing and centralizing consistent with organizational and control needs of the strategy is provided by the structure.

Structure is not the only way for getting "organized" to implement the strategy. Few examples that should be employed are reward systems, planning procedures and information and budgetary systems. These elements operate interdependently in the day-to-day implementation of strategy with the formal organizational structure to shape how things are done. The internal efficiency and overall effectiveness within a broader environment is balanced through structure that strategists attempt. There are five basic types of structural choices that are currently used by most business firms:

i. Simple,

ii. Functional,

iii. Divisional,

iv. Strategic business unit, and

v. Matrix.

Simple and Functional Organizational Structures

The simple structure prevails in the smallest business enterprise. All strategic and operating decisions are under the control of the owner-manager. The entire responsibility is vested in the hands of the owner manager but if any bad decision is taken, it could seriously threaten continued existence. Simple structures encourage employee involvement in more than one activity and are efficacious in businesses that serve a localized simple product/market. This structure is beneficial for certain range of volume but as the volume increases, the owner-manager has to give more attention to formulate suitable strategies.

Functional structure generally exists in the firms which concentrate on one or few related products/markets. The grouping of similar tasks and activities, viz., production/operations, marketing, finance/accounting, research and development as separate functional units with the organization is done by functional structures. This specialization encourages greater efficiency and refinement of particular expertise and also allows the firm to promote distinct competencies among the functional areas. Expertise is critical to single product/market companies and to firms that are vertically integrated.

The effective co-ordination of the separate functional units is the strategic challenge in the functional structure. The technical expertise which is narrow, sought through specialization can lead to limited perspectives and different functional units. Specialists begin to see the firm's strategic issues based on their functional area such as marketing, finance, production etc., without understanding the problems of other functional areas. This creates a problem for the top management in the effective implementation of the strategy using the functional structure in order to enhance the co-ordination and to facilitate understanding across functional areas, integrating devices such as project teams or planning committees are frequently used in functionally organized businesses.

Divisional Organizational Structure

The firm covers broad geographic areas when it diversifies its product and service lines. As the product/service lines diversification leads to the utilization of unrelated market channels or begins to serve distinctly different customer groups, a functional structure rapidly becomes inadequate. For example, functional managers may end up overseeing the market or production of numerous and different products or services. Further, the top management must co-ordinate these activities, but they are beyond the capacity of a functional structure which may create some problems in efficient strategy formulation. So, in order to meet the co-ordination and decision-making requirements resulting from increased diversity and size, some form of divisional structure is essential.

Days Inn's strategy in the year 1970s expanded via new geographic markets, required it to more to a divisional structure from a functional structure with three geographic divisions. Each division manager had major operating responsibility in the geographic region in which he operates for the company owned properties. Based on different customer groups, IBM has adopted a divisional organization. The classic divisional structures organized by product groups were adopted by Ford and General motors for many years.

A divisional structure helps the corporate management to delegate authority for the strategic management of a distinct business entity. Help the progress in critical decision-making within each division in response to different competitive environment, and compels the corporate management to stress upon corporate level decisions. The profit responsibility is usually given to the semi-autonomous divisions. Thus, accurate assessment of profit and loss can be done with the help of divisional structure.

Strategic Business Units

Some firms find it difficult in controlling their divisional operations because of the increase in diversity, size and number of divisional units. So, it becomes a tough task for the corporate management to evaluate and control its numerous, to improve strategy implementation, promote synergy and gain greater control over the diverse business interests, it may become essential to add another layer of management when corporate management finds difficulty in managing the organization. This can be successfully achieved by grouping various divisions in terms of common strategic elements. These groups commonly called strategic business units and are usually structured based on the independent segments of the product/market served by the firm.

General Electric, faced with massive sales growth but with little profit growth, was considered to be a leader in the Strategic Business Units (SBU) organization. Over 48 divisions into six SBUs were restructured by General Electric. For example, three separate divisions making food preparation appliances were merged into a single SBU serving the house wares market. General Foods restructured along menu lines after originally defining SBUs along product lines. SBUs allowed General Foods to target specific markets for breakfast foods, beverages, main meals, desserts and pet foods.

Matrix Organization

In large companies, increased diversity leads to numerous product and project efforts, all with major strategic significance. So, there 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 contracts, construction companies and large firms, has increasingly been used to meet this need. The companies such as 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. Essentially, subordinates are put into basic functional area as well as in project or product manager. The matrix form has the combined advantages of both functional specialization as well as the product specialization.

The number of middle managers gets increased with the help of matrix structure exercising general management responsibilities and broadens their exposure to organization wide strategic concerns. Thus, a varied and changing project, product/market is accommodated by matrix structure and it can increase the efficient use of functional specialists who otherwise might be idle.

In order to implement an international expansion strategy focusing on both geographically different financial service requirement and at the same time targeting the multinational corporation market segment, Citicorp used the matrix organization. The change was designed to increase the priority given to large organizations. Through this strategy, the Citicorp ultimately got the better understanding of financial needs and activities of multinational corporations. Citicorp could gain a competitive advantage by using matrix structure as a strategic tool.

The matrix structure is easy to design but it is difficult to implement, as it is said that no system is perfect in the world.

Misunderstanding and confusion among the subordinates are created through negotiating shared responsibilities, use of resources and priorities. Some firms are using a temporary or flexible overlay structure in order to overcome the deficiencies that might be associated with a permanent matrix structure and to complete a particular strategic task successfully. This approach is followed recently by General Motors, IBM and Texas Instruments. Thus, the basic idea of matrix structure is 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.

THE ROLE OF STRUCTURE: LINKING STRUCTURE TO STRATEGY

The structure is considered to be the best, based on the strategy of the firm. The key activities and resources of the firm are tied together by the structural design. Therefore, it must be closely aligned with the needs/demands of the firm's strategy.

A landmark study in understanding the choice of structure as a function of strategy is provided by Alfred Chandler. Over an extended time period, Chandler studied large corporations and found a common strategy-structure sequence.

i. Choice of new strategy.

ii. Emergence of administrative problems; decline in performance.

iii. A shift to an organizational structure more in line with the strategy's needs.

iv. Improved profitability and strategy execution.

The recent history of General Electric supports Chandler's thesis. In the late 1950s, General Electric was operating with a simple divisional structure and embarked on a broad diversification strategy. GE experienced impressive sales growth in 1960s. However, GE also experienced administrative difficulties in trying to control and improve the corresponding lack of increase in profitability. GE executives redesigned its organizational structure in the early 1970s, to accommodate the administrative needs of strategy, subsequently improving profitability of and control over the diversification strategy.

Chandler's research and GE example allow us to make four important observations. Firstly, in implementing strategy, all forms of organizational structure are not equally effective. Second, in larger organizations, in particular, structures seem to have a life of their own. As a result, the need for immediate and radical changes in structure is not immediately perceived. Once the needs are perceived, lagging performance may be necessary before politically sensitive structure is changed or organizational power redistributed. Thirdly, sheer growth can make restructuring essential. Eventually, as the firms diversify into numerous related or unrelated products and markets, structural change is necessary for the efficient performance of the firm.

Research on corporate stages of development provides further understanding of the structure and strategy relationship. After conducting studies on numerous business firms, researchers concluded that the companies move through several stages as size and diversity increase. For competing effectively at different stages, they require different structures.

Again, the choice of structure appears contingent on the strategy of the firm in terms of size, diversity of the products/services offered and the markets served. This is illustrated by two firms in metal container industry. The divisional structure is employed by the industry leader named Continental Can. This is used to implement a diversification strategy intended to serve virtually every user of metal containers, as well as to compete in related markets like forest products. The modified functional structure is employed by crown, cork and seal, the industry's fourth largest company, to serve a limited domestic and international market of users with specialized container needs. Both firms are successful. The maximum revenues from the same industry are derived by both of them. But the organizational structure employed by each of them is different because of their varied strategies.

ORGANIZATION STRUCTURE AND SYSTEMS

Most organizations have structures that have emerged overtime rather than resulting from deliberate attempts to design the ideal organization. These emerging structures must be efficient to maintain the growth of organization. Due to the lack of ideal structure all firms suffer from weaknesses and problems that derive from the way people are organized. For example, most firms adopt a functional structure as they grow. This type of structure gives us the benefits of having specialists in sales, production, engineering, personnel – but there are disadvantages that can stem from this form of specialization.

i. Different functions tend to have different ways of seeing the world. This leads to communication problems and can make it difficult to get all parts of the firm pulling in the same direction.

ii. Each function has its own priorities, and these priorities can bring it into conflict with other functions (for example, Production prefers long runs of the same product sales like to offer customers flexibility and variety).

iii. Over time, these two combine to set-up walls between functions that make it difficult to achieve co-ordination and communication across the organization.

Structure can influence the strategy of the firm particularly where one function tends to dominate the senior management positions. For example, in the strategic apex, if the professionals are the process engineers, then they give excessive concern to the capacity expansion and process innovation, which might be out of line with the needs of the buyers. Some organizations which are excessively rigid impede flexibility and can suppress creativity and initiative. Some firms adapt their strategies over time but they do not readjust their structure to match the new strategy. For instance, consider a firm that grows through the success of a single product. The firm then introduces new products in the same broad market to sustain the past growth rate, finally leading to a highly expanded multi-product firm. What tends to happen to the structure during the phase of expansion and product diversification is as follows:

i. The early phase of rapid growth is coped with through an informal structure, with little specialization.

ii. This is followed by a professionalization of the firm as the need for systems and specialists becomes essential to cope with the expanding size of the business. Typically, functional specialization emerges in finance and accounting, production, administration and sales.

iii. The problems arise when firms stick with this functional structure as they become increasingly large and diverse. As more people join, the number of management level increases, resulting in communication problems up and down the hierarchy. Functional goals tend to leave no-one looking after the needs of a particular product or customer, people just do their bit and pass it on to the next department.

Co-ordination is a must in the organization for a smooth functioning. But, if the co-ordination is lacking in the large functional structure across the organization, the company's performance will get disturbed. There are number of ways of tackling this problem.

i. Break the firm up into smaller business units that can focus on particular products or markets.

ii. Introduce staffs who are responsible for co-ordinating activities across the functions (product managers, project leaders).

iii. Formalize the role of the Product/Project managers in a matrix structure.

Generally, most management avoids structural change. Uncertainty, anxiety and resentment is created if it is badly managed. As a result, reorganization is not only delayed but when it does occur managers tends to opt for structures that have already been tried elsewhere.

The implementation of strategy can be helped or hindered by the systems. In some government offices staff at lower levels have to get approval from higher authorities for taking trivial decisions. If you grow up in this type of structure you are unlikely to feel comfortable about taking responsibility and exercising initiative.

Structure and Style of Management

The management perceptions of the world change according to his or her background and experience. So, the awareness of the limitations of the individual manager and the management team should be known before injecting some analysis and structure into the strategy-making process.

Take, for example, the manager's views of the competition. These will be influenced by a whole host of factors, including comments made by customers, ex-employees, other managers, and by their advertisements, reported performance as well as rumors that move around in the industry. The interpretation of this information should be well done in the management team to fit a well-accepted, shared stereotype of a particular competitor. This could be based around some collective past experience where the firm either 'won' or 'lost' some battle with the competition. For this, effective management style is essential.

In some organizations predominant management style is found. Thus, style gets reinforced where firms generally promote from within. Along with the shared values, the style also plays a vital role in the strategy formulation, but in some firms the domination of one style can lead to problems. Consider the large mass production firm which has an operating core comprising hundreds of staff doing routine, repetitive jobs. Autocratic style prevails in many of these organizations. In some organizations there may be the benevolent autocratic style, in others it is expressed in the form of rather more unsavory, authoritarian regimes.

The autocratic style in many respects is suitable in the particular requirements of the mass-production firm. The decision-making is centralized by this style and it helps to reinforce discipline on the shop floor. In some situations this style becomes very effective. The problems arise when this style enters into other parts of the organization where it is not appropriate, for example, the R&D department. Here it can be counter productive in case conflicts, resentment etc., are created, and generally it demotivates highly skilled staffs who prefer to be managed in a less interfering way.

A question arises that how do you preserve islands of consultative management style in a sea of authoritarianism? Though participation is the correct style, there are great pressures to manage it efficiently. The pressures come from colleagues, bosses and staff in this type of style.

Therefore, top management should carefully analyze as to which style suits the best to the organization in order to achieve the organizational effectiveness.

The Role of General Managers

The general manager is the catalyst in strategic management. The individual is most closely identified with and ultimately accountable for a strategy's success. General Managers spend upto 80 percent of their time developing and guiding strategy. This is followed mostly in larger firms.

In strategy implementation, the nature of the general manager's role is both symbolic and substantive. This individual's actions and the perceived seriousness of his or her commitment to a chosen strategy, particularly if the strategy represents a major change exert a significant influence on the intensity of subordinate managers commitment to implementation.

Secondly, the personal goals and the values of the General Manager influence the firm's mission strategy and key long-term objectives. During the implementation of strategy, the General Manager represents an important source for clarification, guidance and adjustment. The general manager invests his time and personal values in choosing an appropriate strategy.

Research has concluded that a successful turnaround strategy will require almost without exception either a change in top management or a substantial change in the behavior of the existing management team. Clearly, successful strategy implementation is directly linked to the unique characteristics, orientation and actions of the General Manager.

Resource Management and Control

If strategies are to be implemented and objectives are to be achieved, then the allocation of resources has to be planned. The principle of resource allocation is applied at every level in the organization. It is obvious that the strategic leader plans the overall strategy, but at the lower levels of the management hierarchy, the allocation of time, raw material, personnel etc., is planned as part of a continuous scheduling activity. These plans are basically statements of intent. Thus, strategies are implemented when resources have been allocated and used. The work of individual salespersons and shop floor workers is affected by strategic decisions. It is, therefore, important to ensure that daily activities are directed by the strategy.

Resources are mainly allocated through the budgeting process. The manner in which the resources are controlled depends on the rigidity of the policy in question. Control mechanisms are required to evaluate whether the resources are being allocated according to the plan. Control mechanisms are also required to find out whether the plans and actions are efficient and effective, and enabling the organization to achieve its objectives.

CORPORATE RESOURCE PLANNING

Corporate resource planning relates to the allocation of resources between various parts of the organization together with corporate investment decisions concerning the acquisition of additional resources. If investment funds are limited, their allocation will be based on the strategic importance of the various spending opportunities. Also, the financial evaluation of the viability of each project has to be considered. If funds are not available, they need to be borrowed to finance the projects. In such a case, the return on investment should exceed the cost of capital. Companies should seek the best possible returns from investments because they may be seen as undesirable but necessary freezing of corporate funds. Sometimes, managers see investments as a reflection of status, especially if they are invested in new plant and technologically advanced equipment. In this case, there would be a sub-optional allocation of corporate resources.

The organization structure forms a basis for the allocation of corporate resources. If the organization is multi-divisional, the extent of decentralization will determine the freedom that is given to general managers to allocate resources amongst their functional managers and departments. If the power to change strategies is delegated, authority is required to change resource allocations. For instance, if directors delegate the authority to change a particular strategic move to the General Manager of the company, the General Manager should also be empowered to change the allocation of resources accordingly. This implies moving resources within the General Manager's area of responsibility. Sometimes, additional resources need to be acquired from outside the organization. In such cases, the resources must be allocated to those areas that are most significant in the creation of competitive advantage. If strategic resources are located centrally, but are used by various divisions, then their effectiveness needs to be carefully monitored. The resources should be allocated to the areas in which they can yield the most benefit for the organization.

Corporate Resource Planning and Organizational Growth

Resource allocation at the corporate level is closely tied to the planning system. The corporate resources may be allocated in different ways, in line with the degree of stability in the environment and the speed of growth in the organization. The various factors to be considered are:

RAPID GROWTH

Where the business is growing rapidly, the resource allocation process must be able to accommodate the continual demand for additional resources. The resource allocation process could be centralized, decentralized or both. If it is centralized, the head office will establish priorities. In a decentralized approach, priorities would be decided centrally, but after allowing all divisions and business units to formulate their own preferred strategies. In any case, the decisions should balance the potential financial gains with the strategic logic implied. Moreover, when business units make individual requests for resources to support certain programs, the opportunities for synergy, sharing activities and transferring skills across activities should be assessed.

LIMITED CHANGE AND STABILITY

Where businesses are growing more steadily and in a relatively stable environment, resource allocation for continuing programs could be a straight-forward extrapolation of previous budgets. The basic premise is that strategies without evaluation and proper review may be ineffective.

DECLINE SITUATIONS

When business units/businesses are in decline stage, the strategic leader must search for new opportunities for re-deploying resources. If certain business units are experiencing decline, resources should be transferred to activities with better growth and profit potential, unless there are opportunities for turnaround.

Once resources are allocated to divisions, they would be further allocated to individual managers within each area. This allocation will be delegated to the general manager or functional manager in charge of each division or function.

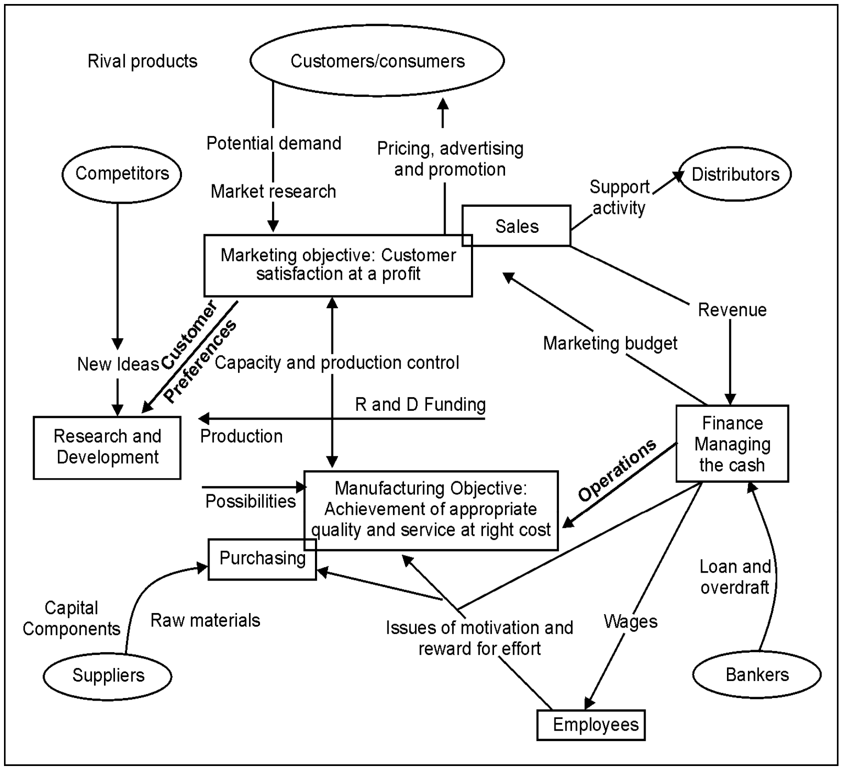
FUNCTIONAL RESOURCE PLANNING

When resources are allocated to functions or to particular activities within functions, it is important to consider the relative importance of each function. Due to the competitive advantage offered by functional activities, an appreciation of the key success factors and competitive opportunities is crucial if the resource allocation is to lead to strategic effectiveness. Also, the important linkages between functions, which are the sources of potential synergy, should be considered. The sharing of resources should be ensured so that the necessary resources are available before implementing competitive strategies.

Functional Interrelationships

The development of any new venture has to be planned in detail. Time, money and other resources have to be allocated to the project. Market research must also be undertaken to assess the potential demand for the new product and assess its viability. The principle of functional links is illustrated in Figure 1. The figure features the various organizational functions in rectangles and external stakeholders in ovals. Lines with direction indicators indicate the flow of information, money and resources.

Figure 1: Functional Inter Relationships



Source: John L. Thompson, Strategic Management Awareness and Change (Chapman and Hall, 2nd Edition) 673.

When developing functional interrelationships, a decision has to be taken concerning the amount of money and time and the staff and facilities that should be allocated to the particular project. After the development of the project, a marketing budget is required to finance the necessary test marketing. If the test marketing proves successful, the venture is handed to the production department. They will be in charge of producing the products with quality standards, and within certain cost constraints. Then an advertising and promotion campaign would be required for launching the product. Finally, the necessary distribution network has to be established. All these activities must take place before the product is able to earn any revenue.

For developing new products, it is necessary to set priorities between established and continuing products and services. Also, appropriate allocation for the development of “tomorrow’s products and services” should be established. For instance, most corporates develop new products in their existing divisions. Ultimately these new products may see the light through the creation of another division with its own resources being allotted and transfer of such new product development research findings. For example, ITC diversified itself into many new products from its own core existing divisions. Later, such new products were launched into the market by the creation of new divisions with their own resources to form a new business unit.

Efficiency and Effectiveness in Resource Allocation and Management

Efficiency and effectiveness measures in relation to the allocation, and deployment of resources should be considered. The way in which resources are employed and managed in the production and marketing of existing products and services has to be examined. Based on the feedback of the examination, necessary improvements can be identified. For example, savings in time and cost (without compromising on quality) lead to higher productivity and higher profits. This leads to freeing up of resources, which can be deployed elsewhere. This is essentially a search for greater efficiency.

The management should also consider whether resources are being allocated to those products and activities that are most important for the organization as a whole and for the achievement of organization’s objectives. If resources are finite and limited to an extent, then choices have to be made giving priority to those products that generate higher revenue for the organization. If growth or profitability, or both, are important objectives, resources should be allocated to those products that best fulfill the organizational objectives. However, sufficient resources should be allocated to development programs that will lead to growth and profits in the future.

Policies, Procedures and Budgets

A policy is a general guide that specifies the broad parameters within which organizational members are expected to operate in pursuit of organizational goals. Policies provide general boundaries for action, but they do not dictate exactly the actions that should be taken. Policies frequently spell out important constraints. For example, retail stores generally have a policy requiring that returned merchandize should be accompanied by a sales receipt.

Policies guide either thoughts or actions, or both, by indicating what is expected by the managers in certain decision areas. Over time, policies place constraints upon the decision-making freedom that managers have by establishing the way that certain tasks should normally be carried out. The process of strategy formulation is a planned activity, but managers at times wish to pursue objectives that are personally important to them. Therefore, policies should be related to stated strategies but, at the same lime, they should not restrict managers to the extent that they are unable to make adaptive changes, when such changes are appropriate or necessary. Policies need to be written down and formulated.

Policies may emerge out of certain behavioral patterns. For example, a policy can exist simply because that is how something has always been done. Sometimes, policies can be advisory, leaving the decision-makers with some flexibility. On the other hand, they can be mandatory, whereby managers have no discretion. Mandatory policies tend to stop the efficient and effective thinking of managers and employees. Moreover, mandatory policies are unlikely to motivate managers. Therefore, advisory policies should be preferred because it is essential to allow managers some flexibility in order to adapt to changes in the organization and environment. Thus, policies should guide rather than remove discretion.

The Creation and Use of Policies

Policies can be created both consciously and unconsciously. The main stated policies are those that the managers draw up in relation to their areas of discretionary responsibility. The key policies are created by the strategic leader and then filtered down the organization. There should be consistency between the policies created by the general manager and those created by the divisional or functional managers. Sometimes, external stakeholders force certain policies on the company. For example, the government may set a policy of safety at work that would affect an organization’s personal policies. In certain circumstances, powerful shareholders or bankers can dictate financial policies.

The major functional areas of the business should be covered by explicit policies. All employees who will be affected by them should know such policies. Explicit policies provide a clear framework in which decisions can be made. They also allow people to understand the behavior patterns that are expected of them in particular circumstances. Lastly, changes in strategies may require changes in policies to be implemented successfully.

Principles of Good Policy

The potential effectiveness of policies in relation to strategy implementation is determined by the following principles:

- **Policies should Reflect Objectives:** Policies are justified only if they lead to the achievement of a company's objectives. Policies should be reviewed from time to time and assessed whenever strategies are changed in any significant way. Policies that have evolved unconsciously may have a negative impact on the objectives, making them harder to achieve.
- **Policies should be Consistent:** An organization's policies should be consistent and conflicting policies should be avoided. For instance, in most organizations there are clear-cut rules and regulations leading to policies in the area of human resources, i.e., employee designations, employee levels in the hierarchy, compensation slabs, etc.
- **Policies should be Flexible:** Policies exist to provide consistent guidelines to the decision-making process. They advice managers how to behave in particular circumstances. Regular reviews and changes in policy (when necessary) will provide the appropriate flexibility in a turbulent environment. Policies become unhelpful if they are seen as mandatory and inflexible when there is a clear need to make changes.
- **Policies should be Communicated, Taught and Understood:** The formulation of policies does not guarantee that they are followed and that the desired strategies are implemented. The policies should be communicated to the employees so that they understand the existence and meaning of policies. Only then will they be more closely tied in with the performance objectives.
- **Policies should be Controlled:** Stated policies can be assessed and controlled during any strategic review. But the evaluation may fail to take the non-stated policies into account.

Procedures

A procedure is a prescribed series of related steps to be taken under certain recurring circumstances. Well-established and formalized procedures are called Standard Operating Procedures (SOPs). In other words, a procedure is a type of plan designed to establish the steps that employees should follow when carrying out certain routine tasks. A well-conceived and straightforward procedure ensures that the necessary action in certain circumstances is clear to everyone. Such procedures can also provide a useful control mechanism. Procedures provide detailed, step-by-step instructions as to what should be done. For example, banks typically have procedures that govern how tellers handle deposits. Therefore, they do not allow much flexibility or deviation.

Budgets

A budget is a financial plan listing the resources or funds assigned to a particular program, project, product or division. Budgets represent the objectives of the organization in monetary terms. They indicate how much should be spent, by which department, when and for what purpose. Budgets involve the allocation of resources to individual managers who are responsible for the completion of particular tasks. Budgets are assigned to individual products and business units. Unless the future prospects and viability of products and business units are evaluated objectively, budgeting may become more financially oriented than strategic.

ALLOCATION OF RESOURCES

The allocation of resources in an organization requires planning and controlling. To achieve this, the method used by most organizations is budgeting. Budgeting is an instrument for putting plans and policies into effect for the achievement of objectives, thereby functioning as a major vehicle for organizational strategy implementation. The budgeting function generates formal written statements called budgets. Budgets are financial statements of the resources required to achieve a set of finite, short-term objectives, or put into action a formulated strategy. Organizations have several types of budgets that are combined into an overall master budget.

The Budgeting Process

A budgeting process begins with the development of detailed economic, revenue and profit forecasts. These forecasts are designed to meet organization goals and produce guidelines that can be used in budget preparation. Most organizations use a top-down approach. That is, they develop budgets at the top management level and allocate them throughout the hierarchy. But the 'bottom-up' approach to budget development also has many advantages such as:

- Personnel in each department are likely to be familiar with their own needs.
- The supervisors and personnel are more likely to be motivated to accept and meet a budget if they have participated in its development.
- The members of a department are less likely to overlook a factor from their own departments that might prove to be a crucial element in budget development.

Once the preliminary budget proposals are developed by the various departments, they are submitted to a budget committee. This committee reviews the proposals and attempts to reconcile the various budgets to construct a final budget. Thus, budgets represent agreed targets that relate closely to the organization's objectives. Also, individual budgets will be a part of master budget because the objectives of individual managers contribute towards the objectives of the departments, business units, divisions, and ultimately the organization as a whole. Budgets and objectives are clearly related and resources are allocated to those areas in the organization that are seen as priorities. Where resources are available and new developments are being considered, the previous record and contribution of managers is likely to have an influence on the allocation of resources. Furthermore, the ability of certain managers to exercise power and influence within an organization also has an impact on the resource allocation process.

Building Flexibility in a Budget

A serious drawback for many budgets is their rigidity in the face of changing conditions. The budgeting process normally takes place on an annual basis, but as the targets are utilized for regular performance reviews, there should be scope to adjust budgets either upwards or downwards. The allocation of resources to managers is dependent upon the strategies that the organization has decided to continue, but adaptive changes require flexibility that must be accounted for. Thus, budgets should provide a means of adjustment because they are forward looking and changes affect the forecasts upon which they are based. In order to avoid the problem of inflexibility, organizations often develop variable or flexible budgets. A variable budget is a series of different budgets based on different levels of output. Since, expenses and allowances are computed for different levels of activities, department budgets can be adjusted easily by a predetermined formula to reflect more realistically the actual costs related to actual output.

Zero-Base Budgeting (ZBB)

An assumption behind any budget prepared is that this year's budget is a reasonable starting point for next year's budget preparation. This assumption inhibits the relevance of many activities within the organization. The elimination of this assumption is the essence of Zero-Base Budgeting. Zero-Base Budgeting is a forced periodic justification of any expenditure program in which each department calculates its resource needs based on next year's priorities rather than on last year's budget or expenditure patterns. With zero-base budgeting, no previous experience is assumed, and every proposed activity must be justified afresh. ZBB requires that objectives and priorities be reviewed in every budgeting cycle. In the first step of ZBB, managers justify each item in their budget, as if they were proposing a completely new project. The second step requires the evaluation and ranking of all activities to benefit the organization, followed by the actual allocation of resources based on the final ranking.

Zero-base budgeting is conceptually very attractive, as it distinguishes between low and low priority areas and contains the pursuit of personal objectives by managers. However, the implementation of ZBB presents a number of difficulties, which often results in a preference for traditional budgeting. Thus, it can be concluded that a zero-base budgeting process provides greater justification for the continuation or termination of activities and allows greater participation in planning. However, the process is more costly and requires more time to complete.

STRATEGIC CONTROLS

The need to measure and evaluate performance and make changes exists in all levels of the organization. According to Henri Fayol, control consists in verifying whether everything occurs in conformity with the plan adopted, the instructions issued and principles established. The objective of control is to point out weaknesses and errors in order to rectify them and prevent recurrence. The control function includes three procedures. They are:

- Measuring actual performance,
- Comparing actual performance to standards, and
- Taking corrective action to ensure that planned events actually occur.

ESTABLISHING STRATEGIC CONTROLS

Strategic control focuses on monitoring and evaluating the strategic management process to ensure that it moves in the right direction. In other words, strategic control is concerned with tracking the strategy when it is implemented, detecting problems or changes in underlying premises, and making necessary adjustments. Strategic control answers questions such as:

- Are the organization's internal strengths still holding good?
- Are its internal weaknesses still present?
- Has the organization added other internal strengths?
- Does it have other weaknesses?
- Are there new opportunities?
- Do the threats to the organization still exist, and are there any new threats?
- Are the decisions consistent with the organizational policy?
- Are there sufficient resources to achieve the objectives?
- Are goals and targets being met?
- Are the organizational vision, mission and objectives appropriate to the changing environment?

Thus, strategic control provides feedback about the various steps of strategic management. It enables tile management to find out whether the strategic management process is appropriate and compatible with organizational goals and whether it is functioning in the desired direction. Sometimes, strategic controls may initiate changes in objectives as well.

Premise Control

Premise means an assumption. Every strategy is based on some assumptions. A firm's strategy is built around these assumptions. Premise control helps to check, systematically and continuously, whether or not the assumptions set during the planning and implementation process are still valid. If a premise or an assumption is no longer valid, then the strategy is changed along with the assumptions. Premises are primarily concerned with two types of factors. They are:

- **Environmental Factors:** Environmental factors have a considerable influence on the success of a strategy. Examples of environmental factors are inflation, technology, interest rates, government regulation, demographic/ social changes etc. A company has little or no control over such factors and strategies are usually based on key premises about these factors.
- **Industry Factors:** Industry factors affect the performance of companies in a given industry. Strategic assumptions are made about factors such as competitors, suppliers, substitutes, barriers to entry etc. These factors differ from industry to industry. So a company should be aware of the factors that influence success in the industry in which it operates.

Various premises are made about numerous industry and environmental variables. Tracking every premise is expensive and time-consuming. So managers should select only those premises that are likely to change and those that are likely to have a major impact on the company and its strategy. After the key premises are identified, they should be monitored, and responsibility should be assigned to the persons/departments who arc qualified to provide information. Premises should be updated, on the basis of new information. Finally, key areas of the strategy that are likely to be influenced by the changes in assumptions should also be identified. For example, senior managers have to be aware of changes in a competitor's pricing policies. This is required so that they can bring about necessary changes in their own pricing or other types of strategies. In the same way, managers have to be aware of technological changes such as the growth of the internet, which has enabled many companies to market their products internationally without even knowing their customers. Awareness and willingness to change can help create strategic advantages for the organization.

Implementation Control

The action phase of strategic management consists of a series of steps, programs and moves undertaken over a period of time to implement the strategy. In this phase, managers undertake programs, add people, and mobilize resources. In other words, managers translate broad strategic plans into concrete actions. These actions act as goals for specific units and individuals as they go about implementing the strategy. These actions take place over the intended period of time and are designed to achieve long-term objectives.

The strategic control undertaken within this context is known as implementation control. Implementation control determines whether or not the overall strategy should be changed, in light of unfolding events, and results of incremental steps and actions. There are two types of implementation control: monitoring strategic thrusts, and milestone reviews.

- **Monitoring Strategic Thrusts:** The implementation of broad strategies involves undertaking several new strategic projects that represent part of what needs to be done if the overall strategy is to be accomplished. Through these projects or thrusts, managers can obtain feedback that helps to determine whether the overall strategy is progressing as planned, or whether it needs to be adjusted or changed.

- **Milestone Reviews:** Managers often identify the critical milestones that will occur over the time period when the strategy is being implemented. These milestones may be critical events or major resource allocations. A milestone review involves a full-scale reassessment of the strategy and the advisability of continuing or refocusing the direction of the company. Thus, the critical purpose of a milestone review is to undertake a thorough review of the firm's strategy at a critical juncture, so as to control the direction of the strategy and the company.

Strategic Surveillance

Strategic surveillance is designed to monitor a broad range of events inside and outside the company that are likely to threaten the course of firm's strategy. It is a form of general monitoring through multiple information sources. The specific intent of strategic surveillance is to uncover important, yet unanticipated information. Surveillance must be kept unfocussed as much as possible and should be designed as a loose "environmental scanning" activity. Trade magazines, trade conferences, intended and unintended observations are sources for strategic surveillance. Thus, the purpose of strategic surveillance is to provide an ongoing vigilance of daily operations so as to uncover information that may prove relevant to the firm's strategy.

Special Alert Control

A special alert control reflects the need to thoroughly reconsider the firm's basic strategy based on a sudden, unexpected event. Such an occurrence should trigger an immediate and intense reassessment of the company's strategy and its current strategic situation. Many firms delegate crisis teams to handle the initial response and co-ordination needed when faced with unforeseen occurrences. When unforeseen occurrences have an immediate effect on the firm's strategy, companies develop contingency plans which are put into operation by crisis teams, under such circumstances.

Thus, strategic controls are concerned with "steering" the company's future direction. These are useful to the top level management for monitoring and determining the basic strategic direction of the company.

OPERATIONAL CONTROL SYSTEMS

Operational controls are action controls. Operational control systems help operating managers to implement strategy at their level. These systems help to guide, monitor and evaluate progress in meeting the annual objectives of the company. They provide post-action evaluation and control over short time periods (usually one month to one year). For operational control systems to be effective, the following four steps should be taken:

- Set standards of performance.
- Measure actual performance.
- Identify deviations from standards.
- Initiate corrective action or adjustment.

The three types of operational control systems are budgets, schedules and key success factors.

Budgets

A budget is a plan to show how much money a person or organization will earn and how much they will need or be able to spend. It states planned organizational activities for a given period of time in quantitative terms. Budgets set standards against which action can be measured and include figures such as projected income, expenditure and profits. A budget is simply a resource allocation plan that helps managers co-ordinate operations, and facilitates managerial control of performance. Budgets also provide a basis for negotiating short-term resource requirements to implement strategy at the operating level. Most firms use the budgeting system to control strategy implementation. Though budgets differ from organization to organization, they can be classified into three general types of budgets, i.e., revenue, capital and expenditure.

- **Revenue Budgets:** A revenue budget provides for the daily management of financial resources. It also provides key feedback as to whether the strategy is working or not. A sales budget is one such revenue budget: it gives a formal and detailed expression of the sales forecast. This sales forecast is the cornerstone of planning and also acts as the foundation for budgetary control. Sales revenue budgets give feedback on the effectiveness of a firm's approach. If the deviation is more than expected, managers can re-evaluate and adjust the firm's operational or strategic posture.
- **Capital Budgets:** Capital budgets outline specific expenditure for plants, equipment machinery, inventories and other capital items needed during the budget period. Preparation of these budgets needs great care, as these budgets give a definite form to the spending plans of an enterprise. Cash budgets and balance sheet budgets are often developed to control the use of capital resources along with the capital budget.
- **Expenditure Budgets:** An expenditure budget presents the financial plan for each department during the budget period. The expenditure budget for each functional unit and for sub-functional activities guides and controls the execution of strategy for each function. For example, firms prepare separate expenditure budgets for marketing activities and advertising activities.

Depending on how budgets are used, they can have either positive or negative effects on managerial effectiveness in organizations. On the positive side, budgets keep managers informed about organizational activities and enhance co-ordination across various units. Negative effects arise if the budgets are used in a rigid manner.

Scheduling

Scheduling as a planning tool involves allocation of time and constrained resources, and their arrangement into a sequence of interdependent activities. Scheduling helps managers by providing a plan about when the work commences, when it concludes, in what sequence the work will be accomplished, what part of the work will be accomplished by what time. Clarity in the work schedule ensures a systematic flow of work.

Key Success Factors

Operational managers can ensure control over their operations by focusing on "key success factors". Key success factors identify performance areas that must receive continuous management attention. Some key success factors are:

- High employee morale,
- Improved product service quality,
- Increased earnings per share,
- Growth in market share, and
- Completion of new facilities.

The achievement of these standards is possible only through successful teamwork. Operating control systems require the establishment of performance standards. In addition, in implementing the strategy, managers identify deviations in the strategy, determine the underlying causes, and make corrections to get the most out of the strategy.

REWARD SYSTEMS

The execution and control of strategy ultimately depends on individual members of the organization. Motivating and rewarding good performance are the key ingredients in effective strategy implementation. Based on the organization's strategy, managers decide which behaviors to reward. They create a control system to measure these behaviors and link the reward systems to them. Both positive reinforcements and negative reinforcements are useful in controlling and adjusting performance. Examples of various reward mechanisms for motivating and controlling individual efforts include:

- Compensation,
- Raises,
- Bonuses,
- Stock options,
- Incentives,
- Promotions/demotions,
- Recognition and praise,
- Criticism,
- More (or less) responsibility,
- Performance appraisal, and
- Tension and fear.

These reward mechanisms are either positive or negative, and are employed in both the short run as well as in the long run. Determining how to relate rewards to performance is a strategic decision because it affects the way managers and employees at all levels in the organization behave. For example, top management teams rewarded with stock options may be more entrepreneurial and more concerned with increasing quality and innovation, than those that are not rewarded.

Rewards/incentives are useful for controlling performance when they are directly linked to specific activities and results.

Control through organizational reward systems complements all the other forms of control. Rewards should be closely linked to an organization's strategy, in order to ensure that the right strategic behavior is being rewarded. Moreover, rewards should be so designed that they do not lead to conflicts among functions, divisions or/and individuals. As the organizational structure and the organizational reward system are closely interrelated, they must be compatible if an organization is to implement its strategy successfully.

CRISIS MANAGEMENT

Crisis management addresses certain risks and uncertainties that arise over period of time. Crises can be of different types: accidental (for example, fires and computer failure) deliberate (for example, poisoning scares, contamination of food products). Wherever possible, firms prepare contingency plans to mitigate the effect of these crises. Sometimes, strategic changes, can also lead to a crisis of confidence. For example, rumors that a firm is going to be acquired by some other company might lead to falling sales, reduction of profits etc. Three decisions are important in ensuring that crisis strategy is effective:

- Decisions concerning what can go wrong, the probability of it happening, and the impact it will have if it does happen.
- Decisions about investing in preventive measures, in order to reduce or minimize the risk.
- Decisions on mechanisms for contingency management.

Steps for Managing Crisis

The various steps in the process of crisis management are:

- Identification of the most obvious areas of risk.
- Establishment of policies and procedures to avoid chances of risks becoming crises.
- Identification of trained crisis management team to take care of a crisis situation whenever it arises.
- Stakeholder analysis is another crucial aspect of the process. It is important to identify which stakeholders are most likely to be affected by a particular crisis and how. Where stakeholder perspectives, and expectations differ it may be necessary to deal with each group on an individual basis.
- Formulation of a clear communication strategy is essential. Sometimes, ethical issues may be involved and the company is expected to be co-operative, open, honest and consistent. The company should be in control but should not attempt to cover up its failings.

Overall, an effective information system is required for gathering and disseminating the salient facts. Therefore, crisis management is important from a strategic point of view. Failure to deal effectively with crises can lead to loss of confidence, competitiveness, profits and market share.

SUMMARY

- Strategy formulation, analysis of alternative strategies and strategic choice precede implementation. A strategy must have clear, measurable annual objectives. It is also important that employees from all the levels in the organization are involved in strategy formulation.
- A strategy must have clear, measurable annual objectives. Annual objectives are specific, measurable statements of what an organization's subunit is expected to achieve in the year as a part of the business's grand strategy. Identification and communication of annual objectives that relate logically to the strategy's long-term objectives is a crucial step in the successful implementation of a strategy.
- An annual objective must be linked clearly to the long-term objectives of the organization. The annual objectives should be integrated and co-ordinated; without this the long-term objectives will not be achieved due to the conflicts that arise between the various departments. Annual objectives add breadth and specificity in identifying what must be completed successfully in order to achieve the long-term objectives. Specific annual objectives provide targets for achieving the long-term objectives. They clearly identify the performance requirements of the various operating areas.
- A functional strategy is a short-term game plan for a key functional area within a company. Functional strategies clarify grand strategy and provide more specific details about how key functional areas are to be managed in the near future. There are three basic characteristics which differentiate functional strategies from grand strategies: time horizon covered: specificity; participation in their development.
- Resources are required for strategy implementation and their availability is a determinant of the feasibility of a particular strategic option. In this chapter, we discussed a number of issues regarding resource allocation and control. We began the chapter by discussing corporate and functional resource planning. However, the existence of resources does not guarantee the effective implementation of strategies. The way in which resources are used and managed is also important. In this context, policies, procedures and budgets were discussed.

Chapter XI

Business Strategy: The Road Ahead

After reading this chapter, you will be conversant with:

- Defining Value Chain
- Value Chain and Buyer Value
- Competitive Scope and the Value Chain
- Value Chain and Industry Structure
- Value Chain and Organization Structure
- Change of Strategy and Organizational Change
- Forces and Types of Change
- Resistance to Change
- Strategies for Implementation and Change
- Role of the Strategist
- Global Competitiveness in the New Millennium

Introduction

One cannot predict with certainty what lies in the future in the areas of international business and economic relationships. But one can determine the hazy outlines of future trends when one looks at the several factors that shape international business and social relationships. Global socio-political, technological and economic forces that are under no one's control but affect everyone, constitute one set of factors. Further, business and social relations will be affected by the decisions and actions of sovereign nation-states and international organizations. In addition, the perceptions, choices, and actions of individual managers and their business organizations will shape the future. International managers must equip themselves with an understanding of the interactive power of global trends, national actions, organizational and individual choices, and prepare to face this uncertain future.

A firm derives its value from value addition activities such as designing, producing, marketing, delivering, and supporting activities. Efficiency in one or more than one of these activities can lend either cost advantage or differentiation advantage to the firm. A firm can gain cost advantage from a low-cost physical distribution system, superior sales force utilization, or an efficient assembly process. Similarly, differentiation advantage can be gained by procuring high quality raw materials, having a superior product design, or a responsive order entry system.

THE VALUE CHAIN AND BUYER VALUE

A firm influences the buyer's performance by influencing its value chain. It can do this by providing inputs to the customer. Some times the firm's product influences the buyer both directly and indirectly. For example, a customer wants to buy a typewriter and finds it too heavy. This heavy weight will affect his purchase decision. A firm influences the buyer not only through its product but also through its logistical system, sales force, applications engineering group, and order entry system. Although, the activities of a firm sometimes represent only a fraction of the buyer's total cost, these activities determine the extent of differentiation. Hence, the buyer's value chain is highly dependent the supplier's value chain.

A firm's differentiation depends on how its value chain is related to the buyer's value chain. This in turn depends on the way a firm's physical product is used in a particular buyer activity and also the other points of contact between a firm's value chain and the buyer's value chain. A firm creates value when it creates competitive advantage for its buyer. The competitive advantage can be created in the form of lowering the buyer's cost or raising the buyer's performance.

COMPETITIVE SCOPE AND THE VALUE CHAIN

Competitive scope influences the competitive advantage by shaping the structure and economics of the value chain. It has different dimensions such as segment scope, vertical scope, geographic scope and industry scope.

Segment Scope

Here the emphasis is on the variety of products and the types of buyers. A firm can employ different focus strategies while serving different product or buyer segments. For example, a firm may need a particular value chain to serve sophisticated minicomputer buyers with in-house servicing capabilities and it might need a different value chain to serve small business users.

Vertical Scope

This refers to the extent of activities that are performed in-house. A firm with vertical scope of operations streamlines its value activities between a firm and its suppliers, channels and buyers. A firm can take advantage of vertical linkages without going in for vertical integration by purchasing its components rather than designing them in-house. Although channels perform firm's distribution, service, and marketing functions. A firm might differentiate itself by taking up various buyer activities and in rare cases it might enter the buyer's industry itself. This is an instance of vertical integration.

Opportunities for integration are often more than realized by the firm. Vertical integration may involve replacing supplier products with the firm's own products, and supplier relationships with business unit relationships. For example, a firm might rely on a supplier for its engineering applications and services. or design them on its own.

Geographic Scope

This refers to the range of regions, countries or groups of countries in which a firm operates with a well directed strategy. Geographic scope allows a firm to share value activities across different regions. Canon, for example, manufactures its copiers in Japan and provides sales and services in different countries. Thus, Canon derives a cost advantage by sharing technology development and manufacturing costs across different regions.

Similarly, Monarch, a food service distributor has separate operating units in major cities. These units share the firm's infrastructure, procurement, and other support value activities. These geographic relationships increase the competitive advantage of the firm by lowering costs. However, it is important for firms to consider costs of co-ordination that might nullify the potential advantages.

Industry Scope

This refers to the potential inter-relationships among the value chains required to compete in related industries. Sometimes a firm's value chain might span across different industries. There are potential advantages a firm can gain by operating in various related industries. A firm has to be involved in primary and secondary activities in order to gain these advantages. A firm can gain strong competitive advantage by exploiting interrelationships among its business units. These interrelationships help reduce costs and gain differentiation. Advantages of economies of scale can be realized from a shared logistical system. Similarly, a firm can gain differentiation advantage when the sales force of the firm also handles related products of the firm. This knowledge of related products enhances the effectiveness of the sales force. However, a firm should be careful while sharing activities, because all shared activities need not be effective. Each business unit might have different needs and expectations from a value activity.

THE VALUE CHAIN AND INDUSTRY STRUCTURE

The industry structure also defines the value chain of a firm. The industry structure is a reflection of collective value chains of the players in the industry. Sometimes the industry structure also influences the bargaining relationships with buyers and suppliers that is reflected in the configuration of the firm's value chain and how margins are shared with buyers, suppliers, and coalition partners. Similarly, the threat of substitution to an industry influences the value activities desired by the buyer. Likewise, entry barriers too determine the sustainability of value chain configurations.

On the other hand, the array of industry players' value chain is the basis for most of the elements of industry structure. For example, proprietary learning, and scale economies result from the technology involved in the players' value chains. The capital needed to compete in the industry depends on the collective capital required in the chain. Industry product differentiation too depends on how the products of the firms in the industry are used in the value chains of buyers in the other industry. Thus, one can understand the industry structure by analyzing the value chains of different players' in the industry.

THE VALUE CHAIN AND ORGANIZATION STRUCTURE

As mentioned earlier, a value chain can be used effectively to identify and gain competitive advantage. Similarly, the value chain can also be used for designing the structure of an organization. An organization comprises different departments, each of which performs different functions. However, all these functions are interrelated and interdependent. Organizational structure brings together some interrelated activities under functions such as marketing or production. The purpose behind this classification is to ensure greater efficiency. However, to achieve the intended effectiveness, all these activities must be integrated.

A value chain helps the strategist to identify and classify the various activities systematically. However, functions such as purchasing and R&D contain only a small fraction of the similar type of activities performed in the firm. An organization often consists of many linkages in the value chain and generally, organizational structures are inadequate to co-ordinate these linkages. For example, HR and technology managers are not sure of how their roles contribute to the overall competitive position of the organization. Hence, the need to integrate the various business functions within an organization. By using the value chain, a firm can demarcate its functional boundaries according to its competitive advantage, and make arrangements for proper co-ordination. Thus, an organizational structure that aligns itself with the value chain can ensure enduring competitive advantage to the firm.

CHANGE OF STRATEGY

In today's global environment, change rather than stability is the order of the day. Rapid changes in technology, competition, customer demands have increased the rate at which companies need to alter their strategies and structures to survive in the marketplace. The effect of this change on the organization is gradual, incremental and piecemeal. In other words, some strategies remain as they are, some change slightly, some new strategies are formed and certain old strategies are dropped out gradually. Strategic change is thus, not sudden and dramatic.

During the process of change, minor improvements or deletions in a strategy take place. These little changes are implemented over a period of time because if they are major changes and sudden shifts in strategy, many organizations cannot manage the change. As the sudden shift in the strategy may lead to collapse of the company, strategies need to be formulated. In this chapter we will discuss the issues and problems in the management of change. We begin the chapter by discussing the meaning and nature of organization change.

ORGANIZATIONAL CHANGE

Organization change means any substantive modification to some part of the organization. This means that the change can involve any aspect of the organization. For example, these could be changes in work schedules, span of management, key strategies and so on. Organizations and management face change on a continuous basis (especially in volatile environments). Some changes are reactions to threats, whereas others are proactive attempts to seize opportunities. Organizations that seek to create and sustain competitive advantage should be ready to change and implement the proposed changes. When strategies change, there are accompanying changes in structures and responsibilities, and people are clearly affected. In such organizations, managers and employees should be supportive rather than resistant or hostile.

FORCES FOR CHANGE

Why do organizations change? The basic answer is that either something relevant to the organization has changed or is going to change. Consequently, the organization has to change. The five major forces for change are as follows:

Technical Obsolescence and Technical Improvements

A need for technical change stems up when new developments are made by competitors. Another reason could be that the strategists might wish to harness new technologies. Internal research and development ideas can generate technical change internally. In high technology industries, this is a significant issue because the product life cycles are short.

Political and Social Events

The socio-cultural dimension, reflecting societal values, determines what kind of products will be accepted in the market. Generally, the political and social events are beyond the control of the firms, but they are forced to respond to such events. For example, government's encouragement for protecting environment has forced Chemical and Pharmaceutical Manufacturers to respond.

THE TENDENCY FOR LARGE ORGANIZATIONS AND MARKETS TO BECOME INCREASINGLY GLOBAL

Globalization has provided opportunities and growth for many organizations. But many firms are forced to change so as to respond to the competitive conditions.

INCREASES IN THE SIZE, COMPLEXITY AND SPECIALIZATION OF ORGANIZATIONS

The growth of organizations creates pressure for further changes. Large organizations have started using information technology in their operations, introducing automation and JIT systems. These create a need for greater specialist expertise, training and changes in jobs of managers and employees.

THE GREATER STRATEGIC AWARENESS AND SKILLS OF MANAGERS AND EMPLOYEES

Able and ambitious employees need opportunities for growth within the organization for job satisfaction. This could be in the form of promotion for changes in the scope of jobs. Such changes require strategic development and growth by the company as well.

The Current Dynamics of Change

The competitive forces in an organization determine how proactive and change-oriented an organization must be if it is to be effective. There are several factors that require the organizations to be receptive to the need for change. Such factors are:

- The general dynamics and uncertainty of economies
- *Time horizons:* As product life cycles shorten, the development time for new products must be cut and this requires change.
- *Quality, design and service:* These must be responsive to customer perceptions if firms have to gain competitive advantage.

Though certain common factors are illustrated above, these forces and their relative intensity varies between organizations and industries.

Levels of Change

Change decisions can be categorized in terms of their significance to the organization. The levels of change forms a vertical hierarchy. This hierarchy is needed because it is crucial to clarify and tackle needs and problems appropriately. For example, if the problem is of operating efficiencies, then it has to be dealt at the functional level. Moreover, as one ascends the hierarchy, the challenges and difficulties increase.

TYPES OF CHANGE

Strategic Change is the movement of a company away from its present state toward some desired future state to increase its competitive advantage. The various types of strategic change are re-engineering, restructuring and innovation.

Re-engineering

Re-engineering is the fundamental rethinking and radical redesign of business processes to achieve dramatic improvements in critical, contemporary measures of performance such as cost, quality, service and speed. The strategists who use re-engineering must completely rethink how their organization goes about in its business. In re-engineering, the strategic managers make business processes the focus of attention. A business process is any activity that is vital to delivering goods and services to customers quickly or at low cost. Some examples of business processes are order processing, inventory control or product design.

The organizations that take up re-engineering ignore the existing arrangement of work activities. Such organizations start the change process by asking the customers "How can we reorganize the way we do our work to provide the best quality and the lowest cost goods?" Such companies realize that there are more effective ways to reorganize their activities. Often individual jobs (that become increasingly complex) and people are grouped into cross-functional teams (as business processes) and are reengineered to reduce costs and increase quality.

Therefore, re-engineering adopts a different approach in optimizing its activities. This may be because of drastic unexpected changes in the environment such as emergence of aggressive new competitors or technological breakthroughs, etc.

Restructuring

Restructuring programs involve changes in the relationships between divisions and function. There are two basic steps to restructuring. They are:

- In the first step, the organization reduces its level of differentiation and integration by eliminating divisions, departments or levels in the hierarchy.
- Next, it downsizes by reducing the number of its employees to reduce operating costs.

There are many reasons as to why organizations go in for restructuring. Sometimes, unforeseen changes might occur in the business environment. For example, worldwide recession can reduce the demand for the firm's products. Sometimes, organizations have excess capacity because customers do not want its products. At times, firms on top position restructure to build and improve their competitive position (so that they can stay on top). Also, organizations downsize because over time they have grown too tall and bureaucratic and due to this operating costs increase to a large extent. Moreover, companies are forced to downsize because they have not paid attention to the need to re-engineer themselves. In such a situation, restructuring becomes the only way they can survive and compete in an increasingly competitive environment.

Innovation

Innovation involves the use of a new idea or method. A firm which brings out an innovative product usually enjoys the 'first mover' advantage. This advantage can help it to gain market share and later, economies of scale. Thus, an innovation correctly exploited, can create a strategic advantage for an organization.

Innovation need not be dramatic to bring success to the organization. Even incremental improvements can add significant value to the organization. Launching a new product, entering a different – industry or operating through a new distribution channel, can all be considered innovative. Pepsi, for example, has been innovative in launching new products such as Diet Pepsi, Pepsi One, Diet Pepsi Twist, etc. Similarly, when a tobacco company such as ITC diversifies into a completely unrelated industry such as food, this is considered an innovative move.

Innovation depends on the collective enterprise and expertise of employees. Though organizations are well aware of the need for innovation, their ability to innovate is limited by many obstacles. Complacency with the past success comes in the way of potential innovations. Complacent people prefer predictability and conformity. This preference discourages different ways of thinking. The personal priorities of managers may discourage innovations. Arrogance, a short-term mentality, and the 'expert' syndrome are also the blocks for innovation. Some managers are intolerant of mavericks and significantly adverse to risk – this too discourages innovation in a firm.

Managers in organizations should focus on long-term opportunities, and expect and accept contributions from employees at all levels. They should encourage those who have new ideas, accept bigger risks, and set ambitious goals. Corporate control systems often establish convergent thinking in preference to lateral thinking in their decision-making. Convergent thinking focuses on well-defined problems and suggests time-tested and well-known solutions immediately. This approach has great advantages. However, its use in areas requiring innovation is limited. Lateral thinking, on the other hand, stresses the importance of change, and movement in a non-linear direction. Convergent thinking or vertical thinking moves step by step; by taking the right step each time, a solution is reached. In contrast, lateral thinking takes into consideration a lot of information that appears irrelevant to the problem at hand. This approach is similar to that employed in brainstorming sessions. In brainstorming sessions, irrational ideas are never discouraged because irrational ideas can lead to brilliant ideas. Innovations demand such a flexible approach.

Creativity and risk taking are important prerequisites for any innovation. Creativity needs paradigm shifts. Shifts in thinking are difficult to achieve. Changing the pattern of thinking involves risk. In some cases, managements' inflexibility itself is an obstacle to changing the way people think.

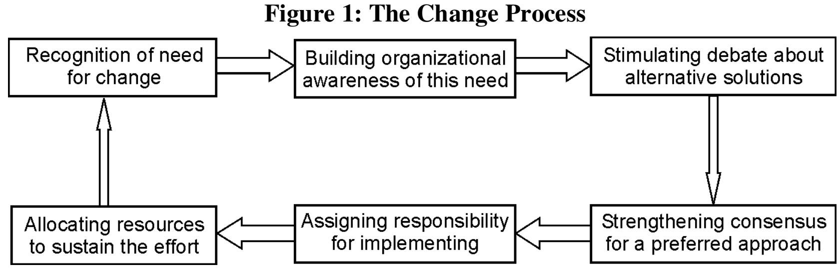
Innovation is a result of creative action or thought or both. Creativity is the ability to develop new ideas. However, in organizations, creative ideas are hardly ever encouraged because these ideas threaten the status quo. A concerted effort should therefore be made to encourage creativity.

Co-ordination, productivity requirements and control systems may also undermine creativity in an organization. Organizations should establish systems that encourage creativity in the workplace. The employee's intrinsic motivation should also be kept alive.

CHANGE PROCESS

Change frequently disrupts normality whilst the organization may be facing strong external pressures, it is unrealistic to expect managers and employees not to query or resist the need to change. The change process becomes difficult when individuals perceive that they are losing out rather than benefiting or are not being rewarded for cooperating when managers engage in planned change, they typically follow a process such as the one illustrated in Figure 1.

Figure 1: The Change Process



Change involves actions based on a carefully thought-out process that anticipates future difficulties, threats and opportunities. The various steps in the change process are:

RECOGNITION OF NEED FOR CHANGE

In the first step, the senior management must develop an early awareness of the need for change. Information leading to such awareness can come from the various stakeholders of the firm. Another source of information is scientific associations, which may know more about developments in product and manufacturing technologies. Moreover, examining the actions of competitors gives an additional lens to managers through which they can monitor the environment.

BUILDING AWARENESS OF NEED TO CHANGE

Once senior managers have gained a general idea of the kind of change required, they must build awareness of this need among employees in the firm. Awareness can be built among employees during routine contacts with them. These conversations will stimulate people's thoughts about possible change without raising anxieties too quickly. Thus, sharing information and establishing trust are critical in building support for change.

FOSTER DEBATE

Stimulating debate about alternative solutions and a diversity of perspectives is essential. Diversity of ideas raises the chances that both the best and worst aspects of each alternative are brought to light. The debates and various perspectives contribute towards building a commitment to new goals.

CREATE CONSENSUS

Evidence will accumulate in favor of particular approach by analyzing the results of debates. This evidence will help in creating a consensus about the direction, change should take. In this process, opposition is likely and retaining entrenched opponents to a change initiative that can result in trouble. In this stage, continuous training and management development can reap big dividends in implementing change. By teaching new skills to employees, the management can eliminate fear, the major source of resistance to transformation.

ASSIGN RESPONSIBILITY

Once the appropriate response to change has been determined, responsibility for carrying it out must be assigned. In this context, a new effort towards change can be placed within an existing department. Also, the firm can set a new autonomous unit. To ensure that an initiative receives proper attention, it may need to be established as a separate unit headed by someone who has only its welfare in mind.

ALLOCATE RESOURCES

A variety of resources may be needed to carry-out a new initiative. Management must ensure that sufficient resources are available for the initiative. Otherwise, the initiative will atrophy for the lack of sustenance. Allocating these resources is the final step of the change process.

RESISTANCE TO CHANGE

Managers promoting change often possess insufficient knowledge to determine as to how a firm should respond to change. A senior manager interested in bringing about change must rely on employees to implement the new response once it has been developed. Therefore, they need to support managers and employees in designing a change initiative and implementing it. In certain organizations, employees withhold such support. Certain reasons for withholding support are:

Lack of Awareness

Change requires a broad view of both the competitive and general environment. Manager (at middle and lower level) and employees are often too focused on current activities to develop this kind of perspective. They become narrowly focused to be aware of potential changes over the horizon. They fail to appreciate the need for change, especially if change means learning new methods, processes or techniques.

Lack of Interest

Even when managers and employees recognize the need for change, they often perceive it with lack of interest. This kind of reaction is common even with new developments.

Incompatibility with Cherished Values

Mostly firms develop their own sense of shared values and corporate cultures. Managers and employees oppose new strategies, products or approaches that appear to conflict with established practices. Therefore, strongly held values and corporate cultures can become significant obstacles to change.

Fear of Cannibalization

Developing new products that are distinct from those of the firm's current lineup means admitting the possibility that alternative or substitute products exist. Facing the threat of substitute products is hard for any company. Therefore, cannibalization is one of the main reasons that prevent companies from investing in new technologies/products before competitors compel them to do so.

Fear of Personal Loss

The fear of restructuring that would eliminate entire divisions or businesses, along with people involved in it, makes corporate change painful. Moreover, change may reduce the career opportunities for employees and may even cost them their jobs.

Different Perception

A manager may make a decision and recommend change based on his/her own assessment of a situation. Others may resist the change because they may perceive the situation differently. As a result of different perception, it becomes difficult for organizations to implement change.

The opposition to change must be overcome, if it is to be implemented successfully. Casualties are possible and sometimes inevitable. Moreover, some people will leave because they are uncomfortable with the changes. But there are several techniques to overcome resistance. They are:

PARTICIPATION

Change: Change occurs when people who perceive the need for change tryout new ideas. Changes could be introduced gradually or it may be dramatic. Organizations in difficulty often appoint a new strategic leader to introduce fresh ideas and implement the changes. Changes need to be planned and everyone must be reassured that these changes will be for the betterment of the company and its stakeholders.

Refreezing: This takes place when change patterns are accepted and followed willingly. Often, rewards are influential in ensuring that refreezing takes place.

Throughout the change process, it is essential that people are aware of why changes are being proposed and are taking place, and that they understand the reasons.

STRATEGIES FOR IMPLEMENTATION AND CHANGE

Implementation is an activity in which structures and systems are changed to accommodate changes in strategy. Implementation of a strategy is considered in depth before final decisions are made. Implementation and formulation operate simultaneously. There are five distinct approaches to strategy implementation and strategic change, which are given below:

- The strategic leader defines the changes of strategy and then hands it over to management for implementation. In this sense, he/she is a planner/thinker rather than a doer.

- The strategic leader again decides major changes of strategy. They then consider the appropriate changes in structure, personnel, reward systems etc., if the strategy is to be implemented effectively.
- The strategic leaders and senior managers meet for lengthy discussions with a view to formulate proposed strategic changes. The managers are briefed and the aim is to reach decisions to which they will all be committed. Managers who have been instrumental in their formulation then implement the strategies.
- The strategic leader concentrates on establishing and communicating a clear mission for the organization. He/she pursues this through a decentralized structure by developing an appropriate organization culture. The strategic leader retains the responsibility for changes in strategic perspective. The decisions concerning functional strategy are decentralized, but constrained by the mission, culture and policies established by the strategic leader.
- In this approach, managers throughout the organization are encouraged to be innovative and come up with proposals. The strategic leader establishes a framework for evaluating these proposals. The accepted and resourced proposals result in an increased status of the manager concerned.

ROLE OF THE STRATEGIST

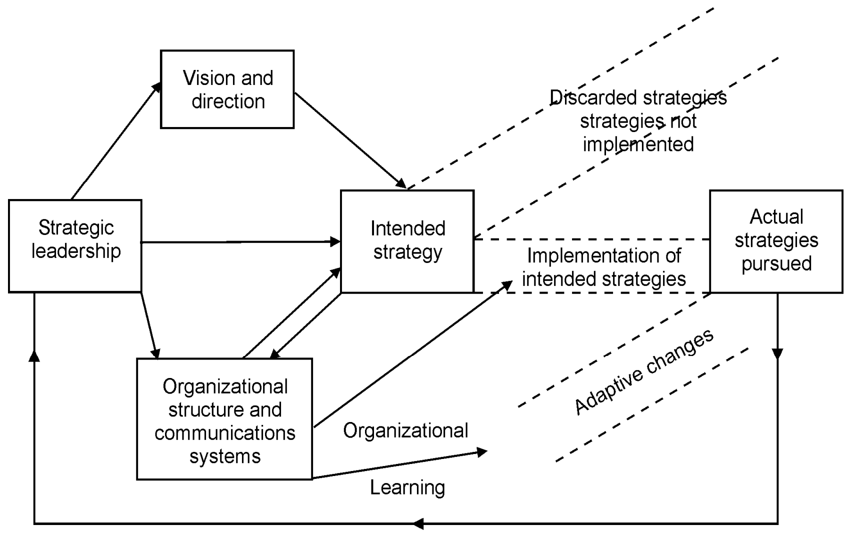
A strategist is primarily responsible for creating and implementing strategic change. Anyone in the organization who controls key or precedent setting actions can be called a strategist. Also, strategist can be a collection of people. It is the responsibility of the strategist to clarify the mission and objectives of the organization, to define the corporate strategy and establish and manage the organization's structure. The strategist also influences the organization's culture and values, which are key determinants of the ways in which strategies are created and implemented. However, he is not the only creator of strategic change. Managers who are in charge of strategic business units are responsible for strategic changes concerning their products, services, geographic territories, etc about all aspects of the business, monitor the environment and the organization and watch for opportunities and threats. In this chapter we will discuss the roles and responsibilities of strategist, manager, general manager, board of directors and the chief executive officer. We begin the chapter by discussing the role of the strategist.

The primary role of the strategist is to ensure that long-term strategies have been determined, understood and supported by managers within the organization who will be responsible for implementing them. The more feasible the strategies, the more likely they are to be supported. The responsibilities of the strategist are:

- Providing direction in the form of a mission or purpose.
- Providing policies and guidelines for managers to facilitate the management of operations and changes in competitive/functional strategies.
- Monitoring and control operations, with special reference to financial results, productivity, quality, innovation, customer service and staff development.
- Formulating and implementing changes to corporate strategies.
- Managing the business on behalf of all the stakeholders.

The strategist has to build a system of communications within the organization. This system should enable the managers to be strategically aware. Moreover, the system should ensure that the strategic leader stays informed of the changes that are taking place. As an analogy, the strategist provides a survival kit. There is a map (mission), but managers need emergency provisions, ways of summoning assistance when the map proves inadequate. The policies and communication networks provide this flexibility. Figure.2 illustrates strategic leadership and strategic change.

Figure 2: Strategic Leadership and Strategic Change



Leadership Qualities

Successful organizations are those that are well led rather than those that are well managed, emphasizing the need for a clear vision. An organization may be very efficient without a vision, but it is less likely to be effective than those organizations with a clear and shared direction. Also, market forces can determine short-term success, but long-term success requires a clear vision of where the organization is going. The qualities and skills for effective strategic leadership are:

- He should possess the ability to build and control an effective team of managers.
- The ability to recognize and synthesize important developments, both inside and outside the organization. This requires strategic awareness, the ability to judge the significance of an observed event and conceptualization skills.
- He should have credibility and competence. This requires the ability to exercise power and influence and to create change.
- He should have implementation skills, i.e., getting things done. This requires drive, decisiveness and dynamism.
- He should possess perseverance and persistence in pursuing the mission or vision, plus mental and physical stamina.

In addition, the strategic leader should believe more in success than in failure. He/she should understand clearly where the strengths of the organization are, concentrate on them and develop them to make the company more successful.

Leadership Style

The success of an organization is strongly influenced by the style adopted. Different leaders behave individually. Some strategic leaders will be entrepreneurial, i.e., they seek out opportunities for change and are willing to take the necessary risks. Some leaders are more conservative, i.e., they do not take or are less likely to take major risks. In relatively stable environments both the leaders can be appropriate and successful.

The strategic leader can adopt autocratic or democratic style. In this context, generally small organizations are run autocratically. Where organizations are divisionalized much depends on the amount of freedom and encouragement that the strategic leaders of each division are given. Leadership style also relates to the role of planning and the importance of incremental change in strategic management.

For example, some leaders rely heavily on forecasts and plans for determining strategic change and this could be linked to a strict adherence to financial targets.

Ambitions and Values of Strategic Leader

The strategic leader may be very ambitious to create a certain type of organization. Some strategic leaders are appointed to rescue a company in difficulties and they have a clear remit. On the other hand, others may have considerable freedom to choose their own terms of reference. When a new strategic leader is appointed, the results could be either positive or negative. The result depends on various factors such as the need to change the directions for change that are chosen and how well they match existing skills. Similarly, companies might face difficulties when a strong and charismatic leader departs. Due to tins, there can be temporary or even permanent decline. Thus, organizations can change markedly with changes of strategic leader.

The strategic leader may have certain values and this in turn influences his/her style and culture in the organization. For example, if the strategic leader has a marketing background, he is more likely to focus his concentration on consumers and competition. If a new strategic leader is appointed (from another organization), it is inevitable that he/she will bring values which have been learned elsewhere. This may involve change. Strategic leaders are generally appointed because of their successful record in previous companies, and as a newcomer they may be determined to establish their presence by introducing changes. However, these perceptions are generalizations and may not always prove to be true.

Strategic leader and change

Change results from decisions taken and implemented in response to perceived opportunities or threats. It therefore requires strategic awareness and strategic planning. Managing change implies interpreting signals from the environment. Environmental signals come in numerous ways and it is essential that they are monitored and filtered in such a way that the important information reaches decision makers. For example, if strategic change is dependent on marketing managers, they must feel that they have the authority to make changes. In this context, strategic leadership is required to direct activity. The major decisions fall to the strategic leader and therefore he/she must decide upon' the most appropriate planning system and manage it.

Managers should be constantly aware and alert to changes in the environment. Also, they should be constantly alert to new ways of producing/marketing their products in order to improve or strengthen their competitive advantage. If this is to happen effectively, the strategic leader must ensure that the managers are encouraged, motivated and rewarded for acting accordingly. The strategic leader must design and manage an appropriate organization structure to ensure this.

Risk Factor

Certain business environments involve higher risks than others. For example, a high technology industry where there is constant innovation and technological change involves high levels of risk. Here a question arises as to what is risk? Risk occurs whenever anyone must make a choice and the potential outcome involves uncertainty. For example, if a person has to make a decision and the alternative choices involve potential gains and losses that are not certain, the situation involves risk. In general management, the outcome of a typical decision will be dependent on factors such as customer reaction, levels of demand, competitor reactions, etc.

There should be compatibility between the strategic leader's attitude towards risk and demands of the industry. For example, a risk-averse strategic leader in a high-risk industry may miss valuable opportunities. Another factor associated with risk is loss. Risk increases as the amount of potential loss increases. Also, the willingness to take risk is affected by the amount and by its relative importance to the decision taker. The criteria that are to be considered while taking decisions regarding risk are:

- The attractiveness of each option to the decisionmaker.
- The estimated probabilities of success and failure.
- The extent to which the decisionmaker is prepared to accept the potential loss in each alternative.
- The degree to which the decisionmaker is likely to affect the success or failure.

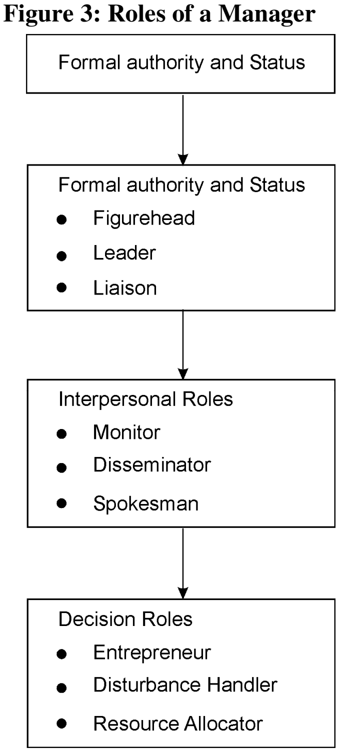
In considering risk and strategic leadership in an organization, a number of factors are to be investigated. The culture and values of the organization with regard to reward for success and sanction for failure are to be considered in taking risks. Moreover, attitudes towards risk also affect the way managers make decisions. Generally high-risk takers tend to make more rapid decisions than low risk takers. Another factor that influences risk taking is environment. Examples of environmental factors could be the availability and cost of finance, forecasts of market opportunities and market buoyancy, suitability of internal resources etc. Factors in the internal environment of the organization such as styles of leadership, reward systems also influence risk taking.

Manager and Strategy

In general management, the task of a manager is to plan, organize, direct and control. But these words are too vague to understand the reality of managerial work. To be specific, managerial task involves performing a number of regular duties (ritual and ceremonial), negotiations and processing of soft information that links the organization with its environment. Further managers have to schedule time, process information, make decisions and so on.

Managers perform different roles (Fig. 3). The roles of a manager are:

Figure 3: Roles of a Manager



Interpersonal Roles

The three interpersonal roles of a manager are:

Figurehead Role

The figurehead role is important for the smooth functioning of an organization. As a figurehead, managers perform duties of ceremonial nature as head of the organization/strategic business unit/department.

Leader Role

As a leader, the manager has to co-ordinate the work of others and lead his subordinates.

Liaison Role

As a liaison, the manager has to perform the functions of motivation, communication, encouraging team spirit and the like.

Informational Role

Managers are nerve centers of their organizations/departments. Therefore, he/she has to play the role more effectively to let the information flow from one corner to other comer. The information roles of a manager are:

Monitor Role

Managers have network of contacts and gets information by scanning the environment, subordinates, peers and superiors. Managers play the role of monitor by collecting information.

Disseminator Role

After collecting the information, the manager has to pass some of the information to his subordinates. The manager's role becomes important when the subordinates do not have contact with one another.

Spokesman Role

The organization operates in and around its external and internal environment. The directors and shareholders are to be informed about the developments in the company, its products etc. Thus, the image forms a bridge between his/her superior and the organizational environment.

Decisional Roles

Managers play a key role in the decision-making system of the unit. The decisional roles of a manager are:

Entrepreneurial Role

As an entrepreneur, the manager is a creator and innovator. He seeks to improve his department, adapt to the environmental factors and initiate new projects.

Disturbance Handler

As a disturbance handler, the manager responds involuntarily to pressures. Examples of various pressures could be worker strike, declining sales. bankruptcy of a major customer, etc.

Resource Allocator Role

The most important resource that a manager allocates to his subordinates is his time. This role helps both the manager and subordinates in making effective decisions.

Negotiator Role

Managers spend considerable time in negotiation with subordinates, peers, workers, government, etc. These negotiations are an integral part of the manager's job.

Though the different roles of manager are discussed separately, in reality, they are inseparable. These roles have to be integrated. Therefore, as a strategist, the manager has to integrate all the roles in decision-making and performing his tasks.

The General Manager and Strategy

There are various functions in an organization such as marketing, finance, human resource etc. These functions act as sub systems and the organization acts as a whole in a single system. The responsibility of this single system rests upon the general management in general and on general managers to be specific. General management consists of board of directors, chief executive officers, functional heads, middle level and junior level executives and so on. The principal general management functions are:

- Setting objectives,
- Monitoring the environment,
- Establishing strategies,
- Obtaining resources,
- Allocating resources,
- Developing plans and budgets,
- Approving plans and budgets,
- Performance review of the organization,
- Employment of officers,
- Co-ordinating the work of the board of directors and executives,
- Providing expert help and consultancy,
- Representing the firm to outside parties,
- Utilizing outside contacts to the benefit of the firm,
- Utilizing outside consultants and experts,
- Human resource development, and
- Managing operations.

The general manager is an entrepreneur, strategist, leader and chief implementer. The general managers integrate various activities, roles and functions for achieving organizational objectives. The strategic management responsibilities of a general manager are:

i. Establishing the Mission – Deciding on the business or businesses that the company or division should engage in and other fundamentals that will guide and characterize the business, such as continuous growth. A mission is usually enduring and timeless.

ii. Formulating a Company Philosophy – Establishing the beliefs, values, attitudes and unwritten guidelines and add up to, “the way we do things around here”.

iii. Establishing Policies – Deciding on plans of action to guide the performance of all major activities in carrying out strategy in accordance with company philosophy.

iv. Setting Objectives – Deciding on achievement targets within a defined time range. Objectives are narrower in scope than the mission and are designed to aid in making operational plans for carrying out strategy.

v. Developing Strategy – Developing concepts, ideas and plans for achieving objectives successfully and meeting and beating the competition. Strategic planning is part of the total planning process that includes management and operation planning.

vi. Planning the Organization Structure – Developing the plan of organization and the activities that help people work together to perform activities in accordance with strategy, philosophy and policies.

vii. Providing Personnel – Recruiting, selecting and developing people to fill the positions in the organization plan.

viii. Establishing Procedures – Determining and prescribing how all important and recurrent activities will be carried out.

ix. Providing Facilities – Providing the plant, equipment, and other physical facilities required to carry on the business.

x. Providing Capital – Making sure the business has the money, and credit needed for working capital and physical facilities.

xi. Setting Standards – Establishing measures of performance that will enable the business to best achieve its long-term objectives successfully.

xii. Establishing Management Programs and Operational Plans – Developing programs and plans governing activities and the use of resources that, when carried out in accordance with established strategy, policies, procedures and standards, will enable people to achieve particular objectives. These are phases of total planning process, which includes strategic planning.

xiii. Providing Control Information – Supplying facts and figures to help people follow the strategy, policies, procedures and programs, to keep alert to forces at work inside and outside the business, to measure overall company performance against established plans and standards.

xiv. Activating People – Commanding and motivating people to act in accordance with philosophy, policies, procedures and standards in carrying out the plans of the company.

The general managers need a variety of skills. This is because they are required to perform variety of functions and different roles. For instance, top level managers are expected to have more conceptual skills and junior managers, more technical skills. The degree of skills required for the General Managers at different levels are discussed in Table 1.

Table 1: Degree of Skill Requirement for the General Managers at Different Levels

General Management Level	Degree of Skill Requirements		
	Conceptual Skills	Human Relations Skills	Technical Skills
Top Level Managers	High	Moderate	Low
Middle Level Managers	Moderate	High	Moderate
Lower Level Managers	Low	Moderate	High

The Chief Executive Officer and Strategic Management

The Chief Executive Officer (CEO) or the Managing Director is the person responsible for the functioning of the entire organization. The CEO has to play crucial and multiple roles in formulating and implementing mission, objectives, policies and strategies. His multiple roles include:

Organization Builder

The CEO has the responsibility for organization building through organizational change. But in general, people resist change due to reasons such as misunderstanding and lack of trust, low tolerance for change etc. The CEO can deal with resistance through.

- Education and communication,
- Participation and involvement,
- Negotiation and agreement,
- Manipulation and cooperation, and
- Explicit and implicit coercion.

Organization Leader

The CEO must have a base for leadership. The CEO should have leadership skills such as:

- Favorable attitude towards those in positions of authority, such as supervisors,
- Desire to assist oneself to take charge,
- Desire to behave in a distinctive and different way,
- Sense of responsibility in carrying out routine duties associated with managerial work, and
- Desire to engage in competition.

Success Sharing by CEO

Monitoring, sponsoring and helping others is an important activity of CEO. The CEO has to help the organization staff by training, coaching, assisting, informing, writing letters of correspondence etc.

Executive Qualities

Personalities of successful CEOs tend to vary but they have some commonalties such as:

- Knowing the strengths and spend most of their time in perfonl1ing those activities in which they are strong.
- Managing time effectively.
- CEOs are intuitors in the sense that they deal well with ideas, theories and innovations.
- He is generally an organized thinker.
- Motivated by power and ability to make things happen.
- Comfortable with a wide range of people, but prefers casual associates.
- Has a high energy level.

Personal Dimensions for Selection of CEO

Various criteria have to be taken into consideration, while selecting CEO. Some of these criteria are:

i. Capacity to abstract, conceptualize, organize and integrate data into a coherent frame of reference.

ii. Sensitivity, ability to perceive subtleness of others feelings.

iii. Articulateness, making a good impression.

iv. Sense of humor.

v. Vision, clear about his/her career as well as where the organization should go.

vi. Personal organization and having a good sense of time.

vii. Adaptability, managing stress well.

viii. Stamina, having physical and mental energy.

ix. Maturity.

x. Involvement sees oneself as a participating member of the organization.

xi. Achievement, oriented towards organization's success rather than personal success.

xii. Authority has the feeling that he/she is the boss.

xiii. Judgment, knows when to act.

Role of CEO in Strategic Management

Among all the strategists, CEO is tile key person in the organization. Being at tile top most position, he integrates functional areas of manager and visualizes the total organization. He foresees external environment and its impact on business. He evaluates the present mission, policies, and strategies against the future changes and reformulates them. Further new policies and strategies are formulated as and when changes in the environment take place. Also, the CEO provides information to the board regarding strategy formulation. Moreover, he advises the board to continue tile present strategy or formulate a new strategy. Thus the CEO guides the senior managers in formulating, implementing, evaluating and reformulating strategies.

GLOBAL COMPETITIVENESS IN THE NEW MILLENNIUM

The phenomenon of the globalization of markets and competition is a relatively recent one. According to Michael Porter, strong global competitors to the US began to arise after 1950. The global marketplace has developed on account of the factors listed below:

- Explosive growth in world gross domestic product, especially in the developed countries.
- Even more rapid expansion in merchandise trade (exports and imports) reflecting a new demand for goods from affluent customers.
- Cost cutting and improvement of product quality by companies seeking a new demand for goods from affluent customers.
- Cost cutting and improvement of product quality by companies seeking competitive advantage, resulted in the growth of large corporations, with worldwide operations. A revolution in manufacturing, distribution, and product quality control, further enhanced the competitive positions of these large corporations.
- A revolution in communications technology.

Other significant forces, which have also been responsible for facilitating the rise of great global corporations are:

- Growth of large pools of liquid funds and more efficient capital markets to employ them quickly.
- Improved financial, logistics and business management techniques.

The ease with which technology is transferred globally and introduced into new products increases the intensity of global competition.

The International Institute for Management Development, in its World Competitiveness Report, 2002, gave the United States the highest competitiveness rating of all nations. The report covered 49 industrialized and emerging economies. The ranking was based on some 314 criteria grouped into five competitiveness factors – economic performance, domestic economy, government efficiency, business efficiency and infrastructure.

Facing the Global Competitive Challenges

Although the global competitive position of many leading companies of the world has strengthened significantly in recent years, there are still weaknesses that require correction. It is a challenge for both private and public sector companies to maintain and strengthen their competitive positions and to rectify their weaknesses. Certain policies and practices to move in this direction are suggested below:

What should corporations do?

According to Michael Porter, corporations should seek long-term investors and give them a voice in governance. A manager's compensation should be linked to the firm's competitive position. Improving worker-training programs in the company, collaborating with local educational institutions to advance worker-training programs, promoting managers with skills in dealing with global markets, increasing funding for basic research, and taking a special interest in adherence to international codes of social responsibility and ethics are other recommendations.

What should governments do?

Steps that should be taken by governments include:

Technology Policy

- Urgent national priority to be given to technology leadership.
- Greater emphasis on R&D allocations to improve transfer of basic research to new products and processes. Setting up of technology centers, dissemination of technology to industry and assistance to companies to transfer new technology more quickly into products and processes.
- Better co-ordination among government agencies in policy setting and allocation of funds to R&D.
- Increased tax credits for R&D investments in industry.
- Encouragement to industries to form consortia for developing new technology.

Industrial Policy

Those who favor government support for specific technologies say that technological strength is critical to economic strength and the government should help industry strengthen its technological muscle. They add that foreign governments subsidize technological development by private companies.

Critics of such policies, however, caution against government involvement in picking technological winners and losers. They say that governments are simply inept in making such decisions, because political considerations will override economic and technical factors. In reality, government policies supporting commercial technological growth have been in existence for many years.

Strengthening Education Programs

Reform and improvement of the present education system should occupy top most priority and include revitalizing elementary and secondary schools in order to improve both general learning and technical knowledge. The greater the excellence in technical skills, greater the generation of new ideas, and the more advanced a nation's knowledge base, stronger will be its economy and higher the standards of living of its people.

Business people also recommend that universities place more emphasis on manufacturing, engineering, product innovation and international management. A national policy of stipends encouraging the best students in science and engineering could pay high dividends.

Financial Reforms

Financial reforms could include a change in tax laws to stimulate a higher rate of savings, change in capital gains laws to provide incentives for entrepreneurs and long-term investments, permission to banks to invest in equities with safeguards assuring long-term rather than short-term trading, and finally, removal of incentives for financial manipulation in buying and selling corporations.

CONSIDERATIONS FOR STRATEGISTS IN THE 21ST CENTURY

At the start of the 21st century, we find that there is an increasing need for managers who understand their role under conditions of rapid change. In certain situations, there are forces which are beyond the control of managers. These situations require managers who can adjust to new developments. Managers are also themselves involved in initiating and directing change. Some of the challenges that managers face at the start of the new century are described below:

Corporate Strategy

The last decade of the twentieth century is likely to be viewed by historians as an era in which a remarkable redefinition of business took place. Many companies re-engineered operations in order to become more efficient, but often less dependent on people than in the past. Massive dislocation of people from all levels of companies has taken place as a result of waves of restructuring, during the past decade. As a result of restructuring many of the middle-and senior-level managers lost their jobs, and upon failing to find comparable jobs in other large firms, these managers were instrumental in founding new companies. The 1990s thus saw a great burst of new business formation. The effects of restructuring and lay-offs also affected a new generation of employees. Many talented people who might have once strived to join large companies began to view better opportunities and more happiness in smaller, independent businesses of their own.

It has become necessary for managers to consider whether, and how, their companies can integrate commitments towards their employees with the changing needs and demands of customers for products and services. Further, the need for high performance workplace environments has made it essential for companies to invest in education of its employees, development of their skills, and process changes to effectively empower employees. Although some companies have made significant efforts in creating an environment encouraging excellent performance in the workplace, others have been excessively cautious in this regard. The trade-off between the benefits of initiating these changes relative to the costs is one of the key strategic issues managers have to face.

Ethics, Public Values and Social Responsibility

The ever-changing conditions in which business is conducted test the ability of companies to adhere to core values and principles. Technological changes, for example, are throwing up a host of new issues regarding the ownership, use, and distribution of intellectual property.

Managers can expect further complications in ethical issues, many of which will relate to global business activity. These issues will culminate in one central question for strategic managers – how can business be conducted within a framework of ethical ideals, norms, and standards that are understood and accepted by people globally? Social responsibility and environmentalism are important related issues in this context.

GLOBAL CHALLENGES

Strategic managers in the twenty first century are likely to face one central question: How can businesses operate in a global environment in ways that serve societal objectives by meeting real needs, yet accommodate the diverse demands and often conflicting interests of stakeholders?

ROLE OF THE GOVERNMENT

Governments around the world are in the process of redefining and reinventing their role in the global economy of the 21st century. The choices of individual nations will be influenced by many factors, including the new reality of global financial markets that react instantaneously to financial news in any part of the world.

ECOLOGICAL CHALLENGES

In the twenty-first century ecological challenges have emerged as the most important vector of change. Understanding the interconnectedness of economic and demographic variables will be crucial in the twenty-first century.

QUALITY AND PRODUCTIVITY

Another challenge faced by strategy managers in recent years has been issues of quality, productivity, and their relationships. Companies in the US have come to understand that the success of the Japanese and German firms lies in the edge in quality of their products. As a result, US firms are moving towards the enhancement of the quality of their products and services. Products of higher quality using fewer resources are developed by globally competitive companies. More and more interest is therefore, being shown by US Managers on ways to improve the productivity of American workers.

WORKFORCE DIVERSITY

Workforce diversity is another issue that managers today must learn to deal with various factors such as globalization, aging population, influx of workers into new careers and occupations, and influx of women into organizations, have made the workforce much more heterogeneous than at any time in the past. The workplace, likewise, is very different from what it was in the past. It has, therefore, become important for managers in every organization to become more sensitive to the needs, perceptions, and aspirations of many different kinds of workers. Managers of today must also be in a position to utilize the talents of all their employees.

CHANGE

Managers of today face more change than their predecessors did. The requirements, demands and expectations from managers and their organizations, as well as the complexity of the competitive environment are far greater than was the case in the past. In the past, managers viewed change as something to be addressed periodically, whereas it has become a fact of everyday life for present day managers.

Empowerment

Issues dealing with empowerment of the organization's human resources are another challenge for managers in the 21st century. The various techniques and methods of empowerment range from increased participation in decision-making to the use of integrated work teams.

EMERGENCE OF A KNOWLEDGE WORKER

According to Peter Drucker what we refer to as the information revolution is in fact a knowledge revolution. Software is the reorganization of traditional work based on centuries of experience, through the application of knowledge and especially of systematic, logical analysis. Electronics is not the key here. Cognitive science is. This suggests that organizations which want to maintain leadership in the economy and the technology that are going to emerge in the future need to give enough consideration to the social position of the knowledge professionals and their values.

Traditionally, capital has been treated as the key resource, the financier as the boss, and knowledge workers as employees who would be content with bonuses and stock options. Drucker says that this attitude will work only as long as the stock-markets are booming. The major industries are likely to grow more like traditional industries – slowly, painfully and laboriously – unlike Internet companies. These major industries are going to depend on knowledge workers. These workers would not be content with fringe benefits such as stock options and bonuses. Financial incentives won't prevent people from leaving.

Companies that implemented compensation systems that offered benefits and stock options have the highest turnover. In fact, ex-Microsoft people hate Microsoft. They feel that the only thing that was offered to them at Microsoft was money. They resent lack of recognition at Microsoft. In other words, they could not adapt themselves to a value system that is entirely financial because they regarded themselves as professionals and applied scientists. In other words, their value system was different from Microsoft's value system.

Running an organization with "shareholder value" as its goal and justification can become counterproductive, because the performance of these knowledge-based organizations will depend to a large extent on how they can attract, hold, and motivate knowledge workers. Since these people can't be satisfied with money, they should be offered recognition and power within the organization. This is possible only when subordinates are treated as fellow executives, and employees as partners.

ROLE OF A KNOWLEDGE WORKER

It is through the means of formal education that a knowledge worker gains access to work, job and social position. A fairly limited amount of knowledge may be required in some kinds of knowledge work, for example, some paramedical technicians such as an X-ray machine operator, a clinical laboratory technician, or a pulmonary technologist. On the contrary, far more advanced theoretical knowledge is required for some other kinds of knowledge work such as market research, product planning, advertising and promotion etc.

Since knowledge workers work in teams and since knowledge work is more effective when it is more specialized, the team rather than the individual becomes the actual work unit. Further, the effectiveness of a knowledge worker will depend upon the manager's ability to diagnose what kind of team is required for full effectiveness of a certain kind of knowledge work, and the ability to organize such a team and to integrate the worker into it.

Knowledge, unlike any of the traditional key resources like land, labor, and capital, is not tied to any country but is transnational, portable, and can be created everywhere, fast and cheap. Knowledge is forever changing and makes itself obsolete within a short period of time. The only thing that can be predicted about a competitive advantage of a country, an industry, an institution, or an individual, based on knowledge, is that the advantage will soon be challenged, possibly by a total newcomer.

Acquisition of knowledge, or learning, therefore, can no longer stop at any age. Lifelong learning or continuous learning during one's working life will increasingly be a requirement for all knowledge workers.

Also, while it is possible to define what productivity is with respect to the manual worker, it is not so in the case of a knowledge worker. The measurements of productivity for a manual worker such as number of pieces turned out per hour or per dollar wage prove to be irrelevant if applied to the knowledge worker. Productivity in case of a knowledge worker is primarily in terms of quality.

THE CEO IN THE NEW MILLENNIUM

Corporate Governance

In future, the governance of corporations will be significantly different from what it is now. Fundamental change in the corporate ownership structure will, in all probability, lead to changes in corporate governance. All over the world, particularly in developed countries, financial considerations are determining ownership interests. In the majority of developed countries, the population is aging. Consequently more people are worried about their future financial resources. This makes the investment of pension funds an important issue. Factors such as these will have an impact on corporate owners.

Educating (about corporate governance) corporate owners, who are generally financial people, is a highly difficult task. Though this task appears to be easy, it is in reality difficult to accomplish. Financial people are hardly aware of the issue of balance between short-term versus long-term, current improvements versus future creations, and change versus continuity. CEOs can understand the conflicts involved, but financial people can rarely do so.

CEOs must try to find ways to strike the right balance. With their experience, CEOs can do what needs to be done even when it is difficult to do so, and even when they are prone to committing mistakes. It is unfortunate that many CEOs try to avoid the issue of governance. This neglect has harmed organizations such as WorldCom and Enron. Many CEOs try to excuse their behavior by arguing that they are running this place for the short-term interest of the shareholder. Not only governance, but also related concepts and tools need to be transformed or designed over the next fifteen years.

Approach to Information

It was widely believed that new information capacities would completely change the way businesses are run. But, this has not been evident anywhere, except in military organizations. The impact of new information capacities has been significant only on the way organizations manage their operations. For example, using software, a single architect today can draw building designs that earlier require the efforts of hundreds of individuals. Similarly, young surgeons can learn and practice surgical techniques with virtual reality equipment without endangering the health of patients.

Though information technology has had an impact on all types of businesses, it has hardly had any influence over strategy and innovation. Till now, a CEO rarely benefited from the new information available for decision-making. This will change. Organizations are changing basic record-keeping to accommodate present economic reality. Simultaneously, they are merging the record-keeping function with the data producing function to create all information system that is entirely different from the existing one. Even this system will not provide CEOs with the complete information necessary for making decisions.

Organizations do not know completely what is happening in the external environment. Even when an organization is a leader in a particular product category, most of the people who buy that product may not be its customers. A firm is generally considered a giant if it has a 30 percent market share. But 70 percent of the customers do not buy that firm’s product, and the firm does not have any information on these customers. The firm should take this 70 percent seriously because it can provide the information that will help the firm understand the changes that affect the industry. Irrespective of the business they are in senior managers should spend some time outside their company to know about the culture of the society in which they are operating. For example, executives of US companies who created successful businesses in Japan studied Japanese history carefully before operating in Japan.

SUMMARY

- Organizational change is a complex and difficult process for companies to manage successfully. Global marketplace has developed because of factors such as explosive growth in world GDP, rapid expansion in merchandise trade, cost cutting and increasing product quality by firms seeking competitive advantage, and revolution in communication technology. Considerations for strategists in the 21st century are many. These include corporate strategy; ethics, public values and social responsibility; global challenges; the role of the government; ecological issues; quality and productivity; workforce diversity; change; and empowerment.
- Organizations that want to maintain leadership in the economy and the technology that are going to emerge in the future need to give enough consideration to the social position of the knowledge professionals and their values.
- It is through the means of formal education that a knowledge worker gains access to work, job, and social position. A fairly limited amount of knowledge may be required in some kinds of knowledge work, for example, some paramedical technicians such as an X-ray machine operator, a clinical laboratory technician, or a pulmonary technologist. On the contrary, far more advanced theoretical knowledge is required for some other kinds of knowledge work such as market research, product planning, advertising and promotion, etc.
- In future, the delivery of goods, services, and spare parts will be done by e-commerce organizations. Different yardsticks will be required to measure the performance of such organizations. All over the world, particularly in developed countries, financial considerations are determining the ownership interests. In the majority of developed countries, the population is aging. Consequently more people are worried about their future financial resources. This makes the investment of pension funds an important issue. Factors such as these will have an impact on corporate owners.
- Though information technology has had an impact on all types of businesses, it has hardly had any influence over strategy and innovation. Till now, a CEO did not benefit significantly from the new information available for decision-making. This situation will change.

Glossary

Adaptive Mode	:	This mode is characterized by reactive solutions to existing problems. This mode of decision-making results in a fragmented strategy with incremental improvement.
Annual Objectives	:	These are the objectives that the firm seeks to achieve in one year.
BCG Growth-Share Matrix	:	BCG Growth-Share matrix is widely used in corporate strategic analysis. This matrix helps in analyzing likely "generators" and optimum "users" of corporate resources.
Budget	:	This is a statement of the programs to be implemented in monetary terms and is used for planning and control.
Business Ethics	:	Ethics is defined as "the discipline dealing with what is good and bad, and right and wrong, or with moral duty and obligation." Business ethics encompasses the morality of issues in business.
Buy-back of Shares	:	Buy-back of shares is the best tool for managements to use to counter a hostile takeover attempt. Buy-back of shares protects the existing management by consolidating the holdings and the promoter's stake in the company.
Company Goals	:	Company goals indicate a desired future state that a company attempts to realize.
Company Mission	:	The term 'mission' is defined as "the fundamental and enduring purpose of an organization that sets it apart from other organizations of a similar nature."
Company Philosophy	:	Company philosophy and values give a framework/ boundary for individual actions aimed at achieving corporate goals.
Company Profile	:	The profile of a company depicts the quantity and quality of the company's financial, human and physical resources.
Company Self-concept	:	A company's mission reveals its self-concept. The idea that the organization/firm must "know itself" is the essence of the term 'company self-concept'.
Concentration	:	A firm following this strategy focuses its resources on a single product, in a single market, using one tested technology to ensure profitable growth.
Conglomerate Mergers	:	When two firms from unrelated business activities merge, it is known as a conglomerate merger.
Cost Leadership	:	Cost leadership demands construction of efficient-scale facilities, tight cost and overhead controls, avoidance of small customer accounts, and minimization of costs in areas such as service, advertising, research and development, and sales force.
Declining Industries	:	Declining industries are industries that have experienced an absolute decline in unit sales over a sustained period.
Differentiation	:	This strategy aims at creating a product that is perceived as unique in the marketplace.
Diversification	:	Diversification is the process of entering into different industries either to exploit untapped potential or to minimize the risk of changing business trends.
Divestiture	:	A divestiture is the sale of a part or a division of a company to a third party. The division may include assets, product lines or subsidiaries.
Economic Environment	:	Prime interest rates, inflation rates and trends in the growth of the Gross National Product (GNP), the general availability of credit, the level of disposable income and the propensity to spend at the national and international levels influence the strategic planning of the organization. All these factors constitute the economic environment of the organization.

Entrepreneurial Mode	:	In this mode, strategies are framed by one powerful individual. The entrepreneurial mode focuses solely on the organization's opportunities.
Environmental Scanning	:	Environmental scanning involves monitoring the environment, and evaluating and disseminating information obtained from the internal and external environments.
Evaluation and Control	:	Evaluation and control refer to the processes in which corporate activities and performance results are compared with the desired performance. This information is used to take corrective action and resolve problems.
Exchange Offers	:	An exchange offer provides holders of one or more classes of securities, the right or option to exchange part or all of their holdings for a different class of securities of the firm.
External Environment	:	The external environment consists of all the conditions and forces that affect an organization's strategic options and define its competitive situation.
Emerging Industries	:	Emerging industries are created by technological innovations, emergence of new consumer needs, or shifts in relative cost relationships. In these industries, fundamental rules of competition change due to changes in the environment.
Five Forces Model	:	Michael E. Porter of the Harvard Business School has developed a framework known as the 'Five Forces Model' to help managers to analyze the business environment. According to Porter, the five forces, namely, the threat of new entrants, the bargaining power of buyers, the bargaining power of suppliers, the rivalry among existing players, and the threat of substitute products, play a vital role in shaping the company's future.
Focus	:	Focusing on a particular buyer group, segment of the product line, or geographic market is a focus strategy. This strategy assumes that a firm can serve its strategic target market more effectively than its competitors who are serving much bigger market.
Fragmented Industries	:	In fragmented industries, no firm has significant market share. These industries contain privately owned small- and medium-sized companies. Such industries can be found in service, retailing, distribution, wood and metal fabrications, agricultural products, and creative business sectors.
Functional Strategies	:	The grand strategy is split into strategies for each business division or function. These strategies are referred as functional strategies.
Grand Strategy	:	A grand strategy is a statement of means that indicates the methods to be used to achieve the company's objectives.
Horizontal Integration	:	If a firm grows through acquiring one or more similar businesses which are operating at the same stage of the production-marketing chain, then the firm is said to be following a strategy of horizontal integration.
Horizontal Mergers	:	If two firms operating and competing in the same business activity merge, it is known as a horizontal merger.
Innovation	:	Innovation involves the use of a new idea or method. A firm which brings out an innovative product usually enjoys the 'first mover' advantage.
Joint Ventures	:	In contrast to licensing and franchising arrangements, joint ventures allow companies to own a stake and play a role in the management of the foreign operation. Joint ventures require more direct investment and training, management assistance and technology transfer.
Long-term Objectives	:	Long-term objectives refer to those objectives that an organization seeks to achieve over a number of years.

Market Development : This process involves marketing existing products with little modification, to customers in related market areas. The organization employs different channels of distribution, changes the content of advertising or the medium of promotion.

Maturing Industries : Industries in which the growth rates are reaching saturation stage are called Maturing industries.

Mergers : Mergers can be defined as the integration of two or more firms on co-equal basis. In mergers, firms pool all their resources together to create a sustainable competitive advantage.

Mission Statement : The mission statement is an enduring statement of purpose for an organization; it refers to the philosophy of the business and serves to build the image of the company in terms of activities currently pursued by the organization, and its future plans.

Operating Strategies : Operating strategies provide the means for achieving annual objectives.

Organizational Learning : Organizational learning is defined as the improvement in skills and abilities while working with an organization.

Political Environment : Political forces influence the legislations and government rules and regulations under which the firm operates. An environment that constitutes these political forces is called political environment.

Planning Mode : In this mode, appropriate information for situational analysis is gathered systematically. A few feasible alternative strategies are developed and the most appropriate strategy is selected.

Policies : These are directives or guidelines given to managers and their subordinates as the framework to guide their thoughts, decisions and actions while implementing the organization's strategy.

Primary Activities : These activities include designing, creation, marketing, delivery, support and after sales service of the product.

Product Development : This process involves the modification of existing products or the creation of new items in a related category. These products are marketed to current customers through established channels.

Re-engineering : Re-engineering involves the critical analysis and radical redesign of existing business processes to achieve breakthrough improvements in measured performance.

Restructuring : Restructuring is a process in which business firms engage in a broad range of activities that change the structure of the firm.

Reverse Engineering : Reverse engineering is basically aimed at discovery and learning. Engineers can acquaint themselves of happenings in their industries not only by reading printed publications, going to technical conferences, and working on projects for their firms, but also by reverse engineering the products of other firms.

Social Environment : The social environment of an organization constitutes the values, beliefs, attitudes, opinions and lifestyles in society.

Social Responsibility : Corporate social responsibility is a public movement that has gained momentum over the past few decades as citizens have started demanding that corporations be accountable for their actions.

Spin Offs : A spin off is a type of divestiture in which a company divests a business unit such as a standalone subsidiary or division. The business unit is not sold for cash or securities; instead, common stock in the unit is distributed to shareholders on a pro rata basis.

Strategic Alliances	:	Strategic alliance means a cooperative agreement between potential or actual competitors. Some examples of strategic alliances are agreements between General Motors and Toyota to assemble automobiles, between Siemens and Philips to develop new semiconductor technology.
Strategic Analysis	:	Strategic analysis is done at corporate and business levels. Tools such as BCG Growth-Share Matrix, and GE Nine-Cell planning Grid are used at corporate level to examine each business as a separate entity and as a contributor to the organization's total business portfolio.
Strategic Intent	:	The term strategic intent refers to the purpose(s) an organization strives to achieve.
Strategic Management	:	Strategic management can be defined as the set of decisions and actions resulting in formulation and implementation of strategies designed to achieve the objectives of an organization.
Strategic Management process	:	A process in management is defined as a perceptible flow of information through interrelated stages of analysis directed towards the achievement of an item.
Strategy	:	Strategy refers to the plans made and actions taken to enable an organization fulfill its intended objectives.
Strategy Formulation	:	Strategy formulation refers to the development of long-term plans for managing opportunities and threats in the external environment, and for utilizing the strengths and overcoming the weaknesses within the organization.
Strategy Implementation	:	The process by which strategies are put into action is called strategy implementation. Programs, budgets and procedures are developed for this purpose.
Structure	:	The firm's structure plays a vital role in achieving firm's objectives. A proper structure is essential for strategy to be operational.
Support Activities	:	Support activities provide inputs to the primary activities and include activities like materials management.
SWOT Analysis	:	SWOT analysis is the most commonly used technique for environmental scanning. SWOT is an acronym for the Strengths, Weaknesses, Opportunities and Threats faced by a firm.
Takeovers	:	A takeover refers to the acquisition of a certain block of paid-up equity capital of a company with the intention of acquiring control over the affairs of the company.
Turnaround	:	A turnaround occurs when "a firm perseveres through an existence – threatening performance decline; ends the threat with a combination of strategies, systems, skills and capabilities; and achieves sustainable performance recovery. The obverse of performance recovery is failure and eventual death."
Value Chain	:	A value chain segregates a firm into strategically relevant activities to understand the cost behavior of each activity. By performing these activities economically and efficiently, a firm can gain competitive advantage.
Value Creation	:	The value created through a merger depends on the nature of the deal that has been struck as well as the integration process. A wrongly conceived merger will fail, no matter how good the integration process; and a deal based on sound logic might stumble if the integration process is poor.
Vertical Integration	:	This type of integration involves the acquisition of suppliers of inputs (such as raw materials), or the buyers of output (such as retailers for finished products).
Vision	:	The company's vision is a description of what the organization is trying to do and to become.