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Subject Area - Business

Devising a strategy

Devising a strategy should be a product of logical and external analysis, yet often appears to be a product of the power of stakeholders. Discuss using recent business examples.

Johnson and Scholes (2002) p10 define strategy as "the direction and scope of an organisation over the long term, which achieves advantage for the organisation through its configuration of resources within a changing environment and to fulfil stakeholder expectations." A strategic plan is therefore large scale future oriented activities that allow interaction with the competitive environment in order to achieve company objectives. It follows that strategic management is the process whereby a strategy is formulated, evaluated, and continuously improved. Strategic planning flows from the definition of an organisation's vision, mission and objectives and subsequent environmental scanning, to understand the organisation's strategic position with respect to the macro external environment, its industry, competitors, internal resources, competencies and expectations and influence of stakeholders. (Stoner, Freeman and Gilbert, 1995) This initial process establishes a basis for strategic choice by means of a match of identified strengths to opportunities. The translation of strategic choice into action is then implemented across all levels of the organisation through programmes, resources, technologies, and performance management structures. (Johnson and Scholes, 2002 and Davis, 2005) This essay focuses on the strategic position of the organisation in the context of its environment, its strategic capability, and stakeholder expectations.

The purpose of an environmental scan is to develop a list of diverse variables from an uncertain and complex world to offer actionable responses and in so doing allow a structured framework for defensive or offensive actions. There are a variety of available analysis tools such as a PESTEL framework from a macro-environmental level, Porter's Five Forces framework at an industry level, strategic groupings within an industry and individual market analysis. The results can then be applied in a SWOT (Strengths, Weaknesses, Opportunities, and Threats) analysis to determine strategic choice. (Johnson and Scholes, 2002)

PESTEL is an acronym representing the key forces that exist or are emerging in the external environment and suggests how they will, or might impact on future strategy and resources. These comprise Political, Economic, Sociocultural, Technological, Environmental and Legal factors. (Johnson and Scholes, 2002) Changes in these forces and their interaction affect the types of products and services offered and impact on suppliers and distributors to the organisation. An example of political and legal forces in setting the climate for business, are the tax harmonisation processes in the European Union (EU) which have caused many multinational firms, including John Deere and Cargill, to relocate their head offices to Switzerland, a non EU member to avoid tax costs. Consequentially, the global competitive ratings for the Netherlands, Germany and other home countries of these firms plunged whilst the rating for Switzerland has surged. (Davis, 2005) The use of PESTEL in isolation and a mere listing of possible influences without an understanding of the combined impact of a number of these forces could lead to inaction with respect to countering threats or pursuing opportunities to the detriment of the business. The combined effect of the factors can be understood by identifying structural drivers of change that affect the structure of an industry sector or market. These include an increasing convergence of markets as customer needs and wants become similar (eg standardisation of strategy textbooks across international higher education institutions), maximising cost advantages achieved through economies of scale by

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centralised production in low cost, labour efficient countries such as India and China, or the differential impact of the factors dependant on industry type. (eg Pharmaceutical sales to an aging population in a first world country) (Johnson and Scholes, 2002) This reinforces the need to regard strategy formulation as an interactive multidisciplinary process requiring creative thinking.

Porter suggests that industry selection and analysis is a vital component of strategic planning. An industry is "a group of firms producing products that are close substitutes for one another." (Johnson and Scholes, 2002, p110) Competitive forces within an industry can be analysed in the contexts of the sources of competition, the dynamics of that competition and strategic groupings. Although criticised as being too generic in nature, Porter's Five Forces framework is useful in addressing key interacting forces affecting a strategic business unit with a distinct market for goods or services within an industry. Porter referred to these forces as the microenvironment so as to contrast it with the more general term, macro environment. They consist of those forces close to an organisation that affect its ability to serve its customers and make a profit. A change in any of the forces normally requires a company to re-assess the marketplace. (Porter, 1996) An example is that of the mobile phone network industry where the barrier to entry by new competitors is the huge entry cost associated with 3G broadband licenses. The purchasing power of buyers is high with a significant range of choices between networks and the power of suppliers increasing through alliances such as that of Casio and Hitachi in 2003. (Davis, 2005) The threat of substitute products is increasing as Personal Digital Assistance (PDA) convergence with phones and voice-over-internet technology emerges with the potential to bypass the network operators. Competitive rivalry between firms with similar products is high with a broad range of products on offer to the consumer. (Johnson and Scholes, 2002)

The concept of strategic grouping addresses the criticism of Porter's model where an industry is considered to be too generic to provide a basis for understanding the competitive environment by applying the Five Forces framework. Johnson and Scholes, 2002, p122 define strategic groups as "organisations within an industry with similar strategic characteristics following similar strategies or competing on similar bases." These firms are not homogeneous within the industry and follow strategies common to the group, but different to firms in other groups in the same industry. An example is a pharmaceutical manufacturer with a unique medication product protected by patent serving a common market using a similar strategy. (Davis, 2005)

Understanding the competitive environment together with current and potential customer needs and wants will determine the success or failure of an organisation. Porter suggests that there are two generic strategies: cost or differentiation. Marketing segmentation identifies similarities and differences between individual and customer groups based on geographic, demographic lifestyle and benefit segmentation. An appreciation of customer values in a market segment and matching needs against the organisation's capacity to meet those needs, is a critical aspect of determining strategic capability. (Pitt, 1997) The emergence of global firms suggests that traditional models are limited in application and that there is a need for the development of a broader integrative international strategic business model framework. (Ricart et al, 2004)

Strategic capability involves the identification and evaluation of an organisation's strengths and weaknesses in the functional areas of the business in the context of the external environment analyses. It is typically recorded in a SWOT framework. It represents an understanding of customer's perceptions of value, the critical success factors through which that value is realised and unique competencies, processes, and technology to achieve competitive advantage. (Hussey,

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2002.)

The core competencies of the organisation are the unique capabilities that are critical success factors in achieving competitive advantage and hence key to the delivery of customer value. They form the foundation for differentiation and for increasing perceived customer benefits. Competencies must evolve as the needs and wants of customers change and a focus on developing critical competencies that affect market position, share and power is key. (Hamel and Prahalad, 1994) A useful model to analyse an organisation's core competencies that underpin its competitive advantage is Porter's Value Chain Analysis. This attempts an understanding of how the organisation creates customer value by examining the contributions of various activities within the business to that value. An organisation's value chain is normally part of a broader value system that represents a set of inter-organisational linkages and relationships to create the product or service. It separates primary and support activities through which that value is generated. (Johnson and Scholes, 2002) Porter argues that competitive strategy is about being different, and focussing on those activities that deliver a unique mix of value and doing them better than competitors. (Porter, 1996)

The structured and systematic process of analysing the external and internal environment described thus far is carried out by a consultative process with stakeholders and should present a sound basis for establishing the foundation for the organisation's strategy formulation. However, the impact of stakeholders and the complex role that people play from a political and cultural perspective should be taken into account. (Johnson and Scholes, 2002) Davis, 2005, suggests that stakeholders are individuals or groups with an interest in the success of an organisation to deliver intended results and on whom the organisation itself depends.

Donaldson and Preston, 1995, p64, argue that this general statement is too wide should be qualified to "be those persons or groups with a legitimate interest in procedure and / or substantive aspects of corporate activity." Walsh, 2005, suggests that too broad a definition creates a situation whereby managers function in order benefit a stakeholder group or act as a continuous conduit to stakeholders. Stakeholders may include employees, unions, customers, financial institutions, suppliers, shareholders etc depending on the accepted definition. The definition of stakeholder is therefore important to the organisation because it impacts on the strategic plan formulation.

The relationship between stakeholders and the organisation encompasses the field of stakeholder management that ranges in complexity from stakeholder mapping through to stakeholder collaboration and social capital. The corporate governance structure of the organisation and the regulatory framework within which it operates should determine who the organisation serves and how the purpose and direction of the organisation is determined. This includes the management of the capacity of a stakeholder to influence the organisation as well as accountability issues in the formal structure. This is typically structured through a separation of ownership and management at main board level, balanced by non-executive directors and a non executive chairperson. Internal or organisational stakeholders may blur this line through the inappropriate use of power and politics. Society in turn creates expectations of the organisation in terms of ethics and within a cultural context that need to be congruent with that of the organisation. (Donald and Preston, 1995)

The organisational field approach suggests that networks of related organisations develop which share common assumptions, values, and processes that may incorporate common organisational views on stakeholders. Under this scenario, relationship with stakeholders are taken for granted leading to legitimised strategies shaped by expectations being accepted without a structured strategic planning process occurring. (Walsh, 2005)

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A stakeholder map is a tool that inventories and categorises a company's stakeholders, shows their inter-relationships, expectations, and power. It illustrates the approaches that the organisation can follow to achieve its business objectives while winning support from its stakeholders. It raises the dilemma of ethics in that stakeholder management through such a strategy can be subverted to the detriment of the organisation. (Johnson and Scholes, 2002) The Enron debacle is manifestation of both this dilemma and the organisational field phenomenon which allowed the failure of corporate governance structures when unethical conduct was accepted in the areas of finance and management by organisational stakeholders. The Enron case was one of the largest bankruptcy cases in US history. In 2001, it was the fifth largest company on the Fortune 500 with revenues of USD 100 billion, 19,000 employees, and rated the "most admired company" six years in a row by Fortune magazine. (Culpan and Trussell, 2005) The basic premise of Enron's strategy was to create markets for goods and services traditionally transacted through complex distribution channels. It leveraged off its competitive advantage of delivering services efficiently and stretching it's competency through added risk management features. The high growth phase of the organisation during the 1990's and changed business strategy and corporate culture of Enron was driven by top management. In the process, Enron appeared innovative and profitable to the extent that the traditional agency relationship underpinning the firm as a nexus of contracts between the shareholders (principals) and the management as agents were left unchecked, which in turn impacted negatively on the broader spectrum of stakeholders. (Donald and Preston, 1995 and Culpan and Trussell, 2005) An ostensibly well structured, high profile corporation within the highly regulated environment of a security exchange, audited by a major audit firm was bought down by unethical conduct of its senior executive team with possible collusion by external stakeholders.

The ultimate test of how well a strategy has been thought out is at implementation level and the controls around that implementation. Unless a strategy can be executed effectively with appropriate checks and balances then it will almost certainly fall short in achieving objectives. This means that strategy has to be linked to the organisation's objectives, mission, operations, and measurable outcomes within a corporate governance framework that meets the needs of the stakeholders. The evolution of the Kaplan and Norton's Balanced Scorecard to incorporate financial, customer, learning and growth, and internal process metrics evaluated against the vision and strategic objectives of the organisation provide one such strategic management control methodology across the organisation. (Kaplan and Norton, 1996 and Kaplan and Norton, 2001)

In conclusion, this essay has examined the formal process of strategy development and given examples of tools from the literature to systematically evaluate the external and internal environments of the organisation. It has sought to demonstrate that organisations are facing dynamic and rapidly evolving forces that influence its strategic direction. This is especially true with the emergence of globalisation and intensively competitive world markets. The eventual choice of a strategic direction for an organisation is a function of the values and expectations of a broad range of stakeholders which influence strategic decision making through political power over the organisation within a cultural and ethical context. It is the control through governance structures, and ongoing measurement of the strategic implementation process that will determine the successful outcome of the strategy and concomitant success of the organisation.

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