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Ministry of Education and Science of Ukraine
Sumy State University
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Economics and Management

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STRATEGY OF ENTERPRISE

LECTURE NOTES

Sumy
Sumy State University
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STRATEGY OF ENTERPRISE

LECTURE NOTES

on the discipline “***Strategy of Enterprise***”
for students of the specialty 051 “***Economics***”
all forms of training

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Contents

Introduction

This course helps students understand the basics of strategic planning process and choose strategic alternatives in conditions of uncertainty. Students will examine strategy hierarchy for single-business organisations (competitive strategy, which develops and sustains a competitive advantage for the goods and services that are produced) and multi-business organisations (corporate strategy, which is the hierarchically highest strategic plan of the organisation, which defines the global goals and ways of their achieving within strategic management).

For strategy formation purposes students will:

1. Conduct environment analysis, forecasting future development, identify opportunities and threats, strengths and weaknesses, competitive evaluation, forecast of change.
2. Set mission, goals, and objectives.
3. Compare goals and objectives of the environment analysis, identifying and eliminating gaps, develop alternative strategies.
4. Model variant scenarios (optimistic, pessimistic and most likely).
5. Choose the most appropriate alternative strategy.
6. Formulate final version of the strategic plan of the company.
7. Develop strategic plan.
8. Develop operational plans and projects.
9. Implement strategic plan and strategic management.
10. Give practical assessment, monitoring and feedback, if errors, defects in the formation of a strategic plan on any of the stages were detected.

This course will help students positioning the business against rivals; anticipating changes in demand and technologies; adjusting the strategy to accommodate them; influencing the nature of competition through strategic actions such as vertical integration and through political actions such as lobbying as well as achieving greater market penetration by becoming highly efficient at servicing its market with a limited product.

Topic 1. Strategy: concept, evolution and planning

1.1. Strategy concept, characteristics, evolution
1.2. Hierarchical levels of strategy
1.3. The strategic planning process

1.1 Strategy concept, characteristics, evolution

Strategy (from Greek στρατηγία stratēgia, "art of troop leader; office of general, command, generalship") is a high level plan to achieve one or more goals under conditions of uncertainty. In the sense of the "art of the general", which included several subsets of skills including "tactics", siegecraft, logistics etc., the term came into use in the 6th century C.E. in East Roman terminology, and was translated into Western vernacular languages only in the 18th century. From then until the 20th century, the word "strategy" came to denote "a comprehensive way to try to pursue political ends, including the threat or actual use of force, in a dialectic of wills" in a military conflict, in which both adversaries interact.

Strategy is important because the resources available to achieve these goals are usually limited.

Strategy generally involves setting goals, determining actions to achieve the goals, and mobilizing resources to execute the actions. A strategy describes how the ends (goals) will be achieved by the means (resources). The senior leadership of an organization is generally tasked with determining strategy. Strategy can be intended or can emerge as a pattern of activity as the organization adapts to its environment or competes. It involves activities such as strategic planning and strategic thinking.

Henry Mintzberg from McGill University defined strategy as "a pattern in a stream of decisions" to contrast with a view of strategy as planning, while Max McKeown (2011) argues that "strategy is about shaping the future" and is the human attempt to get to "desirable ends with available means". Dr. Vladimir Kvint defines strategy as “a system of finding, formulating, and developing a doctrine that will ensure long-term success if followed faithfully”.

Professor Richard P. Rumelt described strategy as a type of problem solving in 2011. He wrote that good strategy has an underlying structure he called a kernel. The kernel has three parts: 1) A diagnosis that defines or explains the nature of the challenge; 2) A guiding policy for dealing with the challenge; and 3) Coherent actions designed to carry out the guiding policy.

1.2. Hierarchical levels of strategy

Strategy can be formulated on three different levels:

- corporate level;
- business unit level;
- functional or departmental level.

While strategy may be about competing and surviving as a firm, one can argue that products, not corporations compete, and products are developed by business units. The role of the corporation then is to manage its business units and products so that each is competitive and so that each contributes to corporate purposes.

Consider Textron, Inc., a successful conglomerate corporation that pursues profits through a range of businesses in unrelated industries. Textron has four core business segments:

- Aircraft – 32 % of revenues;
- Automotive – 25 % of revenues;
- Industrial – 39 % of revenues;
- Finance – 4 % of revenues.

While the corporation must manage its portfolio of businesses to grow and survive, the success of a diversified firm depends upon its ability to manage each of its product lines. While there is no single competitor to Textron, we can talk about the competitors and strategy of each of its business units. In the finance business segment, for example, the chief rivals are major banks providing commercial financing. Many managers consider the business level to be the proper focus for strategic planning.

Corporate Level Strategy

Corporate strategy is the hierarchically highest strategic plan of the organization, which defines the global goals and ways of their achieving within strategic management.

A vision and mission are parts of the strategy. When developing the strategy, numerous analytical techniques are used (see PESTLE, SWOT, VRIO). When implementing the strategy, for example, the BSC is used.

Sometimes, the global strategy is distinguished as an overall plan, as well as specialized strategies dedicated to specific areas of functioning of the organization (financial or personal strategy, etc.)

Business Unit Level Strategy

A strategic business unit may be a division, product line, or other profit centre that can be planned independently from the other business units of the firm.

At the business unit level, the strategic issues are less about the coordination of operating units and more about developing and sustaining a competitive advantage for the goods and services that are produced. At the business level, the strategy formulation phase deals with:

- positioning the business against rivals;
- anticipating changes in demand and technologies and adjusting the strategy to accommodate them;
- influencing the nature of competition through strategic actions such as vertical integration and through political actions such as lobbying.

Michael Porter identified three generic strategies (*cost leadership*, *differentiation*, and *focus*) that can be implemented at the business unit level to create a competitive advantage and defend against the adverse effects of the five forces.

Functional Level Strategy

The functional level of the organization is the level of the operating divisions and departments. The strategic issues at the functional level are related to business processes and the value chain. Functional level strategies in marketing, finance, operations, human resources, and R&D involve the development and coordination of resources through which business unit level strategies can be executed efficiently and effectively.

Functional units of an organization are involved in higher level strategies by providing input into the business unit level and corporate level strategy, such as providing information on resources and capabilities on which the higher level strategies can be based. Once the higher-level strategy is developed, the functional units translate it into discrete action-plans that each department or division must accomplish for the strategy to succeed.

Stages of strategy formation

1. The first stage: environment analysis, forecasting future development, identify opportunities and threats, strengths and weaknesses, competitive evaluation, forecast of change.

2. The second stage or parallel (for start-ups – the first stage) – mission, goals, objectives.

3. The third stage: compare goals and objectives of the environment analysis, identifying and eliminating gaps, develop alternative strategies (strategic development options).

4. The fourth stage – modeling variant scenarios. Scenario (optimistic, pessimistic and most likely), research on the impact of each alternative strategies is formulated.

5. The fifth stage – choice of the most appropriate alternative strategies.

6. The sixth stage is a final version of the strategic plan of the company.

7. The seventh stage is based on the strategic plan development of medium tactical plans.

8. The eighth stage – developing operational plans and projects, and this strategic planning process is completed.

9. The ninth stage – implementation of the strategic plan, the process of strategic management.

10. The tenth stage – practical assessment, monitoring and feedback, if errors, defects in the formation of a strategic plan on any of the stages were detected.

1.3. The strategic planning process

In today's highly competitive business environment, budget-oriented planning or forecast-based planning methods are insufficient for a large corporation to survive and prosper. The firm must engage in **strategic planning** that clearly defines objectives and assesses both the internal and external situation to formulate strategy, implement the strategy, evaluate the progress, and make adjustments as necessary to stay on track.

Mission and Objectives

The mission statement describes the company's business vision, including the unchanging values and purpose of the firm and forward-looking visionary goals that guide the pursuit of future opportunities.

Guided by the business vision, the firm's leaders can define measurable financial and strategic objectives. Financial objectives involve measures such as sales targets and earnings growth. Strategic objectives are related to the firm's business position, and may include measures such as market share and reputation.

Environmental Scan

The environmental scan includes the following components:

- Internal analysis of the firm
- Analysis of the firm's industry (task environment)
- External macro-environment (PEST analysis)

The internal analysis can identify the firm's strengths and weaknesses and the external analysis reveals opportunities and threats. A profile of the strengths, weaknesses, opportunities, and threats is generated by means of a SWOT analysis.

An industry analysis can be performed using a framework developed by Michael Porter known as Porter's five forces. This framework evaluates entry barriers, suppliers, customers, substitute products, and industry rivalry.

Topic 2. Mission & Goals of Companies

2.1. Vision and mission statement
2.2. Goals and objectives: types and characteristics
2.3. Company's objectives formation mechanisms

2.1. Vision and mission statement

Your **mission** is what you intend to become or accomplish. It should be challenging but achievable. A well-written mission statement demonstrates that you understand your business, have defined your unique focus, and can articulate your objectives concisely to yourself and others.

Mission: Defines the fundamental purpose of an organization or an enterprise, succinctly describing why it exists and what it does to achieve its vision.

For example, the charity above might have a mission statement as "providing jobs for the homeless and unemployed" [11].

When you're coming up with the concept for your business, an important component of your overall strategy plan is a mission statement. This brief statement declares the purpose of an organization and defines the reason for the company's existence. It provides the framework and context to help guide the company's strategies and actions by spelling out the business's overall goal. Ultimately, a mission statement helps guide decision-making internally while also articulating the company's mission to customers, suppliers and the community.

What is the purpose of a mission statement?

A mission statement is not the same as your company's slogan, which generally serves as marketing tool designed to grab attention quickly. The mission statement is also not necessarily the same as your vision statement, which defines where you want your company to go. While you may include the statement in your business plan, a mission statement is not a substitute for the plan itself.

It's also important to remember that a mission statement is not evergreen. As a company evolves over time, its mission and intent may also change. A mission statement will keep your company on track, but it shouldn't become stale or irrelevant, so revisit it every few years to fine-tune it if necessary.

What does a mission statement include?

A good mission statement answers several key questions about your business:

1. What are the opportunities or needs that the company addresses?
2. What is the business of the organization? How are these needs being addressed?
3. What level of service is provided?
4. What principles or beliefs guide the organization?

The mission statement should be short, yet resonate with both employees and those outside of the organization. A statement should express the organization's purpose in a way that inspires support and ongoing commitment. It is up to the mission statement to set the tone of the company and to outline concrete goals.

2.2. Goals and objectives: types and characteristics

Business Goal: Goals are the broad primary outcomes towards which effort and actions are directed in a business. They are whats, not hows and a business might have multiple goals to achieve. For example, "we must be a leader player and increase our share in the home loan market". Normally there is no measurement in the definition of a goal and it only gives you the general direction of the company.

Business goals represent a clear statement of intent. Business goals are high-level and strategic, encompassing the entire team and every department in your business. Employee objectives are the measurable targets employees pursue in support of the business goals.

Goals are general statements of what you want to achieve. So they need to be integrated with your vision. They also need to be integrated with your mission of how you are going to achieve your vision. Examples of company goals are:

- To improve profitability
- To increase efficiency
- To capture a bigger market share
- To provide better customer service
- To improve employee training
- To reduce carbon emissions

Make sure the goals are focused on the important properties of the business. Be careful not to set too many goals. You run the risk of losing focus. Also, design your goals so that they don't contradict and interfere with each other.

Other than internal cost reductions, most goals that involve increasing sales have a marketing component. Growing market share, entering new markets and increasing a sales force's productivity can all be achieved at least in part through marketing. With this in mind, marketing objectives should be able to be directly aligned to corporate goals.

Marketing Objectives

Marketing objectives are directly linked to ways that a marketing department can move a big picture goal forward. For instance, if a company wants to grow its sales, one marketing objective could be open to a new geographic market. Another objective would be to convince existing clients to purchase more products from the company. Both would help achieve the broad goal, but both also pose marketing challenges.

2.3. Company's objectives formation mechanisms

The concept of "objectives tree" was first proposed by Charles Cherchmenom and R. Ackoff in 1957. It allows a person to arrange their own plans, to see their goals in the group.

These include the tree of goals that can identify which possible combinations provide the best returns. The term “tree” involves the use of a hierarchical structure, obtained by dividing the common goal to subgoals.

The method of tree targets is focused on obtaining a relatively stable framework of goals, problems, trends. To achieve this, the construction of the original structure should take into account patterns of goal formation and use the principles of formation of hierarchical structures.

The so-called tree of goals is closely linked to each other long-term goals and specific objectives for each level of the hierarchy. The goal of higher-order corresponds to the top of the tree, and later in several tiers there are local goals (objectives), which enable the achievement of the upper level.

The principle of partitioning the common goal to objectives and subgoals is illustrated in Figure 2.1.

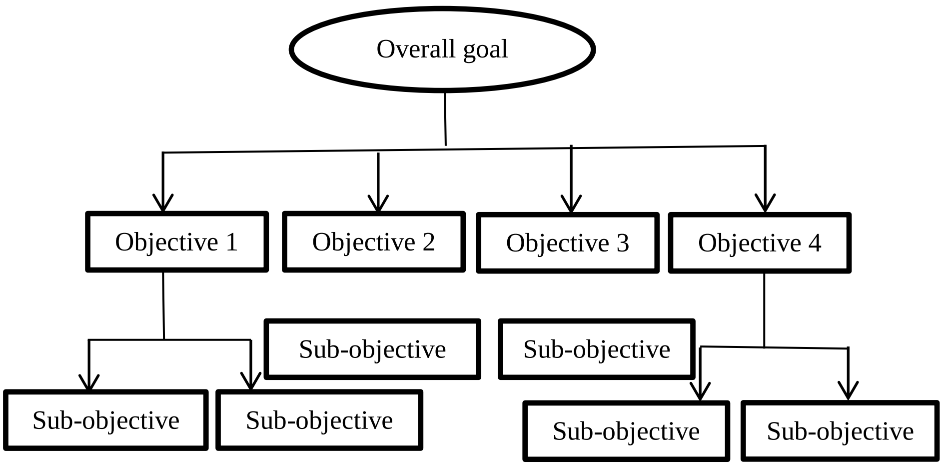

Figure 2.1 – The principle of partitioning the common goal to objectives and subgoals

Topic 3. Business Environment

3.1. General idea about business environment
3.2. Analysis of macro-environment
3.3. Analysis of microenvironment

3.1. General idea about business environment

The term business environment is composed of two words 'business' and 'environment'. In simple terms, the state in which a person remains busy is known as business. The word 'business' in its economic sense means human activities like production, extraction or purchase or sales of goods that are performed for earning profits.

On the other hand, the word 'environment' refers to the aspects of surroundings. Therefore, business environment may be defined as a set of conditions – social, legal, economical, political or institutional that is uncontrollable in nature and affects the functioning of organization. Business environment has two components:

1. Internal Environment
2. External Environment

Internal Environment: It includes 5 Ms, i. e. man, material, money, machinery and management, usually within the control of business. Business can make changes in these factors according to the change in the functioning of enterprise.

External Environment: Those factors which are beyond the control of business enterprise are included in external environment. These factors are: government and legal factors, geo-physical factors, political factors, socio-cultural factors, demographical factors, etc. It is of two Types: 1. Micro/Operating Environment 2. Macro/general Environment

Micro/Operating Environment: The environment which is close to business and affects its capacity to work is known as microenvironment or operating environment. It consists of suppliers, customers, market intermediaries, competitors and public.

Suppliers**:** They are the persons who supply raw material and required components to the company. They must be reliable and business must have multiple suppliers, i. e. they should not depend upon only one supplier.

Customers: Customers are regarded as the king of the market. Success of every business depends upon the level of their customer's satisfaction. Types of customers:

- wholesalers;
- retailers;
- industries;
- government and other institutions;
- foreigners.

Market Intermediaries: They work as a link between business and final consumers. Types are as follows:

- middleman;
- marketing agencies;
- financial intermediaries;
- physical intermediaries.

Competitors: Every move of the competitors affects the business. Business has to adjust itself according to the strategies of the Competitors.

Public: Any group having actual interest in business enterprise is termed as public, e. g. media and local public. They may be the users or non-users of the product.

Macro/General Environment: It includes factors that create opportunities and threats to business units. The elements of macro-environment are as follows:

1) ***Economic Environment:*** It is very complex and dynamic in nature that keeps on changing with the change in policies or political situations. It has three elements:
   - economic conditions of public;
   - economic policies of the country;
   - economic system.

Other economic factors: infrastructural facilities, banking, insurance companies, money markets, capital markets, etc.

2) ***Non-Economic Environment:*** The following elements are included in non-economic environment:

Political Environment: It affects different business units extensively. Its components are:

- political belief of government;
- political strength of the country;
- relation with other countries;
- defense and military policies;
- centre state relationship in the country;
- thinking opposition parties towards business unit.

Socio-Cultural Environment: Influence exercised by social and cultural factors, not within the control of business, is known as socio-cultural environment. These factors include: attitude of people to work, family system, caste system, religion, education, marriage etc.

Technological Environment: A systematic application of scientific knowledge to practical task is known as technology. Everyday there has been vast changes in products, services, lifestyles and living conditions, these changes must be analyzed by every business unit and should adapt these changes.

Natural Environment: It includes natural resources, weather, climatic conditions, port facilities, topographical factors such as soil, sea, rivers, rainfall, etc. Every business unit must look for these factors before choosing the location for their business.

Demographic Environment: It is a study of perspective of population i. e. its size, standard of living, growth rate, age-sex composition, family size, income level (upper level, middle level and lower level), education level, etc. Every business unit must see these features of population and recognize their various need and produce accordingly.

International Environment: It is particularly important for industries directly depending on import or exports. The factors that affect the business are: globalization, liberalization, foreign business policies, and cultural exchange.

Characteristics:

1. Business environment is compound in nature.
2. Business environment is constantly changing process.
3. Business environment is different for different business units.
4. It has both long term and short term impact.
5. The influence of external environment factors is unlimited.
6. It is very uncertain.

3.2. Analysis of macro-environment

The macro-environment analysis is traditionally the first step of a strategic analysis; it is sometimes referred to as an external analysis, PEST analysis or PESTLE analysis.

The purpose of the macro-environment analysis is to identify possible opportunities and threats to your industry as a whole that are outside the control of your industry. (Note: You will often be forecasting trends – like "interest rates will remain static" which may or may not be the case).

When completing a macro-environment analyses you will be seeking to answer the questions "what will affect the growth of our industry as a whole" and "what is the likely impact of all of the things that affect the growth of your industry".

For example: An aging population is a demographic trend in many western counties, which will result in an increase in the total number of caravans sold – if you are in the caravan industry you should expect to see growth in the total size of your industry.

These opportunities and threats may affect many industries, such as possible interest rate rises, but you should only be concerned if interest rate rises affect your industry.

For example: If you are in the greeting card industry and fluctuations in interest rates will not affect the size of your industry then you do not need to consider interest rates in your macro-environment analysis. (However, if you are heavily geared or have large borrowings, you will need to consider interest rates in your internal analysis).

PESTLE – Macro-Environmental Analysis

The PESTLE Analysis is a framework used to scan the organization's external macro-environment. The letters stand for Political, Economic Sociocultural, Technological, Legal and Environmental.

Some approaches will add in extra factors, such as International, or remove some to reduce it to PEST.

However, these are all merely variations on a theme. The important principle is identifying the key factors from the wider, uncontrollable external environment that might affect the organization.

The PESTLE Factors

We start with the political forces. First of all, *political factors* refer to the stability of the political environment and the attitudes of political parties or movements.

This may manifest in government influence on tax policies, or government involvement in trading agreements. Political factors are inevitably entwined with legal factors such as national employment laws, international trade regulations and restrictions, monopolies and mergers' rules, and consumer protection. The difference between political and legal factors is that political refers to attitudes and approaches, whereas legal factors are those which have become law and regulations. Legal needs to be complied with whereas political may represent influences, restrictions or opportunities, but they are not mandatory.

Legal factors: 1. Monopolies legislation. Antitrust regulation. 2. Employment law. 3. Health and safety. 4. Product safety.

Economic factors represent the wider economy so may include economic growth rates, levels of employment and unemployment, costs of raw materials such as energy, petrol and steel, interest rates and monetary policies, exchange rates and inflation rates. These may also vary from one country to another.

Economic factors:

1. GNP trends
2. Interest rates/savings rate
3. Money supply
4. Inflation rate
5. Unemployment
6. Disposable income
7. Business cycles
8. Trade deficit/surplus

Sociocultural factors represent the culture of the society that an organization operates within. They may include demographics, age distribution, population growth rates, level of education, distribution of wealth and social classes, living conditions and lifestyle.

1. Population demographics
    - ethnic composition
    - aging of population
    - regional changes in population growth and decline
2. Social mobility
3. Lifestyle changes
4. Attitudes to work and leisure
5. Education – spread or erosion of educational standards
6. Health and fitness awareness
7. Multiple income families

Technological factors refer to the rate of new inventions and development, changes in information and mobile technology, changes in internet and e-commerce or even mobile commerce, and government spending on research. There is often a tendency to focus technological developments on digital and internet-related areas, but it should also include materials development and new methods of manufacture, distribution and logistics.

3.3. Analysis of microenvironment

Porters Five Forces – Competitive Analysis

Porter's Five Forces Context

Generally, strategic planning commences with an analysis phase, where you seek to refresh your understanding of your businesses 3 key strategic environments. These three strategic environments that you analyze during your strategic analysis are:

- Macro-environment,
- Industry environment, (or Porter's Five Forces),
- Internal environment.

Porter's five forces is a competitive analysis model, it helps you to understand the nature of competition within your industry, and hence it is used when completing your industry analysis.

Porter's model provides a good, simple yet powerful, framework for developing comprehension of the competitive forces in your industry.

Discovering the Five Forces

Michael Porter developed a framework, which identified 5 forces that act to either increase or reduce the competitive forces within an industry. These five forces are:

- the bargaining power of your customers;
- the threat of new entrants into your industry;
- the bargaining power of suppliers;
- threat of substitute products or services;
- rivalry amongst existing firms.

Porters Five Forces – Overview of Each Force

By completing a competitive analysis you are becoming informed on who has the bargaining power before you commence negotiations with your customers and suppliers. Being informed ensues that your negotiations are less influenced by the skill of the negotiator and more by your commercial reality.

Now let us look at each of these five forces in more detail.

The Bargaining Power of Your Customers

When analyzing the power of your customers you are really determining who needs who the most. This is driven, in part, by the number of prospective customers compared to the number of suppliers (suppliers are your competitors).

A strong or powerful customer can play you off against your competitors. Your strong customers may ask for higher quality or improved service at the same price or simply, for a lower price. Where a less strong customer may simply try to bluff you.

The Threat of New Entrants to Your Industry

A new entrant to your industry is a brand new competitor or maybe a new brand from on old competitor.

A new competitor to your industry may erode some of your customer base, your challenge is to determine if it is likely that a new competitor will come along and try to steal your customers away.

New competitors are restricted by up front capital costs, access to technology or requirements to obtain licenses then your market position is likely to be protected. However, if there are no barriers to entry, your position could be weakened.

The Bargaining Power of Your Suppliers

The bargaining power of your suppliers is like the bargaining power of customers only in reverse, you are now the customer, where before you were the supplier.

Analyzing the bargaining power of your suppliers you are to answer the following questions: How dependent on your business is your supplier, or are you dependent on your supplier? How much power do your suppliers have? Can they raise prices or reduce service without the fear of losing your business?

Topic 4. Analysis of Internal Environment

4.1. Factors of internal environment that influence organizational decisions
4.2. Organization resources, capabilities, and core competencies
4.3. Approaches for scanning and analyzing internal environment

4.1. Factors of internal environment that influence organizational decisions

Forces or conditions, or surroundings with in the boundary of the organization are the elements of internal environment of organization. The internal environment consists mainly of the owners, board of directors, employees and culture of the organization.

1. **Owners:** Owners are people who invested in company and have property rights and claims on the organization. Owners can be an individual or group of persons who started the company; or who bought a share of the company in the share market. They have the right to change the company's policy at any time.

2. **Board of Directors:** The board of directors is the governing body of the company who are elected by stockholders, and they are given the responsibility of overseeing top managers of the firm such as general managers.

3. **Employees:** Employees, or the workforce are the most important element of organizations internal environment, who performs the tasks of the administration. Individual employees and also the labor unions they join are important parts of the internal environment. If managed properly they can positively change the

organizations policy. But ill-management of the workforce could lead to a catastrophic situation for the company.

4. **Culture:** Organizational culture is the collective behaviour of members of an organization and the values, visions, beliefs, habits that they attach to their actions. An organization's culture plays a major role in shaping its success, because culture is an important determinant of how well their organization will perform. As the foundation of the organization's internal environment, it plays a major role in shaping managerial behaviour.

Similarly if a manager does not know and understand the environment of organization, he or she will definitively get wet or dry, as well as the organization in today's fast and hyper moving organizational environment.

4.2. Organization resources, capabilities, and core competencies

The internal environment of a business is that part over which you have control as a manager. You can influence the things that go on in the business.

One must recognize that resources are only half the battle. The firm must also have the capability to take those resources and use them effectively. This is usually related to the strength of the management team and their capacity to make the right short and long-term decisions about the allocation of resources to the various pursuits of the company.

Core competencies are created by the superior resources put to use in a way that no other firm can replicate. Core competencies are those things that are fundamental to a firm's success. Core competencies are rare, not many firms can do what you do in this area. Core competencies are difficult if not impossible for another company to copy, usually because of capability and intangible resources of the firm, not because of physical resources. Core competencies are valuable to customers, that is, the things that your company does better than anyone else, someone else must be willing to pay for, or you are simply good at something, but it does not create long-term success of the company.

If you attempt to develop 10 core competencies, how are you going to develop and maintain all of them?

Successful firms tend to focus on 2 or 3 things they clearly do better than others.

Valuable Capabilities

A unique capability is to hire employees that are good with equipment and capable of fixing problems.

Rare Capabilities

In today's farm labor pool, loyal long-term employees that are good with equipment and can work on it are pretty few and far between. A farm that has this type of satisfied employee base likely has a key competitive advantage.

Because of the historical knowledge base contained by these "key" employees, it is costly if not impossible for other farms to gain this capability. Many times it is not even clear why these employees are so much better with equipment than others. Of course, the educational focus of our society puts well trained employees with the kind of skills needed in too high of a wage bracket for most farm businesses

Certainly there are some substitutes for employees that are good with machinery: good mechanics in the region, renting equipment, etc. However these are imperfect substitutes at best and erode the competitive advantage obtained with "key" employees.

4.3. Approaches for scanning and analyzing internal environment

Among approaches for scanning and analyzing internal environment we can emphasize *value chain analysis, functional analysis, core competencies analysis, value proposition – resource model.*

What is internal analysis?

Internal analysis is a component of situational analysis and the strategic marketing plan. The organization, marketing and financial situation are analyzed. The outcome of the analysis serves as input for SWOT. Where the external part of the situation analysis (competition, industry, distribution and customer analysis) takes care of opportunities and threats, the strong and weak points stem from the internal analysis. Internal analysis is thus of essential importance in formulating a strategy of business.

What does an internal analysis consist of?

Internal analysis usually consists of three components.

1. Organisation

Here is a description of the present strategy, organisational structure, and company structure. Describe and analyse the important strategy and objectives. Make an organigram and evaluate them. Do problems appear within the corporate culture that hamper growth? Countless factors must be researched according to the marketer's insight. There is no fixed "format". Subsequently a competence analysis can be made.

2. Marketing

The present fulfillment of the marketing mix, targeting, segmentation and positioning. Relevant points can be handled according to the marketer's insight. Are the chosen segments and positioning the correct ones? Conduct also a portfolio analysis (BCG-matrix, PLC: product lifecycle, MABA analysis).

3. Financial situation

Analysis of the present financial situation in relations to rentability, liquidity and solvability indicators.

Internal analysis. Understanding a business in depth is the goal of internal analysis. This analysis is based on the resources and capabilities of the firm.

Resources. A good starting point to identify company resources is to look at tangible, intangible and human resources.

Tangible resources are the easiest to identify and evaluate: financial resources and physical assets are identified and valued in the firm's financial statements.

Intangible resources are largely invisible, but over time become more important to the firm than tangible assets because they can be a main source for a competitive advantage. Such intangible recourses include reputational assets (brands, image, etc.) and technological assets (proprietary technology and know-how).

Resources are not productive on their own. The most productive tasks require that resources collaborate closely together within teams. The term organizational capabilities is used to refer to a firm's capacity for undertaking a particular productive activity. Our interest is not in capabilities per se, but in capabilities relative to other firms. To identify the firm's capabilities we will use the ***functional classification approach***. A functional classification identifies organizational capabilities in relation to each of the principal functional areas.

The value chain analysis (VCA) is one way to help identify core competencies in your business.

The value chain is a systematic approach to examining the development of competitive advantage. It was created by Michael Porter in his book, Competitive Advantage (1980). The chain consists of a series of activities that create and build value. They culminate in the total value delivered by an organization. The 'margin' depicted in the diagram is the same as added value. The organization is split into 'primary activities' and 'support activities'.

There are two different approaches on how to perform the analysis, which depend on what type of competitive advantage a company wants to create (cost or differentiation advantage).

Cost advantage

To gain cost advantage a firm has to go through 5 analysis steps:

Step 1. Identify the firm's primary and support activities. All the activities (from receiving and storing materials to marketing, selling and after sales support) that are undertaken to produce goods or services have to be clearly identified and separated from each other. This requires an adequate knowledge of company’s operations because value chain activities are not organized in the same way as the company itself. The managers who identify value chain activities have to look into how work is done to deliver customer value.

Step 2. Establish the relative importance of each activity in the total cost of the product. The total costs of producing a product or service must be broken down and assigned to each activity. Activity based costing is used to calculate costs for each process. Activities that are the major sources of cost or done inefficiently (when benchmarked against competitors) must be addressed first.

Step 3. Identify cost drivers for each activity. Only by understanding what factors drive the costs, managers can focus on improving them. Costs for labour-intensive activities will be driven by work hours, work speed, wage rate, etc. Different activities will have different cost drivers.

Step 4. Identify links between activities. Reduction of costs in one activity may lead to further cost reductions in subsequent activities. *For example,* fewer components in the product design may lead to less faulty parts and lower service costs. Therefore identifying the links between activities will lead to better understanding how cost improvements would affect the whole value chain. Sometimes, cost reductions in one activity lead to higher costs for other activities.

Step 5. Identify opportunities for reducing costs. When the company knows its inefficient activities and cost drivers, it can plan on how to improve them. Too high wage rates can be dealt with by increasing production speed, outsourcing jobs to low wage countries or installing more automated processes.

Differentiation advantage

VCA is done differently when a firm competes on differentiation rather than costs. This is because the source of differentiation advantage comes from creating superior products, adding more features and satisfying varying customer needs, which results in higher cost structure.

Step 1. Identify the customers' value-creating activities. After identifying all value chain activities, managers have to focus on those activities that contribute the most to creating customer value. *For example,* Apple products' success mainly comes not from great product features (other companies have high-quality offerings too) but from successful marketing activities.

Step 2. Evaluate the differentiation strategies for improving customer value. Managers can use the following strategies to increase product differentiation and customer value:

- add more product features;
- focus on customer service and responsiveness;
- increase customization;
- offer complementary products.

Step 3. Identify the best sustainable differentiation. Usually, superior differentiation and customer value will be the result of many interrelated activities and strategies used. The best combination of them should be used to pursue sustainable differentiation advantage.

Internal analysis – value proposition – resource model

To develop a value proposition using the resource model you will identify the resources that your firm has or that exist in your industry (with your competitors), then you compare your organization's competitive strength to that of your competitors. Essentially, the resource where you have the largest strength becomes your value proposition.

The types of resources that you will consider include tangible resources: which are assets that can be seen, touched and/or quantified.

Financial Aspect

Balance Sheet Ratio Analysis

Important balance sheet ratios measure liquidity (a business's ability to pay its bills as they come due) and leverage (the extent to which the business is dependent on creditors' funding). They include the following ratios:

Liquidity Ratios

These ratios indicate the ease of turning assets into cash. They include the current ratio, quick ratio, and working capital.

Current Ratios. The current ratio is one of the best known measures of financial strength. The main question this ratio addresses is: “Does your business have enough current assets to meet the payment schedule of its current debts with a margin of safety for possible losses in current assets, such as inventory shrinkage or collectable accounts?” A generally acceptable current ratio is 2 to 1. But whether or not a specific ratio is satisfactory depends on the nature of the business and the characteristics of its current assets and liabilities. The minimum acceptable current ratio is obviously 1:1, but that relationship is usually playing it too close for comfort.

If you decide your business’s current ratio is too low, you may be able to raise it by:

- paying some debts;
- increasing your current assets from loans or other borrowings with a maturity of more than one year;
- converting non-current assets into current assets;
- increasing your current assets from new equity contributions;
- putting profits back into the business.

Quick Ratios. The quick ratio is sometimes called the “acid-test” ratio and is one of the best measures of liquidity. The quick ratio is a much more exacting measure than the current ratio. By excluding inventories, it concentrates on the really liquid assets, with value that is fairly certain. It helps answer the question: “If all sales revenues should disappear, could my business meet its current obligations with the readily convertible ‘quick’ funds on hand?”

Working Capital. Working Capital is more a measure of cash flow than a ratio. The result of this calculation must be a positive number. Bankers look at Net Working Capital over time to determine a company's ability to weather financial crises. Loans are often tied to minimum working capital requirements.

Inventory Turnover Ratio

This ratio reveals how well inventory is being managed. It is important because the more times inventory can be turned in a given operating cycle, the greater the profit is.

Return on Investment (ROI) Ratio.

The ROI is perhaps the most important ratio of all. It is the percentage of return on funds invested in the business by its owners. In short, this ratio tells the owner whether or not all the effort put into the business has been worthwhile. If the ROI is less than the rate of return on an alternative, risk-free investment such as a bank savings account, the owner may be wiser to sell the company, put the money in such a savings instrument, and avoid the daily struggles of small business management.

Return of Total Assets (ROA), also known as return on investment, measures a firm's effectiveness at generating profits with its assets.

This measures how efficiently profits are being generated from the assets employed in the business when compared with the ratios of firms in a similar business. A low ratio in comparison with industry averages indicates an inefficient use of business assets.

Gross Profit and Gross Profit Margin

As explained above, the gross profit is calculated by deducting the cost of sales from the revenue or the sales that a company has generated in a financial year.

However, the gross profit margin is presented as a percentage and it tries to add comparability and correct for the fact that different companies have different sales figures.

SWOT Analysis

SWOT is an acronym used to describe the particular Strengths, Weaknesses, Opportunities, and Threats that are strategic factors for a specific company. A SWOT should represent an organizations core competencies while also identifying opportunities it cannot currently use to its advantage due to a gap in resources.

The SWOT analysis framework has gained widespread acceptance because of its simplicity and power in developing strategy. Just like any planning tool, a SWOT analysis is only as good as the information that make it up. Research and accurate data is vital to identify key issues in an organization's environment.

Assess your market:

- What is happening externally and internally that will affect our company?
- Who are our customers?
- What are the strengths and weaknesses of each competitor?
- What are the driving forces behind sales trends?
- Assess your company:
- What do we do best?

A challenge posed by an unfavorable trend or development that would lead (in absence of a defensive marketing action) to deterioration in profits/sales.

An evaluation needs to be completed drawing conclusions about how the opportunities and threats may affect the firm.

INTERNAL RESOURCES: the firm

- Identify the actual competitors as well as substitutes.
- Assess competitors' objectives, strategies, strengths & weaknesses, and reaction patterns.
- Select which competitors to attack or avoid.

The Internal Analysis of strengths and weaknesses focuses on internal factors that give an organization certain advantages and disadvantages in meeting the needs of its target market. Strengths refer to core competencies that give the firm an advantage in meeting the needs of its target markets. Any analysis of company strengths should be market oriented/customer focused because strengths are only meaningful when they assist the firm in meeting customer needs. Weaknesses refer to any limitations a company faces in developing or implementing a strategy (?). Weaknesses should also be examined from a customer perspective because customers often perceive weaknesses that a company cannot see. Being market focused when analyzing strengths and weaknesses does not mean that non-market oriented strengths and weaknesses should be forgotten. Rather, it suggests that all firms should tie their strengths and weaknesses to customer requirements. Only those strengths that relate to satisfying a customer need should be considered true core competencies.

Leave blank	**Strengths – S** List strengths	**Weaknesses – W** List weaknesses
Opportunities – O List opportunities	**SO Strategies** Use strengths to take advantage of opportunities	**WO Strategies** Overcoming weaknesses by taking advantage of opportunities
Threats – T List strengths	**ST Strategies** Use strengths to avoid threats	**WT Strategies** Minimize weaknesses and avoid threats

Figure 4.1 – SWOT matrix

Focus on your strengths. Shore up your weaknesses. Capitalize on your opportunities. Recognize your threats.

Identify:

- Against whom do we compete?
- Who are our most intense competitors? Less intense?
- Makers of substitute products?

Topic 5. Enterprise Resource Planning

5.1. ERP definition & evolution
5.2. Balance Score Card
5.3. Key Performance Indicators

5.1. ERP definition & evolution

ERP is the acronym of Enterprise Resource Planning. ERP utilizes ERP software applications to improve the performance of organizations' resource planning, management control and operational control. ERP software is multi-module application software that integrates activities across functional departments, from product planning, parts purchasing, inventory control, product distribution, to order tracking. ERP software may include application modules for the finance, accounting and human resources aspects of a business.

ERP vs. CRM and SCM

CRM (Customer Relationship Management) and SCM (Supply Chain Management) are two other categories of enterprise software that are widely implemented in corporations and non-profit organizations. While the primary goal of ERP is to improve and streamline internal business processes, CRM attempts to enhance the relationship with customers and SCM aims to facilitate the collaboration between the organization, its suppliers, the manufacturers, the distributors and the partners.

ERP Definition – Systems Perspective

ERP, often like other IT and business concepts, is defined in many different ways. A sound definition should serve several purposes:

1. It answers the question of "what is ... ?".

2. It provides a base for defining more detailed concepts in the field – ERP software, ERP systems, ERP implementation etc.

3. It provides a common ground for comparison with related concepts – CRM, SCM etc.

4. It helps answer the basic questions in the field – benefits of ERP, the causes of ERP failure etc.

A definition of ERP based on **Systems Theory** can serve those purposes.

ERP is a system which has its goal, components, and boundary.

The Goal of an ERP System is to improve and streamline internal business processes, which typically requires reengineering of current business processes.

The Components of an ERP System are the common components of a Management Information System (MIS).

- **ERP Software** – module based ERP software is the core of an ERP system. Each software module automates business activities of a functional area within an organization. Common ERP software modules include product planning, parts purchasing, inventory control, product distribution, order tracking, finance, accounting and human resources aspects of an organization.
- **Business Processes** – business processes within an organization falls into three levels – strategic planning, management control and operational control. ERP has been promoted as solutions for supporting or streamlining business processes at all levels. Much of ERP success, however, has been limited to the integration of various functional departments.
- **ERP Users** – the users of ERP systems are employees of the organization at all levels, from workers, supervisors, mid-level managers to executives.
- **Hardware and Operating Systems** – many large ERP systems are UNIX based. Windows NT and Linux are other popular operating systems to run ERP software. Legacy ERP systems may use other operating systems.

The Boundary of an ERP System – the boundary of an ERP system is usually smaller than the boundary of the organization that implements the ERP system. In contrast, the boundary of supply chain systems and e-commerce systems extends to the organization's suppliers, distributors, partners and customers. In practice, however, many ERP implementations involve the integration of ERP with external information systems.

ERP Software

ERP software applications are module-based. Each software module automates business processes within a functional department. ERP applications can be implemented and deployed module-by-module. Major ERP software modules cover the major functional areas of organizations. Common ERP modules include product planning module, parts and material purchasing module, inventory control module, product distribution module, order tracking module, finance module, accounting module, marketing module, and HR module. Organizations often selectively implement the ERP modules that match their business needs.

ERP Production Planning Module

In the process of evolution of manufacturing requirements planning (MRP) into ERP, while vendors have developed more robust software for production planning, consulting firms have accumulated vast knowledge of implementing production planning module. Production planning optimizes the utilization of manufacturing capacity, parts, components and material resources using historical production data and sales forecasting.

ERP Purchasing Module

Purchasing module streamlines procurement of required raw materials. It automates the processes of identifying potential suppliers, negotiating price, awarding purchase order to the supplier, and billing processes. Purchase module is tightly integrated with the inventory control and production planning modules. Purchasing module is often integrated with supply chain management software.

ERP Inventory Control Module

Inventory module facilitates processes of maintaining the appropriate level of stock in a warehouse. The activities of inventory control involves in identifying inventory requirements, setting targets, providing replenishment techniques and options, monitoring item usages, reconciling the inventory balances, and reporting inventory status. Integration of inventory control module with sales, purchase, finance modules allows ERP systems to generate vigilant executive level reports.

ERP Sales Module

Revenues from sales are live blood for commercial organizations. Sales module implements functions of order placement, order scheduling, shipping and invoicing. Sales module is closely integrated with organizations' ecommerce websites. Many ERP vendors offer online storefront as part of the sales module.

ERP Marketing Module

ERP marketing module supports lead generation, direct mailing campaign and more.

ERP Financial Module

Both for-profit organizations and non-profit organizations benefit from the implementation of ERP financial module. The financial module is the core of many ERP software systems. It can gather financial data from various functional departments, and generates valuable financial reports such balance sheet, general ledger, trail balance, and quarterly financial statements.

ERP HR Module

HR (Human Resources) is another widely implemented ERP module. HR module streamlines the management of human resources and human capitals. HR modules routinely maintain a complete employee database including contact information, salary details, attendance, performance evaluation and promotion of all employees. Advanced HR module is integrated with knowledge management systems to optimally utilize the expertise of all employees.

5.2. Balance Score Card

The Balanced Score Card is a strategic planning and management system that is used extensively in business and industry, government, and nonprofit organizations worldwide to align business activities to the vision and strategy of the organization, improve internal and external communications, and monitor organization performance against strategic goals. It was originated by Drs. Robert

Kaplan (Harvard Business School) and David Norton as a performance measurement framework that added strategic non-financial performance measures to traditional financial metrics to give managers and executives a more 'balanced' view of organizational performance.

The balanced scorecard suggests that we view the organization from four perspectives, and to develop metrics, collect data and analyze it relative to each of the following perspectives:

The Learning & Growth Perspective

This perspective includes employee training and corporate cultural attitudes related to both individual and corporate self-improvement. In a knowledge-worker organization, people – the only repository of knowledge – are the main resource. In the current climate of rapid technological change, it is becoming necessary for knowledge workers to be in a continuous learning mode. Metrics can be put into place to guide managers in focusing training funds where they can help the most. In any case, learning and growth constitute the essential foundation for success of any knowledge-worker organization.

The Business Process Perspective

This perspective refers to internal business processes. Metrics based on this perspective allow the managers to know how well their business is running, and whether its products and services conform to customer requirements (the mission). These metrics have to be carefully designed by those who know these processes most intimately; with our unique missions these are not something that can be developed by outside consultants.

The Customer Perspective

Recent management philosophy has shown an increasing realization of the importance of customer focus and customer satisfaction in any business. These are leading indicators: if customers are not satisfied, they will eventually find other suppliers that will meet their needs. Poor performance from this perspective is thus a leading indicator of future decline, even though the current financial picture may look good.

In developing metrics for satisfaction, customers should be analyzed in terms of kinds of customers and the kinds of processes for which we are providing a product or service to those customer groups.

The Financial Perspective

Kaplan and Norton do not disregard the traditional need for financial data. Timely and accurate funding data will always be a priority, and managers will do whatever necessary to provide it. In fact, often there is more than enough handling and processing of financial data. With the implementation of a corporate database, it is hoped that more of the processing can be centralized and automated. But the point is that the current emphasis on financials leads to the "unbalanced" situation with regard to other perspectives. There is perhaps a need to include additional financial-related data, such as risk assessment and cost-benefit data, in this category.

Strategy Mapping

Strategy maps are communication tools used to tell a story of how value is created for the organization. They show a logical, step-by-step connection between strategic objectives (shown as ovals on the map) in the form of a cause-and-effect chain. Generally speaking, improving performance in the objectives found in the Learning & Growth perspective (the bottom row) enables the organization to improve its Internal Process perspective Objectives (the next row up), which in turn enables the organization to create desirable results in the Customer and Financial perspectives (the top two rows).

Balanced Scorecard Software

The balanced scorecard is not a piece of software. Unfortunately, many people believe that implementing software amounts to implementing a balanced scorecard. Once a scorecard has been developed and implemented, however, performance management software can be used to get the right performance information to the right people at the right time.

5.3. Key Performance Indicators

Key Performance Indicators or KPIs are performance measures that indicate progress toward a desirable outcome. Strategic KPIs monitor the implementation and effectiveness strategies of an organization, determine the gap between actual and targeted performance and determine organization effectiveness and operational efficiency.

Key Performance Indicators (KPIs) have become the standard term that organisations use to define goals and objectives that ensure employees are achieving. Analysts describe KPIs as the business metrics that drive a business forward. But what does that mean to individuals and how do you know if you are on target?

When starting a new job, it is vital to get your KPIs down on paper, especially if the success of your probation period is dependant on achieving them.

Many of you will know where you want to be in one, two, five or more years. You may want to move into management, become the head of department or set up your own business, for example. And you may already have a plan in place to help you achieve your goal so that you know what you need to do and how to get there.

A business will also have short, mid and long-term objectives and will put measures, or KPIs, in place to achieve these goals. Therefore, as part of the company, the measures that you are given as an employee are designed to reflect the organisation's overall goals, to help them get to where they want to go.

To make them effective, each KPIs should be SMART:

Specific – a well defined goal that is clearly understood by everyone.

Measurable – can you track your progress towards the goal?

Agreed – both employer and employee must agree on what the goals are.

Realistic – can you achieve the goal with the resources provided?

Time related - will there be enough time to complete the task?

Topic 6. Strategy Analysis & Choice

6.1. Strategy-formulation analytical framework
6.2. BCG and GE/McKinsey matrix

6.1. Strategy-formulation analytical framework

The SWOT is the most basic form of strategic analysis. SWOT stands for Strengths, Weaknesses, Opportunities, and Threats. Simply list the organisation's Strengths, Weaknesses, Opportunities and Threats.

A SWOT analysis is conventionally represented as a 2×2 matrix with the Strengths listed in the top left quadrant, Weaknesses in the top right, Opportunities in the bottom left, and Threats in the bottom right quadrant. There is a logic to that presentation (which we'll come to next) but at the end of the day it boils down to 4 simple lists, and presentation is probably a matter of taste.

The Strengths and Weaknesses represent the internal dimension of the business unit under consideration. These cover factors which are or should be under management's control. A McKinsey 7-S analysis is a good way of making sure you've covered all your bases.

The Opportunities and Threats represent external environment of the business unit. These cover factors which are typically not under management's control.

SPACE matrix

The **SPACE matrix** is a management tool used to analyze a company. It is used to determine what type of a strategy the company should undertake.

The **Strategic Position & Action Evaluation matrix** or short a *SPACE matrix* is a strategic management tool that focuses on strategy formulation especially as related to the competitive position of an organization.

The *SPACE matrix* can be used as a basis for other analyses, such as the SWOT analysis, BCG matrix model, industry analysis, or assessing strategic alternatives.

SPACE matrix strategic management method

To explain how the SPACE matrix works, it is best to reverse-engineer it. First, let us take a look at what the outcome of a SPACE matrix analysis can be, take a look at the picture below. The SPACE matrix is broken down to four quadrants where each quadrant suggests a different type or nature of a strategy:

- Aggressive
- Conservative
- Defensive
- Competitive

This is what a completed SPACE matrix looks like:

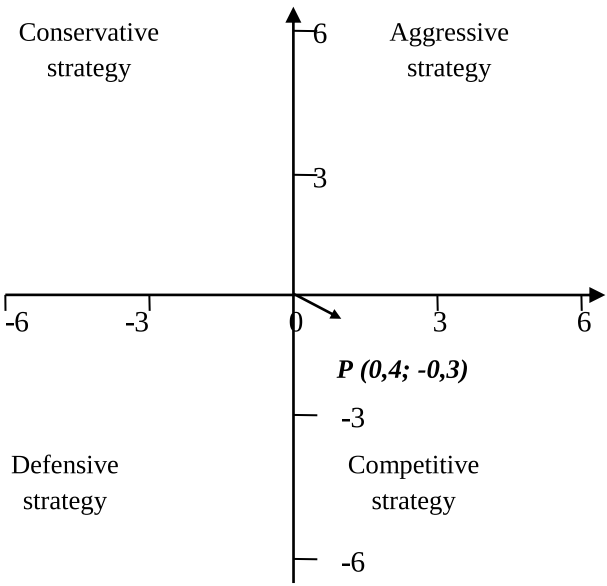

Fig. 6.1 – SPACE matrix

This particular SPACE matrix tells us that our company should pursue an *aggressive strategy*. Our company has a strong competitive position in the market with rapid growth. It needs to use its internal strengths to develop a market penetration and market development strategy. This can include product development, integration with other companies, acquisition of competitors, and so on.

6.2. BCG and GE/McKinsey matrix

The BCG Matrix can be applied to any business with more than one product or service line, or more than one customer segment. In simple terms, it involves plotting the market share against the market growth rate for each product, service or customer segment, and then basing strategic decisions on their relative position on the chart.

The BCG Matrix

The BCG (named after the Boston Consulting Group) Matrix, is a strategy analysis tool which helps to understand the different strategic contexts of different parts of a business portfolio. That is, it recognises that not all parts of the business are strategically equal, and so helps to facilitate more nuance strategic analysis.

In its simplest form, the BCG matrix charts each source of value by its share of its market and the rate at which that market is growing. Source of value could be business units, products, services, customer segments or channels (that is you would choose one of these criteria, say product, and then chart all of the organisation's products relative to each other).

The resultant portfolio analysis can then be roughly divided into 4 quadrants. Each of the four quadrants suggests a different strategic approach. *For example*: Stars – continue to invest; Cash Cows – improve efficiencies; Question Marks – decide; Dogs – exit.

For example, Cash Cows may more readily lend themselves to "Competitive" strategic thinking (e. g. Porter's 5 Forces Analysis), while Stars may lend themselves to more "Blue Ocean" strategic thinking (e. g. The Strategy Canvas). You can read more at Blue Ocean vs. 5 Forces for further insight into this subject.

In addition, one could vary the size with which you plot each source of value to represent, say, profitability.

Critical success factors:

- How you define the scope of each market (for measuring market share and growth) is key to the placement of each source of value.
- Don't ignore cross synergies, for example, taking into consideration sources of value which may serve as loss leaders.
- Don't ignore cyclical effects.
- When considering the allocation of costs across sources of value, remember that all costs are variable in the long term. That is, don't think that you need to keep an unprofitable product, channel etc. going just because it is absorbing some of your "fixed" costs.

GE/McKinsey Matrix

In consulting engagements with General Electric in the 1970's, McKinsey & Company developed a nine-cell portfolio matrix as a tool for screening GE's large portfolio of strategic business units (SBU). This business screen became known as the **GE/McKinsey Matrix** and is shown below:

The GE / McKinsey matrix is similar to the BCG growth-share matrix in that it maps strategic business units on a grid of the industry and the SBU's position in the industry. The GE matrix, however, attempts to improve upon the BCG matrix in the following two ways:

- the GE matrix generalizes the axes as "Industry Attractiveness" and "Business Unit Strength" whereas the BCG matrix uses the market growth rate as a proxy for industry attractiveness and relative market share as a proxy for the strength of the business unit;
- the GE matrix has nine cells vs. four cells in the BCG matrix.

GE/McKinsey Matrix

		Business Unit Strength		
		High	**Medium**	**Low**
	High			
	Medium			
	Low			

Figure 6.2 – GE/McKinsey Matrix

Industry attractiveness and business unit strength are calculated by first identifying criteria for each, determining the value of each parameter in the criteria, and multiplying that value by a weighting factor. The result is a quantitative measure of industry attractiveness and relative performance of the business unit in that industry.

Industry Attractiveness

The vertical axis of the GE/McKinsey matrix is industry attractiveness, which is determined by factors such as the following:

- market growth rate;
- market size;
- demand variability;
- industry profitability;
- industry rivalry;
- global opportunities;
- macro-environmental factors (PEST).

Topic 7. Corporate Level Strategies

7.1. Definition of corporate strategy
7.2. Types of basic corporate strategies

7.1. Definition of corporate strategy

A convenient way to classify levels of strategy is to view corporate level strategy as responsible for market definition, business level strategy as responsible for market navigation, and functional level strategy as the foundation that supports both of these.

Corporate level strategies address the entire strategic scope of the enterprise. This is the “big picture” view of the organization and includes deciding in which product or service markets to compete and in which geographic regions to operate. For multi-business firms, the resource allocation process – how cash, staffing, equipment and other resources are distributed – is typically established at the corporate level. In addition, because market definition is the domain of corporate level strategists, the responsibility for diversification, or the addition of new products or services to the existing product/service line-up, also falls within the realm of corporate-level strategy. Similarly, whether to compete directly with other firms or to selectively establish cooperative relationships – strategic alliances – falls within the purview corporate-level strategy, while requiring ongoing input from business-level managers

7.2. Types of basic corporate strategies

Critical questions answered by corporate-level strategists thus include:

1. What should be the scope of operations (i. e. what businesses should the firm be in?)
2. How should the firm allocate its resources among existing businesses?

3. What level of diversification should the firm pursue (i. e., which businesses represent the company’s future? Are there additional businesses the firm should enter or are there businesses that should be targeted for termination or divestment?
4. How diversified should the corporation’s business be? Should we pursue related diversification (i. e., similar products and service markets), or unrelated diversification (i. e., dissimilar product and service markets) a more suitable approach given current and projected industry conditions? If we pursue related diversification, how will the firm leverage potential cross-business synergies? In other words, how will adding new product or service businesses benefit the existing product/service line-up?
5. How should the firm be structured? Where should the boundaries of the firm be drawn and how will these boundaries affect relationships across businesses, with suppliers, customers and other constituents? Should the firm enter into strategic alliances – cooperative, mutually-beneficial relationships with other firms? If so, for what reasons? If not, what impact might this have on future profitability?

Corporate Grand Strategies

As the previous discussion implies, corporate-level strategists have a tremendous amount of both latitude and responsibility. The myriad decisions required of these managers can be overwhelming considering the potential consequences of incorrect decisions. One way to deal with this complexity is through categorization; one categorization scheme is to classify corporate-level strategy decisions into three different types, or grand strategies. These grand strategies involve:

- efforts to expand business operations (growth strategies);
- decrease the scope of business operations (retrenchment strategies);
- maintain the status quo (stability strategies).

Growth Strategies

Growth strategies are designed to expand an organization's performance, usually as measured by sales, profits, product mix, etc. Typical growth strategies involve one or more of the following:

1. With a concentration strategy the firm attempts to achieve greater market penetration by becoming highly efficient at servicing its market with a limited product line (e. g., McDonald's in fast foods).
2. By using a vertical integration strategy, the firm attempts to expand the scope of its current operations by undertaking business activities earlier performed by one of its suppliers (backward integration) or by undertaking business activities performed by a business in its channel of distribution (forward integration).
3. A diversification strategy entails moving into different markets or adding different products to its mix. If the products or markets are related to existing product or service offerings, the strategy is called concentric diversification. If expansion is into products or services unrelated to the firm's existing business, the diversification is called conglomerate diversification.

Stability Strategies

When firms are satisfied with their current rate of growth and profits, they may decide to use a stability strategy. This strategy is essentially a continuation of existing strategies. Such strategies are typically found in industries having relatively stable environments. The firm is often making a comfortable income operating a business and see no need to make the psychological and financial investment that would be required to undertake a growth strategy.

Retrenchment Strategies

Retrenchment strategies involve a reduction in the scope of the corporation's activities, which also generally necessitates a reduction in number of employees, sale of assets associated with discontinued product or service lines, possible restructuring of debt through bankruptcy proceedings, and in the most extreme cases, liquidation of the firm.

Firms pursue a turnaround strategy by undertaking a temporary reduction in operations in an effort to make the business stronger and more viable in the future. These moves are popularly called downsizing or rightsizing. The hope is that going through a temporary belt-tightening will allow the firm to pursue a growth strategy at some future point.

A divestment decision occurs when a firm elects to sell one or more of the businesses in its corporate portfolio. Typically, a poorly performing unit is sold to another company and the money is reinvested in another business within the portfolio that has greater potential.

Bankruptcy involves legal protection against creditors or others allowing the firm to restructure its debt obligations or other payments, typically in a way that temporarily increases cash flow. Such restructuring allows the firm time to attempt a turnaround strategy. For example, since the airline hijackings and the subsequent tragic events of September 11, 2001, many of the airlines based in the U.S. have filed for bankruptcy to avoid liquidation as a result of stymied demand for air travel and rising fuel prices. At least one airline has asked the courts to allow it to permanently suspend payments to its employee pension plan to free up positive cash flow.

Liquidation is the most extreme form of retrenchment. Liquidation involves the selling or closing of the entire operation. There is no future for the firm; employees are released, buildings and equipment are sold, and customers no longer have access to the product or service. This is a strategy of last resort and one that most managers work hard to avoid.

Topic 8. Business Level Strategies

8.1. Definition of business level strategies
8.2. Analysis of business level strategies

8.1. Definition of business level strategies

Business level strategies are similar to corporate strategies as they focus on overall performance. In contrast to corporate level strategy, however, they focus on only one rather than a portfolio of businesses. Business units represent individual entities oriented toward a particular industry, product, or market. In large multi-product or multi-industry organizations, individual business units may be combined to form strategic business units (SBUs). An SBU represents a group of related business divisions, each responsible to corporate head-quarters for its own profits and losses. Each strategic business unit will likely have its own competitors and its own unique strategy. A common focus of business level strategies are sometimes on a particular product or service line and business-level strategies commonly involve decisions regarding individual products within this product or service line. There are also strategies regarding relationships between products. One product may contribute to corporate level strategy by generating a large positive cash flow for new product development, while another product uses the cash to increase sales and expand market share of existing businesses. Given this potential for business level strategies to impact other business level strategies, business level managers must provide ongoing, intensive information to corporate level managers. Without such crucial information, corporate level managers are prevented from best managing overall organizational direction. Business level strategies are thus primarily concerned with:

1. Coordinating and integrating unit activities so they conform to organizational strategies (achieving synergy).
2. Developing distinctive competencies and competitive advantage in each unit.

3. Identifying product or service-market niches and developing strategies for competing in each.
4. Monitoring product or service markets so that strategies conform to the needs of the markets at the current stage of evolution.

In a single-product company, corporate-level and business-level strategies are the same. For example, a furniture manufacturer producing only one line of furniture has its corporate strategy chosen by its market definition, wholesale furniture, but its business is still the same, wholesale furniture. Thus, in single-business organizations, corporate and business level strategies overlap to the point that they should be treated as one united strategy. The product made by a unit of a diversified company would face many of the same challenges and opportunities faced by a one-product company. However, for most organizations, business unit strategies are designed to support corporate strategies. Business level strategies look at the product's life cycle, competitive environment, and competitive advantage much like corporate level strategies, except the focus for business-level strategies is on the product or service, not on the corporate portfolio.

8.2.Analysis of business-level strategies

Porter’s Generic Strategies

Harvard Business School Professor Michael Porter developed a framework of generic strategies that can be applied to strategies for various products and services, or the individual business-level strategies within a corporate portfolio. The strategies are (1) overall cost leadership, (2) differentiation, and (3) focus on a particular market niche. The generic strategies provide direction for business units in designing incentive systems, control procedures, operations, and interactions with suppliers and buyers, and with making other product decisions.

Cost-leadership strategies require firms to develop policies aimed at becoming and remaining the lowest cost producer and/or distributor in the industry. Note here that the focus is on cost leadership, not price leadership. This may at first appear to be only a semantic difference, but consider how this fine-grained definition places emphases on controlling costs while giving firms alternatives when it comes to pricing (thus ultimately influencing total revenues). A firm with a cost advantage may price at or near competitors prices, but with a lower cost of production and sales, more of the price contributes to the firm's gross profit margin. A second alternative is to price lower than competitors and accept slimmer gross profit margins, with the goal of gaining market share and thus increasing sales volume to offset the decrease in gross margin. Such strategies concentrate on construction of efficient-scale facilities, tight cost and overhead control, avoidance of marginal customer accounts that cost more to maintain than they offer in profits, minimization of operating expenses, reduction of input costs, tight control of labour costs, and lower distribution costs. The low-cost leader gains competitive advantage by getting its costs of production or distribution lower than the costs of the other firms in its relevant market. This strategy is especially important for firms selling unbranded products viewed as commodities, such as beef or steel.

Cost leadership provides firms above-average returns even with strong competitive pressures. Lower costs allow the firm to earn profits after competitors have reduced their profit margin to zero. Low-cost production further limits pressures from customers to lower price, as the customers are unable to purchase cheaper from a competitor. Cost leadership may be attained via a number of techniques. Products can be designed to simplify manufacturing. A large market share combined with concentrating selling efforts on large customers may contribute to reduced costs. Extensive investment in state-of-the-art facilities may also lead to long run cost reductions. Companies that successfully use this strategy tend to be highly centralized in their structure. They place heavy emphasis on quantitative standards and measuring performance toward goal accomplishment.

Firms that succeed in cost leadership often have the following internal strengths:

• access to the capital required to make a significant investment in production assets; this investment represents a barrier to entry that many firms may not overcome;

• skill in designing products for efficient manufacturing, for example, having a small component count to shorten the assembly process;

• high level of expertise in manufacturing process engineering;

• efficient distribution channels.

Efficiencies that allow a firm to be the cost leader also allow it to compete effectively with both existing competitors and potential new entrants. Finally, low costs reduce the likely impact of substitutes. Substitutes are more likely to replace products of the more expensive producers first, before significantly harming sales of the cost leader unless producers of substitutes can simultaneously develop a substitute product or service at a lower cost than competitors. In many instances, the necessity to climb up the experience curve inhibits a new entrants ability to pursue this tactic.

Differentiation strategies require a firm to create something about its product that is perceived as unique within its market. Whether the features are real, or just in the mind of the customer, customers must perceive the product as having desirable features not commonly found in competing products. The customers also must be relatively price-insensitive. Adding product features means that the production or distribution costs of a differentiated product will be somewhat higher than the price of a generic, non-differentiated product. Customers must be willing to pay more than the marginal cost of adding the differentiating feature if a differentiation strategy is to succeed.

Differentiation may be attained through many features that make the product or service appear unique. Possible strategies for achieving differentiation may include warranty (Sears tools have lifetime guarantee against breakage), brand image (Coach handbags, Tommy Hilfiger sportswear), technology (Hewlett–Packard laser printers), features (Jenn-Air ranges, Whirlpool appliances), service (Makita hand tools), and dealer network (Caterpillar construction equipment), among other dimensions. Differentiation does not allow a firm to ignore costs; it makes products of a firm less susceptible to cost pressures from competitors because customers see the product as unique and are willing to pay extra to have the product with the desirable features.

Differentiation often forces a firm to accept higher costs in order to make a product or service appear unique. The uniqueness can be achieved through real product features or advertising that causes the customer to perceive that the product is unique. Whether the difference is achieved through adding more vegetables to the soup or effective advertising, costs for the differentiated product will be higher than for non-differentiated products. Thus, firms must remain sensitive to cost differences. They must carefully monitor the incremental costs of differentiating their product and make certain the difference is reflected in the price.

Focus, the third generic strategy, involves concentrating on a particular customer, product line, geographical area, channel of distribution, stage in the production process, or market niche. The underlying premise of the focus strategy is that the firm is better able to serve its limited segment than competitors serving a broader range of customers. Firms using a focus strategy simply apply a cost-leader or differentiation strategy to a segment of the larger market. Firms may thus be able to differentiate themselves based on meeting customer needs through differentiation or through low costs and competitive pricing for specialty goods.

Topic 9. Functional Level Strategies

9.1. Definition of functional level strategies
9.2. Types of functional level strategies

9.1. Functional level strategy

This strategy relates to single functional operation and the activities involved therein. This level is at the operating end of the organization. The decisions at this level within the organization are different functions of the enterprise like marketing, finance, manufacturing, etc. contribute to the strategy of other levels. Functional strategy deals with a relatively restricted plan providing objectives for specific function, allocation of resources among different operations within the functional area and coordination between them for achievement of strategic business unit (SBU) and corporate level objectives. Sometimes a fourth level of strategy also exists. This level is known as the operating level. It comes below the functional level strategy and involves actions relating to various subfunctions of the major function. For example, the functional level strategy of marketing function is divided into operating levels such as marketing research, sales promotion, etc.

Functional level strategies are concerned with coordinating the functional areas of the organization (marketing, finance, human resources, production, research and development, etc.) so that each functional area upholds and contributes to individual business level strategies and the overall corporate level strategy. This involves coordinating the various functions and operations needed to design, manufacture, deliver, and support the product or service of each business within the corporate portfolio. Functional strategies are primarily concerned with:

- efficient utilizing specialists within the functional area;
- integrating activities within the functional area (e. g., coordinating advertising, promotion, and marketing research

in marketing; or purchasing, inventory control, and shipping in production/operations);

- assuring that functional strategies mesh with business level strategies and the overall corporate level strategy.

Functional strategies are frequently concerned with appropriate timing. For example, advertising for a new product could be expected to begin sixty days prior to shipment of the first product. Production could then start thirty days before shipping begins. Raw materials, for instance, may require that orders are placed at least two weeks before production is to start. Thus, functional strategies have a shorter time orientation than either business level or corporate level strategies. It is also easier to establish accountability with functional strategies because results of actions occur sooner and are easier attributed to the function than is possible at other levels of strategy. Lower level managers are most directly involved with the implementation of functional strategies.

Strategies for an organization may be categorized by the level of the organization addressed by the strategy. Corporate level strategies involve top management and address issues of concern to the entire organization. Business level strategies deal with major business units or divisions of the corporate portfolio. Business level strategies are generally developed by upper and middle-level managers and are intended to help the organization achieve its corporate strategies. Functional strategies address problems commonly faced by lower level managers and deal with strategies for the major organizational functions (e. g., marketing, finance, production) considered relevant for achieving the business strategies and supporting the corporate level strategy. Market definition is thus the domain of corporate level strategy, market navigation the domain of business level strategy, and support of business and corporate level strategy by individual, but integrated, functional level strategies.

9.2. Types of functional strategies

Marketing strategy is the fundamental goal of increasing sales and achieving a sustainable competitive advantage. Marketing strategy includes all basic, short-term, and long-term activities in the field of marketing that deal with the analysis of the strategic initial situation of a company and the formulation, evaluation and selection of market-oriented strategies and therefore contribute to the goals of the company and its marketing objectives.

Marketing strategies may differ depending on the unique situation of the individual business. However, there is a number of ways of categorizing some generic strategies. A brief description of the most common categorizing schemes is presented below:

Strategies based on market dominance. In this scheme, firms based on their market share or dominance of an industry are classified. Typically there are four types of market dominance strategies: leader; challenger; follower; nicher.

Here is a framework for marketing strategies.

- Market introduction strategies

"At introduction, the marketing strategist has two principle strategies to choose from: penetration or niche."

- Market growth strategies

"In the early growth stage, the marketing manager may choose from two additional strategic alternatives: segment expansion or brand expansion."

- Market maturity strategies

"In maturity, sales growth slows, stabilizes and starts to decline. In early maturity, it is common to employ a maintenance strategy (BCG), where the firm maintains or holds a stable marketing mix."

- Market decline strategies

At some point the decline in sales approaches and then begins to exceed costs. And not just accounting costs, there are hidden costs as well; as Kotler observed: 'No financial accounting can adequately convey all the hidden costs.' At some point, with declining sales and rising costs, a harvesting strategy becomes unprofitable and a divesting strategy necessary”.

Marketing strategy deals with pricing, selling and distributing a product.

There are several types of Marketing Strategy: Market & Product Development, Push & Pull Strategy, Distribution System. Pricing.

Market development

1) capturing a larger share of an existing market for current products through market saturation and market penetration;

2) developing new uses and/or markets for current products.

Consumer product giants such as P&G, Colgate Palmolive, and Unilever are experts at using advertising and promotion to implement a market saturation/penetration strategy to gain the dominant market share in a product category. As seeming masters of the product life cycle, these companies are able to extend product life cycle almost indefinitely through “new and improved” variations of product and packaging that appeal to most market niches.

Product Development

1) develop new products for existing markets;

2) develop new products for new markets: use of brand baking soda, sodium toothpaste, deodorant, and detergent.

Using a successful brand name to market other products is called brand extension, and it is a good way to appeal to a company’s current customers.

Push Strategy: Product is created 1st and later is created on need.

Pull Strategy: Need is created 1st and later is created on product because of that product.

Research has found that a high level of advertising (a key part of a pull strategy) is beneficial to leading brands in a market. Strong brands provide a competitive advantage to a firm because they act as entry barriers and usually generate high market share.

Distribution System. Should a company use distributors and dealers to sell its products, or should it sell directly to mass merchandisers?

Pricing. Marketers develop an overall pricing strategy that is consistent with the organization's mission and values. This pricing strategy typically becomes part of the company's overall long-term strategic plan.

Financial Strategy

A financial strategy is a written down plan or guideline that deals with key elements in raising funds, managing organization funds and the implementation of the organization objectives within the limited financial capabilities. Financial strategies are very important for the survival of any institution, because without good financial strategies, organizations will run bankrupt and can be closed down.

Financial strategy examines the financial implications of corporate and business level strategic options and identifies the best financial course of action. It can also provide competitive advantage through a lower cost of funds and a flexible ability to raise capital to support a business strategy. Financial strategy usually attempts to maximize the financial value of a firm.

Why Need a Financial Strategy

Financial sustainability is part of organizational sustainability. It has to do with the ongoing ability of the organization to generate enough resources to work towards its vision.

To be financially sustainable, an organization must:

- have more than one source of income;
- have more than one way of generating income;
- do strategic, action and financial planning regularly;
- have adequate financial systems;
- have a good public image;
- be clear about its values (value clarity);
- have financial autonomy.

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