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STRATEGIC MANAGEMENT

(Common to all MBA Programs)

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Strategic Management

Objectives

- Integrating the knowledge gained in functional areas of management
- Helping the students to learn about the process of strategic management, and
- Helping the students to learn about strategy formulation and implementation

Unit-I

Concepts of Strategy - Levels at which strategy operates; Approaches to strategic decision making; Mission and purpose, objectives and goals; Strategic business unit (SBD); Functional level strategies

Unit-II

Environmental Analysis and Diagnosis - Environment and its components; Environment scanning and appraisal; Organizational appraisal; Strategic advantage analysis and diagnosis; SWOT analysis

Unit-III

Strategy Formulation and Choice - Modernization, Diversification Integration - Merger, take-over and joint strategies - Turnaround, Divestment and Liquidation strategies - Strategic choice - Industry, competitor and SWOT analysis - Factors affecting strategic choice; Generic competitive strategies - Cost leadership, Differentiation, Focus, Value chain analysis, Bench marking, Service blue printing

Unit-Iv

Functional Strategies: Marketing, production/operations and R&D plans and polices- Personnel and financial plans and policies.

Unit-V

Strategy Implementation - Inter - relationship between formulation and implementation - Issues in strategy implementation - Resource allocation - Strategy and Structure - Structural considerations - Organizational Design and change - Strategy Evaluation- Overview of strategic evaluation; strategic control; Techniques of strategic evaluation and control.

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UNIT- I

Lesson 1 - Concept Of Corporate Strategy

Lesson Outline

- Introduction
- What Is Strategy?
- Why Corporate Strategy?
- Levels Of Strategy
- Crafting A Strategy
- An Ongoing Process
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Define and understand the concept of corporate strategy
- Identify the different levels of corporate strategy
- Examine the reasons for developing strategies
- See corporate strategy as an on going process

Organizations are facing exciting and dynamic challenges in the 21st century. In the gloabalized business, companies require strategic thinking and only by evolving good corporate strategies can they become strategically competitive. A sustained or sustainable competitive advantage occurs when firm implements a value – creating strategy of which other companies are unable to duplicate the benefits or find it too costly to initiate. Corporate strategy includes the commitments, decisions and actions required for a firm to achieve strategic competitiveness and earn above average returns. The goals of corporate strategy are challenging not only for large firms like Microsoft but also for small local computer retail outlets or even dry cleaners. Table 1.1 lists the top ten strategists in India in 2005.

TABLE 1.1 - INDIA'S TOP TEN STRATEGISTS

Name of the company	Position in the industry
Infosys Technologies	1
Reliance Industries	2
Wipro	3
Hindustan Lever	4
Maruti Udyog	5
Dr. Reddy's Laboratories	6
HDFC Bank	7
Jet Airways	8
ICICI Bank	9
Ranbaxy Laboratories	10

Source - Internet

What is strategy?

Strategy", narrowly defined, means "the art of the general" (the Greek stratos, meaning 'field, spread out as in 'structure'; and agos, meaning 'leader'). The term first gained currency at the end of the 18th century, and had to do with stratagems by which a general sought to deceive an enemy, with plans the general made for a campaign, and with the way the general moved and disposed his forces in war. Also was the first to focus on the fact that strategy of war was a means to enforce policy and not an end in itself. Strategy is a set of key decisions made to meet objectives. A strategy of a business organization is a comprehensive master plan stating how the organization will achieve its mission and objectives.

> I keep six honest serving men.
> They taught me all I know. Their names are What, Why, When, How, Where and Who.
>
> - **Rudyard Kipling**

Here are some definitions of strategy.

> Chandler(1962)Strategy is the determinator of the basic long-term goals of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out these goals.
>
> Mintzberg (1979) Strategy is a mediating force between the organization and its environment: consistent patterns in streams of organizational decisions to deal with the environment.
>
> Prahlad (1993) Strategy is more then just fit and allocation of resources. It is stretch and leveraging of resources.
>
> Porter (1996) Strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value .

Mintzberg has identified the 5 P's of strategy. Strategy could be a plan, a pattern, a position, a ploy, or a perspective.

1. A plan, a "how do I get there"
2. A pattern, in consistent actions over time
3. A position that is, it reflects the decision of the firm to offer particular products or services in particular markets.
4. A ploy, a maneuver intended to outwit a competitor
5. A perspective that is, a vision and direction, a view of what the company or organization is to become.

Why Corporate Strategy?

Strategic management is basically needed for every organization and it offers several benefits.

1.Universal

Strategy refers to a complex web of thoughts, ideas, insights, experiences, goals, expertise, memories, perceptions, and expectations that

provides general guidance for specific actions in pursuit of particular ends. Nations have, in the management of their national policies, found it necessary to evolve strategies that adjust and correlate political, economic, technological, and psychological factors, along with military elements. Be it management of national polices, international relations, or even of a game on the playfield, it provides us with the preferred path that we should take for the journey that we actually make.

2. Keeping Pace With Changing Environment

The present day environment is so dynamic and fast changing thus making it very difficult for any modern business enterprise to operate. Because of uncertainties, threats and constraints, the business corporations are under great pressure and are trying to find out the ways and means for their healthy survival. Under such circumstances, the only last resort is to make the best use of strategic management which can help the corporate management to explore the possible opportunities and at the same time to achieve an optimum level of efficiency by minimizing the expected threats.

3. Minimizes Competitive Disadvantage

It minimizes competitive disadvantage and adds up to competitive advantage. For example, a company like Hindustan Lever Ltd., realized that merely by merging with companies like Lakme, Milk food, Ponds, Brooke bond, Lipton etc which make fast moving consumer goods alone will not make it market leader but venturing into retailing will help it reap heavy profits. Then emerged its retail giant "Margin Free' which is the market leader in states like Kerala. Similarly, the R.P. Goenka Group and the Muruguppa group realized that mere takeovers do not help and there is a need to reposition their products and reengineer their brands. The strategy worked.

4. Clear Sense of Strategic Vision and Sharper Focus on Goals and Objectives

Every firm competing in an industry has a strategy, because strategy refers to how a given objective will be achieved. 'Strategy' defines what it is we want to achieve and charts our course in the market place; it is the basis for the establishment of a business firm; and it is a basic requirement for a firm to survive and to sustain itself in today's changing environment by providing vision and encouraging to define mission.

5.Motivating Employees

One should note that the labor efficiency and loyalty towards management can be expected only in an organization that operates under strategic management. Every guidance as to what to do, when and how to do and by whom etc, is given to every employee. This makes them more confident and free to perform their tasks without any hesitation. Labor efficiency and their loyalty which results into industrial peace and good returns are the results of broad-based policies adopted by the strategic management

6. Strengthening Decision-Making

Under strategic management, the first step to be taken is to identify the objectives of the business concern. Hence a corporation organized under the basic principles of strategic management will find a smooth sailing due to effective decision-making. This points out the need for strategic management.

7. Efficient And Effective Way Of Implementing Actions For Results

Strategy provides a clear understanding of purpose, objectives and standards of performance to employees at all levels and in all functional areas. Thereby it makes implementation very smooth allowing for maximum harmony and synchrony. As a result, the expected results are obtained more efficiently and economically.

8. Improved Understanding of Internal and External Environments of Business

Strategy formulation requires continuous observation and understanding of environmental variables and classifying them as opportunities and threats. It also involves knowing whether the threats are serious or casual and opportunities are worthy or marginal. As such strategy provides for a better understanding of environment.

Levels of Strategy

A typical business firm should consider three types of strategies, which form a hierarchy as shown in Figure 1.1

Corporate Strategy

This describes a company's overall direction towards growth by managing business and product lines. These include stability, growth and retrenchment.

For example, Coco cola, Inc., has followed the growth strategy by acquisition. It has acquired local bottling units to emerge as the market leader.

Business Strategy

Usually occurs at business unit or product level emphasizing the improvement of competitive position of a firm's products or services in an industry or market segment served by that business unit. Business strategy falls in the in the realm of corporate strategy.

For example, Apple Computers uses a differentiation competitive strategy that emphasizes innovative product with creative design.

Functional Strategy

It is the approach taken by a functional area to achieve corporate and business unit objectives and strategies by maximizing resource productivity. It is concerned with developing and nurturing a distinctive competence to provide the firm with a competitive advantage.

Operating Strategy

These are concerned with how the component parts of an organization deliver effectively the corporate, business and functional -level strategies in terms of resources, processes and people. They are at departmental level and set periodic short-term targets for accomplishment.

Crafting A Strategy

Companies and strategists craft strategies in different ways. In extreme cases it is only the Chairman cum Managing Director who crafts the strategy. But in firms, which have participative management style of functioning, it is a group or team exercise involving key personnel and all functional executives in the organization.

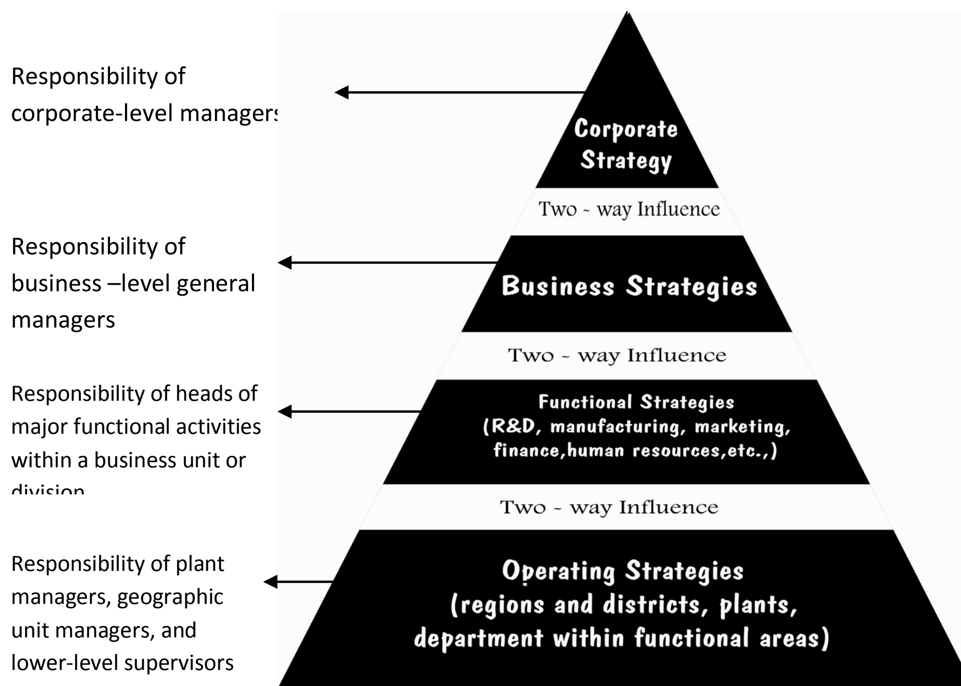

Figure 1.1 Hierarchy of strategy

There are basically four approaches to crafting a strategy

1. The Chief Architect approach: A single person – the owner or CEO –assumes the role of chief strategist and chief entrepreneur, single handedly shaping most or all of the major pieces of strategy. This does not mean that one person is the originator of all the ideas underlying the resulting strategy or does all the background data gathering and analysis: there may be much brainstorming with subordinates and considerable analysis by specific departments.

The chief architect approach to strategy formation is characteristic of companies that have been founded by the company's present CEO. Michael Dell at Dell Computer, Steve Case at America Online, Bill Gates at Microsoft, and Howard Schultz at Starbucks are prominent examples of corporate CEOs who exert a heavy hand in shaping their company's strategy.

2. The Delegation Approach: Here the manager in charge delegates big chunks of the strategy-making task to trusted subordinates, down-the-line managers in charge of key business units and departments, a high-level task force of knowledgeable and talented people from many

parts of the company, self-directed work teams with authority over a particular process or function, or, more rarely, a team of consultants brought in specifically to help develop new strategic initiatives.

3. The Collaborative or Team Approach: This is a middle approach when by a manager with strategy-making responsibility enlists the assistance and advice of key peers and subordinates in hammering out a consensus strategy. Strategy teams often include line and staff managers from different disciplines and departmental units, a few handpicked junior staffers known for their ability to think creatively, and near-retirement veterans noted for being keen observers, telling it like it is, and giving sage advice.

Electronic Data Systems conducted a year-long strategy review involving 2,500 of its 55,000 employees and coordinated by a core of 150 managers and staffers from all over the world.

Nokia Group, a Finland-based global leader in wireless telecommunications, involved 250 employees in a strategy review of how different communications technologies were converging, how this would affect the company's business, and what strategic responses were needed.

4. The Corporate Entrepreneur Approach: In the corporate entrepreneur approach, top management encourages individuals and teams to develop and champion proposals for new product lines and new business ventures. The idea is to unleash the talents and energies of promising corporate entrepreneurs, letting them try out business ideas and pursue new strategic initiatives. Executives serve as judges of which proposals merit support, give company entrepreneurs the needed organizational and budgetary support, and let them run with the ball.

W.L. Gore & Associates, a privately owned company famous for its Gore-Tex waterproofing film, is an avid and highly successful practitioner of the corporate intrapreneur approach to strategy making. Gore expects all employees to initiate improvements and to display innovativeness.

As on going process

Corporate strategy is a continuous on going process and extends company wide over a diversified company's business. It is a boundary spanning planning activity considering all the elements of the micro and macro environments of a firm. The following are the key tasks of the process of developing and implementing a corporate strategy.

- Exploring and determining the ***vision*** of the company in the form of a vision statement.
- Developing a **mission** ***statement*** of the company that should include statement of methodology for achieving the objectives, purposes, and the philosophy of the organization adequately reflected in the vision statement.
- Defining the ***company profile*** that includes the internal analysis of culture, strengths and capabilities of an organization.
- Making ***external environmental analysis*** to identify factors as threats, opportunities etc.
- Finding out ways by which a company profile can be ***matched*** with its environment to be able to accomplish mission statement
- Deciding on the most desirable ***courses of actions*** for accomplishing the mission of an organization
- Selecting a set of ***long-term objectives*** and also the corresponding strategies to be adopted in line with vision statement.
- Evolving short-term and ***annual objectives*** and defining the corresponding strategies that would be compatible with the mission and vision statement.
- ***Implementing*** the chosen strategies in a planned way based on budgets and allocation of resource, outlining the action programs and tasks.
- Installation of a continuous comparable ***review system*** to create a controlling mechanism and also generate data for selecting future course of action

The over all corporate strategy of a diversified company is depicted in Figure 1.2

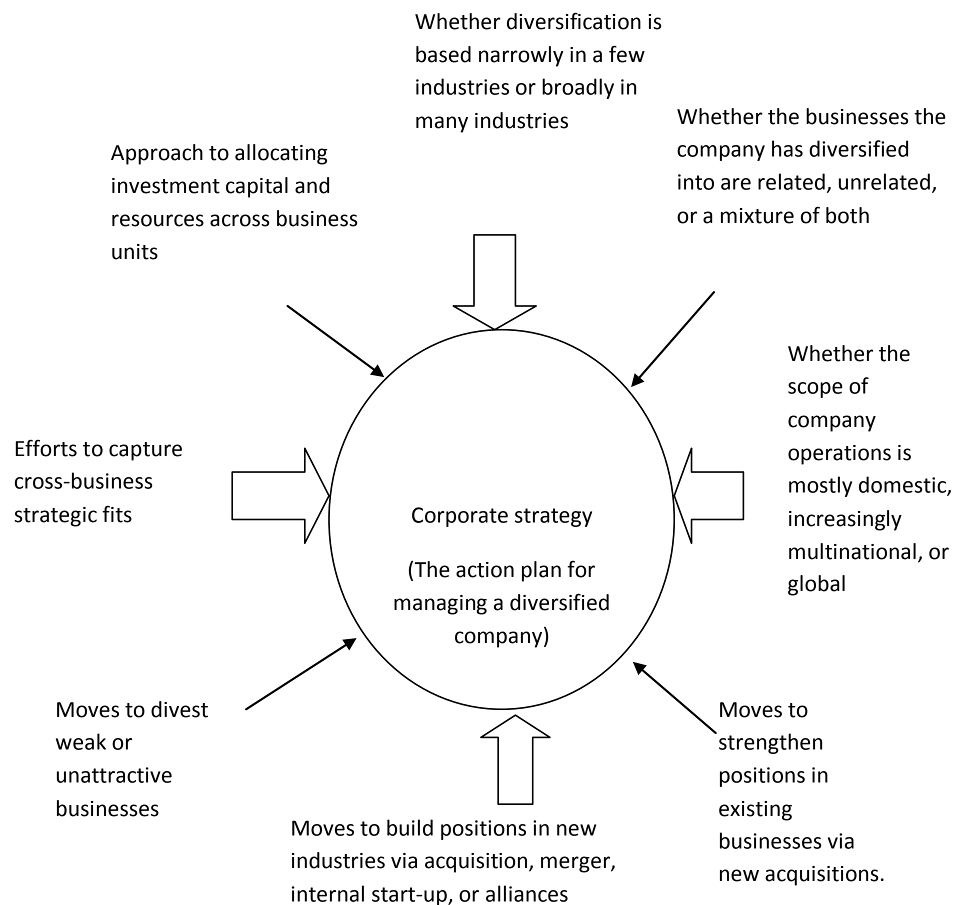

Figure 1.2 Strategy of a diversified company

Source : Thompson & Strickland (2003), Strategic Management, Tata McGraw Hill, New Delhi.

The process of developing corporate strategy or the overall managerial plan for involves the following processes.

1. Making the moves to establish in different businesses and achieve diversification.
2. Initiating actions to boost the combined performance of the businesses the firm has diversified into.
3. Pursuing ways to capture valuable cross-business strategic fits and turn them into competitive advantage.
4. Establishing investment priorities and steering corporate resources into the most attractive business units

Summary

In the globalized business, companies require strategic thinking and only by evolving good corporate strategies can they become strategically competitive. A strategy of a business organization is a comprehensive master plan stating how the organization will achieve its mission and objectives. Strategy is significant because it is universal. It helps corporate to keep pace with changing environs, provides better understanding of external environment, minimizes competitive disadvantage by forcing to think clearly about mission, vision and objectives of enterprise. It improves motivation of employees and strengthens decision-making. It forms the basis for implementing actions. Strategy can be classified based on hierarchy into four levels: corporate level, strategic business level, functional level and operating level. The approaches to strategy making are: the Chief Architect approach, the delegation approach, the collaborator or team approach and the corporate entrepreneur approach. Strategy making is an ongoing process involving activities like defining vision, mission and goals, analyzing organization and environment and matching them to decide suitable actions and objectives, and implementing with a review system.

Self -Assessment Questions

1. Define the concept of strategy
2. Write two definitions of strategy and identify the key elements in them.
3. Distinguish strategy and plan. Which one is more suitable in a competitive environment?
4. What are the 5 Ps of a strategy?
5. Explain the significance of a strategy.
6. What are the different levels of strategy making?
7. Identify the people responsible for strategy making at different levels in an organization
8. Explain the different approaches to strategy making.
9. "Corporate strategy making is an on going process " –Discuss
10. Explain the strategy of a diversified company.

Activities

1. Visit a local business organization, a hospital and educational institution and interview the director or owner of these organizations to identify the mission, vision, goals of the organizations. Also identify the achievements and future plans of these organizations.
2. Refer management journals like Vikalpa of IIM-A or IIMB Management Review or Global CEO or visit websites like India infoline.com and identify articles on strategy and prepare a write up on " Strategy for modern organizations".

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Lesson 2 - Strategic Management Process

Lesson Outline

- Introduction
- Process Of Strategic Management – Basic Model
- Role Of Strategists
- Mintzberg's Modes Of Strategic Decision Making
- Strategic Management In India
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Describe the strategic management process
- Know the role of different persons in an organization in strategy making
- Explain Mintzberg's modes of executive decision making
- Appreciate the initiatives taken by corporate in India for effective strategy management

Once there were two company presidents who competed in the same industry. These two presidents decided to go on a camping trip to discuss a possible merger. They hiked deep into the woods. Suddenly, they came upon a grizzly bear that rose up on its hind legs and snarled. Instantly, the first president took off his knapsack and got out a pair of jogging shoes. The second president said, "Hey, you can't outrun that bear. The first president responded, " May be I can't outrun that bear but I surely can outrun you!" (Fred R. David, 2003,p.5)

This story captures the notion of strategic management, which is to achieve and maintain competitive advantage. How do business or-

ganizations operate successfully in the changing business environment? Strategic management has evolved as a primary value in helping organization operate successfully in a dynamic, complex environment. Even the most successful Fortune 500 companies would accept that it is definitely not by following traditional ways of doing business.

Most successful companies like General Electric have found internet mentors to tutor their managers to world wide web. The company has launched its financial network www.gefn.com in the year 2000 for its consumers.

Launch of Apna PC is a strategic decision. The leader in PC business HCL Info systems has launched one PC below Rs.10, 000 (its sticker price is Rs.9, 990). It has committed to manufacture one million of them every year and expand its dealer network from 800 to 3,000. This strategy is to tap the small businesses and lower income classes in urban and rural India.

BHEL for example uses strategic management to create or modify its long-range plans, which range from 5 to 20 years.

Process of Strategic Management

Strategic management consists of four basic elements.

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

Figure 2. 1 shows simply how these elements interact. Figure 2 .2 expands each of these elements and serves as the model

Environmental Scanning is the monitoring, evaluating, and disseminating of information from the external and internal environments to key people within the corporation. Its purpose is to identity strategic factors – those external and internal elements that will determine the future of the corporation.

The external environment consists of variables (Opportunities and Threats) that are outside the organization and not typically within the short-run control of top management. These variables form the context within which the corporation exists.

Figure 2.1 Basic model

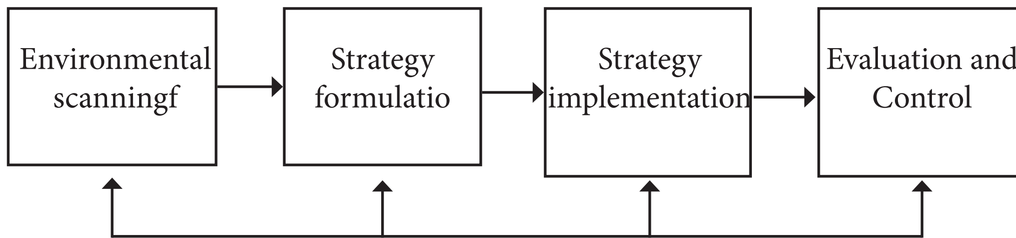
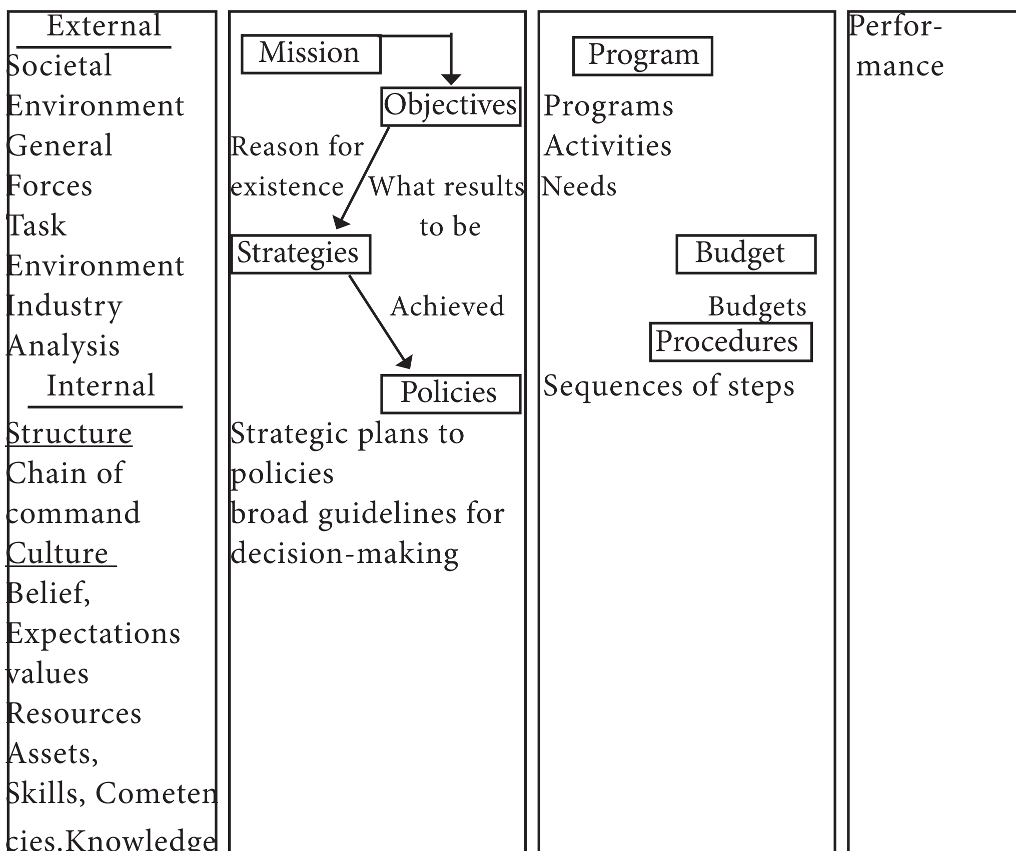


Figure 2.2 Expanded model for strategic Management



The internal environment of a corporation consist of variables (Strengths and Weakness) that are within the organization itself and are not usually within the short run control of top management. These variables form the context in which work is done. They include the corporation's structure, culture, and resources.

The simplest way to conduct environmental scanning is through SWOT analysis . SWOT is an acronym used to describe those particular Strengths, Weaknesses, Opportunities, and Threats that are strategic factors for a specific company.

Strategy formulation is the development of long-range plans for the effective management of environmental opportunities and threats, in light of corporate strengths and weaknesses. It includes defining the corporate mission, specifying achievable objectives, developing strategies and setting policy guidelines.

Strategy Implementation is the process by which strategies and polices are put into action through the development of programs, budgets and procedures. This process might involve changes within the overall culture, structure, and/or management system of the entire organization. Most of the times strategy implementation is carried out by middle and lower level managers with top management's review. Some times refereed to as operational planning, strategy implementation often involves day-to-day decisions in resource allocation. It includes programs, budgets and procedures.

Evaluation and control is the process in which corporate activities and performance results are monitored so that actual performance can be compared with desired performance. Managers at all levels use the resulting information to take corrective action and resolve problems. Although evaluation and control is the final major element of strategic management, it also can pinpoint weaknesses in previously implemented strategic plans and thus stimulate the entire process to begin again.

Role of strategists

Strategists are individuals or groups who are primarily involved in the formulation, implementation, and evaluation of strategy. In a limited sense, all managers are strategists. There are persons outside the organization who are also involved in various aspects of strategic management. They too are referred to as strategists. We can identify nine strategists who, as individuals or in groups, are concerned with and play a role in strategic management.

1. Consultants
2. Entrepreneurs
3. Board of Directors
4. Chief Executive Officer
5. Senior management
6. Corporate planning staff
7. Strategic business unit (SBU) level executives

8. Middle level managers
9. Executive Assistant

A brief description of how the different strategists approach the process is outlined here.

1) Consultants: Many organizations which do not have a corporate planning department owing to reasons like small size, infrequent requirements, financial constraints, and so on, take the help of external consultants in strategic management. Besides the Indian consultancy firms, such as, A.F.Ferguson, S.B. Billimoria and several others, now there are many foreign consultancy firms. They offer a variety of services.

McKinsey and Company, specializes in offering consultancy in the areas of fundamental change management and strategic visioning; Andreson Consulting, is in business restructuring, and info tech and systems; Boston Consulting helps in building competitive advantage; and KPMG Peat Marwick is in strategic financial management and feasibility studies for strategy implementation.

2) Entrepreneurs are promoters who conceive the idea of starting a business enterprise for getting maximum returns on their investment. They are waiting for an environment change and thereby for an opportunity to exploit the situation in their best interest. Thus they start playing their role right from the promotion of the proposed venture. So, their strategic role to make the venture a success is very conspicuous in a new business enterprise. Therefore, it is expected of an entrepreneur that he should posses foresight, sense of responsibility, desire to work hard and dashing spirit to bear any future contingencies. According to Drucker, "the entrepreneur always searches for change, responds to it and exploits it as an opportunity". Here is an example of a successful women entrepreneur.

Kiran Mazumdar Shaw, a young entrepreneur, set up an export-oriented unit manufacturing a range of enzymes. As an expert in brewing technology, Mazumdur entered the field of biotechnology after experiencing problems in getting a job. Later she set up another plant for manufacturing two new enzymes created by her own research and development (R&D) department. As managing director, Mazumdar was actively involved in all aspects of policy formulation and implementation for her companies.

3) Board of Directors are professionals elected on the Board of Directors (BOD) by the shareholders of the company as per rules and regulations of the Companies Act, 1956. They are responsible for the general administration of the organization. They are supposed to guide the top management in framing business strategies for accomplishing predetermined objectives. It is also the responsibility of the Board to review and evaluate organizational performance whether it is as per the strategy laid down or not. The Board is also empowered to make appointments of senior executives. In this connection, it should be noted that the success of strategies much depends on the relative strength in terms of power held by the Board and the Chief Executive (CE).

4) Chief Executive Officer: In the management circle, the chief executive is the top man, next to the directors of the Board. He occupies the most sensitive post, being held responsible for all aspects of strategic management right from formulation to evaluation of strategy. He is designated in some companies as the managing director, executive director or as a general manager. Whatever the designation be, he is considered the most important strategist being responsible to play major role in strategic decision-making.

5) Senior Management: Starting from the chief executive to the level of functional or profit-centre heads, these managers are involved in various aspects of strategic management. Some of the members of the senior management act as directors on the board usually on a rotational basis. All of them serve on different top-level committees set up by the board to look after matters of strategic importance and other policy issues. Executive committees, consisting of senior managers, are responsible for implementing strategies and plans, and for a periodic evaluation of performance.

Strategic planning at MRF Ltd. used senior management expertise by dividing them into five groups dealing with products and markets, environment, technology, resources, and manpower. Each group had a leader who helped to prepare position papers for presentation to the board. The executive directors in the company were actively involved in SWOT analysis through the help of managers and assistant managers.

6) SBU level executives: "SBU" stands for strategic business unit. Under this approach, the main business unit is divided into different

independent units and is allowed to form their own respective strategies. In fact, the business is diversified and thus the departmental heads are supposed to act as the main strategist, keeping an eye on optimum benefit for their departments. Hence strategists i.e., the departmental heads enjoy the maximum amount of authority and responsibility within their strategic business units.

At Shriram Fibres, the strategic planning system covered the different businesses ranging from nylon yarn manufacture to the provision of financial services. Strategic plans were formulated at the level of each SBU as well as at the corporate level. The corporate planning department at the head office coordinated the strategic planning exercise at the SBU-level. Each SBU had its own strategic planning cell.

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

8) Middle level managers: They are basically operational planners they may, at best, be involved as 'sounding boards' for departmental plans, as implementers of the decisions taken above, followers of policy guidelines, and passive receivers of communication about functional strategic plans. As they are basically involved in the implementation of functional strategies, the middle-level mangers are rarely employed for any other purpose in strategic management.

9) Executive Assistant: An executive assistant is a person who assists the chief executive in the performance of his duties in various ways. These could be : to assist the chief executive in data collection and analysis, suggesting alternatives where decisions are required, preparing briefs of various proposals, projects and reports, helping in public relations and liaison functions, coordinating activities with the internal staff and outsiders, and acting as a filter for the information coming from different sources. Among these "the most important and what one manager

labels the "bread and butter role" of EA (executive assistant) could be that of corporate planner".

Mintzberg's Modes of Strategic Decision-Making

Henry Mintzberg has given three most typical approaches of strategic decision making which include:

- Entrepreneurial mode
- Adaptive mode
- Planning mode

We will now examine the three modes of strategic decision making.

Entrepreneurial Mode

Strategy is made by one powerful individual who has entrepreneurial competencies like innovation and risk taking. The focus is on opportunities. Problems are secondary. Generally the founder is the entrepreneur and the strategy is guided by his or her own vision of direction and is exemplified by bold decisions.

The success of Biocon India founded by Kiran Mazumdur shaw is an example of this mode of strategic decision making.

Adaptive Mode

Sometimes referred to as "muddling through," this decision-making mode is characterized by reactive solutions to existing problems, rather than a proactive search for new opportunities. Much bargaining goes on concerning priorities of objectives. Strategy is fragmented and is developed to move the corporation forward incrementally. This mode is typical of most universities, many large hospitals and a large number of governmental agencies.

Planning Mode

This decision making mode involves the systematic gathering of appropriate information for situation analysis, the generation of feasible alternative strategies, and the rational selection of the most appropriate strategy. It includes both the proactive search for new opportunities and the reactive solution of existing problems.

Hewlett-Packard (HP) is an example of the planning mode. After a careful study of trends in the computer and communications industries, management noted that the company needed to stop thinking of itself as a collection of stand-alone products with a primary focus on instrumentation and computer hardware. Led by its new CEO, Carly Florina, top management felt that the company needed to become a customer-focused and integrated provider of information appliances, highly reliable information technology infrastructure and electronic commerce service.

A fourth mode of 'logical incrementalism' was later added by Quinn.

Logical Incrementalism

In this mode, top management first develops reasonably clear idea of the corportion's mission and objectives. Then, in its development of strategies, it chooses to use "an interactive process in which the organization probes the future, experiments and learns from a series of partial (incremental) commitments rather than through global formulations of total strategies". Thus the strategy is allowed to emerge out of debate, discussion, and experimentation. This approach appears to be useful when

- The environment is changing rapidly,
- It is important to build consensus, and
- Needed resources are to be developed before committing the entire corporation to a specific strategy.

Strategic management in India

After the economic liberalization announced in India in 1991, strategic management has gained greater relevance. In fact it is a major thrust area after the WTO meet of December 2005 held in Hong Kong. Figure 2.3 lists the environmental changes that have increased the relevance of strategic management. In view of this to make strategic management effective organizations are showing some new initiatives described here.

1. The abolition of public sector monopoly or dominance in a number of industries has enormously increased business opportunities. Many of them are high-tech and heavy investment sectors which make strategic management all the more relevant.

2. The delicensing has removed not only an important entry and growth barrier but also a consumption (and, therefore, demand) barrier. In the past, because of non-production/limited production and import restrictions, many goods were non-available or had limited availability (in quantity and /or variety).

3. The scrapping of most of the MRTP Act restrictions on entry, growth and Mergers &Acquisitions (M&As) , along with the dereservation and delicensing of industries referred to above, have opened up flood-gates of business opportunities for large enterprises.

4. The liberalization in policy towards foreign capital and technology, imports and accessing foreign capital markets provides companies opportunities for enhancing their strengths to exploit the opportunities.

5. The liberalization in other countries, the expanding foreign markets, the growing competition in India, the new policy environment etc., increase the importance of foreign markets and strategic management.

6. The grant of more autonomy to the public sector enterprises, as in the case of the navarathnas, increases the scope of strategic management.

Trend Setters in Indian Economy

Source: Cherunilam, Francis(2002) Strategic Management,

Himalaya Publishing Company, New Delhi

(i) Developing learning organization

Strategic flexibility demands a long-term commitment to the development and nurturing of critical resources. It also demands that the company become a learning organization – an organization skilled at creating, acquiring, and transferring knowledge, and at modifying its behavior to reflect new knowledge and insights. Organizational learning is a critical component of competitiveness in a dynamic environment. It is particularly important to innovation and new product development.

For example, Hewlett-Packard uses an extensive network of informal committees to transfer knowledge among its cross-functional teams and to help spread new sources of knowledge quickly.

(ii) TQM Implementation

The very purpose of strategic management is to win over its competitors. Total quality Management (TQM) is an organizational philosophy that aims at maximizing customer satisfaction by constantly striving to enhance operational efficiency through out the organization. It is a start to finish process that systematically integrates the strategy and all the function activities of the organization. Most of the Japanese companies adopted TQM practices in 1970 itself.

TQM method measures customers' needs, measures and evaluate customer satisfaction delivered by the product or service ,and engages the organization in continuous improvement to stay tuned-in to changes in customers' needs".

The essential characteristics of TQM are:

- A customer-driven definition of quality
- Strong quality leadership
- Emphasis on continuous improvement
- Reliance on facts, data, and analysis
- Encouragement of employee participation

It is imperative for a company, which has adopted the TQM to integrate it with every phase of the strategic management.

Environmental Analysis and TQM

The environmental analysis of a company with TQM connects the needs of the external customer (the entirety that buys the good or service of the company) with the various activities of the company.

Organizational Decision and TQM

TQM influences the organizational direction by embodying the quality philosophy in the organizational mission. Indeed, the missions of a number of organizations emphasize that quality and continuous improvement must drive every action of the organization.

Strategy Formulation and TQM

TQM helps make strategy implementation very efficient because of the clarity of organizational goals and direction, and the work and relationships culture fostered by TQM.

Strategic Control and TQM

Systems established under TQM and the favorable change in the organizational culture make strategic control more effective. Benchmarking also helps efficient control.

Information technology adaptation

Until the mid 1989 business firms were successfully making profits without using Internet or launching their websites. Today virtual shopping and online retailing supplement brick and mortar sales. A great success is that of amazon.com, which do not involve in brick and mortar retailing at all. All their sales come from online business only today.

Space providers like e-bay.com are becoming increasingly popular in India after taking over bazee.com. Executives today are electronic executives who cannot operate without World Wide Web.

Globalizing Operations

Nike and Reebok, for example, manufacture their athletic shoes in various countries thorough out Asia for sale on every continent. Instead of using one international division to manage everything outside the home country, large corporations are now using matrix structures in which product units are interowen with country or regional units. International assignments are now considered key for anyone interested in reaching top management.

As more industries become global, strategic management is becoming an increasingly important way to keep track of international developments and position the company for long-term competitive advantage.

Summary

Strategic management has evolved as a primary value in helping organization operate successfully in a dynamic, complex environment

BHEL for example uses strategic management to create or modify its long-range plans, which range from 5 to 20 years. Strategic management consists of four basic elements: Environmental scanning, Strategy formulation, Strategy implementation and Evaluation and control. Nine persons or groups are identified to have interest in strategic management. They are-Consultants, Entrepreneurs, Board of Directors, Chief Executive Officer, Senior management, Corporate planning staff, Strategic business unit (SBU) level executives, Middle level managers and Executive Assistant. Henry Mintzberg has given three most typical approaches of strategic decision making which include: Entrepreneurial mode, Adaptive mode and Planning mode. In India, abolition of public sector monopoly, the delicensing, scrapping of MRTP Act, liberalization policy towards technology and capital,

expanding foreign markets and competition and grant of autonomy to navarathnas etc., created the need for strategic management. The key elements in strategic management are: developing learning organization, TQM implementation, and information technology adaptation and globalsing operations.

Self -Assessment Questions

1. Describe the strategic management process with examples.
2. Explain environment canning and analysis.
3. What do you understand by strategy implementation and control?
4. Explain the role of different persons in an organization in strategy making.
5. What is the role of entrepreneur and entrepreneur in strategy making?
6. Examine the Mintzberg's modes of executive decision-making and identify the companies adapting such modes.
7. What factors in India are responsible for growing importance of strategy?
8. Describe with examples the initiatives taken by corporate in India for effective strategy management.
9. What is TQM and how it is made an element in strategy?
10. What is the impact of IT on corporate strategy?

Activities

1. Read the Chairman's speech of two different companies in the Annual General Meetings and prepare a note on their strategies.

2. Refer the websites of three organizations –one from service sector, one from manufacturing sector and one from IT sector- and compare their strategic approaches.

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Lesson 3 - Mission and Objectives

Lesson Outline

- Introduction
- Process Of Establishing Organizational Direction
- Strategic Intent
- Mission Or Purpose
- Objectives
- Synergy
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to.

- Understand and need for strategic direction and strategic intent
- Define mission statements for different organizations
- Appreciate the types of organization objectives
- Know how to set objectives in of Key Result Areas (KRAs)

Introduction

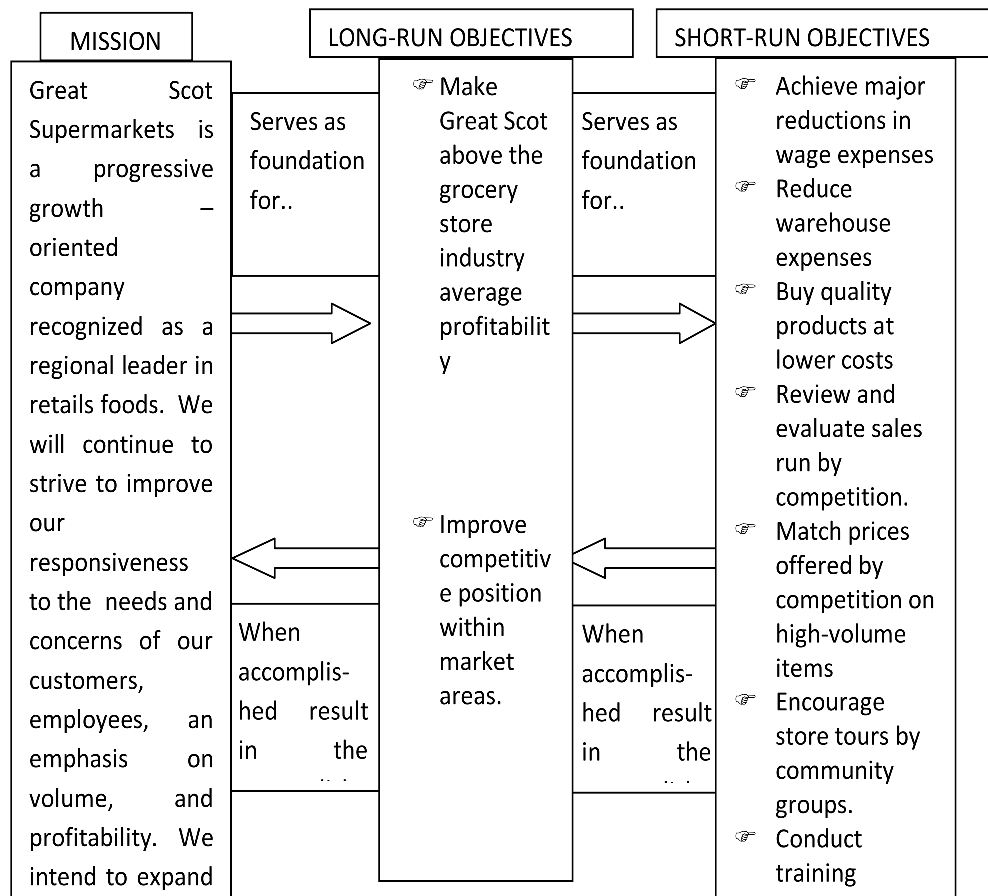
Planning is way of organization life but it differs from individuals to organizations. It is futuristic, decision oriented and goal driven. Planning bridges the gap from where we are to where we want to go. It involves the process of establishing direction, identifying a strategic intent, selecting missions and objectives and ways of achieving them.

Process of Establishing Organizational Direction

The process of establishing direction consists of three major steps as shown in Figure 3.1

1. Reflecting on the results of an environmental analysis,
2. Establishing an appropriate organizational mission, and
3. Establishing appropriate organizational objectives.

Figure 3.1 Strategic Management –Process focus



Source: Samuel C. Certo & J Paul Peter, Strategic M

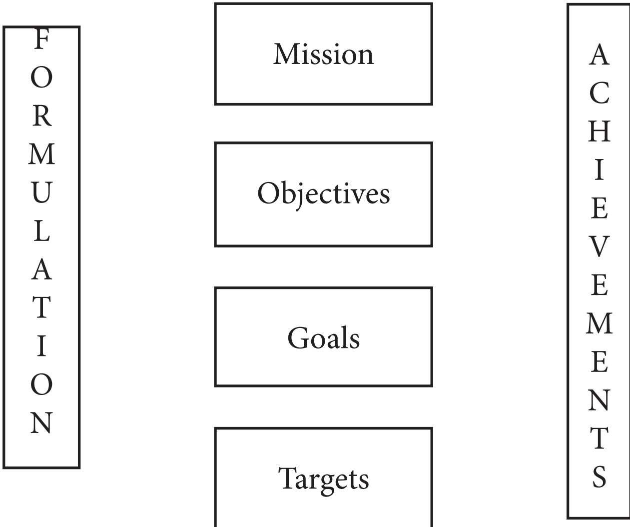
anagement A Focus on Process, Mc Graw Hill International, New York.p

Developing mission and objectives helps a manager to

- Contribute primarily to manager's purpose
- Identify primarily among manager's tasks
- Examine the pervasiveness of planning and
- Outline the efficiency of resulting plans.

The terms mission, objectives, goals and targets are used many a time interchangeable. However, in corporate literature they are often used distinctively. Mission leads to objectives (which are designed to achieve the mission), objectives lead to goals (which are designed to achieve the objectives) and goals lead to targets (which are set to achieve the goals) as shown in Figure3.2.

Figure 3.2 Elements in Strategy Formulation



Strategic Intent

CK Prahald and Hamel coined the term 'strategic intent' to indicate an obsession of an organization, some times having ambitions that may even be out of proportion to their resources and capabilities. They explain the term 'strategic intent' like this.

"On the one hand, strategic intent envisions a desired leadership position and establishes the criterion the organization will use to chart its progress…. At the same time, strategic intent is more than simply unfettered ambition.

The concept also encompasses an active management process that includes

- focusing the organization's attention on the essence of winning,
- motivating people by communicating the value of the target,
- leaving room for individual and team contributions,
- sustaining enthusiasm by providing new operational definitions as circumstances change and
- using intent consistently to guide resource allocations".

Hamel and Prahlad quote several examples of global firms, almost all of American and Japanese origin, to support their view. In fact, the concept of strategic intent –as evident from their path breaking article, published in 1989 in the Harvard Business Review- seems to have been proposed by them to explain the lead taken by Japanese firms over their American and European counterparts.

Indian examples of companies with strategic internet are late Dhirubai Ambani's Reliance group with the strategic intent of being a global leader of being the lowest cost producer of polyester products a status achieved with vertical integration and operational effectiveness. The Indian hardware giant, HCL's aspiration to become global software and service company is working with the strategic intent of putting hardware, software and networking together and making it work At Procter & Gamble (P&G) employees participate in a program the CEO calls "combat training, "The program's intent is to focus on ways P&G can beat the competition.

Mission or Purpose

Its name or articles of incorporation do not define a business. The business mission defines it. Only a clear definition of mission and purpose of the organization makes possible clear and realistic business objectives.

Mission statements can vary in length, content, format, and specificity. Most practitioners and academicians of strategic management feel that an effective statement exhibits 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:

1. Customers: Who are the firm's customers?
2. Product 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: Is the firm responsive to social, community, and environmental concerns?
9. Concern for employees: Are employees a valuable asset of the firm?

Pepsi Co's mission is to increase the value of our shareholders' investment. We do this through sales growth, cost controls, and wise investment resource. We believe our commercial success depends upon offering quality and value to our consumers and customers; providing products that are safe, wholesome, economically efficient, and environmentally sound; and providing a fair return to our inventors while adhering to the highest standards of integrity.

Dell Computer's mission 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.

Establishing an organizational mission is an important part of management's job, because the existence of a formally expressed organizational mission generally makes it more likely that the organizational will succeed. Having an established and documented organizational mission accomplishes several important things. A mission statement once established serves an organization for many years. But a mission may become unclear as the organization grows and adds new product, markets and technologies to its activities. So a mission statement should be broad enough to accommodate any new changes to avoid reformulation.

Objectives

An organization's mission gives a framework or direction to a firm. The next step in planning is focusing on establishing progressively more specific organizational direction by setting objectives. An organizational objective is a target toward which the organization directs its efforts. Objectives in organizations, as shown in Figure 3.3 exhibit a hierarchy.

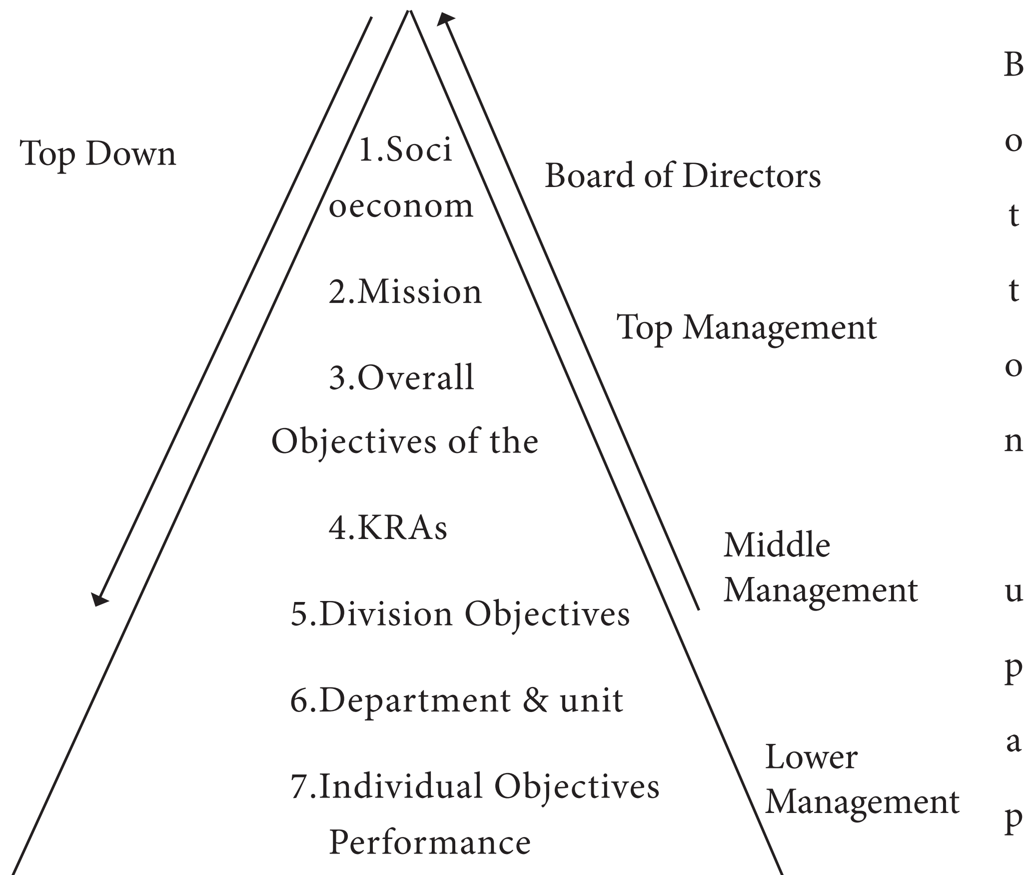


Figure 3.3 Hierarchv of Objectives

The BOD are more concerned with mission, purpose and overall objectives. Middle managers are involved in key result areas(KRAs), division and department objectives. At the lower level, group personal

objectives are set. The objectives can be top down or bottom up taking the initiative from lower management.

Managers should develop organizational objectives that are

- Specific
- Require a desirable level of effort
- Flexible
- Measurable and operational
- Consistent in the long and short run

Peter Drucker, perhaps the most influential business writer of modern times, has pointed out that it is a mistake to manage organizations by focusing primarily on one and only one objective. According to Drucker, organizations should aim at achieving several objectives instead of just one. Enough objectives should be set so that all areas important to the operation of the firm are covered. Eight key areas in which organizational objectives should normally be set are:

1. **Market standing:** The position of an organization – where it stands – relative to its competitors
2. **Innovation:** Any change made to improve methods of conducting organizational business.
3. **Productivity:** The level of goods or services produced by an organization relative to the resources used in the production process. Organizations that use fewer resources to produce a specified level of products are said to be more 'productive than organizations that require more resources to produce at the same level.
4. **Resource levels:** the relative amounts of various resources held by an organization, such as inventory, equipment, and cash. Most organizations should set objectives indicating the relative amount of each of these assets that should be held.
5. **Profitability:** The ability of an organization to earn revenue dollars beyond the expenses necessary to generate the revenue. Organizations commonly have objectives indicating the level of profitability they seek.
6. **Manager performance and development:** The quality of managerial performance and the rate at which managers are developing personally.

Because both of these areas are critical to the long-term success of an organization, emphasizing them by establishing and striving to reach related organizational objectives is very important.

7. **Worker performance and attitude:** The quality of non-management performance and such employee's feelings about their work. These areas are also crucial to long-term organizational success. The importance of these considerations should be stressed through the establishment of organizational objectives.
8. **Social responsibility:** The obligation of business to help improve the welfare of society while it strives to reach organizational objectives.

Table 3.1 shows the usage of the different objectives by various companies.

Table 3-1

Types and Usage Levels of Organizational Objectives

Type of objective	Number of companies studied having objective type	Percent of companies studied having objective type
Profitability	73	89
Growth	67	82
Market share	54	66
Social responsibility	53	65
Employee welfare	51	62
Product quality and service	49	60
Research and Development	44	54
Diversification	42	31
Efficiency	41	50
Financial stability	40	49
Resource conservation	32	39

Management development	29	35
Multinational enterprise	24	29
Consolidation	14	17
Miscellaneous other goals	15	18

*Adds to more than 100 percent because most companies have more than one goal

Source : Y.K. Shetty, New Look at Corporate Goals," California Management Review, 22 , No.2 (Winter 1979).

Synergy

Derived form the Greek word "synergos," which means "working together" exceeds the value those units could create working independently. Another way of saying this is that synergy exists when assets" are worth more when used in conjunction with each other than separately. Synergies can involve physical and non-physical assets" such as human capital. For shareholders, synergy generates gains in their wealth that they could not duplicate or exceed through their own portfolio diversification decisions.

Synergy exists when the value created by business units, working together exceeds the value those same units create working independently. But, as a firm increases its relatedness between business units, it also increases its risk of corporate failure, because synergy produces joint interdependence between business units and the firm's flexibility to respond is constrained. This threat may force two basic decisions. First, the firm may reduce its level of technological change by operating in more certain environments. Alternatively, the firm may constrain its level of activity sharing and forego the benefits of synergy. Either or both decisions may lead to further diversification. The latter may produce additional, but unrelated, diversification. Synergetic effects occur across functional areas and core competencies emerge as a result of the concentration of resources to the areas where an organization wishes to build up strategic advantages. This can be observed in the case of a company, which is, or intends to be, a market leader, a low-cost producer, a technologically superior competitor, or an ideal employer. For achieving

each of these objectives, an integrated approach to functional plans and policies would be necessary. For instance, a company, which intends to be a market leader, would have to offer products of the best quality at a competitive price through an efficient distribution network supported by an aggressive promotion policy. The other functional area plans and policies would have to supplement these marketing policies.

Summary

Two main organizational ingredients are commonly used to establish organizational direction: Organizational mission and organizational objectives. Organizational mission is the purpose for which, or reason why, the organization exists. An organizational mission should help focus human effort, ensure compatibility of organizational purposes, provide a rationale for resource allocation, indicate broad areas of job responsibility, and provide the foundations for organizational objectives. Objectives are the end points of an activity. They help define the direction of an organization in concrete form for accomplishment. Objectives of an organization form a hierarchy and are multiple. Objectives are needed in key result areas. They include market-standing, innovation, productivity, profitability, public responsibility, physical and financial resources, employee performance and attitude and manager performance and development. Synergy is necessary for competitive advantage. For instance, a company, which intends to be a market leader, would have to offer products of the best quality at a competitive price through an efficient distribution network supported by an aggressive promotion policy. The other functional area plans and policies would have to supplement these marketing policies.

Self-Assessment Questions

1. Define mission and objectives and give examples.

2. Examine the significance of mission statement and goals and objectives in giving strategic direction to a firm

3. What do you understand by strategic intent? Explain the concept with corporate examples

4. Explain why a mission statement should accommodate the future growth of a company

5. Outline the typical characteristics of a mission statement and list its components
6. Illustrate the hierarchy of objectives as it cascades down the hierarchy
7. Identify and briefly explain the Key Result Areas of Peter F. Drucker
8. What are the characteristics of goals?
9. Describe the concept of 'synergy' and discuss its significance to strategic planning.
10. Identify companies having clear strategic direction, mission and objectives.

Activities

1. Find the mission statements of the following organizations:
2. (a) Procter & Gamble India Ltd (a) Glaxo Laboratories (c) Appolo Hospitals
3. Study the objectives of Bharat Heavy Electrical Limited. Figure out the strategic intent of the company.

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Lesson 4 - Strategic Business Unit and Functional Level Strategies

Lesson Outline

- Introduction
- Strategy Management Outcomes
- Evolution Of Structures
- Types Of Structures
- Decision-Making Hierarchy Of Business Firms
- Strategy - Structure Combinations
- Role Of Sbu Level Executives And Strategies
- Functional Level Strategies
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand significance of strategy implementation
- Know different structures of organizations.
- Explain strategy structure relationships
- Outline the role of SBU level executive
- Know what functional strategies are

Introduction

The true success of an organization depends upon effective formulation and implementation of strategies. According to Thomas Peters and Robert Waterman innovative companies are good at strategy implementation. Effective managers often work back and forth between

strategy formulation and strategy implementation. In this process, there is a need to understand the concept of Strategic Business Units (SBUs) and functional level strategies. There is a need to understand the hen and egg dilemma-strategy follows structure or structure follows strategy.

Strategy Management outcomes

Strategy formulation and strategy implementation when depicted on a matrix form suggests four probable outcomes of the four combinations of variables: Success, roulette, trouble and failure.

		STRATEGY FORMULATION		
		Good	**Poor**	
STRATEGY		Success	Roulette	**Good**
IMPLEMENTATION		Trouble	Failure	**Poor**

Success is the most likely outcome when an organization has a good strategy and implements it well. In this case, all that can be done to ensure success has been done. Environmental factors outside the company's control such as competitive reactions or customer changes may still make a strategy unsuccessful. However, organizational objectives have the best chance of being achieved in this cell.

Roulette involves situations wherein a poorly formulated strategy is implemented well. Two basic outcomes may ensue. The good execution may overcome the poor strategy or at least give management an early warning of impending failure. Perhaps the field sales force recognizes a problem in the strategy and changes its selling approach to a more successful one. Alternatively, the same good execution can hasten the failure of the poor strategy. Thus, it is impossible to predict exactly what will happen to strategies in the roulette cell, and that's where it gets its name.

The trouble cell is characterized by situations wherein a well-formulated strategy is poorly implemented. Because managers are more accustomed to focusing on strategy formulation, the real problem with the strategy – faulty implementation-is often not diagnosed. When

things go wrong, managers are likely to reformulate the strategy rather than question whether the implementation was effective. The new (and often less appropriate) strategy is then re-implemented and continues to fail.

Failure is the most likely to occur when a poorly formulated strategy is poorly implemented. In these situations, management has great difficulty getting back on the right track. If the same strategy is retained and implemented in a different way, it is still likely to fail. If the strategy is reformulated and implemented the same way, failure remains the probable result. Strategic problems in this cell of the matrix are very difficult to diagnose and remedy. The analysis of the matrix makes two things clear.

- First, strategy implementation is at least as important as strategy formulation.
- Second, the quality of a formulated strategy is difficult to assess in the absence of effective implementation.

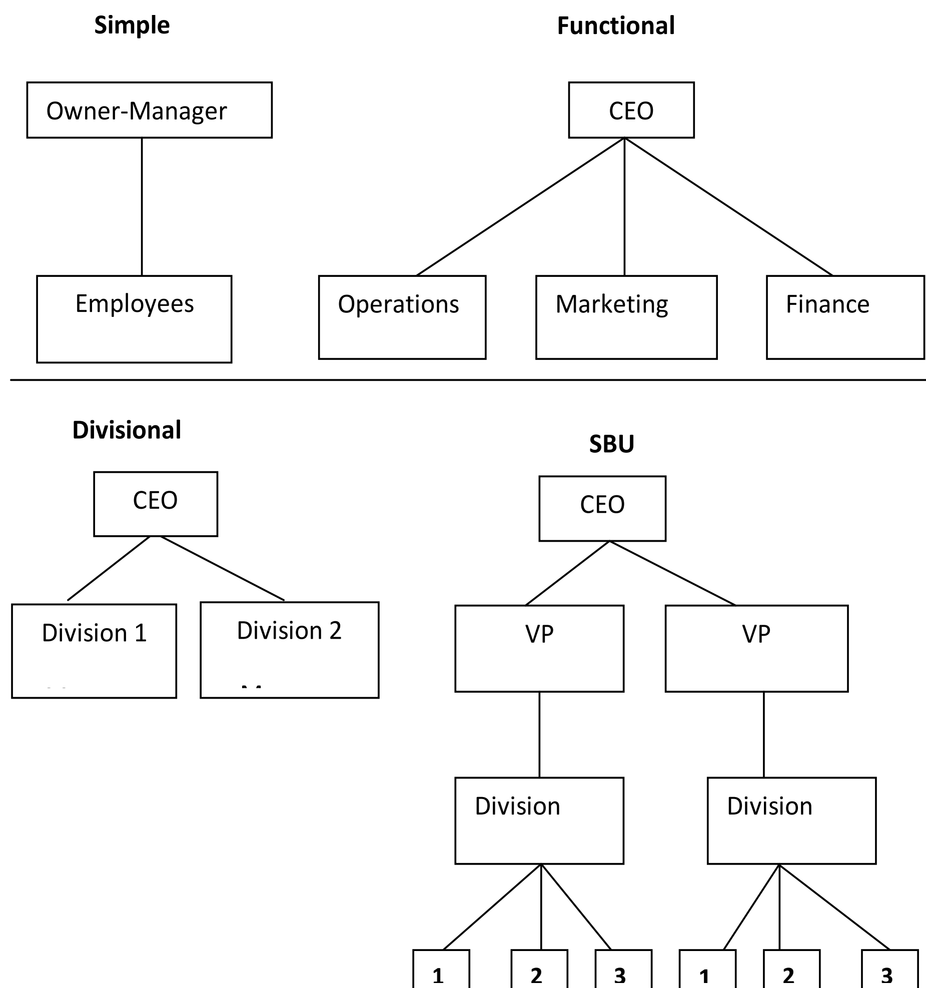
Evolution of Structures

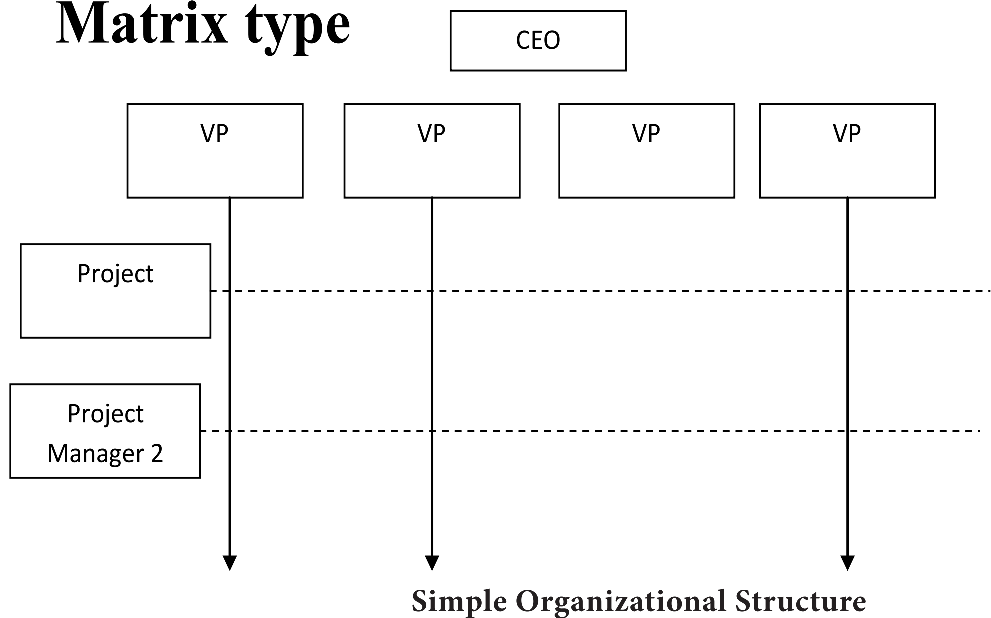
A firm's organizational structure is a formal configuration that largely determines what the firm will do and how it will complete its work. Different structures are required to implement different strategies. A firm's performance increases when strategy and structure are properly matched. Business-level strategies are usually implemented through the functional structure. The cost leadership strategy requires a centralized functional structure-one in which manufacturing efficiency and process engineering are emphasized. The evolution from the functional structure to the three types of multidivisional structure (M-form) occurred from the 1920s to the early 1970s. The cooperative M-form, used to implant the related-constrained corporate-level strategy, has a centralized corporate office and extensive integrating mechanisms. Divisional incentives are linked to overall corporate performance. The related-linked SBU M-form structure establishes separate profit centers within the diversified firm.

Types of Organization Structures

Two basic kinds of organizational structures exist-Formal and informal. There is the formal organizational structure which represents the relationships between resources as designed by management. The formal organizational structure is conveyed in the organization chart. Then there is the informal organizational structure, which represents the social relationships based on friendships or interests shared among various members of an organization. The informal organizational structure is evidenced in the patterns of communication commonly called the "grapevine." The informal network can be used to encourage rapid execution of strategies.

In formal organization structure there is the question of what management levels and personnel with the organization will be responsible for various implementation tasks. The five types of organizational structures that are commonly seen are the simple, functional, divisional, strategic business unit (SBU), and matrix structures. A schematic diagram of each of these structures is shown in Figure 4-1





Simple Organizational Structure

Figure 4-1 Different organization structures

A simple organizational structure has only two levels, the owner-manager and the employees. Small firms with one product or only a few related ones usually exhibit this structure.

Functional Organizational Structure

As organizations grow and develop a number of related products and markets, their structures frequently change to reflect greater specialization in functional business areas. Such line functions as production and operations, marketing and research and development (R&D) may be organized in departments.

Divisional Organizational Structure

As firms acquire or develop new products in different industries and markets, they may evolve a divisional organizational structure. Each division may operate autonomously under the direction of a division manager, who reports directly to the CEO. Divisions may be formed on the basis of product lines (automotive, aircraft), markets (customer, industrial buyers), geographic areas (north, south, international), or channels of distribution (retail store, catalog sales). Each division not only has its own line and staff functions to mange but also formulates and implements strategies on its own with the approval of the CEO.

Strategic Business Unit Structure

When a divisional structure becomes unwieldy because a CEO has too many divisions to manage effectively, organizations may reorganize in the form of strategic business units (SBUs) or strategic groups. This structure groups a number of divisions together on the basis of such things as the similarity of product lines or markets. Vice presidents are appointed to oversee the operations of the newly formed strategic business units, and these executives report directly to the CEO.

Matrix Organizational Structure

A matrix organizational structure is used to facilitate the development and execution of various programs or projects. Each of the department vice presidents listed at the top has functional responsibility for all the projects, whereas each of the project managers listed down the side has project responsibility for completing and implementing the strategy. This approach allows project mangers to cut across departmental lines and can promote efficient implementation of strategies.

The advantages and disadvantages of the different structures are presented below.

Simple	
Advantages	**Disadvantages**
1. Facilitates control of all the business activities. 2. Makes possible rapid decision-making and ability to change with market signals. 3. Offers simple and informal motivation/reward/control systems.	1. Relies totally on the owner-manger 2. Grows increasingly inadequate as volume expands. 3. Does not facilitate development of future managers 4. Owner-manager is forced to focus on day-to-day matters and not on future strategy.

Functional	
Advantages	**Disadvantages**
1.Boosts efficiency through specialization 2.Fosters improved development of functional expertise 3.Differentiates and delegates day-to-day operating decisions 4.Sharply focuses on accountability for performance 5.Retains functional specialization within each division 6.Serves as good training ground for strategic mangers.	1.Promotes narrow specialization and potential functional rivalry or conflict 2.Fosters difficulty in functional coordination and inter functional decision making 3.Can occasion staff-line conflict. 4.Limits internal development of general managers.

Strategic Business Units	
Advantages	**Disadvantages**
1.Tightens the strategic management and control of large, diverse business enterprises. 2.Facilitates distinct and in-depth business planning at the corporate and business levels. 3.Channels accountability to distinct business units.	1.May increase dysfunctional competition for corporate resources 2.May make defining the role of the group vice president difficult 3.May increase difficulty in defining the degree of autonomy for the group vice presidents and division mangers

Decision-Making Hierarchy Of Business Firms

The decision-making hierarchy of business firms typically contains three levels as shown in Figure 4.2 At the top is the corporate level, composed principally of members of the board of directors and the chief executive and administrative officers. They are responsible for the financial performance of the corporation as a whole and for achieving the

non-financial goals of the firm, for example, corporate image and social responsibility.

Matrix	
Advantages	**Disadvantages**
1.Accommodates a wide variety of project oriented business activity. 2.Serves as good training ground for strategic managers. 3.Maximizes efficient use of functional managers. 4.Fosters creativity and multiple sources of diversity. 5.Provides broader middle management exposure to strategic issues for the business.	1.Can create confusion and-contradictory policies by allowing dual accountability. 2.Necessitates tremendous horizontal and vertical coordination.

The second rung of the decision-making hierarchy is the business level composed principally of business and corporate mangers. These managers must translate the general statements of directions and intent generated at the corporate level into concrete, functional objectives and strategies for individual business divisions or SBUs. In essence, business-level strategic mangers must determine the basis on which a company can compete in the selected product-market arena.

The third rung is the functional level, composed principally of managers of product, geographic, and functional areas . It is their responsibility to develop annual objectives and short-term strategies in such areas as production, operations, and research and development; finance and accounting, marketing: and human relations. However, their greatest responsibilities are in the implementation or execution of a company's strategic plans. While corporate and business-level managers centre their planning concerns on "doing the right things," managers at the functional level must stress "doing things right." Thus, they directly address such issues as the efficiency and effectiveness of production and marketing systems, the quality and extent of customer service, and the

success of particular products and services in increasing their market shares.

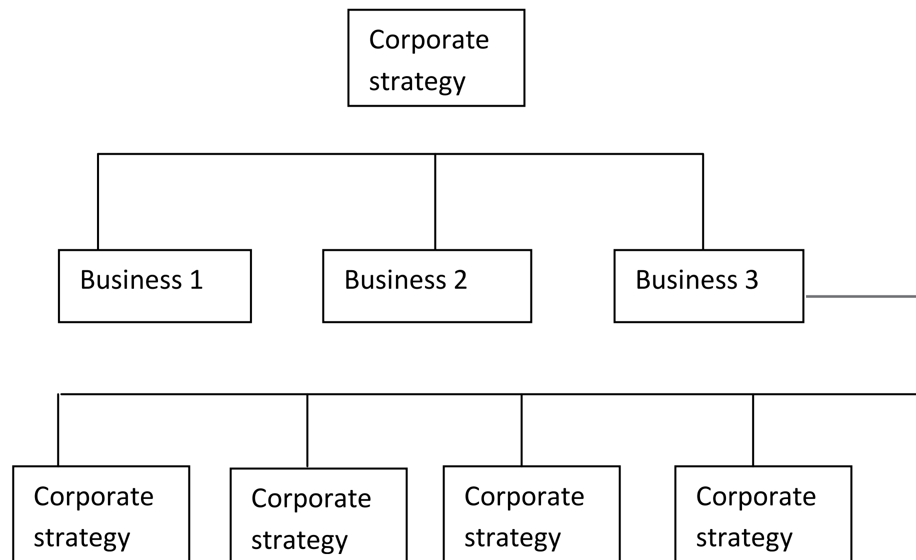


Figure 4.2 Decision Making hierarchy

Table 4-1 depicts the characteristics of strategic management decisions at different levels. Examples of corporate-level decisions include the choice of business, dividend policies, sources of long-term financing, and properties for growth. Functional-level decisions usually determine actions requiring minimal company wide cooperation. These activities supplement the functional area's present activities and a re adaptable to ongoing activities so that minimal cooperation is needed for successful implementation. Business –level descriptions of strategic decisions fall between those for the other two levels. For example, business-level decisions are less costly, risky, and potentially profitable than corporate level decisions, but they are more costly, risky, and potentially profitable than functional-level decisions. Some common business-level decisions involve plant location marketing segmentation and geographic coverage, and distribution channels.

Table 4-1 Characteristics of strategic management decisions at different levels

Level of strategy			
Characteristic	**Corporate**	**Business**	**Functional**
Type	Conceptual	Mixed	Operational
Measurability	Value judgments dominant	Semi quantifiable	Usually quantifiable
Frequency	Periodic or sporadic	Periodic or sporadic	Periodic
Adaptability	Low	Medium	High
Relation to present activities	Innovative	Mixed	Supplementary
Risk	Wide range	Moderate	Low
Profit potential	Large	Medium	Small
Cost	Major	Medium	Modest
Time horizon	Long range	Medium range	Short range
Flexibility	High	Medium	Low
Cooperation required	Considerable	Moderate	Little

Corporate Level Strategy And Structure Combinations

The need for having the right structure for implementation of strategy need not be over emphasized. Cost. The structural characteristics of specialization, centralization, and formalization play important roles in the successful implementation of the cost leadership strategy. Specialization refers to the type and number of job specialties that are required to perform the firm's work. For the cost leadership strategy, mangers divide the firm's work into homogeneous subgroups. The basis for these subgroups is usually functional areas, products being produced, or clients served. By dividing and grouping work tasks into specialties, firms reduce their costs through the efficiencies achieved by employees specializing in a particular and often narrow set of activities. Additional characteristics of the form of the functional structure used to implement the differentiation strategy are shown in Figure 4-4

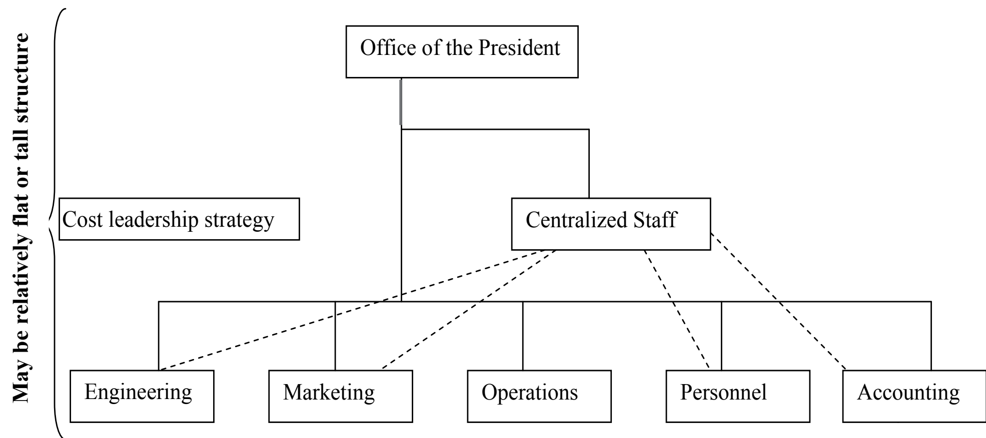
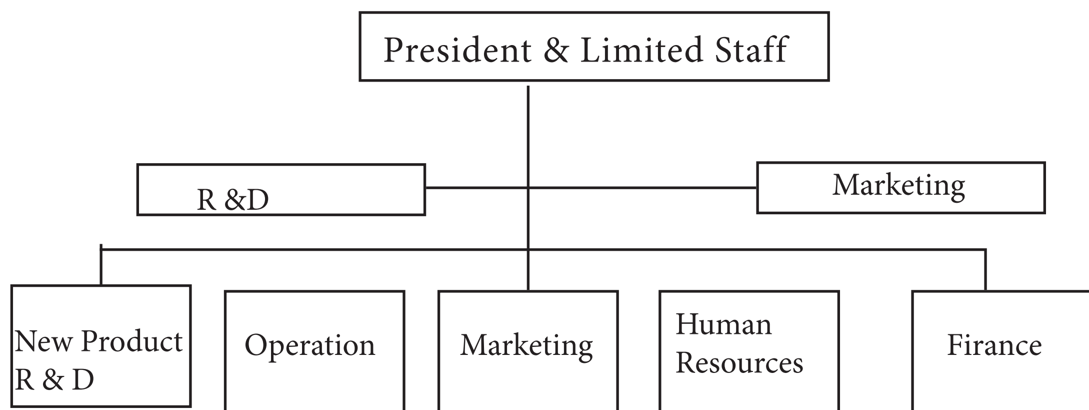


Figure 4-3 Functional organization for cost leadership strategy



Notes:

- Marketing is the main function for keeping track of new product ideas
- New product R & D is emphasized
- Most functions are decentralized, but R & D and marketing may have centralized staffs that work closely with each other.
- Formalisation is limited so that new product ideas can emerge easily and change is more readily accomplished.

Overall structure is organic. Job roles are less structured.

Role of SBU Level Executives

The role of SBU level executive is very important to strategic management since each product-market segment has a unique strategy. These executives are profit centre heads or divisional heads and are

considered the chief executives of a defined business unit for the purpose of strategic management. An SBU level executive wields a lot of authority within the SBU and also works in coordination with other SBUs.

Many public and private sector companies have adopted the SBU concept in some form or the other "There are several family-managed groups today who boast of their professionally-managed organizations structure. Each of their companies has a chief executive who has total responsibility and authority over the profit center.

Strategic planning at MRF Ltd used senior management expertise by dividing them into five groups dealing with products and markets, environment, technology, resources, and manpower. Each group had a leader who helped to prepare position papers for presentation to the board. The executive directors in the company were actively involved in SWOT analysis through the help of managers and assistant managers.

At Shriram Fibers, the strategic planning system covered the different businesses ranging from nylon yarn manufacture to the provision of financial services. Strategic plans were formulated at the level of each SBU as well as at the corporate level. The corporate planning department at the head office coordinated the strategic planning exercise at the SBU-level. Each SBU had its own strategic planning cell

Functional Strategies

Functional strategies which are short-term game plans for the key functional areas are the means to accomplish the annual plans. Functional strategies by clearly specifying the various measures to be taken in different functional areas in different time horizons help operationalize the grand strategy. In other words, functional strategies provide the short-term operational details for accomplishing the long term objectives systematically. Pearce II and Robinson Jr. (1988) maintained

"Functional strategies help in implementation of grand strategy by organizing and activating specific subunits of the company (marketing, finance, production, etc) to pursue the business strategy in daily activities. In a sense, functional strategies translate thought (grand strategy in to action designed to accomplish specific annual objectives. for every major subunit of a company, functional strategies identify

and coordinate actions that support the grand strategy and improve the likelihood of accomplishing annual objectives."

Operationalizing the corporate strategy requires the development of functional strategies in key areas like marketing, production, R &D, finance and human resources. Figure.4.5 Illustrates annual objectives and functional strategies

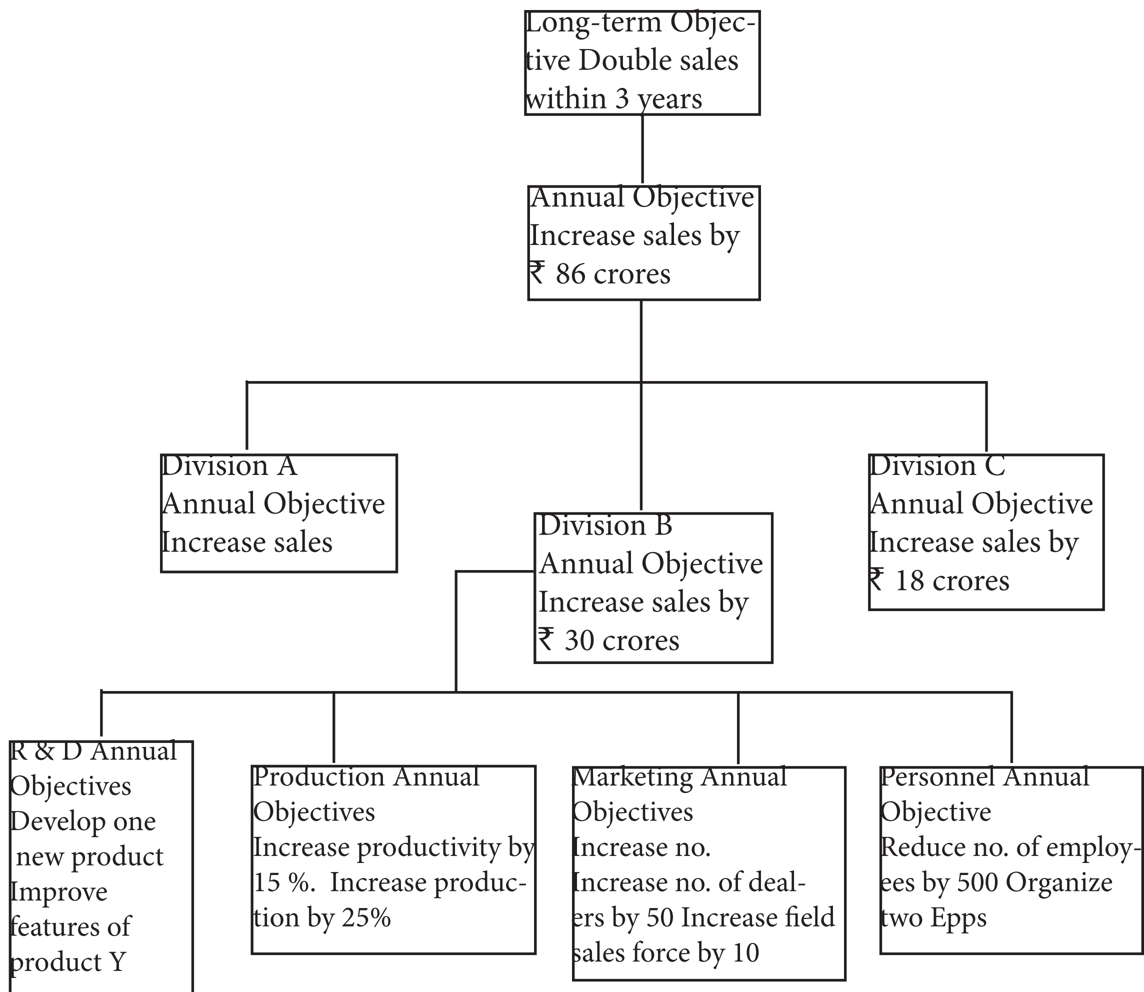


Figure.4.5 Annual Objectives and Functional Strategies

The annual objective is to increase sales by ₹ 86 crores. Strategies for this include, for example, increasing the sale of division A by ₹38 crores, division B by ₹ 30 croes, division C by ₹18 crores, developing a new product, intensifying promotion by increasing the size of the filed sales force, increasing the number of dealers etc.

The functional strategy for marketing must cover all the factors of the marketing mix. Mutually consistent strategies for each of the factors must be developed to help achieve the annual marketing objective.

R & D strategy may involve improving product or packing, developing new product etc.

Similarly every key functional area must develop strategies to achieve the annual objectives. The functional strategies are discussed in detail in unit III of this study material for all the functional areas viz., R & D operations, finance, human resources, logistics, information systems and marketing

Summary

The true success of an organization depends upon effective formulation and implementation of strategies. There is a need to understand the hen and egg dilemma-strategy follows structure or structure follows strategy. Strategy formulation and strategy implementation when depicted on a matrix form suggests four probable outcomes of the four combinations of variables: Success, roulette, trouble and failure. Designing sound organization structures would enable strategists to accomplish the implementation of strategies in a proper way. There are four types of organization structures. The five types of organizational structures that are commonly seen are the simple, functional, divisional, strategic business unit (SBU), and matrix structures. Decision making in the hierarchy is found at three levels – corporate, business and functional. Functional strategies enable the implementation of corporate level strategies.

Self Assessment Questions

1. Why is it important that strategy implementation and strategy formulation be integrated carefully?
2. What is the meaning of the following statement? “In organizations, there is a consistent path of structure following strategy and then strategy following structure.”
3. Explain the different types of organizational structures and state their merits and demerits.

4. Why do you think divisional organization is necessary for strategic management ?
5. Explain the relevance of matrix structures for corporate strategies
6. What type of organizational structure is used to implement the cost leadership, and differentiation ?
7. What organizational structures should be used to implement the multi domestic, global, and transnational international strategies?
8. Explain the decision making hierarchy in an organization.
9. What is Strategic business unit and what type of leadership is required?
10. Explain the significance of functional strategies.

Activities

1. From the management journals collect two articles on corporate strategy and structure and draw conclusions on the question whether strategy follows structure.
2. From the internet identify the structure and strategy elements of two organizations and prepare a paper on strategy decision making in modern enterprises

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UNIT- II

Lesson 5 - Environmental Analysis

Lesson Outline

- Introduction
- Concept Of Environment
- Taxonomy Of A Firm's Environment
- Macro Environment Analyzed
- Impact Of Macro Environment On Business
- Environment And Strategic Analysis
- Environmental Changes In India
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand the concept and different types of environment
- Examine the elements of external environment and their influences on business
- Know how strategic analysis and response takes place relating to environment

Introduction

Business organizations operate in a turbulent environment and the changes in the environment impacts business. The changes that take place in the internal and external environments impinge on the policy

decisions of business enterprises and cast profound influence in their working and efficiency. The external environmental factors are in a continual flux creating new opportunities and new threats to the company. They are always capable of producing major shocks, which Peter Drucker has called as, “an Age of Discontinuity.” In order to survive and succeed a company must consider and understand the environment and make policies to adopt to or alter the environment.

Concept of Environment

Unilever recently sued Proctor & Gamble (P&G) over that company’s corporate espionage activities to obtain the secrets of its Unilever hair-care business. After spending $3 million to establish a team to find out about competitors in the domestic hair care industry, P&G allegedly took roughly eighty documents from garbage bins outside Unilever’ s hair-care brands such as ThermaSilk, Suave, Salon Selective, and Finesse.

Prof. Keith Davis defines business environment as, “the aggregate of all conditions events and influences that surround and affect it.” These surroundings are constantly changing and uncertain.

Unilever recently sued Proctor & Gamble (P&G) over that company’s corporate espionage activities to obtain the secrets of its Unilever hair-care business. After spending $3 million to establish a team to find out about competitors in the domestic hair care industry, P&G allegedly took roughly eighty documents from garbage bins outside Unilever’ s hair-care brands such as ThermaSilk, Suave, Salon Selective, and Finesse.

Taxonomy of a Firm’s Environment

The total environment can be classified into two broad categories

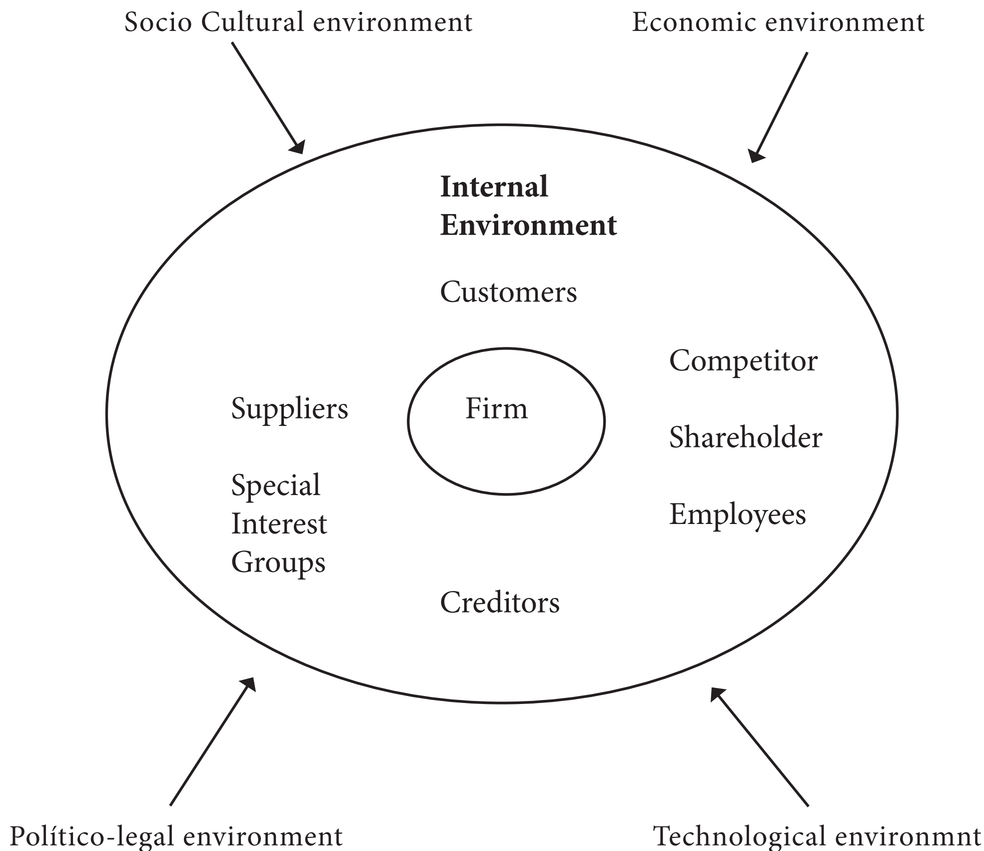
- Internal environment
- External environment

The internal environment includes the goals and value system, the hierarchical authority structure, the technological equipment and processes, the social groups and teams, the management groups, organizational climate and culture,etc.

The external environment can be classified into two segments.

- Macro environment or Mega environment, or
- Micro environment or task environment.

Figure 4-1 Environment types



Macro Environment

Also referred to as general or remote environment, Mega' environment, skirts the 'micro', or the relevant environments.The major constituents of mega environment are PEST or STEP (P refers to Politico-legal environment, E-Economic environment, S-Socio-cultural environment and T-Technological environment) or PESTEL (Political, environmental, socio-cultural, technological, economic and legal). These environments can further be classified into international, regional, national etc. Thus, depending upon the situation, an analyst may refer to the global economic environment, the regional political environment or the national social environment.

Micro Environment

Microenvironment includes employees, shareholders, creditors, suppliers, customers and financial institutions, regulatory organizations, channels of distribution, and special interest groups like consumer associations, and community organizations. This environment has a substantial impact on an organization's current business. Consequently, developments in microenvironment become the dominant preoccupation of the management for strategic decisions. To avoid obsolescence and promote innovation, a firm must be aware of technological changes that might influence its industry.Creative technological adoptions can improve manufacturing and marketing techniques.

A company like L& T which has diversified product mix like machinery for cement, switchgear, material handling equipment, machinery for dairy plants, computer peripherals etc., may have many 'micro' environments. Only necessary information should be gathered by L & T from the relevant environment.

Macro Environment Analyzed

Now, we will examine the various factors in the macro environment and identify the type of impact they make on business organizations.

Socio -Cultural Environment

The socio cultural environment is one of the key elements of macro environment. Figure 4-3 lists the key variables in this environment. Demographics like literacy rates, sex ratios, child birth rates, age distribution, educational levels life style, geographic distribution, mobility of the pollution cultural variables like beliefs, values, faiths, religion, customs and traditions, environment folkways, etc., are part of the social changes in society may be slow or fast but change is inevitable in any business environment. Examples in the Indian business environment include –

- Growing fast food culture
- Women moving from kitchens to corporate
- Burgeoning middle class
- Increasing literacy levels
- Declining birth rates and increasing senior citizens

- Increasing health consciousness

Socio-cultural factors affect buying preferences, usage patterns and life style adaptations. Firms, which ignore the socio cultural environments, tend to loose.

McDonalds, the world's fastest growing fast food chains extended Indian market with beef and pork as ingredients in its pizzas and burgers. Since Hindus are religiously against cow slaughter and do not consume beef and Muslims hate pork these was great opposition in Bombay and the local shiv sena activities broke down McDonald's fast food center at Mumbai. Today the company relaunched its products with 'no beef and no pork' sign boards and even gave wide publicity that animal fat is not used in its restaurants. Further to Indianise its products new versions for Indians like Mc. Imli (with tamarind), Mc spic (with Indian spices) etc are introduced exclusively for Indian market.

Peculiar usage forms include:

Vicks Vaporub is used as a mosquito repellent in some tropical countries. Hair dyes are used for marking animals and washing machines for making Lassi in some rural areas of Punjab.

Key Social, Cultural and Demographic Variables

1. Childbearing rates
2. Number of specific interest groups
3. Birth and death rates
4. Life expectancy rates
5. Attitude towards work and organization
6. Attitude towards government
7. Attitude towards authority
8. Ethical norms
9. Value system
10. Composition of work force
11. Attitude towards income, savings and capital formation
12. Social ethos towards work and organization

Technological Environment

Technology is knowledge to create new things. Mangers need technology to design, produce, distribute and sell goods and services. Impact of technology is mixed. Positive benefits are seen in new products, new machines, new tools, new materials and services. Benefits include greater productivity, higher living standards, more leisure time and greater variety of products. Ex: Range of cars – subcompacts, compacts, intermediates, sports, specialty, variations in engine power, steering A/c, speed control, roof etc. Negative effects include pollution, energy shortage, loss of privacy, traffic jam etc. A balanced approach is therefore needed.

Xerox dominated the world photocopier market with 93 percent of the market share. It guarded its technology with over 500 patents. Cannon was a camera company from Japan that entered into this business around 1970. It did not have the process technology to by-pass Xerox's patents. Yet over the next three decades, Canon rewrote the rule book of how copiers were to be produced and sold. Canon's copiers are a business of around Rs.300,000 crore in annual revenues and it sells more copiers than Xerox does. Canon succeeded, not by coping Xerox, but Canon believed that individuals and small businesses would find the product useful if only they could afford it. The technology appropriate for this product would therefore be different from Xerox's patent protected technologies.

In 1975, revolutionary technological changes and discoveries have brought about dramatic impact of organizations. Among such discoveries mention may be made of super conductivity, computer engineering, "thinking" computers, robotics, unmanned factories, miracle drugs, fiber optics biometrics and electronic funds transfer. Superconductivity is expected to revolutionize business operations especially in such areas as transport, utility, health care, electrical and computers.

Technological Change is of Two Types

Convergent change - where incremental innovation and improvement optimizes the ability of the organization to succeed in the existing environment. In India this change occurs in 10-12 years, in western firms five to six years and in Japan it is four years. Presently

some Japanese firms like Nissan make changes from 14 months to 2 years time.

Divergent change – Involves changes where the framework of the organization undergoes discontinuities. Whether it is in response to events over which the corporation has no control, like deregulation, major shift in economic policies, nationalization or events related to radical changes in technology like product life cycle shifts, new process technologies, radical innovations, etc., these changes involve organizational re-formation or transformation. Example includes replacement of Swiss mechanical watches with high innovation by simple battery operated electronic watches. Some of the winners and losers of technological changes are given in the following Table 4-1.

Table 4-1: Disruptive Technologies : Winners and Losers

Dominant Firm	Product	Disruptive Technology	Winning Challengers
GM and Ford	Small cars	Japanese quality & manufacturing expertise	Totyoto and Honda
Gillette	Razor blades	Stainless steel technology	Wilkensen
Gillette	Cheap razors	Plastic technology	Bic
Parker	Fountain pens	Ball point pen technology	Timex
Swiss watchmakers	Time pieces	Lever-action watch technology	Timex
Timex	Watches	Electronic technology	Casio. Etc.

Economic Environment

The various forces of economic environment can be explained as follows.

- Capital –machinery, buildings, investments office equipment, tools and cash. Business organizations issue shares and debentures and borrow from commercial banks.
- Labour –availability of skilled labor at affordable wage rates. US companies are outsourcing from India because labor is very cheap here.
- Prices – The price changes caused by business cycles are a major

concern. The price raise in one industry affects the other ones. It is like a chain reaction. It reduces the buying power of consumers and reduces demand.

- Government Fiscal and tax policies – Government's control on availability of credit through fiscal policy has considerable impact on business. If business profit taxes are high, the interest to go into business gets marginalized. If sale, tax is high people don't buy.

- Customers- Customers are the foundation of business. Business must serve the public. People want value for the money they pay and service that satisfy their needs. Companies are customizing products to specific groups or individuals. Refrigerator companies are introducing bare bone models for the low income groups. Auto companies are opening up service centers. Also thee are CRM (customer relationship management) programs in many organizations today.

- General Economic Conditions - The general economic conditions like national income, per capita income, economic resources, distribution of income and assets, economic development, etc. are important determinants of the business strategies. In countries and regions where income of people is low, the demand for the product will be low. It discourages the companies to enter the market. However in economies where the income of people is rising and hence business prospects will be brighter; investment will get automatic attraction. Recently growing income of middle class in India, encouraged foreign investors to operate in India.

- Economic Systems. All business organizations operate in at least one type of economic system-socialist, communist and capitalistic. In capitalistic type of economic system, free play of market mechanism takes place, whereas in state-controlled economies, there are restrictions, on the private sector's role. It has been noticed that with the collapse of communist Soviet Union multinational corporations are searching their market in East European Countries.

- Economic Policies. The economic policies of the government have tremendous impact on the business. For example, in India, before July 1991 public sectors were encouraged to play dominant role to achieve commanding heights of the economy; as a result competition was not there. With the new economic policies of liberalization and

globalization, the era of protectionism and preferential treatment is giving way to competition and cost-consciousness.

- Economic Growth The general economic growth in the economy has direct impact on the business strategies. Increased economic growth rate, leading to increase in consumptions, expenditure, lowers the general pressure within an industry and offers more opportunities than threats. On the other hand, decline in economic growth reduces consumer expenditure , that leads to competitive pressures and threatens the profitability.

- Interest rates. The rate of interest affects the demand for the products in the economy, particularly when general goods are to be purchased through borrowed finance. If the interest rate is low, the demand for certain products like autos, appliances, capital equipments, housing materials, etc. will rise. This provides good opportunity for these industries to expand whereas rising interest rates pose a threat to these industries. Interest rates also determine the cost of capital of the company. When rates of interests are lower, companies can adopt ambitious strategy with borrowed funds.

- Currency exchange rates. Currency exchange rates have direct impact on the business environment. When the rupee was devalued in 1991, it was to make Indian products cheaper in the world market and consequently boost India's exports. That was a great opportunity for Indian exporters.

- Taxes- the imposition of taxes like income tax, sales tax and excise duties have impact on business. The chocolate manufactures in India suffered a set back in the new millennium when the excise duty on confectionery items increased from 8 to 16 percent. Nutrine Confectionery company which sells a popular brand of chocolate called 'Aasey' with a price of 0.25 paise to had to increase its price from 0.25 paise had 0.50 paise since the price cannot be increased by 0.04 paise due to coinage problem. A child who goes to nearly kiosk with 0.25 paise used to return home to his mother without a chocolate. It took three months for the customers (children) to adjust to the new price and the company lost crores of rupees it gets from Children's pocket money.

Politico- Legal Environment

The various forces in political and legal environment direct and restrict business decision-making.

Political environment – Attitudes of Government and legislators change with social demands and beliefs. Government affects every aspect of life. For instance, strong pollution norms many result in closure of a company. Government not only promotes but also constrains business. Promotion is possible by stimulating economic extension and development, by providing subsidies to SSIs, tax advantages, support to R&D and protecting business in priority sector. Also, government can be the biggest customer. The public announcements of government, the observations in plan documents indicate government policies. E.g.: Industrial policy resolution, 1948 and the economic policy, 1991.

Several European Countries restrain the use of children in commercial advertisements. In India advertisement of cigarettes must carry the statutory warning that "Cigarette smoking is injurious to health."

The prevalence of political uncertainty has effect on the business strategies. In the presence of political uncertainty, no business likes to commit itself for long term strategies or investments while the uncertainty countries. Therefore the companies focus more on preparing alternative plans for different emerging situations.

Legal environment – It consists of judiciary and legislation. It constrains and regulates business. There are several legislation like the Company act 1956, the Payment of wages Act, 1936 and Factories Act 1948. There are judiciary arrangements like courts and tribunals.

Indian business environment is undergoing a sea change since 1991 after economic reforms were introduced. Fredrick Gluck, Director of Mckinsey & Company concludes his observations in the following words:

"It is no exaggeration that in an industry that is, or is rapidly becoming global, the riskiest possible posture is to watch as more aggressive companies use this growth to capture economies of scale and learning. The domestic competitor will then be faced with an attack

on domestic markets using different (and possibly superior) technology, product design, manufacturing, marketing approaches, and economies of scale. A few examples suggest how extensive the phenomenon of world markets has already become. Hewlett Packard's manufacturing chain reaches half-way around the globe, from well paid, skilled engineers in California to low range assembly in Malaysia. General Electric has survived as a manufacturer of inexpensive audio products by centralizing its world production in Singapore.

A number of measures have been announced to facilitate private entry into areas of infrastructure which were formerly the prerogative of the public sector with a view to freeing scarce public resources for social sector. These include natural resource sectors, and non-tradable infrastructure services such as electricity, internal transport telecommunications.

1. The National Mineral Policy was revised and the Mines and Mineral Development Act amended to open up this sector to private and foreign investment. Thirteen minerals were de-reserved for exploitation by the private sector.
2. The R.B.I passed automatic approval policy for foreign investment was made applicable to mining (except for atomic minerals and mineral fuels) subject to a limit of 50% on foreign equity.
3. The power sector policy framework attracted 138 private proposals for creating 58,745 mega watts of capacity with an investment of Rs.2,19,927 crores. Of these, 41 proposals are from foreign investors or are joint ventures with foreign partners, of which thirteen have already been cleared by the government.
4. The National Tele-communication Policy, 1994 allows private provision of basic telecom services. Implementation has begun after announcement of rules and procedures.
5. The New Air Corporation Act, 1994 enables private Air Taxi Companies to operate as regular domestic airlines. Nine Air Taxi operators, complying with Aircraft Rules have been granted "scheduled airlines" status.
6. The National Highway Act, has been amended to enable levy of tolls on national highway users. Government intends further amendment of the Act of allow private participation in construction, maintenance and operation of roads on Build-operate-Transfer (BOT) basis.

Natural Environment

Geographical and ecological factors, such as natural resources endowments, weather and climatic conditions, topographical factors, location aspects in the global context, port facilities etc., are all relevant to business. Differences in geographical conditions between markets may sometimes call for changes in the marketing mix. Geographical and ecological factors also influence the location of certain industries.

Natural Resource Availability

For example, industries with high material index tend to be located near the raw material sources. Climate and weather conditions affect the location certain industries like the cotton textile industry in Mumbai, Ahmedabad and Coimbatore. Topographical factors They may affect the demand pattern.

For example, in hilly areas with a difficult terrain, jeeps may be in greater demand than cars.

Ports - Air ports and seaports offer an advantage in transport. Many commercial cities are those, which have this port advantage.

In India business has flourished near ports. For example, Visakhapatnam in Andhra Pradesh, which has a natural harbour, has many major industries like BHPV, steel plant, Hindustan Shipyard, Coromandel Fertilizers etc., located there due to the advantage of port.

Green concerns Government is becoming increasingly concerned about protecting the environment. Use of plastic bags is banned in several states and Union Territories like Andhra Pradesh and Sikkim. Government is investing on water harvesting schemes to conserve ground and natural water resources Cliamtic conditions Variations in climatic conditions cause differences in demand for goods.

More number of air conditioners and refrigerators are sold in the South India during summer due to warm weather. Impact of macro environment on business The trends in mega environment, from the viewpoint of a company, have long-term implications. Figure 4-2 shows some of the trends that impacted business.

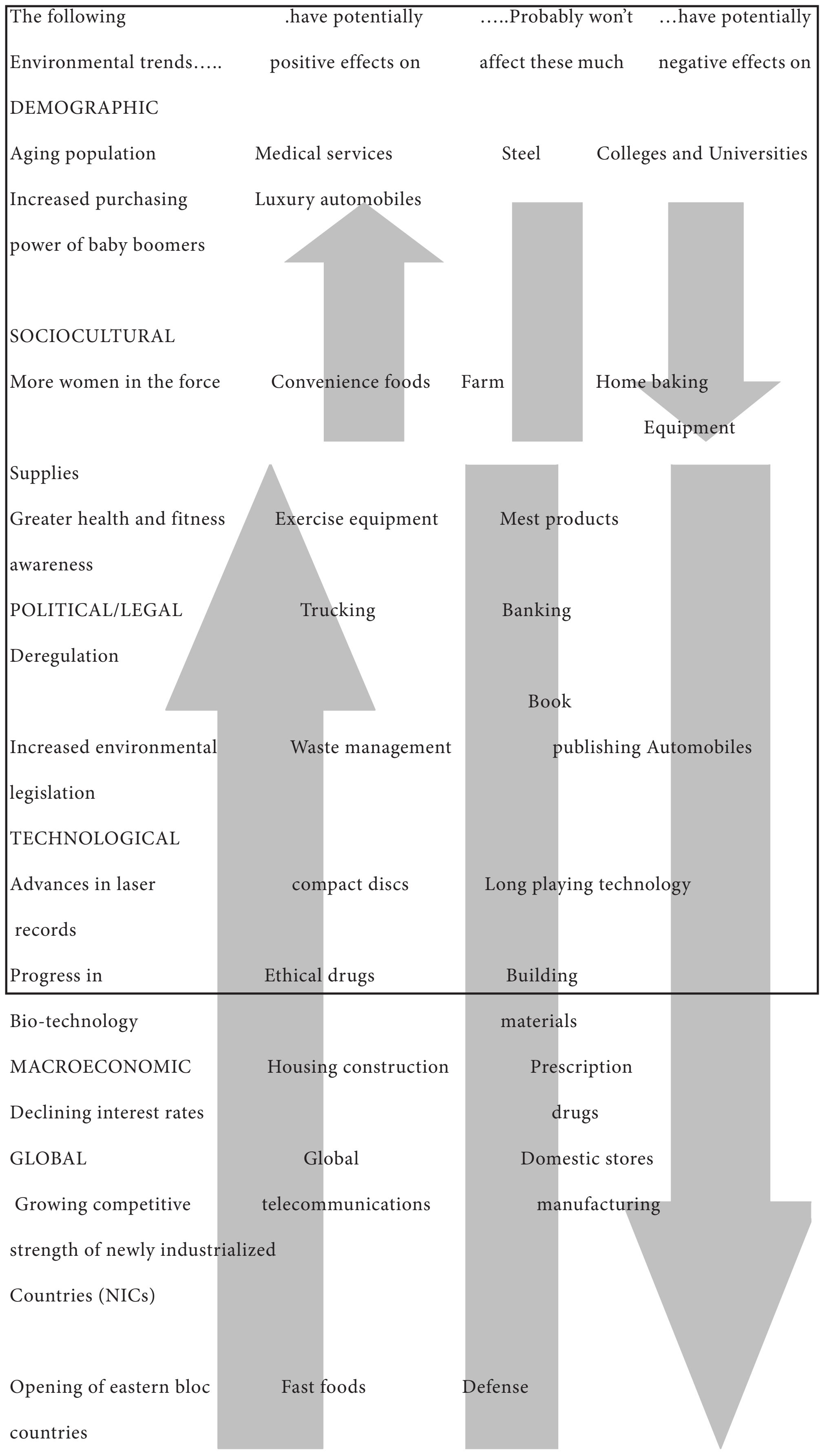


Figure 4-2: Trends in Environment and Their Impact

(Source: Alex Miller and Geogory G. Dess(1996), Strategic Management McGraw -Hill, New York, p. 61.)

Environment and Strategic Analysis

By the very principle of its operation, industry never reaches a point of equilibrium. Strategic analysis provides the framework on study, forecast, anticipates and prepares the organization to tackle the challenges posed by the changes, head on.

Organizations have to recognize the dynamic nature of the environment in which they operate. The environment is affected by a number of factors that include events and influences from a number of sources, resulting in a complex play of forces that are not easy to analyze in their totality.

Internal factors are those over which the business enterprise can exercise its control and are regarded as controllable variables. External environmental factors are regarded as uncontrollable factors. As the external factors of environment are beyond the control of a business enterprise, its progress, success and survival largely depends upon its capacity and ability to adapt successfully to environmental changes. In order to do this, it will have to reorganize, readjust its controllable internal factors to suit the external business environment.

Effective strategic management begins with assessment of business risk. Business risk arises as much from the likelihood that something good will not happen as it does from the threat that something bad will happen. Each organization has its own unique set of business risks and these risks keep changing constantly. Some risks are external, e.g. competitors, economic conditions, and capital availability etc. Others are internal, resulting from the company's own organization, processes, products, and relationship with customers, shareholders, suppliers and employees; information; and contractual commitments.

There are two mainstreams of thought on strategy. These are represented by the 'fit' concept of the 'positioning school' and the 'stretch' concept of the resource based' school. Each of these schools views strategy differently, as a result of which strategic capability is also viewed differently.

The ‘Fit’ Concept

The traditional concept of organizational strategy is based on the ‘fit’ concept. This concept is propagated by the ‘positioning’ school and more particularly by Michael Porter in his development of the theory of competitive strategy. According to this, strategies should aim at achieving fit between environment and organizations.

The ‘Stretch’ Concept

Gary Hamel and C.K. Prahlad opined that the conventional framework of strategy using the ‘fit’ concept is incomplete as a strategy for the organization. Though the long-term strategy should have a consistency and purpose and supplement the idea of ‘fit’, the importance of competitive strategy is not about how the organization fits its strategy to match its resources, but about how the organization marshals its resources. They said, “competitiveness is born in the gap between a company’s resources and its managers goals. “The long term competitive success depends on managers’ willingness to continually challenge their existing frames of reference. Leveraging resources can do this. Leveraging resources is as important as allocating them. This concept of leveraging resources so as to extend the capabilities of the organization and its competitiveness is called ‘stretch’.

Summary

Business organizations are subject to its internal and external environmental factors. The internal factors are its personnel, physical facilities, organization structure, production system, marketing mix, technical facilities etc. These internal factors are those over which the business enterprise can exercise its control and are regarded as controllable variables.

The external factors are those over which the business organization has no control such as social and political atmosphere, economic environment etc. These environmental factors are regarded as uncontrollable factors. As the external factors of environment are beyond the control of a business enterprise, its progress, success and survival largely depends upon its capacity and ability to adapt successfully to environmental changes. In order to do this, it will have to reorganize, readjust its controllable internal factors to suit the external business

environment. There are two mainstreams of thought on strategy. These are represented by the 'fit' concept of the 'positioning school' and the 'stretch' concept of the resource based' school

Self Assessment Questions

1. What do you understand by environment? How do you classify it?
2. What is internal environment? Is it controllable?
3. What PESTEL means to you? Which of the external factors are controllable ?
4. What factors in social environment affect business and how?
5. Discuss the implications of political environmental forces in India?
6. Examine the impact of changing technology on business.
7. What are the major economic environmental factors?
8. Identify the major changes in Indian environment impacting domestic and foreign business.
9. How do strategists look at environment and take decisions?
10. Write a note on the long tem impact of microenvironment on business as given by Miller and Dess in the lesson.

Activities

1. Visit websites of any two companies and from the annual reports or publicity material and figure out the environment in which they are operating.
2. What steps are taken now a days by companies in response to green issues? Collect material from Vikalpa and other journals and make a 3 page report..

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Lesson 6 - Environmental Scanning Techniques

Lesson Outline

- Introduction
- Why Scanning?
- Techniques Of Scanning
- Issues Priority Matrix
- Environmental Threats And Opportunities Profile (Etop)
- Strategic Advantage Profile (Sap)
- Functional – Area Profile And Resource Deployment Matrix
- Swot Analysis
- The Opportunity And Threat Matrices
- The Impact Matrix
- The Impact Scale
- Gap Analysis
- Balanced Score Card
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand the importance of scanning techniques.
- Describe the different scanning techniques

Since the Strategic Advantage Profile is a summary statement of corporate capabilities, in summarizing the functional competencies a comparative view needs to be taken in the light of external conditions

and the time horizon of projections. For example, while comparing the level of inventory holding, one may find it to be relatively higher than that of competing firms; as such it should be regarded as a weakness. But if the market demand shows an increasing trend, apparent weakness should be considered strength.

III.Functional – area profile and resource deployment matrix.

Developed by Hofer and Schendel, this method requires the preparation of a matrix of functional areas with characteristics common to each, e.g., focus of financial outlay, physical resource position, organizational system, and technological capability. The functional area profile of a manufacturing company is given by way of illustration. Following this exercise, it is required that the resource outlay and focus of efforts over time in the respective functional areas be presented also in the form of a matrix.

Techniques of Scanning

There are various scanning techniques used by organizations

i. Issues Priority matrix

ii. Environmental Threats and opportunities Profile (ETOP)

iii. Strategic advantage profile (SAP)

iv. Functional – area profile and resource deployment matrix

v. SWOT Analysis

vi. The opportunity and Threat matrices

vii. The Impact Matrix

viii. The Impact scale

ix. Gap Analysis

x. Balanced Score card

i) Issues Priority Matrix (IPM)

One way to identify and analyze developments in the external environment is to use the issues priority matrix (Figure 8-1) as follows:

1. Identify a number of likely trends emerging in the societal and task environments. These are strategic environmental issues – those important trends that, if they occur, determine what the industry or the world will look like in the near future.

2. Assess the probability of these trends actually occurring from low to high.
3. Attempt to ascertain the likely impact (from low to high) of each of these trends on the corporation being examined.

Figure 8-1s

Issues Priority Matrix

Probable Impact On Corporation

Probability Occurrence	**High**	**Medium**	**Low**
High	High Priority	High Priority	Medium Priority
Medium	High Priority	Medium Priority	Low Priority
Low	Medium Priority	Low Priority	Low Priority

Source: L. L. Lederman, "Foresight Activities in the U.S.A: Time for a Re-Assessment?" Long – Range Planning (June 1984), p-46.

A corporation's **External Strategic Factors** are those key environmental trends that are judged to have both a medium to high probability of occurrence and a medium to high probability of impact on the corporation. The issues priority matrix can then be used to help managers decide which environmental trends should be merely scanned (low priority) and which should be monitored as strategic factors (high priority). Those environmental trends judged to be a corporation's strategic factors are then categorized as opportunities and threats and are included in strategy formulation.

II)Environmental Threats and Opportunities Profile (Etop)

Assessment of the environmental information and determining the relative significance of threats and opportunities require a systematic evaluation of the information developed in the course of environmental

analysis. For this purpose, preparation of a profile of environmental threat and opportunity (ETOP) is considered to be a useful device.

An illustrative profile is given in Figure 8-2 on the basic of environmental analysis carried out by Bharat Heavy Electricals Ltd.

BHEL: ENVIRONMENTAL THREAT AND OPPORTUNITY PROFILE (ETOP)

Environmental Sector	**Impact (+) Opportunity (-) Threat**
Socio – economic	(+_) continued emphasis on infrastructural development which includes power supply for industry, transport, and domestic consumption.(-) Severe resource constraints.
Technological	(+) High growth envisaged in industrial production and technology upgradation.
Supplier	(-) Sources of technology will become scarce due to formation of technology cartels.
Government	(+) Liberalization of technology import policy

Competition	(-) Customers will become more discerning in their requirements due to an increasing role of power plant consultants. (-) Public sector will find it increasingly difficult to retain specialists and highly qualified personnel.

Figure 8-2 Environmental analysis at BHEL

III. Strategic Advantage Profile

A Profile of strategic advantages (SAP) is a summary statement, which provides an overview of the advantages and disadvantages in key areas likely to affect future operations of the firm. It is a tool for making a systematic evaluation of the strategic advantage factors, which are significant for the company in its environment. The preparation of such a profile presupposes detailed analysis and diagnosis of the factors in each of the functional areas (Marketing, Production, Finance and Accounting, Personnel and Human Resources, R& D). The relevant data for the critical areas may go as a supplement to the profile. The following Strategic Advantage Profile relates to a food processing company in India.

Figure 8-3 Strategic Advantage Profile (SAP) of ABC India Ltd.

Internal Area	(+) Strength (-) Weakness
Marketing	(+) Capable sales force; sales agents dispensed with. (-) Shrinking market for most products.
Operations	(-) Stagnating sales performance.
	(+) Profits after tax picking up after 1982. (-) Plant facilities are old.

R&D	(-) No R&D effort so far. (+) Backing in R &D expected from parent US company.

Finance	(-) No additional investment since 1980. (-) Heavy reliance on fixed deposits and bank loans. (+) Parent US company now interested in expansion.
Corporate Resources	(+) Management team comprises young, ambitious executives.

Since the Strategic Advantage Profile is a summary statement of corporate capabilities, in summarizing the functional competencies a comparative view needs to be taken in the light of external conditions and the time horizon of projections. For example, while comparing the level of inventory holding, one may find it to be relatively higher than that of competing firms; as such it should be regarded as a weakness. But if the market demand shows an increasing trend, apparent weakness should be considered strength.

IV. Functional – area profile and resource deployment matrix.

Developed by Hofer and Schendel, this method requires the preparation of a matrix of functional areas with characteristics common to each, e.g., focus of financial outlay, physical resource position, organizational system, and technological capability. The functional area profile of a manufacturing company is given by way of illustration. Following this exercise, it is required that the resource outlay and focus of efforts over time in the respective functional areas be presented also in the form of a matrix. Figure 8-4 Functional – Area Resource – Deployment Matrix

Figure 8-4 Functional – Area Resource – Deployment Matrix

Functional Area	Resource Deployment and Focus of Efforts							
Marketing	Development							
	Focus of Effort							
Production	Development outlay (%) Amount ₹)							
	Focus of Effort							
Finance	Development outlay (%) Amount ₹).							
	Focus of Effort							
R&D	Development outlay (%) Amount ₹)							
	Focus of Effort							
Management	Development outlay (%) Amount (₹)							
	Focus Effort							

V. SWOT Analysis

SWOT is an acronym for the internal Strengths and Weaknesses of a business and environmental Opportunities and Threats facing that business. SWOT analysis is a systematic identification of these factors and the strategy that reflects the best match between them. It is based on the logic that an effective strategy maximizes a business's strengths and opportunities but at the same time minimizes its weaknesses and threats. This simple assumption, if accurately applied, has powerful implications for successfully choosing and designing an effective strategy.

Opportunities

An opportunity is a major favorable situation in the firm's environment. Key trends represent one source of opportunity. Identification of a previously overlooked market segment, changes in competitive or regulatory circumstances, technological changes, and improved buyer or supplier relationships could represent opportunities for the firm.

Threats

A threat is a major unfavorable situation in the firm's environment. It is a key impediment to the firm's current and / or desired future position. The entrance of a new competitor, slow market growth, increased bargaining power of key buyers or supplier, major technologies change, and changing regulations could represent major threats to a firm's future success.

The second fundamental focus in SWOT analysis is identifying key strengths and weakness based on examination of the company profile. Strengths and weaknesses can be defined as follows:

Strengths

A strength is a resource, skill, or other advantage relative to competitors and the needs of markets a firm serves or anticipates serving. a strength is a distinctive competence that gives the firm a comparative advantage in the marketplace. Financial resources, image, market leadership, and buyer / supplier relations are examples.

Weaknesses

A weakness is a limitation (or) deficiency in resources, skills, and capabilities that seriously impedes effective performance. Facilities, financial resources, management capabilities, marketing skills, and brand image could be sources of weaknesses. Sheer size and level of customer acceptance proved to be key strengths around which IBM built its successful strategy in the personal computer market.

How is it useful?

Understanding the key strengths and weaknesses of the firm further aids in narrowing the choice of alternatives and selecting a

strategy. Distinct competence and critical weakness are identified in relation to key determinants of success for different market segments; this provides a useful framework for making the best strategic choice.

SWOT analysis can be used in at least three in strategic choice decisions. The most common application provides a logical framework guiding systematic discussions of the business's situation, alternative strategies, and ultimately, the choice of strategy. What one manager sees as an opportunity, another may see as a potential threat.

A second application of SWOT analysis is illustrated in Figure.8-5. Key external opportunities and threats are systematically compared to internal strengths and weaknesses in a structured approach. The objective is identification of one of four distinct patterns in the match between the firm's internal and external situation. The four cells in Figure 8-5 represent these patterns.

- Cell 1 is the most favorable situation; the firm faces several environmental opportunities and has numerous strengths that encourage pursuit of such opportunities. This condition suggests growth – oriented strategies to exploit the favorable match. IBM's intensive market development strategy in the personal computer market was the result of a favorable match between strengths in reputation and resources and the opportunity for impressive market growth.

- Cell 2, a firm with key strengths faces an unfavorable environment. In this situation, strategies would use current strengths to build long – term opportunities in other products/ markets.

- Cell 3 faces impressive market opportunity but is constrained by several internal weaknesses. Businesses in this predicament are like the question marks in the BCG matrix. The focus of strategy for such firms is eliminating internal weaknesses to more effectively pursue market opportunity.

- Cell 4 is the least favorable situation, with the firm facing major environmental threats from a position of relative weakness. This condition clearly calls for strategies that reduce or redirect involvement in the products markets examined using SWOT analysis.

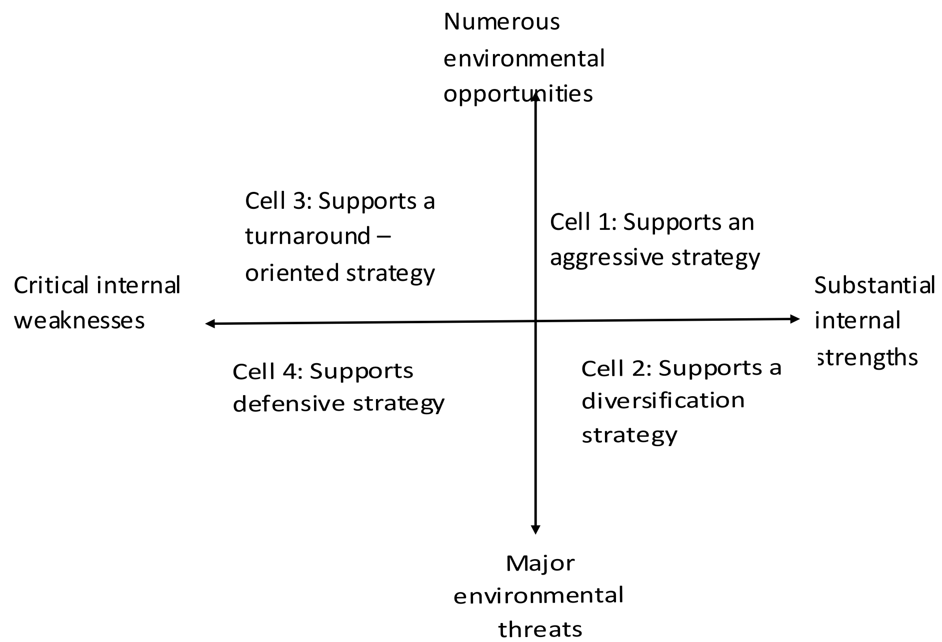


Figure 8-5 Swot Analysis

SWOT analysis helps resolve one fundamental concern in selecting a strategy: What will be the principal purpose of the grand strategy? Is it to take advantage of a strong position or to overcome a weak one? SWOT analysis provides a means of answering this fundamental question. And this answer is input to one dimension in a second, more specific tool for selecting grand strategies: the grand strategy selection matrix.

VI. The Opportunity and Threat Matrices

A company, after identifying the threats, can use judgment to place the threats in any of the four cells shown in Figure 8-6

Figure 8-6 Threat Matrix

Seriousness	High	Low
High	1 Majorthreat	2 Majorthreat
Low	3 Majorthreat	4 Majorthreat

Probability of Occurrence

For an aluminum plant erratic and high cost of power can became a threat if the probability of occurrence is high (cell.1). There is a need to set up captive plant or shifting the plant to another location.

Figure 8-7 Opportunity Matrix

Seriousness	High	Low
High	1 Very attractive	2 Moderately attractive
Low	3 Moderately attractive	4 Least attractive

Probability of Occurrence

A company's success probability with a particular opportunity depends on whether to strength (distinctive competence) matches the success requirement of the industry.

Ex: - Entry into LCVs is an attractive opportunity for TELCO.

VII. The Impact Matrix

The impact of various strategies (opportunities and threats) is examined with the help of impact matrix. After identifying the trends in mega, micro and relevant environments the degree of impact can be measured on an impact scale. The impact matrix can be for a specific business unit or to overall company Eg. Diversified company.

Figure 8-8 The Impact Matrix

		Impact on strategies			
Trends	Pr. of Occurrence	S1	S2	S3	S4
T1					
T2					
T3					
T4					

VIII. The Impact Scale

A futuristic orientation and an ability to synthesize are two critical requirements for strategic decisions. On studying the environmental issues, the major trends can be identified and examine for the degree of impact they make on the business. A 'five point ' scale can be used to assess the 'degree' and 'quality' of impact of each trend on different strategies. The scoring pattern can be:

+ 2 - Extremely favorable impact

+1 - Moderately favorable impact

0 - No impact favorable impact

-1 - Moderately unfavorable impact

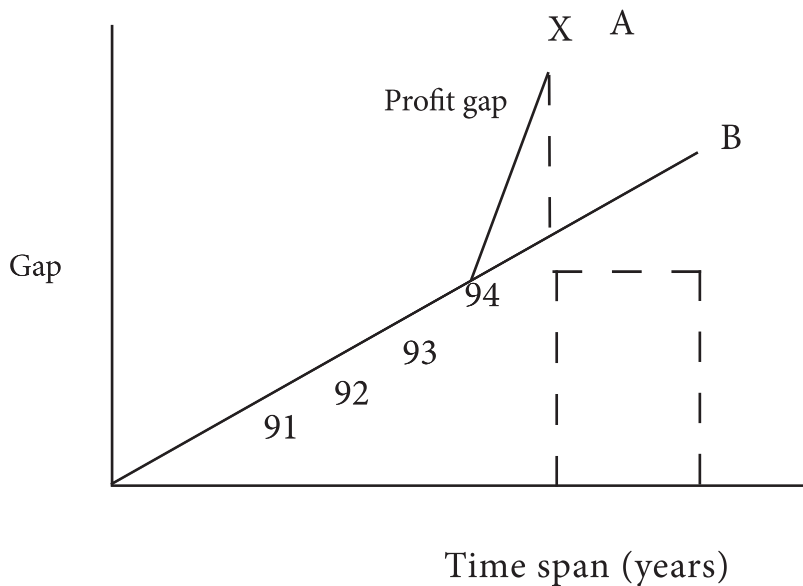
-2 - Extremely unfavorable impact

For each trend probabilities of occurrences can be assigned.

IX. Gap Analysis

It is a useful method to describe the process involved in deciding what course of action should be taken to remove any potential profit or sales gap or risk gap.

Figure 8-9 Gap analysis



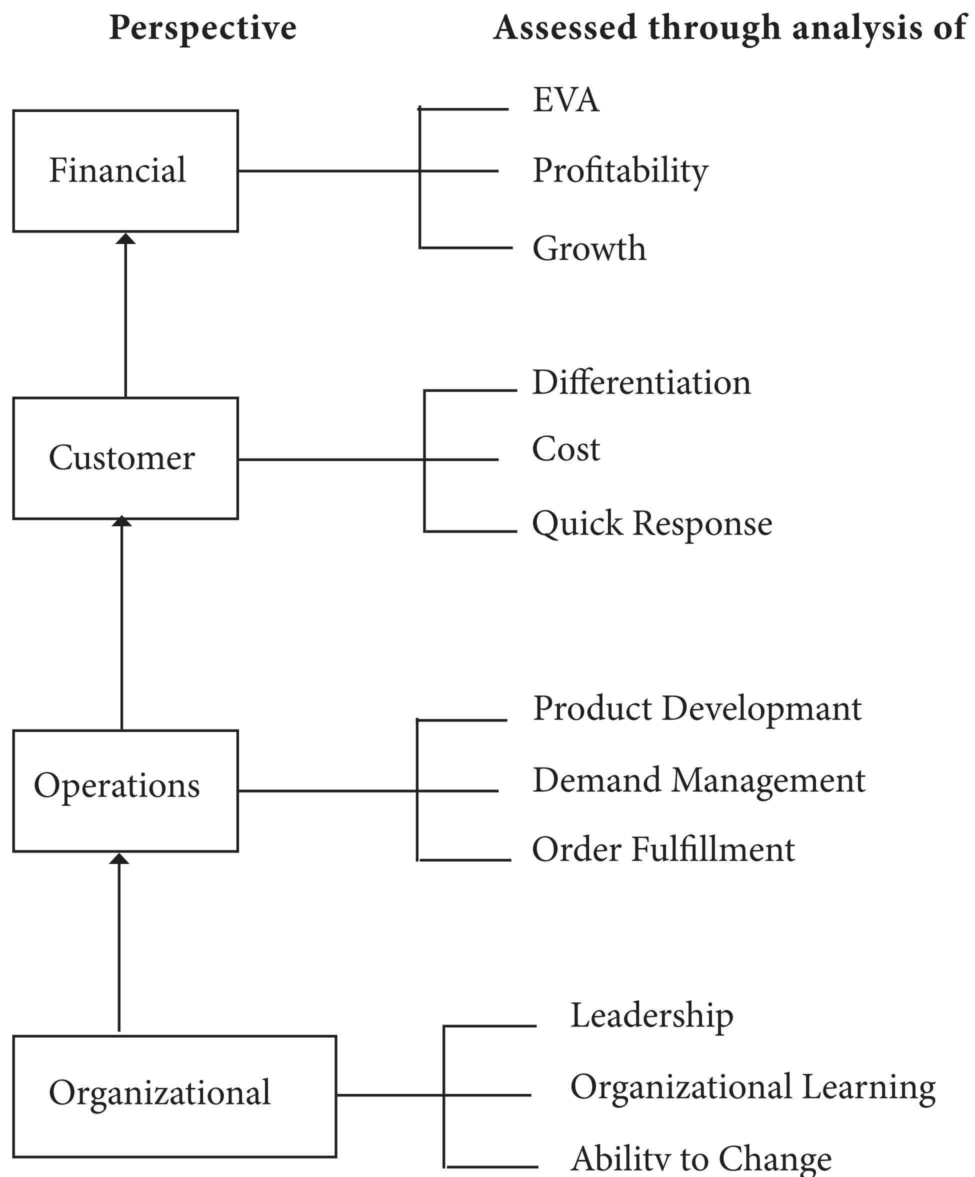
- **Profit Gap:** Gap between profit for the past few years and profit projection based on freehand projection, linear regression coefficient or exponential smoothing.
- **Sales Gap:** Gap between planned & actual sales.
- **Product gap:** Difference between what a firm offers in terms of product items and what the industry provides in terms of product line.
- **Risk gap:** Gap between anticipated risk with strategic decision and the actual happening.

X. Balanced Score Card

Balanced Scorecard is another useful tool to assess the internal strength and weakness of a company. This Balanced Scorecard attempts to examine firm's strengths and weaknesses from different perspective, instead of focusing on a narrow set of criteria. This Balanced Scorecard does not out weigh one perspective and underscores other, rather it balances all of them.

To generate superior return for shareholders, company should have competitive advantage that depends upon its ability to provide certain values to customers. These values can be provided by offering them better, cheaper and faster products or services. For this company requires development of operations that supports product development and responsiveness to fulfill orders. To facilitate quality operations, company needs organization with required creativity, skill and learning. Thus financial score board is dependent upon many dimensions which contribute to the strength and success of the company. It requires to delve deeper to those perspective (beyond financial perspective) to have balanced insight of the company's internal analysis.

Therefore we consider these four perspectives of the Balanced Scorecard: financial, Customer, Operations and Organizational.



Source: Alex Miller and Gregory G. Dess, Strategic Management, McGraw Hill, New York, 1996, Page 117.

This balanced scorecard, as a tool of internal analysis, provides definite advantages to the company.

First, it evaluates the strengths and weaknesses of a company by providing equal and balanced weight to different factors.

Second it "reflects the idea of a hierarchy of intent with elements linked in a series of means – ends relationship" (Alex Milles and Gregory G. Dess,1996).

Third, it explicitly cites competitive advantage as the core element for the success of a strategy.

Glueck's Scanning Techniques

Glueck Suggests three major search techniques for environmental scanning.

(A) Information gathering

(B) Spying

(C) Forecasting.

(A) Information Gathering

By gathering information, strategic manager can know about the business environment. The soures of information may be either written or verbal.

The written sources of information may be published in various publications

a. Business magazines like Business Today, Business India, Advertising and Marketing, Harvard Business Review, etc;

b. Newspapers like Economic Times, Financial Express, Business Line, etc;

c. Publications of Trade Directories, Reports, Guides;

d. Annual reports and profiles of companies; etc.

(B) Spying

Spying is one of the methods of collecting and analyzing the information required for business scanning. For this, specialized individuals can be employed to get trade secrets or clues about strengths of supplier, customer or competitor. These clues are further processed for scanning business environment. Here business has to ensure avoiding breach of law.

(C) Forecasting

"Good anticipation is the result of good strategic exploration." Joel Arthur Barker, author of the book Paradigms: The Business of discovering the future, rightly remarks. Like Peter Drucker, he also agrees that future managers will be more anticipators and proactive than problem solver or reactors.

Forecasting is the techniques of estimating those events that may occur in the future. Though future is uncertain and unexpected, yet it can be predicted to a certain extent by correlating the various parameters through their analysis and combining intuitions with that analysis.

Some of the popular techniques of forecasting include

- Time series analysis
- Casual modeling and
- Delphi Technique

Self Assessment Questions

1. Explain the significance of scanning techniques.
2. Describe Issues Priority matrix
3. Using Environmental Threats and opportunities Profile (ETOP), find the threats and opportunities a of a firm
4. What is Strategic advantage profile (SAP)?
5. Explain the utility of Functional – area profile and resource deployment matrix

6. Conduct SWOT Analysis for a firm of your choice.
7. What is the benefit of using opportunity and threat matrices?
8. Explain the Impact Matrix
9. How do you make use of the Impact scale
10. Explain Gap Analysis
11. Why do you think balanced score card is a better techniques of scanning?

Activities

1. Motorola is a company with a highly efficient scanning system. Visit its website to identify how they are using market research and technology research to scan their internal and external environment. Note them down.
2. Identify the scanning system of Hindustan Lever Limited by discussing with their local dealers and executives carefully record their observations.

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Lesson 7 - Internal Analysis

Lesson Outline

- Introduction
- Internal Analysis –Definition
- Companies With Strong Internal Environment
- Internal Analysis –Process
- Resource Audit
- Vrio Frame Work
- Grant's Approach
- Continuum Of Sustainability
- Value Chain Analysis
- Upstream
- Downstream
- Core Competence Identification
- Experience Curve
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand the concept importance and process of internal analysis
- Know the techniques of conducting internal analysis
- Identify firms with internal capabilities and their strategies

Introduction

Understanding the elements of external environment helps identify opportunities and threats and decide which opportunities to tap. But for formulation of strategy mere identification of the environment is not enough. A firm needs to identify its internal strengths and weaknesses and find ways to overcome the weaknesses. Therefore an integrated strategy must emerge from the combined assessment of market attractiveness and internal strength.

Internal analysis – Definition

Lawrence R. Jauch and William F. Gleuck define Internal analysis and Internal diagnosis in following words:

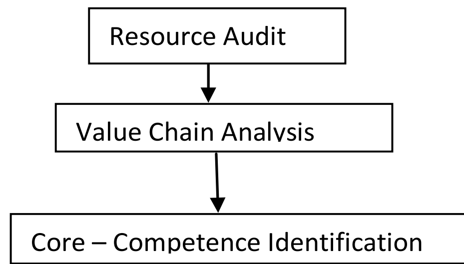
"Internal analysis is the process by which the strategists examine the firm's marketing and distribution, research and development, production and operations, corporate resources and personnel, finance and accounting factors to determine where the firm has significant strengths and weaknesses. Internal diagnosis is the process by which strategists determine how to exploit the opportunities and meet the threats the environment is presenting by using strength and repairing weakness in order to build sustainable competitive advantage."

Internal analysis is the process of reviewing organizational resources (resource audit), scanning organizational activities and linking them with creation of value to the organization (value chain analysis) and identifying the unique strengths and capabilities (core competences).

As is obvious from the above words, that the internal analysis involves three steps as shown in Figure 7-1:

1. Resource Audit.
2. Value Chain Analysis
3. Core-competence Identification.

Figure 7.1 Steps in Internal Analysis



Companies With Strong Internal Environment

Examples of firms with strong strength which pertain to the internal environment are many. According a report in Business Today published in 1997 the strengths of Asia's top twenty companies and commons of Indian companies with internal distinctive competencies is given below.

Table: 7.1 Asia's 50 Most Competitive Companies

Rank	Company	Country	Industry	Competitive Strength
1	SONY CORP	Japan	Electronics	Possesses one of the world's best – known brand names
2	ACER INCE.	Taiwan	Computers	Has become a global player with its user – friendly PCs
3	HONDA MOTOR CO.	Japan	Automobiles	Moving more and more production to North America
4.	TOYOTA MOTOR CORP.	Japan	Automobiles	Combated rising costs at home with more factories abroad

5	CANON INC.	Japan	Electronics	Thrives on cameras, printers, and PC-related products.
6	TAIWAN SEMI CONDUCTOR	Taiwan	Semiconductors	World's targets silicon – foundry, supplying global chip-makers.
7.	SUZUKI MOTOR CORP.	Japan	Automobiles	Well – positioned to penetrate Asian mobiles markets.
8.	HYUNDAI MOTORS CORP.	South Korea	Automobiles	Executing major plans for automobiles in China and India
9	RELIANCE INDUSTRIES	India	Petro chemicals / textiles	A powerful Vertically – integrated textile manufacturer.
10.	ROHM CO.	Japan	Electronic components	Profitable niche player in resistors and LCD screens
11.	RANBAXY LABORATORIES	India	Petrochemicals	Has stepped up R & D and penetrated developing markets
12	SHANGRI – LA ASIA	Hong Kong	Hotels	Operates as many as 34 hotel chains in 12 Asian countries
13	SINGAPORE INTL AIRLINES	Singapore	Aviation	Runs are of the world, most highly-rated airlines

14	GIORDANO INTL	Hong Kong	Retail clothing	Manager 450 high-profile fashion outlets in 12 countries
15	JOLLIBEE FOODS CORP	Philippines	Food	Holds 55 per cent of the Philippines fast-food market
16	SUNDRAM FASTENERS	Indian	Auto pars	A prominent supplier of auto parts, notably radiator caps.
17.	VENTURE MFG.	Singapore	Contract manufacturing	Produces over 200 varieties of electronic equipment
18.	UNITED MICROELEC.	Taiwan	Semiconductors	A fully – integrated firm, which is reverting to a foundry business
19.	ARVIND MILLS	India	Textiles	Soon to be the world's second-largest denim-maker
20.	BAJAJ AUTO	India	Automobiles	Leads scooter manufacture in India, with exports to Thailand

21.	MOSEL VITELIC INC.	Taiwan	Semiconductors	Makes specialized chips with a plant under way in China
22.	AYALALAND INC	Philippines	Real estate	A big developer in Hong Kong, Singapore, and the Philippines
23	TELEVISION BROADCASDTS	Hong Kong	Media	Has the world's largest Chinese film library for TV
24	NINTENDO CO.	Japan	Electronic games	Has launched powerful game machines to fight competitors
25	SAMSUNG ELECTRONICS	Korea	Electronics	Has added global reach by buying AST Research
26	ASIA PACIFIC BREWERIES	Singapore	Brewing	Is brewing foreign JVs to combat stagnant home sales
27	PT INDOFOODSM	Indonesia	Food	Has a virtual monopoly in the home noodles marker

28	KEEPPEL LAND	Singapore	Real estate	Thriving property arm of the well-known Keppel Corp.
29	GENTING BHD	Malaysia	Gaming/ leisure	Concentrating on expanding casino business abroad
30	HITACHI	Japan	Electronics	Business cover semicon-doctor, printing, and property
31	GOLD PEAK INDUSTRIES	Hong Kong	Electronics	Has achieved economicsof scale with battery – aking
32	EVERGREEN MARINE CORP.	Taiwan	Shipping/ aviation	One of the world's largest shippers with an airline in addition
33	SAN MIGUEL CORP	Philippines	Food / brewing	Excels at training and is expanding its food Business
34	CREATIVE TECHNOLOGY	Singapore	Electronics	Has set a new standard with its sound blaster cards

35	KOMATSU	Japan	Construction equipment	Operates a construction – tools business on four continents
36	SUNHUNG KAI PROPS	Hong Kong	Real estate	Owns a broad investment portfolio and substantial Land
37	TOSHIBA CORP.	Japan	Electronics	Very strong in laptop PCs, multimedia, and chips
38	KYOCERA CORP	Japan	Electronics	Leads the world in ceramic semiconductor components
39	AZTECH SYSTEMS	Singapore	Electronics	Expanding into internet and PC photo-output products
40	CHAROEN POKPHAND	Thailand	Agro-business	A huge agricultural business, with interests in poultry
41	FUJI PHOTO FILM CO.	Japan	Electronics	Diversifying from photo-film into hardware

42	BROKEN HILL PROPRIETARY	Australia	Mining	A mining giant, with worldwide interests in exploration
43	BRIDGESTONE CORP.	Japan	Auto parts	Became the 'highest tyro-maker after buying Firestone
44	CHEUNG KONG	Hong Kong	Real Estate	Holds a controlling interest in Hutchison Whampoa
45	PT INDAH KIAT PULP	Indonesia	Pulp and paper	A pulp and paper – maker, part of the Sinar Mas Group
46	PTPOLYSINDOEP	Indonesia	Textiles	A major polyester – maker on a self – sufficiency Drive
47	AIR NEW ZEALAND	New Zealand	Aviation	Has broken out of its corner through a deal with UA

48	SWIRE PACIFIC LTD.	Hong Kong	Diversified / aviation	Investments include a majority holding in Cathay Pacific
49	SHINAWATRA COMPUTER	Thailand	Tele communications	Businesses cover cellophanes and Sitcom
50	POHANG IRON & STEEL	Korea	Steel	Has shrugged off the financial problems of its steel business

Source: Business Today, July 7-21, 1997.

Resource Audit

This audit reviews the resources of an organization for the purpose of assessing the inherent strengths of those resources. Resources include physical, financial, human and intangible assets of an organization, "a Resource is an asset, competency, process, skill or knowledge controlled by an organization". It can be a positive strength if competitors do not possess it or negative when a firm has lesser strength than competitors".

1. **Physical Resources** The physical resources include plant and machinery, land and building, vehicles, stock, etc. Their numbers and book values are not as important as their expected benefits are. Therefore an assessment is made in terms of their potential benefits by examining their age, condition, location, capabilities, etc.

2. **Financial Resources** Financial resources include cash, bank, debtors, marketable securities, etc. In assessing the financial resources, the various sources of finance like equity shares, debentures, retained earnings, long – term and short term loans are considered. Their cost of capital, availability and their effect on the overall liquidity and solvency of the firm is examined.

3. **Human Resources** Human resources are the most valuable assets of the organization, especially in the present business scenarios – where we find people competing than corporations. Traditionally top management were grand strategists, junior managers were implementers and middle the administrators of the strategy. Now the trend has been changed. Top managers are creators of vision for the organization and expect others to deliver. Therefore emphasis has shifted from 'strategy, structure and systems' model towards 'purpose process and people' model. To implement the second model you must have a lot of faith in your people. Companies like Asea Braun Boveri, General Electric, Intel, 3M or even Infosys have made that shift.

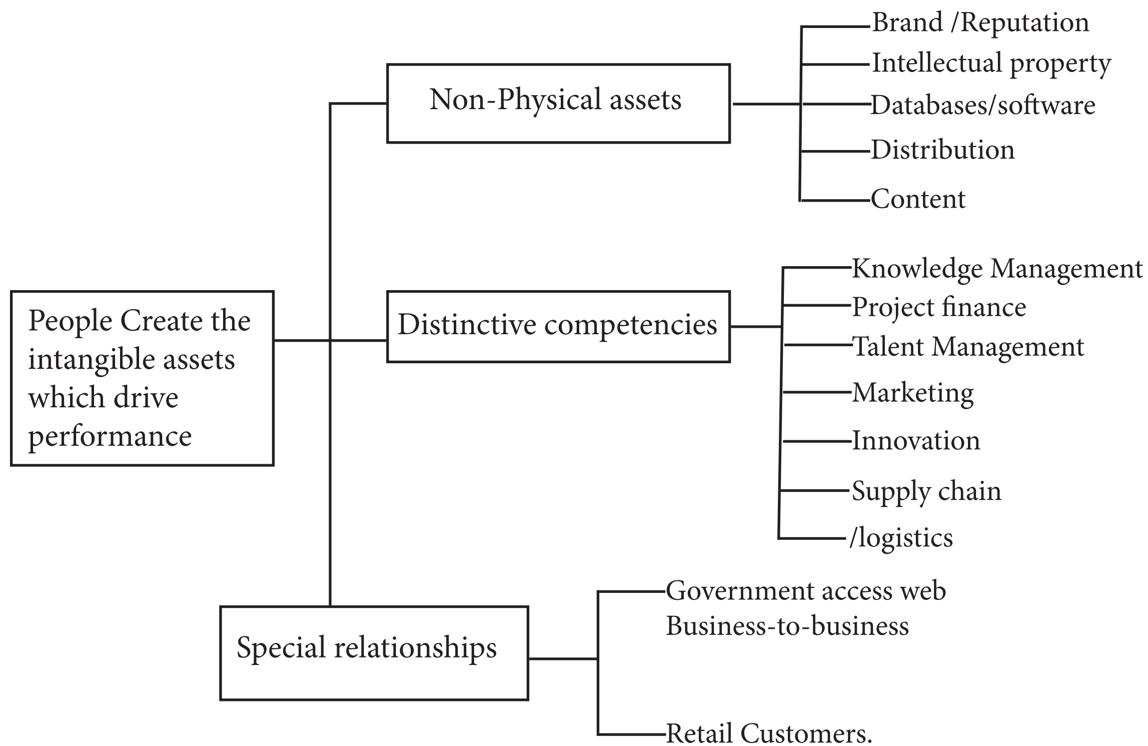
Sumantra Ghoshal remarks

Therefore the human resources audit is done to assess the quality of human resources. Their individual qualities like knowledge, capabilities, learning skill, etc. as well as their loyalty and commitment to organization are assessed.

1. Intangible Assets In the contemporary business world, organizations stress on building intangible assets such as brand, customer relationship, intellectual property, etc. Why so? Earlier capital, technology etc., are scarce and are difficult to obtain. Therefore, they were considered as competitive advantage. Now hey are available and tradable. Something is of competitive advantage is to be hence created. It should be not openly available; not easily leverageable across businesses and not easily substitutable. Intangible assets meet all the three requirements, for example employee commitment or relationships are difficult to imitate."

Look at the tangible assets like machinery in a factory. If company has required capital, it can buy. Look at money which was considered as competitive advantage, is now easily available at inexpensive rates from any where on the globe. Globalization and deregulation of markets have facilitated their easy and cheap accessibility. Only non-replicable and unique competitive advantages of the company are its intangible assets. That is why companies like Reliance, BPL, Krebs Biochemical's, etc. are reporting about their intangible assets. Consider the aspects in Figure 7-2

Figure 7-2 The Intangible Advantage



Source: McKinsey & Co.. adapted from Business World, 9-22 November – 6 December, 1998).

We will now consider the three approaches to internal analysis

- VRIO framework
- Grant's approach
- Continuum of sustainability

Vrio Framework

The framework help raise the following questions.

- VALUE: Does it provide competitive advantage?
- RARENESS: Do other competitors posses it?
- IMITABILITY: Is it costly for others to imitate?
- ORGANISATION: Is the firm organized to exploit the resource?

If the answer is 'yes', there is distinctive competence. Measure these with

- The company's past performance,
- The company's key competitors, and
- The industry as a whole

Grant's Approach

It is a five step approach

1. Identify and classify a firm's strengths & weaknesses
2. Combine the strengths to core competencies
3. Appraise the profit potential of these resources and capabilities.
4. Select the strategy that exploits the firms resources and capabilities to external opportunities
5. Identify resource gaps and invest in upgrading weaknesses.

United Airlines is a very successful, full service international airline. However, South West Airlines was dominating in California due to low cost carriers. UA tried to imitate SWA and had to reduce flying costs form 10.5/- to 7.4/-, speed up boarding and take offs and reduce idle time on the ground. The same being 737 was introduced in 1994. By Feb, 1996 only 8/- cost per passenger mile could be discounted compared to SWAS 7.1/-. It had to pull out from all routes that did not connect with carrier's hubs in San Francisco and Los Angels. For shorter flights like San Francisco to California UA's tariff was higher by $30 while SWA's was $ 69. Slowly UA lost its loyal customers for short route flights to SWA.

So far, no one knows the competitive advantage of SWA. SWA had two capabilities:

- low costs per passenger mile
- Energizing its people to provide safe, on time flight service.

Continuum of Sustainability

Sustainability of an advantage can be determined by considering two factors

1. Durability—rate at which a firm's resources and capabilities depreciate or become obsolete Ex: Intel's R&D weakness & mere imitation.
2. Imitability—Rate at which others can duplicate a firm's core competencies. It can duplicated early when it is

- Transparent Ex: Gillette's sensor blades, difficult to copy, expensive manufacturing equipment.
- Transferable Ex: French winery's land and climate.

- Replicable Ex: Brand Mgt of P&G cannot be replicable

An organization's resources and capabilities can be placed on a continuum as follows –

Level of Resource Sustainability

High (Hard to imitate) — Low (Easy to imitate)

SLOW CYCLE RESOURCES	STANDARD CYCLE RESOURCES	FAST CYCLE RESOURCES
• Strongly shielded • Patents, brand name Ex: Gillette's sensor razor	• Standardized mass production • Economies of scale complicated processes Ex: Chrysler Minivan	• Easy to duplicated • Idea driven Ex: Sony Walkman

Value Chain Analysis

The resources audit provides an understanding of an organization's capabilities. The next step is to identify how the organizational activities contribute to the value - the price the customers are willing to pay for the goods and services of the organization. If this value exceeds the costs of performing those activities, company is said to be profitable, otherwise it is a loss making company. Therefore to achieve the long run objective of maximization of wealth and short –run goals of generating reasonable profits, it is imperative that the company should gain a competitive edge over its competitors.

Charles W.L. Hill and Gareth R. Jones maintain

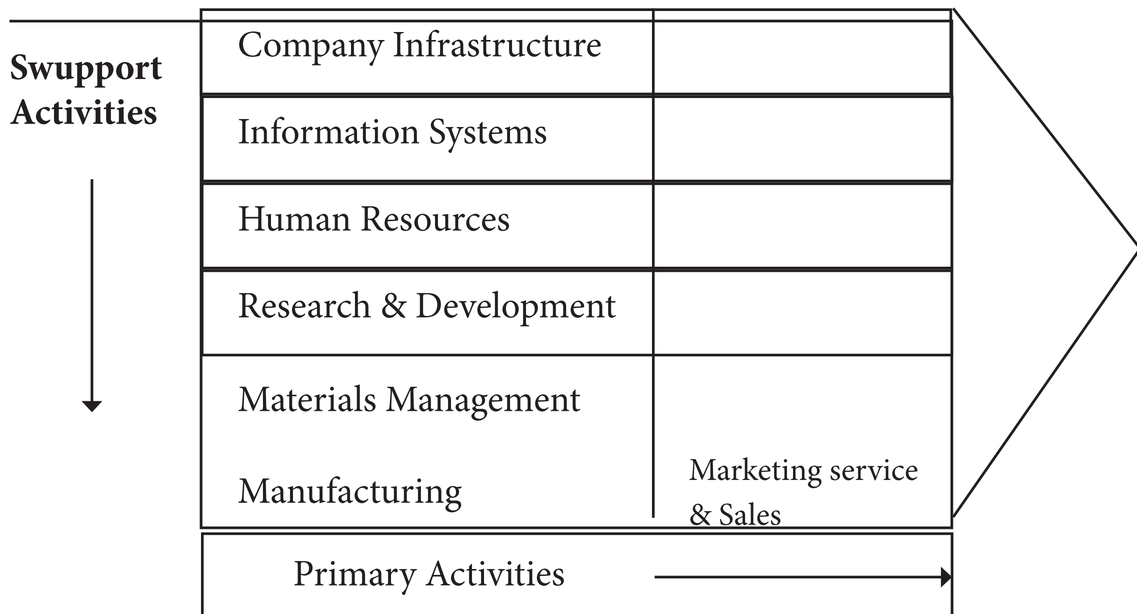
"To gain a competitive advantage, a company must either perform value – creation functions at a lower cost then its rivals or perform them in a way that leads to differentiation and a premium price. To do either, it must have a distinctive competence in one or more of its value – creation functions. If it has significant weaknesses in any of these functions, it will be at a competitive disadvantage"

Michael Porter suggested the concept of "value – chain" that sequences the activities related with creation of value (figure 7-3). These activities can be divided between

(a) Primary activities, and

(b) Support activities.

Figure 7-3 Value chain



The primary activities are concerned with physical creation of the product, its marketing and delivery to buyers and after-sales service. The support activities provide the inputs and infrastructure for the primary activities.

Primary Activities

Some authors classify primary activities into five categories

a. Inbound logistics (activities concerned with receiving, storing and distributing the material, inventory control, warehousing, etc.)

b. Operations (activities concerned with transformation of inputs into final product or service: for example, matching, packing, assembly testing etc.)

c. Outbound logistics (activities concerned with collection, storage and physical distribution of finished goods to the consumers)

d. Marketing and sales (activities concerned with advertising, selling, administration of sales personnel, etc.)

e. Service (activities that enhance or maintain the value of a product / service, such as installation, repair, training, etc.)

Some others classify primary activities into two main functions

a. Manufacturing (physical creation of the product)

b. Marketing (concerned with marketing, delivery and after sales service)

Support Activities

The support activities that provide inputs and infrastructure for primary activities of manufacturing and marketing are classified as follows

a. Material management activities

b. Research and Development activities

c. Human Resources activities

d. Information systems activities

e. Company infrastructure activities

Material Management activities are concerned with procurement, storage and issuance of material to the production departments. The inventory control that aims at keeping uninterrupted supply of material at minimum associated costs is undertaken under this function.

Research and Development activities permeate manufacturing as well as marketing activities. It aims at developing new products or process technology that provide additional benefits to customers, improve quality, lower the cost of manufacturing and ultimately contribute to the creation of value.

The human resource activities aim at meeting the personnel requirement of manufacturing and marketing departments by proper selection of staff, their training and development.

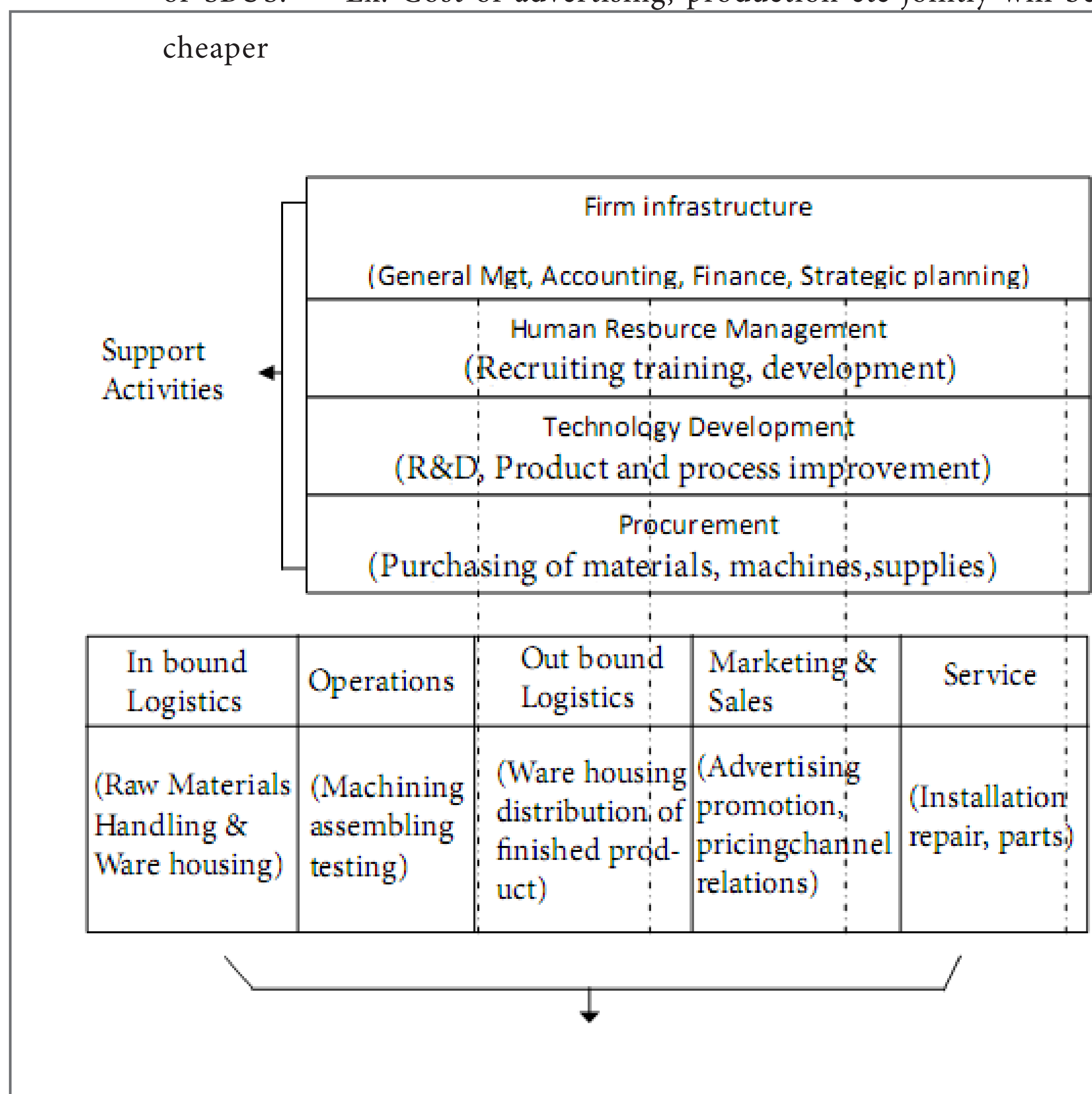
The information system activities ensure efficient and expeditious flow of needed information to the concerned managers for taking decisions and actions.

The infrastructure activities embrace all other activities like finance, legal, public relations, etc which are essential for the company.

Corporate Value Chain Analysis

It involves the following steps. Figure 7-4 depicts a corporate value chain.

- Examine each product lines value chain in terms of various activities involved in producing a product or service. Examine the S&W
- Identify the linkages in product lines value chain. Ex: quality control, check 100% instead of 10% to avoid repairs and returns
- Examine the synergies among value chains of different product lines or SBUS. Ex: Cost of advertising, production etc jointly will be cheaper



Primary Activities

Figure 7.4 A Corporate value chain

JR Galbraith suggests the other method of analyzing a firm's value chain. This analysis helps ascertain where a firm's products are located in the overall value chain. An illustrative value chain is given in Figure 7-5 below. Henry ford I during 1920s and 1930s did this Value Chain analysis. Visitors watched the entire process from an elevated walk way.

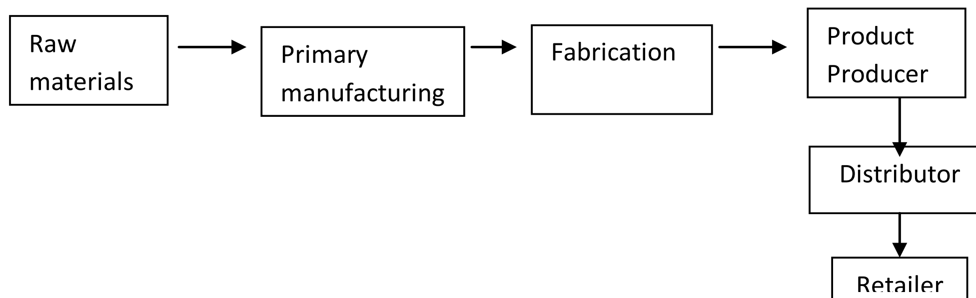


Figure 7-5 Corporate value chain

Industry Value Chain Analysis

This can be split into two

- **Upstream – Ex:** Refers to oil exploration, drilling, moving crude to refiners
- **Downstream – Ex:** Refining the oil + transporting and marketing to distributors & retailers.

Some companies are experts in down stream like P&G & Texaco and some in upstream like British Petroleum.

According to Galbraith firm's centre of gravity is usually the point at which the company started. After a firm establishes well in this point it can move forward or backward along the value chain to reduce costs, access to raw material and guarantee distribution. This process is

VERTICAL INTEGRATION.

Core Competence Identification

A detailed discussion on the concept of core competence is given in lesson 4 of Unit I in this material.After identifying the resources and relating them to strategic purpose through value chain analysis, the next step is identification of company's core competence. The core competence refers to unique strength of the company that competitors cannot easily match or imitate.

To Gary Hamel and C.K. Prahalad,

"A core- competence is a bundle of skills and technologies that enables a company to provide a particular benefit to customers". Following are the examples of core-competence at global level:

Company	Benefit to customer	Core – competence
Sony	Pocketability	Miniaturization
Federal Express	on –time Delivery	Logistics Management
Wal-Mart	Choice, availability, value	Logistics Management
E D S	Seamless Information	Systems Integration
Motorola	Unlettered' communication.	Wireless communication

According to C.K. Prahalad and Gary Hamel,

"The diversified corporation is a large tree. The trunk and major limbs are core products, the smaller branches are business units; the leaves, flowers and fruit are end products. The root system that provided nourishment, sustenance, and stability is the core competence. You can miss the strength of competition by looking only at their end products in the same way you miss the strength of a tree if you look only at its leaves."

Core competence provides strategic advantage to the company. In the short run, a company can achieve competitiveness from its price / Performance attributes; but in the long run core competence will provide profitability. With its core – competence, company can produce at lower

cost and more speedily than competitors and can differentiate. Thus the real strategic advantage to a company comes from its core competence. Thus core- competence is the bedrock of a company's strategy.

Features of Core Competence

Core competence exhibits the following features(Gary Hamel and C.K.Prahalad).

1. Core competence does not reside in one particular product or business unit. It underlies leadership in a range of products or services. "Core competencies transcend any single business unit within the corporation. Core competences are also longer lasting than any individual product or service." Sony's miniaturization competence is not only confined to walkman, but also other products like portable CD player, pocket television, etc.

2. As Core – competence contributes to competitiveness as winning or losing the battle for leadership is highly dependent upon it. "If Motorola lost its leadership position in wireless competencies, a broad spectrum of business would suffer including pagers, two – way mobile radios and cellular telephones."

3. A Core – competence is not a single discrete skill or technology, rather a bundle of skills and technologies. Thus a core competence "represents the sum of learning across individual skill sets and individual organizational units unlikely to reside in its entirety in a single individual or small team." This Core-competence has to be nurtured through collective learning of the team members.

Competitive Cannons of Indian Companies

Some of the Indian companies with ability to use internal strengths to make strategies effective are explained here.

Reliance

- Use vertical integration to control the market
- Attain global scales in each and every product –line
- Build production capacities ahead of demand
- Leverage technology for process efficiencies
- Manage project engineering to control costs
- Service the customer at his door- step.

Ranbaxy Laboratories

- Benchmark costs globally to keep them in check
- Focus relentlessly on only some chosen products
- Seek out niches unprofitable for the bigger players
- Use R &D to build unique, unmatched skills
- Seek differentiation in delivery, not product
- Integrate vertically to attain economies of scale

Sundram Fasteners

- Focus on only one segment of customers
- Adopt the customer's quality standards to avoid rejection
- Use demanding customers to raise quality levels
- Seek out large customers to operate on a global scale
- Develop a full range of products to meet complete buyer needs
- Build unique skills that are expensive to duplicate

Arvind Mills

- Create global capacities quickly to attack older players
- Target large commodity buyers for the benefits of scale
- Focus on one basic product, but diversify into new markets
- Use value – addition to provide a basket of related products
- Keep every element of cost below the level of competitors
- Integrate forward to cash in on low-cost in –house supplies

Bajaj Auto

- Control costs to keep the product affordable
- Reengineer processes to improve time utilization
- Forge relationships with vendors to minimize costs
- Build global capacities if the domestic market is large enough
- Steer clear of diversification even if synergies are available
- Focus on chosen segments without straying into new ones

Self Assessment Questions

1. What is internal resource analysis? How does it help in strategy formulation?
2. What is internal resource audit? Discuss the internal resources of a company.
3. What is competitive advantage of a firm? How a firm can have competitive advantage?
4. What is value chain analysis? Discuss in detail.
5. What is core- competence? How it can be exploited to have competitive advantage?
6. What is the relevance of the resource – based view of the firm to strategic management in a global environment?
7. How can value – chain analysis help identify a company's strengths and weaknesses?
8. In what ways can a corporation's structure and culture be internal strengths or weaknesses?
9. What are the pros and cons of management's using the experience curve to determine strategy?
10. Take a company of your choice and conduct SWOT analysis for it.

Activities

1. Take an industry and identify the major firms for three of them conduct SWOT analysis and identify core competencies
2. Visit websites of any two companies in pharma industry and identify the major threads and the strategies adopted by them to face them

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Lesson 8 - Competitive Analysis

Lesson Outline

- Introduction
- Concept And Types Of Competition
- Hyper Competition
- Analysis For Developing Competitive Strategy
- Porter's Analysis
- Mckinsey's Framework
- Key Factors For Success
- Competitive Strategies
- Generic Strategies Of Porter
- Marketing Warfare
- Summary
- Self Assessment Questions
- Activities
- Reference

Learning Objectives

After reading this lesson you should be able to

- Know the concept and types of competition
- Analyze competition from strategic point of view
- Illustrate and explain Porter's five forces analysis, Mckinsey's 7-s framework and Key success factor approach
- Outline the generic competitive strategies and explain marketing warfare

Introduction

Developing a competitive strategy is developing a broad framework for the business-how is it going to compete; what are its objectives; and what policies will be needed to carry out its objectives. The competitive strategy is a combination of 'ends' for which an organization is striving and 'means' by which it is seeking to get there.

Concept and Types of Competition

The exchange process between seller and buyer characterizes market. Seller has a product to offer at a price and buyer has a need that can be satisfied by the product. In this sense, the seller and buyer are major actors in the market. Competition is said to exist when there is more than one seller and more than one buyer. Thus there are two views of competition.

- Economist's view of competition form seller point of view
- Marketer's view of competition from buyer point of view

The economists view of competition

Economists have taken the resource distribution trough price mechanism as the keyhole and viewed competition. They analyzed competition, therefore, from sellers' point of view or the industry structure. Industry is defined as a collection of sellers who offer similar or same product to the same type of customers.

Take for example, toothpastes. There are several competitors. For instance, HUL (Close up), Colgate (Colgate), and Dabur Balsara (Promise) are in the race along with many others.

Economists describe the industry or market structures based on demand and supply forces. Table 7-1 shows the different market situations and describes their characteristics.

Table 7-1. Market structures

Type of competition/ Characteristics	Perfect competition	Monopoly	Oligopoly	Monopolistic
Number of sellers	Many	One	Few (around 20)	Many

Number of buyers	Many	Many	Many	Many
Type of product	Homogeneous	Unique	Homogeneous/Heterogeneous	Similar
Entry and Exit	Free. No restrictions	Barriers exist. Restrictions like patent laws and licensing	Barriers exist Restrictions like patent laws and licensing	Barriers exist Restrictions like patent laws and licensing
Transportation costs	Nil	Exist	Exist	Exist

Price of the product	Uniform and varies with changes in demand and supply forces.	High price with limited supply or Low price with large supply. Price discrimination is often found.	Kinky demand curve. Leadership of a firm or collusion of marketers fixes Price. Price rise is not followed. Secret discounts are common.	Non-price competition. Products are offered depending upon the quality in price range. Promotion and product differentiation (positioning) play a big role.
Examples	Vegetable markets and stock market	Electricity	Steel, oil and cement	Soaps, detergents, and TVs

In this sense, even though 'physical products' may belong to different industries or technologies, they become competitors to each other to satisfy a specific need or desire. This ubiquitous view can be perceived as belonging to four types of competitors. Kotler((1988) has labeled them as desire competitors, generic competitors, form competitors and brand competitors.

Figure 7-1 provides an illustration for a situation where the need is to 'break monotony' at the 'desire level' and terminates into a specific 'brand' situation for a south Indian Restaurant.

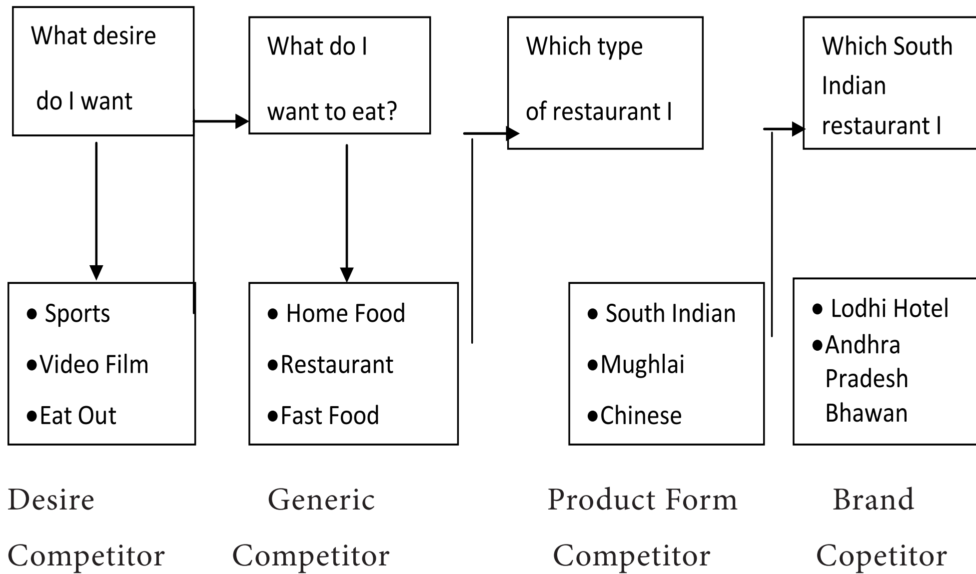
1. **Desire competitors** The alternative suppliers of different products that can satisfy a basic desire- the need expression of a consumer. For example, you desire to break monotony. You have several options and you choose to eat out.

2. **Generic competitors** The suppliers of a specific product/service category. In this example, the next question is where and what? The physical product or service is visualized here. You have again options by variety of foods and places. You decide, say, in favor of restaurant.

3. **Form competitors** The suppliers of different product/service form. They are explored here. Which form of restaurant? is the next choice problem. Say South Indian.

4. **Brand competitors** Different marketers of different brands of a particular product form. The consumer now focuses on brand choices. Say India coffee house.

Figure 7-1 : The Marketing View of Competition



In the backdrop of this framework, the South Indian Restaurant owners will be myopic if they focus only on their brand competitors. A challenge to any marketer is to expand the primary demand and hence enhance the area of opportunities. To do this, the South Indian Restaurant owners have to be concerned about the trends in the 'eating-out' environment. And this has been done very successfully by some of the South Indian Restaurants in large cities. Having gained a wide popularity amongst a large segment, they have also started offering Non-South Indian dishes and have thus expanded their market size and fairly their opportunities.

This kind of a view provides a wide terrain to radar the competitive environment. Theodore Leavitt's classic article. "The Marketing Myopia", is an excellent illustration of shifting the focus from product to need to ensure long-term survival and growth of a firm.

Hyper Competition

Most industries today are facing an ever-increasing level of environmental uncertainty. They are becoming more complex and more dynamic. Industries that used to be multi domestic are becoming global. New flexible, aggressive, innovative competitors are moving into established markets to erode rapidly the advantages of previously dominant firms. Distribution channels vary from country to country and are being altered daily through the use of sophisticated information

systems. Closer relationships with suppliers are being forged to reduce costs, increase quality, and gain access to new technology. Companies learn to quickly initiate the successful strategies of market leaders, and it becomes harder to sustain any competitive advantage for very long. Consequently, the level of competitive intensity is increasing in most industries. Richard D'Aveni (1994) contends that as this type of environmental turbulence reaches more industries, competition becomes hyper competition.

According to D'Aveni

In hyper -competition the frequency, boldness, and aggressiveness of dynamic movement by the players accelerates to create a condition of constant disequilibria and change. Market stability is threatened by short product life cycles, short product design cycles, new technologies, frequent entry by unexpected outsiders, repositioning by incumbents, and tactical redefinitions of market boundaries as diverse industries merge. In other words, environments escalate toward higher and higher levels of uncertainty, dynamism, heterogeneity of the players and hostility.

In hyper-competitive industries such as computers, competitive advantage comes from an up-to-date knowledge of environmental trends and competitive activity coupled with a willingness to risk a current advantage for a possible new advantage. Exhibit 7-1 describes how Microsoft is operating in the hyper competitive industry of computer software.

Exhibit 7-1:Hyper competition-The case of Microsoft

Microsoft is a hyper competitive firm operating in a hyper competitive industry. It has used its dominance in operating systems (DOS and Windows) to move into a very strong position in application programs like word processing and spreadsheets (Word and Excel). Even though Microsoft held 90% of the market for personal computer operating systems in 1992, it still invested millions in developing the next generation – Windows 95 and Windows NT. Instead of trying to protect its advantage in the profitable DOS operating system, Microsoft actively sought to replace DOS with various versions of Windows. Before hyper competition, most experts argued against cannibalization of a company's own product line because it destroys a very profitable product instead of harvesting it like a "cash cow." According to this line of thought, a company would be better off defending its older products.

New products would be introduced only if it could be proven that they would not take sales away from current products. Microsoft was one of the first companies to disprove this argument against cannibalization.

Bill Gates, Microsoft's Confounder, Chairman, and CEO, realized that if his company didn't replace its own DOS product line with a better product, someone else would (such as IBM with OS/2 Wrap). He knew that success in the software industry depends not so much on company size but on moving aggressively to the next competitive advantage before a competitor does. "This is a hyper competitive market," explained Gates. "Scale is not all positive in this business. Cleverness is the position in this business." By 2000, Microsoft still controlled over 90% of operating systems software and had achieved a dominant position in applications software as well.

Analysis for Developing a Competitive Strategy

Every business has a competitive strategy. However, some strategies are implicit, having evolved over time, rather than having been explicit (evolved by deliberate planning process). Implicit strategies lack focus, produce inconsistent decisions, and unknowingly become obsolete. Without a well-defined strategy, organizations will be driven by current operational issues rather than by a planned future vision. The broad considerations in an effective competitive strategy can be extended into a generalized approach to the formulation of strategy. In order to do this, the organization must be in a position to answer the following questions:

1. What is the current strategy, implicit or explicit?
2. What assumptions have to hold for the current strategy to be viable?
3. What is happening in the industry, with our competitors, and in general?
4. What are our growth, size, and profitability goals?
5. What products and services will we offer?
6. To what customers or users?
7. How will the selling/buying decisions be made?
8. How will we distribute our products and services?
9. What technologies will we employ?

10. What capabilities and capacities will we require?
11. Which ones are core?
12. What will we make, what will we buy, and what will we acquire through alliance?
13. What are our options?
14. On what basis will be compete?

We will now discuss three analytical procedures given by Porter, Mckinsey and Ohmae in that order.

Porter's five forces analysis of competition

A useful approach to formulating business strategies is based on Michael Porter's "competitive analysis". Porter's model provides a process to make your competitive strategy explicit so it can be examined for focus, consistency, and comprehensive. Porter's approach is based on the analysis of five competitive forces (see Figure 7-2).

1. Threat of new entrants,
2. Bargaining power of suppliers,
3. Bargaining power of buyers,
4. Threat of substitute products,
5. Rivalry among existing firms.

Threat of New Entrants

Firms entering an industry bring new capacity and a desire to gain market share and profits, but whether new firms enter an industry depends on the barriers to entry. (A number of these are shown in Figure7-2). In addition, established firms in an industry may benefit from "experience curve" effects. That is, their cumulative experience in producing and marketing a product often reduces their per-unit costs below those of inexperienced firms. Is general, the higher the entry barriers, the less likely outside firms are to enter the industry.

Bargaining Power of Suppliers

Suppliers can be a competitive threat in an industry because they can raise the price of raw material or reduce their quality. Powerful suppliers can reduce the profitability of an industry if companies in the industry cannot pay higher prices to cover price increases that the supplier imposes. Some determinants of supplier power are listed in

Figure7-2

Bargaining Power Buyers

Buyers compete with the industry by forcing prices down, bargaining for higher quality or more services, and playing competitors off against each other all at the expense of industry profitability. Some determinants of buyer power are shown in Figure 7-2

Threat of Substitute Products

In a broad sense, all firms in an industry are competing with industries producing substitute products. Substitutes limit the potential return in an industry by placing a ceiling on the prices that firms in the industry can profitably chare. The more attractive the price-performance alternative offered by substitutes, the tighter the lid on industry profits. For example, the price of candy, such as Raisinettes chocolate-covered raisins, may limit the price Del Monte can charge for "healthy snacks," such as Strawberry Yogurt Raisins. Some determinants of the degree of substitution threat are shown in Figure 7-2

Rivalry Among Existing Competitors

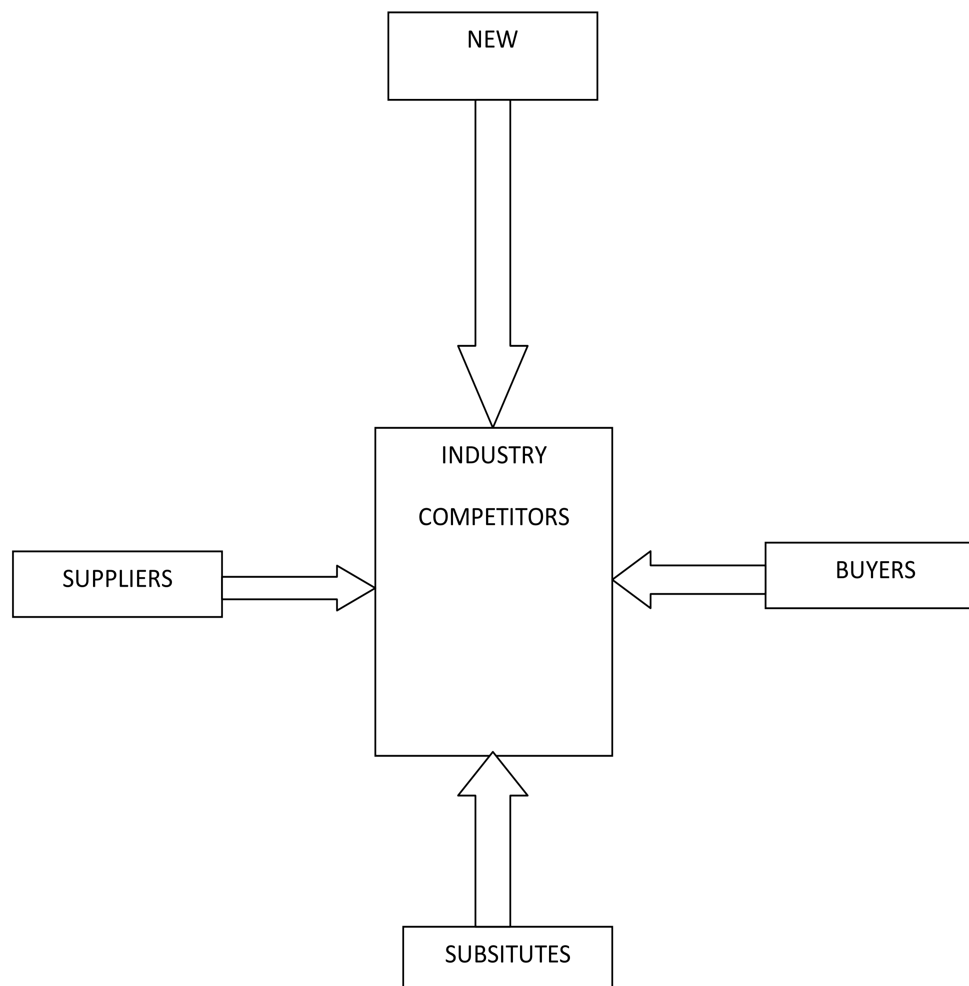
Rivalry determinants include industry growth, product differences and barriers. This is the conventional type of competition in which firms try to take customers from one another. Strategies such as price competition, advertising battles, new product introductions, and increased customer service are commonly used to attract customers from competitors. The factors influencing intensity of rivalry are shown in Figure 7-2.

McKinsey's 7- s Framework

This framework developed in the 1970's by US based management consulting firm McKinsey and Company has received attention from strategists. The framework rests on the proposition that effective organizational change is best understood in terms of the complex relationship between the seven S's. as shown in Figure 7-3. Stated in general terms, the proposition of the7-S model suggests that there are

multiple factors which influence an organization's ability to change and its proper mode of change. Since the variables are interconnected, significant progress cannot be made in one area (e.g., strategy) unless corresponding progress is made in other areas too.

Figure 7.2 Rivalry factors



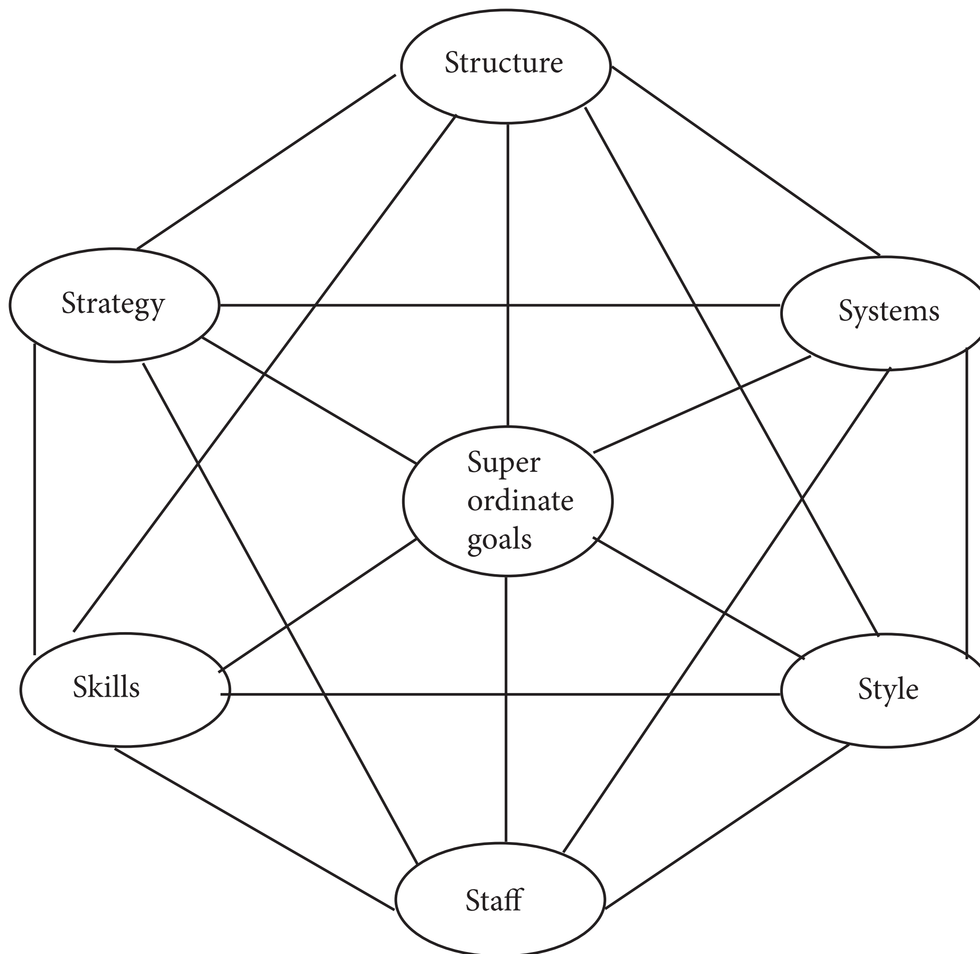


Figure 7-3 Mckinsey 7-s Framework

1. Structure refers to the authority relationships, the hierarchical arrangement of positions in the organization.

2. Systems' may be called the 'infrastructure' and include sub-systems relating to production planning and control, cost accounting procedures, capital budgeting, recruitment, training and development, planning and budgeting, performance evolution, etc. Rules, regulations and procedures constitute 'systems' in the framework, which complement the organizational structure

3. Strategy refers to the long range plan of action with a set of goals for accomplishment

4. Staff' carriers a specific meaning in the 7-S framework. It refers to the way organizations induct young recruits into the mainstream of activities and the manner in which they manage their careers as the new entrants develop into managers.

5. Skills refer to the 'distinctive competence' which reflects the dominant skills of an organization, and may consist of competence in terms of engineering skills, or competence in the area of new product development, customer service, quality commitment, market power, and so on.

6. Style is another variable, which may determine the effectiveness of organizational change effort. According to the 7-S framework, the style of an organization becomes evident through the patterns of actions of the top management team over a period of time, the emphasis laid on aspects of business, reporting relationships and aspects of organizational culture.

7. Shared values (or super ordinate goals) in the Mckinsey model refer to the set of values and aspirations that go beyond the formal statement of corporate objectives. In other words, these are fundamental ideas around which a business is built and which constitute its main values. Typical examples are: Hewlett-Packard's "innovative people at all levels in organization" as the dominant aspiration or value; A T & T's "universal services" goal; "customer service" which guides IBM's marketing drive.

Mckinsey's framework has significance in strategic planning. The following points explain it.

- It provides a good framework of the seven 's' and align them to energies and executive strategies
- It is an excellent multivariate model of organizational change
- It provides a convenient means of checking whether an organization has the necessary conditioning for implementing strategy
- Organizational capabilities (strengths and weaknesses may be evaluated along each of the seven dimensions)

Ohmae's Key factors for success

Ohmae suggests that in the event of limited resources, it may be wise to concentrate on key functional or operating areas that are the determinants of success for a particular business. This calls for identifying the key factors of success (KFS) for a given industry. There are two approaches to identify the KPS.

1. The first is to dissect the market as imaginatively as possible to identify its key segments.

2. The other is to discover what distinguishes successful companies from losers, and then analyze the differences between them.

The key factors for success of different industries may live in different functions, areas, distribution, channels and so on. These can be identified along the various functional activities of business starting from raw material to customer servicing. Table 7-2 provides the key factors for success to increase profit and gain market share for various industries.

Table 7-2 Key Factors for Success

Key factor or function…	….to Increase profit	…..to gain share
Raw materials sourcing	Uranium	Petroleum
Production facilities (economic of scale)	Shipbuilding, Steel-making	Shipbuilding, Steel making
Design	Aircraft	Aircraft, Hi-Fi
Production technology	Soda, Semiconductctors	Semiconductctors
Product rage/variety	Departmental stores	Components
Application engineering/engineers	Minicomputers	LSI, Microprocessors
Sales Force (quality & quantity)	ECR	Automobiles
Distribution network	Beer	Films, Home appliances

Servicing	Elevators	Commercial vehicles e.g. taxis

Ohmae Observes

Business history indicates that the "most effective shortcut to major success appears to be to jump quickly to the top by concentrating major resources early on a single strategically significant function, become really good and competitive at it, and then move to consolidate a lead in the other functions by using the profit structure that the early top status has been made possible. All of to-day's industry leaders without exception began by bold deployment of strategies based on KFS.

Competitive Strategies

We will now discuss the generic strategies given by Porter and the generally found marketing warfare strategies.

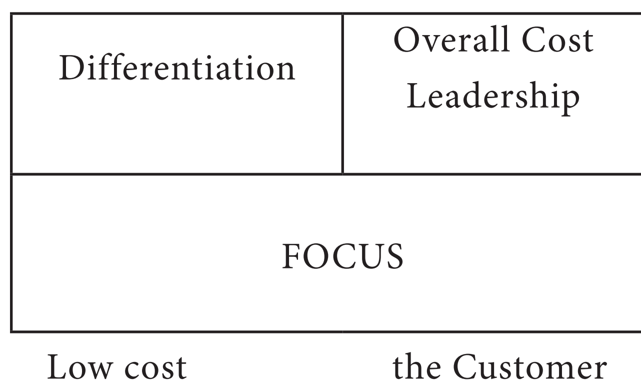
Generic Strategies

tAccording to Porter there are three potentially successful generic strategies (see Figure 7-3) to cope up with the five competitive forces as well as gain advantage (See Figure 7-2and Table 7- 3). These are:

- Overall cost leadership
- Differentiation and
- Focus

Figure 7- 2 Three Generic Strategies

Strategic Advantage



Low cost the Customer

Overall Cost Leadership

In this strategy company makes all possible attempts to achieve the lowest costs in production and marketing. The aim is to gain a large market share. Efficiency is the keyword guiding all decisions to keep the costs low.

Differentiation

Here the aim is to achieve class leadership by creating something, which is perceived as unique. Creating highly differentiated products and marketing programmes-like design or brand image, customer service or dealer network, or any other feasible dimension can achieve it. Companies pursuing this strategy have major strengths in R&D design, quality control and marketing.

Chiragh Din Shirts, Bata Shoes, OTIS Elevators, Cini Fans are some examples where this strategy seems to be the dominant guiding force.

Focus

The underlying assumption in 'Focus' is that a firm should be able to serve a narrow strategic target effectively and efficiently. As a result the firm achieves either differentiation from meeting the need of a particular target, on both.

Genteel', a liquid detergent for expensive clothes by Swastik, and Ponds Talcum Powder are some handy examples for this strategy.

Table 7-3 Requirements for generic competitive strategies

Generic strategy	Commonly required skills and resource s	Common organizational requirements

Overall Cost Leadership	• Sustained capital investment and access to capital • Process engineering skills • Intense supervision of labour • Products designed for ease of manufacture • Low-cost distribution system ‘	• Tight cost control • Frequent, detailed control reports • Structured organization and responsibilities • Incentives based on meeting strict quantitative tares
Differentiation	• Storing marketing abilities • Product engineering • Creative fair • Strong capability in basic research • Corporate reputation for quality or technological leadership. • Long tradition in the industry or univque combination of skills drawn from other businesses • Storing cooperation from channels	• Strong coordination among fucntons in R & D product development, and marketing • Subjective measurement and incentives instead of quanttiate meastues • Amenities to attract hightly skilled labour, scientists or creative people.
Foucs	• Combination of the above policies directed at the particular strategic target	• Combination of the above policies directed at the particular strategic target.

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Marketing warfare strategies

Al Ries and Trout (1986) Observed

In the plan for future, many more pages will be dedicated to the competition. More and more successful marketing campaigns will have to be planned like military campaigns".

Four types of combat positions are identified here for discussion.

The Defensive Warfare

This is essentially recommended for market leaders. It aims at protecting against regulatory provisions like M.R.T.P industrial licensing restrictions, etc. according to authors, a leader has to spend more time in safeguarding its interests against government, social and public environment rather than the immediate next competitor. A leader should also be able to attack itself i.e., drop products, which may appear to make the leadership position vulnerable. The three principles of defensive warfare are:

1. Only the market leader should consider playing the defense,
2. The best defensive strategy is the courage to attract yourself,
3. Strong competitive moves should always be blocked.

The Offensive Warfare

'Offensive' warfare is almost like a mirror image of the defensive warfare. The numbers twos of the industry are suggested to follow the offensive strategy by identifying a weakness in leaders strength and at that point. The principles of 'offensive warfare' are

1. The main consideration is the strength of the leaders position,
2. Find a weakness in the leader's strength and attack at that point.
3. Launch the attack on as narrow a front as possible.

The Flanking Warfare

According to Ries and Trout, 'flanking' the most innovative form of marketing warfare. Over the years, most of the biggest marketing success has been flanking moves. It is recommended to firms with limited

resources. These firms cannot afford to fight the large firms holding number one or two positions on the same battleground. Flanking can be achieved in any manner such as flanking with low price, flanking with high price, flanking with small size, flanking with large size, flanking with distribution, flanking with product form. The principles of flanking warfare are:

1. A good flanking move must be made in an uncontested area
2. Tactical surprise ought to be an important element of the plan
3. Consider the pursuit as critical as the attack itself.

The Guerrilla Warfare

The last form is the guerrilla warfare. Most of the players in a marketing war would be fighting in the market place like the guerrillas. According to Ries and Trout, "smaller companies can be highly successful as long as they do not try to emulate the giants in their field, "Like flanking form there can be many guerrillas; geographic guerrillas, demographic guerrillas, industry guerrillas, product guerrillas and high end guerillas. The principles of guerrilla warfare are:

1. Find a segment of the market small enough to defend,
2. No matter how successful you become, never act like the leader
3. Be prepared to a buyout at a moment's notice.

Self-assessment Questions

1. Explain the concept of competition with suitable examples.
2. What are the competitive situations according to economists?
3. Identify the competitive situations from marketing point of view.
4. Explain the role of marketer in perfect and monopoly situations
5. Examine the role of marketer in oligopoly and monopolistic situations.
6. With example, explain how marketer identifies competition taking buyer point of view.
7. How do you analyze competition situation using porter model?
8. Using Mckinsey framework analyze competition.

9. What are merits of Key success factor method?

10. Identify and explain generic strategies.

11. Discuss military strategies used by marketer.

Activities

1. From marketing magazines, collect information about strategies of select companies of a specific product and analyze competitive situation and strategy directions.

2. Visit websites of companies and examine the competitive situation in which a company of you choice is. Gather information from business news papers on their moves regularly.

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Case Study

SE Ltd is a defence contractor faced with a changing environment. In the past, all the work done by SE was for the government, and it was performed on a 'cost plus' basis. The company was exposed to minimal competition. Now, government believes that the 'cost plus' system encouraged inefficiency. In the future, SE will be required to quote fixed prices for government business, a Government defence contracts are being increasingly given to SE's foreign competitors, who have understanding SE's prices. In addition, SE is faced with a general contraction of defence expenditure by the government. SE's existing costing system is aggregated, that is, all overheads are recovered on direct labour cost. SE's has to have confidence in its costs, in order to get the government orders at an economic price, and to complete internationally.

Questions

1. State the factors that would influence SE in the formulates a strategic plan to meet the new situation.
2. State the strategic responses that are available to Se in the new environment.
3. State what SE's management accounting response should be?

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UNIT – III

Lesson 9 - Strategic Alternatives & Choice of Strategy

Lesson Outline

- Introduction
- Strategic Alternatives
- Generic Strategies
- Grand Strategies
- Growth Strategies
- Stability Strategies
- Retrenchment
- Portfolio Restructuring
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Identify generic and grand strategies.
- Understand generic strategies and know how to adopt in different strategic situations.
- Examine how portfolio restructuring helps in strategic choices.

Introduction

Most companies today including most successful Indian companies like Bajaj Auto, Reliance and ITC have embraced strategic

planning fully in their quest for higher revenues and profits. In this process, there identify multiple strategies that they can adopt.

Strategic alternatives revolve around the question of whether to continue or change the business an enterprise is currently in or improve the efficiency and effectiveness of its current and future operations. Then, how do these companies make the choices? What factors influence their decisions?

Kent Nelson, former chair of UPS, explains why his company has created a new strategic planning department: "Because we're making bigger bets on investment in technology, we can't afford to spend a whole lot of money in one direction and then find out five years later it was the wrong direction".

Tomorrow always arrives. It is always different. And even the mightiest company is in trouble if it has not worked on the future. Being surprised by what happens is a risk that even the largest and richest company cannot afford, and even the smallest business need not run. Peter Drucker

DRUCKER

Strategic Alternatives

After analyzing the environment and assessing the internal environment, the next step in the strategic planning process is to develop strategic alternatives to help the organization in achieving its objectives. Different kinds of strategic alternatives are presented in Figure9-1.

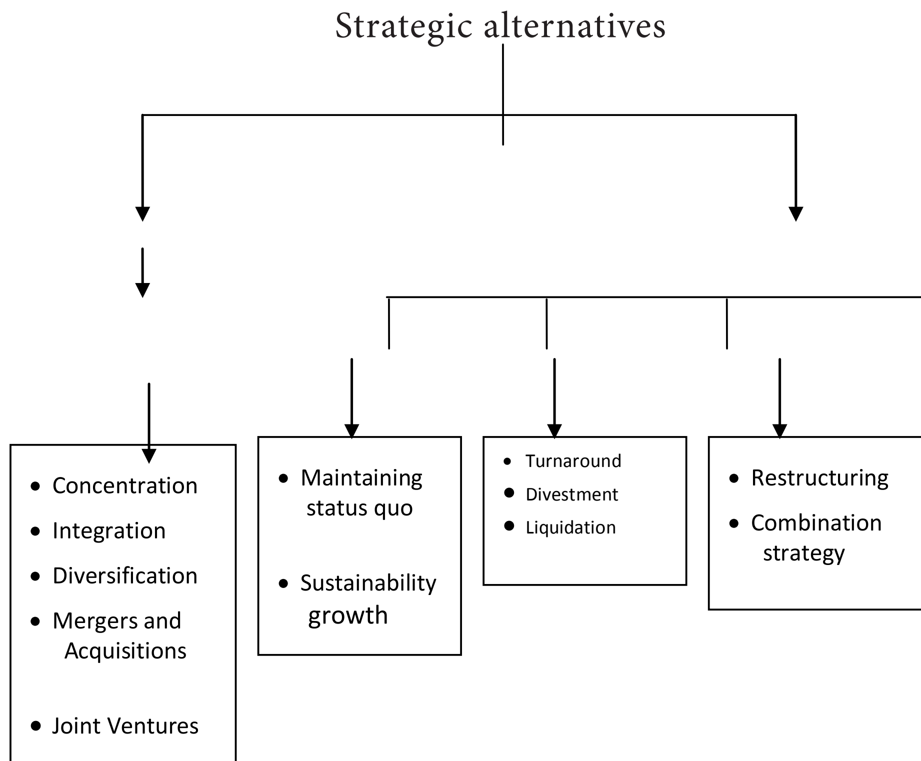


Figure 9-1 Types of strategic alliances

Generic strategies

According to Micheal E. Porter strategies allow organisations to gain competitive advantage from three different bases.

- Overall cost leadership
- Differentiation, and
- Focus.

Organizations achieve competitive advantage by providing their customers with what they want, or need, better or more effectively than competitors and in ways the competitors find difficult to imitate. A firm's relative position within its industry determines whether a firm's profitability is above or below the industry average. The fundamental basis of above average profitability in the long run is sustainable competitive advantage. There are two basic types of competitive advantage a firm can possess: low cost or differentiation. The two basic types of competitive advantage combined with the scope of activities by which a firm seeks to achieve them, lead to three internally consistent generic competitive strategies that can be used by the organization to

outperform competition and defend its position in the industry. These strategies are:

- Cost Leadership
- Differentiation, and
- Focus and Niche Strategies.

Each of these strategies is designed to give a firm a competitive advantage. The focus strategy has two variants, cost focus and differentiation focus as shown in Figure 9-2.

Competitive Advantage

Lower Cost	Differentiation
1. Cost Leadership	2. Differentiation
3. Cost Focus	4. Differentiation Focus

Figure 9-2 Strategies for competitive advantage

Overall cost leadership emphasizes producing standardized products at a very low per-unit 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.

Overall cost leadership yields a firm above – average returns in its industry despite the presence of strong competitive forces. However, this strategy often requires high relative market share or other advantages, such as favorable access to raw materials or the ready availability of cash to finance the purchase of the most efficient equipment. National Can Company, for example, is in a no-growth industry but depends on being the low-cost producer of cans and bottles to increase its profits.

Reliance became number one company of India because of its cost leadership strategy. Presently it is the lowest-cost polyester producer

in the world. Reliance's project management skills, among the best in its business anywhere in the world, and its competencies in mobilizing large amount of low-cost finance enables them to set up world –scale plants at the highest speeds and lowest capital costs.

"In the competition for markets, it has won through an aggressive strategy based largely on scale and pre-emption. By continuously investing in capacity, often ahead of manifest demand, Reliance has not only expanded its market share but has also wrested all investment initiative from its competitors. In essence, it has played a 'chicken game' to see who blinks first – and given its reputation of always putting its money where its mouth is, it is competitors who have blinked. The net result is that Reliance has come to command between 33 and 80% market share in India for all its key products. These market shares have translated into cost advantages making Reliance the most profitable company in its industry during an upswing and robust in a downswing." Sumantra Ghoshal profoundly remarks.

Ranbaxy laboratories, number two most competitive company of India (after Reliance) attained cost leadership through upgrading technology, vertical integration and benchmarking against international competitors.

Gujarat Ambuja made a success by following this cost leadership strategy. It benchmarked itself against the best practices of cement companies across the world.

Differentiation involves creating and marketing unique products for the mass market. Approaches to differentiation include developing unique brand images (Levi's jeans), unique technology (MacIntosh stereo components), unique features (Jenn – Air electric ranges), unique channels (Tupperware), unique customer service (IBM), or the like. In other words, the key to differentiation is obtaining a differential advantage that is readily perceived by the consumer. Differentiation is a viable strategy for earning above – average returns in an industry, because it creates a defensible position for coping with the five competitive forces.

Presently Titan and its sister company Timex together hold 77% market share while HMT has 12%. There was time when HMT had 90% share because of its low price strategy. Titan with its focus on exterior design, was able to charge a premium price and gain more market share.

Focus is essentially a strategy of segmenting markets and appealing to only one or a few groups of consumers or industrial buyers. The logic of this approach is that a firm that limits its attention to one or a few market segments can serve those segments better than firms that seek to influence the entire market. For example, products such as Rolls – Royce automobiles, Cross pens, and Hartmann luggage are designed to appeal to the upscale market and serve it well rather than trying to compete in the mass market.

Strategy of opening hotels in Himachal is focused strategy of Himachal Tourism Development Corporation, which is pursued on geographic grounds. Rolls – Royce pursues the strategy of selling cars to status conscious high –income consumers. Ranbaxy focused on just two categories of drugs – antibiotics and antibacterial (product – line)

Choices

The requirements for adopting the strategies are listed in Table 9-1 and risks associated with them are given in Table 9-2. Of course, the specific strategies that it is best to use depend on the characteristics of, and opportunities and constraints in, the industry.

Table 9-1 Porter's three Generic Strategies and their requirements

Generic strategy	Required skills and resources	Organizational requirements
Overall Cost Leadership	Sustained capital investment and access to capital Process engineering skills Intense supervision of labor Products designed for ease in manufacture Low-cost distribution system	Tight cost control Frequent, detailed control reports Structured organization and responsibilities Incentives based on meeting strict quantitative targets

Differentiation	Strong marketing abilities Product engineering Strong capability in basic research Corporate reputation for quality or technological leadership Long tradition in the industry or unique combination of skills drawn from other businesses Strong cooperation from channels	Strong coordination among functions in R&D, product development, and marketing Subjective measurement and incentive instead of quantitative measures Amenities to attract highly skilled labor, scientists, or creative people
Focus	Combination of the above policies directed at the particular strategic target	Combination of the above policies directed at the particular strategic target

Source:

Michael E. Porter, Competitive Strategy: Techniques for Analyzing Industries and Competitors. The Free Pres, New York

Grand Strategies

Grand strategies, which are often called master or business strategies, are intended to provide basic direction for strategic actions. Thus, they are seen as the basic of coordinated and sustained efforts directed toward achieving long-term business objectives. Grand strategies indicate how long-range objectives will be achieved, thus, a grand strategy can be defined as a comprehensive general approach that guides major actions. Grand strategies fall under four categories.

Table 9-2 Risks of the Generic Strategies

Risks of cost leadership	Risks of differentiation	Risks of focus
Cost leadership is not sustained • Competitors imitate • Technology changes • other bases for cost leadership erode	Differentiation is not sustained • Competitors imitate • bases for differentiation become less important to buyers	The focus strategy is imitated The target segment becomes structurally unattractive • Structure erodes • Demand disappears
Proximity in differentiation is lost	Cost proximity is lost	Broadly targeted competitors overwhelmthe segment • The segment's differences from other segments narrow • The advantages of a a broad line increase
Cost focusers achieve even lower cost in segments	Differentiation focusers achieve even greater differentiation in segments	New focusers sub-segment the industry

Source:

Michael E. Porter, Competitive Advantage: Creating and Sustaining Superior Performance.

The Free Pres, New York.

1. Growth
2. Stability
3. Retrenchment

4. Portfolio restructuring

We will now discuss each one of them.

Growth Strategies

Organizations usually seek growth in sales, profits, market share, or some other measure as a primary objective. The different grand strategies in this category are:

- Concentration
- Integration
- Diversification
- Mergers and acquisitions
- Joint Ventures

Concentration

The most common grand strategy is concentration on the current business. A concentration strategy is one in which an organization focuses on a single line of business The firm directs its resources to the profitable growth of a single product, in a single market, and with a single technology. Some of America's largest and most successful companies have traditionally adopted the concentration approach. For example, Mc Donald's concentrates on the fast food industry and Holiday Inns. Other examples include W.K. Kellogg and Gerber Foods, which are known for their product; Shaklee, which concentrates on geographic expansion; and Lincoln Electric, which bases its growth on technological advances.

Concentration strategies succeed for so many businesses – including the vast majority of smaller firms – because of the advantages of business – level specialization. By concentrating on one product, in one market, and with one technology, a firm can gain competitive advantages over its more diversified competitors in production skill, marketing know-how, customer sensitivity, and reputation in the marketplace. The reasons for selecting a concentration grand strategy are easy to understand. Concentration is typically lowest in risk and in additional resources required. It is also based on the known competencies of the firm. On the negative side, for most companies concentration tends

to result in steady but slow increases in growth and profitability and a narrow range of investment options. Further, because of their narrow base of competition, concentrated firms are especially susceptible to performance variations resulting from industry trends.

Integration

Integration may take two forms: vertical and horizontal integration.

Vertical Integration

Vertical integration strategy involves growth through acquisition of other organizations in a channel of distribution. When an organization purchases other companies that supply it, it engages in backward integration. The organization that purchases other firms that are closer to the end users of the product (such as wholesalers and retailers) engages in forward integration. Vertical integration is used to obtain greater control over a line of business and to increase profits through greater efficiency or better selling efforts.

Horizontal Integration

This strategy involves growth through the acquisition of competing firms in the same line of business. It is adopted in an effort to increase the size, sales, profits, and potential market share of an organization. This strategy is sometimes used by smaller firms in an industry dominated by one or a few large competitors, such as the soft drink and computer industries.

BHEL had undertaken the path of backward integration for the manufacture of assorted equipments such as, switchgears and transformers, to the full-fledged production of thermal, hydel, and nuclear power generation equipment.

Diversification

This strategy involves growth through the acquisition of firms in other industries or lines of business as explained below.

1. Organizations in slow-growth industries may purchase firms in faster-growing industries to increase their overall growth rate.
2. Organizations with excess cash often find investment in another industry (particularly a fast-growing one) a profitable strategy.
3. Organizations may diversify in order to spread their risks across several industries.
4. The acquiring organization may have management talent, financial and technical resources, or marketing skills that it can apply to a weak firm in another industry in the hope of making it highly profitable.

Diversification may be of different types

Related or concentric diversification When the acquired firm has production technology, products, channels of distribution, and /or markets similar to those of the firm purchasing it, the strategy is called concentric diversification.. This strategy is useful when the organization can acquire greater efficiency or market impact through the use of shared resources. A case of related or concentric diversification is the tie-up of McDonald with Coco-cola.

McDONALD'S India Pvt Ltd (MIPL), the wholly-owned subsidiary of the US-based fast-food giant McDonald's Corporation, along with Coca-Cola, is developing a fruit-based beverage, to be retailed exclusively at McDonald's outlets. The beverage will be made available under the Maaza brand name, but will be different from the regular Maaza brand.

McDonald's has an international tie-up with Coca-Cola, which extends to the domestic market as well. Apart from Coca-Cola, in India, McDonald's has an existing tie-up with Cadbury India, for McSwirl ice-cream cones. McDonald's India is also running a promotion with foods major Nestle, specific to the KitKat chocolate brand. The quick service chain, meanwhile, is in talks with synergistic marketers for similar associations. McDonald's currently operates through 48 outlets in the country, and has set a target of 100 restaurants by 2005.

The quick service chain is looking to set up larger format restaurants for now, rather than exploring the option of setting up smaller format convenience outlets. The company will consider the

small format stores option in the second stage of expansion. For the time being, the focus is on setting up larger restaurants. In addition to setting up standalone outlets in residential areas and entertainment complexes, they have set up outlets on highways and railway stations

Unrelated or conglomerate diversification When the acquired firm is in a completely different line of business, the strategy is called unrelated or conglomerate diversification An example of unrelated conglomerate diversification is Marico's venture into cooling oil segment.

TAKING a cue from Dabur's recent entry into the cooling oil segment with its Himsagar brand, the market leader in hair oils, Marico Industries, has decided to venture into the same segment with its Shanti brand. Under the sub brand of `Thanda Tel', the Shanti brand will soon see an extension from its existing Amla hair oil. Pegged at Rs 38 for 100 ml, the `value-added' oil will have ingredients such as neem and camphor to induce the cooling effects.

"Cooling oil is the fastest growing segment under hair oils pegged at 16 per cent. It is a category that is growing even faster than shampoos." Even the coconut oil market is pegged to grow at 0-2 per cent while the hair oil segment has been generally stagnant. The market leader in hair oils with its leading brand of Parachute has thus decided to venture into the category previously untapped except for a few players with brands such as Himsagar, Himtej and Navratan. They intend spending heavily behind this brand and the ad agency Triton is developing a new campaign for the brand. Its existing Shanti Amla brand of hair oil enjoys a 13 per cent volume and has a second position in the amla segment after Dabur Amla. Besides, in the overall non-coconut oil segment, the company enjoys a 15 per cent share together with its brands such as Mediker. In fact, in the recent past, Mediker did stretch the franchise of its Mediker shampoo with an anti-lice oil, including the same cooling ingredients such as neem and camphor. Marico claims it has made a success of its Parachute Jasmine variant with a turnover of Rs 23 crore. It also withdrew Parachute anti-dandruff hair oil since it was not generating the necessary volumes

Mergers and Acquisitions

In a merger, a company joins with another company to form a new organization.

There are several examples of mergers. Ponds, Lakme, Lipton, Brooke bond India, Milk food ice creams etc have merged with Hindustan Lever Ltd. More examples are given in the lesson on Mergers and Acquisitions in the same Unit..

Joint Ventures

In a joint venture, an organization works with another company on a project too large to handle by itself, such as some elements of the space program. Similarly, organizations in different countries may work together to overcome trade barriers in the international market or to share resources more efficiently.

For example, GMF Robotics is a joint venture between General Motors Corporation and Japan's Fanuc Ltd. to produce industrial robots.

Stability Strategy

The organization that adopts a stability strategy focuses on its existing line or lines of business and attempts to maintain them through one of the following ways.

- Maintaining status quo-continue to do what it has been doing
- Sustainability- reinforcing the organization with more competencies to carry on things in a better or innovative way.

This is a useful strategy in several situations.

- An organization that is large and dominates its market(s) may choose a stability strategy in an effort to avoid government controls or penalties for monopolizing the industry.
- Another organization may find that further growth is too costly and could have detrimental effects on profitability.
- Finally, an organization in a low- growth or no-growth industry that has no other viable options may be forced to select a stability strategy.

Hindusthan Lever keeps its Lux soap updated to retain its hold in market. According to a press release, recently the soap has been enriched with nourishing natural ingredients, which are visible in the soap. There are four variants - Rose extracts, Almond oil, Fruit extracts and Sandal saffron with a base of rich milk cream. The last is a completely different and new variant. These soaps are packed in a metallic wrapper to retain the freshness and fragrance for a longer period than usual, the press release said. The content of TFM (Total fatty matter) has been raised from 60 per cent to 71 per cent.

Retrenchment Strategies

When an organization's survival is threatened and it is not competing effectively, retrenchment strategies are often needed. The three basic types of retrenchment are

- Turnaround,
- Divestment, and
- Liquidation.

Turnaround

Strategy is used when an organization is performing poorly but has not yet reached a critical stage. It usually involves getting rid of unprofitable products, pruning the work force, trimming distribution outlets, and seeking other methods of making the organization more efficient. If the turnaround is successful, the organization may then focus on growth strategies.

Divestment

Strategy involves selling the business or setting it up as a separate corporation. Divestment is used when a particular business doesn't fit well in the organization or consistently fails to reach the objectives set for it. Divestment can also be used to improve the financial position of the divesting organization.

Liquidation

Strategy involves closure of the business, which is no longer profitable. It may be technologically obsolete or out of times with market trends.

Choices

How do firms choose strategies?

Stability strategy is adopted because

1. It is less risky, involves fewer changes and people feel comfortable with things as they are
2. The environment faced is relatively stable
3. Expansion may be perceived as being threatening
4. Consolidation is sought through stabilizing after a period of rapid expansion.

Expansion strategy is adopted because

5. It may become imperative when environment demands increase in pace of activity
6. Psychologically, strategists may feel more satisfied with the prospects of growth from expansion: chief executives may take pride in presiding over organizations perceived to be growth-oriented.
7. Increasing size may lead to more control over the market vis-à-vis competitors
8. Advantages from the experience curve and scale of operations may accrue

- Retrenchment strategy is adopted because:

9. The management no longer wishes to remain in business either partly or wholly due to continuous losses and inviability
10. The environment faced is threatening
11. Stability can be ensured by reallocation of resources from unprofitable to profitable businesses.

- Combination strategy is adopted because:

12. The organization is large and faces a complex environment
13. The organization is composed of different businesses, each of which lies in a different industry requiring a different response

Portfolio Restructuring

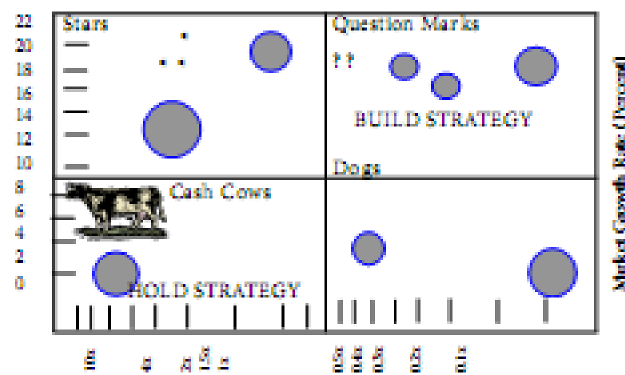
Large, diversified organizations commonly use a number of these strategies in combination. For example, an organization may simultaneously seek growth through the acquisition of new businesses, employ a stability strategy for some of its existing businesses, and divest itself of other businesses. Clearly, formulating a consistent organizational strategy in large, diversified companies is very complicated, because a number of different business – level strategies need to be coordinated to achieve overall organizational objectives. Business portfolio models are designed to help managers deal with this problem.

Business portfolio models are tools for analyzing (1) the relative position of each of an organization's businesses in its industry and (2) the relationships among all the of the organization's businesses. Two well-known approaches to developing business portfolios include:

- Boston Consulting Group (BCG) growth – share matrix
- General Electric's (GE's) multi-factor portfolio matrix.

BCG's Growth – Share Matrix

The Boston Consulting Group, a leading management consulting firm, developed and popularized a strategy formulation approach called the growth – share matrix, which is shown in Figure 9-3. The basic idea underlying this approach is that a firm should have a balanced portfolio of businesses such that some generate more cash than they use and can thus support other businesses that need cash to develop and become profitable. The role of each business is determined on the basis of two factors: the growth rate of its market and the share of that market that it enjoys.



Relative Market Share

Figure9-3 BCG's Growth – Share Matrix (Source: Adapted from B. Hedley, "Strategy and the Business Portfolio," Long Range Planning, February 1977, p.12.

The vertical axis indicates the market growth rate, what is the annual growth percentage of the market (current or forecasted) in which the business operates. The horizontal axis indicates market share dominance or relative marker share. It is computed by dividing the firm's market share (in units) by the market share of the largest competitor).

The growth – share matrix has four cells, which reflect the four possible combinations of high and low growth wit high and low market share. These cells represent particular types of businesses, each of which has a particular role to play in the overall business portfolio. The cells are labeled:

1. **Question marks (sometimes called problem children)** Company business that operate in a high-growth market but have low relative market share. Most businesses start off as question marks, in that they enter a high – growth market in which there is already a market leader. A question mark generally requires the infusion of a lot of funds. It has to keep adding plant, equipment, and personnel to keep up with the fast – growing market, and it wants to overtake the leader. The term question mark is well chosen, because the organization has to think hard about whether to keep investing funds in the business or to get out.
2. **Stars** They are question – mark businesses that have become successful. A star is the market leader in a high – growth market, but it does not necessarily provide much cash. The organization has to spend a great deal of money keeping up with the market's rate of growth and fighting off competitors' attacks. Stars are often cash – using rather than cash –generating Even so, they are usually profitable in time.
3. **Cash cows** Businesses in markets whose annual growth rate is less than 10 percent but that still have the largest relative market share. A cash cow is so called because it produces a lot of cash for the

organizations. The organization does not have to finance a great deal of expansion because the market's growth rate is low. And the business is a market leader, so it enjoys economies of scale and higher profit margins. The organization uses its cash-cow businesses to pay its bills and support its other struggling businesses.

4. **Dogs** Businesses that have weak market shares in low-growth markets. They typically generate low profits or losses, although they may bring in some cash. Such businesses frequently consume more management time than they are worth and need to be phased out. However, an organization may have good reasons to hold onto a dog, such as an expected turnaround in the market growth rate or a new chance at market leadership.

After each of an organization's businesses is plotted on the growth – share matrix, the next step is to evaluate whether the portfolio is healthy and well balanced. A balanced portfolio has a number of stars and cash cows and no too many questions marks or dogs. This balance is important because the organization needs cash not only to maintain existing businesses but also to develop new businesses. Depending on the position of each business, four basic strategies can be formulated:

1. **Build market share** This strategy is appropriate for question marks that must increase their share in order to become stars. For some businesses, short-term profits may have to be forgone to gain market share and future long-term profits.
2. **Hold market share** This strategy is appropriate for cash cows with strong share positions. The cash generated by mature cash cows is critical for supporting other businesses and financing innovations. However, the cost of building share for cash cows is likely to be too high to be a profitable strategy.
3. **Harvest** Harvesting involves milking as much short-term cash from a business as possible, even allowing market share to decline if necessary. Weak cash cows that do not appear to have a promising future are candidates for harvesting, as are question marks and dogs.
4. **Divest** Divesting involves selling or liquidating a business because the resources devoted to it can be invested more profitably in other businesses. This strategy is appropriate for those dogs and question

marks that are not worth investing in to improve their positions.

However the growth share matrix is not fool proof. It has the following loopholes.

- Focuses on balancing cash flows only but organizations are mostly interested in return on investments.
- Is not always clear what share of what market is relevant in the analysis.
- Believes that there is a strong relationship between market share and return on investment. But research proves that only a 10% change in market share is associated with only 'percent change in return on investment.
- The other factors like size and growth profile of the market and distinctive competences of the firm, competition etc is not considered.
- It does not provide direct assistance in comparing different businesses in terms of investment opportunities. For example it is difficult to decide between two question marks and decide which should be developed into a star.
- Offers only general strategy recommendations without specifying how to implement them.

Ge Multi-Factor Port Folio Matrix

This approach has a variety of names, including the nine -cell GE matrix, GE's nine-cell business portfolio matrix, and the market attractiveness – business strengths matrix. The basic approach is shown in Figure 9-4. Each circle in this matrix represents the entire market, and the shaded portion represents the organization's business market share

Each of an organization's businesses is plotted in the matrix on two dimensions, industry attractiveness and business strength. Each of these two major dimensions is a composite measure of a variety of factors. To use this approach, an organization must determine what factors are most critical for defining industry attractiveness and business strength. Table below lists some of the factors that are commonly used to locate businesses on these dimensions.

The next step in developing this matrix is to weight each variable on the basis of its perceived importance relative to the other factors (hence the total of the weight must be 1.0). Then managers must indicate, on a scale of 1 to 5, how low or high their business scores on that factor.

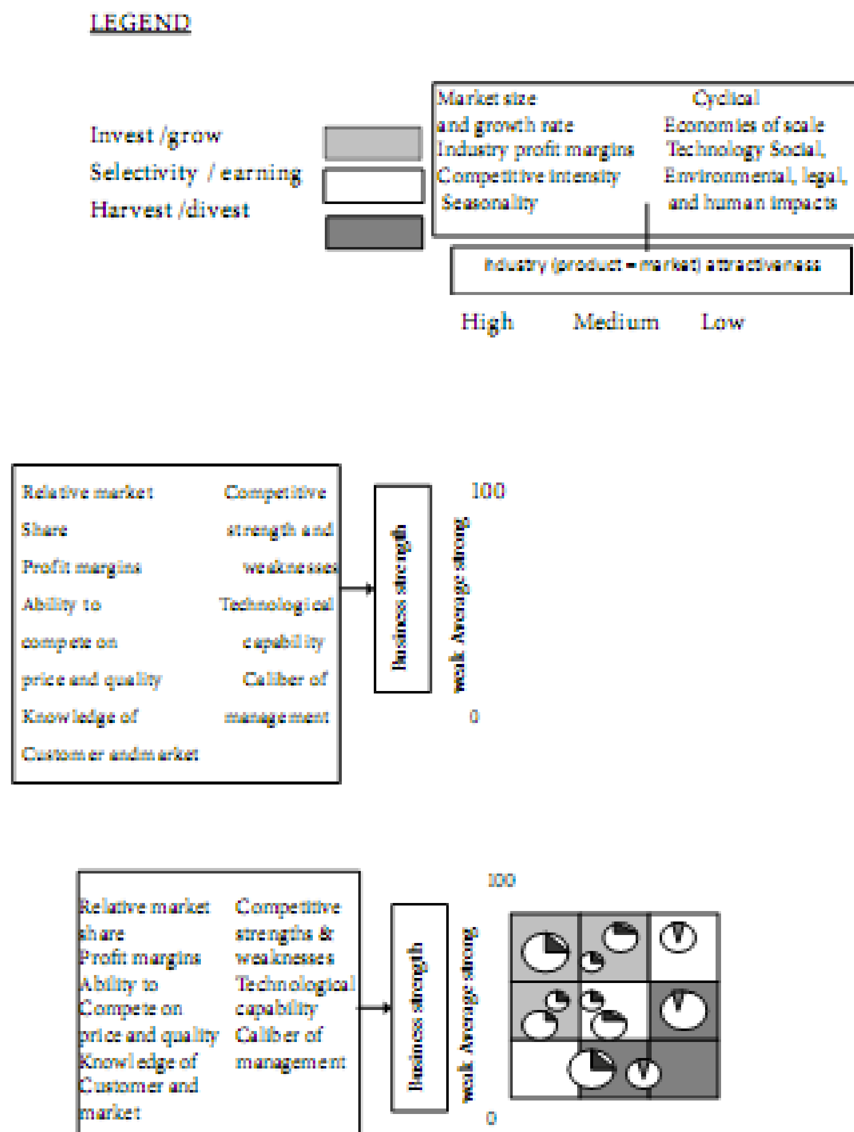
Table 9-3 Factors Contributing to Industry Attractiveness and Business Strength.

INDUSTRY ATTRACTIVENESS	BUSINESS STRENGTH
Market Factors	
Size (dollars, units or both)	Your share (in equivalent terms)
Size of key segments	Your share of key segments
Growth rate per year:	Your annual growth ratae:
Total	Total
Segments	Segments
Diversity of market	Diversity of your participation
Sensitivity to price, service features, and external factors	Your influence on the market
Cyclicality	Lags or leads in your sales
Seasonality	Bargaining power of your suppliers
Bargaining Power of Upstream Suppliers	Bargaining power of your customers
Bargaining Power of Downstream Suppliers	
Competition	

Types of competitors Degree of concentration Changes in type and mix Entries and exits Changes in share Substitution by new technology Degrees and types of integration	Where you fit, how you compare in terms of products, marketing capability, service, production strength, financial strength, management Segments you have entered or left Your relative share change Your vulnerability to new technology Your own level of integration
Financial and Economic Factors	
Contribution margins Leveraging factors, such as economies of scale and experience Barriers to entry or exit (both financial and non-financial) Capacity utilization	Your margins Your scale and experience Barriers to your entry or exit (both financial and non-financial) Your capacity utilization
Technological Factors	
Maturity and volatility Complexity Differentiation Patents and copyrights Manufacturing process technology required	Your ability to cope with change Depths of your skills Types of your technological skills Your paten protection Your manufacturing technology
Socio-Political Factors in Your Environment	

Social attitudes and trends Laws and government agency regulations Influence with pressure groups and government representatives Human factors, such as unionization and community acceptance.	Your company's responsiveness and flexibility Your company's ability to cope Your company's aggressiveness Your company's relationships.

Figure 9-4 GE Matrix General Electric's nine- cell planning grid



Depending on where businesses are plotted on the matrix, three basic strategies are formulated

- Invest/grow,
- Selective investment, and
- Harvest/divest.

Businesses falling in the cells that form a diagonal from lower left to upper right are medium-strength businesses that should be invested in only selectively. Businesses in the cells above and to the left of this diagonal are the strongest; they are the ones for which the company should employ an invest/grow strategy. Businesses in the cells below and to the right of the diagonal are low in overall strength and are serious candidates for a harvest/divest strategy.

This approach has several advantages over the growth-share matrix.

- First, it provides a mechanism for including a host of relevant variables in the process of formulating strategy.
- Second, as we have noted, the two dimensions of industry attractiveness and business strength are excellent criteria for rating potential business success.
- Third, the approach forces managers to be specific about their evaluations of the impact of particular variables on overall business success.

However, the multifactor portfolio matrix also suffers some of the same limitations as the growth –share matrix.

- It does not solve the problem of determining the appropriate market, and it does not offer anything more than general strategy recommendations.
- The measures are subjective and can be very ambiguous, particularly when one is considering different businesses.

Portfolio models provide graphical frameworks for analyzing relationships among the businesses of large, diversified organizations, and they can yield useful strategy recommendations. However, no such model yet devised provides a universally accepted approach to dealing with these issues. Portfolio models should never be applied in a mechanical fashion, any conclusion they suggest must be carefully considered in the light of sound managerial judgment and experience.

Self -Assessment Questions

1. "Grand strategies are intended to provide basic direction for strategic actions" – Discuss.
2. Identify generic and grand strategies that firms adopt.
3. Explain the generic strategies given by Michel E. Porter with Indian examples.
4. Examine the significance of Gluek's grand strategies and discuss how they help achieve overall objectives of a firm.
5. Explain horizontal and vertical integration strategies.
6. What is diversification? Explain why it is followed.
7. What are stability strategies? When do firms employ them?
8. What are the methods adopted for turnaround?
9. Explain retrenchment strategy? Do firms employ it?
10. Examine the significant of portfolio strategies.

Activities

1. Go to a business firm near your college. Discuss with the Managing Director and top level strategists and identify the generic strategies you believe they are using.
2. Identify the Indian companies that have adopted the grand strategies in India from www.blonnet.com website of The Hindu – Business Line and list them briefly.

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Lesson 10 - Strategic Alliances And Joint Ventures

Lesson Outline

- Introduction
- Strategic Alliances
- Reasons For Forming Alliances
- Types Of Alliances
- Typology Of Alliance
- Continuum Of Alliances
- Mutual Service Consortia
- Joint Venture Licensing Arrangement
- Value-Chain Partnership
- Forms Of Alliances In India
- Managing Strategic Alliances

Learning Objectives

After reading this lesson you should be able to

- Understand and define strategic alliances
- Examine the reasons for forming alliances
- Outline the types of alliances
- Know how Indian companies have formed alliances
- Explain the methods of managing alliances

Introduction

Intense competition, changing technology and need for expansion drive firms to look out for opportunities to take over other firms or form alliances. When geographical boundaries are open for business operations, international tie-ups are common. Strategic alliances may take different forms from just marketing or production tie-ups to mergers. Managing alliances requires special caution, and managers should be aware of the principle of managing them.

Strategic Alliances – Defined

Strategic alliances are cooperation arrangements between two or more companies for achieving a common objective. Yoshino and Rangan define strategic alliances in terms of three necessary and sufficient characteristics

1. Two or more firms unite to pursue a set of agreed upon goals but remain independent subsequent to the formation of the alliance,
2. The partner firms share the benefits if the alliance and control over the performance of assigned tasks –perhaps the most distinctive characteristic of alliances and the one that makes them so difficult to manage,
3. The partner firms contribute on a continuing basis on one or money key strategic areas, for example, technology, product, and so forth.

In similar words , Lando Zeppi, Managing partner of Booz, Allen and Hamilton, defines strategic alliance as :

a cooperative arrangement between two or more companies where:

- A common strategy is developed in unison and a win-win attitude is adopted by all parties
- The relationship is reciprocal, with each partner prepared to share specific strengths with each other, thus lending power to the enterprise.
- A pooling of resources, investments, and risks occurs for mutual (rather than individual gain)

Strategic alliances can be defined simply as:

"a cooperation between two or more independent firms involving shared control and contributing contributions by all partners for mutual benefit".

Some alliances are short term and some are long term leading to full mergers of companies.

Reasons for Forming Strategic Alliances

The basic reason for entering into strategic alliance is to enhance their organizational capabilities and there by gain competitive advantage. Towards this they strive to gain access to new markets and new supply

resources sufficiently they enter into strategic alliances. Specifically speaking the following are the principal reasons.

1. To obtain technology and / or manufacturing capabilities

For example, Intel formed a partnership with Hewlett-Packard to use HP's capabilities in RISC technology in order to develop the successor to Intel's Pentium microprocessor.

2. To obtain access to specific markets

Rather than buy a foreign company or build breweries of its own in other countries, Anheuser-Busch chose to license the right to brew and market Budweiser to other brewers, such as Labatt in Canada, Modelo in Mexico, and Kirin in Japan. The alliance of coco cola Inc. with local bottling mergers in the global market and even in India.

3. To reduce financial risk

To reduce the risk of financial investment a company may join hands with another company or companies

Because the costs of developing a new large jet airplane is becoming too high for any manufacturer, Boeing, Aerospatiale of France, British Aerospace, Constucciones Aeronautics of Spain, and Deutsche Aerospace of Germany planned a joint venture to design such a plane.

4 To reduce political risk

Political risk is another important factor. Besides cultural factors, political factors are complex and difficult to mange. It is better to tie up with a local firm to find way s of overcoming such risks.

To gain access to China while ensuring a positive relationship with the often restrictive Chinese government, Maytag Corporation formed a joint venture with the Chinese appliance maker, RSD.

5 To achieve or ensure competitive advantage

Alliances may be formed for mutual advantage to use of the specialized nature of resources or skills.

General Motors and Toyota formed Nummi Corporation as a joint venture to provide Toyota a manufacturing facility in the United States and GM access to Toyota's low-cost, high-quality manufacturing expertise.

IBM's strategy

IBM's current alliance strategy in large measure is due to several key driving factors:

(1)To enter new markets,

(2) To fill gaps in its product line with other firm's offerings,

(3) To shorten product development time,

(4) To learn new technologies,

(5) To restructure some existing operations, and

(6) To block other key rivals from encroaching on the U.S. and European markets too quickly.

IBM has formed more than 500 strategic alliances (of varying degrees of complexity) with partners around the world. These strategic alliances involved not only shared marketing and software development efforts, but also major commitments of investment funds to build ultra-modern facilities that are beyond the financial means of any one company. The following Table 10-1 portrays some of the most significant alliance relationships the IBM has entered as of December 1997.

Table 10-1: IBM Alliance Strategy

Personal Computers	Semiconductor Technology	Software and Processing
• Matsushita (Lowend PCs) • Ricoh (Hand-held PCs) **Computer Hardware/ Screens** • Toshiba (Display tech) • Mitsubishi (Mainframes) • Canon (Printers) • Hitachi (Large printers) **Factory Automation** • Texas Instruments • Sumitomo Metal • Nippon Kokan technology • Nissan Motor **Telecommunications** • NTT (Value-added Networks) • Motorola (Mobile data mets)	• Micron Technology • Motorola (X-ray lithography) • Motorola (Micro processor designs) • Sematech (U.S. Consortium) • Intel (Microprocessor designs) • Siemens (16 M and 64 Megabit chips) • Apple Computer (Operating Systems and multimedia • Integration • Elec (Electron bean technology) • Toshiba & Siemens (256 Megabit chips) • Toshiba (Flash memories) • Advanced Micro Devices (Microprocessors) • Silicon Valley Group (Photolithography)	• Microsoft • Oracle • Sun Microsystems • Silicon Graphics • Metaphor • Hewlett-Packard • Netscape Communications **Customer Linkages** • Mitsubishi Bank • Eastman Kodak • Baxter Healthcare • Xerox **Consumer Electronics** • Philips Electronics • Sega • Blockbuster Entertainment • Sony

Typology of Strategic Alliances

Several typologies of strategic alliances are available in business literature. One such classification is by Yoshino and Rangan. This is a two-dimensional model with the two dimensions being, the extent of organizational interaction and conflict potential between alliance patterns. The classification is shown in Figure 10-1.

Figure 10-1 Typology of Strategic Alliances

Low **Conflict** High

interaction

Non-competitive	Competitive
Pro-competitive	Pre-competitive

Pro-Competitive Alliances

These are generally alliances within the industry exemplified by vertical value-chain relationships between manufactures and their suppliers and distributors. Such relationships are advantageous to both parties. Supplier and buyer organizations entering upon long-term contracts constitute pro-competitive alliances.

Noncompetitive Alliances

These are partnerships within the industry. Such alliances are entered upon by organizations that operate in the some industry yet do not perceive each other's as rivals. This can be because their areas of activity do not coincide and/or their products and services are sufficiently dissimilar to prevent competition. Organizations that have carved out distinct areas in the industry geographically or otherwise, adopt the noncompetitive alliances. For example, a number of automotive manufacturers in Europe have entered into a strategic alliance for engine development.

Competitive Alliances

These are relationships that bring rival organizations in a cooperative arrangement. These alliances may be intra –industry or inter-industry.

For example Coca-Cola entered into an agreement with Parle Products, the manufacturers of Thumps Up their main competitors in western India.

Pre-competitive Alliances

These partnerships bring two organizations from different, often unrelated industries to work on well-defined activities. This is often seen in activities such as, mass awareness campaigns or environmental and social issues. Sometimes inter industry and inter disciplinary cooperation is necessary for development.

For example, Intel has pre-competitive alliances with software, hardware and other manufacturers.

Continuum of Alliances

The types of alliances range from mutual consortia to value chain partnerships as described below.

- Mutual service consortia- A mutual service consortium is a partnership of similar companies in similar industries who pool their resources to gain a benefit that is too expensive to develop alone, such as access to advanced technology. For example, IBM of the United States, Toshiba of Japan, and Siemens of Germany formed a consortium to develop new generations of computer chips.
- Joint venture – A joint venture is a "cooperative business activity formed by 2 or more separate organizations for strategic purposes, that creates an independent business entity and allocates ownership, operational responsibilities, and financial risks and rewards to each member, while preserving their separate identity autonomy.
- Licensing arrangement – A licensing arrangement is an agreement in which the licensing firm grants rights to another firm in another country or market to produce and / or sell a product. The licensee

pays compensation to the licensing firm in return for technical expertise.

- Value-chain partnership – The Value-chain partnership is a strong and close alliance in which one company or unit forms a long-term arrangement with a key supplier or distributor for mutual advantage.

Forms of Alliances in India

A statistical sample of different strategic alliances in India with number of companies in different alliances and their percentage is listed in Table 10-2.

Table 10-2 Type of alliances in India

Type of alliance	Number of Companies	Percentage (%)
Marketing tie ups	34	26.3
Operations handling	21	16.2
Joint ventures	15	11.6
Technology licensing	14	108
Manufacturing	14	10.8
MOUs	9	6.9
Services	6	4.6
Supply	6	4.6
Setting up new business	6	4.6

After liberalization, JVs are less since MMCs can set up a 100% subsidiary after 1991. Therefore Indian market is witnessing breaking up of joint ventures. On the other hand, Indian firms are going for JV abroad for reasons like.

- Source of learning and development
- Access to better infrastructure
- Access to greater market share
- Availability of raw materials

Delta Industries took over Netherlands Jute Industries (NJI) in 1994 which led to cost effective production in the country with advanced technology. Several alliances such as TVS-Sujuki, Mahindra-Ford, BPL-Sanyo and Videocon- Sansui have withstood the test of the time. Ranbaxy went into a strategic alliance with Eli Lilly of the US to realize its mission of becoming a research based international and pharmaceutical company.

The opening up of infrastructure sector in India led to forming of a number of alliances.

- The telecommunications sector has witnessed the coming together of several local and global firms such as Crompton Greaves and Millicom, the SPIC group and Telstra, Max (GSM) and Brtisih Telecom, Usha Martin and Telecom Malaysia, among several others.
- The roads and highways sector has created conditions for several global giants joining hands with reputed Indian companies like the alliances of Unitech and Hyndai, Engineering and Constructions, THC India and Trafalgar House International, Tarmat and Samsung, and others.

Liberalization and globalization have spurred the growth of strategic alliances. A good example of synergetic benefits arising out of a strategic alliance is that of Taj Hotels and British Airways, where both create advantages for each other through complementarities of airline and hotel services.

Besides this, other reasons, which lead to strategic alliances, are the availability of professional management expertise, international reputation, global brand name and brand equity, and confidence to gain a foothold in the international markets.

Alliances are often used by not- for- profit organization as a way to enhance their capacity to serve clients or to acquire resources while still enabling them to keep their identity services can be provided efficiently through cooperation with other organizations them if they are done alone.

Four Ohio Universities agreed to start a new school of international business at a cost of $ 30 million. This cannot be done singly.

Managing Strategic Alliances

The following guidelines will be of help in successfully managing alliances.

- Have a clear strategic purpose. Integrate the alliance with each partner's strategy. Ensure that mutual value is created for all partners.
- Find a fitting partner with compatible goals and complementary capabilities
- Identify likely partnering risks and deal with them when the alliance is formed.
- Allocate tasks and responsibilities so that each partner can specialize in what it does best.
- Create incentives for cooperation to minimize differences in corporate culture or organization fit.
- Minimize conflicts among the partners by clarifying objectives and avoiding direct competition in the market place.
- If an international alliance, ensure that those managing it should have comprehensive cross-cultural knowledge.
- Exchange human resources to maintain communication and trust. Don't allow individual egos to dominate
- Operate with long-term time horizons. The expectations of future gains can minimize short-term conflicts.
- Develop multiple joint projects so that any failures are counterbalanced by successes
- Agree upon a monitoring process. Share information to build trust and keep projects on target. Monitor customer responses and service complaints.
- Be flexible in terms of willingness to renegotiate the relationship in terms of environmental changes and new opportunities.
- Agree upon an exist strategy for when the partners' objectives are achieved or the alliance is judged a failure

Self -Assessment Questions

1. What do you understand by strategic alliances?
2. Why are strategic alliances necessary?
3. What are the forms of strategic alliances?
4. Illustrate and explain the continuum of Alliances
5. What are joint ventures? When are they formed?
6. With examples of Indian companies, discuss the significance of joint ventures
7. Examine the advantages and disadvantages of join ventures.
8. Why do joint ventures fail? Explain with examples.
9. In the globalization era, which form of alliances work?
10. How do you make strategic alliances successful?

Activities

1. Describe the long-term strategy of the firm or institution in which you are working or studying. Identify the alliances needed to make the institution strong in the globalized set up.
2. Identify the companies that have entered into mutual service consortia, joint venture licensing agreement and value chain partnerships in India. Visit a library, search dailies and business, weeklies and identify some of them and prepare a list.

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Lesson 11 - Diversification Strategies

Lesson Outline

- Introduction
- Why diversify?
- Types of diversification
- Advantages and disadvantages of Diversification
- Diversifications in India
- Planned Diversification
    - Assessment of industry attractiveness
    - Assessment of degree of mesh
    - Combination of attractiveness And mesh
- When to diversify
- When not diversify
- Summary
- Self assessment questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand the concept of diversification
- Describe the types, merits and demerits of diversification
- Know how to assess systematically for diversification
- Know when to diversify and not diversify

Introduction

Diversification is one of the grand strategies, which basically is a growth strategy. Basically diversification involves a substantial

change the business definition in terms of product range, customers or alternative technologies. Diversification strategies have been adopted a number of business groups and individual companies both in the public and private sectors. 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. Overall, diversification strategies are becoming less popular as organizations are finding it more difficult to manage diverse business activities. Diversification is now on the retreat. Michael Porter of the Harvard Business School says, "Management fount [it] couldn't manage the beast." Hence, businesses are selling or closing, less profitable divisions in order to focus on core business.

Why Diversify?

Organizations diversify due to the following reasons. Some of the common reasons are as follows.

Synergy

Synergy is cited in the most common cause of diversification. Synergy occurs when two or more activities produce their combined effect greater than the sum of its parts i.e., 2 + 2 = More than 4.

- Related diversification produces synergies rooted in production technology. With the additional technical facilities, a by-product or joint product may be produced.
- Both related and unrelated enable the companies to sell the products with same distribution network and advertisement facilities. The advertisement of one product spontaneously advertises other products with enhanced brand loyalty. This is marketing synergy.
- Synergetic effect can also be noticed in financial operations, when the positive cash flow of one business utilized in other business helps to generate more positive cash flows.

Spreading of Risk

Diversification helps to avoid over dependence on one product/ market. It spreads the risk associated with one product line or few products.

Better opportunities

With diversification, company can exploit the better opportunities in new product line. Every product has it own product life cycle. To gain better market share, company has to either differentiate or diversify.

Better utilization of Resources

With diversification, company can better use hitherto unexploited resources like finance, market channels, production facilities, technological capabilities, managerial knowledge, etc. The idle retained earnings could be utilized to produce new products. Their marketing may not be a problem because the same dealers will sell the new products. Same production facilities and technology can be utilized sometimes adding more capacity to it.

Competitive Strategy

Diversification is a good competitive strategy. A company may enter new product lines of business to gain a competitive edge over the competitors or discourage them by entering before their arrival.

Market Dominance

Diversification take place to exploit tremendous market opportunities in home as well as in foreign countries with the objective of gaining market dominance.

Finnish producer Nokia leads the world in sales of cell-phone handsets. When the telecom industry crashed in 2000. Chairman Jorma Ollila invested heavily to turn Nokia into a major mobile phone software player. Under his leadership, the organization licensed its interface software to cell-phone competitors. It also invested heavily in billing and messaging service software. The result: millions of customers using Nokia and other software can now use their handsets to get e-mail, send photos, and download games. Research organization IDC forecasts that global mobile-data business will increase almost 47% in 2003 to $29.5 billion. Diversifying into mobile phone software helped keep Nokia on top of a troubled industry.

Source: "The Comeback kids" "Business week, September 29, 2003 p. 122

Types of Diversification

There are three general types of diversification strategies: concentric horizontal, and conglomerate.

Concentric Diversification

Under concentric diversification new products and services are added to the line with the condition that these products and services are related to their existing products/services carried by the organization. For concentric diversification it becomes necessary that the products or services that ate added must be within the framework of the know how and experience in technology, product line, distribution channels or customer base of the organization.

When the industry grows, the organization will get strength where concentric diversification becomes an important strategy for its survival and growth. A study of 460 corporations accounting for two/thirds of the US corporate industrial assets concluded, "that diversification that has led to relatively rapid rates of corporate growth has been to markets that are related to the entering organization's original market. Concentric diversification has been successfully practiced by a large number of organizations in India. For instance "Amul" has diversified in chocolates, Ice creams, Butter, Ghee etc. On the same pattern, "Milk Food" has diversified. Similarly, Honda has diversified into to Motor Cycles, Cars etc. In conclusion, it may be stated that concentric diversification has been quite successful in the past; it is expected to be successful in future also.

Horizontal Diversification

Where an organization adds unrelated products and services for existing customers, this is called horizontal diversification. The strategy is comparatively less risky because the customers are known. The organization is fully acquainted with their consumers' preference and their expectations about the quality and price of the goods and services.

Horizontal diversification can be accomplished by acquiring the shareholding of the competitor, by the purchase of the assets or by pooling of the interests of two organizations. .Horizontal diversification seeks to eliminate competitors.

In our country a T.V. manufacturing company Uptron has created a new division for spreading computer education in the country. It is a combination of hardware and software.

Conglomerate Diversification

Conglomerate diversification is a growth strategy in which new products and services are added which are significantly different from the organization's present product and services. Conglomerate diversification is effected in the hope that the addition of new products and services may bring about some turnaround by way of conversion of losses into profits. Mechanics for adopting conglomerate diversification has been summarized as follows:

1. Supporting some divisions with cash flow from other divisions during the period of development or temporary difficulty.
2. Using the profits of one division to cover the expenses of another division without payment of taxes from the first division.
3. Encouraging growth for its own sake or to satisfy the values and ambitions of management or the owners.
4. Taking advantage of unusually attractive growth opportunities.
5. Distributing risk by serving several different markets.
6. Improving overall profitability and flexibility of the organization by moving into industries that have better economic prospects than those of the acquiring organizations.
7. Gaining better access to capital markets and better stability or growth in the earnings.
8. Increasing the price of an origination's stock
9. Reaping the benefits of synergy. Synergy results from "a conglomerate merger when the combined organization is more profitable than the two organizations operating independently.

The scheme of Conglomerate Diversification should be implemented with caution and patience. It will create big business and will bring in turn, the problems of management associated with big businesses. Big businesses involve greater risk in the event of abnormal economic situation like recession or stagflation. In the light of the above, the success of the conglomerate diversification will depend on the following factors:

1. A clear definition of organizational objectives.
2. A determination of the organization's ability to diversify, which includes an analysis of its present operations (internal organizational analysis) and resources available for diversification.
3. Establishment of specific criteria for purchasing other organizations
4. A comprehensive search for organizations and their evaluation against the criteria.

Examples of companies that have diversified into related business concentric diversification

GILLETTE

- Blades and razors
- Toiletries (Right Guard, Foamy, Dry Idea, Soft & Dry , White Rain)
- Oral-B toothbrushes
- Braun shavers, coffeemakers, alarm clocks, mixers, hair dryers, and electric toothbrushes
- Duracell batteries.

JOHNSON & JOHNSON

- Baby products (powder, shampoo, oil, lotion)
- Band-Aids and other first-aid products
- Women's health and personal care products (Stay free, Carefree, Sure & Natural)
- Neutrogena and Aveeno skin care products
- Nonprescription drugs (Tylenol, Motrin, pepcid AC, Mylanta, Monistat)
- Prescription drugs

- Prosthetic and other medical devices
- Surgical and hospital products
- Accuvue contact lenses

PEPSICO

- Soft drinks (Pepsi, Diet Pepsi, Pepsi One, Mountain Dew, Mug, Slice)
- Fruit juices (Tropicana and Dole)
- Sports drinks (Gatorade)
- Other beverages (Aquafina bottled water, SoBe, Lipton ready-to-drink tea, Frappucino-in partnership with Starbucks, international sales of 7UP)
- Snacks foods (Fritos, Lay's Ruffles, Doritos, Tostitos, Santitas, Smart Food, Rold Gold pretzels, Chee-tos, Grandma's cookies, Sun Chips, Cracker jack, Frito-Lay dips and salsas)
- Cereals, rice, and breakfast products (Quaker oatmeal, Cap'n Crunch, Life, Rice-A-Roni, Quaker rice cakes, Aunt Jemina mixes and syrups, Quaker grits)

Examples of companies that have diversified into unrelated business.
THE WALT DISNEY COMPANY

- Theme parks
- Disney Cruise Line
- Resort properties
- Move, video, and theatrical productions (for both children and adults)
- Television broadcasting (ABC, Disney Channel, Toon Disney, Classic Sports, Network, EPSN and EPSN2, E!, Lifetime, and A&E networks)
- Radio broadcasting (Disney Radio)
- Musical recordings and sales of animation art
- Anaheim Angles major league baseball franchise (25 percent ownership)
- Books and magazine publishing
- Interactive software and Internet sites
- The Disney Store retail shops.

THE TVS GROUP

- Auto & auto parts
- Coach body building
- Transport
- Fasteners
- Brake linings & clutch facings
- A citation systems for commercial vehicles
- Hire purchase
- Wheel structure & parts
- Foundation brakes
- Two wheelers
- Automobile electrical parts
- Tyres & tubes.

Advantages and Disadvantages of Diversification

A company planning to diversification should define its business, conduct SWOT analysis, Risk analysis, competition and Gap analysis and also assess the advantages and disadvantages of diversification. The following Table11-1 briefly outlines the advantages and disadvantages of different types of diversification.

Table 11-1 Advantages and disadvantages of diversification strategies

Diversification strategy	Advantages	Disadvantages
Horizontal integration	Eliminates competitors. Access to new markets.	Less flexibility. Increasing risk and commitment.
Concentric diversification	Synergy by sharing skills and resources. Economics of scale and tax benefits.	Reduction is flexibility. Additional investment. Untried markets and technologies.

Conglomerate diversification	Better management and high ROI. Reducing risk by spreading business.	Lack of concentration. Risks of managing entirely new business.

Diversifications in India

Diversification strategy is widely adopted in India. Some examples are given here.

- A public sector giant, Oil India Ltd. (OIL), which had been operating in oil exploration and production, diversified into related areas, such as, gas cracking.
- The reputed multinational affiliate, ITC Ltd. has diversified into hotels, papers, agri-business packaging, and priming from its original cigarette business in response to national objectives and priorities.
- Smaller companies, like, Blowplast in the moulded luggage industry is in plastic seating systems, and marketing of branded toys.
- Unitech in civil engineering is into steel-making, exports, consumer electronics, power transmission, and real estate.
- The service sector has not been left untouched by the motivation to diversify.
- LIC in the insurance business is also in a related area of mutual funds.
- Banks, like SBI and Canara Bank too have moved from traditional banking to merchant banking and mutual funds.
- Peerless General Finance & Investment Co, one of the country's larger non-banking investment companies, has moved into related areas of finance, adopting a defensive diversification strategy to generate more resources to contain rising establishment costs.

Planned Diversification

The one best way of diversifying an organization is to carry the work through systematic planning. Though many organizations have

diversified without any systematic planning, the chances for a successful outcome are considerably increased when diversification decision is organic part of the comprehensive strategic planning.

In this process, it is preferable to constitute a tasks force, which is entrusted with the total work of diversification because it requires separate emphasis on some aspects at least for some period of time. When this task force is created, it can move in the direction of thinking about possible diversification. The work of the task force becomes easier if it has the full support of top management. The role of this task force may be to collect and analyze relevant information, which helps in arriving at diversification decision.

The basic problem in a diversification strategy is to identify the suitable industry sector, which meets basic criteria of diversification. Figure 11-1 presents a process thorough which identification of diversification opportunities becomes systematic. The process provides the facility for assessing and measuring each business sector against a number of different criteria so that judgment can be reached on two separate factors .

- Attractiveness of the sector as an investment in its own right and
- The extent to which the qualities required for success in the sector match the own strengths of the organization.

There are basically three major measurements involved in this process.

- Measurements of industry attractiveness,
- Measurement of mesh, and

Combination of attractiveness and mesh to arrive at some strategic alternatives

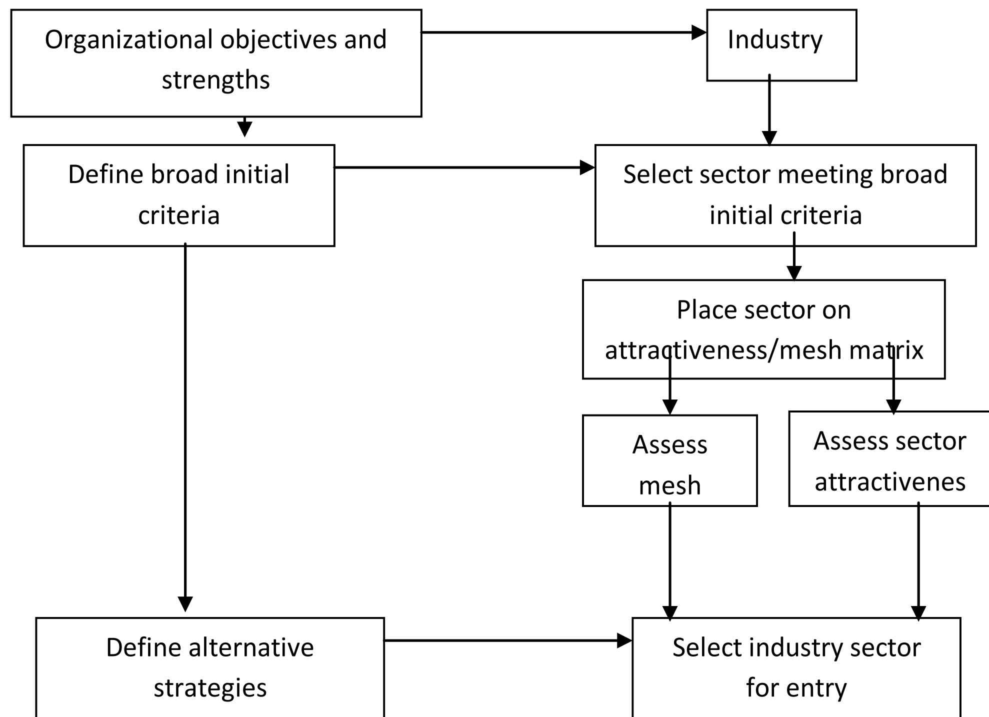
(i) Assessment of Industry Attractiveness

At the initial stage, various sectors of the industry can be taken for identifying diversification opportunities. Such criteria may be in the form of:

i. Acceptable product groups or functions,
ii. Minimum sales volume within a specified period of time, say five years or so,

iii. Minimum projected growth rate in the market
iv. Minimum profitability criteria,
v. Maximum and minimum investment required in the project, and so on.

Figure11-1 Process for identifying diversification opportunities



These criteria may be used in weeding out the industry sectors which cannot be considered. The assessment of the attractiveness of a sector as an area for potential investment is based on its profitability and maturity. The profitability of a sector is measured in terms of return on investment (ROI) of the principal companies within the sector. The profitability ratio may be assigned scores. Scoring pattern may differ from organization to organization depending on manager's preference and interpretation. For example, following scores may be given to various levels of profitability:

ROI per cent	Scores
Less than 10	2

10 -15	4
15-20	6
20-25	8
25-30	10
Above 30	12

The maturity of industry is taken on the basis of level of growth and future potential. Thus industry sectors can be classified into growing, maturing, ageing. In growing sector, the rate of growth is more than the rate of gross national product; in maturing industry, the rate of growth is almost similar to gross national product; while in ageing sector, the rate of growth is lower than the rate of gross national product. These stages can further be classified on the basis of time taken by a sector to move from one stage to another and scores can be assigned in the following way.

Maturity level	Scores
Ageing	0
Late mature	2
Early mature	4
Late growth	6
Growth	8
Early growth	10

Adding the scores for profitability to the sector maturity arrives at the scoring for over all attractiveness of each sector.

(ii) Assessment of Degree Mesh

Degree of mesh suggests the extent to which a particular organization can match the requirements of an industry sector. It is assess on the basis of organizational strengths and critical success factors (CSFs) required for success in the industry sector. CSFs are those

characteristics, conditions, or variables that when properly sustained, maintained, or managed can have a significant impact on the success of an organization competing in a particular industry. From the structure and maturity of sector, certain general conclusions can be drawn on CSFs and its investment characteristics.

1. In growth sector, high market share at the time of entry is not crucial because opportunities exist for rationalization and consolidation. Further investment is normally needed.

2. In mature sector, high market share at the time of entry is critical; cost cutting and control is important and further investment is generally not appropriate.

3. In ageing sector, a high market share at the time of entry is critical. Little or no further investment is desirable.

Taking both the factors-organizational strengths and CSFs, mesh matrix can be constructed as depicted in Figure 11-2.

	Critical (4)	High (3)	Medium (2)	Low (1)
(4)	16	12	8	4
(3)	12	9	6	3
(2)	8	6	4	2
(1)	4	3	2	1

Figure11-2 Mesh Matrix

High score in the matrix will increase the upside potential of investment because

- The organization can add something to the operation of the new business, and

- Will decrease the downside risk because the management will have experience of the sort of problems that are likely to occur.

(iii) Combination of Attractiveness and Mesh

Having rated each sector's attractiveness and mesh, we can combine both to form another matrix. Because two measures are independent of each other, we can expect some sectors to score high on attractiveness but low on mesh whereas other sectors score low on attractiveness and high on mesh. The attractiveness/mesh matrix has been presented in Figure 11-3 below

According to this matrix, best diversification opportunities are those that score high on both characteristics having score of 9; least proffered is with low degree of both characteristics having score of 1. The selection of sectors from elsewhere depends on the strategy the organization selects.

- If it wishes to go for growth and earnings, pays low regard to the relationship which a sector has with the organizational strengths may select the alternatives in order of sectors failing in 6,3,8,5,7 and 4 in that preference order. In such a case, the rate of growth and profitability may be high but the risk involved is also high.
- If the organization wishes to minimize mesh risk and pursues business in those sectors which mesh high with its own strengths, it would select sectors in the order of 8,7,6,5,4,3 and 2. These strategies are low-risk ones for the organization.
- If the organization wishes to select business on the basis of both measures, it would select in the order of 9,6,8(6 and 8 equal) 5.
- In the remaining sector, the preference would be in the order of 3,7 (equal) and 2,4 (equal). The strategies in the third alternatives would be balanced ones.

Degree of mesh

High (3)	Medium (2)	Low (1)
9	6	3
8	5	2
7	4	1

Figure 11-3 Attractiveness/mesh matrix

When To Diversify

Diversification merits strong consideration whenever a single-business company is faced with diminishing market opportunities and stagnating sales in its principal business. But there are four other instances that signal the for diversifying:

- When it can expand into industries whose technologies and products complement its present business.
- When it can leverage existing competencies and capabilities by expanding into businesses where these same resource strengths are valuable competitive assets.
- When diversifying into closely related businesses open new avenues for reducing costs.
- When it has a powerful and well-known brand name that can be transferred to the products of other businesses.

When Not Diversify?

All the organizations cannot think of diversification as a strategy. Organizations do not diversify under the following conditions.

- When they are small and cannot afford to try
- When they have no power to sustain
- When they anticipate some pitfalls
- When they are the first to bell the cat in that area.
- When on checking they find their functional skills are insufficient to diversify
- When they don't want to gamble with public investments
- When they do not have attractive tax benefits after diversification

Summary

Pursuing a single-or dominant-business may be preferable to seeking a more diversified business strategy, unless a corporation can develop competitive advantage. The primary reasons for diversification

are value creation through economies of scope, financial economies, or market power; some actions are taken because of government policy, performance problems, uncertainties about future cash flow, or managerial motivations (e.g. to increase compensation). Managerial motives to diversify can lead to over diversification. On the other hand, managers can also be good stewards of the firm's assets.

The level of a firm's diversification is a function of the incentives the firm has to diversify, its resources, and the managerial movies to diversity. Related diversification can create value by sharing activities of transferring core competencies. Sharing activities usually involves sharing tangible resources between businesses. Transferring core competencies involves transferring the core competencies developed in one business to another business. Efficiently allocating resources or restructuring a target firm's assets and placing them under rigorous financial controls accomplish successful unrelated diversification.

Self -Assessment Questions

1. What do you understand by diversification? Is diversification now popular?
2. What motivates a company to diversify?
3. What are the major considerations in diversification?
4. What are the advantages and advantages of various diversification strategies?
5. Explain why unrelated diversification is often said to be riskier than related diversification.
6. What advice would you like to give to a small business owner who is planning to diversify his business?
7. What are the major areas of synergy in related diversification? Is it possible to develop any synergistic effects in case of unrelated diversification? If yes, how?
8. What step as an entrepreneur would you like to take before, actually embarking upon diversification scheme? Discuss the importance of planned diversification in today's business.

9. Critically examine the corporate diversification activity in India.

10. What suggestions you would like to make so that diversification activity in India proceeds on a sound basis?

Activities

1. Study the product/service portfolio of ITC group. ITC is considered to be one of the most diversified firms in India. List its major products and services.

2. Find out from different published sources and the website of Shri Ram group of companies or contact its local office in your place and identify its diversification activity. Record it carefully in writing.

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Lesson 12 - Turnaround Strategies & Corporate Restructuring

Lesson Outline

- Introduction
- Turnaround Defined
- Signals Of Turnaround
- Turnaround Process Models
- Turnaround Management
- Corporate Restructuring
- Forms Of Restructuring
- Types Of Restructuring
- Process And Barriers
- Summary
- Self Assessment Questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Define turnaround strategy
- Identify the signals of corporate sickness
- Know the process models of turnaround and analyze turnaround management issues
- Understand the forms, types, process and barriers of corporate restructuring

Introduction

Turn round strategy is often necessitated during recession times in an industry or in the economy as a whole. It is aimed at halting the present declining trend in performance while improving the long run efficiency of operation.

Turnaround Defined

Turnaround derives its name from the action involved that is reversing a negative trend. Turnaround management refers to the measures, which reverse the negative trends in the performance indicators of the company. In other words, turnaround management refers to the management measures which turn a sick-company back to a be healthy one or those measures which reverse the deteriorating trends of the performance indicators such as falling market share, sales (in constant rupees), and profitability and worsening debt-equity ratio.

Examples of turn around

During 1970-80 IBM dominated the computer industry world wide particularly the PCS. During early 1990s computer sales were falling. HP, Dell, Compaq, Gateway etc entered the market PC clones in IBM style were offered cheaply by them. Industry experts called IBM "bureaucratic dinosaur" and profits kept on falling in 1992-93. The BOD hired a new CEO, Louis Gerstner to lead a 'Corporate turn around' who leads the 'BIG BLUE' strategy following the rigid dress code. The work force was reduced to 40%. Emphasis was on quicker decision making and strong customer orientation. The CEO spoke to atleast one customer a day. A new mainframe was released once in a year. PC business increased its market share to 8.9% in 1996. Stock price moved from $ 40 in 1990 to $ 140 in 1996. Revenue increased by 40% and profits rose by 3.6%. IBM is still in the process of turning around.

Gram co, a subsidiary of UK based EMI UK was successful in the early seventies with brand name HU. The cassette boom hit the company and EMI UK reduced its equity from 38.9% to 20%. RPG was given an equity participation of 16%, financial institutions 26%. Udayam Bose was appointed as MD to run on profit sharing that is from credit capital Finance Corporation. Grams co expanded to consumer electronics

& cassette making and diversified into domestic kitchen equipment, furniture, pumps and automotives. It planned to revive its packaging section also. However the turnaround is a failure

Signals of Turnaround

We need to examine whether companies suddenly turn sick or qualify as potential candidates for turnaround. Sometimes the companies themselves may not be able to identify that they are turning into red. If recognized early prevention can be tried instead of curing the problem. Though the factors leading to industry varies from one firm to the other, there are some common signals of sickness which herald on the onset of sickness. Companies becoming sick would exhibit one or more of the following characteristics.

1. ***Decreasing market share*** This is the most significant symptom of a major sickness. A company, which is losing its market share to competition, needs to sit up and take careful note. Regular monitoring of market share helps companies to keep a tab on their performance in the market vis-a-vis their competitors. Any indication of declining market share should trigger-off immediate corrective action.

2. ***Decreasing constant rupee sales Sales*** figures, to be meaningful, should be adjusted for inflation. If constant rupees sales figures are showing a declining trend, then this is a danger signal to watch out.

3. ***Decreasing profitability*** Profit figures are a good indication of a company's health. Care must be taken to interpret the profit figures correctly, so as to avoid any misjudgments. Decreasing profitability can show up as smaller profits in absolute terms or lower profits per rupee of sale or decreasing return on investment or smaller profit margins.

4. ***Increasing dependence on debt*** A company overly reliant on debts soon gets into a tight corner with very few options left. A substantial rise in the amount of debt, a lopsided debt to equity ratio and a lowered corporate credit rating may cause banks and other financial institutions to apply restrictions and become reluctant to lend more. Once financial institutions are hesitant to lend money, the company's rating on the stock market also slides and it becomes very difficult for the company to raise funds from the public too.

5. ***Restricted dividend policies*** Dividends frequently missed or restricted dividends signal danger. Often such companies may have earlier paid substantially higher proportion of earnings as dividends – when in fact they should have been reinvesting in the business. Current inability to pay dividends in an indication of the gravity of the situation.

6. ***Failure to reinvest sufficiently in the business*** For a company to stay competitive and keep on the fast growth track, it is essential to reinvest adequate amounts in plant, equipment and maintenance, when a business is growing, the combinations of new investments and reinvestments often warrants borrowing. Companies, which fail to recognize this fact and try to finance growth with only their internal funds, are applying brakes in the path of growth.

7. ***Diversification at the expense of the core business*** It is a well-observed fact that once companies reach a particular level of maturity in the existing business they start looking for diversifications. Often this is done at the cost of the core business, which then starts to deteriorate and decline. Diversification in new ventures should be sought as a supplement and not as a substitute for the primary core business.

8. ***Lack of planning*** In many companies, particularly those built by individual entrepreneurs, the concept of planning is generally lacking. This can often result in major setbacks as limited thought or planning go into the actions and their consequences.

9. ***Inflexible chief executives*** A chief executive who is unwilling to listen to fresh ideas from others is a signal of impending bad news. Even if the CEO recognizes the danger signals, his unwillingness to accept any proposal from his subordinates further blocks the path towards recovery.

10. ***Management succession problems*** When nearly all the top managers are in their mid-fifties there may be a serious vacuum at the second line of command. As these older managers retire or leave because of perception of decreasing opportunities there is bound to be serious management crisis.

11. ***Unquestioning board of directors*** Directors who have family, social or business ties with the chief executive or have served every long on the board, may no longer be objective in their judgment. Thus these directors serve limited purpose in terms of questioning or cautioning the CEO about his actions.

12. ***A Management team unwilling to learn from its competitors*** Companies in decline often adopt a closed attitude and are not willing to learn anything from their competitors. Companies, which have survived tough competitive times continuously, analyze their competitors' moves.

13. ***Legal requirements for turnaround*** Turnaround is applicable to sick industrial units. An organization is sick when the accumulated losses at the end of a financial year exceed 50% of the peak net worth attained during the preceding five years. In order to an Indian company to quality for turnaround, it has to be first declared as a sick company. This declaration is required under the Sick industrial Companies (Special Provisions) Act (SICA), 1985 which provides for the Board for industrial and Financial Reconstruction (BIFR) to act as the 'corporate doctor' whenever companies fall sick. Though this act was initially envisaged to be applicable to private sector units only, as a part of restructuring of public sector enterprises, the SICA was amended to bring Central and State public sector units under its purview.

Turn Around Process Models

Hoffer has identified choice of strategies that include changes in management, organizational process, improved financial controls, growth via acquisition and new financial strategies in addition to the strategic and operating turnaround suggested by him. Figure12-1 below presents the causes of decline and the appropriate strategies required.

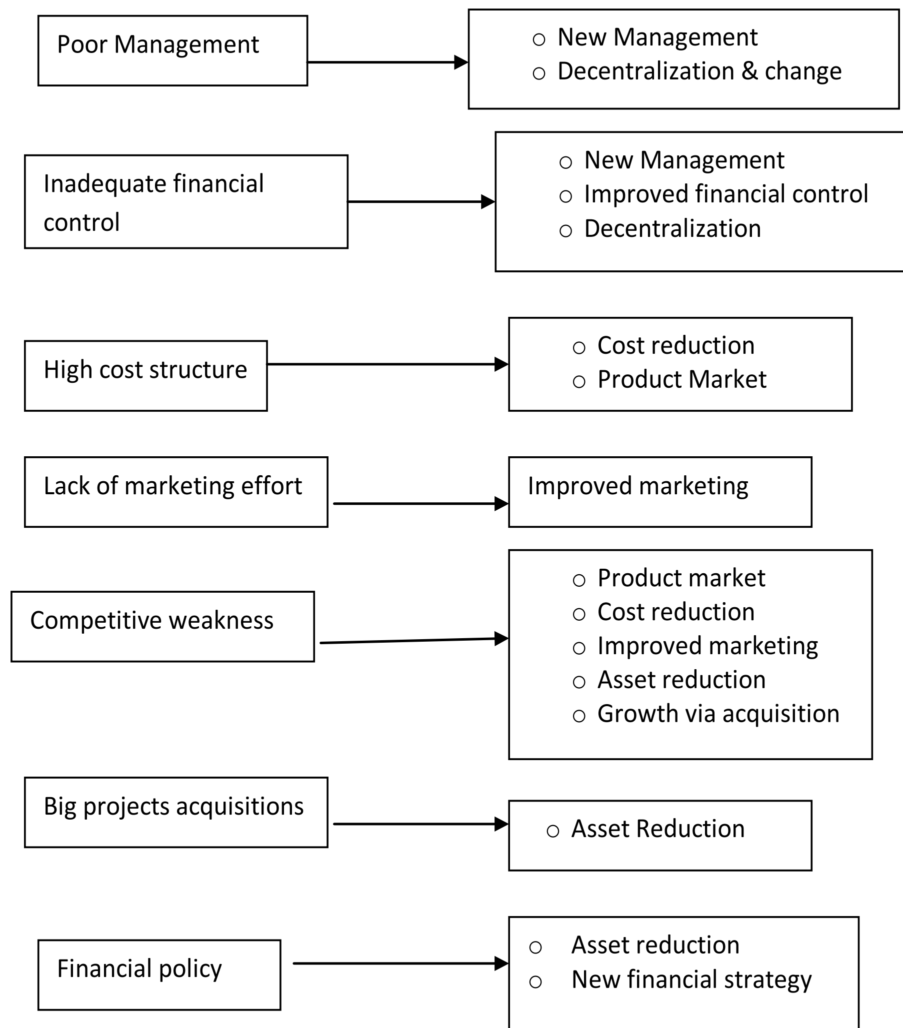

Figure12-1 Causes of decline and appropriate strategies

Grinyer and spender have suggested a process of turnaround shown in Figure 12-2. As soon as the parameters of corporate performance are indicative of unsatisfactory corporate performance, it becomes necessary to immediately tighten the controls within the organization. Effective controls have a positive impact on cost-reduction, that is, profit improvement and also on the net cash-flows of the firm. But this tightening of the financial and administrative control do not guarantee a stable turnaround process. In fact-controls coupled with poor quality image of the product may hasten the process of corporate failure. So while the controls are being affected, it is necessary that the strategic posture of the company may also be overhauled. This involves major changes in the product-mix, customer-mix and the patterns of resources deployment in the company. These two stages of change further need to be complemented by changes in top management and may organizational processes. If these changes produce early results which are satisfactory,

then for long-term effects it is necessary to reinforce these changes.

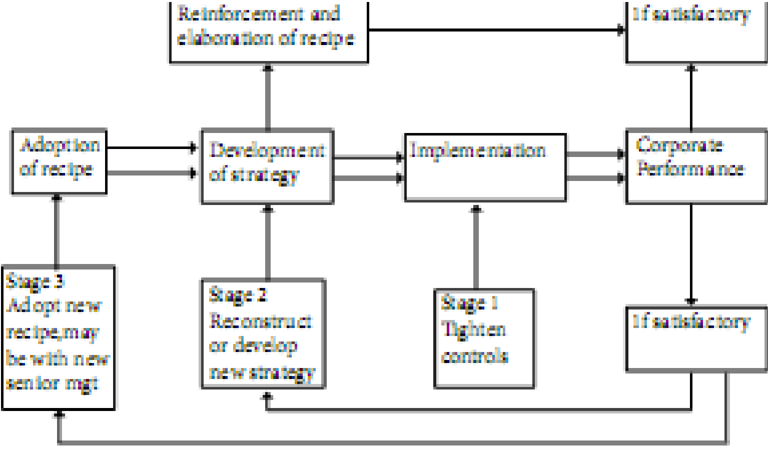

Figure 12-2 A Model of Turnaround Process

Source : O.H. Grinyer and I.C Spender , "Recipes, Crises and Adaptation in Mature Business", International Studies of Management and Organization. Vol. IX No.3

Turnaround process can be summarized as a five-step change process as shown in Figure 12-3

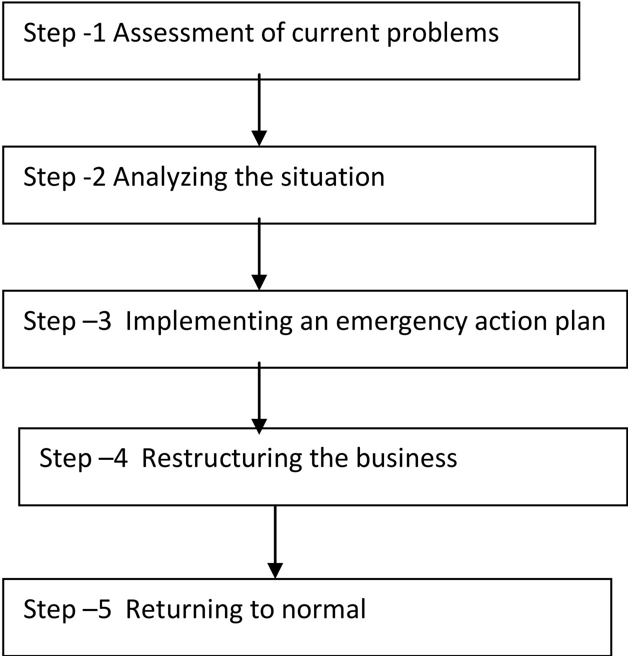

Figure 12-3: Turnaround as change process model

Turnaround Management

The focus of turn around is on reduction in assets and costs and increases in revenues and profits. This is similar to a weight reduction direct where two basic issues are :contraction and consolidation.

Contraction – "Stop the bleeding" attempt. Cutting back size and costs. It involves harsh decisions like the following.

- **Rid of** unprofitable products, pursuing workforce, trimming distribution outlets and seeking methods to make the organization more efficient
- **Divestment,** which involves selling the business and setting up a new corporation. This strategy improves the financial performance of a company and is opted when fit well to reach the organization's objectives.
- **Liquidation** is termination of assets and selling off. This is less preferred since it involves losses to stockholders and employees. But in a multi- business firm the impact of liquidation of one business may not be much.

Consolidation – A programme to stabilize a leaner corporation. Reducing overheads to make the firm cost effective

Another way of carrying turnaround may be as follows.

Stage One – Cost Cutting

A cost cutting program should be preceded by careful thought and analysis. The possibilities are that some departments or projects may need additional funding, while others need modest cuts, and still others need drastic cuts or need to be eliminated altogether. If you consider cost cutting as part of your strategy implantation in a case, be sure to specify exactly how it would be implemented across the organization. Support why the cost cutting should take the form you propose.

Stage Two-Re-engineering

Reengineering involves casting aside old assumptions about how an organization's business processes should be done and starting form

scratch to design more efficient processes. This may cut costs. This is easiest to see in a manufacturing process, where each step of assembly is scrutinized for improvement or elimination. Be sure to recommend wise use of reengineering. It is better to abandon processes that are not efficient.

Stage Three -Downsizing

Downsizing means laying-off people. It is a good way to cut costs quickly. But unless downsizing is tied to a rational strategy, problems can result. Cutting staff without changing the amount and type of work may result in costs cuts, but product quality and customer service may suffer, if they do, the organization's performance measures will suffer. The downsizing plan you recommend should fit logically with the strategy proposed.

Measures

The ten elements of turnaround strategy as identified by Pradip N. Khandwalla are as follows.

1. Changes in the top management
2. Initial credibility-building actions
3. Neutralizing external pressures
4. Initial control
5. Identifying quick payoff activities
6. Quick cost reductions
7. Revenue generation
8. Asset liquidation for generating cash
9. Mobilization of the organizations
10. Better internal coordination

These ten elements are identified based on the case studies of turnaround of 10 companies in India.The following are the factors that are commonly employed in turnaround management.

Management Factor Managerial inefficiency is the root cause of the problems in a number of cases. Therefore, improvement of the management becomes a prerequisite. For carrying out the turnaround management, a new efficient chief executive officer is usually appointed. The new CEO should streamline things and in many cases will have to change the organizational culture. This was true of several successful cases of turnaround management such as E.I.D Parry and Travancore Cochin Chemicals (TCC).

Human Resource Factor In many of the companies, which are in very bad shape, the human resource is redundant, demoralized and surplus. The surplus manpower should be got rid of, morale should be restored and the quality of the manpower should be improved through training and recruitment of competent people for the key positions, if needed.

Production Facilities Modernization and other improvements of plant, equipments etc., are also often an important part of the turnaround management. Such measures helps to achieve uninterrupted production flow and better capacity utilization, quality improvement, and reduction in wastage, increase in productivity and cost reduction. Proper management of the plant and equipments like preventive maintenance etc., have also been found to be absent in several sick units.

Finance Management Arranging additional finance, financial discipline, financial restructuring (described under Business Reorganization) etc., are usually an inevitable part of the turnaround management.

Product Mix Modification A number of turnaround management cases involve modification of the product mix. Unprofitable products may have to be dropped and new products may have to be introduced. Sometimes current products require quality improvement or some other modification. In some cases new models may have to be introduced.

Marketing Strategy Absence of a proper marketing strategy is a major reason for the problems of several companies. An appropriate marketing strategy could help improve such cases. Even product mix modification may form a part of such strategy. Marketing strategy may also involve market modification like entering new markets or market segments, withdrawing from certain markets/segments, developing new customers etc.

Miscellaneous Turnaround management may also involve several measures like liquidation of assets which are not in use, closing down of some divisions or lines of business, restraints on emoluments of employees, better management of procurement of raw materials etc.

Corporate Restructuring

Corporate restructuring may involve expansion or contraction of the portfolio or changes in the nature and volume of business. Change in the business conditions may necessitate restructuring of the business.

Restructuring strategies involve divesting some businesses and acquiring other so as to put a whole new face on the company's business line up. Performing radical surgery on the group of businesses a company is in becomes an appealing strategy alternative when a diversified company's financial performance is being squeezed or eroded by:

- Too many businesses in slow-growth, declining, low-margin, or otherwise unattractive industries.
- Too many competitively weak businesses.
- Ongoing declines in the market shares of one or more major business units that are falling prey to more market-savvy competitors.
- An excessive debt burden with interest costs that eat deeply into profitability.
- Ill-chosen acquisitions that haven't lived up to expectations.

Over the past decade corporate restructuring has become a popular strategy at many diversified companies, especially those that had diversified broadly into many different industries and lines of business. One struggling diversified company over a two-year period divested four business units, closed down the operations of four others, and added 25 new lines of business units, closed down the operations of four others and added 25 new lines of business to its portfolio (16 through acquisition and 9 through internal start-up).

During Jack Welch's first four years as CEO of General Electrical (GE), assets: these divestitures, coupled with several important acquisitions, provided GE with 14 major business divisions and led to Welch's challenges to the managers of GE's divisions to become number

one or number two in their industry. Ten years after Welch became CEO, GE was a different company, having divested operations worth $9 billion, made new acquisitions totaling $ 24 billion, and cut its workforce by 100,00 people. Then, during the 1990-2001 period, GE continued to reshuffle its business lineup, acquiring over 600 new companies including 108 in 1998 and 64 during a 90-day period in 1999. Most of the new acquisitions were in Europe, Asia, and Latin America and were aimed at transforming GE into truly global enterprise.

Forms Of Corporate Restructuring

The important forms of restructuring are:

- Mergers & Acquisitions
- Tender Offers
- Joint Ventures
- Divestitures
- Spin-Offs
- Corporate Control
- Changes in Ownership Structure
- Exchange Offers
- Share Repurchases
- Leveraged Buy-outs

Mergers and Acquisitions

An organization can expand through mergers and acquisitions. In a merger a company joins with the other company to form a new organization Acquisitions occur between firms in the same basic industry. For example Nestle acquired Richardson Vicks (both in Consumer Products). The acquiring firm not only obtains new product and markets but also confronts legal problems, structural deficiencies and diverse values.

Tender offers

Alternatively a public Tender Offer may be made to the shareholders for purchase of shares. These are easy only when the shareholding by the management and directors is comparatively very

low. In many Indian companies such shareholding is comparatively very low and, they are easily vulnerable to hostile takeovers.

Joint ventures

Joint ventures occur when an independent firm is created by at least two other firms. In an era of globalization, joint ventures have proved to be an invaluable strategy for companies looking for expansion opportunities globally.

Divestitures

Divestiture strategy involves the sale or liquidation of a portion of business, a major division profit centre of SBU. Divestment is usually a part of restructuring plan and is adopted when an unsuccessful turnaround has been attempted.

Spins offs

Spin - off refers to creation of new legal entity by the parent company. The existing shareholder of the parent company will be allocated shares in the new entity on a prorata basis. Unlike in a divestiture, the parent company does not receive any payment in case of a spin-off.

Spin-offs are resorted mostly for the purpose of better focus on different businesses. The new entity can develop its own strategies for the development of its business. The original parent, on the other hand, can now concentrate more on its core businesses. There are two variations of Spin-off: Split-off and split-up.

In the case of a Split-off, a portion of existing shareholders receives stocks in a subsidiary in exchange for parent company stock.

In the case of a Split-up, the entire firm is broken up in a series of spin-offs, so that the parent ceases to exist.

Corporate Control

There are several means of consolidating and enhancing corporate control. “Premium buy-backs represent the repurchase of a substantial stockholder’s ownership interest at a premium above the market price (called greenmail). Often in connection with such buy-back, a standstill

agreement is written. This represents a voluntary contract in which the stockholder agrees not to make further attempts to take over the company in the future. When a standstill agreement is made without a buy-back, the substantial stockholder is simply agrees not to increase his or her ownership which presumably would put him or her in an effective control position.

Anti-takeover amendments seek to make an acquisition of the company more difficult or expensive. These include (1) supermajority voting provisions requiring a high percentage (for example, 80 percent) of stockholders to approve a merger, (2) staggered terms for directors which can delay change of control for a number of years, and (3) golden parachutes which award large termination payment to existing management if control of the firm is changed and management is terminated.

The proxy contest is a dubious way by which the management of a company seeks to undermine the control position of the 'incumbents' or existing board of directors. This is sought to be achieved by an outside group, referred to as dissidents or insurgents obtaining representation on the board of defectors of the company.

Changes in Ownership Structure

The ownership structure of a firm may be changed due to various reasons. As a firm grows the ownership structure may undergo change. For example, a sole proprietorship may be converted into a partnership, when a partnership firm grows and when more ownership capital needs to be brought in a private limited company may be formed.

Exchange Offers

Exchange offer may involve exchange of debt or preferred stock for common stock, or conversely, of common stock for more senior claims. Several cases of turnaround involve exchange of debt for equity. For example, the government loan to a public or joint sector unit may be converted into equity. Such a measure helps to reduce the interest burden and reduces cash outflow by loan repayment also.

Share Repurchase

Buy-back of shares by a company help tilt the management control. If the company buys back shares from those who hold substantial

shares it could tilt the control in favour of the promoters, although the percentage of shares they hold does not increase. Buy back of shares can also guard against take-overs to some extent. It can also help stabilize the share prices. A major objection to the buy back of shares is that it provides scope for manipulation of share prices by the management.

Buy-Outs

Management buy-out may involve the purchase of a division of a company or even a whole company by a new entity formed specifically for this purpose. When such a purchase is financed by large debt (i.e., highly leveraged) it is referred to as Leveraged buy-out(LBO). LBOs are very risky because of the high interest burden and loan repayment obligation. A default in repayment would aggravate the interest burden and cash flow problem. LBOs have landed many companies is serious crisis.

Types of Restructuring

1. Portfolio restructuring
2. Organizational restructuring
3. Functional restructuring
4. Financial restructuring

Portfolio Restructuring

Portfolio restructuring refers to change in the portfolio of businesses of the company. This has become widespread since the liberalization ushered in 1991. The increase in competition has provoked many companies to divest businesses in which they are not competitive and to concentrate on their core businesses in which they tend to grow by setting up new capacity and/or by acquisition. The dismantling of the entry barriers (de-licensing, de-reservation, liberalization of policy towards foreign technology and capital participation, etc.) has opened up enormous new opportunities for expanding the business.

Organizational Restructuring

Decentralization, de-layering or flattering and regrouping of activities are important organizational restructuring measures.
Changes in corporate strategy, such as portfolio strategy, sometimes call for organizational restructuring. Often, structure follows strategy.

Increase or decrease in activity levels, expansion or contraction of portfolio or functions etc. may cause modification of organizational structure.

Functional Restructuring

The AMA survey reveals that restructuring of corporate functions (marketing operations, personnel and finance) has been very significant both in the public and private sectors.

1. Marketing Function: The survey results show that the revamping of the marketing function meant the creating of a product management team, building up sales force, restructuring distribution system, and creating marketing research cell.
2. Financial Function: As far as the modifying of the financial function was concerned the emphasis was on improving the financial reporting system.
3. Operations . Restructuring of operations has been very significant. Re-engineering has become very popular. Technological up gradation has been an important concern. The acceptance of total quality management and the requirements of ISO 9000 certification etc. have had significant influence on operational restructuring.
4. Personnel Function. Personnel function was found to receive high priority in restructuring. The emphasis in both public and private sectors was on training and succession planning. The private sector also gave the creation of appropriate rewards and punishments for performance high priority. This was, however, not so in the case of the public sector.

Process and Barriers of Restructuring

According to the American Management Association (AMA) survey, the common process adopted by a majority of the responding units was decentralization of decision making. Retraining and redeployment of staff was the second most important process of corporate restructuring in the private sector.

Flattering of organizational hierarchies was found to be the next important restructuring process adopted by companies. This was of

greater importance in the private than in the public sector. The public sector has, because of rigidities due to its ownership, far less flexibility in this action. Along with these were measures to improve quality, creating strategic business units, and creating representation in more market segments. These processes are giving importance. Considered to be of even less importance in the public sector. Other factors revealed by the survey include going for joint ventures, overseas expansion, acquisition of synergistic businesses etc.

The major barrier to restructuring has been the cost of doing it. In private sector lack of accountability for key performance indicators is also one reason. Some top managements lacked entrepreneurial skills. Salary structures based on seniority, which need to be changed to performance, related structures are the next immediate barriers. Contrary to general impressions problems of labour are not serious barriers to restructuring

Summary

Turnaround strategy is adopted when an organization is performing poorly but has not yet reached a critical stage. It involves getting rid of unprofitable products, pruning the workforce, training distribution outlets and seeking all the measures to make organization efficient. An organization may concentrate on focus only after successful turnaround. Industrial sickness is growing in India due to increasing competition, obsolete technology, poor product quality, lack of financial and administrative disciple and poor mgt. Turnaround is the most appropriate way of reviving sick units. Corporate restructuring strategies involve divesting some businesses and acquiring other so as to put a whole new face on the company's business line up. Four types of restructuring are found: portfolio restructuring, organizational restructuring, functional restructuring and financial restructuring. The forms of restructuring are :Mergers & Acquisitions, Tender Offers, Joint Ventures, Divestitures, Spin-Offs, Corporate Control, Changes in Ownership Structure, Exchange Offers, Share Repurchases and Leveraged Buy-outs.

Self -Assessment Questions

1. Define turnaround strategy and outline its significance.
2. What are the various indicators of industrial sickness?

3. What could be the major issues in turn around management?
4. Explain the process of turnaround management.
5. Explain any one model of turnaround.
6. What is corporate restructuring?
7. Discuss the different forms of restructuring
8. Explain the process and barriers to restructuring
9. Examine the different types of restructuring with examples
10. Explain: (i) leveraged by outs (ii) Spin offs (iii) Divestitutes

Activities

1. Visit the state Finance Corporation. Discuss with the executives and find out how the organization could turnaround sick units.
2. Identify a sick unit and interview its manages about the reasons for its sickness
3. Visit the website of Board for Industrial Financial Reconstruction (BIFR) and examine their successful cases of turnaround.

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Lesson 13 - Mergers and Acquisitions

Lesson Outline

- Introduction
- Corporate growth strategies
- Concept and types of mergers
- Mergers and acquisitions in India
- International scenario
- Merger motives
- Screening and valuation process
- Summary
- Self Assessment questions
- Activities
- References

Learning Objectives

Improve valuation theory(last sub head)

After reading this lesson you should be able to

- Understand corporate growth through mergers and acquisitions
- Describe the types of mergers
- Discuss Indian and international examples of mergers and acquisitions
- Explain why mergers takes place
- Describe the screening and valuation processes of mergers and acquisitions

Introduction

Mergers and acquisitions as external growth strategies have been the regular feature of corporate enterprises in all developed countries. The largest number of mergers took place at the turn of the century, which transformed many industries. The Indian business environment

has altered radically since 1991 with the changes in economic policies. The Indian corporate though benefited due to decontrol and deregulation has been threatened by hostile takeovers. Pharmaceuticals and ad agencies are the primary targets of merger and acquisitions in India. Family businesses are finding it hard to survive with low profiles and credit availability.

Corporate Growth Strategies

Growth can be achieved by different means. One approach is form within and another is from outside –that is combinations. Different forms of combinations are:

1. ***Amalgamation/Merger*** Merger take place when there is a combination of two or more organizations. Merger does create a new corporation.

2. ***Acquisition/takeovers*** One Company acquires another company's controlling interest. The acquired company operates as a separate division or subsidiary by offering cash or securities in exchange for majority of shares of another company.

3. ***Sales of Assets*** A company can sell its assets to another and cease to exist.

4. ***Holding company acquisition*** This is a quasi merger. Either the total or majority of a firm's stock will be acquired. The purpose is only management and control of other.

Concept and Types of Mergers

A merger is a combination (other terms used: amalgamation, consolidation, or integration) of two or more organizations in which one acquires the assets and liabilities of the other in exchange for shares or cash, or both the organizations are dissolved, and the assets and liabilities are combined and new stock is issued. In mergers, all the combining firms relinquish their independence and cooperate, resulting in common cooperation.

For the organization, which acquires another, it is an acquisition. For the organization, which is acquired, it is a merger. If both organizations dissolve their identity to create a new organization, it is consolidation More time is taken for merger than acquisition. Mergers are three types: horizontal mergers, vertical mergers and concentric mergers.

1. Horizontal mergers take place when there is a combination of two or more organizations in the same business, or of organizations engaged in certain aspects of the production or marketing process.

For instance a company making footwear combines with another retailer in the same business.

2. Vertical mergers take place when there is a combination of two or more organizations not necessarily in the same business, which complement either in terms of supply of materials (inputs) or marketing of goods and services (outputs).

For instance a footwear company combines with a leather tannery or with a chain of she retail stores.

3. Concentric mergers take place when there is a combination of two or more organizations related to each other either in terms of customer functions, customer groups, or the alternative technologies used.

A footwear company combining with a hosiery firm making socks or another specialty footwear company, or with a leather goods company making purses, handbags, and so on.

4. Conglomerate mergers take place when there is a combination of two more organizations unrelated to each other, either in terms of customer functions, customer groups, or alternative technologies used. A foot wear company combining with a pharmaceuticals firm.

Mergers carried out in reverse are known as demergers or spin-offs. Demerger involves spinning off an unrelated business/division in a diversified company into a stand-alone company along with a free distribution of its shares to the existing shareholders of the original company.

There are a few cases of demergers in India namely the demerger of Hoechst Schering Agrevo Ltd. From Hoeschst India Ltd, Ciba Specialty from Hindustan Ciba Geigy Ltd., from Sandoz renamed as Chariant India, and Aptech from Apple Industries Ltd.

Mergers and Acquisitions in India

Mergers and acquisitions in India are as given below.

The Murugappa group and RPG group have benefited of merger and acquisitions by becoming conglomerates of diverse businesses into one group. There are several examples of mergers in the Indian corporate world, such as, Polyolefin Industries with NOCIL, TVS Whirlpool Ltd with Whirlphool of India ltd., Sandoz (India) Ltd with Hindustan Ciba Geigy Ltd., and Shiva Soaps and Detergents Ltd with Nirma Ltd. Other examples are:

- Spartek acquired Neycer India a sick company under BIFR in 1985. It acquired Styles India in 1998.
- Godrej soaps acquired Transelektra Domestic Products Ltd (TDPL) and formed Godrej Hicone. TDPL has good brand equity and wide distribution network. It wanted a partner with strong finance, managment and systems competencies
- Tata Telecom merged with Tata Keltron in 1995. Tata Keltron was named Tatafone and made it profitable which was earlier with BIFR
- Sterlite communications & Sterlite industries merged to cross Rs, 1,000 crore turnover mark in June 1996.

Murugappa group: Growth of Acquisition 1980-95

Company	**Products**
EID Parry	Fertilizers, sugar, ceramics confectionery
Coromandal Fertilizers	Fertilizers
Bharat Pulverizing Mills	Pesticides
Pugalur syars	sugar
Falcon Gulf ceramics	Sanitayware
Parma Agro	Plantation
Wedt (India)	Cutting tools
Press Metal corp.	Metal sections
Satavahara Chains	chains
Sterling Abrasives	Abrasives
Eastern Abrasives	Abrasives
Cut fast Abrasives	Abrasives

RPG has grown from Rs 80 crore in 1979-80 to Rs 5,600 crore in 1996. RPG Groups acquisitions include cables, tyres, transmission and electronics. The list includes

- Asian cables
- Ceat Ltd
- Calcutta Electric Supply Corporation Ltd
- Carbon & Chemicals industries

UB group acquired

- Tamil channel GEC (Vijay TV)
- Berger Jenson & Nicholson UK with manufacturing base in 21 countries
- Sold away petrochemicals to SPIC
- Acquired Best & Cromption

The other groups include Shaw Wallace, Rajarathinam group, Manu Chabbria group, JVG, etc MA Chidambaram group, BPL, Sri ram group, Videocan, Maxworth Orchards,

HLL growth map is as given below

1992—Acquires Kothari foods

1993—Dollops from Cadburys

Kissan from UB groups &

Brooke Bond & Lipton (BBLIL)

1993—Merges with TOMCO

1994—Alliance with Quality ice cream

1995—Acquired Milk food

1995—Alliance with Lakme to form Lakme lever Ltd

- Ponds

International Scenario

We will now survey different nations to have a feel of mergers and acquisitions taking place globally.

USA

The US government promotes free competition. However M & A result in monopolistic situations where barriers are created for entry of small firms. The Sherman Anti Trust Act of 1890 restricts building up

monopoly beyond a market share of 75%. US law prohibits horizontal mergers. In the US 75% of the M&As are failure while in UK 8 out of 9 is failures. In US M&As resulted in legal battles. Huge legal costs and waste of time are common.

Japan

Adopted from US and revised in 1977, the Japanese policy allows break up of powers to companies with a large market share. However, the extent of litigation is low.

Europe

Market domination is restricted in Rome at 40%, in UK at 25% and in West Germany at 33%. The Federal cartel office may divorce a merger after one year in West Germany. Tax levies on premium values above books values are there. In UK the Monopolies & Mergers Commission tends to delay and restrict creation of monopolies. The Restrictive Trade Practices Act of 1956 & Company Fair Trading Act of 1975 and Consolidating Act of 1975 control the power of concentrated private companies. In 1978, it was reviewed that concentration is required for international trade in UK

In France, Control of merger started in 1977. Mergers (horizontal) causing market share of 40% and mergers with companies of a market share of over 25% are allowed when advantages out weigh disadvantages. Take over bids are to be submitted to bankers, chamber syndicates and stock brokers appointed by the ministry of economy. The proposals should be published in newspapers and must undergo extended legal formalities. The share holders should be informed and the stock movements regulated.

India

The companies Act brought the system misused by British to an end in 1956. The Government also controls the number and remuneration of Board of Directors. The companies are restricted in loans given to other companies to avoid interlocking of funds.

The MRTP Act of 1970 and FERA of 1973 impose control in the conduct of companies. MRTP act restricts concentration of economic power and encourages free trade. The asset limit for MRTP firms is raised to Rs.1000 million.

FERA gives guidelines for foreign business in India. Permissible foreign shareholding is 74% and in other manufacturing items' like construction, consultancy & non tea plantation the limit is 40%.

Merger Motives

Sellers opt for mergers and acquisitions to reduce taxes, to diversify, to restrict working capital financing, for technological synergies, when worthy successor is not there and due to the inability to cope with competition. Buyers go for mergers to acquire new product or capacities or permanent, or more synergy, to achieve economies of scale, when outside capital is available; there is more control of patents and tax advantages.

Organizations opt for merges with the following motives.

- Improving economies of scale
- Gaining managerial expertise
- Market supremacy
- Acquiring a new product or brand name
- Diversifying the Portfolio
- Reducing risk and borrowing costs
- Taxation or investment incentives

Screening and Valuation Process

A Taker over company scans the environment to find out the right candidate for take over. The process involves following steps.

- Identification of industries
- Selection of sectors
- Choosing companies (which are 5 to 10% of size bidding companies)
- Finding cost of acquisition and returns: compare candidates with respect to ROIs.
- Ranking of candidates
- Identify good candidate(s)

After going through the screening process the fooling considerations merit attention.

- Funds availability
- Likely positive synergies
- Negative synergies an weaknesses
- Appropriate timing
- Availability of required management style.

Next step is valuation. Valuation determines the worth or value of the M & A. Mergers & Acquisitions involve share of stocks of different companies and exchange. The valuation procedures are similar to the capital budgeting procedures.

(1) Valuation by P/E Ratio.

$$= \frac{\text{Market price per share}}{\text{Net earnings after tax per share}}$$

If market price of a share is Rs 40/- and EPS is Rs 2/- the PE ratio = 40/2=20.

This means this company would have to sustain profit at this level for 20 years to pay back its current price. The differences in P/E ratio for different companies are attributed to differences in the following.

- Growth rate of a company
- Risk associated with investment
- Competition & environment

Essential commodities have shorter business cycles and more uniform earning compared to sectors like heavy Engineering which are linked with growth of the economy.

(2) Earnings Per Share (EPS)

Compare the EPS of acquirer and acquired and two together. Refer the balance sheet and profit and loss account for sources and uses of funds.

(3) Divest loss making operations

The acquirers should divest loss making subsidiaries and reduce cash drain to invest in attractive ventures. Unwanted assets should be disposed off at book value.

(4) Use ratio analysis: Calculate key ratios

(a) Current ratio = Current Assets /Current liabilities

This should be checked with industry's average to know if it is on the higher side. If high, the individual assets and liabilities should be checked. If current assets are high excess money will be with debtors or stocks may be high. This should be checked with industry's average. Reduce current liability like bank over draft and working capital loans to save on interest charges.

(b) Level of stock (in months) = (Stocks/Cost of goods sold) x 12

If the firm's level of stock is 8 months and industry's average is 6 months then the stock level should be reduced. The funds should be deployed for better purposes.

(c) Average age of debtors (in days) = (Debtors / Sales) x 365

If the acquiring company's average age of debtors is low follow the same policy of the acquired one.

(d) Revise Balance sheet and profit & loss account-

The new EPS after merger should be better for the new company.

(5) Incorporate growth and expectation rates

Prepare proforma statements with expected growth rates.

(6) Market value of assets: Find the current market value of assets. It is a good measure of strength.

(7) Replacement value (RV) of assets

Replacement cost is better than historical cost particularly in an inflationary economy.

Replacement value of an asset = 1- Age of Assets/ Total Economic life of Asset) x Current value of asset.

Self -Assessment Questions

1. Explain the concept of mergers and acquisitions.
2. Describe the process of merger as a method of corporate growth
3. Examine the different types of mergers and acquisitions
4. Describe the screening process of mergers and acquisitions
5. Evaluate and assess the suitability of a merger proposal.
6. Why do sellers opt for mergers
7. Examine why buyers opt for mergers
8. Explain the international scenario of mergers and acquisitions

Activities

1. Visit the website of Hindustan Lever Ltd and list the companies that are merged with it. Also evaluate the reasons for the mergers.
2. Examine how NRIs like Lakhsmi Mittal have additional advantages to work out mergers and acquisitions in India than their Indian counterparts.

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Lesson 14 - Functional Strategies

Lesson Outline

- Introduction
- Functional strategies
- R & D strategy
- Operation strategy
- Logistics /supply chain strategy
- Information systems strategy
- Coordination of strategies
- Summary
- Self Assessment questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Examine the characteristics of functional strategies
- Understand functional strategies in R&D and operations
- Coordinate the strategies for maximum effectiveness

Introduction

Strategic management process involves determining appropriate courses of action for achieving objectives. In the process of formulation it is necessary to gear the organization in such a way that all the functional areas are synchronized viz, finance, marketing, human resources and operations. Off late logistics is also included as a key functional area. Further the functional strategies must cover all the three levels of management – top, middle and lower. It is in this context that we need to study functional strategies in detail.

Functional Strategies

Functional experts like R&D, operations, finance, marketing and human resources devise functional strategies. The characteristics of functional strategies are as follows.

- Short term
- They provide short-term operational details for achieving long-term objectives systematically.
- Limited scope

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

Derivative

Functional strategies are derived from business and corporate strategies. Functional strategies specify the grand plans in different functional areas in time horizons and help operationalize the strategies. They cascade down the hierarchy and percolate from corporate strategies to divisional strategies and further down to departmental strategies. Hindustan Lever Ltd's functional strategies at the above three levels can be depicted as follows in Figure 14-1.

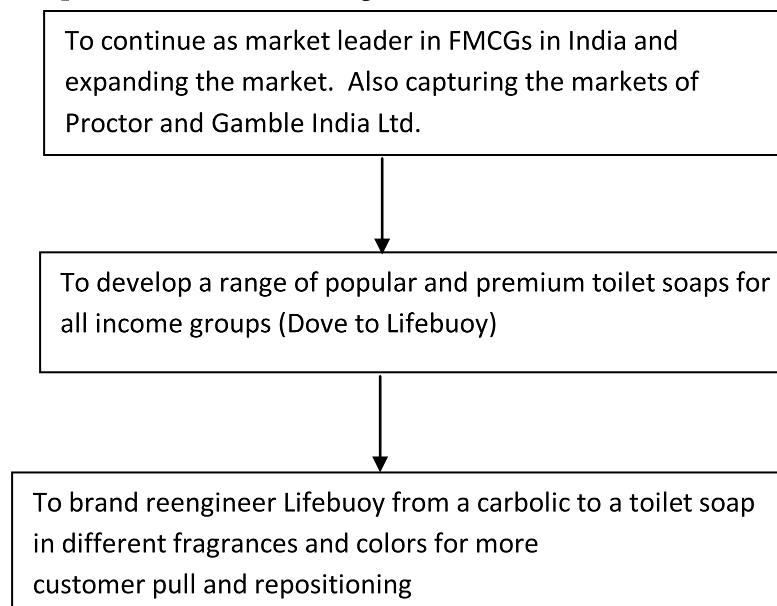

Figure 14-1 Derivative nature of functional strategy

R & D Strategy

New technologies may make the business obsolete like the way Photostat technology rooted out the carbon paper technology. Software and pharmaceutical companies need good R & D strategies for survival itself.

Motorola recently announced that it had figured out how to combine silicon and gallium arsenide in one semiconductor chip. The company said this discovery will greatly reduce manufacturing process costs and result in smaller, faster products. The discovery is expected to yield products by the end of 2003 and may lead to cell phones as small as shirt buttons. Intel and Microsoft are continuing to increase their expenditures on research and development. Intel spent just over $4 billion on R&D in 2001, nearly 15 percent of sales, while Microsoft spent $4.8 billion, up 37 percent from two years earlier. Both companies expect to increase R&D spending an additional $500 million in 2002. Intel is developing more powerful and smaller chips to power computers, while Microsoft is improving its Windows XP operating system. In India we can take the example of companies like Dr. Reddy's Laboratories who are spending huge amounts for developing new drugs and vaccine.

But the disadvantage of R & D strategy is the high costs and time involved, also the risk associated with. According to a finding an average of 30 to 35 percent of new products fail after being put on the market, so innovation strategies –those that focus heavily on developing new products-can be very risky. For this reason, many organizations use imitation strategies, that is, they rapidly copy new competitive products that are doing well.

A number of Japanese electronics companies were quite successful in copying American technology and, by avoiding many R&D costs, improved their competitive positions significantly.

Operations Strategy

This strategy adds value to the raw materials to create a product or service. This value addition should be cost effective, fast and without quality rejects or reworks. The emphasis should be on cost-reduction while enhancing quality. Areas like safety, breakdown, downtime,

inventory control scheduling etc. should be adequately covered with policies and strategies at functional level.

Table 14-1: Categories of Strategy Decisions in Manufacturing Operations

1. **Capacity** – amount, timing, type
2. **Facilities** – size, location, specialization
3. **Technology** – equipment, automation, linkages
4. **Vertical integration** – direction, extent, balance
5. **Work force** – skill level, wage polices, employment security
6. **Quality** – defect prevention, monitoring, intervention
7. **Production planning materials control** – sourcing polices, centralization, decision rules
8. **Organization** – structure, control/reward systems, role of staff groups.

(a) Inventories

India is known for high cost of inventories. Companies spend huge amounts on storage and warehousing in this country unlike countries like Japan which follow 'Just in time (JIT) in production and operations.

Raw materials arrive eight hours before they are put in process for making finished goods in Japan. This is true with M/S Toshiba of Japan, where they can get the required plates from just across the waters from M/S Nippon steels unlike many companies in India who have to order thick plates at least eight to ten months in advance.

(b) Training to workers

Many Japanese manufacturers have also provided extensive training and cross training of their workers so that they will have multi- skilled workers. This versatile work force, coupled with plant arrangements and equipment that can easily changed over from one product to another, provides greater flexibility without a significant increase in cost.

(c) Low cost materials by strategic location

Regarding procurement of materials, strategies on right qualities of material, at the right qualities of material, at the right time and price, the number of sources, their reliability and price patterns analysis and decision, vendor relationships, forward buying etc. must be chalked down to enable managers to work according to them.

Industries like Bharat Heavy Plates and Vessels which are strategically located closer to steel plant in Visakhapatnam in Andhra Pradesh have the advantage to get raw materials like steel and coke with less carrying cost and storage cost. Industries located closer to ports like Chennai, Mumbai and Calcutta have also strategic advantage of location not only for getting raw material but also for shipping finished products.

(d) Product Design – Technology and Marketing Concerns

The product, or output, desired from the operations system will certainly affect the type of inputs needed and the capabilities that must be available to transform the inputs into the desired goods or services. As the product is designed, a cost-benefit evaluation should be performed, taking into account the kind and amount of materials, labour and processing equipment that each alternative design will require.

The company must also recognize that the potential consumer will also perform some sort of cost-benefit evaluation before deciding whether to purchase the product. Some processes and materials are more expensive and should be used only if the functions of the product make them necessary or the aesthetic appeal of the results justifies the expense.

Myriad alternative designs for a product are usually possible, and alternative production methods may be possible even after the product is designed. Production engineers often serve as advisers to designers, helping them develop product designs that are reasonably economical to produce.

Here is an example of retail firm design of products and operations for consumer acceptance The Loft, the first of its kind multi brand footwear store in India, is based in Mumbai. The Loft is a one-stop shop for anyone who is looking for a good pair of footwear. It has found favour with many first time, visitors, thanks to its unique services, intensely

trained sales men who understand shoes and customer preferences intimately and all that it takes to give the right footwear to the discerning customer.

Spread over 18,000 sq.ft of space, The Loft stocks almost 100 plus brands, has facilities like pedicure, cobbler, and jogging track. It also boasts of the biggest socks shop which houses a staggering 15,000 pairs of stocks from over ten brands and all price points. The Loft also stocks numerous footwear accessories like, shoe polishes, shoe trees, brushes, shoe cleaners, shoe shiners, insoles, laces, shoe norms, shoe bags etc. In short, The Loft is the destination if one is looking for anything in footwear or foot care. (Source: www.thelofitnindia.cpm)

Information Systems Strategy

Corporations are increasingly adopting information system strategies in that they are turning to information systems technology to provide business units with competitive advantage.

Multinational corporations are finding that the use of a sophisticated intranet for the use of its employees allows them to practice follow – the –sun management, in which project team members living in one country can pass their work to team members in another country in which the work day is just beginning. Thus, night shifts are no longer needed.

The development of instant translation software is also enabling workers to have online communication with coworkers in other countries who use a different language. Lotus Translation Services for Same time is a Java –based application that can deliver translated text during a chart session or an instant in 17 languages. Software, e-lingo (www.e-lingo.com) offers a multilingual search function and Web surfing as well as text and e-mail translation.

The use of information systems for improving competitive advantage has become common. The case of Wal-Mart described in Exhibit 14-1 exemplify this argument.

Exhibit 14-1 Wal-Mart Information Strategy

In 1989, Wal-Mart started building a huge database of customer information in its data warehouse systems located at its headquarters at Bentonville, Arkansas. The company collected sales and customer

related information for each store and fed that information into the warehouse systems.

In the early 1990s, Wal-Mart continued to employ new technologies to facilitate better analysis of customer data as they became available. Wal-mart's IT experts used 3-D visualization tools to make accurate estimates of products most likely to be bought by customers on the basis of parameters such as ethnicity, geographic location, weather patterns, local sports affiliations, and around 10,000 other varied parameters. Wal-Mart made around 90% of its stock replenishments every month, based on the analysis of customer data generated through the data warehouse.

To make shopping at Wal-Mart a pleasant experience, Wal-Mart installed customer information kiosks in its stores in 1996. The kiosks helped customers find out the price of any product and get a brief description of it. In 1996, Wal-Mart launched its website – www.walmart.com - to provide information to its customers on all the products it stocked and to enable online sales.

IT played an important role in improving the efficiency of operations at Wal-Mart. The benefits which accrued were passed on to customers, as per Wal-Mart's policy. Wal-Mart's annual report 1999 said, "The first and the most important thing about Wal-Mart's information systems is precisely that the customer's needs come first. By using technology to reduce inventory, expenses and shrinkage, we can create lower prices for our customers and better returns for our shareholders".

At the dawn of the new millennium, Wal-Mart was one of the world's largest companies, with revenues of $165 bn in fiscal 2000. Wal-Mart's 'store of the community' program made effective use of bar code technology and advanced data mining techniques. The 'store of the community' program was a very successful initiative by Wal-Mart, which contributed to increased customer loyalty. By 2003, Wal-Mart was the world's largest company, with revenues in fiscal 2002 amounting.

Logistics /Supply Chain Strategy

Logistics/supply chain strategy deals with the flow of products into and out of the manufacturing process. Three trends are evident.

- Centralization,
- Outsourcing, and
- Use of the Internet.

To gain logistical synergies a cross business unit, corporations began centralizing logistics in the headquarters group. This centralized logistics group usually contains specialists with expertise in different transportation modes such as rail or trucking. They work to aggregate shipping volumes across the entire corporation to gain better contracts with shippers. Companies like Amoco Chemical, Georgia – Pacific, Marriott, and Union Carbide view the logistics function as an important way to differentiate themselves from the competition, to add value, and to reduce costs.

May companies have found that outsourcing of logistics reduces costs and improves delivery time. Many companies are using the Internet to simplify their logistical system. For example, Ace Hardware created an online system for its retailers and suppliers.

Coordination

The functional strategies can be effective only when they are aligned with corporate strategies and integrated with one another. One must understand that strategies must be coordinated to have a vertical fit which aligns the functional areas. Simultaneously, horizontal fit leads to alignment of activities. Table 14-2 shows the impact of strategy elements on operations and R&D management.

Table 14-2 Impact of Strategy Elements on Operation and R&D Management

S.No	Elements of Strategy	Operations management	R&D Management
1.	Compete as low – cost provider of goods or services	Requires longer production runs and fewer product changes Requires special – purpose equipment and facilities	Research on cheap input alternatives Low cost processing equipments
2.	Compete as high quality provider Requires more precise equipment, which is more expensive Requires highly skilled workers, necessitating higher wages and greater training efforts	Requires more quality –assurance effort and higher operating cost	Quality inputs High tech, high quality processes
3.	Strive for absolute growth	Requires accepting some projects or products with lower marginal value, which reduces ROI	New product alternatives
4.	Maintain reserve capacity for flexibility	Requires capital investment in idle capacity	-
5.	Consolidate processing (Centralize)	Locate near one major customer or supplier	Technology improvements

6.	Disperse processing of service (Decentralize)	Requires more complex coordination network: perhaps expensive data transmission and duplication of some personnel and equipment at each location. If each location produces one product in the line, then other products still must be transported to be available at all locations. If each location specializes in a type of component for all products, the company is vulnerable to strike, fire, flood, etc. If each location provides total product line, then economies of scale may not be realized	Product improvements and differentiation

Summary

Functional strategies give more clarity to corporate and business level strategies and operate at third level. They provide specific plans for achieving objectives with optimal contribution for organizational advancement. Operational strategies take into account production system, operations planning and control and R & D. R & D strategies aim at innovation and new product development. Logistics minimize transportation and delay costs. Information systems provide effective communication and knowledge sharing opportunities. One must understand that strategies must be coordinated to have a vertical fit which aligns the functional areas. Simultaneously horizontal fit leads to alignment of

activities. Operational implementation adopted by a firm achieves more effectiveness and perform value-creating opportunities.

Self -Assessment Questions

1. Outline the various functional strategies and examine their significance in the process of strategic management.
2. Review the major R & D strategies of firms with examples.
3. What are the concerns of operations plans and policies?
4. Examine the impact of corporate strategies on the operational management of a firm.
5. Why do you think production / operations managers often are not directly involved in strategy - formulation activities? Why can this be a major organization weakness?
6. How can you coordinate operations and R&S strategies?
7. What is the significance of information systems strategy?
8. How can logistics strategy help a firm achieve its goals?

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UNIT- IV

Functional Strategies

Lesson 15 - Finance Marketing, Human Resource, Management Information Systems and logistics

Lesson Outline

- Introduction
- Functional Strategies
- Marketing Strategies
  - Marketing Warfare
  - Promotion Strategies
- Finance Strategies
- Hr Strategies
- Information Systems Strategies
- Logistics
- Strategies To Avoid
- Selecting The Best Strategy

Learning Objectives

After reading this lesson you should be able to

- Synchronies the functional strategies for organizational effectiveness
- Understand and translate functional strategy at corporate level to action plans.
- Examine the synergies among functional strategies

Functional Strategies are devised by specialist in each functional area of business. They spell out the spell out the specific tasks that must be performed to implement business strategy. Companies may vary in

organizational responsibilities and also devise varieties of functional strategies.

Marketing specialists focus on determining the appropriate markets for business offerings and on developing effective marketing mixes. The marketing mix includes four strategic elements: price, product, promotion, and channels of distribution.

Financial specialists are responsible for forecasting and financial planning evaluating investment proposals, securing financing for various investments, and controlling financial resources. Financial specialists contribute to strategy formulation by assessing the potential profit impact of various strategic alternatives and evaluating the financial condition of the business.

Marketing Strategies—Competition Based

Marketers have to evolve strategies to fight competition, to gain and retain market shares. The right tool for analyzing market situation is SWOT analysis. Based on the SWOT analysis competitors can be classified as follows:

1. Based on the ability to engage and sustain warfare—strong and weak
2. Based on the percentage of market share—close and distant held by a competitor

These competitors can, in turn, be assigned following competitive positions.

- Market leader—the firm with largest market share and strong in designing and implementation plans.
- Market challenger—close and strong competitors to market leader, who aggressively or mildly challenge him
- Market follower—the distant and weak competitor who is content in following leaders and challenger.
- Market Nicher—the independent, non-fighter, who carves his niche for peaceful and profitable specialized operations.

Market shares of the competitive firms are:

40%	30%	20%	10%
Leader	challenger	Follower	Nicher

What are the moves of the competitors? Are they preemptive or predatory? Are they defensive or offensive? Companies in different competitive positions work different strategies. The possible moves of a leader, challenger, follower and nicher are:

- Grow strong—become invincible
- Defend—develop protection against attack
- Offend—weaken or destroy competitor
- Play safe—select less competitive areas and cultivate.

Leader

Expansion strategy

- Market penetration strategy
  - Increase use of the product
  - Find new uses for the product
- Market development strategy
  - Convert non-users to users
  - Find new markets in other places
- Product development strategies
  - Create new products/services
  - Modify existing products

Defending strategy

- Continuous innovation and quality platform

Position defense - Product—Line complete

Flanking defense - Varieties of Variants

Preemptive defense - Price reduction through sales promotion

Counter offensive defense - Match with ads and others at tacks

Mobile defense - Concentrate in successful markets

Contraction defense - Prune brands

Market Challenger

A market challenger may choose to attack

- The leader
- The followers
- The nichers.

By pass attack — Diversifying into unrelated products
Diversifying into new geographic markets
Leap frogging into new technologies

Frontal attack — Price and promotion aggressiveness

Flank attack — find gaps in product line and set up variety competition Encirclement attack - Wide range of products with heavy advertising and promotion

Guerilla attack — New product or promotions of short life cycle with marketing blitzkrieg

Market follower

The options are:

Following closely — imitate immediately

Following at a distance — slow imitation

Following selectively— imitation in select areas

The companies are generally small in size. Some companies in the unorganized sector may follow 'fakes' strategy.

Market—Nicher

- The niche is sufficient size in size and purchasing power to be profitable.
- The niche has growth potential
- The niche is of negligible interest to major competitors
- The firm has the required skills and resources to serve the niche effectively
- The firm can defend itself against and attacking major competitor through the customer good will it has built up.

Computer companies are among the newest converts to the "end user" type of niche marketing, but they call it vertical marketing. For years, computer fought to sell general hardware and software systems horizontally across many markets, and the price battles got rougher. Smaller companies started to specialize by vertical slices—law firms, medical practices, banks, etc,--studying the specific hardware and software needs of their target group and designing high-value added products that had a competitive advantage over more general products. Their sales forces were trained to understand and service the particular vertical market. Computer companies also worked with independent value-added resellers (VARS), who customized the computer hardware and software for individual clients or customer segments and earned a price premium in the process.

Designing a Promotion Strategy

There are many successful companies which proved professional with faster growth due to high power promotion. A good example is reliance group in India. It has built brand loyalty with a different mix of a media.

Reliance has a high budget promotion for all its textile brands. It has specific promotion strategies for suiting, dress materials and saris. "ONLY VIMAL" 'ONLY' concept in the promotion made Reliance a super success. Effective media selection and 80% budget for press and after 1978 more focus on TV ads made their promotion No.1. Miss Universe Contest' 'Oscar awards nite' etc were sponsored including the 'Reliance cup'

Choosing Pull or Push Strategy for sales promotion:

(a) ***Push strategy*** – A promotion strategy mainly aimed at channels of distribution is called a push strategy. Marketers promote their products heavily among distributors wholesalers and retailers. Retailer promotes to customers. This includes trade shows, personal selling and contests.

Producer Distributor Wholesaler Retailer Consumer

(b) ***Pull Strategy*** – Here promotion is directed towards ultimate consumers. Manufacture tries to stimulate demand and attracts consumers to buy his product.

Manufacturer Consumer

This includes advertising, publicity and sales promotion like discounts, free goods and contests.

Tools of Sales Promotion

The most commonly used sales promotion tools in India are

(i) Prize schemes

A prize scheme is designed for both the public and the dealers. Sales competition is arranged, prizes are announced or special offers are made.

(ii) Trade Fairs and Exhibitions

These exhibitions attract a lot of people especially from rural areas who find them as a very convenient place to make their purchases of consumer goods. Many state Governments announce relief or concession in sales Tax; for example, a passenger car can be purchased in Gwalior Mela without payment of any sales tax.

(iii) Free Samples

Free samples are generally used to introduce a new product and as a sales tool to attract the attention of prospects, not only much time is saved, but it also eliminates the need for inspection or testing of goods by the buyer.

(iv) Correspondence

Sending letters or brochures. A specialized correspondence section can communicate very effectively with prospects as well as potential customers.

(v) Catalogues

Catalogues are largely used when a firm manufactures different types of products which are distinguished by size, shape and other features. The following purpose can be served by catalogues:

- To get orders
- To make the customers aware about the specifications

- To provide detailed information
- To solicit product sales

(vi) Advertising Novelties

Small, interesting, or personally useful items, etc., can be used for sales promotion. To be effective an advertising novelty should meet the following requirements:

(a) It should not be a high cost item

(b) The novelty item should be usually eye-catching

(c) The item should be useful.

(vii) Entertainment of Customers

Entertainment of customers acts as a primary promotional device. But when the product is sold on a routine basis, customer entertainment is neither necessary nor justified.

(viii) Sales Contests

The main aim of sales contests is to motivate the sales personnel and increase sales, and bring more profit to the company. Under this scheme special incentives in the form of prizes or awards are offered.

(ix) Price—off

A price-off is simply a reduction in the price of the product to increase sales and is very often used in introducing a new product. Price-offs should generally be considered:

- For introducing new brands or existing brands with new uses
- For products/brands which are already doing better than the competing brands
- In conjunction with sales activities aimed at increasing retail distribution

Henkel, the German toiletries major, gave Rs. 10 off on a Rs. 40 pack when it introduced Pril scouring concentrate

(x) Refunds

It is an offer made by a manufacturer to give back a certain amount of money to a consumer.

(xi) Point-of-sales materials

The POS display persuades reminds and gives details to the consumers about a specific brand. Companies using this method are Procter and Gamble, Nestle and Parle.

(xii) Boosters for Dealers

In a bid to reduce its mounting inventories and boost the sagging morale of its dealers, Telco offered a 2 per cent discount to dealers on purchase of a truck if payment is made up-front. Also confessional interest rates were offered to expedite payments.

Strategy for new products

Train salesmen about the product, familiarize with the market segment and integrate advertising & sales promotion

i. Let the dealer be given details of the new product, his margins and promotion support

ii. Ensure sufficient quantity to get orders from dealers

iii. Deliver the merchandise at the retail outlets

iv. Arrange to advertise in media

v. Sample the product door to door with coupons

Promotion strategy should be focused on

(i) Sales force promotion

- Bonuses
- Sales rallies
- Best salesman award

(ii) Trade promotion

- Discounts
- Displays
- Force good
- Best dealer awards

(iii) Consumer promotion

- Point of purchase promotion
- Free samples
- Cash discounts
- Free trials
- Demonstrations

- Prizes
- Contests

Promotion Strategy for Industrial Products

Industrial products require different promotion strategies due to varied price range

(a) Documentation

Documentation is essential for improving the marketing effectiveness of a company. Documentation may include;

- Product literature
- Selection and performance charts
- Technical manuals
- Operation manuals
- Installation manuals
- Price lists

(b) Working models

Many firms supply the working or cutout models of their products to the dealers for display. This helps the customer understand the product easily. In addition, the companies also supply photographs and other display material.

(c) Exhibitions

Participation in a technical exhibition gives a higher visibility to a company. It is a meeting place for sellers and the buyers. Participation in India Machine Tools Exhibition (IMTEX). Hanover (Germany) Engineering Trade Fair and many other such exhibitions has proved beneficial to many engineering units.

Financial Strategy

May types of financial analyses are used in strategic decision making these include ration analysis, break –even analysis and not present value analysis. Financial strategies are needed to

1. To raise capital with short-term debt, long-term debt, preferred stock, or common stock.
2. To lease or buy fixed assets.

3. To determine an appropriate dividend payout ration.
4. To use LIFO (Last –in, First –out), FIFO (First-in, First – out), or a market-value accounting approach.
5. To extend the time of accounts receivable.
6. To establish a certain percentage discount on accounts within a specified period of time.
7. To determine the amount of cash that should be kept on hand.

1. Ratio Analysis

(i) Ration analysis has been accepted as an effective tool of financial analysis. The systematic use of ratios leads to interpreting financial statements of a business enterprise. Ration is expressed in terms of proportion or percentage relationship between two sets of phenomena. For instance, the proportion (ratio) of gross profit to sale.

Analysis of financial ratios as a tool of strategic analysis may be utilized in two ways: Firstly – an analyst may compare the present ratio with the past and the expected future. For instance, the current ratio i.e. the ratio of current assets to current liabilities – for the present year may be compared with current ratio of the preceding year to ascertain the level of improvement or deterioration.

This trend analysis may be the pace setter or the eye opener for future performance of the organization. Secondly – ratios may trend analysis may be the pace setter or the eye opener for future performance of the organization. Secondly – ratios may also be utilized to compare the performance of the firm with an identical firm in the same industry or the other industry. This comparison will provide the basis of assessing the strength and weaknesses of other competitors in the market.

Ratios may be classified under four broad heads:

1. Liquidity
2. Activity
3. Profitability
4. Capital structure / Leverage Ratio.

(ii) Liquidity Ratios

Liquidity ratios seek to confirm the ability of the firm to fulfil its short term obligations. If the firm has greater liquidity than the

commitments due for payment, it means the firm has unutilized surplus which may be invested or used in such a manner that the rate of return is optimal. The firm may also put the funds in the expansion of business or diversification of its activities to increase rate of return on investment.

The ratios which indicate the liquidity of the firm are: (i) Net working capital (current assets – current liabilities) (ii) Current ratio (current assets ÷ current liabilities (iii) Acid Test Ratio/ quick Ratio (iv) Super quick ratios (v) Turnover Ratios.

(iii) Acid test ratio / quick ratio

= Current assets – (Inventories + Repayments)

Current liabilities

(iv) Turnover Ratios /Activity Ratios

Another way to ascertain the liquidity is how quickly a certain current asset could be converted into cash. Ratios measuring its ability is known as turnover ratios. These ratios may be classified under three heads: (1) Total Assets Turnover Ratio (2) Accounts Receivable Turnover Ratio (3) Inventory Turnover Ratio.

Inventory / Turnover Ratio

Inventory / Turnover Ratio may be worked out in the following manner.

Cost of goods sold

(Inventory I year + Inventory II year) ÷ 2

Profitability Ratios

Profit is the end result of all business activities including the use of capital. Profit is an objective index of judging the efficiency of the business enterprise.

Profitability ratios may be of two kinds:

(i) Return on sales (ROS) and

(ii) Return on Assets (ROA)

Return on Investment (ROI) is not different from Return on Assets (ROA). In a multi- product organization, a Return on Investment (ROI) is not different from Return on Assets (RoA). In a multi-product organization, a lower Return on Assets indicates a weak product or sub-optimal product or a few strong and more weaker products which lower down ROA or even ROI.

Capital Structure / Leverage Ratios

Financial solvency of the firm may be computed by establishing relationship between borrowed funds and owner's capital. Debt /Equity ratio seeks to establish this relationship. "This ratio reflects the relative claims of creditors and shareholders against the assets of the firm".

$$\text{D/E Ratio} = \frac{\text{Long –term Debt}}{\text{Shareholders Equity}}$$

Earnings per Share (EPS)

Another way of computing the profitability of a company from share holder's view point is the Earnings per share. It measures the profit available to equity holders. Profit available to equity holders are represented by the net profits after taxes and preference divided divided by the number of ordinary shares.

$$\text{EPS} = \frac{\text{Net Profit} - (\text{Interest} + \text{Tax} + \text{Preference dividend})}{(\text{No . of ordinary Shares I year} + \text{Ordinary Shares II Year}) \div 2}$$

Price Earning Ratio

It may be worked out as follows:

$$\text{Price Earning Ratio} = \frac{\text{Market Price of the Share}}{\text{EPS}}$$

2. Break – Even analysis – Case

3. Net Present Value (NPV) analysis.

This method involves calculation of the present value of estimated

cash inflows using the cost of capital as the discounting rae and subtracting from the aggregate present value of inflows the present value of cash outflows using the same discounting rate. IF NPV is positive or equal to zero, the investment project is accepted as economically viable. If it is negative the proposal is rejected. Using this, strategic investment proposals may be ranked in the descending order of the net present values. The market value of shares may increase with projects with positive NPVs are accepted.

HR Strategies

The HR strategy of many multinational companies to take part time temporary employees or leasing temporary employees from learing companies. Employees specially working in IT firms in India are working on one to five year projects and re experiencing ‘Pink – slip syndrome’ as to what to do after the project is completed. The worst hit are those employees who are sacked from their jobs after September, 11 2002 attack of world trade centre.

The number of employees who work only part – time is steadily increasing. Part-timers are attractive to a company because the firm does not need to pay fringe benefits, such as health insurance and pension plans.

Telecommuting, office at home, flexi time and career breaks are the order of the day firms also resort for employing from diverse cultures. Pharma companies like Hoechst and cosmetic firms like Avon could turnaround unprofitable inner city markets by taking local persons to manage local markets.

Information systems strategy

Corporations are increasingly adopting information system strategies in that they are turning to information systems technology to provide business units with competitive advantage.

In 1989, Wal-Mart started building a huge database of customer information in its data warehouse systems located at its headquarters at Bentonville, Arkansas. The company collected sales and customer related information for each store and fed that information into the warehouse systems.

In the early 1990s, Wal-Mart continued to employ new technologies to facilitate better analysis of customer data as they became available. Wal-mart's IT experts used 3-D visualization tools to make accurate estimates of products most likely to be bought by customers on the basis of parameters such as ethnicity, geographic location, weather patterns, local sports affiliations, and around 10,000 other varied parameters. Wal-Mart made around 90% of its stock replenishments every month, based on the analysis of customer data generated through the data warehouse.

To make shopping at Wal-Mart a pleasant experience, Wal-Mart installed customer information kiosks in its stores in 1996. The kiosks helped customers find out the price of any product and get a brief description of it. In 1996, Wal-Mart launched its website – www.walmart.com - to provide information to its customers on all the products it stocked and to enable online sales.

IT played an important role in improving the efficiency of operations at Wal-Mart. The benefits which accrued were passed on to customers, as per Wal-Mart's policy. Wal-Mart's annual report 1999 said, "The first and the most important thing about Wal-Mart's information systems is precisely that the customer's needs come first. By using technology to reduce inventory, expenses and shrinkage, we can create lower prices for our customers and better returns for our shareholders".

At the dawn of the new millennium, Wal-Mart was one of the world's largest companies, with revenues of $165 bn in fiscal 2000. Wal-Mart's 'store of the community' program made effective use of bar code technology and advanced data mining techniques. The 'store of the community' program was a very successful initiative by Wal-Mart, which contributed to increased customer loyalty. By 2003, Wal-Mart was the world's largest company, with revenues in fiscal 2002 amounting to $244.5 bn. Multinational corporations are finding that the use of a sophisticated intranet for the use of its employees allows them to practice follow – the –sun management, in which project team members living in 1 country can pass their work to team members in another country in which the work day is just beginning. Thus, night shifts are no longer needed. The development of instant translation software is also enabling workers to have online communication with coworkers in other countries who use a different language. Lotus Translation Services for Same time is a Java –based application that can deliver translated text during a chart session

or an instant in 17 languages. Software, e-lingo (www.e-lingo.com) offers a multilingual search function and Web surfing as well as text and e-mail translation.

Logistics Strategy

Logistics strategy deals with the flow of products into and out of the manufacturing process. Three trends are evident: centralization, outsourcing, and the use of the Internet. To gain logistical synergies a cross business unit, corporations began centralizing logistics in the head-quarters group. This centralized logistics group usually contains specialists with expertise in different transportation modes such as rail or trucking. They work to aggregate shipping volumes across the entire corporation to gain better contracts with shippers. Companies like Amoco Chemical, Georgia – Pacific, Marriott, and Union Carbide view the logistics function as an important way to differentiate themselves from the competition, to add value, and to reduce costs.

May companies have found that outsourcing of logistics reduces costs and improves delivery time. Many companies are using the Internet to simplify their logistical system. For example, Ace Hardware created an online system for its retailers and suppliers.

Strategies to Avoid

If managers lack analysis and creativity they may get trapped into weak strategies leading to failure. The following strategies should be avoided.

Follow the Leader

Imitating a leading competitor's strategy might seem to be a good idea, but it ignores a firm's particular strengths and weaknesses and the possibility that the leader may be wrong.

Hit Another Home Run

If a company is successful because it pioneered an extremely successful product, it tends to search for another super product that will ensure growth and prosperity. Like betting on long shots at the horse races, the probability of finding a second winner is slight. Polaroid spent

a lot of money developing an "instant" movie camera, but the public ignored it in favor of the camcorder.

Arms Race

Entering into a spirited battle with another firm for increased market share might increase sales revenue, but that increase will probably be more than offset by increases in advertising, promotion, R&D, and manufacturing costs. Since the deregulation of airlines, price wars and rate "specials" have contributed to the low profit margins.

Do Everything

When faced with several interesting opportunities, management might tend to lead at all of them. At first, a corporation might have enough resources to develop each idea into a project, but money, time, and energy are soon exhausted as the many projects demand large infusions of resources.

Ex:- Walt Disney

Losing Hand

A corporation might have invested so much in a particular strategy that top management is unwilling to accept its failure. Believing that it has too much invested to quit, the corporation continues to throw" good money after bad".

Ex:- Indian Airlines is one such company.

Selecting the Best Strategy

Perhaps the most important criterion is the ability of the proposed strategy to deal with the specific strategic factors developed earlier in the SWOT analysis. IF the alternative doesn't take advantage of environmental opportunities and corporate strengths / competencies, and lead away from environmental threats and corporate weaknesses, it will probably fail.

Another important consideration in the selection of a strategy is the ability of each alternative to satisfy agreed – on objectives with

the least resources and the fewest negative side effects. It is, therefore, important to develop a tentative implementation plan so that the difficulties that management is likely to face are addressed.

Self Assessment Questions

1. What is marketing strategy? How will u design a promotional strategy for a company?

2. What is push-pull strategy in sales promotion?

3. What is financial strategfy and what is its necessity?

4. What do you mean by information system strategy?

References

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Lesson 16 - Logistics And Information Strategies

Lesson Outline

- Introduction
- Logistics strategies
- Information system strategies
- Summary
- Self-assessment questions
- Activities
- References

Learning Objectives

After reading this lesson you should be able to

- Understand the key issues in logistics and information system
- Appreciate the strategies companies adopt for effective contribution to corporate goals.

Introduction

Among the functional strategies a firm, logistics and information systems have become important in the new era of globalization, integration and IT development. Physical distribution along with channel development has moved from logistics to supply chain management with the advent of information and communication technology. Companies are developing information system strategies as derivatives of corporate strategies.

Logistics Strategies

The process of getting goods to customers has traditionally been called physical distribution. It includes location of plants and warehousing, transportation mode, inventory and packing. The systems concept of physical distribution takes into account the interdependence of costs of each activity. It is now being termed as integrated market logistics which can be conceptualized as the series of sales-satisfying

activities that begin when the customer places the order and that end with the delivery of the product to the customer. The main elements are:

- Order processing
- Ware housing
- Inventory
- Transportation

Recently, the concept of integrated market logistics system is referred to as supply chain management, which is broader in it s scope. It is concerned with all the flows starting from supplier to manufacturer to customer. As such integrated market logistics system is a subset of supply chain management of a firm.

Significance of logistics

Responsive logistical service advances customer satisfaction and creates the opportunity for closer and more profitable buyer-seller relationships.. Logistics service is often ranked by buyers right behind "quality" as a criterion for selecting a vendor

(1) Time factor

Logistics creates place and time utilities to consumers. Companies lose their customers when they fail to supply goods on time.

(2) Cost factor

Experts believe that substantial savings can be effected in physical distribution area, which has been described as 'the lost frontier for cost economies'. Physical distribution decisions when uncoordinated, result in high cost. There is a need to make use of modern decision tools for coordinating inventory levels, transportation modes, and plant, ware house and store locations.

(3) Promotion factor

It is not only a cost, it is a potent tool in competitive marketing. Companies can attract additional customers by offering better service or lower price through improvements in physical distribution.

Objectives

The objective of physical distribution is getting the right goods to the right places at the right time for the least cost. Evidently, this involves a trade—off between customer service and cost.

Maximum customer service implies large inventories, premium transportation and multiple warehouses all of which raise distribution cost. Minimum distribution cost implies cheap transportation, low stocks and few ware houses.

As such physical distribution decisions must aim at optimization of total system and not the sub optimization at the subsystem levels i.e., order processing, warehousing, inventory and transportation.

(i) Customer service

Marketers have to decide their service standards based on key information about customers and competitors.

1. What the customers are looking for?
2. What the competitors are offering?

Table 16-1 describes the various elements of service. Typical service standards are:

- Put the product within an arms length of customers
- To deliver at least 95 per cent of the dealer's orders within seven days of the receipt
- To ensure that damage to merchandise in transit does not exceed 5 percent

However, not all products or all customers require the same level of logistical service.

Many business products that are made to order—such as heavy machinery—have relatively low logistical service requirements. Others, such as replacement parts, components, and subassemblies, require extremely demanding logistical performance. Similarly, customers may be more or les responsive to varying levels of logistical service.

Table 16-1 Elements of Logistics Service

Elements	Description
Delivery time	The time from the creation of an order to the fulfillment and delivery of that order encompasses both order-processing time and delivery or transportation time.
Delivery reliability	The most frequently used measure of logistics service, delivery reliability focuses on the capability of having products available to meet customer demand.
Order accuracy	The degree to which items received conform to the specification of the order. The key dimension is the incidence of orders shipped complete and without error.
Information access	The firm's ability to respond to inquires about order status and product availability
Damage	A measure of the physical conditions of the product when received by the buyer.

Ease of doing business	A range of factors including the ease with which orders, returns, credits, billing, and adjustments are handled
Value-added services	Such features as packaging, which facilitates customer handling, or other services such as pre pricing and drop shipments.

Source

Jonathon L. S. Byrnes, William C. Copacino, and Peter Metz, "Forge Service into a Weapon with Logistics," Transportation & Distribution, Presidential Issue 28 (September 1987): p.46.

(ii) Cost

The next step is developing a cost function for a service level as shown below.

$$D = T + FW + VW + S$$

Where

D = total distribution cost of proposed system

T = total freight cost

FW = total fixed warehouse costs

VW = total variable warehouse costs

S = Total cost of sales lost due to average delivery delay under proposed system.

The company should aim at minimizing the distribution cost of reaching a target level of customer service.

Key Decisions

1. We will now examine the four major decision issues
2. How should orders be handled? (order processing)
3. Where should stocks be located? (warehousing)

4. How much stock should be held? (inventory), and
5. How should goods be shipped? (transportation).

(a) Order Processing

The first phase in physical distribution is order – shipping – billing cycle. A customer order initiates several steps

1. Order department prepares multi copy invoices and dispatches them to various departments.
2. Order is checked with available stock. Items out of stock are back ordered
3. Items are shipped. Shipped items are accompanied by shipping and billing documents with copies going to various departments.

The whole process is now expedited with the help of computers by warehousing

(b) Warehousing

A storage function is necessary because the production will be more than customer orders in general. Striking a balance between customer service standards and distribution costs, marketers has to

1. Decide on a desirable number of stocking locations depending upon the markets the firm intends to serve
2. Choose the type of warehouses. Today a variety of warehouses, with advanced material handling systems and storage facilities are available.

(c) Inventory

Inventory management requires decisions relating to

1. Level of stock – Determining optimum order quantity
2. Time of ordering – Reorder point
3. Minimum stock level to meet emergencies – safety stock

Today, just – in – time production practices and product customization are changing the inventory planning practices

(d) Transportation

Marketers have to make careful choice of transportation mode and organizations. In choosing a transportation mode for a particular

product, shippers consider such criteria as

1. Speed
2. Frequency
3. Dependability
4. Capability
5. Availability
6. Cost

Logistics and supply chain strategies

Supply chain strategy determines the nature of procurement of raw materials, transportation of materials to and from the company, manufacture of the product or operation to provide the service, and distribution of the product to the customer, along with any follow-up service. From a value chain perspective, supply chain strategy specifies what operations, distribution, and service will try to do particularly well. Additionally, in each company, strategies will also be devised for finance, accounting, information technology, and human resources. The value chain emphasizes the close relationship between all the functional strategies within a company. .

The strategic fit requires that a company achieve the balance between responsiveness and efficiency in its supply chain that best meets the needs of the company's competitive strategy. Table 16-2 makes a comparison of efficient and responsive supply chains.

Table 16-2 Comparison of Efficient and Responsive Supply chains

Aspect	**Responsive supply chain**	**Efficient supply chain**
Primary goal	Supply demand at the lowest cost	Respond quickly to demand
Product design Strategy	Maximize performance at a minimum product cost	Create modularity to allow postponement of product differentiation