Debre Markos University

College of Business & Economics

Department of Management

Strategic Management Distance module

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Prepared by: -

Hassen Adgo (MBA)

Edited by: - Walie Zewudu (MBA)

Debre Markos University
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Debre Markos, Ethiopia

PREPARED BY:

1. Hassen Adigo(MBA)
2. Walie Zewudu (MBA)

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Module introduction

Dear distance learners, this material is prepared with a due considerate so as to enhance your understanding about concepts in strategic management .With regard to this, this module is sorted from different types of relevant strategic management books to assure the quality of the material as well as to equip you with an in-depth understanding about different strategies of management.

Moreover, this module contains seven chapters; under chapter one you will be introduced with the general overview of strategic management, importance of strategic management, historical background of strategic management, strategic management process and different types of strategies (emergent and intended). In chapter two you will discuss basic concepts about strategy formulation which includes; developing and evaluating vision and mission statements of different organizations, formulate and evaluate goals and objectives. Chapter three deals about external environment analysis which emphasized on monitoring evaluating and forecasting how macro factors, circumstances and issues changes from time to time and determining how they influences organizations strategic plan. Developing external factor evaluation (EFE) matrix is one topic in third chapter.

Chapter four introduces you with a remarkable concept regarding internal environment audit. Chapter five deals with different types of strategies with the corresponding merits and demerits. Strategy formulation frame work, strategy formulation(matching) matrices such as SWOT, BCG, SPACE and IE matrices would be discuss in this chapter. In addition to matching matrixes you will be introduced with strategy selection matrices called quantitative strategy planning matrix (QSPM). Chapter six deals with strategy implementation phase of strategic management process and lastly, chapter seven deals with a crucial knowledge regarding strategy evaluation and strategy evaluation frame. Under each chapter, you are provided a sorts of exercises by which you can check your understanding about the central issues of the course.

CHAPTER ONE

OVERVIEW OF STRATEGIC MANAGEMENT

Aim of the chapter

Knowledge of both the art and the science of strategic management is needed to help guide organizations as their strategies emerge and evolve over time. Such tools will also help you effectively chart a course for your career as well as to understand the effective strategic management of the organizations for which you will work.

The aim of this chapter is to introduce you with the different concepts of strategic management, definitions of strategic management, the importance of strategic management and types of strategic management.

Learning objectives

Dear learners, at the end of this chapter, you will be able to:

- Define Strategic management
- Describe stages of Strategic management
- Explain the key terms and model of Strategic management
- Describe benefits of Strategic management
- Elaborate Business ethics & Strategic management

1. Introduction

The term *strategy* is derived from the Greek "*strategos/strategia"*, meaning "general or *art of being a general"*. In a military sense, strategy involves the planning and directing of battles or campaigns on a broad scale, that is, the responsibility of the general. In this context, strategy is distinguished from *tactics*, which involve the initiation of actions to achieve more immediate objectives. *In the business parlance, there is no definite meaning assigned to strategy*, however, "strategy" often is used to refer to specific actions taken to offset actual or potential actions of competitors. In a more fundamental sense, the term denotes linkages with the goal-setting process, the formulation of more immediate objectives, and the selection of specific actions required in the application of resources to achieve these objectives.

Definition of Strategy

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

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

Generally, strategy is:

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

"Strategy is a unified, comprehensive, & integrated plan relating the strategic advantages of the firm to the challenges of the environment. It is designed to ensure that basic objectives of the enterprise are achieved."

The term 'strategy' proliferates in discussions of business. Scholars and consultants have provided myriad models and frameworks for analyzing strategic choice. For us, the key issue that should unite all discussion of strategy is a clear sense of an organization's objectives and a sense of how it will achieve these objectives. It is also important that the organization has a clear sense of its distinctiveness.

1.1 Definitions of Strategic Management

Strategic management can be defined in various ways.

Strategic management is;

- The set of managerial decisions and actions that determines the long-run performance of an organization. It includes environmental scanning, strategy formulation, strategy implementation, evaluation and control.

- A stream of decisions and actions which leads to the development of an effective strategy or strategies to help achieve corporate objectives. According to this definition, the end result of strategic management is a strategy or a set of strategies for the organization.
- Is the process of managing the pursuit of the organization's mission while managing the relationship of the organization to its environment; especially with respect to environmental stakeholders and the major constitutes in its internal and external environments that affect the actions.
- The set of activities related to the formulation and implementation of strategies to achieve organizational objectives. The emphasis in strategic management is on those general management responsibilities which are essential to relate the organization to the environment in which a way that its objectives may be achieved.
- Is the process of specifying an organization's objectives, developing policies and plans to achieve these objectives, and allocating resources so as to implement the plans. It is the highest level of managerial activity, usually performed by the company's Chief Executive Officer (CEO) and executive team. It provides overall direction to the whole enterprise. An organization's strategy must be appropriate for its resources, circumstances, and objectives. The process involves matching the companies' strategic advantages to the business environment the organization faces.

1.2 Historical Development of strategic Management

Strategic management as a discipline originated in the 1950s/ 60s. Although there were numerous early contributors to the literature, the most influential pioneers were Alfred D. Chandler, Philip Selznick, Igor Ansoff, and Peter Drucker.

Alfred Chandler recognized the importance of coordinating the various aspects of management under one all-encompassing strategy. Prior to this time the various functions of management were separate with little overall coordination or strategy.

Chandler also stressed the importance of taking a long term perspective when looking to the future. In his 1962 ground breaking work Strategy and Structure, Chandler showed that a long-term coordinated strategy was necessary to give a company structure, direction, and focus. He says it concisely, "structure follows strategy."

Philip Selznick (in 1975) introduced the idea of matching the organization's internal factors with external environmental circumstances. This core idea was developed into what we now call SWOT

analysis by Learned, Andrews, and others at the Harvard Business School General Management Group. Strengths and weaknesses of the firm are assessed in light of the opportunities and threats from the business environment.

Igor Ansoff built on Chandler's work by adding a range of strategic concepts and inventing a whole new vocabulary. He developed a strategy grid that compared market penetration strategies, product development strategies, market development strategies and horizontal and vertical integration and diversification strategies.

He felt that management could use these strategies to systematically prepare for future opportunities and challenges. In his 1965 classic Corporate Strategy, he developed the gap analysis still used today in which we must understand the gap between where we are currently and where we would like to be, then develop what he called "gap reducing actions".

Peter Drucker's contributions to strategic management were many but two are most important.

Firstly, he stressed the importance of objectives. An organization without clear objectives is like a ship without a rudder. As early as 1954 he was developing a theory of management based on objectives. This evolved into his theory of management by objectives (MBO). According to Drucker, the procedure of setting objectives and monitoring your progress towards them should permeate the entire organization, top to bottom.

His other seminal contribution was in predicting the importance of what today we would call intellectual capital. He predicted the rise of what he called the "knowledge worker" and explained the consequences of this for management. He said that knowledge work is non-hierarchical. Work would be carried out in teams with the person most knowledgeable in the task at hand being the temporary leader.

Activity 1.1

1. Who are early pioneers of strategic management concepts? (You can use the space provided below)

____

____.

2. How does they contribute for the development of strategic management?

1.3 Dimension of Strategic Decisions

There are several dimensions that distinguish a company's strategic decisions from other decisions. Typically, strategic issues have the following six dimensions.

1.3.1 Require Top-Management Decisions and Commitment

Since strategic decisions cover wider areas of a firm's operations, they require top-managements' involvement. Usually only top management has the perspective needed to understand the broad implications of such decisions and the power to authorize the necessary resource allocations.

1.3.2 Require Large Amounts of the Firm's Resources

Strategic decisions involve substantial allocations of people, physical assets, or money. These resources are either redirected from internal sources or swerved from outside the firm. Strategic decisions also commit the firm to actions over an extended period.

1.3.3 Affect the Firm's Long-Term Prosperity

Strategic decisions commit the firm for a long time, typically five years. However, their impact often lasts much longer. Once a firm has committed itself to a particular strategy, its image and competitive advantages usually are tied to that strategy. Firms become known in certain markets, for certain products, with certain technologies. They would jeopardize their previous gains if they shifted from these markets, products, or technologies by adopting a radically different strategy.

1.3.4 Future Orientation

Strategic decisions are based on what managers forecast rather than on what they know. In such decisions, emphasis is placed on the development of projections that will enable the firm to select the most promising strategic options.

1.3.5 Multi-functional or Multi business consequences

Strategic decisions have complex implications for most areas of the firm. Decisions about such materials as customers mix, competitive emphasis, or organizational structure necessarily involve a number of the firm's strategic business units (SBUs), divisions, or program units. All of these areas will be affected by allocations or reallocations of responsibilities and resources that result from these decisions.

1.3.6 Require considering External Environment

All business firms operate in an open system. They affect and are affected by external conditions that are largely beyond their control. Therefore, to successfully position a firm in competitive situations, its strategic managers must look beyond its operations by "thinking outside of the box."

1.4 The Strategic Management Process (Stages)

As mentioned above, strategic management is a process that consists of different phases, which are sequential in nature. The process of strategic management is depicted through a model, which

consists of different phases; and these phases are considered as sequentially linked to each other and each successive phase provides a feedback to the previous phases. Most authors agree that there are four essential phases in the strategic management process, though they may differ with regard to the sequence, emphasis or nomenclature.

These four phases could be put in a nutshell as follows: 1) Environmental Scanning 2) Strategy Formulation 3) Strategy Implementation 4. Evaluation and Control

1. Environmental Scanning: Environmental Scanning is the monitoring, evaluating, and disseminating of information from the external and internal environment to key people within the corporation. Its purpose is to identify strategic factors --- those external and internal elements that will determine the future of the corporation. The simplest way to conduct environmental scanning is through SWOT analysis. **SWOT** is an acronym used to describe those particular **S**trength, **W**eakness, **O**pportunity, and **T**hreats that are strategic factors for a specific company.

2. Strategy Formulation: this is the development of long range plans for the effective management of environmental opportunities and threats, in light of corporate strength and weakness.

3. Strategy Implementation: it is the process by which strategies and policies are put into action through the development of programs, budgets and procedures.

4. Evaluation and Control: this is the process in which corporate activities and performance results are monitored so that actual performance can be compared with desire performance.

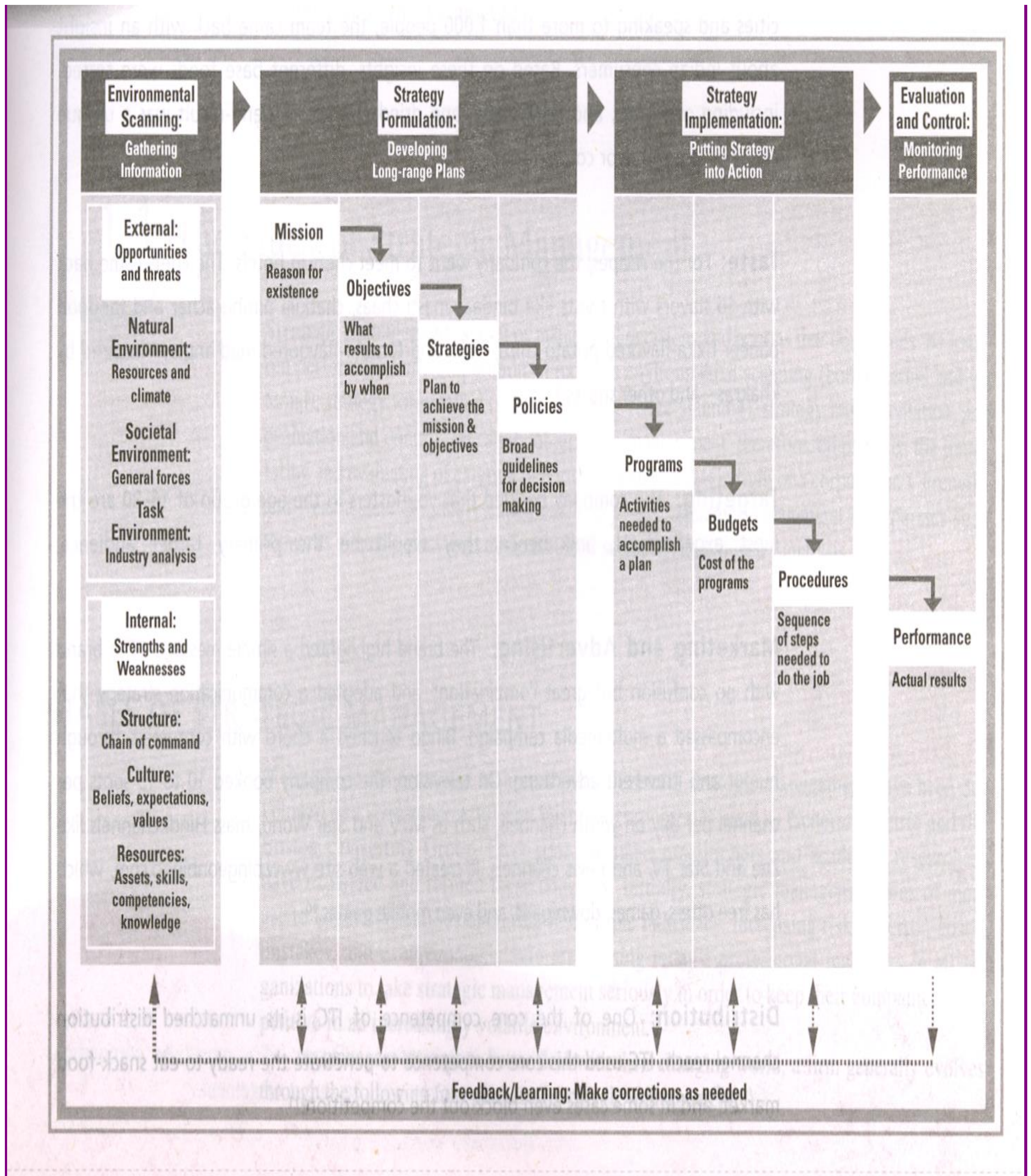


Fig: 1 Phases of the Strategic Management Process

Source: Thomas L. and David Hunger (2012) Strategic Management and Business Policy toward global sustainability, 13th edition.

Viewing strategic management as a process has several important implications.

1) First, a change in any component will affect several or all of the other components. Most of the arrows in the model point two ways, suggesting that the flow of information usually is reciprocal. For example, forces in the external environment may influence the nature of a company's mission, and the company may in turn affect the external environment by heightening competition.
2) The second implication is that strategy formulation and implementation are sequential. The process begins with the environmental scanning. Not every component of the strategic management process deserves equal attention each time planning activity takes place.
3) The third implication of viewing strategic management as a process is the necessity of feedback from implementation, review, and evaluation to the early stages of the process. Feedback can be defined as the collection of post implementation results to enhance future decision making. As shown in the model, strategic managers should assess the impact of implemented strategies on external environment and the company policy. Strategic managers should also analyze the impact of strategies on the possible need for modifications in the company mission.
4) The fourth implication is the need to regard the strategic management process as a dynamic system. The term dynamic characterizes the constantly changing conditions that affect interrelated and interdependent strategic attitudes. Since change is continuous, the dynamic strategic planning processes must be monitored constantly for significant shifts in any of its components as a precaution against implementing an obsolete strategy.

Self-test exercise

1. Among the following leading questions one should be addressed at strategy formulation phase of strategic management process
   A. Where organization want to go?
   B. How can organization achieve strategic plan?
   C. Where organization exist currently?
   D. What does the environment looks like?
   E. All are answers.
2. Which one of the following is incorrect;
   A. Strategic management is both art and science.

B. Strategic management model is always guarantee for action

C. Components in strategic management model are interrelated.

D. Strategic management is dynamic and continuous process.

E. None of the above.

1.5 Key Terms in Strategic Management

Activity 1.2

1. Define the following terms? Competitive advantage, strategy, tactic, policy and goal.

____
____
____
_______________________________.

Before we further discuss strategic management, we should define nine key terms: competitive advantage, strategists, vision and mission statements, external opportunities and threats, internal strengths and weaknesses, long-term objectives, strategies, annual objectives, and policies.

1. Competitive Advantage

Strategic management is all about gaining and maintaining competitive advantage. This term can be defined as "anything that a firm does especially well compare to rival firm".' When a firm can do something that rival firms cannot do, or owns something that rival firm's desire, that can represent a competitive advantage. Getting and keeping competitive advantage is essential for long-term success in an organization. Theories of organization present different perspectives on how best to capture and keep competitive advantage—that is, how best to manage strategically. Pursuit of competitive advantage leads to organizational success or failure. Strategic management researchers and practitioners alike desire to better understand the nature and role of competitive advantage in various industries. Normally, a firm can sustain a competitive advantage for only a certain period due to rival firms imitating and undermining that advantage. Thus it is not adequate to simply obtain competitive advantage.

A firm must strive to achieve sustained competitive advantage by

(1) Continually adapting to changes in external trends and events and internal capabilities, competencies, and resources; and by

(2) Effectively formulating, implementing, and evaluating strategies that capitalize upon those factors.

2. Strategists

Strategists are the individuals who are most responsible for the success or failure of an organization. Strategists have various job titles, such as chief executive officer, president, owner, chair of the board, executive director, chancellor, dean, or entrepreneur. Writers on organizational behavior say, "All strategists have to be chief learning officers. We are in an extended period of change. If our leaders aren't highly adaptive and great models during this period, then our companies won't adapt either, because ultimately leadership is about being a role model"

Strategists help an organization gather, analyze, and organize information. They track industry and competitive trends, develop forecasting models and scenario analyses, evaluate corporate and divisional performance, spot emerging market opportunities, identify business threats, and develop creative action plans. Strategic planners usually serve in a support or staff role. Usually found in higher levels of management, they typically have considerable authority for decision making in the firm. The CEO is the most visible and critical strategic manager. Any manager who has responsibility for a unit or division, responsibility for profit and loss outcomes, or direct authority over a major piece of the business is a strategic manager (strategist). Strategists differ as much as organizations themselves and these differences must be considered in the formulation, implementation, and evaluation of strategies. Some strategists will not consider some types of strategies because of their personal philosophies. Strategists differ in their attitudes, values, ethics, willingness to take risks, concern for social responsibility, concern for profitability, concern for short-run versus long-run aims, and management style.

3. Vision and Mission Statements

Many organizations today develop a vision statement that answers the question, "What do we want to become?" Developing a vision statement is often considered the first step in strategic planning, preceding even development of a mission statement. Many vision statements are a single sentence. For example, the vision statement of the Ethiopian Electric Power Corporation (EEPCo) is "To be

a centre of Excellence in providing quality electric service at every one's door and being competitive export industry."

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

An example of a mission statement is provided below for Microsoft.

Microsoft's mission is to create software for the personal computer that empowers and enriches people in the workplace, at school and at home. Microsoft's early vision of a computer on every desk and in every home is coupled today with a strong commitment to Internet-related technologies that expand the power and reach of the PC and its users. As the world's leading software provider, Microsoft strives to produce innovative products that meet our customers' evolving needs. At the same time, we understand that long-term success is about more than just making great products. Find out what we mean when we talk about Living Our Values (www.microsoft.com/mscorp/).

Another example of a mission statement of the Ethiopian Electric Power Corporation (EEPCo) is To provide adequate and quality electricity generation, transmission, distribution, and sales services, through continuous improvement of utility management practices responsive to the socio-economic development and environmental protection need of the public"

4. External Opportunities and Threats

External opportunities and external threats refer to economic, social, cultural, demographic, environmental, political, legal, governmental, technological, and competitive trends and events that could significantly benefit or harm an organization in the future.

Opportunities and threats are largely beyond the control of a single organization-thus the word external. The wireless revolution, biotechnology, population shifts, changing work values and attitudes, space exploration, recyclable packages, and increased competition from foreign companies are examples of opportunities or threats for companies. These types of changes are creating a different type of consumer and consequently a need for different types of products,

services, and strategies. Many companies in many industries face the severe external threat of online sales capturing increasing market share in their industry.

Other opportunities and threats may include the passage of a law, the introduction of a new product by a competitor, a national catastrophe, or the declining value of the dollar. A competitor's strength could be a threat. Unrest in the Middle East, rising energy costs, or the war against terrorism could represent an opportunity or a threat.

A basic tenet or principle of strategic management is that firms need to formulate strategies to take advantage of external opportunities and to avoid or reduce the impact of external threats. For this reason, identifying, monitoring, and evaluating external opportunities and threats are essential for success. This process of conducting research and gathering and assimilating external information is sometimes called environmental scanning or industry analysis. Lobbying is one activity that some organizations utilize to influence external opportunities and threats.

5. Internal Strengths and Weaknesses

Internal strengths and internal weaknesses are an organization's controllable activities that are performed especially well or poorly. They arise in the management, marketing, finance/accounting, production/operations, research and development, and management information systems activities of a business. Identifying and evaluating organizational strengths and weaknesses in the functional areas of a business is an essential strategic-management activity. Organizations strive to pursue strategies that capitalize on internal strengths and eliminate internal weaknesses.

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

Internal factors can be determined in a number of ways, including computing ratios, measuring performance, and comparing to past periods and industry averages. Various types of surveys also can be developed and administered to examine internal factors such as employee morale, production efficiency, advertising effectiveness, and customer loyalty.

6. Long-Term Objectives

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

7. Strategies

Strategies are the means by which long-term objectives will be achieved. Business strategies may include geographic expansion, diversification, acquisition, product development, market penetration, retrenchment, divestiture, liquidation, and joint venture.

Strategies are potential actions that require top management decisions and large amounts of the firm’s resources. In addition, strategies affect an organization’s long-term prosperity, typically for at least five years, and thus are future-oriented. Strategies have multifunctional or multidivisional consequences and require consideration of both the external and internal factors facing the firm.

8. Annual Objectives

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

9. Policies

Policies are the means by which annual objectives will be achieved. Policies include guidelines, rules, and procedures established to support efforts to achieve stated objectives. Policies are guides to decision making and address repetitive or recurring situations.

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

Substantial research suggests that a healthier workforce can more effectively and efficiently implement strategies. Take for example the "No Smoking" policies with in most organizations. No Smoking policies are usually derived from annual objectives that seek to reduce corporate medical costs associated with absenteeism and to provide a healthy workplace.

1.6 Approaches (Models) of Strategic Management

A. Industrial Organization (I/O) Model
B. Resource-Based Model

A. I/O Model of Above-average Returns

The Industrial Organization model suggests that above-average returns for any firm are largely determined by characteristics outside the firm. This model largely focuses on industry structure or attractiveness of the external environment rather than internal characteristics of the firm.

External Environments

1. Strategy dictated by the external environment of the firm (what opportunities exist in these environments?)

2. Firm develops internal skills required by external environment (what can the firm do about the opportunities?)

Four Assumptions of the I/O Model

1. The external environment is assumed to possess pressures and constraints that determine the strategies that would result in above-average returns

2. Most firms competing within a particular industry or within a certain segment of it are assumed to control similar strategically relevant resources and to pursue similar strategies in light of those resources
3. Resources used to implement strategies are highly mobile across firms
4. Organizational decision makers are assumed to be rational and committed to acting in the firm's best interests, as shown by their profit-maximizing behaviors

I/O Model of Above-Average Returns guide lines

1. Study the **external environment**, especially the industry environment
   - ✓ economies of scale
   - ✓ barriers to market entry
   - ✓ diversification
   - ✓ product differentiation
   - ✓ degree of concentration of firms in the industry

2. Locate an attractive industry with a high potential for above-average returns

Attractive industry: one whose structural characteristics suggest above-average returns

3. Identify the strategy called for by the attractive industry to earn above-average returns

Strategy formulation: selection of a strategy linked with above-average returns in a particular industry

4. Develop or acquire assets and skills needed to implement the strategy

Assets and skills: those assets and skills required to implement a chosen strategy

5. Use the firm's strengths (its developed or acquired assets and skills) to implement the strategy

Strategy implementation: select strategic actions linked with effective implementation of the chosen strategy

Industrial Organization Model

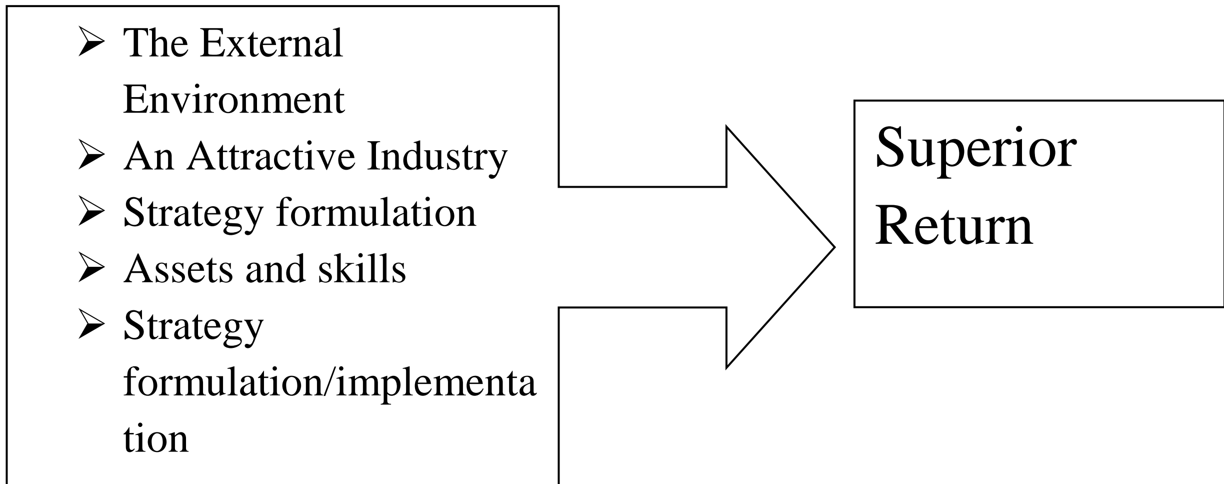


Fig: 2 industrial organization model

B. Resource-Based Model of Above-average Returns

The Resource-Based model suggests that above-average returns for any firm are largely determined by characteristics inside the firm. This model focuses on developing or obtaining valuable resources and capabilities which are difficult or impossible for rivals to imitate.

1. Strategy dictated by the firm's unique resources and capabilities
2. Find an environment in which to exploit these assets (where are the best opportunities?)

Resource-based Model of above Average Returns guidelines:

1. Identify the firm's resources--strengths and weaknesses compared with competitors

Resources: inputs into a firm's production process

2. Determine the firm's capabilities--what it can do better than its competitors

Capability: capacity of an integrated set of resources to perform a task or activity in an integrative manner. Four Attributes of Resources and Capabilities (Competitive Advantage)

i. **Valuable:** When they allow the firm to exploit opportunities or neutralize threats in its external environment
ii. **Rare:** When possessed by few, if any, current and potential competitors
iii. **Costly to imitate:** When other firms cannot obtain them or must obtain them at a much higher cost
iv. **Non-substitutable:** When they have no structural equivalents

Resources and capabilities that meet these four criteria become a source of:

core competencies: Core Competencies are the basis for a firm's Competitive **advantage,** Value **Creation and** Ability **to earn above-average returns**

3. Determine the potential of the firm's resources and capabilities in terms of a competitive advantage

Competitive advantage: ability of a firm to outperform its rivals

4. Locate an attractive industry

An attractive industry: an industry with opportunities that can be exploited by the firm's resources and capabilities

5. Select a strategy that best allows the firm to utilize its resources and capabilities relative to opportunities in the external environment

Strategy formulation and implementation: strategic actions taken to earn above average returns

Resource Based Model

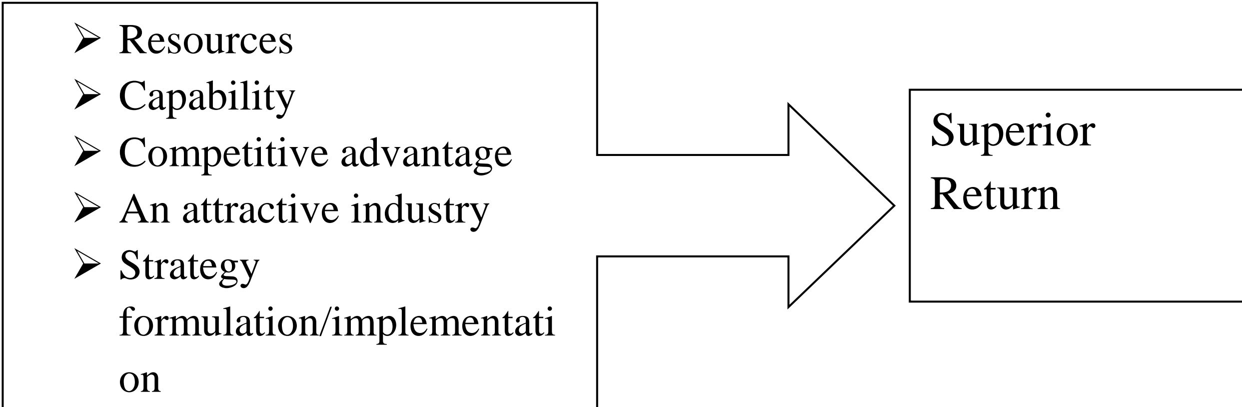
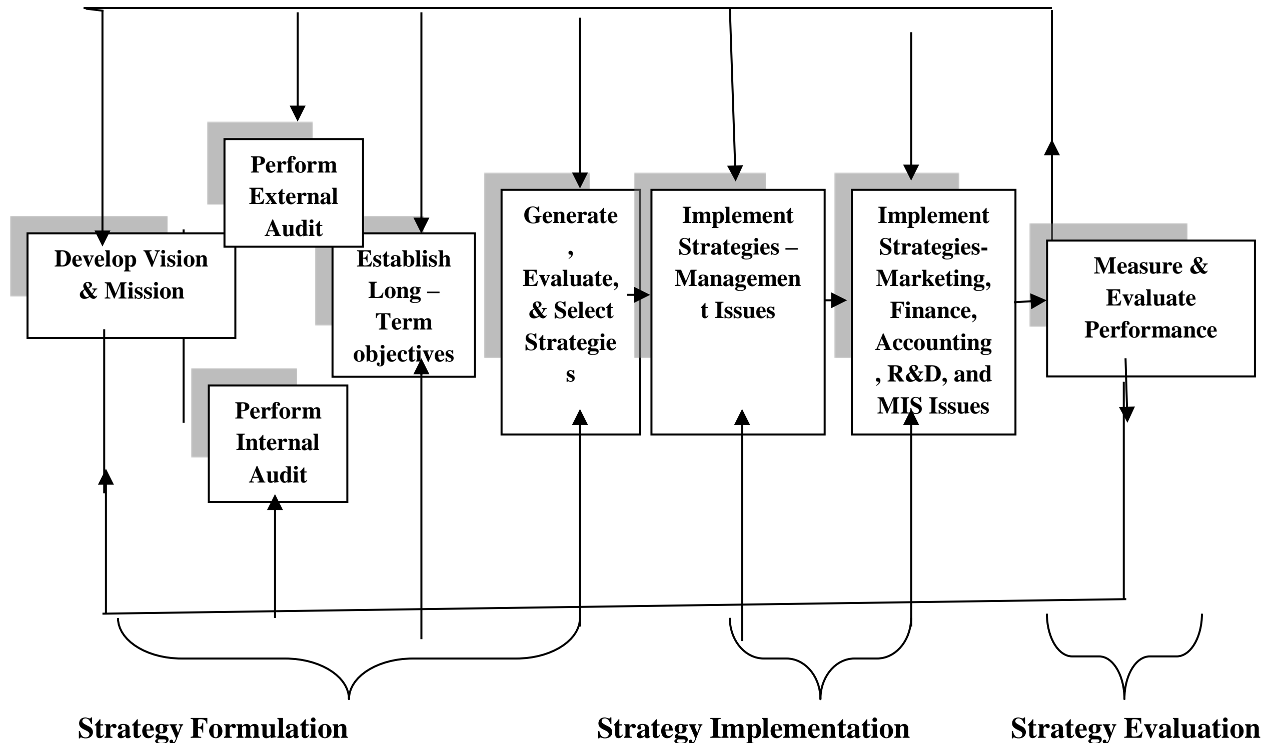


Fig: 3 Resource based model

1.7 The Strategic Management Model

The Strategic Management process can best be studied and applied using a model. Every model represents some kind of process. The framework illustrated in the following diagram is a widely accepted, comprehensive model of the Strategic Management process. This model does not guarantee success, but it does represent a clear and practical approach for formulating, implementing, and evaluating strategies.

Figure: 4 A comprehensive Strategic Management Model



Source: Fred R. David, "How Companies Define Their Mission," *Long Range Planning* 22, no. 3 (June 1988): 40

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

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

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

Application of the strategic-management process is typically more formal in larger and well-established organizations. Formality refers to the extent that participants, responsibilities, authority, duties, and approach are specified. Smaller businesses tend to be less formal. Firms that compete in complex, rapidly changing environments, such as technology companies, tend to be more formal in strategic planning. Firms that have many divisions, products, markets, and technologies also tend to be more formal in applying strategic-management concepts. Greater formality in applying the strategic-management process is usually positively associated with the cost, comprehensiveness, accuracy, and success of planning across all types and sizes of organizations.

1.8 Benefits of Strategic Management

Activity 1.3

1. What are the importance of strategic management?

   ____
   ____
   ______________________________________.
2. Few scholars stated that strategic management process is more important than the document (strategy) do you agree?

   ____
   ____

Historically, the principal benefit of strategic management has been to help organizations formulate better strategies through the use of a more systematic, logical, and rational approach to strategic choice. This certainly continues to be a major benefit of strategic management, but research studies now indicate that the process, rather than the decision or document, is the more important contribution of strategic management. Communication is a key to successful strategic management. Through involvement in the process, managers and employees become committed to plan supporting the organization. Dialogue and participation are essential ingredients. The manner in which strategic management is carried out is thus exceptionally important. A major aim of the process is to achieve the *understanding* and *commitment* from all managers and employees. Understanding may be the most important benefit of strategic management, followed by commitment.

Strategic Management

- ✓ allows an organization to be more proactive than reactive in shaping its own future;
- ✓ It allows an organization to initiate and influence (rather than just respond to) activities- and thus to exert control over its own destiny.

a) Financial Benefits of Strategic Management

Research indicates that organizations using strategic-management concepts are more profitable and successful than those that do not. High-performing firms tend to do systematic planning to prepare for future fluctuations in their external and internal environments.

Strategic management enhances the problem-prevention capabilities of organizations because it promotes interaction among managers' at all divisional and functional levels. Firms that have nurtured their managers and employees, shared organizational objectives with them, empowered them to help improve the product or service, and recognized their contributions can turn to them for help in a pinch because of this interaction.

In addition to empowering managers and employees, strategic management often brings order and discipline to an otherwise floundering firm. It can be the beginning of an efficient and effective managerial system. Strategic management may renew confidence in the current business strategy or point the need for corrective actions. The strategic-management process provides a basis for

identifying and rationalizing the need for change to all managers and employees of a firm; it helps them view change as an opportunity rather than as a threat.

Businesses using strategic management concepts show significant improvement in

- ✓ sales,
- ✓ profitability, and
- ✓ productivity

High-performing firms seem to make more informed decisions with good anticipation of both short- and long-term consequences. On the other hand, firms that perform poorly often engage in activities that are shortsighted and do not reflect good forecasting of future conditions.

b) Non-financial Benefits

Besides helping firms avoid financial demise, strategic management offers other tangible benefits, such as

- ✓ an enhanced awareness of external threats,
- ✓ an improved understanding of competitors' strategies,
- ✓ increased employee productivity,
- ✓ reduced resistance to change, and
- ✓ A clearer understanding of performance-reward relationships.

1.9. Business Ethics and Strategic Management

Activity 1.4

1. What ethical responsibilities does strategic managers have?

____
____
____.

Business ethics can be defined as principles of conduct within organizations that guide decision making and behavior. Good business ethics is a prerequisite for good strategic management; ***good ethics is just good business!***

Managers and employees of firms must be careful not to become scapegoats blamed for company environmental wrongdoings. Harming the natural environment is unethical, illegal, and costly. When organizations today face criminal charges for polluting the environment, firms increasingly are turning on their managers and employees to win leniency for themselves. Employee firings and demotions are becoming common in pollution-related legal suits. Managers' being fired at in some organizations for being indirectly responsible for their firms' polluting water exemplifies this corporate trend. Therefore, managers and employees today must be careful not to ignore, conceal, or disregard a pollution problem, or they may find themselves personally liable. In this regard, more and more companies are becoming ISO 14001 certified, as indicated in the "Natural Environment Perspective."

A new wave of ethics issues related to product safety, employee health, sexual harassment, AIDS in the workplace, smoking, acid rain, affirmative action, waste disposal, foreign business practices, cover-ups, takeover tactics, conflicts of interest, employee privacy, inappropriate gifts, security of company records, and layoffs has accented the need for strategists to develop a clear code of business ethics. A code of business ethics can provide a basis on which policies can be devised to guide daily behavior and decisions at the work site.

The explosion of the Internet into the workplace has raised many new ethical questions in organizations today. The "E-Commerce Perspective" focuses on business ethics issues related to the Internet.

Merely having a code of ethics, however, is not sufficient to ensure ethical business behavior. A code of ethics can be viewed as a public relations gimmick or device, a set of platitudes, or window dressing. To ensure that the code is read, understood, believed, and remembered, organizations need to conduct periodic ethics workshops to sensitize people to workplace circumstances in which ethics issues may arise. If employees see examples of punishment for violating the code and rewards for upholding the code, this helps reinforce the importance of a firm's code of ethics.

An ethics "culture" needs to permeate or fill organizations! To help create an ethics culture, some organizations have developed a code-of- conduct manual outlining ethical expectations and giving examples of situations that commonly arise in their businesses.

Although primary responsibility for ensuring ethical behavior rests with a firm's strategists, an integral part of the responsibility of all managers is to provide ethics leadership by constant

example and demonstration. Managers hold positions that enable them to influence and educate many people. This makes managers responsible for developing and implementing ethical decision making. Many scholars on the issue offer some good advice for managers.

No society anywhere in the world can compete very long or successfully with people stealing from one another or not trusting one another, with every bit of information requiring notarized confirmation, with every disagreement ending up in litigation, or with government having to regulate businesses to keep them honest. Being unethical is a recipe for headaches, inefficiency, and waste. History has proven that the greater the trust and confidence of people in the ethics of an institution or society, the greater its economic strength. Business relationships are built mostly on mutual trust and reputation. Short-term decisions based on greed and questionable ethics will preclude the necessary self-respect to gain the trust of others. More and more firms believe that ethics training and an ethics culture create strategic advantage.

Some business actions considered to be unethical include misleading advertising or labeling, causing environmental harm, poor product or service safety, padding expense accounts, insider trading, dumping banned or flawed products in foreign markets, lack of equal opportunities for women and minorities, overpricing, hostile takeovers, moving jobs overseas, and using nonunion labor in a union shop.

Internet fraud, including hacking into company computers and spreading viruses, has become a major unethical activity that plagues every sector of online commerce from banking to shopping sites. More than three hundred Web sites now show individuals how to hack into computers; this problem has become endemic nationwide and around the world.

Ethics training programs should include messages from the CEO emphasizing ethical business practices, the development and discussion of codes of ethics, and procedures for discussing and reporting unethical behavior. Firms can align ethical and strategic decision making by incorporating ethical considerations into long-term planning, by integrating ethical decision making into the performance appraisal process, by encouraging whistle-blowing or the reporting of unethical practices, and by monitoring departmental and corporate performance regarding ethical issues.

1.10. Types of strategy (Deliberate and emergent strategy)

Mintzberg and Waters (1985) classify organizational strategies as either deliberate or emergent. A strategy can be described as deliberate where the collective vision, goals and / or intention(s) of an organization (in most cases, as determined by its leadership) is articulated as broadly and in as much detail as possible, communicated to the employees – those responsible for implementation within that organization in order to realize a given outcome.

On the other hand, strategy can be described as emergent where consistencies arise in the actions / behavior of an organization over a period of time, even though the adoption of such behavior / actions was never explicitly intended; an example of this can occur 'when an environment directly imposes a pattern of action on an organization'

Advantages and disadvantage of deliberate and emergent strategy

There is no universal consensus on which approach is better than the other as each has its own advantages and disadvantages and ultimately, determination of the most suitable strategy formulation method is up to an organization's management.

Advantage

Deliberate strategies

- ✓ Where management's intentions are clearly and explicitly spelt out, it becomes easier for actors to understand, identify and work towards a common collective purpose at a minimized level of deviation from the intended objective.
- ✓ Focus on a particular desired outcome is honed and the organization's participants are provided with a clear and unambiguous sense of direction.

Emergent strategy

- ✓ This approach allows flexibility of business decisions.
- ✓ Users of this strategy class are able to adjust their patterns in reaction to realized outcomes of their present actions.

Disadvantage

Deliberate strategies: being fixated on a specific outcome may increase an organizations rigidity and lower its speed of responsiveness in the event of changes in their operating environment or

negative feedback received from the pursuit of a particular strategy (as opposed to the flexibility offered by emergent strategies).

Emergent strategy: By nature, emergent strategy occurs as part of ongoing organizational activity. While a business could forgo a deliberate strategy and rely on an emergent strategy to develop, the odds of such order manifesting from pure, unstructured business activities remains slim. As such, emergent strategy does not offer a genuine alternative to more traditional deliberate strategy, especially for new businesses operating on narrow margins. At best, it serves to complement and serve as a corrective measure for deliberative strategy.

Chapter summary

This chapter provides an overview of strategic management and strategy. Ideas about strategy span many centuries, and modern understanding of strategy borrows from ancient strategies as well as classic militaries strategies. You should now understand that there are numerous ways to Conceptualize the idea of strategy and that effective strategic management is needed to ensure the Long-term success of firms. The study of strategic management provides tools to effectively manage organizations, but it also involves the art of knowing how and when to apply creative thinking.

Strategic management is continuous and dynamic process of strategy formulation, implementation and evaluation. Strategy management requires the involvement and commitment of employees and managers in each phases.

Chapter review questions

Part I: <u>Multiple Choice</u>:

1. Strategist is:
   - **A.** A manager who has responsibility for a unit or division, profit and loss outcomes
   - **B.** President who is most responsible for the success or failure of an organization.
   - **C.** Entrepreneur who can manage change and continuously adapting to it.
   - **D.** Executive director who is most visible and play critical roles strategic plan.
   - **E.** All are answers
2. One of the following is false about ***polices:***

A. They are the means by which annual objectives will be achieved.

B. Policies are guides to decision making and address repetitive or recurring situations

C. Policies allow consistency and coordination within and between organizational departments

D. They are particularly significant in strategy formulation.

E. None of the above

3. One the following influential pioneers of strategic management introduced the idea of "gap analysis".

   A. Igor Ansoff
   B. Philip Selznick
   C. Peter Drucker
   D. Alfred D. Chandler

4. Assume you are management consultant, which idea would you recommend for organizations to maintain their competitive advantage for long time;

   A. Consistently responding to change.
   B. Using strategic management concepts
   C. Effectively formulate and implement strategy.
   D. Properly identify competitive advantages.
   E. None of the above
   F. All are answers

5. Which of the following is incorrect statement:

   A. Deliberate strategies are clearly and explicitly spelt out.
   B. Deliberate strategies provided with a clear and unambiguous sense of direction.
   C. Realized strategy allows flexibility of business decisions.
   D. Realized strategy emerges from collective actions not intention.
   E. None of the above

6. Anything which makes an organization superior to its competitors is:

   A. Threat
   B. Competitive advantage
   C. Strength
   D. Weakness
   E. Policy

7. Which of the following is true about the resource based model?

A. The model suggests that strategy dictated by the firm's unique resources and capabilities.
B. An industries characteristics can have high impact on affirms success.
C. Strategies used to compete against rivalries decided by external environment.
D. All are answers.
E. None of the above

8. Pick the correct sentence.
   A. Strategic decisions have complex implications for most areas of the firm.
   B. Strategic decisions impact often lasts much longer.
   C. Organizations affect and are affected by external conditions.
   D. Strategic decisions require top-managements' involvement.
   E. All are answers
9. Pick the incorrect sentence
   A. Strategy management process is more important than strategy.
   B. Strategy ties all the parts of an organization together.
   C. Strategy is originated from art of military general.
   D. Strategic decisions requires top manager's involvement and commitment.
   E. None of the above.
10. Which one of the following is incorrect;
    A. Strategic management is both art and science.
    B. Strategic management model is always guarantee for action
    C. Components in strategic management model are interrelated.
    D. Strategic management is dynamic and continuous process.
    E. None of the above.

Part II: <u>Give short answers</u>

1. What aspect of strategy management do you think requires the most time? Why?
2. Why is it so important to integrate intuition and analysis in strategic management?
3. Discuss the importance of feedback in the strategic-management model.
4. How can strategist's best ensure that strategies will be effectively implemented?
5. Discuss the role of business ethics in strategic management

CHAPTER TWO-STRATGEY FORMULATION

BUSINESS VISION, MISSION, VALUES, OBJECTIVES AND GOALS

Aim of the chapter

Every organization has a unique purpose and reason for being. This uniqueness should be reflected in vision and mission statements. The nature of a business vision and mission can represent either a competitive advantage or disadvantage for the firm. An organization achieves a heightened sense of purpose when strategists, managers, and employees develop and communicate a clear business vision and mission. Drucker says that developing a clear business vision and mission is the "first responsibility of strategists." A good mission statement reveals an organization's customers; products or services; markets; technology; concern for survival, growth, and profitability; philosophy; self-concept; concern for public image; concern for employees, business value and purpose.

Learning objectives:

After studying this chapter, you should be able to:

- Describe the nature and role of vision and mission statements in strategic management.
- Discuss why the process of developing a mission statement is as important as the resulting document.
- Identify the components of mission statements.
- Evaluate mission statements of different organizations.
- Write good vision and mission statements for your organization.
- Differentiate goal and objective

1. Introduction

This chapter focuses on the concepts and tools needed to evaluate and write business vision and mission statements. Actual mission statements from large and small organizations and for-profit and nonprofit enterprises are presented. The process of creating a vision and mission statement is discussed. The global economic recession has resulted in many firms changing direction and thereby altering their entire vision and mission in order to survive.

We can perhaps best understand vision and mission by focusing on a business when it is first started. In the beginning, a new business is simply a collection of ideas. Starting a New business rests on a set of beliefs that the new organization can offer some product or service to some customers, in some geographic area, using some type of technology, at a Profitable price. A new

business owner typically believes that the management philosophy of the new enterprise will result in a favorable public image and that this concept of the business can be communicated to, and will be adopted by, important constituencies. When the set of beliefs about a business at its inception is put into writing, the resulting document mirrors the same basic ideas that underlie the vision and mission statements. As a business Grows, owners or managers find it necessary to revise the founding set of beliefs, but those Original ideas usually are reflected in the revised statements of vision and mission. Vision and mission statements often can be found in the front of annual reports. They often are displayed throughout a firm's premises and are distributed with company information sent to constituencies. The statements are part of numerous internal reports, such as Loan requests, supplier agreements, labor relations contracts, business plans, and customer Service agreements. In a recent study, researchers concluded that 90 percent of all companies have used a mission statement.

2.1 BUSINESS Vision

2.1.1 What is Vision Statement?

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

While a vision statement doesn't tell you how you're going to get there, it does set the direction for your business planning. That's why it's important when crafting a vision statement to let your imagination go and dare to dream – and why it's important that a vision statement captures your passion. Unlike the mission statement, a vision statement is for you and the other members of your company, not for your customers or clients. When writing a vision statement, your mission statement and your core competencies can be a valuable starting point for articulating your values. Be sure when you're creating one not to fall into the trap of only thinking ahead a year or two. Once you have one, your vision statement will have a huge influence on decision making and the way you allocate resources.

A vision usually precedes the mission statement. It is usually short, concise and preferably limited to one sentence. Organization-wide management involvement is advisable.

Vision defines the desired or intended future state of an organization or enterprise in terms of its fundamental objective and/or strategic direction.

In short, vision statement;

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

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

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

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

2.1.2. Purpose of Vision

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

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

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

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

2.1.3. Features of an effective vision statement includes:

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

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

2.2 What is Business Mission?

Activity 2. 1

1. What does mission statement states about?
   ____
   ____.
2. Differentiate mission and vision statements?
   ____
   ____.
3. What is the importance of formulating vision and mission statement?
   ____
   ____.

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

Mission statement-is an enduring statement of purpose distinguishes one firm from another in the same business. It is a declaration of a firm's reason for existence. Mission is a well convincible statement included fundamental and unique purpose which makes it different from other organization. It identifies scope of it operation in terms of product offered and market served. Mission also means what we are and what we do. A survey in a North America and in Europeans corporation reveal that 60% to 75% have written or formal and remaining has no written or formal mission.

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

Mission statement is;

- general statement about the basic purpose of the organization
- the description of an organization's reasons for existence,
- fundamental purpose clarifies/ declares the purpose
- defines company's business; Product/ market; Territory/ geography
- Is the guiding principle that drives the processes of goal and action plan formulation, "a pervasive, although general, expression of the philosophical objectives of the enterprise."
- Should focus on "long – range economic potentials, attitudes toward customers, product and service quality, employee relations, and attitudes toward owners."
- Provides identity, continuity of purpose, and overall definition, and
- Should convey the following categories of information.
    1. Precisely why the organization exists, its purpose, in terms of
        - ✓ its basic product or service,
        - ✓ its primary markets, and
        - ✓ its major production technology.
    2. The moral and ethical principles that will shape the philosophy and character of the organization.
    3. The ethical climate within the organization.

Thus mission outlines the firm's identity and provides a guide for shaping strategies as all organization Mission statements often contain the purpose and aim of the organization; the organization's primary stakeholders: clients, stockholders, congregation, etc. responsibilities of the organization toward these stakeholders; products and services offered.

A mission statement is like a flag the organization can hold up that gives the essence of what it is about. Some mission statements are complex, long, and very broad; whereas some mission statements are simple and direct.

According to Vern McGinis, a mission should:

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

Criteria for evaluating mission

Criteria for evaluating mission statement include the following. The mission statement

- ☞ Is clear and understandable to all personnel, including rank and file employees.
- ☞ Is brief enough for most people to keep it is mind. This typically means one hundred words or less, which is possible.
- ☞ Clearly specifies the organization's basic function.
- ☞ Should serve as a template and be the means by which officials and others in the organization can make decisions.
- ☞ The wording should help it serves as an energy source and rallying point for the organization.

The role of mission

The role played by mission in guiding the organization is an important one specifically it;

2. Serves as a basis for consolidation around the organization's purpose.
3. Provides impetus to and guidelines for resource allocation.
4. Defines the internal atmosphere of the organization, its climate.
5. Serves as a set of guidelines for the assignment of job responsibilities.
6. Facilitates the design of key variables for a control system.

2.2.1 Characteristics of a Good Mission Statements

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

Mission statement should be

- ✓ **Feasible**: a mission should always aim high but it should not be an impossible statement. In addition it should be realistic and achievable. Its followers must find it to be credible. But feasibility depends on the resources available to work towards a mission.
- ✓ **Precise**: should not be so narrow to restrict the organization's activities nor should it be too broad to make itself meaningless.
- ✓ **Clear**: should be clear enough to lead to action and should not be a high sounding set platitudes meant for publicity purposes.
- ✓ **Motivating**: should be motivating for members of the organization or being its customers.
- ✓ **Distinctive**: the indiscriminate one (random, arbitrary) is likely to have little impact. If all defined their mission in a similar fashion, there would not be much of a difference among them. if defined as providing value for money, for years it created an important distinction in the public mind.
- ✓ **Indicate major components of strategy**: along with the organizational purpose should indicate the major components of the strategy to be adopted.
- ✓ **Indicate how *objectives* are to be accomplished**: Besides indicating the broad strategies to be adopted, it should also provide clues regarding the manner in which the objectives are to be accomplished.

<u>The difference between strategic vision and mission</u>

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

2.2.2. Components of a Mission Statement

Mission statements can and do vary in length, content, format, and specificity. Most practitioners and academicians of strategic management consider an effective statement to exhibit nine characteristics or

components. Because a mission statement is often the most visible and public part of the strategic management process, it is important that it includes all of these essential components. Components and corresponding questions that a mission statement should answer are given here.

Figure 2:1 elements of mission statement

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

Example:

We aspire to make PepsiCo the world's (3) premier consumer products company, focused on convenient foods and beverages (2).We seek to produce healthy financial rewards for investors (5) as we provide opportunities for growth and enrichment to our employees (9), our business partners and the communities (8) in which we operate. And in everything we do, we strive to act with honesty, openness, fairness and integrity (6). (This mission Statement lacks three components: Customers, Technology, and Self-Concept)

Self-test exercise

Identify the components which are mentioned in this mission statement.

2. Dell's mission statement "…… is to be the most successful computer company in the world at delivering the best customer experience in markets we serve. In doing so, Dell will meet customer expectations of highest quality; leading technology; competitive pricing; individual and company accountability; best-in-class service and support; flexible customization capability; superior corporate citizenship; financial stability".

2.2.3. Importance of Mission Statements

- Unanimity of purpose within the organization
- Basis for allocating resources
- Establish organizational climate
- Focal point for direction
- Translate objectives into work structure
- Cost, time and performance parameters assessed and controlled
- Most companies are now getting used to the idea of using mission statements.

2.3 BUSINESS VALUES

What are business values?

Activity 2.2

1. What does business value mean? ____.
2. How does organizations develop sense of mission? ____.

Business values are the core principles or standards that guide the way you do business. They sum up what your business stands for and what makes it special. While business plans and strategies may change the core values of your business remain the same.

For example - some businesses say that innovation is one of their core values - they are constantly developing new products or services and this shapes their whole approach to business.

Other businesses may say that they are agile - they are constantly responding to change and creating new opportunities for customers.

Every business is different and will have its own set of values - whether or not these are articulated. Mission of the company communicates the firm's core ideology and visionary goals. It should contain the company's core values, core purpose, and visionary goals. When the visionary goals are selected, the core values and purpose of the firms should be discovered. Values and purpose are in the company already; the mission just describes them. In that case, the stakeholders are more likely to believe in the company's mission.

Values are desirable qualities and beliefs that are shared among the stakeholders of an organization. They are often linked with our beliefs and commitments and what we see to be the rights of service users. They drive an organization's culture and priorities.

Values define the *philosophy of operation* and the organization culture being practiced by the organization. There must be congruence between the organization's values and the strategic plan.

- Values are the beliefs and moral principles that lie behind the organization's culture.
- Values give meanings to norms and behaviors in the organization.
- In many organizations, ***organizational values*** are *not explicit* and can only be understood by perceiving the philosophical rational that lies behind management behavior.
- Values can provide a rational for behavior that is just as strong as strategy.

For example, values include:

- People having equal access to services irrespective of their country of origin,
- Respecting the worth and dignity of each person,
- Service users being involved in choices about available services.

The values of individuals and organizations will affect their approaches to service delivery and answers to such questions as:

- What are quality services?
- How do you get quality services?

- How do you know you are providing quality services?

Values are:

Individual Values:-

- This is examination of personal values of the organization's manager and staff.
- These values often become part of the organizational system.
- This is important because the organization's values are often reflective of consensual values of individuals.

Strategic Values:-

- These are values related to strategic logic of the organization.
- They define not what kind of people we are but what we do such as commitment to excellence and empowerment.

Operational Values:-

- These are related to day-to-day operations of different parts of the organization.
- They define how things are done.

Acceptance of the values represented by mission can lead *to three characteristics* of firms that accomplish this acceptance.

- *Values stand for something*
    - o the way in which business is to be conducted is widely understood.
- *values are accepted by all employees*
    - o through the firm's organization structure from topmost level of management down to the lowest level of production jobs
- *Employees feel special* because of a sense of identity which distinguishes the firm from other firms.

A sense of mission is an emotional commitment felt by people towards the organization's mission. It occurs when there is a match between the values of an organization and those of an individual. Because organization values are rarely explicit, the individual sense them through the organization's behavior standards.

Making an organization's values explicit does not of course mean that these explicit values will be acted on all the time.

Statements of values that are too general (umbrella like) will not be as useful as more specific statements that identify your organization's values as different from other organizations' values.

2.4. Strategic issues

A strategic issue is "…a forthcoming development, either inside or outside of the organization, which is likely to have an important impact on the ability of the enterprise to meet its objectives.

Strategic issues are those fundamental policy choices or critical challenges that must be addressed for a community to achieve its vision.

Strategic issues are fundamental policy questions or critical challenges that affect:

- ✓ an organization's mandates, mission and values
- ✓ product or service level and mix
- ✓ clients, users, or payers, or
- ✓ Cost, financing, organization or management.

Evaluation Criteria:

A statement of a strategic issue should contain three elements:

1. The issue should be described succinctly, preferably in a single paragraph, and it should be framed as a question the organization can do something about.
2. The factors that make the issue a fundamental challenge should be listed. In particular, what in terms of the organization's mandates, mission, values, internal strengths and weaknesses, and external opportunities and threats, make this a strategic issue?
3. The consequences of failing to address the issue should be identified, so that the organization will know what kind of issues it faces. There are three kinds:

i. those for which no action is required at present, but which must be monitored

ii. those that are coming up on the horizon and are likely to require some action in the future and perhaps some action now

iii. those that require an immediate response

2.5 Setting organizational objectives and goals

Activity 2.3

1. What does goal and objective mean?

 ____
 ________________________________.

2. Differentiate goal and objective?

 ____
 ____.

When you have something you want to accomplish, it is important to set both *goals and objectives*. The two key sides of writing *goals and objectives:* be persistent with your goals, but flexible.

Strategic goals/ objectives

- Convert strategic vision & mission into specific performance targets
- Create yardsticks to track performance
- Pushes firms to inventive & focused on results
- Helps prevent complacency & coasting.

Strategic goals help firms

- Increase firms market share
- Overtake key rivals on quality & customer service or product performance
- Attain lower overall costs than rivals
- Boast firm's reputation with customers
- Attain stronger foothold in international market
- Achieve technological superiority
- Becomes leaders in new product introduction
- Capture attractive growth opportunities

Aims/ goals

- Aims and goals are *often use interchangeably*.
- Aims are *general statements of what we intend to achieve in relation to clients needs.*
- Aim is a broad statement of what we are trying to achieve. Because of this aim/ goals are not usually written in a way that we would know whether we have achieved them.

The first step in managing anything is to define your objective before you release any resources or anytime trying to achieve it.

Objective

- Indicate how goals are achieved.
- Desirable outcomes of organizational activity
- Is very specific statement
- Are more specific than goals.
- Are specific statements of what you intend to achieve.
- Is a very specific statement what is to be done to accomplish the mission.
- Ideally should be SMART:

A statement of an objective makes clear.

- What is to be accomplished
- How much is to be accomplished
- By when it is to be accomplished
- By whom it is to be accomplished

Examples of goals, objectives and targets

- Goal: earn $20,
- Objective: sell second hand shirts for $2 each,
- Target: 10 people Goals: knows about the human body.

Example of objectives

- To achieve 20% - 25% return on equity.
- To achieve 27% return on capital employed.
- For 35 parents each week with to have a 2 hour break from their children for the next 12 months.
- For 10 newly arrived migrants each week to be able to find out the services available for them in their area
- For 35 children under the age of 5 to experience a creative learning environment for four hours per week for the next 12 months.

Objectives are the end results of planned activity. They state what is to be accomplished by when and should be quantified if possible.

What are the differences between goals and objectives?

The two terms are often used interchangeably, confusion sometimes arises. Although both goals and objectives use the language of outcomes, the characteristic that distinguishes goals from objectives is *the level of specificity*.

The *difference between* where we are (current status) and where we want to be (vision and *goals*) is what we do (target *objectives* and action plans).

- *Goals* are statements about general aims or purposes of activities that are broad, long-range intended outcomes; and used primarily in policy making and general program planning.
- *Objectives* are brief, clear statements that describe the desired learning outcomes of instruction.
- *Goals* are what we want to achieve. *Goals* (aims) are where you want to go.
- *Objectives* are how you are going to get.

  Goals express intended outcomes in general terms and objectives express them in specific terms.
- Objectives are short but clear statements about the specific outcomes

- A goal is something personal that you aim to become or have done. An objective is something that is a requirement that should be met in any way possible.
- Goals are what you aim for, what you want to obtain; objectives are the move or plan on how to achieve the goals.
- Goals are written in broad, global, and sometimes vague, language. Objectives are statements that describe the intended results of instruction in terms of specific student behaviors.
- Goals are general directions that are not specific enough to be measured. On the other hand, objectives are specific, measurable and set within a timeframe.
- Goals are broad objectives are narrow.
- Goals are general intentions; objectives are precise.
- Goals are intangible; objectives are tangible.
- Goals are abstract; objectives are concrete.
- Goals can't be validated as is; objectives can be validated
- Goals are *what you set to achieve the mission of your organization or program.* Goals should *include words such* as "increase/decrease," "deliver," "improve" and "create." Objectives are *milestones that are along the way to reaching your goal.*

In reality,

- An aim is a target -something to which you aspire, or something you aim to achieve. An objective on the other hand, is something that you can achieve.
    - *E.g.: My aim is to lose weight, but my objective is to lose one pound a week.*
- Goals are broad statement of desired outcomes – what we hope will know and be able to do as a result of completing the program/course. Objectives are clear, brief statements used to describe specific measurable act.
- Objectives are *potential goals*. Goals are accomplishments (things you wish to complete). Aims are your ability to not be side tracked while reaching for your goals. Visions are visualizing your entire task to complete a goal.
- A goal is a target or a desired result. The aim is the process of orienting yourself and your actions towards a goal or an ambition. An aim is like a relatively long term plan of action.
- Goals are what you aim for, what you want to obtain; objectives are the move or plan on how to achieve the goals `target are the ones, the thing or the place where you must execute the objectives to attain the goals.

Writing Good Goals

Goals should be very clear, and someone should be able to determine what the program's purpose is from reading only your goals. A useful model for writing aims is using: *for*.......... (Such and such a group of people); *to*........... (Gain such and such a benefit).

Linking Goals and Objectives

Each goal should have at least one objective, though most will have several. The objective shows your funder how you will get to your goal.

Setting Objectives

Objective setting requires of all managers regardless of their position. Because every unit in the organization need concert, measurable performance targets that contribute meaningfully toward achieving company objectives.

An alternative *approach to setting objectives* is to write objectives such as: For the client/ customer to

- identify what the need is
- articulate the need
- identify what needs to be done to meet the need
- increase their self-esteem / confidence so it is possible for them to act to meet their needs
- Do what needs to be done to meet their needs.

Purpose of setting objectives

The purpose of setting objectives is to convert managerial statements of business mission and vision into strategic performance targets.

Objective setting implies challenge, establishing performance targets that require stretched and disciplined effort. The challenge of trying to close the gap between actual and desired performance pushes an organization to be more inventive.

The objectives established by managers include both short range and long range performance objectives.

Short range objectives

- Spell out the immediate improvement and outcome management desires.

Long-term objectives

- Prompt managers to consider what to do now to position the company to perform well over the long term.

Self- test exercise

1. Formulate goal for any type organization?
2. Formulate objective for any type of organization?
3. Differentiate goal and objectives

Roles of Objectives

The achievement of corporate objectives should result in the fulfillment of the corporation's mission. *Objectives play an important role* in strategic management, such as

- *Objectives define the organization's relationship with its environment*
  - By stating its objectives, an organization commits itself to what it has to achieve for its employees, customers and the society at large.
- *Objectives help on organization pursue its mission and purpose*
  - By defining the long-term position that an organization wishes to attain and the short-term targets to be achieved
- *Objectives provide the basis for strategic decision making*
  - by directing the attention of strategists to those areas where strategic decisions need to be taken
  - objectives lead to desirable standards of behavior and in this manner, help to coordinate strategic decision making
- *Objectives provide the standard for performance appraisal*
  - By stating goals and targets to be achieved in a given time period, and the measures to be adopted, objectives lay down the standards against which organization as well as individual performance would have no clear and definite basis for evaluating its performance.

Characteristics of Objectives

Objectives as measures of organizational behavior and performance, should possess certain desirable characteristics in order to be effective. Such characteristics are manly:

- *Objectives should be **understandable**:*
  - objectives play an important role in strategic management and are put to use in a variety of ways
  - They should be understandable by those who have to achieve them.

- If something is not understandable by managers no action will be taken or ever a wrong action might be taken.

- *Objectives should be **concrete and specific***
  - Better to say "Our Company plans to achieve a 12% increase in sale" than "our company seeks to increase its sales". The first statement implies a concrete and specific objective and is more likely to lead and motivate the managers.
- *Objectives should be **related to a time frame***
  - If objectives are related to a time frame, then managers knew the duration within which they have to be achieved.
  - If the statement given above is restricted as "our company plans to increase its sales by 12% by the end of two years" it enhances the specificity of objectives.
- *Objectives should be **measurable and controllable**:*
  - Many organizations perceive themselves as companies, which are attractive to work for.
  - If measures like the number and quality of job applications received, it would be possible to measure and control the achievement of this objective with respect to comparable companies in a particular industry and in general.
- *Objectives should be **challenging***
  - Objectives that are too high and too low are both de-motivating and, therefore, should be set at challenging but not unrealistic levels.
  - To set a high sales target in a declining market does not lead to success and also a low sales target in a burgeoning (rapidly increasing, growing, mushrooming) market is easily achievable and therefore, leads to sub-optimal performance.
- *Different objective should **correlate with each other***
  - Organizations set many objectives in different areas. If objectives set in one area are disregarding the other areas, such an action is likely to lead to problems.
  - Different objectives correlate with each other are mutually supportive, and result in synergistic advantages. This is specifically true for organizations, which operate on a profit center basis.
- *Objectives should be **set within constraints***
  - there are many constraints - internal as well as external, which have to be considered in objective-setting
  - for example: resource availability is an internal constraint which affects objective setting.

- o Different objectives compete for scarce resources and tradeoffs are necessary for optimum resource utilization.
- o Organizations face many interests, and environmental pollution. All these limit the organizations ability to set and achieve objective.

In sum, objective setting is a complex process; we will further examine a few issues relevant to objective in order to understand this complex process.

Making Objectives SMART

You should create your objectives to be SMART. SMART objectives means

1. **Specific (S)**

- Well defined, significant, stretching
- Clear to anyone that has a basic knowledge of the project
- Objectives must be clear and un ambiguous, vagaries and platitudes have no place in objective /goal setting
- When objectives are specific, they communicate exactly what is expected, when, and how much
- Focus, creates a powerful force: goal/objective power

The more focused your energies, the more power you generate

N.B:- Too many goals dilute focus, Optimal 2 - 3 goals per unit at any one time!

2. **Measurable (M)**

- Measurable, meaningful, motivational
    - o Know if the goal is obtainable and how far way the completion is
    - o Know when it has been achieved
- Track team progress ; help/ keep the team motivated

N.B:- A goal without a measurable outcome is like a sports competition without a scoreboard or scorekeeper.

3. **Attainable (A)**

- agreed upon achievable, acceptable, action-oriented
- Agreement with all the stakeholders what the goals should be
- Goals must be achievable and attainable by all employees.
- The best goals require employees to stretch a bit to achieve them, but they are not extreme.
- Goals that are set too high or too low become meaningless, and employees naturally come to ignore them.

N.B: Supervisors and managers must work with their employees to set goals.

4. **Relevant (R)**
   - Realistic, relevant, reasonable, rewarding, result-oriented
   - Goals must be aligned to the firm's visions and mission
   - must be based on the current conditions and realities of the environment i.e. with the availability of Rs, Knowledge and time

N.B: Unrealistic goals/ irrelevant goals

- Make firm's loss focus and goals are ignored.
- Loss of team motivation
- Employees feel overburdened, over whelmed and stressed out.

5. **Time-bound (T)**
   - Time-based, timely, tangible, traceable
     - Enough time to achieve the goal.
     - Not too much time, when can affect project performance.
   - Goals must have starting points, ending points and fixed durations.
   - Deadline bolsters employee's commitment to achieving the goal.
   - Creates urgency

N.B: Time must be measurable, attainable and realistic.

- SMART goals = SMART organization
- SMART goals propel firms' fast forward.

2.6 Chapter summary

The nature of a business vision and mission can represent either a competitive advantage or disadvantage for the firm. An organization achieves a heightened sense of purpose when strategists, managers, and employees develop and communicate a clear business vision and mission. A good mission statement reveals an organization's customers; products or services; markets; technology; concern for survival, growth, and profitability; philosophy; self-concept; concern for public image; and concern for employees. These nine basic components serve as a practical framework for evaluating and writing mission statements. As the first step in strategic management, the vision and mission statements provide direction for all planning activities. Well-designed vision and mission statements are essential for formulating, implementing and evaluating strategy. Developing and communicating a clear business vision and mission are the most commonly overlooked tasks in strategic management. Without clear statements of vision and mission, a firm's short-term actions can be counterproductive to long-term

interests. Vision and mission statements always should be subject to revision, but, if carefully prepared, they will require infrequent major changes. Organizations usually reexamine their vision and mission statements annually. Goals and objective should be formulated to ensure the achievement of vision and mission.

Chapter review questions

1. Formulate a mission statement for any organization consisting of the nine elements.
2. Formulate a vision statement for any company
3. Differentiate vision and mission statements?
4. Explain the importance of a vision and a mission statement.
5. Discuss the relationships and differences among objectives and goals.

CHAPTER THREE

EXTERNAL ENVIRONMENTAL ANALYSIS

Aim of the chapter

Before an organization can begin strategy formulation, it must scan the external environment to identify possible opportunities and threats and its internal environment for strengths and weak-nesses. Environmental scanning is the monitoring, evaluation, and dissemination of information from the external and internal environments to key people within the organization. An organization uses this tool to avoid strategic surprise and to ensure its long-term health. Research has found a positive relationship between environmental scanning and profits. Approximately 70% of executives around the world state that global social, environmental, and business trends are increasingly important to corporate strategy.

The aim of this chapter is to introduce you with the different concepts of external environment analysis, major external factors/force which affect the organization's product, market and customers and task environment variables.

CHAPTER OBJECTIVES;

After studying this chapter, you should be able to do the following:

1. Describe how to conduct an external strategic-management audit.
2. Discuss major external forces that affect organizations:
3. Describe key sources of external information, including the Internet.
4. Discuss important forecasting tools used in strategic management.
5. Discuss the importance of monitoring external trends and events.
6. Describe briefly porter's five forces model
7. Develop external factor evaluation matrix for different companies

3. What is environment?

As to the oxford dictionary "environment" is a surrounding objects, regions or circumstances." The business environment consists of all those aspects and forces in the surroundings of business enterprises under which business operations are to be carried out effectively and efficiently.

3.1 The Nature of an External Audit

Activity 3. 1

1. Why organizations conduct environment analysis?
 ____
 ____.
2. Consider organization which are found in your vicinity do they conduct environment analysis, how does they respond to changes?
 ____
 ____.

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

3.2. Environmental Scanning/ Analysis

Pioneering organizations have gone out of success because of their failure to adapt to environmental change or, even worse, by failing to create change. To be successful overtime, an organization needs to be in tune with its external environment. There must be a strategic fit between

What the environment wants and what the organization hat to offer, as well as what the organization needs and what the environment can provide. Before an organization can begin strategy formulation, it must scan the external environment to identify possible opportunities and threats and Its internal environment for strengths and weaknesses.

Environmental scanning is the monitoring, evaluating, and disseminating of information from the external and internal environments to key people within the corporation. It is a tool that organization uses to avoid strategic surprise and to ensure long-term health. Research has found a positive relationship between environmental scanning and success. In undertaking environmental scanning, strategic managers must first be aware of the many variables within an organization societal and task environments.

The societal, or macro environment includes the general forces that do not directly touch on the short-run activities of the organization but that can, and often does, influence its long-run decisions. Environmental analysis involves identifying the major present and future threats and opportunities to or from the organization's principal constituents (components - stakeholders, customers, competitors, suppliers, employees, and general public) along the dimensions of the organization's economic, political/ legal, technological, and social environments.

3.3. Characteristics of Environment

Business environment exhibits many characteristics. Some of the important and obvious characteristics are briefly:-

Environment is complex

Environment consists of a number of factors, events, conditions and influences arising from different sources. All these do not exist in isolation but interact with each other to create entirely new sets of influences. All in all, environment is a complex phenomenon relatively easier to understand in parts but difficult to grasp in its totality.

Environment id dynamic

Environment is constantly changing in nature. Due to many and varied influences operating, there is dynamism in the environment causing it to continuously change its shape and character.

Environment is multi-faceted

What shape and character an environment assumes depends on the perception of the observer. Different observers may view a particular change in the environment, or a new development, differently. This is frequently seen when one company welcomes the same development, as an opportunity while another company perceives it as a threat.

Environment has a far-reaching impact on organizations.

The growth and profitability of an organization depends critically on the environment in which it exists and environmental change has an impact on the organizations is several different ways.

Since the environment is complex, dynamic, & multi-faceted and has a far-reaching impact, dividing it into external and internal components enables us to understand it better.

Environment is further classified as external and internal, it includes all the factors outside the organization, which provide opportunities or pose threats as well as strength and weaknesses to the organization.

Generally environmental influences could be described as

Opportunity: is a favorable condition in the organization's environment, which enables it to consolidate and strengthen its position.

Threat: is an unfavorable condition in the organization's environment, which creates, arises for or causes damage to the organization.

Strength: is an inherent capacity, which an organization can use to gain strategic advantage over its competitors.

A weakness: Is an inherent limitation or constraint, which creates a strategic disadvantage.

3.4 The Process of Performing an External Audit

The process of performing an external audit must involve as many managers and employees as possible. As emphasized in earlier discussions, involvement in the strategic-management process can lead to understanding and commitment from organizational members. Individuals appreciate having the opportunity to contribute ideas and to gain a better understanding of their firm's industry, competitors, and markets. To perform an external audit, a company first must gather competitive intelligence and information about social, cultural, demographic, environmental, economic, political, legal, governmental, and technological trends. Individuals can be asked to monitor various sources of information such as key magazines, trade journals, and newspapers. These persons can submit periodic scanning reports to a committee of managers charged with performing the external audit. This approach provides a continuous stream of timely strategic information and involves many individuals in the external-audit process. The Internet provides another source for gathering strategic information, as do corporate, university, and public libraries. Suppliers, distributors, salespersons, customers, and competitors represent other sources of vital information.

Once information is gathered, it should be assimilated and evaluated. A meeting or series of meetings of managers is needed to collectively identify the most important opportunities and threats facing the firm. These key external factors should be listed on flip charts or a blackboard. A prioritized list of these factors could be obtained by requesting all managers to rank the factors identified, from 1 for the most important opportunity/threat to 20 for the least important opportunity/threat. These key external factors can vary over time and by industry. Relationships with suppliers or distributors are often a critical success factor. Other variables commonly used include market share, breadth of competing products, world economies, foreign affiliates, proprietary and key account advantages, price competitiveness, technological advancements, population shifts, interest rates, and pollution abatement. Freund emphasized that these key external factors should be:

- Important to achieving long-term and annual objectives;
- Measurable;
- Applicable to all competing firms; and
- Hierarchical in the sense that some will pertain to the overall company and others will be more narrowly focused on functional or divisional areas.
- A final list of the most important key external factors should be communicated and distributed widely in the organization. Both opportunities and threats can be key external factors.

3.5. Key External Forces

Activity 3.2

1. Identify major external factors which affect organizations?
____
____.
2. Discuss on how does political, economic, social and technological factors affect organizations?
____
____

External forces can be divided into five broad categories: Economic forces; Social, cultural, demographic, and environmental forces; Political, governmental, and legal forces; Technological forces; and Competitive forces. External trends and events significantly affect all products, services, markets, and organizations in the world. Changes in external forces translate into changes in consumer demand for both industrial and consumer products and services. External forces affect the types of products developed, the nature of positioning and market segmentation strategies, the types of services offered, and the choice of businesses to acquire or sell. In addition, external forces directly affect both suppliers and distributors. Identifying and evaluating external opportunities and threats enables organizations to develop a clear mission, to design strategies to achieve long-term objectives, and to develop policies to achieve annual objectives.

3.5.1 Economic Forces: refers to the nature and direction of the economy in which the business operates. Because consumption patterns are affected by the relative affluence of various market segments, each firm must understand economic trends in the segments that affect its industry. Economic factors have a direct impact on the potential attractiveness of various strategies. For

example, as interest rates rise, then funds needed for capital expansion become more costly or unavailable. Also, as interest rates rise, discretionary income declines, and the demand for discretionary goods falls. As stock prices increase, the desirability of equity as a source of capital for market development increases. Also, as the market rises, consumer and business wealth expands. A summary of economic variables that often represent opportunities and threats for organizations is provided in Table given below. Firms that do not mobilize and empower their managers and employees to identify, monitor, forecast, and evaluate key external forces may fail to anticipate emerging opportunities and threats and, consequently, may pursue ineffective strategies, miss opportunities, and invite organizational demise. Firms not taking advantage of the Internet are falling behind technologically.

Key Economic Variables to Be Monitored

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

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

As far as the exportation of capital and labor is concerned, over the last 300 years Pakistan has seen a tremendous exportation of labor. Capital is not only left a vacuum on organization. Monetary policies

and Fiscal policies are changed every year. The person or businesses engaged in business for profit making or non-profit organizations always have to keep an eye on the economic structure of the countries. As far as the tax rates are concerned, government also changes the tax rate with the passage of time. So it affects the economic forces. ECC and OPEC policies and LDC policies have also a major effect on the economic factors.

3.5.2 Social, Cultural, Demographic, and Environmental Forces; social forces involve the beliefs, values, attitudes, opinions and life styles of those in firm's external environment as developed from ecological, demographic, religious, educational, and ethnic conditioning. Social, cultural, demographic, and environmental changes have a major impact upon virtually all products (Preferences change), services, markets, and customers. Small, large, for-profit and nonprofit organizations in all industries are being staggered and challenged by the opportunities and threats arising from changes in social, cultural, demographic, and environmental variables. In every way, the United States is much different today than it was yesterday, and tomorrow promises even greater changes. We may use the following analysis in understanding the Social, Cultural, Demographic, and Environmental Forces:

i. Population growing older
ii. Increase in younger population
iii. Ethnic balance changing
iv. Gap between rich and poor widening

Key Social, Cultural, Demographic, and Environmental Variables

- Childbearing rates
- Number of special interest groups
- Number of marriages
- Number of divorces
- Number of births
- Number of deaths
- Immigration and emigration rates
- Social security programs
- Life expectancy rates
- Per capita income
- Location of retailing, manufacturing, and service businesses
- Attitudes toward business
- Lifestyles
- Traffic congestion
- Inner-city environments
- Average disposable income
- Trust in government
- Attitudes toward government
- Attitudes toward work
- Buying habits

- Ethical concerns
- Attitudes toward saving
- Sex roles
- Attitudes toward investing
- Racial equality
- Use of birth control
- Average level of education
- Government regulation
- Attitudes toward retirement
- Attitudes toward leisure time
- Attitudes toward product quality
- Attitudes toward customer service
- Pollution control
- Attitudes toward foreign peoples
- Energy conservation
- Social programs
- Number of churches
- Number of church members
- Social responsibility
- Attitudes toward careers
- Population changes by race, age, sex, and level of affluence
- Attitudes toward authority
- Population changes by city, county, state, region, and country
- Value placed on leisure time
- Regional changes in tastes and preferences
- Number of women and minority workers
- Number of high school and college graduates by geographic area
- Recycling
- Waste management
- Air pollution
- Water pollution
- Ozone depletion
- Endangered species

Ethnic balance changes due to the migration of the people from different areas to different areas. This affects the ethical behavior very much. As the traditions and norms are very much different in different areas of Pakistan, therefore the behavior of the migrated people also have a major effect on the behavior of the resident people. Due to the increased gap between rich and the poor, there is a tremendous change in the social behavior of the people.

3.5.3 Political forces

The direction and stability of political factors is a major consideration for managers in formulating company strategy. Political forces define the legal and otherwise governing parameters in which the firm must or may wish to operate. Political considerations are placed on each company through fair-trade decisions, antitrust laws, tax programs, minimum wage legislation, pollution and pricing policies, administrative jawboning, and many other actions aimed at protecting the consumer and the environment. These laws, practices, and regulations are most commonly restrictive, and as a result, they tend to reduce a firm’s potential profits. However, other political actions are designed to benefit and protect a company.

Examples include patent laws, government subsidies, and product research grants. Thus, political forces are both a limitation and a benefit to the firm they influence.

The Key variables of Political forces to be monitored include;

- ✓ Government regulations or deregulations
- ✓ Changes in tax laws
- ✓ Special tariffs
- ✓ Political action committees
- ✓ Voter participation rates
- ✓ Number, severity, and location of government protests
- ✓ Number of patents
- ✓ Changes in patent laws
- ✓ Environmental protection laws
- ✓ Level of defense expenditures
- ✓ Legislation on equal employment
- ✓ Level of government subsidies
- ✓ Antitrust legislation
- ✓ Sino-American relationships
- ✓ Russian-American relationships
- ✓ European-American relationships
- ✓ African-American relationships
- ✓ Import-export regulations
- ✓ Government fiscal and monetary policy changes
- ✓ Political conditions in foreign countries
- ✓ Special local, state, and federal laws
- ✓ Lobbying activities
- ✓ Size of government budgets
- ✓ World oil, currency, and labor markets
- ✓ Location and severity of terrorist activities
- ✓ Local, state, and national elections World oil situation makes a difference to us. So, either the issues is related to currency, oil or labor they should be monitored as key external variables.

3.5.4. Technological forces

Technology can be simply defined as the application of knowledge to practical solutions or tasks. To avoid obsolescence and promote innovation, a firm must be aware of technological changes that might influence its industry. Creative technological adaptations can affect planning in that new products may be suggested or existing ones improved; manufacturing and marketing techniques may also improve.

3.5.5 Competitive forces

By assessing its competitive position a firm can improve its chances of designing strategies that optimize environmental opportunities. Development of competitive profiles enables a firm to more accurately forecast its short and long-term growth and profit potentials. Although, the exact criteria used in constructing a competitor’s profile are largely determined by situational factors in the environment, the following are often included: market share; breadth of product line; effectiveness

of sales distribution; proprietary and key-account advantages; price competitiveness; advertising and promotion effectiveness; location and age of facility; capacity and productivity; experience; raw material costs; financial position; relative product quality R&D advantages/position; caliber of personnel; and general images.

Good competitive intelligence in business is one of the keys to success. The more information and knowledge a firm can obtain about its competitors, the more likely it can formulate and implement effective strategies because major competitor's strength may represent key threats and major competitor's weakness can represent external opportunities.

Key Questions about Competitors

- What are the major competitors' strengths?
- What are the major competitors' weaknesses?
- What are the major competitors' objectives and strategies?
- How will the major competitors most likely respond to current economic, social, cultural, demographic, environmental, political, governmental, legal, technological, and competitive trends affecting our industry?
- How vulnerable are the major competitors to our alternative company strategies?
- How vulnerable are our alternative strategies to successful counterattack by our major competitors?
- How are our products or services positioned relative to major competitors?
- To what extent are new firms entering and old firms leaving this industry?
- What key factors have resulted in our present competitive position in this Industry?
- How have the sales and profit rankings of major competitors in the industry changed over recent years? Why have these rankings changed that way?
- What is the nature of supplier and distributor relationships in this industry?
- To what extent could substitute products or services be a threat to competitors in this industry?

3.6 Porter's five forces' model of industry analysis

Activity 3.3

1. How does a competitor affect an organization's objective?
2. Why organizations conduct task environment analysis?
3. What are the assumptions of porter's five force model?

Michael E. Porter of the Harvard School of Business Administration has developed a framework that helps managers for analyzing the nature and extent of competition within an industry. He says that there are five competitive forces, which determine the degree of competition within an industry. And the framework is known as the Porter's five forces model. This model focuses on five forces that shape competition within an industry.

The Porter's "Five-Force" competition Model: - A key Analytical Tool

Source: Thomas L. and David Hunger (2012) Strategic Management and Business Policy toward global sustainability, 13th edition.

Porter argues that

- The stronger each of these forces, the more limited is the ability of established organizations to raise prices and earn greater profits.
- Within porter's framework, a strong competitive force can be regarded as a threat since it depresses success.

- A weak competitive force can be viewed as an opportunity, for it allows an organization to get better success. Because of factors beyond an organization direct control, such as industry evolution, the strength of the five forces may change through time. In such circumstances, the task facing strategic managers is to recognize opportunities and threats as they arise and to formulate appropriate strategic responses.
- In addition, it is possible for organizations, through its strategy, to alter the strength of one or more of the five forces to its advantages.

1. The Threat of New Entrants to the Industry

A new entrant into industry represents a competitive threat to existing firms. It adds new production capacity and potential to erode the market share of the existing industry. New entrants into the industry are potential competitors. Potential competitors are organizations that currently are not competing in an industry but have the capability to do so if they choose.

Existing (established) organizations try to discourage potential competitors from entering, since the more organizations enter an industry, the more difficult it becomes for established organizations to hold their share of the market and to generate success. Thus a high risk of entry by potential competitors represents a threat to the profitability of established organizations.

On the other hand, if the risk of new entry is low, established organizations could take advantage of this opportunity to raise prices and earn greater returns.

The strength of the competitive forces of potential rivals is largely a function of the height of barriers to entry. The concept of barriers to entry implies that there are significant costs in joining an industry.

The greater the costs that potential competitors must bear, the greater are the barriers to entry. High entry barriers keep potential competitors out of an industry even when industry returns are high.

The principal sources of barriers to entry are:

- Economies of scale
- Absolute cost advantage
- Brand loyalty and switching cost
- Capital requirement
- Product differentiation
- Access to distribution channels
- Government and legal barriers

- Retaliation by established producer when this risk is low, established organizations can charge higher prices and earn greater profits than would have been possible otherwise clearly, then, it is the interest of organizations to pursue strategies consistent with these aims.

Indeed, empirical evidence suggests that the height of barriers to entry is the most important determinant of success rates in an industry.

2. The Threat of Substitute Products

Here, the products of industries that serves similar consumer needs as those of the industry being analyzed.

A substitute may be regarded as something, which meets the same needs as the product in any industry. The extent of threat from particular substitute depends on two factors**.**

- The extent to which price and performance of this substitute can match industries product. If the price and performance of existing product rise above that of the substitute product, customer tends to switch to the substitute.
- The willingness of buyers to switch to the substitute. Buyer will be more willing to change substitute if switching costs are low.

For example:

- Organization in the coffee industry competes indirectly with those in the tea and soft-drink industries. (All three industries serve consumer needs for drinks).

The extent to which substitutes limit price and profit depends on:

- The buyers propensity to substitute
- Relative price and performance of substitutes

The existence of close substitutes presents a strong competitive threat, limiting the price an organization can charge and thus its success.

However, if an organization's products have **few close substitutes** (that is, if substitutes are weak competitive force), then, other things being equal the organizations has the opportunity to raise price and earn additional profits.

3. The Bargaining Power of Buyers

Buyers of an industry product can exert bargaining power over that industry by forcing prices down, by reducing the amount of good they purchased from the industry, and by demanding better quality for the same price.

The strength of buying power that firms face from their customers depends on two sets of factors;

- Buyer's price sensitivity and
- Relative bargaining power.

The extents/ factors to which buyers are sensitive to the prices changed by the firms in an industry depend on:

- Cost of product relative to total costs
- Product differentiation
- Competition between buyers

Some factors that influence the bargaining power of buyers relative to that of seller are:

- Size of concentration of buyers relative to producers
- Buyers' switching cost
- Buyers' information
- Buyers' ability to backward integration

Buyers can be viewed as a competitive threat when they force down prices or when they demand higher quality and better service (which increases operating costs).

Alternatively, weak buyers give an organization the opportunity to raise prices and earn greater returns.

An industry's buyers tend to be powerful relative to the firms if they are buying from when the conditions listed below apply (these factors also apply to a group of consumers and to industrial and commercial buyers):

- Buyers are concentrated as in cooperatives, or they account for a large volume of purchases.
- Products are undifferentiated or standardized.
- The seller's component represents a large portion of the total cost of the buyer's finished product. When the seller's product has a small cost share, buyers tend to be less prices sensitive.
- Buyers are earning low profits and are thus more price sensitive than if they were highly profitable.

- The sellers' product is not critical in one way or another to the buyer. If it is critical to the quality, price, appeal, etc, of an industrial buyer group's finished product, for example, then the sellers will have power over the buyers.
- There is a threat that buyers can integrate backward to make the suppliers' product.

4. The Bargaining Power of Suppliers

Providers of goods and services to an industry have power over their customers through their ability to set price and control quality, delivery time, and order quantity.

If these customers cannot successfully playoff one supplier against another to protect themselves, then the industry's profits can be drained off by suppliers.

The bargaining power of suppliers that can be viewed as a threat when they are able to force up the price that an organization must pay for input or reduce the quality of goods supplied, thereby depressing the organization's success.

Alternatively, week supplies give a company the opportunity to force down prices and demand higher quality.

The power of suppliers is high in the following situations:

- There are few suppliers who are more concentrated than their customers
- Suppliers' product is differentiated
- Customers switching costs are high
- There is little pressure on suppliers to protect themselves from substitutes or replacements for their product
- When suppliers have the capability to integrate forward. A supplier of engines to a manufacturer of lawnmowers would have a strong bargaining position if the mower company realized the engine supplier's ability to make the whole lawnmower.

5. Rivalry among Established/Existing Organizations

It describes the intensity of rivalry among competitors or established organizations within in the industry. Some industries appear "sleepy" because of a low level of rivalry among competitors (example the manufacturers of fasteners, nuts and bolts and other devices used to connect the components of products). On the other hand, some industries are characterized by a high level of competitive activity (example, the brewing industry has many competitors who battle fiercely with each other over market share).

If this competitive force is weak, organizations have an opportunity to raise prices and earn grater profits. But if it is strong, significant price competition, including price wars, may result from the

intense rivalry. Price competition limits profitability by reducing the margins that can be earned on sales.

Factors that play important role in determining the nature and intensity of competition between established firms are:

- Concentration
- Diversity of competitors
- Product differentiation
- Excess capacity
- Exit barriers and
- Cost conditions

Generally, the factors that tend to precipitate intense rivalries in an industry are:

- Relative equilibrium in size and power among a large number of competitors
- Slow or stagnant growth of industry demand such that expansion of one competitor would come at the expense of others
- Undifferentiated products and low switching costs
- High fixed costs or product Perishability
- Even small capacity additions generate large volume increases which raise pressure to cut prices
- High exit barriers causing firms to bear low or negative returns on investment
- Wide spectrum of strategies and types of firms which generates confusion and frequent "collision" in the market. The opposite case might be an oligopoly like the automobile industry where most actions are reactions to another competitor and rivalry is somewhat orderly, albeit intense.

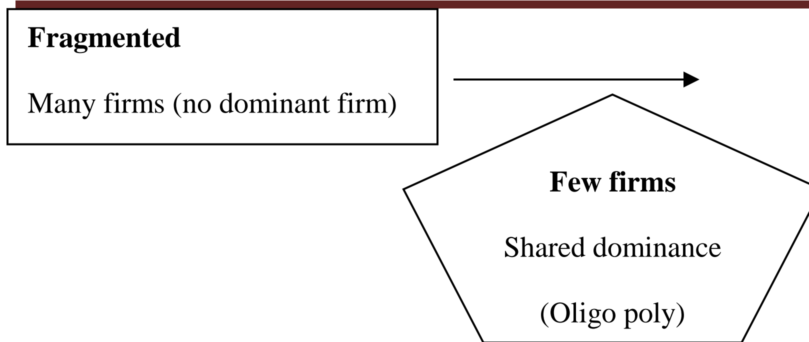
Intense rivalry among established organizations constitutes a strong threat to success. And it is largely a function of **three factors.**

- Industry competitive structure
- Demand conditions and
- The height of exit barriers in the industry

1. **Competitive structure**: refers to the number and size distribution of organizations in an industry. Different competitive structures have different implications for rivalry. Structures vary from fragmented up to consolidated.

Consolidated

One firm or one dominant firm (Monopoly)



The continuum of industry structure

2. Demand conditions: Industry demand conditions are another determinant of the intensity of rivalry among established companies. Growing demand tends to moderate competition by providing greater room for expansion.

Demand grows when the market as a whole is growing through the addition of new consumers or when existing consumers are purchasing more of an industry's product. When demand is growing, companies can increase revenues without taking market share away from other companies. Thus growing demand gives an organization a major opportunity to expand operations.

Declining demand results in more competition as organization fight to maintain revenues and market-share. Demand declines when consumers are leaving the market place or when each consumer is buying less. When demand is declining, an organization can attain growth only by taking market share away from other organization. Thus, declining demand constitutes a major threat, for it increase the extent of rivalry between established organizations.

3. **Exit barrier:** are serious competitive threats when industry demand is declining. They are economic, strategic, and emotional factors that keep organization competing in an industry even when returns are low.

If exit barriers are high, organization can become locked into an unfavorable industry and excess productive capacity can result. In turn, excess capacity tends to lead to intensified price competition, with organizations cutting prices in an attempt to obtain the orders needed to utilize their idle capacity.

Common exit barriers include the following;

- Investments in plant and equipment that have no alternative uses and cannot be sold off. If the organization wishes to leave the industry, it has to write off the book value of these assets.
- High fixed costs of exit, such as severance pay to workers who are being made redundant.

- Emotional attachments to an industry, as when an organization is unwilling to exit from its original industry for sentimental reasons.
- Strategic relationship between business units. For example, within a multi-industry organization, a low-return unit may provide vital inputs from a high return unit based in another industry. Thus the organization may be unwilling to exit from the low-return units.
- Economic dependence on the industry, as when an organization is not diversified and so relies on the industry for its income.

Interactions among these factors

The extent of rivalry among established organization within an industry is a function of competitive structure, demand conditions, and exit barriers. The interaction of these factors determines the extent of rivalry. These issues are summarized as follows: Demand conditions and exit barriers as determinants of opportunities and threats in consolidated industry

Exit barrier	**Demand Conditions** Demand decline	Demand growth
High	**High threat** of excess capacity and price wars.	Opportunities to raise prices through price leadership and to expand operations.
Low	**Moderate threat** of excess capacity and price-wars	Opportunities to raise prices through price leadership to expand operations.

When demand growth is high, the environment of consolidated industry may be favorable. When demand is declining and exit barriers are high, the probable emergency of excess capacity is likely to causes to price wars. Thus, depending on the interaction between these various factors, the extent of rivalry among established organization in a consolidated industry might constitute an opportunity or a threat.

3.7 The External Factor Evaluation (EFE) Matrix

An External Factor Evaluation (EFE) Matrix allows strategists to summarize and evaluate economic, social, cultural, demographic, environmental, political, governmental, legal, technological, and competitive information.

Illustrated in Table 3-12, the EFE Matrix can be developed in five steps:

1. List key external factors as identified in the external-audit process. Include a total of 15 to 20 factors, including both opportunities and threats that affect the firm and its industry. List the opportunities first and then the threats. Be as specific as possible, using percentages, ratios, and comparative numbers whenever possible.
2. Assign to each factor a weight that ranges from 0.0 (not important) to 1.0 (very important). The weight indicates the relative importance of that factor to being successful in the firm's industry. Opportunities often receive higher weights than threats, but threats can receive high weights if they are especially severe or threatening. Appropriate weights can be determined by comparing successful with unsuccessful competitors or by discussing the factor and reaching a group consensus. The sum of all weights assigned to the factors must equal 1.0.
3. Assign a rating between 1 and 4 to each key external factor to indicate how effectively the firm's current strategies respond to the factor, where 4 = the response is superior, 3 = the response is above average, 2 = the response is average, and 1 = the response is poor. Ratings are based on effectiveness of the firm's strategies. Ratings are thus company-based, whereas the weights in Step 2 are industry-based. It is important to note that both threats and opportunities can receive a 1, 2, 3, or 4.
4. Multiply each factor's weight by its rating to determine a weighted score.
5. Sum the weighted scores for each variable to determine the total weighted score for the organization.

Regardless of the number of key opportunities and threats included in an EFE Matrix, the highest possible total weighted score for an organization is 4.0 and the lowest possible total weighted score is 1.0. The average total weighted score is 2.5. A total weighted score of 4.0 indicates that an organization is responding in an outstanding way to existing opportunities and threats in its industry. In other words, the firm's strategies effectively take advantage of existing opportunities and minimize the potential adverse effects of external threats. A total score of 1.0 indicates that the firm's strategies are not capitalizing on opportunities or avoiding external threats. An example of an EFE Matrix is provided in Table 3-12 for a local ten-theatre cinema complex.

TABLE 3-12 EFE Matrix for a Local Ten-Theatre Cinema Complex

Key External Factors	Weight	Rating	Weighted Score
Opportunities			
1. Rowan County is growing 8% annually in population	0.05	3	0.15
2. TDB University is expanding 6% annually	0.08	4	0.32
3. Major competitor across town recently ceased operations	0.08	3	0.24
4. Demand for going to cinema growing 10% annually	0.07	2	0.14
5. Two new neighborhoods being developed within 3 miles	0.09	1	0.09
6. Disposable income among citizens grew 5% in prior year	0.06	3	0.18
7. Unemployment rate in county declined to 3.1%	0.03	2	0.06
Threats			
8. Treand toward healthy eating eroding concession sales	0.12	4	0.48
9. Demand for online movies and DVDs growing 10% annually	0.06	2	0.12
10. Commercial property adjacent to cinemas for sale	0.06	3	0.18
11. TDB University installing an on-campus movie theatre	0.04	3	0.12
12. County and city property taxes increasing 25% this year	0.08	2	0.16
13. Local religious groups object to R-rated movies being shown	0.04	3	0.12
14. Movies rented from local Blockbuster store up 12%	0.08	2	0.16
15. Movies rented last quarter from Time Warner up 15%	0.06	1	0.06
Total	**1.00**		**2.58**

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Note that the most important factor to being successful in this business is “Trend toward healthy eating eroding concession sales” as indicated by the 0.12 weight. Also note that the local cinema is doing excellent in regard to handling two factors, “TDB University is expanding 6 percent annually” and “Trend toward healthy eating eroding concession sales.” Perhaps the cinema is placing flyers on campus and also adding yogurt and healthy drinks to its concession menu. Note that you may have a 1, 2, 3, or 4 anywhere down the Rating column. Note also that the factors are

stated in quantitative terms to the extent possible, rather than being stated in vague terms. Quantify the factors as much as possible in constructing an EFE Matrix. Finally, note that the total weighted score of 2.58 is above the average (midpoint) of 2.5, so this cinema business is doing pretty well, taking advantage of the external opportunities and avoiding the threats facing the firm. There is definitely room for improvement, though, because the highest total weighted score would be 4.0. As indicated by ratings of 1, this business needs to capitalize more on the "two new neighborhoods nearby" opportunity and the "movies rented from Time Warner" threat.

Note also that there are many percentage-based factors among the group. Be quantitative to the extent possible! Note also that the ratings range from 1 to 4 on both the opportunities and threats.

3.8 The Competitive Profile Matrix (CPM)

The Competitive Profile Matrix (CPM) identifies a firm's major competitors and its particular strengths and weaknesses in relation to a sample firm's strategic position. The weights and total weighted scores in both a CPM and an EFE have the same meaning. However, critical success factors in a CPM include both internal and external issues; therefore, the ratings refer to strengths and weaknesses, where 4 = major strength, 3 = minor strength, 2 = minor weakness, and 1 = major weakness. The critical success factors in a CPM are not grouped into opportunities and threats as they are in an EFE. In a CPM, the ratings and total weighted scores for rival firms can be compared to the sample firm. This comparative analysis provides important internal strategic information. A sample Competitive Profile Matrix is provided in Table 3-13. In this example, the

two most important factors to being successful in the industry are "advertising" and "global expansion," as indicated by weights of 0.20. If there were no weight column in this analysis, note that each factor then would be equally important. Thus, having a weight column makes for a more robust analysis, because it enables the analyst to assign higher and lower numbers to capture perceived or actual levels of importance. Note in Table 3-13 that Company 1 is strongest on "product quality," as indicated by a rating of 4, whereas Company 2 is strongest on "advertising." Overall, Company 1 is strongest, as indicated by the total weighted score of 3.15.

TABLE 3-13 An Example Competitive Profile Matrix

		Company 1		Company 2		Company 3	
Critical Success Factors	Weight	Rating	Score	Rating	Score	Rating	Score
Advertising	0.20	1	0.20	4	0.80	3	0.60
Product Quality	0.10	4	0.40	3	0.30	2	0.20
Price Competitiveness	0.10	3	0.30	2	0.20	4	0.40
Management	0.10	4	0.40	3	0.20	3	0.30
Financial Position	0.15	4	0.60	2	0.30	3	0.45
Customer Loyalty	0.10	4	0.40	3	0.30	2	0.20
Global Expansion	0.20	4	0.80	1	0.20	2	0.40
Market Share	0.05	1	0.05	4	0.20	3	0.15
Total	**1.00**		**3.15**		**2.50**		**2.70**

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Other than the critical success factors listed in the example CPM, factors often included in this analysis include breadth of product line, effectiveness of sales distribution, proprietary or patent advantages, location of facilities, production capacity and efficiency, experience, union relations, technological advantages, and e-commerce expertise. A word on interpretation: Just because one firm receives a 3.2 rating and another receives a 2.80 rating in a Competitive Profile Matrix, it does not follow that the first firm is 20 percent better than the second. Numbers reveal the relative strengths of firms, but their implied precision is an illusion. Numbers are not magic. The aim is not to arrive at a single number, but rather to assimilate and evaluate information in a meaningful way that aids in decision making.

Self-test exercise

Select appropriates answer among the given alternatives

1. Pick the correct sentence.
   A. External audit is aimed at developing an exhaustive list of every possible factors.
   B. The process of performing an external audit must involve as many managers and employees as possible.
   C. Suppliers, distributors, customers, and competitors represent other sources of vital information.

D. External trends and events significantly affect all products, services, markets, and organizations.

E. All are answers.

F. All are true except A

2. Which one of the following is not the argument in porter's five force model?

   A. The stronger each of the forces, the more limited is to raise prices and earn greater profits.

   B. A strong competitive force can be regarded as a threat since it depresses success.

   C. A weak competitive force can be viewed as an opportunity.

   D. It is possible for organizations, to alter the strength of one or more of the five forces to its advantages.

   E. None of the above.

3. Assume ABC Company develops the external factor evaluation matrix for formulating strategy and it founds the total weighted score of EFE matrix is 2.43, as a manager how did you interpret it?

   A. The company is responding in outstanding way to external environment.

   B. The company is not good in responding to opportunity and threats

   C. The company's strategies effectively take advantage of existing opportunities and minimize external threats.

   D. The company is doing pretty well for responding opportunity and threats.

   E. All of the above

3.9 Sources of External Information

<u>Activity 3.4</u>

1. What are the sources of external information? (use the space provided here)

____
____
_________________________________.

A wealth of strategic information is available to organizations from both published and unpublished sources. Unpublished sources include customer surveys, market research, speeches at

professional and shareholders' meetings, television programs, interviews, and conversations with stakeholders. Published sources of strategic information include periodicals, journals, reports, government documents, abstracts, books, directories, newspapers, and manuals. The Internet has made it easier for firms to gather, assimilate, and evaluate information. There are many excellent Web sites for gathering strategic information, but six that are used routinely are listed here:

1. http://marketwatch.multexinvestor.com
2. http://moneycentral.msn.com
3. http://finance.yahoo.com
4. www.clearstation.com
5. https://us.etrade.com/e/t/invest/markets
6. www.hoovers.com

Most college libraries subscribe to Standard & Poor's (S&P's) *Industry Surveys*. These documents are exceptionally up-to-date and give valuable information about many different industries. Each report is authored by a Standard & Poor's industry research analyst and includes the following sections:

1. Current Environment
2. Industry Trends
3. How the Industry Operates
4. Key Industry Ratios and Statistics
5. How to Analyze a Company
6. Glossary of Industry Terms
7. Additional Industry Information
8. References
9. Comparative Company Financial Analysis

3.10 Forecasting Tools and Techniques

Forecasts are educated assumptions about future trends and events. Forecasting is a complex activity because of factors such as technological innovation, cultural changes, new products, improved services, stronger competitors, shifts in government priorities, changing social values, unstable economic conditions, and unforeseen events. Managers often must rely on published forecasts to effectively identify key external opportunities and threats.

A sense of the future permeates all action and underlies every decision a person makes. People eat expecting to be satisfied and nourished in the future. People sleep assuming that in the future they

will feel rested. They invest energy, money, and time because they believe their efforts will be rewarded in the future. They build highways assuming that automobiles and trucks will need them in the future. Parents educate children on the basis of forecasts that they will need certain skills, attitudes, and knowledge when they grow up. The truth is we all make implicit forecasts throughout our daily lives.

The question, therefore, is not whether we should forecast but rather how we can best forecast to enable us to move beyond our ordinarily unarticulated assumptions about the future. Can we obtain information and then make educated assumptions (forecasts) to better guide our current decisions to achieve a more desirable future state of affairs? We should go into the future with our eyes and our minds open, rather than stumble into the future with our eyes closed.

USEFUL FORECASTING TECHNIQUES

Various techniques are used to forecast future situations. They do not tell the future; they merely state what can be, not what will be. As such, they can be used to form a set of reasonable assumptions about the future. Each technique has its proponents and its critics.

A. **Trend extrapolation:** to be the most widely practiced form of forecasting—over 70% use this technique either occasionally or frequently. Simply stated, Extrapolation is the extension of present trends into the future. It rests on the assumption that the world is reasonably consistent and changes slowly in the short run. Time-series methods are approaches of this type; they attempt to carry a series of historical events forward into the future. The basic problem with extrapolation is that a historical trend is based on a series of patterns or relationships among so many different variables that a change in any one can drastically alter the future direction of the trend.

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B. **Brainstorming:** is a non-quantitative approach that requires simply the presence of people with some knowledge of the situation to be predicted. The basic ground rule is to propose ideas without first mentally screening them. No criticism is allowed. “Wild” ideas are encouraged. Ideas should build on previous ideas until a consensus is reached. This is a good technique to use with operating managers who have more faith in “gut feel” than in more quantitative number-crunching techniques.

C. **Expert opinion**: is a no quantitative technique in which experts in a particular area attempt to forecast likely developments. This type of forecast is based on the ability of a knowledgeable person(s) to construct probable future developments based on the interaction of key variables.

Forecasting tools can be broadly categorized into two groups: quantitative techniques and qualitative techniques. Quantitative forecasts are most appropriate when historical data are available and when the relationships among key variables are expected to remain the same in the future. *Linear regression*, for example, is based on the assumption that the future will be just like the past—which, of course, it never is. As historical relationships become less stable, quantitative forecasts become less accurate.

No forecast is perfect, and some forecasts are even wildly inaccurate. This fact accents the need for strategists to devote sufficient time and effort to study the underlying bases for published forecasts and to develop internal forecasts of their own. Key external opportunities and threats can be effectively identified only through good forecasts. Accurate forecasts can provide major competitive advantages for organizations. Forecasts are vital to the strategic-management process and to the success of organizations.

3.11 Chapter summary

Environmental scanning involves monitoring, collecting, and evaluating information in order to understand the current trends in the natural, societal, and task environments. The information is then used to forecast whether these trends will continue or whether others will take their place. How will developments in the natural environment affect the world? What kind of developments can we expect in the societal environment to affect our industry? What will an industry look like in 10 to 20 years? Who will be the key competitors? Who is likely to fall by the wayside? We use this information to make certain assumptions about the future—assumptions that are then used in strategic planning. In many ways, success in the business world is like ice hockey: The key to winning is not to assume that your industry will continue as it is now but to assume that the industry will change and to make sure that your company will be in position to take advantage of those changes.

Chapter review questions

DISCUSSION QUESTIONS

1. Discuss how a development in an organization's natural and societal environments can affect the organization through its task environment.
2. According to Porter, what determines the level of competitive intensity in an industry?
3. How can a decision maker identify strategic factors in a corporation's external international environment?
4. Compare and contrast trend extrapolation with the writing of scenarios as forecasting techniques.
5. Select a company or business where you currently or previously have worked. Conduct an external audit for this company. Find 10 opportunities and threats that face this company.
6. Discuss porters' five forces model
7. Compare and contrast competitors profile matrix and external factor evaluation matrix.

CHAPTER FOUR: INTERNAL ASSESSMENT

Aim of the chapter

All organizations have strengths and weaknesses in the functional areas of business. No enterprises equally strong or weak in all areas. Internal strengths/weaknesses, coupled with external opportunities/threats and a clear statement of mission, provide the basis for establishing objectives and strategies. Objectives and strategies are established with the intention of capitalizing upon internal strengths and overcoming weaknesses.

The aim of this chapter is to introduce you with concept of internal environment analysis, major external factors/force which affect the organization's product, market and customers and the relationship between functions in an organization.

Chapter objectives

After studying this chapter, you should be able to:

- Describe how to perform an internal strategic-management audit.
- Discuss key interrelationships among the functional areas of business.
- Identify the basic functions or activities that make up management, marketing, finance/accounting, production/ operations, research and development, and management information systems.
- Explain how to determine and prioritize a firm's internal strengths and weaknesses.

4.1 The Nature of Internal Audit

Involvement in performing an internal strategic-management audit provides vehicle for understanding nature and effect of decisions in other functional business areas of the firm. All organizations have strengths and weaknesses in the functional areas of business. No enterprise is equally strong or weak in all areas. Internal strengths/weaknesses, coupled with external opportunities/threats and a clear statement of mission, provide the basis for establishing objectives and strategies. Objectives and strategies are established with the intention of capitalizing upon internal strengths and overcoming weaknesses.

Internal audit creates an environment of coordination and understanding among managers from all functional areas. Internal audit is parallels process of external audit. It gathers & assimilates information from:

- Management
- Marketing
- Finance/accounting
- Production/operations
- Research & development
- Management information systems

4.2 Key Internal Forces

It is not possible in a business policy text to review in depth all the material presented in courses such as marketing, finance, accounting, management, computer information systems, and production/operations; there are many sub areas within these functions, such as customer service, warranties, advertising, packaging, and pricing under marketing. For different types of organizations, such as hospitals, universities, and government agencies, the functional business areas, of course, differ. In a hospital, for example, functional areas may include cardiology, hematology, nursing, maintenance, physician support, and receivables. Functional areas of a university can include athletic programs, placement services, housing, fund raising, academic research, counseling, and intramural programs. Within large organizations, each division has certain strengths and weaknesses. A firm's strengths that cannot be easily matched or imitated by competitors are called **distinctive competencies**. Building competitive advantages involves taking advantage of distinctive competencies. Strategies are designed in part to improve on a firm's weaknesses, turning them into strengths, and may be even into distinctive competencies. Some researchers emphasize the importance of the internal audit part of the strategic-management process by comparing it to the external audit.

4.3 The Process of Performing an Internal Audit

Activity 4. 1

1. What necessary steps are conducted to develop internal factor evaluation matrix?
   ____
   ______________________________.
2. Why the involvement of all departments in an organization does is needed in the process?
   ____
   ____.

The process of performing an internal audit close

ly parallels the process of performing an external audit. Representative Managers and employees from throughout the firm need to be involved in determining a firm's strengths and weaknesses. The internal audit requires gathering and assimilating information about the firm's management, marketing, finance/accounting, production/operations, research and development (R&D), and computer information systems operations.

Compared to the external audit, the process of performing an internal audit provides more opportunity for participants to understand how their jobs, departments, and divisions fit into the whole organization. This is a great benefit because managers and employees perform better when they understand how their work affects other areas and activities of the firm. For example, when marketing and manufacturing managers jointly discuss issues related to internal strengths and weaknesses, they gain a better appreciation of issues, problems, concerns, and needs in all the functional areas. In organizations that do not use strategic management, marketing, finance, and manufacturing managers often do not interact with each other in significant ways. Performing an internal audit, thus, is an **excellent vehicle or forum for improving the process of communication in the organization**. Communication may be the most important word in management. Performing an internal audit requires gathering, assimilating, and evaluating information about the firm's operations. Critical success factors, consisting of both strengths and weaknesses, can be identified and prioritized in the manner discussed later chapters. The development of conclusions on the 10 to 20 most important organizational strengths and weaknesses can be, as any experienced manager knows, a difficult task, when it involves managers representing various organizational interests and points of view. Developing a 20-page list of strengths and weaknesses could be accomplished relatively easily, but a list of the 10 to 15 most important ones involves significant analysis and negotiation. This is true because of the judgments that are required and the impact which such a list will inevitably have as it is used in the formulation, implementation, and evaluation of strategies.

4.4 Relation Ship among the Functional Areas of Business

Strategic management is a highly interactive process that requires effective coordination among management, marketing, finance/accounting, production/operations, R&D, and computer

information systems managers. Although the strategic-management process is overseen by strategists, success requires that managers and employees from all functional areas work together to provide ideas and information. Financial managers, for example, may need to restrict the number of feasible options available to operations managers, or R&D managers may develop such good products that marketing managers need to set higher objectives. A key to organizational success is effective coordination and understanding among managers from all functional business areas. Through involvement in performing an internal strategic-management audit, managers from different departments and divisions of the firm come to understand the **nature and effect of decisions in other functional business areas** in their firm. Knowledge of these relationships is critical for effectively establishing objectives and strategies. A failure to recognize and understand relationships among the functional areas of business can be detrimental to strategic management, and the number of those relationships that must be managed increases dramatically with a firm's size, diversity, geographic dispersion, and the number of products or services offered. Governmental and nonprofit enterprises traditionally have not placed sufficient emphasis on relationships among the business functions. For example, some state governments, utilities, universities, and hospitals only recently have begun to establish marketing objectives and policies that are consistent with their financial capabilities and limitations. Some firms place too great an emphasis on one function at the expense of others.

1) **MANAGEMENT**

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

Planning- Planning consists of all those managerial activities related to preparing for the future. Specific tasks include forecasting, establishing objectives, devising strategies, developing policies, and setting goals. Strategy Formulation

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

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

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

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

Management Audit Checklist of Questions

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

1. Does the firm use strategic-management concepts?
2. Are company objectives and goals measurable and well communicated?
3. Do managers at all hierarchical levels plan effectively?
4. Do managers delegate authority well?
5. Is the organization's structure appropriate?
6. Are job descriptions and job specifications clear?
7. Is employee morale high?
8. Are employee turnover and absenteeism low?
9. Are organizational reward and control mechanisms effective?

2) **MARKETING**

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

There are seven basic functions of marketing:

(1) Customer analysis,
(2) Selling products/services,
(3) Product and service planning,
(4) Pricing,
(5) Distribution,
(6) Marketing research, and
(7) Opportunity analysis.

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

Customer Analysis

Customer analysis—the examination and evaluation of consumer needs, desires, and wants—involves administering customer surveys, analyzing consumer information, evaluating market positioning strategies, developing customer profiles, and determining optimal market segmentation strategies. The information generated by customer analysis can be essential in developing an effective mission statement. Customer profiles can reveal the demographic characteristics of an organization's customers. Buyers, sellers, distributors, salespeople, managers, wholesalers, retailers, suppliers, and creditors can all participate in gathering information to identify customers' needs and wants successfully. Successful organizations continually monitor present and potential customers' buying patterns.

Selling Products/Services: Successful strategy implementation generally rests upon the ability of an organization to sell some product or service. Selling includes many marketing activities such as advertising, sales promotion, publicity, personal selling, sales force management, customer relations, and dealer relations. These activities are especially critical when a firm pursues a market penetration strategy. The effectiveness of various selling tools for consumer and industrial products varies. Personal selling is most important for industrial goods companies, and advertising is most important for consumer goods companies. Determining organizational strengths and weaknesses in the selling function of marketing is an important part of performing an internal strategic management audit. With regard to advertising products and services on the Internet, a new trend is to base advertising rates exclusively on sale rates. This new accountability contrasts sharply with traditional broadcast and print advertising that bases rates on the number of persons expected to see a given advertisement. The new cost per- sale online advertising rates are possible because any Web site can monitor which user clicks on which advertisement and then can record whether that consumer actually buys the product. If there are no sales, then the advertisement is free. The most popular type of Internet advertisement is the banner. However, many people just ignore online banner advertisements.

Product and Service Planning: Product and service planning includes activities such as test marketing; product and brand positioning; devising warranties; packaging; determining product options, product features, product style, and product quality; deleting old products; and providing

for customer service. Product and service planning is particularly important when a company is pursuing product development or diversification. One of the most effective product and service planning techniques is test marketing. Test markets allow an organization to test alternative marketing plans and to forecast future sales of new products. In conducting a test market project, an organization must decide how many cities to include, which cities to include, how long to run the test, what information to collect during the test, and what action to take after the test has been completed. Test marketing is used more frequently by consumer goods companies than by industrial goods companies. Test marketing can allow an organization to avoid substantial losses by revealing weak products and ineffective marketing approaches before large-scale production begins.

Pricing

Five major stakeholders affect pricing decisions:

- Consumers,
- Governments,
- Suppliers,
- Distributors,
- Competitors.

Sometimes an organization will pursue a forward integration strategy primarily to gain better control over prices charged to consumers. Governments can impose constraints on price fixing, price discrimination, minimum prices, unit pricing, price advertising, and price controls. Competing organizations must be careful not to coordinate discounts, credit terms, or condition of sale; not to discuss prices, markups, and costs at trade association meetings; and not to arrange to issue new price lists on the same date, to rotate low bids on contracts, or to uniformly restrict production to maintain high prices. Strategists should view price from both a short-run and a long-run perspective, because competitors can copy price changes with relative ease. Often a dominant firm will aggressively match all price cuts by competitors.

Distribution

Distribution includes warehousing, distribution channels, distribution coverage, retail site locations, sales territories, inventory levels and location, transportation carriers, wholesaling, and retailing. Most producers today do not sell their goods directly to consumers. Various marketing

entities act as intermediaries; they bear a variety of names such as wholesalers, retailers, brokers, facilitators, agents, middlemen, vendors, or simply distributors.

Distribution becomes especially important when a firm is striving to implement a market development or forward integration strategy. Some of the most complex and challenging decisions facing a firm concern product distribution. Intermediaries flourish in our economy because many producers lack the financial resources and expertise to carry out direct marketing. Manufacturers who could afford to sell directly to the public often can gain greater returns by expanding and improving their manufacturing operations. Even General Motors would find it very difficult to buy out its more than eighteen thousand independent dealers. Successful organizations identify and evaluate alternative ways to reach their ultimate market. Possible approaches vary from direct selling to using just one or many wholesalers and retailers. Strengths and weaknesses of each channel alternative should be determined according to economic, control, and adaptive criteria. Organizations should consider the costs and benefits of various wholesaling and retailing options. They must consider the need to motivate and control channel members and the need to adapt to changes in the future. Once a marketing channel is chosen, an organization usually must adhere to it for an extended period of time.

Marketing Research

Marketing research is the systematic gathering, recording, and analyzing of data about problems relating to the marketing of goods and services. Marketing research can uncover critical strengths and weaknesses, and marketing researchers employ numerous scales, instruments, procedures, concepts, and techniques to gather information. Marketing research activities support all of the major business functions of an organization. Organizations that possess excellent marketing research skills have a definite strength in pursuing generic strategies.

Opportunity Analysis

The eighth function of marketing is opportunity analysis, which involves assessing the costs, benefits, and risks associated with marketing decisions. Three steps are required to perform a cost/benefit analysis:

- Compute the total costs associated with a decision,
- Estimate the total benefits from the decision, and
- Compare the total costs with the total benefits. As expected benefits exceed total costs, an opportunity becomes more attractive. Sometimes the variables included in a cost/benefit

analysis cannot be quantified or even measured, but usually reasonable estimates can be made to allow the analysis to be performed. One key factor to be considered is risk. Cost/benefit analyses should also be performed when a company is evaluating alternative ways to be socially responsible.

Marketing Audit Checklist of Questions

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

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

3) ACCOUNTING / FINANCE

Financial condition is often considered the single best measure of a firm's competitive position and overall attractiveness to investors. Determining an organization's financial strengths and weaknesses is essential to formulating strategies effectively. A firm's liquidity, leverage, working capital, profitability, asset utilization, cash flow, and equity can eliminate some strategies as being feasible alternatives. Financial factors often alter existing strategies and change implementation plans.

Finance/Accounting Functions

- Determining financial strengths and weaknesses key to strategy formulation
- Investment decision (Capital budgeting)
- Financing decision

- Dividend decision

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

Financial ratio analysis is the most widely used method for determining an organization's strengths and weaknesses in the investment, financing, and dividend areas. Because, the functional areas of business
are so closely related, financial ratios can signal strengths or weaknesses in management, marketing, production, research and development, and computer information systems activities. The **investment decision**, also called **capital budgeting**, is the allocation and reallocation of capital and resources to projects, products, assets, and divisions of an organization. Once strategies are formulated, capital budgeting decisions are required to implement strategies successfully.

The financing decision concerns determining the best capital structure for the firm and includes examining various methods by which the firm can raise capital (for example, by issuing stock, increasing debt, selling assets, or using a combination of these approaches). The financing decision must consider both short-term and long-term needs for working capital. Two key financial ratios that indicate whether a firm's financing decisions have been effective are the debt-to-equity ratio and the debt-to-total-assets ratio.

Dividend decisions; concern issues such as the percentage of earnings paid to stockholders, the stability of dividends paid over time, and the repurchase or issuance of stock. Dividend decisions determine the amount of funds that are retained in a firm compared to the amount paid out to stockholders.

Finance/Accounting Audit Checklist of Questions

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

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

8. Are the firm's financial managers experienced and well trained?

4) PRODUCTION/OPERATIONS

The production/operations function of a business consists of all those activities that transform inputs into goods and services. Production/operations management deals with inputs, transformations, and outputs that vary across industries and markets. A manufacturing operation transforms or converts inputs such as raw materials, labor, capital, machines, and facilities into finished goods and services.

Production/Operations Audit Checklist of Questions

Questions such as the following should be examined:

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

5) RESEARCH AND DEVELOPMENT

The fifth major area of internal operations that should be examined for specific strengths and weaknesses is research and development (R&D). Many firms today conduct no R&D, and yet many other companies depend on successful R&D activities for survival. Firms pursuing a product development strategy especially need to have a strong R&D orientation. The purpose of research and development are as follows:

- Development of new products before competition
- Improving product quality
- Improving manufacturing processes to reduce costs. Organizations invest in R&D because they believe that such investment will lead to superior product or services and give them competitive advantages. Research and development expenditures are directed at developing new products before competitors do, improving product quality, or improving manufacturing processes to reduce costs.

Research and Development Audit Checklist of Questions

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

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

6) MANAGEMENT INFORMATION SYSTEMS

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

Management Information Systems Audit checklist Questions

- Do all managers in the firm use the information system to make decisions?
- Is there a chief information officer or director of information systems position in the firm?
- Are data in the information system updated regularly?
- Do managers from all functional areas of the firm contribute input to the information system?
- Are there effective passwords for entry into the firm's information system?
- Are strategists of the firm familiar with the information systems of rival firms?
- Is the information system user-friendly?
- Are computer training workshops provided for users?

- Is the firm's system being improved?

4.6 The value chain analysis

One of the primary goals of any business is to gain an edge on their competition. One way to do so is to conduct a value chain analysis, which examines what organizations can do to create a competitive advantage, while at the same time provide the greatest value to their consumers.

What is a value chain?

To understand how to conduct a value chain analysis, a business must first know what their value chain is. A value chain is the full range of activities — such as design, production, marketing and distribution — businesses go through to bring a product or service from conception to their customers. "**Value chain** represents the internal activities a firm engages in when transforming inputs into outputs."

It is a chain of activities that a firm operating in a specific industry performs in order to deliver a valuable product or service for the market. The concept comes from business management and was first described and popularized by Michael Porter in his 1985 best-seller, Competitive Advantage: Creating and Sustaining Superior Performance.

The idea of the value chain is based on the process view of organizations, the idea of seeing a manufacturing (or service) organization as a system, made up of subsystems each with inputs, transformation processes and outputs. Inputs, transformation processes, and outputs involve the acquisition and consumption of resources - money, labour, materials, equipment, buildings, land, administration and management. How value chain activities are carried out determines costs and affects profits.

For companies that produce goods, the value chain starts with the raw materials used to make their products and consists of everything that is added to it before it ends up being sold to consumers. The process of actually organizing all of these activities so they can be properly analyzed is called value chain management. The goal of value chain management is to ensure that those in charge of each stage of the value chain are communicating with each other to help make sure the product is getting in the hands of customers as seamlessly and quickly as possible.

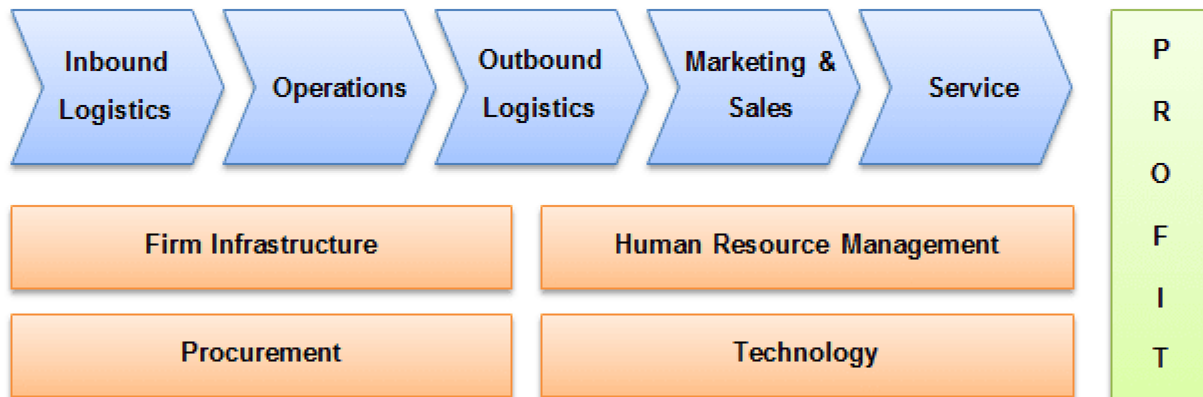
"**Value chain analysis** (VCA) is a process where a firm identifies its primary and support activities that add value to its final product and then analyze these activities to reduce costs or increase differentiation."

VCA is a strategy tool used to analyze internal firm activities. Its goal is to recognize, which activities are the most valuable (i.e. are the source of cost or differentiation advantage) to the firm and which ones could be improved to provide competitive advantage. In other words, by looking into internal activities, the analysis reveals where a firm's competitive advantages or disadvantages are. The firm that competes through differentiation advantage will try to perform its activities better than competitors would do. If it competes through cost advantage, it will try to perform internal activities at lower costs than competitors would do. When a company is capable of producing goods at lower costs than the market price or to provide superior products, it earns profits.

The value chain analysis involves identifying each part of the value chain and seeing where improvements can be made either from a production standpoint or a cost perspective to ensure consumers are getting the most bang for their buck. When consumers are getting the most out of a product for the cheapest cost, businesses will benefit in the long run. The value chain analysis looks at each of the activities in the value chain to determine what steps are necessary and which are not in an attempt to boost the company's bottom line.

M. Porter introduced the generic value chain model in 1985. Value chain represents all the internal activities a firm engages in to produce goods and services. VC is formed of **primary activities** that add value to the final product directly and **support activities** that add value indirectly. Below you can see the Porter's VC model.

Primary Activities



Support Activities

Although, primary activities add value directly to the production process, they are not necessarily more important than support activities. Nowadays, competitive advantage mainly derives from technological improvements or innovations in business models or processes. Therefore, such support activities as 'information systems', 'R&D' or 'general management' are usually the most important source of differentiation advantage. On the other hand, primary activities are usually the source of cost advantage, where costs can be easily identified for each activity and properly managed.

Benchmarking

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

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

4.7 The Internal Factor Evaluation (IFE) Matrix

In multidivisional firms, each autonomous division or strategic business unit should construct an IFE Matrix. Divisional matrices then can be integrated to develop an overall corporate IFE Matrix. Both external and internal evaluation together called SWOT analysis for any business firm. After reading this lecture you will be able to prepare IFE and EFE matrixes for any business planning.

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

1. List key internal factors as identified in the internal-audit process. Use a total of from ten to twenty internal factors, including both strengths and weaknesses. Always list strengths first and then weaknesses. Be as specific as possible, using percentages, ratios, and comparative numbers. The list of all strength and weaknesses should consist of 10-20 factors.
2. Assign a weight (either in %age or in numerical value) that ranges from 0.0 (not important) to 1.0 (all-important) to each factor. The weight assigned to a given factor indicates the relative importance of the factor to being successful in the firm's industry. Regardless of whether a key factor is an internal strength or weakness, factors considered to have the greatest effect on organizational performance should be assigned the highest weights. The sum of all weights must equal 1.0.
3. Assign a 1-to-4 rating (rating means what is the capability of the firm to meet its strength and weaknesses) to each factor to indicate whether that factor represents a major weakness (rating 1), a minor weakness (rating 2), a minor strength (rating 3), or a major strength (rating 4). Note that strengths must receive a 4 or 3 rating and weaknesses must receive a

1 or 2 rating. Ratings are, thus, company based, whereas the weights in Step 2 are industry based.

4. Multiply each factor's weight by its rating to determine a weighted score for each variable.
5. Sum the weighted scores for each variable to determine the total weighted score for the organization.

Highest possible weighted score for the organization is 4.0; the lowest, 1.0. Average = 2.5. Regardless of how many factors are included in an IFE Matrix, the total weighted score can range from a low of 1.0 to a high of 4.0, with the average score being 2.5. Total weighted scores well below 2.5 characterize organizations that are weak internally, whereas scores significantly above 2.5 indicate a strong internal position.

Like the EFE Matrix, an IFE Matrix should include from 10 to 20 key factors.

The number of factors has no effect upon the range of total weighted scores because the weights always sum to 1.0. An example of an IFE Matrix for XYZ Casino Enterprises is provided in Table. Note that the firm's major strengths are its size, occupancy rates, property, and long-range planning as indicated by the rating of 4. The major weaknesses are locations and recent joint venture. The total weighted score of 2.75 indicates that the firm is above average in its overall internal strength.

A Sample Internal Factor Evaluation Matrix for XYZ Casino

Key Internal Factors	**Weight**	**Rating**	**Weighted Score**
Internal Strengths			
1. Largest casino company in the United States	.05	4	.20
2. Room occupancy rates over 95% in Las Vegas	.10	4	.40
3. Increasing free cash flows	.05	3	.15
4. Owns one mile on Las Vegas Strip	.15	4	.60
5. Strong management team	.05	3	.15
6. Buffets at most facilities	.05	3	.15
7. Minimal comps provided	.05	3	.15
8. Long-range planning	.05	4	.20
9. Reputation as family-friendly	.05	3	.15

10.Financial ratios	.05	3	.15
Internal Weaknesses			
1. Most properties are located in Las Vegas	.05	1	.05
2. Little diversification	.05	2	.10
3. Family reputation, not high rollers	.05	2	.10
4. Laughlin properties	.10	1	.10
5. Recent loss of joint ventures	.10	1	.10
TOTAL	1.00		2.75

XYZ Casino has a total weighted score of 2.75 indicating that the firm is above average in its overall internal strength.

4.8 Chapter summary

Management, marketing, finance/accounting, production/operations, research and development, and management information systems represent the core operations of most businesses. A strategic-management audit of a firm's internal operations is vital to organizational health. Many companies still prefer to be judged solely on their bottom-line performance. However, an increasing number of successful organizations are using the internal audit to gain competitive advantages over rival firms. Systematic methodologies for performing strength-weakness assessments are not well developed in the strategic-management literature, but it is clear that strategists must identify and evaluate internal strengths and weaknesses in order to effectively formulate and choose among alternative strategies. The EFE Matrix, Competitive Profile Matrix, IFE Matrix, and clear statements of vision and mission provide the basic information needed to successfully formulate competitive strategies. The process of performing an internal audit represents an opportunity for managers and employees throughout the organization to participate in determining the future of the firm. Involvement in the process can energize and mobilize managers and employees.

Chapter review questions

1. Discuss Tools/ models that help to analyze the internal aspects of the organization
2. Discuss internal analysis process
3. Describe briefly areas of internal audit

4. How can value-chain analysis help to identify a company's strengths and weaknesses?
5. In what ways can a corporation's structure and culture be internal strengths or weaknesses?
6. Select a well-known company to research. Prepare a report of the company:

   I. Does the firm have any core competencies?

   II. Are any of these distinctive (better than the competition) competencies? Does the firm have any competitive advantage?

CHAPTER FIVE

STRATEGY FORMULATION: STRATEGY ANALYSIS AND CHOICE

Aims of the Chapter

This chapter mainly shows the different types of alternative strategies that an enterprise could pursue to achieve their goals. Each alternative strategy has countless variations. You will know The practical use of the Boston matrix to the business problems. This chapter also helps to examine the comprehensive strategy formulation framework.

At the end of this chapter, you will be expected to:

- ♣ Understand the meaning and importance of alternative strategies
- ♣ Be able to differentiate business level strategy and functional level strategy
- ♣ Examine the Michael porter's generic strategies
- ♣ Discuss the strategy-formulation framework

5.1 Introduction

There are many strategies that are used to achieve the goals and objectives of the organization. Each alternative strategy has countless variations. For example, market penetration can include adding salespersons, increasing advertising expenditures, coopering, and using similar actions to increase market share in a given geographic area. Vertical integration strategies allow a firm to gain control over distributors, suppliers, and/or competitors whereas horizontal integration refers to a strategy of seeking ownership of or increased control over a firm's competitors. One of the most significant trends in strategic management today is the increased use of horizontal integration as a growth strategy.

Activity 5.0

1. From your own understanding, what is long term objective?

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____

____

5.2 Long term objectives

Long-term objectives represent the results expected from pursuing certain strategies. Strategies represent the actions to be taken to accomplish long-term objectives. The time frame for objectives and strategies should be consistent, usually from two to five years.

The Nature of Long-Term Objectives

Objectives should be quantitative, measurable, realistic, understandable, challenging, hierarchical, obtainable, and congruent among organizational units. Each objective should also be associated with a time line. Objectives are commonly stated in terms such as growth in assets, growth in sales, profitability, market share, degree and nature of diversification, degree and nature of vertical integration, earnings per share, and social responsibility. Clearly established objectives offer many benefits. They provide direction, allow synergy, aid in evaluation, establish priorities, reduce uncertainty, minimize conflicts, stimulate exertion, and aid in both the allocation of resources and the design of jobs. Long-term objectives are needed at the corporate, divisional, and functional levels in an organization. They are an important measure of managerial performance. Clearly stated and communicated objectives are vital to success for many reasons. First, objectives help stakeholders understand their role in an organization's future. They also provide a basis for consistent decision making by managers whose values and attitudes differ. By reaching a consensus on objectives during strategy-formulation activities, an organization can minimize potential conflicts later during implementation. Objectives set forth organizational priorities and stimulate exertion and accomplishment. They serve as standards by which individuals, groups, departments, divisions, and entire organizations can be evaluated. Objectives provide the basis for designing jobs and organizing activities to be performed in an organization. They also provide direction and allow for organizational synergy. Without long-term objectives, an organization

would drift aimlessly toward some unknown end! It is hard to imagine an organization or individual being successful without clear objectives. Success only rarely occurs by accident; rather, it is the result of hard work directed toward achieving certain objectives.

Activity 5.1

1. List and discuss the different types of strategies.

____

____

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5.3 TYPES OF STRATEGIES

Alternative strategies that an enterprise could pursue can be categorized into thirteen actions integration strategies (forward integration, backward integration, horizontal integration), intensive strategies (market penetration, market development, product development), diversification strategies (concentric diversification, conglomerate diversification, horizontal diversification), defensive strategies (joint venture, retrenchment, divestiture, and liquidation) and a combination strategy. Each alternative strategy has countless variations. For example, market penetration can include adding salespersons, increasing advertising expenditures, coopering, and using similar actions to increase market share in a given geographic area.

5.3.1 INTEGRATION STRATEGIES

Forward integration, backward integration, and horizontal integration are sometimes collectively referred to as vertical integration strategies. Vertical integration strategies allow a firm to gain control over distributors, suppliers, and/or competitors.

A. Forward integration strategy

It refers to the transactions between the customers and firm. Similarly, the function for the particular supply which the firm is being intended to involve itself will be called backward integration. When the firm looks that other firm which may be taken over within the area of its own activity is called horizontal integration. Forward integration strategy involves gaining

ownership or increased control over distributors or retailers. You can gain ownership or control over the distributors, suppliers and Competitors using forward integration.

Guidelines for the use of integration strategies:

Six guidelines when forward integration may be an especially effective strategy are:

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

When your present distributors are expensive and you think that without affecting the quality of the goods you have to carry own the operations, forward integration is advisable. Similarly, if distributors are unreliable, they cannot deliver with a sustained degree of timeliness or they are not in a proper way to meet the needs of the firm, forward integration is advisable. Availability of quality distributors is limited or it is difficult to get the quality of goods, then this need for a quality distributor, forward integration is best alternative. Suppose you have two industries, computers and mobile telephone which are progressing tremendously, it is advisable to think of forward integration due to the changing environment of the business. Organization has both capital and human resources needed to manage new business of distribution. A firm has all the basic elements to run the business safely in that case forward integration is best alternate. For stable production, stable supply is necessary. If you think that present distributors are charging high mark up, you may do that operation yourself in order to avoid the mark up charges. It is advisable that firm itself involve in the operations. By gaining control, stability will be more and profitability will be enhanced.

- When an organization's present distributors are especially expensive, or unreliable, or incapable of meeting the firm's distribution needs
- When the availability of quality distributors is so limited as to offer a competitive advantage to those firms that integrate forward

- When an organization competes in an industry that is growing and is expected to continue to grow markedly; this is a factor because forward integration reduces an organization's ability to diversify if its basic industry falters
- When an organization has both the capital and human resources needed to manage the new business of distributing its own products
- When the advantages of stable production are particularly high; this is a consideration because an organization can increase the predictability of the demand for its output through forward integration
- When present distributors or retailers have high profit margins; this situation suggests that a company profitably could distribute its own products and price them more competitively by integrating forward

B. Backward Integration

Seeking ownership or increased control of a firm's suppliers. Both manufacturers and retailers purchase needed materials from suppliers. Backward integration is a strategy of seeking ownership or increased control of a firm's suppliers. This strategy can be especially appropriate when a firm's current suppliers are unreliable, too costly, or cannot meet the firm's needs.

Guidelines for Backward Integration:

The following guidelines are important when backward integration may be an especially effective strategy are:

- ✓ When present suppliers are expensive, unreliable, or incapable of meeting needs.
    - Number of suppliers is small and number of competitors large
    - High growth in industry sector
    - Firm has both capital and human resources to manage new business
- ✓ Advantages of stable prices are important
    - Present supplies have high profit margins
- ✓ When an organization's present suppliers are especially expensive, or unreliable, or incapable of meeting the firm's needs for parts, components, assemblies, or raw materials
- ✓ When the number of suppliers is small and the number of competitors is large

- ✓ When an organization competes in an industry that is growing rapidly; this is a factor because integrative-type strategies (forward, backward, and horizontal) reduce an organization's ability to diversify in a declining industry
- ✓ When an organization has both capital and human resources to manage the new business of supplying its own raw materials
- ✓ When the advantages of stable prices are particularly important; this is a factor because an organization can stabilize the cost of its raw materials and the associated price of its product through backward integration
- ✓ When present supplies have high profit margins, which suggests that the business of supplying products or services in the given industry is a worthwhile venture
- ✓ When an organization needs to acquire a needed resource quickly

C. Horizontal Integration

Seeking ownership or increased control over competitors. Horizontal integration refers to a strategy of seeking ownership of or increased control over a firm's competitors. One of the most significant trends in strategic management today is the increased use of horizontal integration as a growth strategy. Mergers, acquisitions, and takeovers among competitors allow for increased economies of scale and enhanced transfer of resources and competencies.

Increased control over competitors means that you have to look for new opportunities either by the purchase of the new firm or hostile take over the other firm. One organization gains control of other which functioning within the same industry. It should be done that every firm wants to increase its area of influence, market share and business.

Guidelines for Horizontal Integration:

Five guidelines when horizontal integration may be an especially effective strategy are:

- ➢ When an organization can gain monopolistic characteristics in a particular area or region without being challenged by the federal government for "tending substantially" to reduce competition
- ➢ When an organization competes in a growing industry
- ➢ When increased economies of scale provide major competitive advantages
- ➢ When an organization has both the capital and human talent needed to successfully manage an expanded organization

- When competitors are faltering due to a lack of managerial expertise or a need for particular resources that an organization possesses; note that horizontal integration would not be appropriate if competitors are doing poorly because overall industry sales are declining.

Activity 5.2

1. What types of sub strategies are included under the category of intensive strategies?

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5.3.2 INTENSIVE STRATEGIES

Market penetration, market development, and product development are sometimes referred to as intensive strategies because they require intensive efforts to improve a firm's competitive position with existing products.

A. Market Penetration

A market-penetration strategy seeks to increase market share for present products or services in present markets through greater marketing efforts. This strategy is widely used alone and in combination with other strategies. Market penetration includes increasing the number of salespersons, increasing advertising expenditures, offering extensive sales promotion items, or increasing publicity efforts.

Guidelines for Market Penetration

Four guidelines when market penetration may be an especially effective strategy are:

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

There are two aspects of market penetration: Rapid market penetration: based on two assumptions, to lower the price and promotional activities can be increased. Slow market penetration: also based on two assumptions, to lower the price but promotional activities are not changed.

B. Market Development

Market development involves introducing present products or services into new geographic areas. The climate for international market development is becoming more favorable. In many industries, such as airlines, it is going to be hard to maintain a competitive edge by staying close to home.

Guidelines for Market Development

Six guidelines when market development may be an especially effective strategy are:

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

C. Product Development

Product development is a strategy that seeks increased sales by improving or modifying present products or services. Product development usually entails large research and development expenditures. The U.S. Postal Service now offers stamps and postage via the Internet, which represents a product development strategy. Called PC Postage, stamps can now be obtained online from various Web sites such as stamps.com and then printed on an ordinary laser or inkjet printer. E-Stamp Corporation, Neopost, and Pitney Bowes, too, are actively pursuing product development by creating their own versions of digital stamps.

Guidelines for Product Development

Five guidelines when product development may be an especially effective strategy to pursue are:

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

Activity 5.3

List and discuss the three types of diversification strategies.

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5.3.3 DIVERSIFICATION STRATEGIES

There are three general types of diversification strategies: concentric, horizontal, and conglomerate. Over all, diversification strategies are becoming less popular as organizations are finding it more difficult to manage diverse business activities. In the 1960s and 1970s, the trend was to diversify so as not to be dependent on any single industry, but the 1980s saw a general reversal of that thinking. Diversification is now on the retreat.

A. Concentric Diversification

Adding new, but related, products or services is widely called concentric diversification. An example of this strategy is AT&T recently spending $120 billion acquiring cable television companies in order to wire America with fast Internet service over cable rather than telephone lines.

AT&T's concentric diversification strategy has led the firm into talks with America Online (AOL) about a possible joint venture or merger to provide AOL customers cable access to the Internet.

Guidelines for Concentric Diversification

Five guidelines when concentric diversification may be an effective strategy are provided below:

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

B. Conglomerate Diversification

Adding new, unrelated products or services is called conglomerate diversification. Some firms pursue conglomerate diversification based in part on an expectation of profits from breaking up acquired firms and selling divisions piecemeal.

Guidelines for Conglomerate Diversification

Four guidelines when conglomerate diversification may be an effective strategy are provided below:

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

C. Horizontal Diversification

Adding new, unrelated products or services for present customers is called horizontal diversification. This strategy is not as risky as conglomerate diversification because a firm already should be familiar with its present customers.

Guidelines for Horizontal Diversification

Four guidelines when horizontal diversification may be an especially effective strategy are:

- Revenues from current products/services would increase significantly by adding the new unrelated products
- Highly competitive and/or no-growth industry with low margins and returns
- Present distribution channels can be used to market new products to current customers
- New products have counter cyclical sales patterns compared to existing products

Activity 5.4

What does defensive strategy mean?

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5.3.3 DEFENSIVE STRATEGIES

In addition to integrative, intensive, and diversification strategies, organizations also could pursue retrenchment, divestiture, or liquidation.

A. Retrenchment

Retrenchment occurs when an organization regroups through cost and asset reduction to reverse declining sales and profits. Sometimes called a turnaround or reorganization strategy, retrenchment is designed to fortify an organization's basic distinctive competence. During retrenchment, strategists work with limited resources and face pressure from shareholders, employees, and the media. Retrenchment can entail selling off land and buildings to raise needed cash, pruning product lines, closing marginal businesses, closing obsolete factories, automating processes, reducing the number of employees, and instituting expense control systems.

Guidelines for Retrenchment

Five guidelines when retrenchment may be an especially effective strategy to pursue are as follows:

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

B. Divestiture

Selling a division or part of an organization is called divestiture. Divestiture often is used to raise capital for further strategic acquisitions or investments. Divestiture can be part of an overall retrenchment strategy to rid an organization of businesses that are unprofitable, that require too much capital, or that do not fit well with the firm's other activities.

Guidelines for Divestiture

Five guidelines when divestiture may be an especially effective strategy to pursue are listed below:

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

Divestiture has become a very popular strategy as firms try to focus on their core strengths, lessening their level of diversification.

C. Liquidation

Selling all of a company's assets, in parts, for their tangible worth is called liquidation. Liquidation is recognition of defeat and, consequently, can be an emotionally difficult strategy. However, it may be better to cease operating than to continue losing large sums of money.

Guidelines for Liquidation

Three guidelines when liquidation may be an especially effective strategy to pursue are:

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

D. Joint Venture

Joint venture is a popular strategy that occurs when two or more companies form a temporary partnership or consortium for the purpose of capitalizing on some opportunity. Often, the two or more sponsoring firms form a separate organization and have shared equity ownership in the new entity. Other types of cooperative arrangements include research and development partnerships, cross-distribution agreements, cross-licensing agreements, cross-manufacturing agreements, and joint-bidding consortia.

Guidelines for Joint Ventures

Six guidelines when joint venture may be an especially effective strategy to purse are:

i. Combination of privately held and publicly held can be synergistically combined

ii. Domestic forms joint venture with foreign firm, can obtain local management to reduce certain risks

iii. Distinctive competencies of two or more firms are complementary

iv. Overwhelming resources and risks where project is potentially very profitable (e.g., Alaska

pipeline)

v. Two or more smaller firms have trouble competing with larger firm

vi. A need exists to introduce a new technology quickly

Activity 5.5

1. What are the importance of Michael porter's generic strategies?

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5.4 MICHAEL PORTER'S GENERIC STRATEGIES;

Probably the three most widely read books on competitive analysis in the 1980s were Michael Porter's Competitive Strategy, Competitive Advantage and Competitive Advantage of Nations. According to Porter, strategies allow organizations to gain competitive advantage from three different bases: cost leadership, differentiation, and focus. Porter calls these bases generic strategies. Cost leadership emphasizes producing standardized products at very low per-unit cost for consumers who are price-sensitive. Differentiation is a strategy aimed at producing products and services considered unique industry wide and directed at consumers who are relatively price-insensitive. Focus means producing products and services that fulfill the needs of small groups of consumers. Porter's strategies imply different organizational arrangements, control procedures, and incentive systems. Larger firms with greater access to resources typically compete on a cost leadership and/or differentiation basis, whereas smaller firms often compete on a focus basis. Porter stresses the need for strategists to perform cost-benefit analyses to evaluate "sharing opportunities" among a firm's existing and potential business units. Sharing activities and resources enhances competitive advantage by lowering costs or raising differentiation. In addition to prompting sharing, Porter stresses the need for firms to "transfer" skills and expertise among autonomous business units effectively in order to gain competitive advantage. Depending upon factors such as type of industry, size of firm, and nature of competition, various strategies could yield advantages in cost leadership, differentiation, and focus.

i. **Cost Leadership Strategies**

This strategy emphasizes efficiency. By producing high volumes of standardized products, the firm hopes to take advantage of economies of scale and experience curve effects. The product is often a basic no-frills product that is produced at a relatively low cost and made available to a very large customer base. Maintaining this strategy requires a continuous search for cost reductions in all aspects of the business.

The associated distribution strategy is to obtain the most extensive distribution possible. Promotional strategy often involves trying to make a virtue out of low cost product features. To be successful, this strategy usually requires a considerable market share advantage or preferential access to raw materials, components, labour, or some other important input. Without one or more of these advantages, the strategy can easily be mimicked by competitors. Successful implementation also benefits from:

- Process engineering skills
- Products designed for ease of manufacture
- Sustained access to inexpensive capital
- Close supervision of labour
- Tight cost control
- Incentives based on quantitative targets
- Market of many price-sensitive buyers
- Few ways of achieving product differentiation
- Buyers not sensitive to brand differences
- Large number of buyers with bargaining power
- Pursued in conjunction with differentiation
- Economies or diseconomies of scale
- Capacity utilization achieved
- Linkages with suppliers and distributors

A primary reason for pursuing forward, backward, and horizontal integration strategies is to gain cost leadership benefits. But cost leadership generally must be pursued in conjunction with differentiation. A number of cost elements affect the relative attractiveness of generic strategies, including economies or diseconomies of scale achieved, learning and experience curve effects, the percentage of capacity utilization achieved, and linkages with suppliers and distributors. Other cost

elements to consider in choosing among alternative strategies include the potential for sharing costs and knowledge within the organization, R&D costs associated with new product development or modification of existing products, labor costs, tax rates, energy costs, and shipping costs. Striving to be the low-cost producer in an industry can be especially effective when the market is composed of many price-sensitive buyers, when there are few ways to achieve product differentiation, when buyers do not care much about differences from brand to brand, or when there are a large number of buyers with significant bargaining power. The basic idea is to under price competitors and thereby gains market share and sales, driving some competitors out of the market entirely.

A successful cost leadership strategy usually permeates the entire firm, as evidenced by high efficiency, low overhead, limited perks, intolerance of waste, intensive screening of budget requests, wide spans of control, rewards linked to cost containment, and broad employee participation in cost control efforts. Some risks of pursuing cost leadership are that competitors may imitate the strategy, thus driving overall industry profits down; technological breakthroughs in the industry may make the strategy ineffective; or buyer interest may swing to other differentiating features besides price. Several example firms that are well known for their low-cost leadership strategies are Wal-Mart, BIC, McDonald's, Black and Decker, Lincoln Electric, and Briggs and Stratton.

Low Cost Producer Advantages; The first point depends upon the condition of the price fluctuation in the market; this can also be understood with the help of elasticity of demand. In any market, the demand is sensitive to price this is called price sensitivity of demand. For example, if price of any commodity increases, the customer carry on to buy the things. It means these customers neither are price sensitive. Other is the case where customers move towards the alternates with an increase in demand. The second is the case where there are few ways of achieving product differentiation either by changing features, price, cost or quality of the product.
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Where there are high end products, there are the customers who are brand sensitive, because, people want to express their choices or personality through that brand. In Bargaining power, low

price products have more customers, more suppliers and more bargaining but high priced products there are low bargaining power due to the fewer customers.

ii. Differentiation Strategies:

Differentiation involves creating a product that is perceived as unique. The unique features or benefits should provide superior value for the customer if this strategy is to be successful. Because customers see the product as unrivaled and unequaled, the price elasticity of demand tends to be reduced and customers tend to be more brands loyal. This can provide considerable insulation from competition. However, there are usually additional costs associated with the differentiating product features and this could require a premium pricing strategy.

To maintain this strategy, the firm should have:

- Strong research and development skills
- Strong product engineering skills
- Strong creativity skills
- Good cooperation with distribution channels
- Strong marketing skills
- Incentives based largely on subjective measures
- Be able to communicate the importance of the differentiating product characteristics
- Stress continuous improvement and innovation
- Attract highly skilled, creative people
- Greater product flexibility
- Greater compatibility
- Lower costs
- Improved service
- Greater convenience
- More features

Differentiation strategies Allow firm to charge higher price gain customer loyalty. In the differentiation focus strategy, a business aims to differentiate within just one or a small number of target market segments. The special customer needs of the segment means that there are

opportunities to provide products that are clearly different from competitors who may be targeting a broader group of customers. The important issue for any business adopting this strategy is to ensure that customers really do have different needs and wants - in other words that there is a **valid basis for differentiation** - and that existing competitor products are not meeting those needs and wants.

iii. Focus Strategy - Cost Focus

In this strategy the firm concentrates on a select few target markets. It is also called a focus strategy or niche strategy. It is hoped that by focusing your marketing efforts on one or two narrow market segments and tailoring your marketing mix to these specialized markets, you can better meet the needs of that target market.

The firm typically looks to gain a competitive advantage through effectiveness rather than efficiency. It is most suitable for relatively small firms but can be used by any company. As a focus strategy it may be used to select targets that are less vulnerable to substitutes or where a competition is weakest to earn above-average return on investments.

- Industry segment of sufficient size
- Good growth potential
- Not crucial to success of major competitors
- Consumers have distinctive preferences
- Rival firms not attempting to specialize in the same target segment

Here a business seeks a lower-cost advantage in just one or a small number of market segments. The product will be basic - perhaps a similar product to the higher-priced and featured market leader, but acceptable to sufficient consumers. Such products are often called "me-too's".

iv. Niche strategies

Here the organization focuses its effort on one particular segment and becomes well known for providing products/services within the segment. They form a competitive advantage for this niche market and either succeeds by being a low cost producer or differentiator within that particular segment.

Criticisms of generic strategies

Several commentators have questioned the use of generic strategies claiming they lack specificity, lack flexibility, and are limiting. In many cases trying to apply generic strategies is like trying to

fit a round peg into one of three square holes: You might get the peg into one of the holes, but it will not be a good fit. In particular, Millar (1992) questions the notion of being "caught in the middle". He claims that there is a viable middle ground between strategies. Many companies, for example, have entered a market as a niche player and gradually expanded. According to Baden Fuller and Stop ford (1992) the most successful companies are the ones that can resolve what they call "the dilemma of opposites".

Activity 5.6

Briefly discuss the strategy formulation framework.

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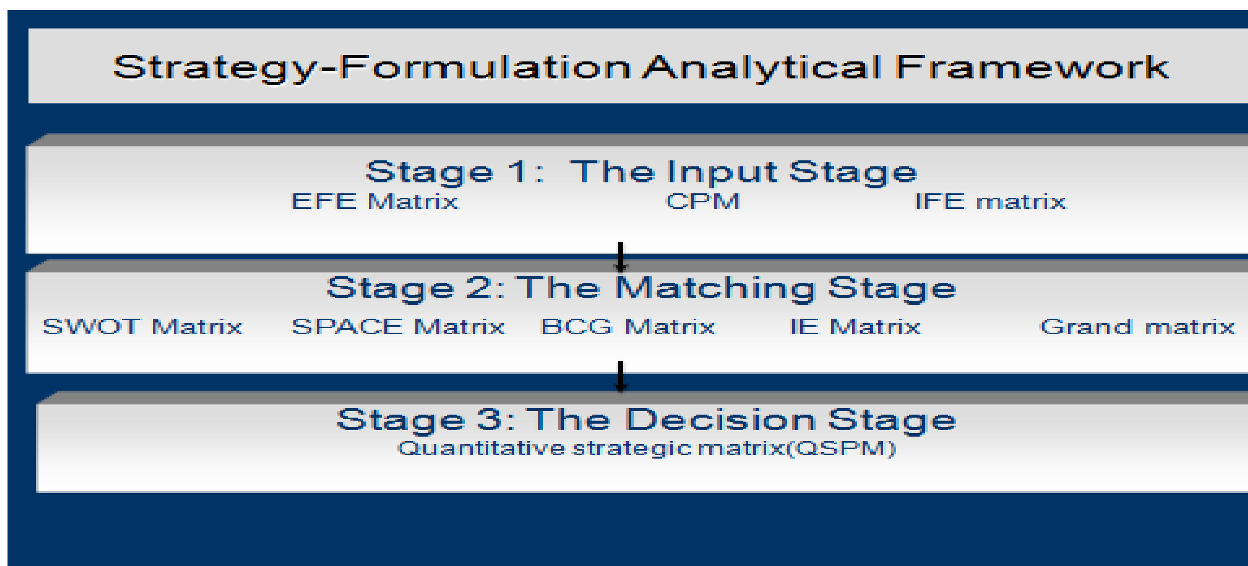
5.5 Strategy-Formulation Framework

A Comprehensive Strategy-Formulation Framework

Important strategy-formulation techniques can be integrated into a three-stage decision-making framework, as shown below. The tools presented in this framework are applicable to all sizes and types of organizations and can help strategists identify, evaluate, and select strategies.



Stage-1 (Formulation Framework)

1. External factor evaluation

2. Competitive matrix profile

3. Internal factor evaluation

Stage-2 (Matching stage)

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

Stage-3 (Decision stage)

1. **QSPM** (Quantitative Strategic Planning Matrix)

Autonomous divisions in an organization commonly use strategy-formulation techniques to develop strategies and objectives. Divisional analyses provide a basis for identifying, evaluating, and selecting among alternative corporate-level strategies. Strategists themselves, not analytic tools, are always responsible and accountable for strategic decisions. Lenz emphasized that the shift from a words-oriented to a numbers-oriented planning process can give rise to a false sense of certainty; it can reduce dialogue, discussion, and argument as a means to explore understandings, test assumptions and foster organizational learning. Strategists, therefore, must be wary of this possibility and use analytical tools to facilitate, rather than diminish, communication. Without objective information and analysis, personal biases, politics, emotions, personalities, and halo error (the tendency to put too much weight on a single factor) unfortunately may play a dominant role in the strategy-formulation process.

Stage 1: The Input Stage

Stage 1 of the formulation framework consists of the External factor evaluation (EFE) Matrix, the internal factor evaluation (IFE) Matrix, and the Competitive Profile Matrix. Called the Input Stage, as you have learned in chapter 3 (EFE and the Competitive Profile Matrix) and chapter 4 (IFE), Stage 1 summarizes the basic input information needed to formulate strategies. For detail refer to chapter 3and 4.

Stage 2: The Matching Stage

Stage 2, called the Matching Stage, focuses upon generating feasible alternative strategies by aligning key external and internal factors. Stage 2 techniques include the Threats-Opportunities-Weaknesses-Strengths (TOWS) Matrix, the Strategic Position and Action Evaluation (SPACE) Matrix, the Boston Consulting Group (BCG) Matrix, the Internal-External (IE) Matrix, and the Grand Strategy Matrix.

5.5.1 The Threats-Opportunities-Weaknesses-Strengths (TOWS) Matrix

The Threats-Opportunities-Weaknesses-Strengths (TOWS) is also named as SWOT analysis. A TWOS Analysis is a strategic planning tool used to evaluate the Threats, Opportunities and Strengths, Weaknesses, involved in a project or in a business venture or in any other situation requiring a decision. This is an important tool in order to formulate strategy. This Matrix is an important matching tool that helps managers develops four types of strategies: SO Strategies (strength-opportunities), WO Strategies (weakness- opportunities), ST Strategies (strength-threats), and WT Strategies (weakness-threats).The most difficult part of TOWS matrix is to match internal and external factor. Once the objective has been identified, TOWS are discovered and listed. TOWS are defined precisely as follows:

Strengths are attributes of the organization that are helpful to the achievement of the objective. **Weaknesses** are attributes of the organization that are harmful to the achievement of the objective. **Opportunities** are external conditions that are helpful to the achievement of the objective. **Threats** are external conditions that are harmful to the achievement of the objective.

Strengths and weaknesses are internal factors. For example, strength could be your specialist marketing expertise. A weakness could be the lack of a new product. **Opportunities and threats are external factors.** For example, an opportunity could be a developing distribution channel such as the Internet, or changing consumer lifestyles that potentially increase demand for a company's products. A threat could be a new competitor in an important existing market or a technological change that makes existing products potentially obsolete. it is worth pointing out that SWOT analysis can be very subjective - two people rarely come-up with the same version of a SWOT analysis even when given the same information about the same business and its environment. Accordingly, SWOT analysis is best used as a guide and not a prescription. Adding and weighting criteria to each factor increases the validity of the analysis.

SO Strategies: Every firm desires to obtain benefit form its resources such benefit can only be obtained if utilize its strength to take external opportunity. Resources (Assets) an important firm's strength to get opportunity for external resources. For example the firm enjoying a good financial position which is strength for a firm and externally opportunity to expand business. The strong financial position provides an opportunity to expand the business. The matched strategy is known as SO strategy.

WO Strategies: WO Strategies developed to match weakness with opportunities of the firm. WO strategy is very useful if the firm take advantage to external resources in order to overcome the weakness. For example the firm is in the critical financial problems that is weakness and firm is availing merger with Multinational Corporation.

ST Strategies: ST Strategies is an important strategy to overcome external threats. This does not mean that a strong organization should always meet threats in the external environment head-on. This strategy is adopted by various colleges by opening new branches in order to overcome competitive threat. These threats also explain by the Porter in its competitive model.

WT Strategies: Every firm has a desire to overcome its weakness and reducing threats. This type of strategy helpful when weaknesses are removed to overcome external threats. It is difficult to target WT strategy. For example weak distribution network creating many problems for the firm if it strong many external threats can be removed.

Steps for developing strategies: There are eight steps involved in constructing a TOWS Matrix:

1. Rank external opportunities
2. Rank external threats
3. Rank internal strength
4. Rank internal weaknesses.
5. Match internal strengths with external opportunities and mention the result in the SO Strategies cell.
6. Match internal weaknesses with external opportunities and mention the result in the WO Strategies cell..
7. Match internal strengths with external threats and mention the result in the ST Strategies cell.
8. Match internal weaknesses with external threats and mention the result in the WT strategies cell.

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

TWOS Matrix Development procedure

5.5.2The Strategic Position and Action Evaluation-

The Strategic Position and Action Evaluation (SPACE) Matrix: The Strategic Position and Action Evaluation (SPACE) Matrix is another important Stage 2 matching tool of formulation framework, is illustrated in Figure 5-1. It explains that what is our strategic position and what possible action can be taken. It is prepared on graph. This follow counter clockwise direction.

Its four-quadrant framework indicates whether aggressive, conservative, defensive, or competitive strategies are most appropriate for a given organization. The axes of the SPACE Matrix represent two internal dimensions (*financial position [FP]* and *competitive position [CP]*) and two external dimensions (*stability position [SP]* and *industry position [IP]*). These four factors are perhaps the most important determinants of an organization's overall strategic position.

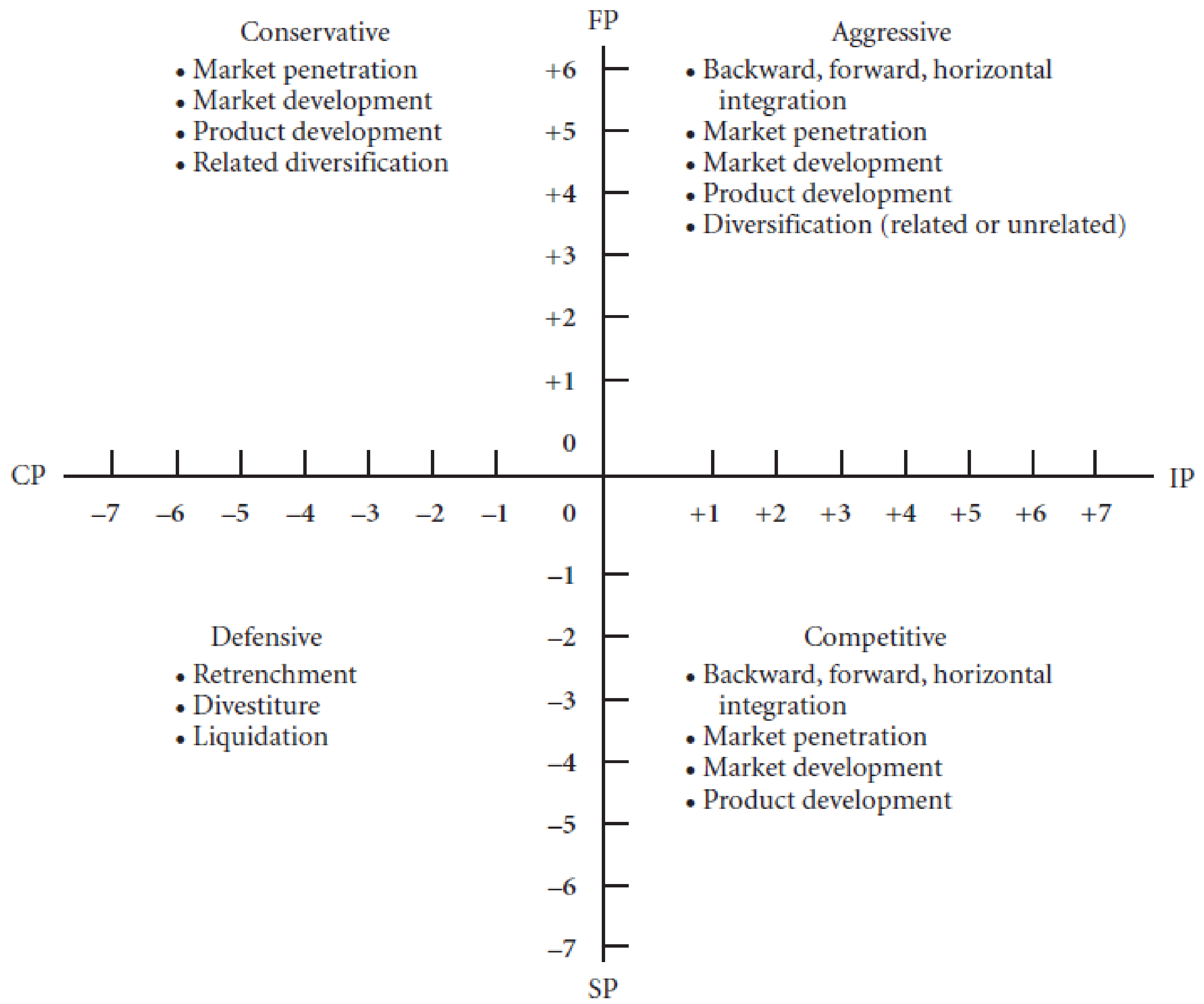
Depending on the type of organization, numerous variables could make up each of the dimensions represented on the axes of the SPACE Matrix. Factors that were included earlier in the firm's EFE and IFE Matrices (**refer to chapter 3&4**) should be considered in developing a SPACE Matrix. Other variables commonly included are given in Table 5-1. For example, return on investment, leverage, liquidity, working capital, and cash flow are commonly considered to be determining

factors of an organization's financial strength. Like the SWOT Matrix, the SPACE Matrix should be both tailored to the particular organization being studied and based on factual information as much as possible.

Steps for the preparation of SPACE Matrix

The steps required to develop a SPACE Matrix are as follows:

1. Select a set of variables to define financial position (FP), competitive position (CP), stability position (SP), and industry position (IP).
2. Assign a numerical value ranging from +1 (worst) to +7 (best) to each of the variables that make up the FP and IP dimensions. Assign a numerical value ranging from -1 (best) to -7 (worst) to each of the variables that make up the SP and CP dimensions. On the FP and CP axes, make comparison to competitors. On the IP and SP axes, make comparison to other industries.
3. Compute an average score for FP, CP, IP, and SP by summing the values given to the variables of each dimension and then by dividing by the number of variables included in the respective dimension.
4. Plot the average scores for FP, IP, SP, and CP on the appropriate axis in the SPACE Matrix.
5. Add the two scores on the *x*-axis and plot the resultant point on *X*. Add the two scores on the *y*-axis and plot the resultant point on *Y*. Plot the intersection of the new *XY* point.
6. Draw a *directional vector* from the origin of the SPACE Matrix through the new intersection point. This vector reveals the type of strategies recommended for the organization: aggressive, competitive, defensive, or conservative.



FP
Conservative
• Market penetration
• Market development
• Product development
• Related diversification
Aggressive
• Backward, forward, horizontal integration
• Market penetration
• Market development
• Product development
• Diversification (related or unrelated)
+6
+5
+4
+3
+2
+1
0
CP
IP
–7 –6 –5 –4 –3 –2 –1 0 +1 +2 +3 +4 +5 +6 +7
–1
–2
–3
–4
–5
–6
–7
Defensive
• Retrenchment
• Divestiture
• Liquidation
Competitive
• Backward, forward, horizontal integration
• Market penetration
• Market development
• Product development
SP

Figure 5.1 the SPACE Matrix

The Strategic Position And ActionEvaluation-2

Internal Strategic Position	**External Strategic Position**
Financial Position (FP) or **Financial Strength (FS)** Risk involved in business Debt to equity ratio Working capital condition Leverage Liquidity Ease of exit from market Cash flow statement Return on investment	**Stability Position(SP) or** **Environmental Stability (ES)** Impact of technology Price elasticity of demand Political situation Demand variability Price range of competing products Rate of inflation Competitive pressure
Competitive Position (CP) or **Competitive Advantage (CA)** Access to the market Market share Quality of product and services Product life cycle Customer loyalty	**Industry Position (IP) or** **Industry Strength (IS)** Demand and supply factors Resource utilization Growth potential Profit potential Financial stability Technological know-how

Capacity, location and layout Technological know-how Backward and forward integration	Productivity, capacity utilization Capital intensity Ease of entry into market

Table 5.1: Example of Factors that Make up the SPACE Matrix Axes

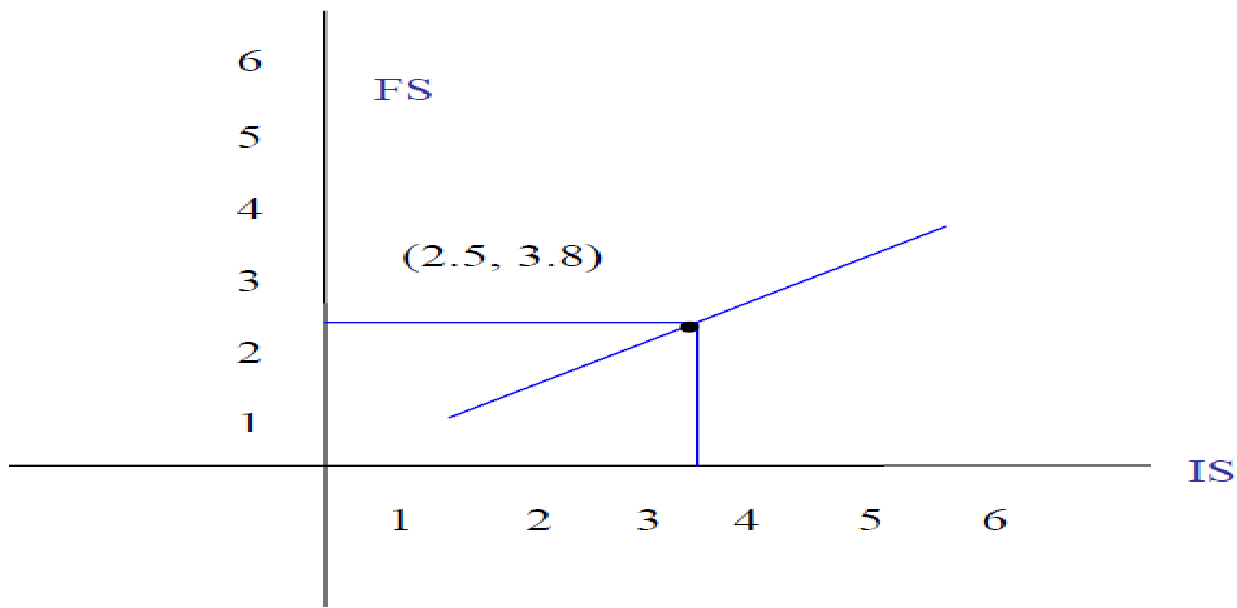
After the selection of variables the rating is assigned to each of the variables that make up the FP, IP, SP, and CP. After the addition of these variables, compute the average. For example financial strength and industry strength is explained below:

Financial Strength (FS)/Financial Position (FP)	**Rating**
High Return on investment	3
Large amount of capital	2
Consistently increasing revenue	4
Working capital condition	1

Financial strength average is (3+2+4+1)/4 = 2.5

Industry Strength (IS)/Industry Position (IP)	Rating
Demand and supply factors	5
Resource utilization	3
Profit potential	3
Technological know-how	6
Ease of entry into market	2

Industry strength average is (5+3+3+6+2)/5 = 3.8. It is plotted on graph:



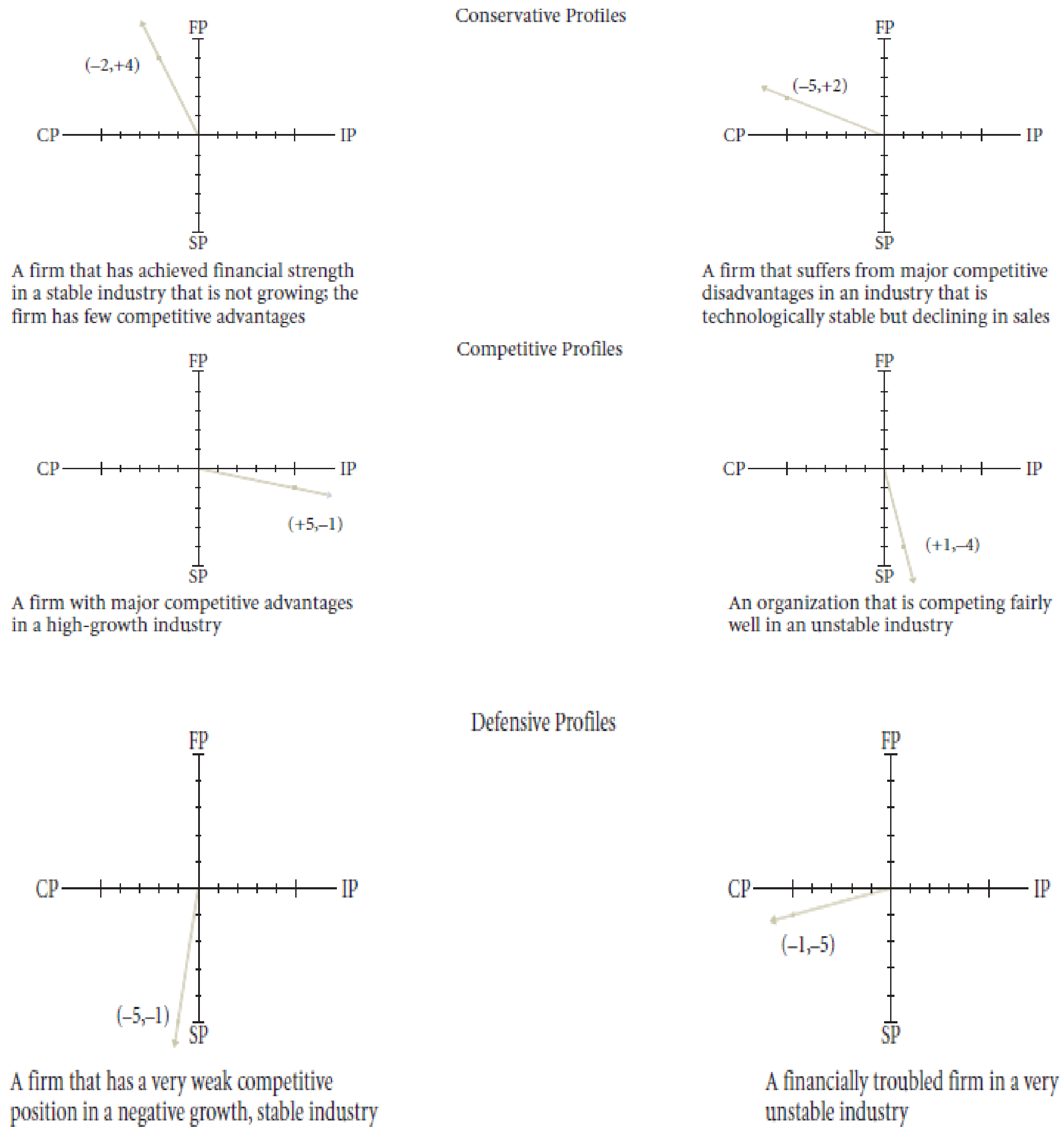
This graph indicates that firm adopts aggressive strategy

Some examples of strategy profiles that can emerge from a SPACE analysis are shown in Figure 5.2 below. The directional vector associated with each profile suggests the type of strategies to pursue: aggressive, conservative, defensive, or competitive. When a firm's directional vector is located in the ***aggressive quadrant*** (upper-right quadrant) of the SPACE Matrix, an organization is in an excellent position to use its internal strengths to (1) take advantage of external opportunities, (2) overcome internal weaknesses, and (3) avoid external threats. Therefore, market penetration, market development, product development, backward integration, forward integration, horizontal integration, or diversification, can be feasible, depending on the specific circumstances that face the firm.

The directional vector may appear in the ***conservative quadrant*** (upper-left quadrant) of the SPACE Matrix, which implies staying close to the firm's basic competencies and not taking excessive risks. Conservative strategies most often include market penetration, market development, product development, and related diversification. The directional vector may be located in the lower-left or ***defensive quadrant*** of the SPACE Matrix, which suggests that the firm should focus on rectifying internal weaknesses and avoiding external threats. Defensive strategies include retrenchment, divestiture, liquidation, and related diversification. Finally, the directional vector may be located in the lower-right or ***competitive quadrant*** of the SPACE Matrix, indicating

competitive strategies. Competitive strategies include backward, forward, and horizontal integration; market penetration; market development and product development.

Figure 5.2: Some examples of strategy profiles that can emerge from a SPACE analysis



Activity 5.7

1. **What is the Boston Consulting Group Matrix?**

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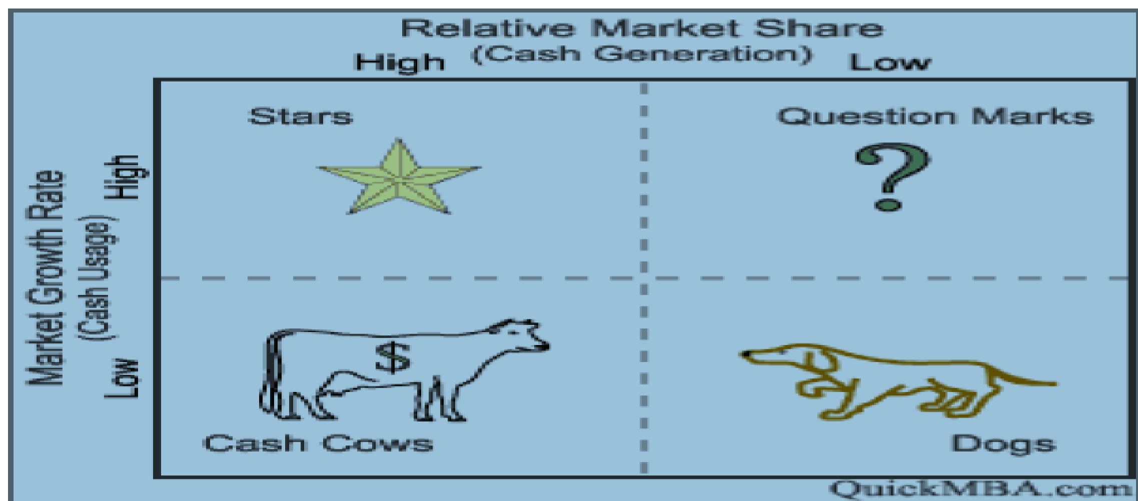
5.5.3 Boston Consulting Group (BCG) Matrix-

The Boston Consulting Group (BCG) is a management consulting firm founded by Harvard Business School alum Bruce Henderson in 1963. The **growth-share matrix** is a chart created by group in 1970 to help corporation analyze their business units or product lines, and decide where to allocate cash. It was popular for two decades, and is still used as an analytical tool. To use the chart, corporate analysts would plot a scatter graph of their business units, ranking their relative market shares and the growth rates of their respective industries. This led to a categorization of four different types of businesses:



The BCG Matrix

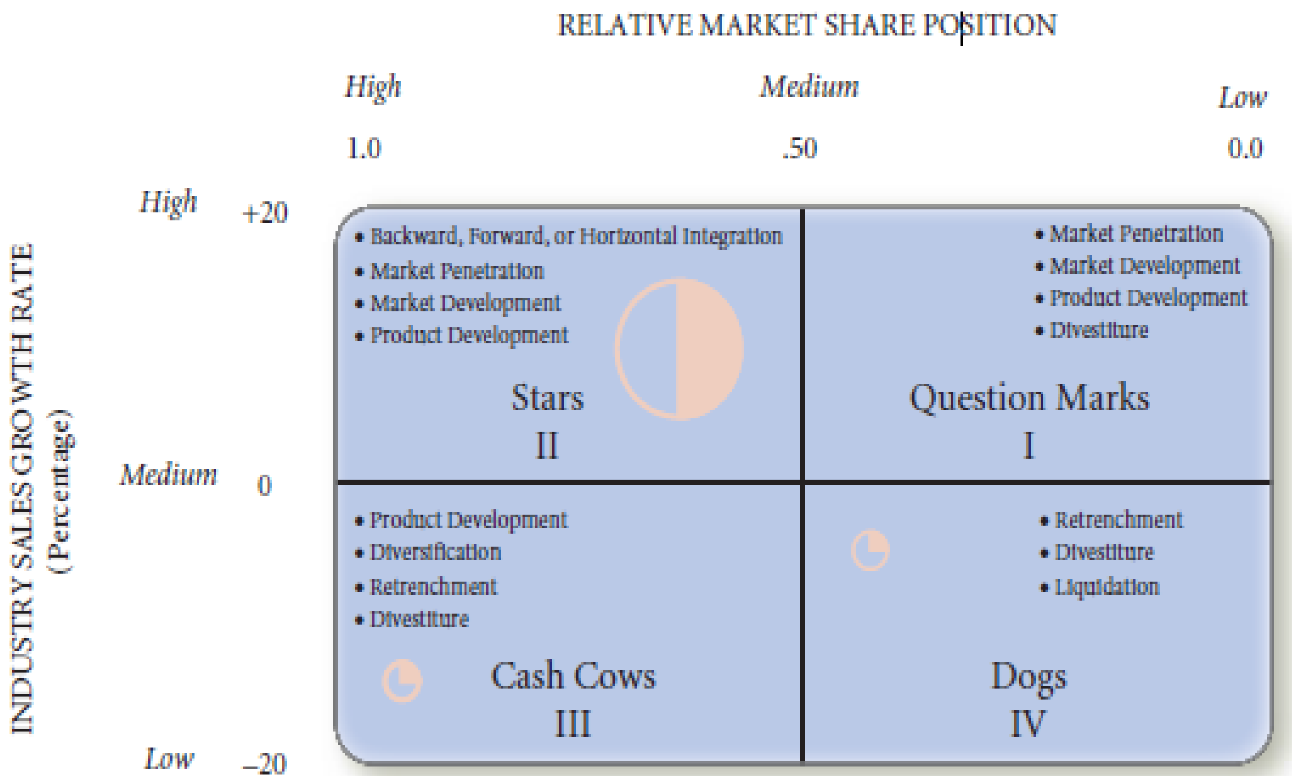


Figure 5-3: BCG matrix

I. Question marks: Units with low market share in a fast-growing industry. Such business units require large amounts of cash to grow their market share. The corporate goal must be to grow the business to become a star. Otherwise, when the industry matures and growth slows, the unit will fall down into the dog's category. ***Question Marks*** are divisions in Quadrant I have a low relative market share position, yet they compute in high growth industry. Generally these firms' cash needs are high and their cash generation is low. These businesses are called *Question Marks* because the organization must decide whether to strengthen them by pursuing an intensive strategy (market penetration, market development, or product development) or to sell them.

II. Stars: Units with a high market share in a fast-growing industry. The hope is that stars become the next cash cows. Sustaining the business unit's market leadership may require extra cash, but this is worthwhile if that's what it takes for the unit to remain a leader. When growth slows, stars become cash cows if they have been able to maintain their category leadership.

Stars-Quadrant II businesses (*Stars*) represent the organization's best long-run opportunities for growth and profitability. Divisions with a high relative market share and a high industry growth rate should receive substantial investment to maintain or strengthen their dominant positions. Forward, backward and horizontal integration; market penetration; market development; and product development are appropriate strategies for these divisions to consider, as indicated in Figure 5-3.

III. *Cash Cows*-Divisions positioned in Quadrant III have a high relative market share position but compete in a low-growth industry. They are regarded as staid and boring, in a "mature" market, and every corporation would be thrilled to own as many as possible. They are to be "milked" continuously with as little investment as possible, since such investment would be wasted in an industry with low growth.
Called *Cash Cows* because they generate cash in excess of their needs, they are often milked. Many of today's Cash hey compete in a high-growth industry. Generally these firms' cash needs are Cows were yesterday's Stars. Cash Cow divisions should be managed to maintain their strong position for as long as possible. Product development or diversification may be attractive strategies for strong Cash Cows. However, as a Cash Cow division becomes weak, retrenchment or divestiture can become more appropriate.

IV. Dogs (Quadrant IV): more charitably called pets, units with low market share in a mature, slow-growing industry. These units typically "break even", generating barely enough cash to maintain the business's market share. Though owning a break-even unit provides the social benefit of providing jobs and possible synergies that assist other business units, from an accounting point of view such a unit is worthless, not generating cash for the company. They depress a profitable company's return on assets ratio, used by many investors to judge how well a company is being managed. Dogs, it is thought, should be sold off.
Because of their weak internal and external position, these businesses are often liquidated, divested, or trimmed down through retrenchment. When a division first becomes a Dog, retrenchment can be the best strategy to pursue because many Dogs have bounced back, after strenuous asset and cost reduction, to become viable, profitable divisions.

As a particular industry matures and its growth slows, all business units become either cash cows or dogs. The overall goal of this ranking was to help corporate analysts decide which of their business units to fund, and how much; and which units to sell. Managers were supposed to gain perspective from this analysis that allowed them to plan with confidence to use money generated by the cash cows to fund the stars and, possibly, the question marks. As the BCG stated in 1970: Only a diversified company with a balanced portfolio can use its strengths to truly capitalize on its growth opportunities. (N.B: An autonomous divisions (or profit centers) of an organization make up what is called a ***business portfolio**.)*

The balanced portfolio has:

- Stars whose high share and high growth assure the future;
- Cash cows that supply funds for that future growth; and
- Question marks to be converted into stars with the added funds.

Practical Use of the Boston Matrix

For each product or service the 'area' of the circle represents the value of its sales. The Boston Matrix thus offers a very useful 'map' of the organization's product (or service) strengths and weaknesses (at least in terms of current profitability) as well as the likely cash flows. The need which prompted this idea was, indeed, that of managing cash-flow. It was reasoned that one of the main indicators of cash generation was relative market share, and one which pointed to cash usage was that of market growth rate.

Relative market share: This indicates likely cash generation, because the higher the share the more cash will be generated. As a result of 'economies of scale' (a basic assumption of the Boston Matrix), it is assumed that these earnings will grow faster the higher the share. The exact measure is the brand's share relative to its largest competitor.

On the other hand, exactly what is a high relative share is a matter of some debate. The best evidence is that the most stable position (at least in FMCG markets) is for the brand leader to have a share double that of the second brand, and treble that of the third. Brand leaders in this position tend to be very stable - and profitable. The reason for choosing relative market share, rather than just profits, is that it carries more information than just cash flow. It shows where the brand is

positioned against its main competitors, and indicates where it might be likely to go in the future. It can also show what type of marketing activities might be expected to be effective.

The major benefit of the BCG Matrix is that it draws attention to the cash flow, investment characteristics, and needs of an organization's various divisions. The divisions of many firms evolve over time: Dogs become Question Marks, Question Marks become Stars, Stars become Cash Cows, and Cash Cows become Dogs in an ongoing counterclockwise motion. Less frequently, Stars become Question Marks, Question Marks become Dogs, Dogs become Cash Cows, and Cash Cows become Stars (in a clockwise motion). In some organizations, no cyclical motion is apparent. Over time, organizations should strive to achieve a portfolio of divisions that are Stars.

Limitations

1. Viewing every business as a star, cash cow, dog, or question mark is overly simplistic.
2. Many businesses fall right in the middle of the BCG matrix and thus are not easily classified.
3. The BCG matrix does not reflect whether or not various divisions or their industries are growing over time.
4. Other variables besides relative market share position and industry growth rate in sales are important in making strategic decisions about various divisions.

Conclusion

After discussion, the BCG matrix is an important matrix regarding strategy adopted by firm. Still this matrix concern four strategy first growth or build strategy enhance market share), second is hold strategy (hold existing position), third Harvesting strategy (no further growth or select other opportunity), fourth is divested (sell out the part of business)

Activity 5.8

1. **Discuss the steps for the development of IE matrix.**

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Boston Consulting Group BCG Matrix-2

The Internal-External (IE) Matrix: This is also an important matrix of matching stage of strategy formulation. This matrix already explains earlier. It relate to Internal Factor Evaluation (IFE) and External Factor Evaluation (EFE). The findings from internal and external position and weighted score plot on it. It contains nine cells. Its characteristics are as follow;

1 Positions an organization's various divisions in a nine-cell display.

2 Similar to BCG Matrix except the IE Matrix: Requires more information about the divisions.

- Strategic implications of each matrix are different

3 Based on two key dimensions

- The IFE total weighted scores on the x-axis
- The EFE total weighted scores on the y-axis

4 Divided into three major regions

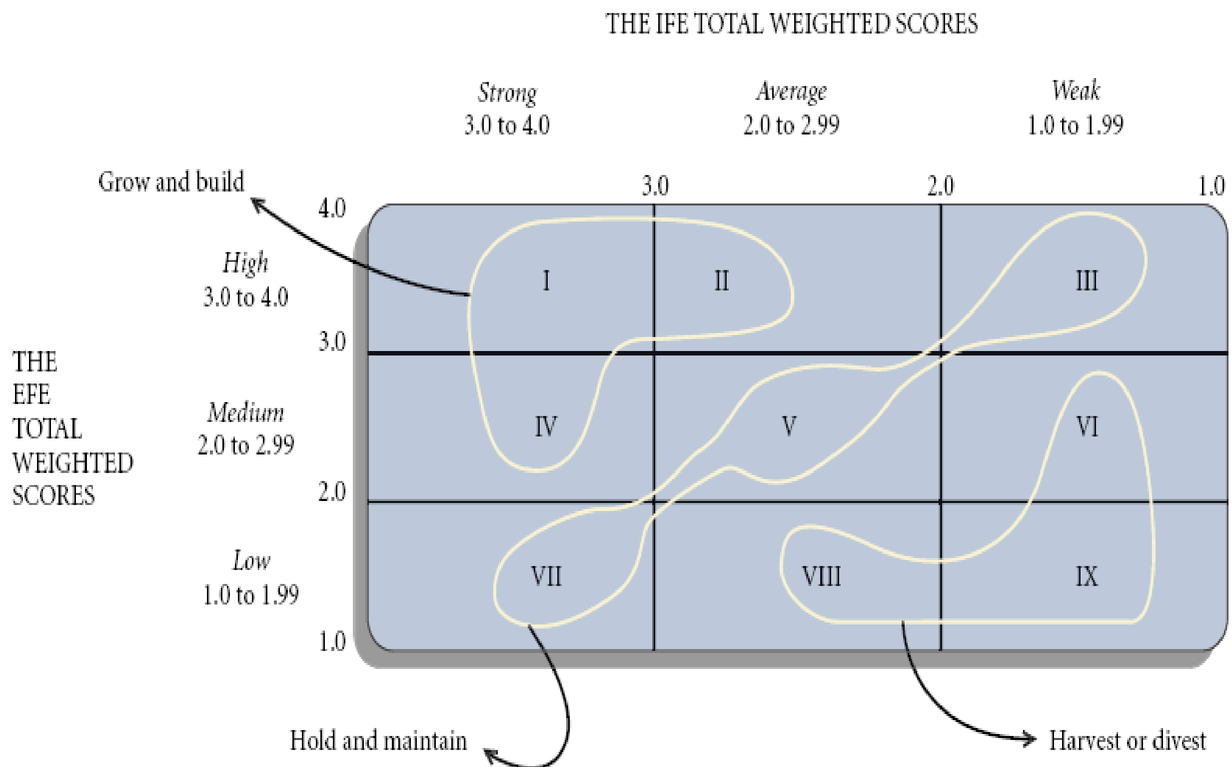
- Grow and build – Cells I, II, or IV
- Hold and maintain – Cells III, V, or VII
- Harvest or divest – Cells VI, VIII, or IX

Steps for the development of IE matrix

1. Based on two key dimensions IFE and EFE.
2. Plot IFE total weighted scores on the x-axis and the EFE total weighted scores on the y axis
3. On the x-axis of the IE Matrix, an IFE total weighted score of 1.0 to 1.99 represents a weak internal position; a score of 2.0 to 2.99 is considered average; and a score of 3.0 to 4.0 is strong.

4. On the y-axis, an EFE total weighted score of 1.0 to 1.99 is considered low; a score of 2.0 to 2.99 is medium; and a score of 3.0 to 4.0 is high.
5. IE Matrix divided into three major regions.
   a. Grow and build – Cells I, II, or IV,
   b. Hold and maintain – Cells III, V, or VII
   c. Harvest or divest – Cells VI, VIII, or IX

The Internal-External (IE) Matrix



5 Grand Strategy Matrix-1

Grand Strategy Matrix: This is also an important matrix of strategy formulation frame work. Grand strategy matrix it is popular tool for formulating alternative strategies. In this matrix all organization divides into four quadrants. Any organization should be placed in any one of four quadrants. Appropriate strategies for an organization to consider are listed in sequential order of attractiveness in each quadrant of the matrix. It is based two major dimensions

- Market growth
- Competitive position. All quadrant contains all possible strategies

Qurdant-1 contains that company's strong having competitive situation and rapid market growth. Firms located in Quadrant I of the Grand Strategy Matrix are in an excellent strategic position. These firms must focus on current market and appropriate to follow market penetration, market development and products development are appropriate strategies.

Qurdant-2 contains that company's having weak competitive situation and rapid market growth. Firms positioned in Quadrant II need to evaluate their present approach to the marketplace seriously. Although their industry is growing, they are unable to compete effectively, and they need to determine why the firm's current approach is ineffectual and how the company can best change to improve its competitiveness. Because Quadrant II firms are in a rapid-market-growth

industry, an intensive strategy (as opposed to integrative or diversification) is usually the first option that should be considered.

Qurdant-3 contains that company's weak competitive situation and slow market growth. The firms fall in this quadrant compete in slow-growth industries and have weak competitive positions. These firms must make some drastic changes quickly to avoid further demise and possible liquidation. Extensive cost and asset reduction (retrenchment) should be pursued first. An alternative strategy is to shift resources away from the current business into different areas. If all else fails, the final options for Quadrant III businesses are divestiture or liquidation.

Qurdant-4 contains that company's strong competitive situation and slow market growth. Finally, Quadrant IV businesses have a strong competitive position but are in a slow-growth industry. These firms have the strength to launch diversified programs into more promising growth areas. Quadrant IV firms have characteristically high cash flow levels and limited internal growth needs and often can pursue concentric, horizontal, or conglomerate diversification successfully. Quadrant IV firms also may pursue joint ventures.

Conclusion

Every firm fall any one four quadrants and if the firm fall in quadrant-1 it must follow the list of strategies given in it. As further if the firm falls in quarrant-2 must adopt the strategies given in quadrant-2 and so on.

Stage 3: The Decision Stage

GRAND STRATEGY MATRIX-2

Stage 3, called the Decision Stage, and involves a single technique, the Quantitative Strategic Planning Matrix (QSPM). A QSPM uses input information from Stage 1 to objectively evaluate feasible alternative strategies identified in Stage 2. A QSPM reveals the relative attractiveness of alternative strategies and, thus, provides an objective basis for selecting specific strategies. All nine techniques included in the strategy-formulation framework require integration of intuition and analysis.

Analysis and intuition provide a basis for making strategy-formulation decisions. The matching techniques just discussed reveal feasible alternative strategies. Many of these strategies will likely have been proposed by managers and employees participating in the strategy analysis and choice activity. Any additional strategies resulting from the matching analyses could be discussed and added to the list of feasible alternative options. As indicated earlier in this chapter, participants could rate these strategies on a 1 to 4 scale so that a prioritized list of the best strategies could be achieved.

The Quantitative Strategic Planning Matrix (QSPM)

Other than ranking strategies to achieve the prioritized list, there is only one analytical technique in the literature designed to determine the relative attractiveness of feasible alternative actions. This technique is the *Quantitative Strategic Planning Matrix (QSPM),* which comprises Stage 3 of the strategy-formulation analytical framework. This technique objectively indicates which alternative strategies are best. The QSPM uses input from Stage 1 analyses and matching results from Stage 2 analyses to decide objectively among alternative strategies. That is, the EFE Matrix, IFE Matrix, and Competitive Profile Matrix that make up Stage 1, coupled with the SWOT Matrix, SPACE Matrix, BCG Matrix, IE Matrix, and Grand Strategy Matrix that make up Stage 2, provide the needed information for setting up the QSPM (Stage 3). The QSPM is a tool that allows strategists to evaluate alternative strategies objectively, based on previously identified external and internal critical success factors. Like other strategy-formulation analytical tools, the QSPM requires good intuitive judgment.

The six steps required to develop a QSPM are discussed here below:

Step-1: ***Make a list of the firm's key external opportunities/threats and internal strengths/weaknesses in the left column of the QSPM.*** This information should be taken directly from the EFE Matrix and IFE Matrix. A minimum of 10 external key success factors and 10 internal key success factors should be included in the QSPM.

Step-2: ***Assign weights to each key external and internal factor.*** These weights are identical to those in the EFE Matrix and the IFE Matrix. The weights are presented in a straight column just to the right of the external and internal critical success factors.

Step-3: ***Examine the Stage 2 (matching) matrices, and identify alternative strategies that the organization should consider implementing.*** Record these strategies in the top row of the QSPM. Group the strategies into mutually exclusive sets if possible.

Step-4: ***Determine the Attractiveness Scores (AS)*** defined as numerical values that indicate the relative attractiveness of each strategy in a given set of alternatives. *Attractiveness Scores (AS)* are determined by examining each key external or internal factor, one at a time, and asking the question "Does this factor affect the choice of strategies being made?" If the answer to this question is yes, then the strategies should be compared relative to that key factor. Specifically, Attractiveness Scores should be assigned to each strategy to indicate the relative attractiveness of one strategy over others, considering the particular factor. The range for Attractiveness Scores is 1 = not attractive, 2 = somewhat attractive, 3 = reasonably attractive, and 4 = highly attractive. By attractive, we mean the extent that one strategy, compared to others, enables the firm to either capitalize on the strength, improve on the weakness, exploit the opportunity, or avoid the threat. Work row by row in developing a QSPM. If the answer to the previous question is *no,* indicating that the respective key factor has no effect upon the specific choice being made, then do not assign Attractiveness Scores to the strategies in that set. Use a dash to indicate that the key factor does not affect the choice being made. *Note:* If you assign an AS score to one strategy, then assign AS score(s) to the other. In other words, if one strategy receives a dash, then all others must receive a dash in a given row.

Step-5: ***Compute the Total Attractiveness Scores (TAS).*** *Total Attractiveness Scores (TAS)* are defined as the product of multiplying the weights (Step 2) by the Attractiveness Scores (Step 4) in each row. The Total Attractiveness Scores indicate the relative attractiveness of each alternative strategy, considering only the impact of the adjacent external or internal critical success factor. The higher the Total Attractiveness Score, the more attractive the strategic alternative (considering only the adjacent critical success factor).

Step-6: ***Compute the Sum Total Attractiveness Score (STAS).*** Add Total Attractiveness Scores in each strategy column of the QSPM. The *Sum Total Attractiveness Scores (STAS)* reveal which strategy is most attractive in each set of alternatives. Higher scores indicate more attractive strategies, considering all the relevant external and internal factors that could affect the strategic

decisions. The magnitude of the difference between the Sum Total Attractiveness Scores in a given set of strategic alternatives indicates the relative desirability of one strategy over another.

	Weight	Strategy 1		Strategy 2		Strategy 3	
		AS	TAS	AS	TAS	AS	TAS
Key External Factors							
Economy conditions							
Social/Cultural/Demographic /Environmental							
Political/Legal/Governmental							
Competitive							
Technological							
Consumer attitude							
Key Internal Factors							
Research and Development							
Computer Information							
Finance/Accounting							
Production/Operations							
Management							
Marketing							
Systems							

Limitations

- Requires intuitive judgments and educated assumptions
- Only as good as the prerequisite inputs
- Only strategies within a given set are evaluated relative to each other

Advantages

- Sets of strategies considered simultaneously or sequentially
- Integration of pertinent external and internal factors in the decision making process

Activity 5.9

1. **How culture of the society affects the strategy of a given organization?**

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5.6 Cultural Aspects of Strategy Choice

All organizations have a culture. *Culture* includes the set of shared values, beliefs, attitudes, customs, norms, personalities, heroes, and heroines that describe a firm. Culture is the unique way an organization does business. It is the human dimension that creates solidarity and meaning, and it inspires commitment and productivity in an organization when strategy changes are made. All human beings have a basic need to make sense of the world, to feel in control, and to make meaning. When events threaten meaning, individuals react defensively. Managers and employees may even sabotage new strategies in an effort to recapture the status quo.

It is beneficial to view strategic management from a cultural perspective because success often rests upon the degree of support that strategies receive from a firm's culture. If a firm's strategies are supported by cultural products such as values, beliefs, rites, rituals, ceremonies, stories, symbols, language, heroes, and heroines, then managers often can implement changes swiftly and easily. However, if a supportive culture does not exist and is not cultivated, then strategy changes may be ineffective or even counterproductive. A firm's culture can become antagonistic to new strategies, and the result of that antagonism may be confusion and disarray.

Strategies that require fewer cultural changes may be more attractive because extensive changes can take considerable time and effort. Whenever two firms merge, it becomes especially important to evaluate and consider culture-strategy linkages. Culture provides an explanation for the difficulties a firm encounters when it attempts to shift its strategic direction, as the following statement explains: Not only has the "right" corporate culture become the essence and foundation of corporate excellence, but success or failure of needed corporate reforms hinges on management's sagacity and ability to change the firm's driving culture in time and in tune with required changes in strategies.

5.7 The Politics of Strategy Choice

All organizations are political. Unless managed, political maneuvering consumes valuable time, subverts organizational objectives, diverts human energy, and results in the loss of some valuable employees. Sometimes political biases and personal preferences get unduly embedded in strategy

choice decisions. Internal politics affect the choice of strategies in all organizations. The hierarchy of command in an organization, combined with the career aspirations of different people and the need to allocate scarce resources, guarantees the formation of coalitions of individuals who strive to take care of themselves first and the organization second, third, or fourth. Coalitions of individuals often form around key strategy issues that face an enterprise. A major responsibility of strategists is to guide the development of coalitions, to nurture an overall team concept, and to gain the support of key individuals and groups of individuals.

In the absence of objective analyses, strategy decisions too often are based on the politics of the moment. With development of improved strategy-formation tools, political factors become less important in making strategic decisions. In the absence of objectivity, political factors sometimes dictate strategies, and this is unfortunate. Managing political relationships is an integral part of building enthusiasm and esprit de corps in an organization.

A classic study of strategic management in nine large corporations examined the political tactics of successful and unsuccessful strategists.9 Successful strategists were found to let weakly supported ideas and proposals die through inaction and to establish additional hurdles or tests for strongly supported ideas considered unacceptable but not openly opposed. Successful strategists kept a low political profile on unacceptable proposals and strived to let most negative decisions come from subordinates or a group consensus, thereby reserving their personal vetoes for big issues and crucial moments. Successful strategists did a lot of chatting and informal questioning to stay abreast of how things were progressing and to know when to intervene. They led strategy but did not dictate it. They gave few orders, announced few decisions, depended heavily on informal questioning, and sought to probe and clarify until a consensus emerged. Successful strategists generously and visibly rewarded key thrusts that succeeded.

They assigned responsibility for major new thrusts to *champions,* the individuals most strongly identified with the idea or product and whose futures were linked to its success. They stayed alert to the symbolic impact of their own actions and statements so as not to send false signals that could stimulate movements in unwanted directions.

Successful strategists ensured that all major power bases within an organization were represented in, or had access to, top management. They interjected new faces and new views into considerations of major changes. This is important because new employees and managers

generally have more enthusiasm and drive than employees who have been with the firm a long time. New employees do not see the world the same old way; nor do they act as screens against changes. Successful strategists minimized their own political exposure on highly controversial issues and in circumstances in which major opposition from key power centers was likely. In combination, these findings provide a basis for managing political relationships in an organization. Because strategies must be effective in the marketplace and capable of gaining internal commitment, the following tactics used by politicians for centuries can aid strategists:

• ***Equi-finality***-It is often possible to achieve similar results using different means or paths. Strategists should recognize that achieving a successful outcome is more important than imposing the method of achieving it. It may be possible to generate new alternatives that give equal results but with far greater potential for gaining commitment.

• ***Satisfying***-Achieving satisfactory results with an acceptable strategy is far better than failing to achieve optimal results with an unpopular strategy.

• ***Generalization***-Shifting focus from specific issues to more general ones may increase strategists' options for gaining organizational commitment.

• ***Focus on Higher-Order Issues***-By raising an issue to a higher level, many short term interests can be postponed in favor of long-term interests. For instance, by focusing on issues of survival, the airline and automotive industries were able to persuade unions to make concessions on wage increases.

• ***Provide Political Access on Important Issues***-Strategy and policy decisions with significant negative consequences for middle managers will motivate intervention behavior from them. If middle managers do not have an opportunity to take a position on such decisions in appropriate political forums, they are capable of successfully resisting the decisions after they are made. Providing such political access provides strategists with information that otherwise might not be available and that could be useful in managing intervention behavior.

5.8 Balanced Scorecard (BSC) Model

The **balanced scorecard** is a strategic performance management tool- a semi- standard structured report supported by proven design methods and automation tools that can be used by managers to keep track of the execution of activities by staff within their control and monitor the consequences arising from these actions.

History: The first balanced scorecard was created by Art Schneider man (an independent consultant on the management of processes) in 1987 at Analog Devices, a mid-sized semi-conductor company. Art Schnieder man participated in an unrelated research study in 1990 led by Dr. Robert S.Kaplan in conjunction with US management consultancy Nolan-Norton, and during this study described his work on balanced Scorecard. Subsequently, Kaplan and David P.Norton included anonymous details of this use of balanced Scorecard in their 1992 article on Balanced Scorecard. Kaplan & Norton's article wasn't the only paper on the topic published in early 1992. But the 1992 Kaplan & Einstein College of Engineering 17 Norton paper was a popular success, and was quickly followed by a second in 1993. In 1996, they published the book The Balanced Scorecard. These articles and the first book spread knowledge of the concept of Balanced Scorecard widely, but perhaps wrongly have led to Kaplan & Norton being seen as the creators of the Balanced Scorecard concept. **Four Perspectives:**

1. **Financial:** Encourages the identification of a few relevant high-level financial measures.
2. **Customer:** Encourages the identification of measures that answer the question "How do customers see us?"
3. **Internal Business Process:** encourages the identification of measures that answer the question "What must we excel at?"
4. **Learning and Growth:** encourages the identification of measures that answer the question "Can we continue to improve and create value?"

5.9 McKinsey's 7'S Model

This was created by the consulting company McKinsey and company in the early 1980s. Since then it has been widely used by practitioners and academics alike in analyzing hundreds of organizations. The Paper explains each of the seven components of the model and the links between them. It also includes practical guidance and advice for the students to analyze organizations using this model. At the end, some sources for further information on the model and case studies available. The McKinsey 7S model was named after a consulting company, McKinsey and company, which has conducted applied research in business and industry. All of the authors worked as consultants at McKinsey and company, in the 1980s, they used the model to analyze over 70 large organizations. The McKinsey 7S Framework was created as a recognizable and

easily remembere model in business. The seven variables, which the authors terms “levers”, all begin with the letter “S”.

Description of 7Ss:

1. **Strategy**: Strategy is the plan of action an organization prepares in response to, or anticipation of changes in its external environment. It is a plan or course of action leading to the allocation of firm’s resources to reach identified goals.
2. **Structure:** Business needs to be organized in a specific form of shape that is generally referred to as organizational structure. Organizations are structured in a variety of ways, depends on their objectives and culture.
3. **Systems:** Every organization has some systems or internal processes to support and implement the strategy and run day-to-day affairs. It is a formal processes and procedures, including management control systems, performance measurement and reward systems, and planning and budgeting systems, and the ways people relate to them. For example, a company may follow a particular process for recruitment.
4. **Shared Values/super ordinate Goals:** All members of the organization share some common fundamental ideas or guiding concepts around which the business is built. This may be to make money or to achieve excellence in a particular field.
5. **Style/culture:** All organizations have their own distinct culture and management style. It includes the dominant values, beliefs and norms which develop over time and become relatively enduring features of the organizational life. It is a reflection of the norms people act upon and how they work and interact with each other, vendors, and customers.
6. **Staff:** Organizations are made up of humans and it’s the people who make the real difference to the success of the organization in the increasingly knowledge-based society. The importance of human resources has thus got the central position in the strategy of the organization, away from the traditional model of capital and land.
7. **Skills** – Organizational competencies, including the abilities of individuals as well as management practices, technological abilities, and other capabilities that reside in the organization. It includes activities like recruitment, selection, development, socialization, and advancement of people in the organization.

The seven components described above are normally categorized as soft and hard components:

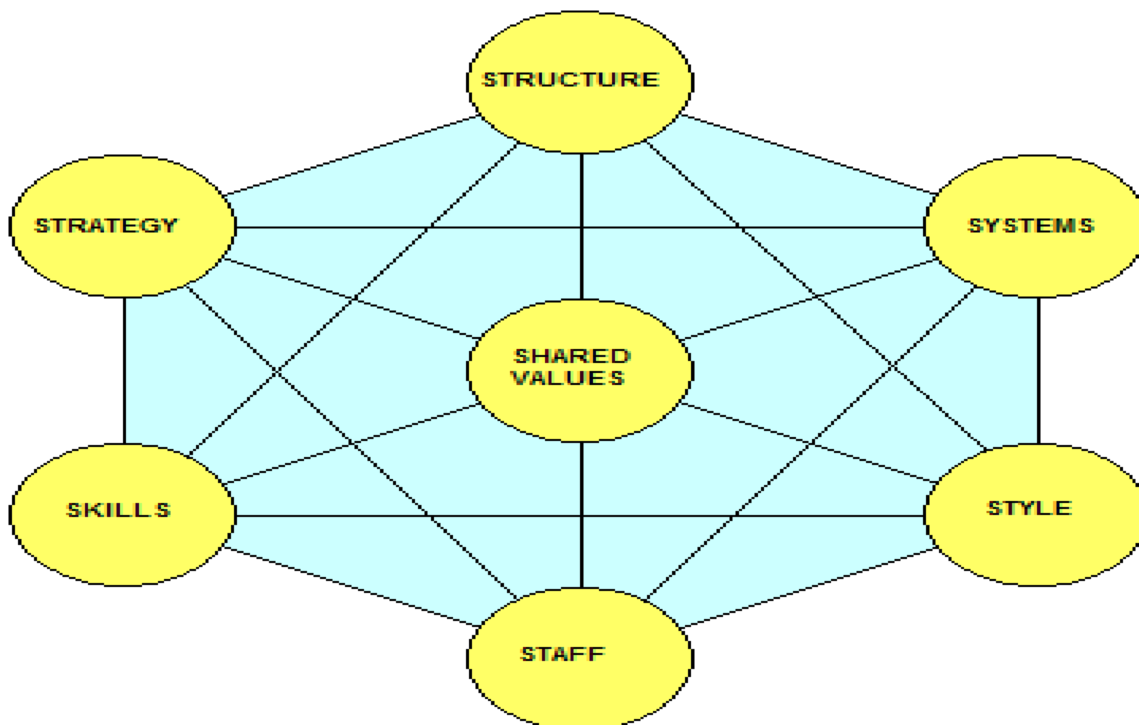
- Hard components
- Soft components

Hard components are:

- Strategy
- Structure
- Systems

Soft components are:

- Shared values
- Style
- Staff
- Skills



Distinctive Competitiveness Meaning: Distinctive Competence is a set of unique capabilities that certain firms possess allowing them to make inroads into desired markets and to gain advantage over the competition; generally, it is an activity that a firm performs better than its competition. To define a firm's distinctive competence, management must complete an assessment of both internal and external corporate environments. When management finds an internal strength

and both meets market needs and gives the firm a comparative advantage in the market place, that strength is the firm's distinctive competence.

Defining and Building Distinctive Competence: To define a company's distinctive competence, managers often follow a particular process.

1. They identify the strengths and weaknesses in the given marketplace.

2. They analyze specific market needs and look for comparative advantages that they have over the competition.

Summary

The main appeal of any managerial approach is the expectation that it will enhance organizational performance. This is especially true of strategic management. Through involvement in strategic-management activities, managers and employees achieve a better understanding of an organization's priorities and operations. Strategic management allows organizations to be efficient, but more important, it allows them to be effective.

Although strategic management does not guarantee organizational success, the process allows proactive rather than reactive decision making. Strategic management may represent a radical change in philosophy for some organizations, so strategists must be trained to anticipate and constructively respond to questions and issues as they arise. The 16 strategies discussed in this chapter can represent a new beginning for many firms, especially if managers and employees in the organization understand and support the plan for action.

Review Questions

1. When backward integration can be an effective strategy?
   - A. When an organization has resources to manage the new business.
   - B. When the advantages of stable prices are particularly important
   - C. When present supplies have high profit margins
   - D. When an organization needs to acquire a needed resource quickly
   - E. All of the above
   - F. All of the above

2. When the business involves in international trade, which one of the following intensive strategies the business followed?
   - A. Market Penetration
   - B. Market Development
   - C. Product Development
   - D. Concentric Diversification
   - E. None of the above

3. In all of the following a given organization can use market development except one?
- A. New channels of distribution that are reliable, inexpensive, and good quality
- B. Excess production capacity
- C. Saturated markets
- D. Firm is very successful at what it does
- E. Basic industry rapidly becoming global
- F. None of the above

4. Which one of the following is conducted based on two assumptions, to lower the price but promotional activities are not changed?
- A. Slow market penetration
- B. Forward integration
- C. Product Development
- D. Rapid market penetration
- E. A and B
- F. None of the above

5. _______ involves adding new, unrelated products or services to the business.
- A. Horizontal Diversification
- B. Concentric Diversification
- C. Conglomerate Diversification
- D. Vertical diversification
- E. All of the above
- F. None of the above

6. One of the following is not recommended for the organization to use retrenchment strategy?
- A. Firm has failed to meet its objectives and goals consistently over time and lack distinctive competencies
- B. Firm is strong competitor in the industry.
- C. Firm has efficiency, profitability and high employee morale
- D. When an organization's strategic managers have success.
- E. All of the above
- F. None of the above

7. When ABC Company is selling a division of the company to raise capital for further strategic acquisitions or investments, which one of the following defensive strategy ABC Company implement.
- A. Liquidation
- B. Joint Venture
- C. Retrenchment
- D. Divestiture
- E. All of the above
- F. None of the above

8. Horizontal integration can be an effective strategy in the following cases **except**?
- A. When increased economies of scale provide major competitive advantages
- B. When an organization can gain monopolistic characteristics in a particular area
- C. When competitors are faltering due to a lack of managerial expertise or a need for particular resources that an organization possesses
- D. When an organization competes in a declining industry
- E. All of the above
- F. None of the above

9. Which one of the following is **incorrect** about cost leadership strategies?
- A. Considerable market share advantage is required to be successful
- B. The most extensive distribution strategy is needed.

C. Buyers are sensitive to brand differences
D. Incentives based on quantitative targets
E. All of the above
F. None of the above

10. All are **correct** about differentiation strategies **except**?

A. Differentiation strategies allow firm to charge higher price gain customer loyalty.
B. Can provide considerable protection from competition.
C. Strong research and development skills
D. Attract highly skilled, creative people
E. All of the above
F. None of the above

CHAPTER SIX: STRATEGY IMPLEMENTATION

Aims of the Chapter

This chapter deals with the techniques used to implement the strategy of the organization. It also presents the key concepts in strategy implementation and the different organizational structures. You will also learn the importance of managing the Natural environment and the different concerns in implementing organizational strategies.

At the end of this chapter, you will be expected to:

- ♣ Understand the concepts of strategic implementation
- ♣ Be able to differentiate restructuring and reengineering
- ♣ Examine the techniques used to managing resistance to change
- ♣ Discuss the human resource concerns when implementing strategies

6.1 Introduction

The strategic-management process does not end when the firm decides what strategy or strategies to pursue. There must be a translation of strategic thought into strategic action. This translation is much easier if managers and employees of the firm understand the business, feel a part of the company, and through involvement in strategy-formulation activities have become committed to helping the organization succeed. Without understanding and commitment, strategy-implementation efforts face major problems.

Implementing strategy affects an organization from top to bottom; it affects all the functional and divisional areas of a business. Even the most technically perfect strategic plan will serve little purpose if it is not implemented. Many organizations tend to spend an inordinate amount of time, money, and effort on developing the strategic plan, treating the means and circumstances under which it will be implemented as afterthoughts! Change comes through implementation and evaluation, not through the plan. A technically imperfect plan that is implemented will achieve more than the perfect plan that never gets off the paper on which it is typed.

Activity 6.1

Discuss how a given organization implement their strategy.

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6.2 The Nature of Strategy Implementation

It is possible to turn strategies and plans into individual actions, necessary to produce a great business performance. But it's not easy. Many companies repeatedly fail to truly motivate their people to work with enthusiasm, all together, towards the corporate aims. Most companies and organizations know their businesses, and the strategies required for success. However, many corporations - especially large ones - struggle to translate the theory into action plans that will enable the strategy to be successfully implemented and sustained. Here are some leading edge methods for effective strategic corporate implementation. These advanced principles of strategy realization are provided by the very impressive Foresight Leadership organization, and this contribution is gratefully acknowledged. Most companies have strategies, but according to recent studies, between 70% and 90% of organizations that have formulated strategies fail to execute them.

Only 1 in 3 companies, in their own assessment, were achieving significant strategic success. The message clear - effective strategy realization is key for achieving strategic success. Successful strategy formulation does not guarantee successful strategy implementation. It is always more difficult to do something (strategy implementation) than to say you are going to do it (strategy formulation)! Although inextricably linked, strategy implementation is fundamentally different from strategy formulation. Strategy formulation and implementation can be contrasted in the following ways:

- ✓ Strategy formulation is positioning forces before the action but strategy implementation is managing forces during the action.
- ✓ Strategy formulation focuses on effectiveness but strategy implementation focuses on efficiency.

- ✓ Strategy formulation is primarily an intellectual process but strategy implementation is primarily an operational process.
- ✓ Strategy formulation requires good intuitive and analytical skills. However, strategy implementation requires special motivation and leadership skills.
- ✓ Strategy formulation requires coordination among a few individuals but strategy implementation requires coordination among many persons.
- ✓ Strategy-formulation concepts and tools do not differ greatly for small, large, for profit, or nonprofit organizations. However, strategy implementation varies substantially among different types and sizes of organizations.

Implementing strategies requires such actions as altering sales territories, adding new departments, closing facilities, hiring new employees, changing an organization's pricing strategy, developing financial budgets, developing new employee benefits, establishing cost-control procedures, changing advertising strategies, building new facilities, training new employees, transferring managers among divisions, and building a better computer information system. These types of activities obviously differ greatly between manufacturing, service, and governmental organizations.

Activity 6.2

What are the main points considered in strategy implementation?

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6.3. Key Concepts in Strategy Implementation

Management Perspectives

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

involved as much as possible in strategy-formulation activities. Of equal importance, strategists should be involved as much as possible in strategy-implementation activities.

Management issues central to strategy implementation include establishing annual objectives, devising policies, allocating resources, altering an existing organizational structure, restructuring and reengineering, revising reward and incentive plans, minimizing resistance to change, matching managers with strategy, developing a strategy-supportive culture, adapting production/operations processes, developing an effective human resource function and, if necessary, downsizing. Management changes are necessarily more extensive when strategies to be implemented move a firm in a major new direction. Managers and employees throughout an organization should participate early and directly in strategy implementation decisions. Their role in strategy implementation should build upon prior involvement in strategy-formulation activities.

6.2.1 Annual Objectives

Objectives set out what the business is trying to achieve.

Objectives can be set at two levels:

(1) Corporate level

These are objectives that concern the business or organization as a whole

Examples of “corporate objectives might include:

• We aim for a return on investment of at least 15%

(2) Functional level

Examples of functional marketing objectives” might include:

• We aim to build customer database of at least 250,000 households within the next 12 months

Both corporate and functional objectives need to conform to the commonly used **SMART** criteria.

Annual objectives are essential for strategy implementation because they

(1) Represent the basis for allocating resources

(2) Are a primary mechanism for evaluating managers?

(3) Are the major instrument for monitoring progress toward achieving long-term objectives?

(4) Establish organizational, divisional, and departmental priorities.

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

The purpose of annual objectives can be summarized as follows:

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

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

6.2.2 Policies

Changes in a firm's strategic direction do not occur automatically. On a day-to-day basis, policies are needed to make a strategy work. Policies facilitate solving recurring problems and guide the implementation of strategy.

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

6.2.3 Budget (Resource Allocation)

In strategic planning, a resource-allocation decision is a plan for using available resources, especially human resources especially in the near term, to achieve goals for the future. It is the process of allocating resources among the various projects or business units.

The plan has two parts: Firstly, there is the basic allocation decision and secondly there are contingency mechanisms. The basic allocation decision is the choice of which items to fund in the

plan, and what level of funding it should receive, and which to leave unfunded: the resources are allocated to some items, not to others.

There are two contingency mechanisms. There is a priority ranking of items excluded from the plan, showing which items to fund if more resources should become available; and there is a priority ranking of some items included in the plan, showing which items should be sacrificed if total funding must be reduced.

Resource allocation is a major management activity that allows for strategy execution.

6.2.4 Organizational Structure

i. Functional Structure

The organization is structured according to functional areas instead of product lines. The functional structure groups specialize in similar skills in separate units. This structure is best used when creating specific, uniform products. A functional structure is well suited to organizations which have a single or dominant core product because each subunit becomes extremely adept at performing its particular portion of the process. They are economically efficient, but lack flexibility. Communication between functional areas can be difficult.

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

ii. Divisional Structure

Divisional structure is formed when an organization is split up into a number of self-contained business units, each of which operates as a profit centre. Such a division may occur on the basis of product or market or a combination of the two with each unit tending to operate along functional or product lines, but with certain key function (e.g. finance, personnel, corporate planning) provided centrally, usually at company headquarters.

As a small organization grows, it has more difficulty managing different products and services in different markets. Some form of divisional structure generally becomes necessary to motivate employees, control operations, and compete successfully in diverse locations. The divisional

structure can be organized in one of four ways: by geographic area, by product or service, by customer, or by process. With a divisional structure, functional activities are performed both centrally and in each separate division.

A divisional structure has some clear advantages. First and perhaps foremost, accountability is clear. That is, divisional managers can be held responsible for sales and profit levels. Because a divisional structure is based on extensive delegation of authority, managers and employees can easily see the results of their good or bad performances. As a result, employee morale is generally higher in a divisional structure than it is in a centralized structure. Other advantages of the divisional design are that it creates career development opportunities for managers, allows local control of local situations, leads to a competitive climate within an organization, and allows new businesses and products to be added easily.

The divisional design is not without some limitations, however. Perhaps the most important limitation is that a divisional structure is costly, for a number of reasons. First, each division requires functional specialists who must be paid. Second, there exists some duplication of staff services, facilities, and personnel; for instance, functional specialists are also needed centrally (at headquarters) to coordinate divisional activities. Third, managers must be well qualified because the divisional design forces delegation of authority; better-qualified individuals require higher salaries. Finally, certain regions, products, or customers may sometimes receive special treatment, and it may be difficult to maintain consistent, companywide practices. Nonetheless, for most large organizations and many small firms, the advantages of a divisional structure more than offset the potential limitations.

iii. The Strategic Business Unit (SBU) Structure

Strategic Business Unit or SBU is understood as a business unit within the overall corporate identity which is distinguishable from other business because it serves a defined external market where management can conduct strategic planning in relation to products and markets. When companies become really large, they are best thought of as being composed of a number of businesses (or SBUs).

These organizational entities are large enough and homogeneous enough to exercise control over most strategic factors affecting their performance. They are managed as self-contained planning units for which discrete business strategies can be developed. A Strategic Business Unit can encompass an entire company, or can simply be a smaller part of a company set up to perform a specific task. The SBU has its own business strategy, objectives and competitors and these will often be different from those of the parent company.

As the number, size, and diversity of divisions in an organization increase, controlling and evaluating divisional operations become increasingly difficult for strategists. Increases in sales often are not accompanied by similar increases in profitability. The span of control becomes too large at top levels of the firm. For example, in a large conglomerate organization composed of 90 divisions, the chief executive officer could have difficulty even remembering the first names of divisional presidents. In multidivisional organizations an SBU structure can greatly facilitate strategy-implementation efforts.

The *SBU structure* group's similar divisions into strategic business units and delegate's authority and responsibility for each unit to a senior executive who reports directly to the chief executive officer. This change in structure can facilitate strategy implementation by improving coordination between similar divisions and channeling accountability to distinct business units. In the ninety-division conglomerate just mentioned, the ninety divisions could perhaps be regrouped into ten SBUs according to certain common characteristics such as competing in the same industry, being located in the same area, or having the same customers.

Two disadvantages of an SBU structure are that it requires an additional layer of management, which increases salary expenses, and the role of the group vice president is often ambiguous. However, these limitations often do not outweigh the advantages of improved coordination and accountability.

iv. The Matrix Structure

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

matrix structure can result in higher overhead because it creates more management positions. Other characteristics of a matrix structure that contribute to overall complexity include dual lines of budget authority (a violation of the unity-of-command principle), dual sources of reward and punishment, shared authority, dual reporting channels, and a need for an extensive and effective communication system.

Despite its complexity, the matrix structure is widely used in many industries, including construction, healthcare, research, and defense. Some advantages of a matrix structure are that project objectives are clear, there are many channels of communication, workers can see visible results of their work, and shutting down a project can be accomplished relatively easily.

Activity 6.3

Try to differentiate restructuring and reengineering

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6.2.5 Restructuring and Reengineering

Restructuring and reengineering are becoming commonplace on the corporate landscape across the United States and Europe. Restructuring—also called downsizing, rightsizing, or delay ring—involves reducing the size of the firm in terms of number of employees, number of divisions or units, and number of hierarchical levels in the firm's organizational structure. This reduction in size is intended to improve both efficiency and effectiveness. Restructuring is concerned primarily with shareholder well-being rather than employee well-being.

In contrast, reengineering is concerned more with employee and customer well-being than shareholder well-being. Reengineering—also called process management, process innovation, or process redesign— involves reconfiguring or redesigning work, jobs, and processes for the purpose of improving cost, quality, service, and speed. Reengineering does not usually affect the organizational structure or chart, nor does it imply job loss or employee layoffs. Whereas restructuring is concerned with eliminating or establishing, shrinking or enlarging, and moving

organizational departments and divisions, the focus of reengineering is changing the way work is actually carried out.

Reengineering is characterized by many tactical (short-term, business function-specific) decisions, whereas restructuring is characterized by strategic (long-term, affecting all business functions) decisions.

6.2.6 Managing Resistance to Change

No organization or individual can escape change. But the thought of change raises anxieties because people fear economic loss, inconvenience, uncertainty, and a break in normal social patterns. Almost any change in structure, technology, people, or strategies has the potential to disrupt comfortable interaction patterns. For this reason, people resist change. The strategic-management process itself can impose major changes on individuals and processes. Reorienting an organization to get people to think and act strategically is not an easy task.

Resistance to change can be considered the single greatest threat to successful strategy implementation. Resistance in the form of sabotaging production machines, absenteeism, filing unfounded grievances, and an unwillingness to cooperate regularly occurs in organizations. People often resist strategy implementation because they do not understand what is happening or why changes are taking place. In that case, employees may simply need accurate information. Successful strategy implementation hinges upon managers' ability to develop an organizational climate conducive to change. Change must be viewed as an opportunity rather than as a threat by managers and employees.

Resistance to change can emerge at any stage or level of the strategy-implementation process. Although there are various approaches for implementing changes, three commonly used strategies are a force change strategy, an educative change strategy, and a rational or self-interest change strategy. A *force change strategy* involves giving orders and enforcing those orders; this strategy has the advantage of being fast, but it is plagued by low commitment and high resistance. The *educative change strategy* is one that presents information to convince people of the need for change; the disadvantage of an educative change strategy is that implementation becomes slow and difficult. However, this type of strategy evokes greater commitment and less resistance than does the force strategy. Finally, a *rational* or *self-interest change strategy* is one that attempts to convince individuals that the change is to their personal advantage. When this appeal is successful,

strategy implementation can be relatively easy. However, implementation changes are seldom to everyone's advantage.

Activity 6.4

What are the importance of managing the natural environment?

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6.2.7 Managing the Natural Environment

The natural environment comprises all living and non-living things that occur naturally on Earth. In its purest sense, it is thus an environment that is not the result of human activity or intervention. The natural environment may be contrasted to "the built environment." All business functions are affected by natural environment considerations or striving to make a profit.

However, both employees and consumers are especially resentful of firms that take from more than they give to the natural environment; likewise, people today are especially appreciative of firms that conduct operations in a way that mends rather than harms the environment.

The ecological challenge facing all organizations requires managers to formulate strategies that preserve and conserve natural resources and control pollution. Special natural environmental issues include ozone depletion, global warming, depletion of rain forests, destruction of animal habitats, protecting endangered species, developing biodegradable products and packages, waste management, clean air, clean water, erosion, destruction of natural resources, and pollution control. Firms increasingly are developing green product lines that are biodegradable and/or are made from recycled products. Green products sell well.

Managing as if the earth matters require an understanding of how international trade, competitiveness, and global resources are connected. Managing environmental affairs can no longer be simply a technical function performed by specialists in a firm; more emphasis must be placed on developing an environmental perspective among all employees and managers of the firm. Many companies are moving environmental affairs from the staff side of the organization to

the line side, to make the corporate environmental group report directly to the chief operating officer.

Societies have been plagued by environmental disasters to such an extent recently that firms failing to recognize the importance of environmental issues and challenges could suffer severe consequences. Managing environmental affairs can no longer be an incidental or secondary function of company operations. Product design, manufacturing, and ultimate disposal should not merely reflect environmental considerations, but be driven by them. Firms that manage environmental affairs will enhance relations with consumers, regulators, vendors, and other industry players—substantially improving their prospects of success.

Firms should formulate and implement strategies from an environmental perspective. Environmental strategies could include developing or acquiring green businesses, divesting or altering environment damaging businesses, striving to become a low-cost producer through waste minimization and energy conservation, and pursuing a differentiation strategy through green product features. In addition to creating strategies, firms could include an environmental representative on the board of directors, conduct regular environmental audits, implement bonuses for favorable environmental results, become involved in environmental issues and programs, incorporate environmental values in mission statements, establish environmentally oriented objectives, acquire environmental skills, and provide environmental training programs for company employees and managers.

6.2.8 Production/Operations Concerns When Implementing Strategies

Strategy in action means implementation requires complete transparent process. Production/operations department that mainly concern with the achievement of organization goals and targets. Production processes typically constitute more than 70 percent of a firm's total assets. Production department plays a crucial role for implementing organization strategy. Production-concerned decisions on plant location, plant size, product design, choice of equipment, size of inventory, inventory control, quality control, cost control, use of standards, shipping and packaging, and technological innovation, job specialization, employee training, equipment and resource utilization. All these factors place an important impact on success and failure of the strategy.

The following examples of adjustments in production systems that could be required to implement various strategies are provided in Table for both for-profit and nonprofit organizations. For instance, note that when a bank formulates and selects a strategy to add ten new branches, a production-related implementation concern is site location.

Strategy Implementation and Production and Service Management		
Type of Organization	**Strategy Being Implemented**	**System Adjustments Production**
Hospital	Adding a TB center (Product Development)	Purchase specialized equipment and add specialized people.
Bank	Opening ten new branches (Market Development)	Perform site location analysis.

Activity 6.5

Discuss the importance of human resource to strategy implementation.

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6.2.9 Human Resource Concerns When Implementing Strategies

The other important concern while implementing the strategy is human resource. Human resource is the backbone of any organization without efficient human resource organization cannot perform well and fail to achieve the organizational strategy. Staffing need of the organization and its cost is an important function of the human resource manager. The other main concerns include health,

safety and security of the workers. The plan must also include how to motivate employees and managers during a time when layoffs are common and workloads are high. The human resource department must develop **performance incentives** that clearly link performance and pay to strategies. The process of empowering managers and employees through involvement in strategic management activities yields the greatest benefits when all organizational members understand clearly how they will benefit personally if the firm does well. Linking company and personal benefits is a major new strategic responsibility of human resource managers. Other new responsibilities for human resource managers may include establishing and administering an *employee stock ownership plan (ESOP),* are corporations owned in whole or in part by their employees.

A well-designed strategic-management system can fail:

If insufficient attention is given to the human resource dimension. Human resource problems that arise when businesses implement strategies can usually be traced to one of three causes:

(1) Disruption of social and political structures, (2) Failure to match individuals' aptitudes with implementation tasks (3) Inadequate top management support for implementation activities.

Inadequate support from strategists for implementation activities often undermines organizational success. Chief executive officers, small business owners, and government agency heads must be personally committed to strategy implementation and express this commitment in highly visible ways. Strategists' formal statements about the importance of strategic management must be consistent with actual support and rewards given for activities completed and objectives reached. Otherwise, stress created by inconsistency can cause uncertainty among managers and employees at all levels. Perhaps the best method for preventing and overcoming human resource problems in strategic management is to actively involve as many managers and employees as possible in the process. Although time-consuming, this approach builds understanding, trust, commitment, and ownership and reduces resentment and hostility. The true potential of strategy formulation and implementation resides in people.

6.3 Summary

Successful strategy formulation does not at all guarantee successful strategy implementation. Although inextricably interdependent, strategy formulation and strategy implementation are characteristically different. In a single word, strategy implementation means change. It is widely agreed that “the real work begins after strategies are formulated.” Successful strategy

implementation requires the support of, as well as discipline and hard work from, motivated managers and employees. It is sometimes frightening to think that a single individual can irreparably sabotage strategy-implementation efforts.

Formulating the right strategies is not enough, because managers and employees must be motivated to implement those strategies. Management issues considered central to strategy implementation include matching organizational structure with strategy, linking performance and pay to strategies, creating an organizational climate conducive to change, managing political relationships, creating a strategy-supportive culture, adapting production/ operations processes, and managing human resources. Establishing annual objectives, devising policies, and allocating resources are central strategy-implementation activities common to all organizations. Depending on the size and type of the organization, other management issues could be equally important to successful strategy implementation.

Review Questions

1. Annual objectives are essential for strategy implementation because they:
   A. Represent the basis for allocating resources
   B. Are a primary mechanism for evaluating managers?
   C. Are the major instrument for monitoring progress toward achieving long-term objectives?
   D. Establish organizational, divisional, and departmental priorities.
   E. All of the above
   F. None of the above
2. Budget (Resource Allocation) is a plan for using available resources and the plan has two parts. Which one of the following part shows the choice of which items to fund in the plan, and what level of funding it should receive, and which to leave unfunded?
   A. Basic allocation decision
   B. Contingency mechanisms
   C. Policy
   D. A and B
   E. All of the above
   F. None of the above
3. **_____** Type of organizational structure has its own business strategy, objectives and competitors and these will often be different from those of the parent company.
   A. The Strategic Business Unit Structure
   B. Functional Structure
   C. Divisional Structure
   D. The Matrix Structure
   E. All of the above
   F. None of the above
4. One of the following is **false** about restructuring and reengineering?
   A. Restructuring is concerned primarily with shareholder well-being rather than employee well-being.

B. Reengineering involves reconfiguring or redesigning work, for the purpose of improving cost, quality, service, and speed
C. Reengineering usually affect the organizational structure and it imply job loss or employee layoffs.
D. Reengineering is concerned more with employee and customer well-being than shareholder well-being.
E. All of the above
F. None of the above

5. From the approaches for implementing change, the one present's information to convince people of the need for change is…….
   A. A force change strategy
   B. The educative change strategy
   C. Self-interest change strategy
   D. B and C
   E. None of the above

6 Which one of the following concerns links company and personal benefits when implementing their strategies?
   A. Human resource concern
   B. Production concern
   C. Marketing concern
   D. Finance concern
   E. All of the above

CHAPTER SEVEN: STRATEGY EVALUATION AND CONTROL

Aims of the Chapter

The aim of this chapter is to show the mechanisms of strategy evaluation and control. You will understand the criteria for evaluating strategies like consistency, consonance, feasibility, and others. It also presents the characteristics of an effective evaluation system.

At the end of this chapter, you will be expected to:

- Identify the Rumelt's criteria for evaluating strategies
- Examine the characteristics of an effective evaluation system
- Discuss strategy-evaluation framework
- List the four basic types of strategic controls.

7.1 Introduction

Strategy evaluation can be a complex and sensitive undertaking. Too much emphasis on evaluating strategies may be expensive and counterproductive. Strategies often do not affect short-term operating results until it is too late to make needed changes. It is impossible to demonstrate conclusively that a particular strategy is optimal or even to guarantee that it will work. One can, however, evaluate it for critical flaws.

An important strategy-evaluation activity is measuring organizational performanc*e*. This activity includes comparing expected results to actual results, investigating deviations from plans, evaluating individual performance, and examining progress being made toward meeting stated objectives. Both long-term and annual objectives are commonly used in this process. Criteria for evaluating strategies should be measurable and easily verifiable. Criteria that predict results may be more important than those that reveal what already has happened.

Strategic controls are necessary to steer the firm through these events. They must provide the basis for correcting the actions and directions of the firm in implementing its strategy as developments and changes in its environmental and internal situations take place.

7.2 THE NATURE OF STRATEGY EVALUATION

The strategic-management process results in decisions that can have significant, long-lasting consequences. Erroneous strategic decisions can inflict severe penalties and can be exceedingly difficult, if not impossible, to reverse. Most strategists agree, therefore, that strategy evaluation is vital to an organization's well-being; timely evaluations can alert management to problems or potential problems before a situation becomes critical.

Strategy evaluation includes three basic activities: (1) examining the underlying bases of a firm's strategy, (2) comparing expected results with actual results, and (3) taking corrective actions to ensure that performance conforms to plans. Adequate and timely feedback is the cornerstone of effective strategy evaluation.

Strategy evaluation can be no better than the information on which it is based. Too much pressure from top managers may result in lower managers contriving numbers they think will be satisfactory.

Strategy evaluation can be a complex and sensitive undertaking. Too much emphasis on evaluating strategies may be expensive and counterproductive.

Strategy evaluation is essential to ensure that stated objectives are being achieved. In many organizations, strategy evaluation is simply an appraisal of how well an organization has performed. Have the firm's assets increased? Has there been an increase in profitability? Have sales increased? Have productivity levels increased? Have profit margin, return on investment, and earnings-per-share ratios increased? Some firms argue that their strategy must have been correct if the answers to these types of questions are affirmative. Well, the strategy or strategies may have been correct, but this type of reasoning can be misleading because strategy evaluation must have both a long-run and short-run focus. Strategies often do not affect short-term operating results until it is too late to make needed changes. It is impossible to demonstrate conclusively that a particular strategy is optimal or even to guarantee that it will work. One can, however, evaluate it for critical flaws.

Richard Rumelt offered four criteria that could be used to evaluate a strategy: consistency, consonance, feasibility, and advantage. *Consonance* and *advantage* are mostly based on a firm's

external assessment, whereas *consistency* and *feasibility* are largely based on an internal assessment. Strategy evaluation is important because organizations face dynamic environments in which key external and internal factors often change quickly and dramatically. Success today is no guarantee of success tomorrow! An organization should never be lulled into complacency with success.

Activity 7.1

1. Discuss the nature of strategy evaluation

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Rumelt's Criteria for Evaluating Strategies

1. Consistency

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

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

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

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

2. Consonance

Consonance refers to the need for strategists to examine *sets of trends*, as well as individual trends, in evaluating strategies. A strategy must represent an adaptive response to the external environment and to the critical changes occurring within it. One difficulty in matching a firm's key internal and external factors in the formulation of strategy is that most trends are the result of interactions among other trends. For example, the day-care explosion came about as a combined

result of many trends that included a rise in the average level of education, increased inflation, and an increase in women in the workforce. Although single economic or demographic trends might appear steady for many years, there are waves of change going on at the interaction level.

3. Feasibility

A strategy must neither overtax available resources nor create unsolvable sub problems. The final broad test of strategy is its feasibility; that is, can the strategy be attempted within the physical, human, and financial resources of the enterprise? The financial resources of a business are the easiest to quantify and are normally the first limitation against which strategy is evaluated. In evaluating a strategy, it is important to examine whether an organization has demonstrated in the past that it possesses the abilities, competencies, skills, and talents needed to carry out a given strategy.

4. Advantage

A strategy must provide for the creation and/or maintenance of a competitive advantage in a selected area of activity. Competitive advantages normally are the result of superiority in one of three areas: (1) resources, (2) skills, or (3) position.

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

Why strategy evaluation is more difficult today? The reasons are

1. A dramatic increase in the environment's complexity
2. The increasing difficulty of predicting the future with accuracy
3. The increasing number of variables
4. The rapid rate of obsolescence of even the best plans
5. The increase in the number of both domestic and world events affecting organizations

6. The decreasing time span for which planning can be done with any degree of certainty

Activity 7.2

1. Discuss on how strategy evaluation frame work helps strategists to conduct strategy evaluation.

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7.3 A Strategy-Evaluation Framework

Corrective actions are almost always needed except when (1) external and internal factors have not significantly changed and (2) the firm is progressing satisfactorily toward achieving stated objectives.

Reviewing Bases of Strategy

Reviewing the underlying bases of an organization's strategy could be approached by developing a revised EFE Matrix and IFE Matrix. A *revised IFE Matrix* should focus on changes in the organization's management, marketing, finance/accounting, production/operations, R&D, and management information systems strengths and weaknesses.

A *revised EFE Matrix* should indicate how effective a firm's strategies have been in response to key opportunities and threats.

TABLE 7.1 A Strategy-Evaluation Assessment Matrix

Have Major Changes Occurred in the Firm Internal Strategic Position?	Have Major Changes Occurred in the Firm External Strategic Position?	Has the Firm Progressed Satisfactorily Toward Achieving Its Stated Objectives?	Result
No	No	No	Take corrective actions
Yes	Yes	Yes	Take corrective actions
Yes	Yes	No	Take corrective actions
Yes	No	Yes	Take corrective actions
Yes	No	No	Take corrective actions
No	Yes	Yes	Take corrective actions
No	Yes	No	Take corrective actions
No	No	Yes	Continue present strategic Course

This analysis could also address such questions as the following:

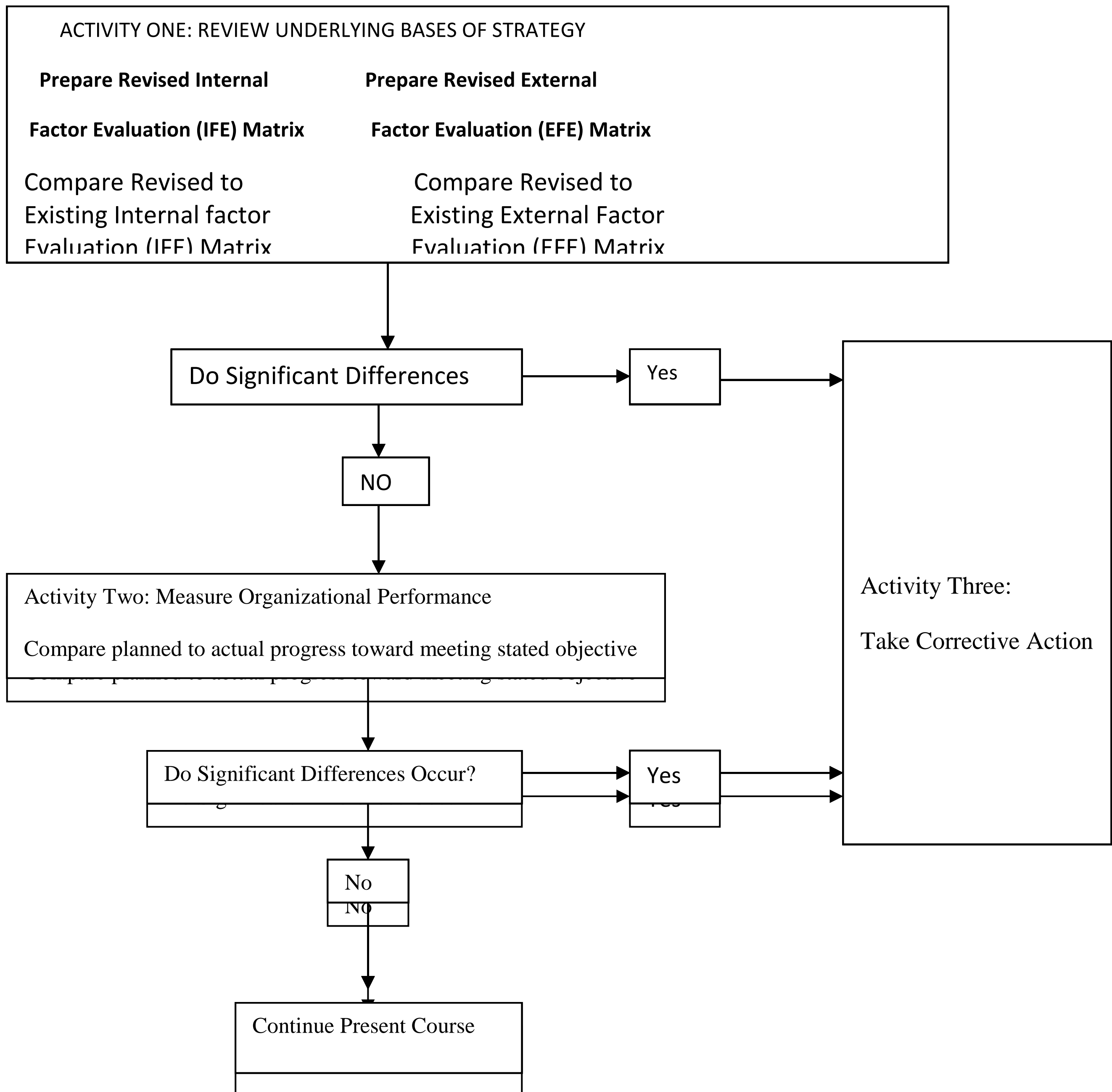
1. How have competitors reacted to our strategies?
2. How have competitors' strategies changed?
3. Have major competitors' strengths and weaknesses changed?
4. Why are competitors making certain strategic changes?
5. Why are some competitors' strategies more successful than others?
6. How satisfied are our competitors with their present market positions and profitability?
7. How far can our major competitors be pushed before retaliating?
8. How could we more effectively cooperate with our competitors?

External opportunities and threats and internal strengths and weaknesses that represent the bases of current strategies should continually be monitored for change. It is not really a question of whether these factors will change but rather when they will change and in what ways.

Here are some key questions to address in evaluating strategies:

1. Are our internal strengths still strengths?
2. Have we added other internal strengths? If so, what are they?
3. Are our internal weaknesses still weaknesses?
4. Do we now have other internal weaknesses? If so, what are they?
5. Are our external opportunities still opportunities?
6. Are there now other external opportunities? If so, what are they?
7. Are our external threats still threats?
8. Are there now other external threats? If so, what are they?
9. Are we vulnerable to a hostile takeover?

Fig 7.1 **A Strategy-Evaluation Framework**



Activity 7.3

1. Discuss strategy Evaluation process

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Measuring Organizational Performance

Another important strategy-evaluation activity is *measuring organizational performance.* This activity includes comparing expected results to actual results, investigating deviations from plans, evaluating individual performance, and examining progress being made toward meeting stated objectives. Both long-term and annual objectives are commonly used in this process. Criteria for evaluating strategies should be measurable and easily verifiable. Criteria that predict results may be more important than those that reveal what already has happened.

Failure to make satisfactory progress toward accomplishing long-term or annual objectives signals a need for corrective actions. Many factors, such as unreasonable policies, unexpected turns in the economy, unreliable suppliers or distributors, or ineffective strategies, can result in unsatisfactory progress toward meeting objectives. Problems can result from ineffectiveness (not doing the right things) or inefficiency (poorly doing the right things).

Determining which objectives are most important in the evaluation of strategies can be difficult. Strategy evaluation is based on both quantitative and qualitative criteria.

Selecting the exact set of criteria for evaluating strategies depends on a particular organization's size, industry, strategies, and management philosophy. An organization pursuing a retrenchment strategy, for example, could have an entirely different set of evaluative criteria from an organization pursuing a market-development strategy. Quantitative criteria commonly used to evaluate strategies are financial ratios, which strategists use to make three critical comparisons:

(1) Comparing the firm's performance over different time periods,

(2) Comparing the firm's performance to competitors', and

(3) Comparing the firm's performance to industry averages.

Some key financial ratios that are particularly useful as criteria for strategy evaluation are as follows:

1.Return on investment (ROI)

2. Return on equity (ROE)

3. Profit margin

4. Market share

5. Debt to equity

6. Earnings per share

7. Sales growth

8. Asset growth

But some potential problems are associated with using quantitative criteria for evaluating strategies. First, most quantitative criteria are geared to annual objectives rather than long-term objectives. Also, different accounting methods can provide different results on many quantitative criteria. Human factors such as high absenteeism and turnover rates, poor production quality and quantity rates, or low employee satisfaction can be underlying causes of declining performance. Marketing, finance/accounting, R&D, or management information systems factors can also cause financial problems.

Taking Corrective Actions

The final strategy-evaluation activity, *taking corrective actions,* requires making changes to competitively reposition a firm for the future.

Corrective Actions Possibly Needed to Correct Unfavorable Variances

1 Alter the firm's structure

2 Replace one or more key individuals

3 Divest a division

4 Alter the firm's vision and/or mission

5 Revise objectives

6 Alter strategies

7 Devise new policies

8 Install new performance incentives

9 Raise capital with stock or debt

10 Add or terminate salespersons, employees, or managers

11 Allocate resources differently

12 Outsource (or rein in) business functions

7.4 Characteristics of an Effective Evaluation System

Strategy evaluation must meet several basic requirements to be effective. First, strategy evaluation activities must be economical; too much information can be just as bad as too little information; and too many controls can do more harm than good. Strategy-evaluation activities also should be meaningful; they should specifically relate to a firm's objectives.

They should provide managers with useful information about tasks over which they have control and influence. Strategy-evaluation activities should provide timely information; on occasion and in some areas, managers may daily need information.

Frequent measurement and rapid reporting may frustrate control rather than give better control. The time dimension of control must coincide with the time span of the event being measured. Strategy evaluation should be designed to provide a true picture of what is happening.

Contingency Planning

A basic premise of good strategic management is that firms plan ways to deal with unfavorable and favorable events before they occur. Too many organizations prepare contingency plans just for unfavorable events; this is a mistake, because both minimizing threats and capitalizing on opportunities can improve a firm's competitive position.

Regardless of how carefully strategies are formulated, implemented, and evaluated, unforeseen events, such as strikes, boycotts, natural disasters, arrival of foreign competitors, and government actions, can make a strategy obsolete. To minimize the impact of potential threats, organizations should develop contingency plans as part of their strategy-evaluation process. *Contingency plans* can be defined as alternative plans that can be put into effect if certain key events do not occur as expected. Only high-priority areas require the insurance of contingency plans. Strategists cannot and should not try to cover all bases by planning for all possible contingencies. But in any case, contingency plans should be as simple as possible.

Some contingency plans commonly established by firms include the following:

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

Strategic Planning gave users three major benefits:

(1) It permitted quick response to change,

(2) It prevented panic in crisis situations, and

(3) It made managers more adaptable by encouraging them to appreciate just how variable the future can be.

They suggested that effective contingency planning involves a seven-step process:

1. Identify both beneficial and unfavorable events that could possibly derail the strategy or strategies.
2. Specify trigger points. Calculate about when contingent events are likely to occur.
3. Assess the impact of each contingent event. Estimate the potential benefit or harm of each contingent event.
4. Develop contingency plans. Be sure that contingency plans are compatible with current strategy and are economically feasible.
5. Assess the counter impact of each contingency plan. That is, estimate how much each contingency plan will capitalize on or cancel out its associated contingent event. Doing this will quantify the potential value of each contingency plan.
6. Determine early warning signals for key contingent events. Monitor the early warning signals.
7. For contingent events with reliable early warning signals, develop advance action plans to take advantage of the available lead time.

Activity 7.4

1. Discuss strategy evaluation types

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7.5 Strategic Control

Control of strategy can be characterized as a form of .steering control.. Ordinarily, a significant time span occurs between initial implementation of a strategy and achievements of its intended results. During that time, numerous projects are undertaken, investments are made, and actions are undertaken to implement the new strategy. Also during that time, both the environmental situation and the firm's internal situation are developing and evolving. Strategic controls are necessary to steer the firm through these events. They must provide the basis for correcting the actions and

directions of the firm in implementing its strategy as developments and changes in its environmental and internal situations take place.

The four basic types of strategic controls are:

A. Premise control
B. Implementation control
C. Strategic surveillance
D. Special alert control.

A. Premise Control

Every strategy is based on assumed or predicted conditions. These assumptions or predictions are planning premises; a firms strategy is designed around these predicted conditions. Premise control is designed to check systematically and continuously whether or not the premises set during the planning and implementation process are still valid. If a vital premise is no longer valid, then the strategy may have to be changed. The sooner an invalid premise can be recognized and revised, the better the chances that an acceptable shift in the strategy can be devised.

B. Implementation Control

The action phase of strategic management is located in the series of steps, programs, investments, and moves undertaken over a period of time to implement the strategy. Special programs are undertaken. Functional areas initiate several strategy-related activities. Key people are added or reassigned. Resources are mobilized. In other words, managers convert broad strategic plans into concrete actions and results for specific units and individuals as they go about implementing strategy. And these actions take place incrementally over an extended period of time designed ultimately to enact the planned strategy and achieve long-term objectives.

Strategic control can be undertaken within this context. We refer to this type of strategic control as implementation control. Implementation control is designed to assess whether the overall strategy should be changed in light of unfolding events and results associated with incremental steps and actions that implement the overall strategy.

C. 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 or the firm's strategy. The basic idea behind strategic surveillance is that some form of general monitoring of multiple information sources should be encouraged, with the specific intent being the opportunity to uncover important yet unanticipated information.

D. Special Alert Control

Another type of strategic control, really a subset of the other three, is special alert control. A special alert control is the need to thoroughly, and often rapidly, reconsider the firms' basic strategy based on a sudden, unexpected event.

7.6 Summary

This chapter presents a strategy-evaluation framework that can facilitate accomplishment of annual and long-term objectives. Effective strategy evaluation allows an organization to capitalize on internal strengths as they develop, to exploit external opportunities as they emerge, to recognize and defend against threats, and to mitigate internal weaknesses before they become detrimental.

Strategists in successful organizations take the time to formulate, implement, and then evaluate strategies deliberately and systematically. Good strategists move their organization forward with purpose and direction, continually evaluating and improving the firm's external and internal strategic positions.

Strategy evaluation allows an organization to shape its own future rather than allowing it to be constantly shaped by remote forces that have little or no vested interest in the well-being of the enterprise. Although not a guarantee for success, strategic management allows organizations to make effective long-term decisions, to execute those decisions efficiently, and to take corrective actions as needed to ensure success.

A key to effective strategy evaluation and to successful strategic management is an integration of intuition and analysis: A potentially fatal problem is the tendency for analytical and intuitive issues to polarize. This polarization leads to strategy evaluation that is dominated by either analysis or intuition, or to strategy evaluation that is discontinuous, with a lack of coordination among analytical and intuitive issues. Strategists in successful organizations realize that strategic management is first and foremost a people process. It is an excellent vehicle for fostering organizational communication. People are what make the difference in organizations.

Chapter review questions

Discuss the following questions

2. Give an example of "consonance" other than the one provided by Rumelt in the chapter.

3. How often should an organization's vision/mission be changed in light of strategy evaluation activities?
4. Why has strategy evaluation become so important in business today?
5. Under what conditions are corrective actions not required in the strategy-evaluation process?
6. Identify types of organizations that may need to evaluate strategy more frequently than others. Justify your choices.
7. Identify some key financial ratios that would be important in evaluating a bank's strategy.
8. Strategy evaluation allows an organization to take a proactive stance toward shaping its own future. Discuss the meaning of this statement.
9. Explain and discuss the Balanced Scorecard.
10. Why is the Balanced Scorecard an important topic both in devising objectives and in evaluating strategies?

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Debre Markos University

Department of management

Strategic management assignment (30%)

Notice

1. ***Your hand writing must be readable.***
2. ***Computer typed work has no value.***
3. ***It must be original work (not copied from any source).***

Good luck!

1. The following are possible external opportunities/threats and internal strengths/weaknesses for the McDonald's company. Develop, SO, ST, TW, WO strategies for McDonald.

   Strengths:

S1: Highly successful and recognized advertising.

S2: Strong employee training and promotion mostly from within.

S3: Strong Investor Reputation.

S4: Strongest Brand Image as the number-1 fast-food company by sales, with more than 32,000 restaurants in 118 countries.

S5: Recognized as a community oriented, socially responsible company.

S6: Strong Global Presence and an ability to weather local economic fluctuations.

S7: Use pure ingredients and take food safety very seriously.

S8: Consistently solid financial performance.

- Gross margins (36.7%) and net profit margins (18.2%) above industry averages.
- Sales revenue up 3.3% in 2008, global comparable sales up 6.9%.
- Net income up 80% in 2008.

S9: Strong innovation and product development.

S10: Large real estate portfolio.

S11: Economies of Scale – Nearest competitor in U.S. is half McDonald's size.

Weaknesses:

W1: Lowest Customer satisfaction rating in the industry (69), even below IRS.

W2: High employee turnover.

W3: Assembly line approach makes it difficult and costly to adapt to changing trends.

W4: Core product line out of sync with trends toward healthier lifestyles for adults and children.

W5: Sales demonstrates seasonal effects.

W6: 80% of restaurants are franchise owned, placing image and reputation in other's hands.

W7: Over-saturation of real estate in the US.

W8: Struggles with fluctuations in operating and net profits:

- Operating profits $4,433M (2006), $3,879M (2007), $6443M (2008).
- Net profits $3,544M (2006), $2,395M (2007), $4,313M (2008).

W9: 70% of operating revenues and 45% of debt are in foreign currency.

Opportunities:

O1: Anticipated 4% growth rate in Quick Service Restaurant industry.

O2: Low fat, low calorie, healthy hamburger – Could be first on market.

O3: Many restaurants (60% in U.S.) have outdated appearance. Remodeling can yield cozier, upscale setting, and upgrade the image.

O4: Respond to social changes by innovation within healthier lifestyle foods.

O5: Increased beverage options (Gourmet coffees) have been shown to increase customer visits in Europe (+7.2%) and takes advantage of faltering Starbuck's.

O6: Breakfast not available at 25% of locations – can increase return on assets and equity.

O7: Joint ventures with retailers (Walmart, etc.) can place new locations in high traffic areas at lower capital cost.

O8: Continued focus on corporate social responsibility, reducing the impact on the environment and community linkages.

O9: International expansion into emerging markets of China, India, Brazil.

O10: Diversify portfolio (i.e., similar to what it did before divesting Chipotle, Boston Market).

Threats:

T1: More health conscious customers.

T2: Particularly vulnerable in older, established markets (US, EU) to upstarts offering healthier food offerings and more modern, high tech surroundings.

T3: Global economic recession causing consumers to spend less (Global GDP Est.-2.3%).

T4: Markets in US and EU are mature and saturated, but 70% of locations.

T5: Subway and YUM! Brands expanding into developing markets at a higher rate.

T6: Litigation:

T7: Brand equity at risk: 80% of restaurants owned by franchisees.

T8: Contamination of the food supply, especially e-coli, or Mad cow disease, could damage sales, reputation, etc.

T9: Intense price pressure from competitors like Burger King, Taco Bell, Wendy's, KFC and any mid-range sit-down restaurants.

T10: Negative public opinion campaigns:

2. Your university (take any company found in your vicinity) faces numerous external opportunities/threats and has many internal Strengths/weaknesses. Developing an EFE and IFE matrix for the company.
3. This exercise is designed to give students practical knowledge about how organizations in their communities are conducting strategic planning. The exercise also gives students experience interacting on a professional basis with local business leaders.

   INSTRUCTIONS:

   - Seek answers for the following questions during the interview:
     a. How does your firm formally conduct strategic planning? Who is involved in the process? How often and where?
     b. Does your firm have a written mission statement? How was the statement developed? When the statement was last changed?
     c. What are the benefits of engaging in strategic planning?
     d. What are the major costs or problems in doing strategic planning in your business?
     e. Do you anticipate making any changes in the strategic planning process at your company? If yes, please explain.
4. Write a vision statement and mission statement for your university **(any company).** Your mission statement should include the nine characteristics