CIMA E3 Course Notes

Chapter 1

Formulating a business strategy

1. Business strategy

Strategy

A strategy is a plan of action designed to achieve a goal or objective. The aim of a strategy is to gain some kind of competitive advantage or to help to exploit future opportunities.

A strategic plan tends to be an overall guide to the way forward rather than a detailed step by step approach due to the tendency of the real world to be uncertain. In the example of a chess game, a 'strategy' provides the over-riding approach that the player will take to win the game, but the exact set of moves they undertake will vary depending on the opponent's moves.

Strategy in business

Applying this to a business scenario, according to the CIMA official terminology a business strategy can be defined as:

"A course of action, including the specification of resources required, to achieve a specific objective"

Or, more complete definition is given by Johnson, Scholes and Whittington as:

"The direction and scope of an organisation over the long term, which achieves advantage for the organisation through its configuration of resources within a changing environment, to meet the needs of the markets and to fulfil stakeholder expectations"

Business strategy therefore is concerned with the overall management of an organisation and includes the management of and taking decisions about:

a) Products

b) Markets

c) Locations (production and sales)

d) Structure

e) Personnel

f) Buildings and machinery

g) How to compete

Key features of strategic management

The key features of strategic management are:

Long term approach – decisions are made over the long term, often for periods exceeding one year

Focused on organisational objectives – the aim being to ensure that the plan of action achieves the most important objectives for a wide group of key stakeholders

Aligned with internal strengths and weaknesses – the aim should be to capitalise on the business strengths and overcome any key weaknesses. Devising a strategy will often follow a position audit of the business to ascertain the businesses current position.

Adapted to the changing business environment – so that changes in political, economic, social and technology factors are taken account of, while adapting to industry changes, such as competitive threats, supply issues or changing customer needs.

The importance of strategy

Strategic management of businesses is important for the following reasons:

- Provides a clear direction, focusing management decision making
- Adapts the organisation to the changing environment ensuring it's continuing survival and success
- Ensures competitiveness through understanding and adapting to competition
- Focuses in building key competences to meet customer needs
- Co-ordinates all elements of the business in a structured planned approach.

Director's role in strategy

Ultimately it is the director's responsibility to decide on and take decisions on strategy in the organisation. Typically strategy will be discussed and agreed in board meetings. Larger organisations often have a small department whose role is to analyse the business, markets and competitors and devise strategy for the board to discuss and agree upon.

The directors have a **fiduciary duty** to make strategic decisions which are in the best interests of the company and its shareholders, and as such it is important that **due diligence** undertaken before key contracts resulting from strategic decisions are signed. This might include an analysis of key suppliers prior to long term supply agreements or review of an acquisition target by an independent accountancy firm prior to purchase.

2. Levels of Strategy

There are three different levels on which strategy can be set:

Corporate Strategy

The corporate strategy provides the direction for the business as whole, including all parts of the business. It includes consideration of:

- The overriding purpose and scope of the business
- Which businesses and markets should the organisation operate in?
- What should the core competencies be?
- Resources and financing
- How to compete
- How to integrate and structure the business

For a company such as Diagio, one of the world's leading premium drinks businesses with brands such as Guiness, Smirnov and Johnie Walker amougst it's group. It needs to decide which products to include in it's brands, which markets to operate in and so on. In 2002 Diagio sold Burger King as they moved out of the 'food' industry into a focus on Premium Branded Drinks. This was a 'corporate level decision'.

Business Strategy

Each business unit or subsidiary of the business is likely to have different goals, competitors, suppliers, manufacturing approaches, IT, financial requirements and so on, and so each strategic business unit (SBU) needs its own strategy. This covers:

- Which competencies?
- Which products?
- Which markets?
- Tactics to beat competition in this market
- Business resources (people, buildings, machinery, processes)
- How to compete in this business area?

In Diagio, different strategies will be required for each drinks brand and each regional market due to the different nature of the products and markets. These are 'business level' strategies.

Operational/Functional Strategy

Each functional area within each business unit will then have its own strategy, so there will be strategies in each department e.g. HR, IT, production, finance and marketing.

These should be designed to be consistent with the business strategy of the SBU.

3. Approaches of Strategy Formulation

There are a number of different approaches to the development of strategies within organisations.

- Planned strategies
- Emergent strategies
- Incrementalism
- Opportunism

These will be examined one by one in the following sections.

4. Planned Strategies

Strategies can be consciously and formally planned in advance, either by the directors or by a specialist department. This provides a clear, justifiable strategy based on the information available about the company's current position, environment and competencies. As such the strategy developed should be well thought through and effective.

Planned strategies are often used in large organisations, and are particularly suitable where the industry is subject to relatively little change.

Planned strategies tend to consist of **four of distinct stages**:

Strategic Analysis

- Defining the direction (e.g. Mission and objectives)
- External analysis of the business environment (e.g. PESTEL analysis, Porter's 5 forces)
- Internal analysis of the firm (e.g. Value chain, Resource audit, Product analysis)

- Corporate appraisal (e.g. SWOT analysis)

Strategic Choice

- Selecting strategic options
- Choosing options the firm is going to take (including financial evaluation using techniques such as NPV, IRR and Payback period).

Strategic Implementation

Putting the strategies into practice including polices and strategies for:

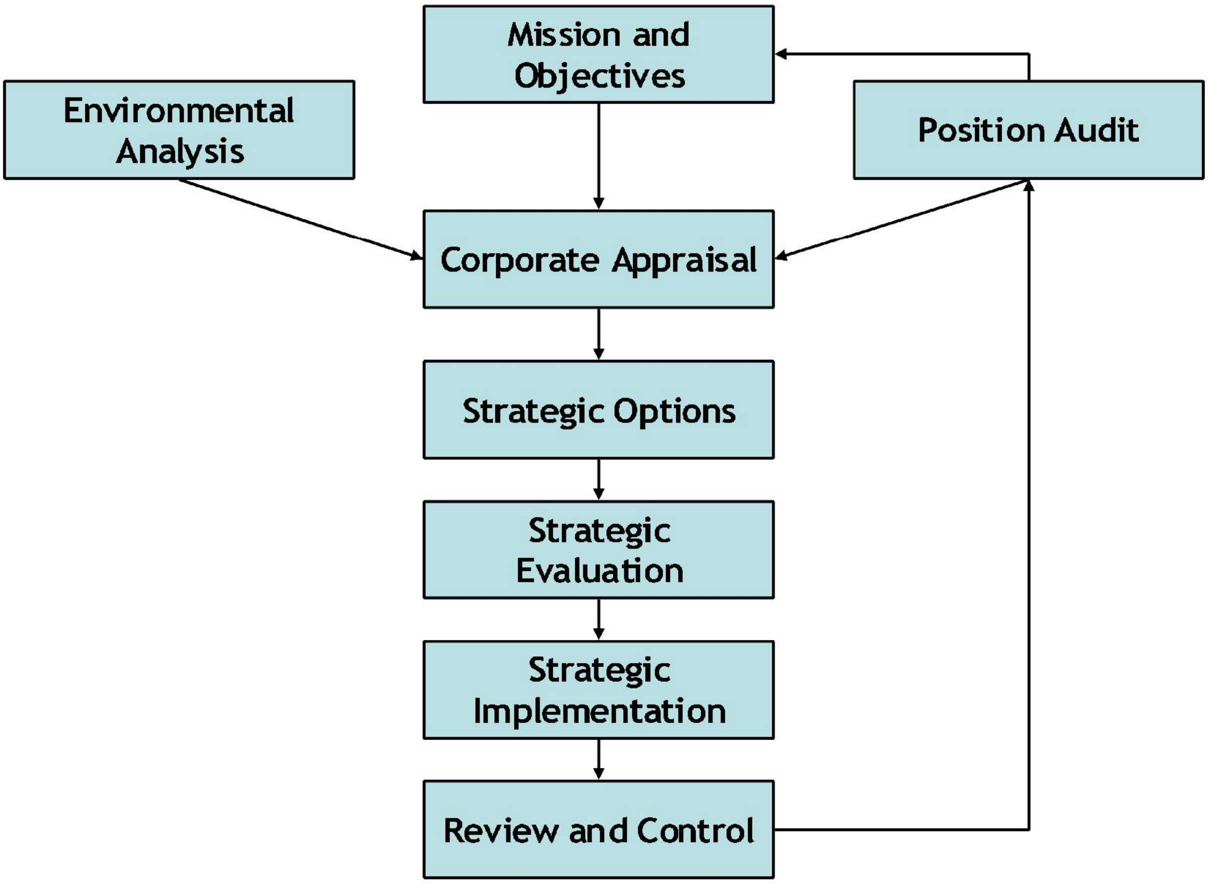
- marketing
- finance
- R & D
- IT
- Human Resources
- Project management
- Change management
- Structure

Strategy Evaluation and control

- Evaluating the success of the strategy by measuring actual performance against objectives
- Taking control action by amending future strategies and objectives.

Rational planning model

The stages of strategic planning can also be shown using the rational planning model, which is an alternative way of showing the same process.



Criticisms of planned strategies

While planned strategies provide logical focused, well organised strategies they have also been criticised:

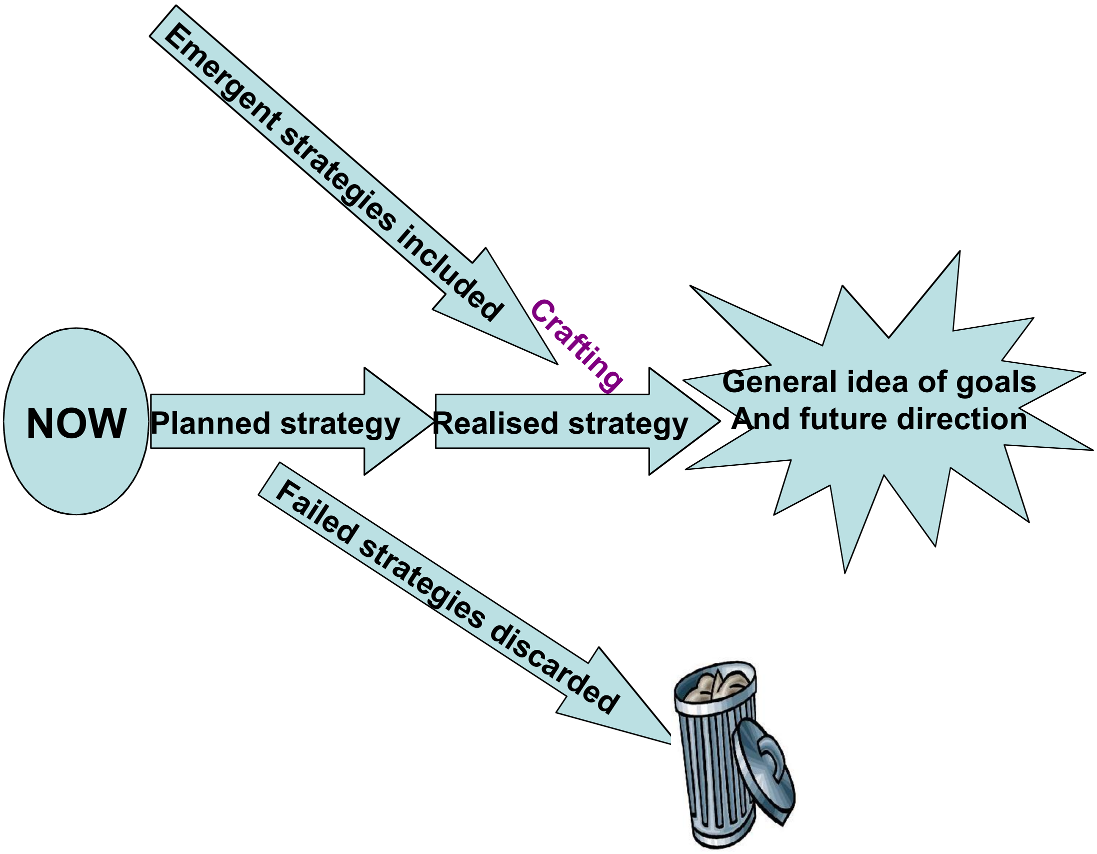
Time commitment – they can be very time consuming to create, for large businesses often taking many months, and may be out of date by the time they are published

Cost – costs include staff time, collecting information, using strategy consultants

Lack of flexibility - The organisation can become constrained by a fixed plan and as a result not take new opportunities that arise or adapt to changes in the business environment (e.g. a new competitive threat).

5. Emergent Strategies (Mintzberg)

Emergent strategies are strategies which emerge out of the course of the business rather than having been formally planned. They could perhaps be due to opportunities which present themselves (e.g. a competitor comes up for sale) or threats which need to be addressed (e.g. a competitor develops a new product and the company must follow suit to remain competitive).



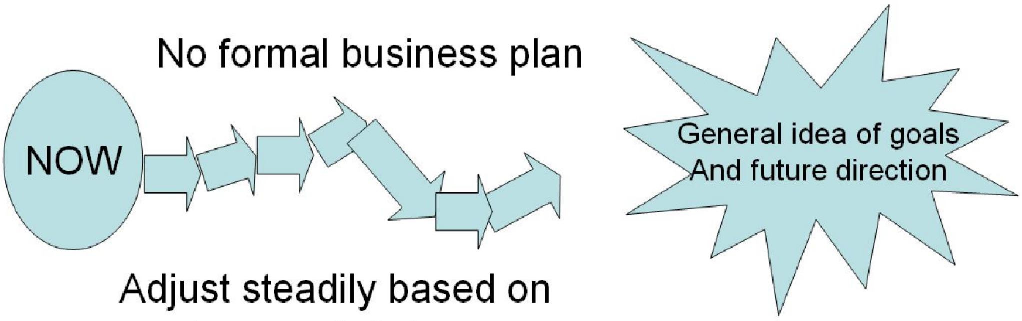
Emergent strategies can be combined with the successful elements of the planned strategy to define the way forward for the business. The process of bringing these together is called **crafting** a strategy.

In the example of a development of a new product, that needs of the new product would need to be **crafted** alongside those of the existing business, including production timings and approaches of both existing and new products, combined marketing strategies, allocation of funds to different product lines and the use of human resources for each area.

This is more appropriate for businesses in a changing environment, such as high technology, where restriction to one planned strategy may be a competitive weakness.

It is also most commonly used in smaller organisations where the organisation relies less of formal plans and processes and more on the knowledge of key managers and staff who can be very flexible to change.

6. Incrementalism



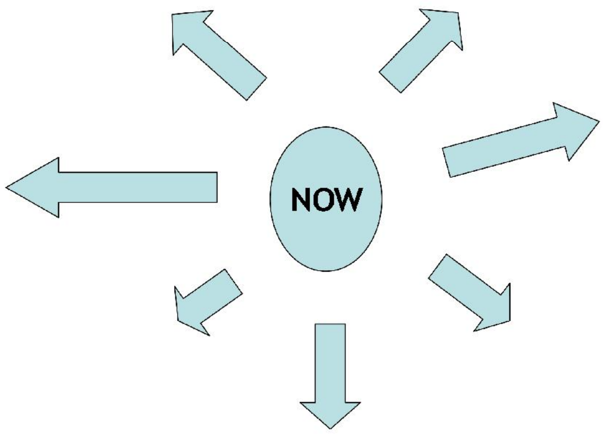
In fast changing environments it may be unrealistic to effectively undertake the full strategic planning process. Instead it is more practical to develop a short term strategy based on the consensus of opinion of major stakeholders.

An incrementalist approach was adopted by many businesses during the ecomonic downturn of the late 2000s as uncertainty made it hard to make accurate long term predictions.

The strategy is then developed regularly using a series of small scale changes as dictated by the changing environment.

Another situation where incrementalism is common in the public sector which while not a rapidly changing environment, is one where there are a wide variety of stakeholder needs to satisfy. It can thus be hard to agree clear long term objectives to keep every stakeholder content, and thus a shorter term 'middle ground' view is taken that 'satisfies' all groups.

7. Freewheeling Opportunism



Take advantage of opportunities as they arise
Little plan or direction, but very flexible and dynamic

In this model there is no formal approach to strategy development.

Directors dictate the business direction through taking whatever opportunities are available at a particular point in time. This allows the business to be very flexible and take opportunities that companies using a more formal approach to strategy development would be slow to take.

Freewheeling opportunism is most common in small companies with an entrepreneurial leader who can direct and focus their organisation down each new track based on the opportunities they identify and wish to pursue. The lack of formal processes makes change quick and easy.

8. The three strategic lenses

According to Johnston, Scholes and Whittington, business strategy can considered from three different perspectives.

Strategy as design

A strategy is planned based on internal and external analysis and logical and rational thought. e.g. Rational model

Strategy as experience

Strategy comes from learning from and adapting to real-world experience e.g. Emergent strategies (and to a lesser extent incrementalism)

Strategy as ideas

Strategy comes from the continuous application of new innovations and business and process change. This depends on staff and structural flexibility, entrepreneurship and idea generation.

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