Corporate Strategy

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Table:2- Basic Features of Corporate Strategies

Strategy	Basic Feature
Stability	The firm stays with its current businesses and product markets; maintains the existing level of effort; and is satisfied with incremental growth.
Expansion	Here, the firm seeks significant growth-maybe within the current businesses; maybe by entering new business that are related to existing businesses; or by entering new businesses that are unrelated to existing businesses.
Retrenchment	The firm retrenches some of the activities in some business (es) or drops the business as such through sell-out or liquidation.
Combination	The firm combines the above strategic alternatives in some permutation/combination so as to suit the specific requirements of the firm.

4.2.1.1. Characteristics of Stability Strategy

- A firm opting for stability strategy stays with the same business, same product-market posture and functions, maintaining same level of effort as at present.
- The endeavour is to enhance functional efficiencies in an incremental way, through better deployment and utilization of resources. The assessment of the firm is that the desired income and profits would be forthcoming through such incremental improvements in functional efficiencies.
- Stability strategy does not involve a redefinition of the business of the corporation.
- It is a safe strategy that maintains status quo.
- It does not warrant much of fresh investments.
- The risk involved in this strategy is less.
- While opting for this strategy, the organization can concentrate on its resources and existing businesses/products and markets, thus leading to building of core competencies.
- The firms with modest growth objective choose this strategy.

4.2.2.1 Characteristics of Growth/Expansion Strategy

- Expansion strategy involves a redefinition of the business of the corporation.
- Expansion strategy is the opposite of stability strategy. While in stability strategy, rewards are limited, in expansion strategy they are very high. In the matter of risks, too, the two are the opposites of each other.
- Expansion strategy leads to business growth. A firm with a mammoth growth ambition can meet its objective only through the expansion strategy.
- The process of renewal of the firm through fresh investments and new businesses/products/markets is facilitated only by expansion strategy.
- Expansion strategy is a highly versatile strategy; it offers several permutations and combinations for growth. A firm opting for the expansion strategy can generate many alternatives within the strategy by altering its propositions regarding products, markets and functions and pick the one that suits it most.
- Expansion strategy holds within its fold two major strategy routes: Intensification Diversification. Both of them are growth strategies; the difference lies in the way in which the firm actually pursues the growth.

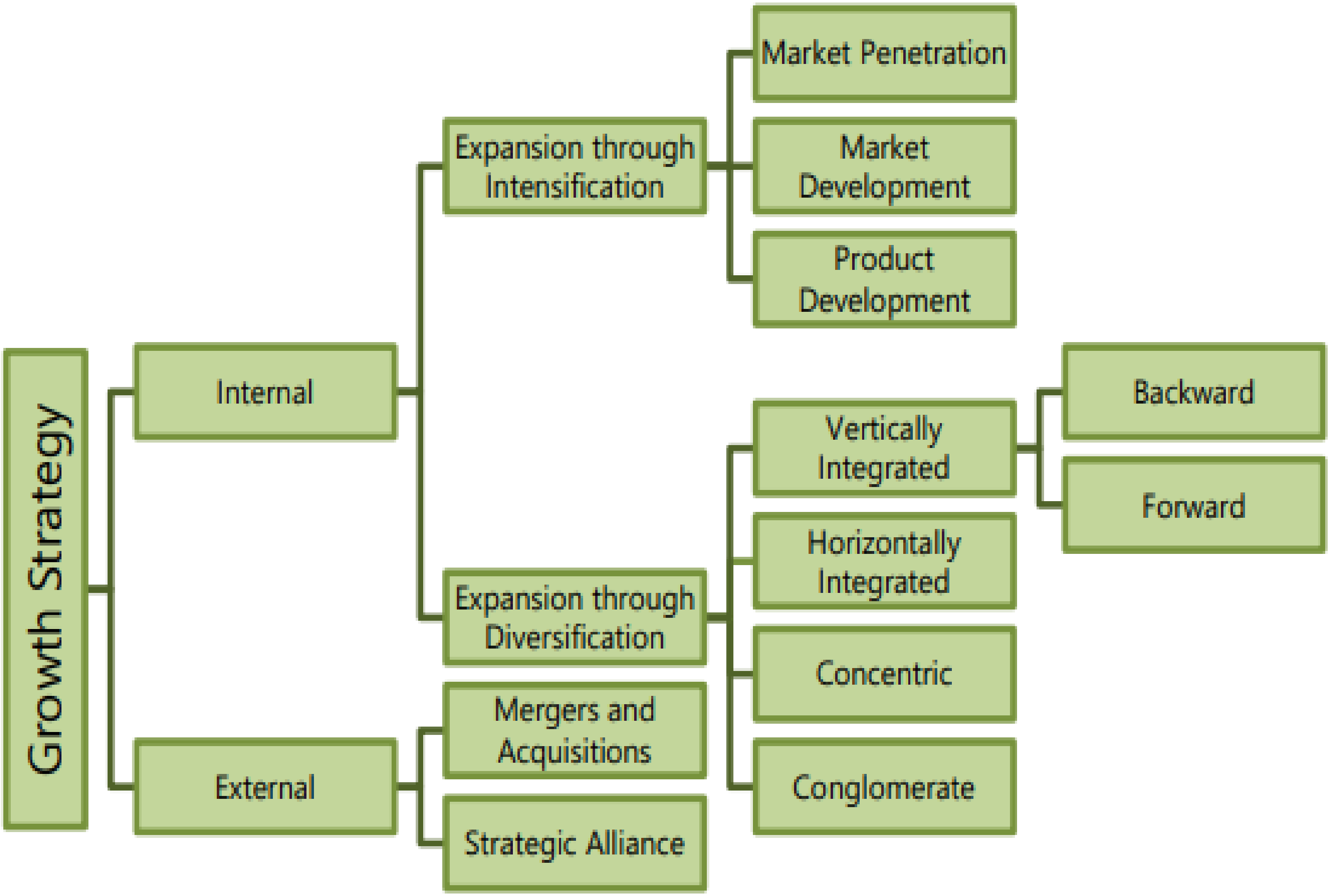


Figure: Types of Growth/Expansion Strategies

I Expansion or growth through Intensification:

Expansion or growth through intensification means that the organisation tries to grow internally by intensifying its operations either by market penetration or market development or by product development. It tries to cash on its internal capabilities and internal resources. The firm can intensify by adopting any of the following strategies:

(i) **Market Penetration:** Highly common expansion strategy is market penetration/concentration on the current business. The firm directs its resources to the profitable growth of its existing product in the existing market.

(ii) **Market Development:** It consists of marketing present products, to customers in related market areas by adding different channels of distribution or by changing the content of advertising or the promotional media.

(iii) **Product Development:** Product development involves substantial modification of existing products or creation of new but related items that can be marketed to current customers through establish channels.

The Ansoff Matrix

II Expansion through Diversification

When a firm tries to grow and expand by diversifying into various products or fields, it is called growth by diversification. This is also an internal growth strategy. Innovative and creative firms always look for opportunities and challenges to grow, to venture into new areas of activity and to break new frontiers with the zeal of entrepreneurship using their internal resources. They feel that diversification offers greater prospects of growth and profitability than intensification.

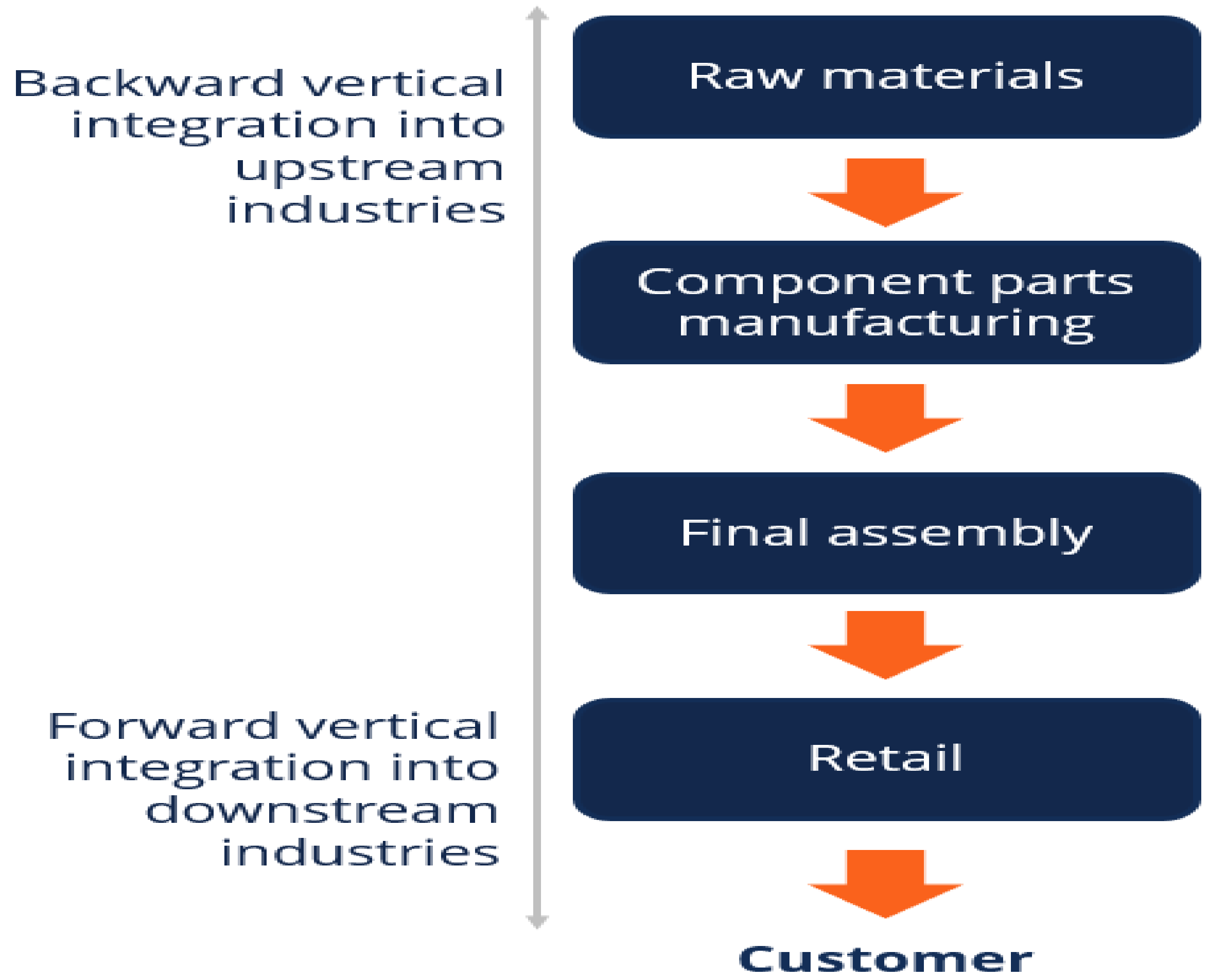
Based on the nature and extent of their relationship to existing businesses, diversification can be classified into four broad categories:

(i) Vertically integrated diversification

(ii) Horizontally integrated diversification

(iii) Concentric diversification

(iv) Conglomerate diversification



Backward vertical integration into upstream industries
Raw materials
Component parts manufacturing
Final assembly
Forward vertical integration into downstream industries
Retail
Customer


Vertical Integration
Thomas Cook
Vertical integration
Ford Automobiles
Travel
Agency
Automobile
Sales
Tour
Operation
Thomas
Cook
Ford
Automobile
Manufacturing
Airline
Operation
Steel Plant
Airline
Operation
Tyre
Manufacturing

(i) **Vertically Integrated Diversification:** In vertically integrated diversification, firms opt to engage in businesses that are related to the existing business of the firm. The firm remains vertically within the same process sequence moves forward or backward in the chain and enters specific product/process steps with the intention of making them into new businesses for the firm. The characteristic feature of vertically integrated diversification is that the firm remains in the vertically linked product-process chain. A firm can either opt for forward or backward integration or horizontal integration.

Forward and Backward Integration: Forward and backward integration forms part of vertically integrated diversification. In vertically integrated diversification, firms opt to engage in businesses that are vertically related to the existing business of the firm. The firm remains vertically within the same process. While diversifying, firms opt to engage in businesses that are linked forward or backward in the chain.

Backward integration is concerned with creation of effective supply by entering business of input providers. Strategy employed to expand profits and gain greater control over production/supply of a product whereby a company will purchase or build a business that will increase its own supply capability or lessen its cost of production. **For example**, *A large supermarket chain considers to purchase a number of farms that would provide it a significant amount of fresh produce.*

On the other hand, forward integration is moving forward in the value chain and entering business lines that use existing products. Forward integration will also take place where organizations enter into businesses of distribution channels. **For example**, *A coffee bean manufacture may choose to merge with a coffee cafe.*

VERTICAL DIVERSIFICATION

- In **Vertical Diversification,** a firm tries to make its presence in the supply chain, either by taking over a supplier or the customer, or both.
- A supply chain consists of several processes, including buying raw materials, converting raw materials into a product, assembling, transporting and sale.

TYPES

- Backward Diversification
- Forward Diversification

DISADVANTAGES

- Use of this strategy may result in less flexibility.
- Company using this grow bigger in size, and thus, faces a higher risk of legal repercussion.
- Combining the synergies of two companies may get difficult

ADVANTAGES

- This can be used to improve coordination in the supply chain.
- A firm may also use this strategy to invest in specialized assets.
- This enables a company to secure the distribution channels, as well as develop new competencies.

(ii) **Horizontal Integrated Diversification:** A firm gets horizontally diversified by integrating through acquisition of one or more similar businesses operating at the same stage of the production-marketing chain. They can also integrate with the firms producing complementary products or by-products or by taking over competitors' products. The following figure explains the horizontal diversification, wherein, textile mill 1 acquires textile mill 2 and 3 as well.

Figure: Horizontal Integrated Diversification

HORIZONTAL DIVERSIFICATION

In **HORIZONTAL DIVERSIFICATION** a firm adds more products that may appeal to the firm's existing clients.

HOW IT WORKS?

- First identify a need for a new product
- Come up with a product to meet that need
- In-depth analysis of its current customers by considering factors such as location, gender, and income level

ADVANTAGES

- Economies of scale
- Enables firm to expand its product line
- Makes product line more robust.
- May allow a company to attract new customers even for its core products.
- Helps a company to better its quality of existing and new products
- Gives companies greater price control
- Opportunity to improve existing products

DISADVANTAGES

- More susceptible to regulatory changes
- No focus on adding new customers

REAL WORLD EXAMPLES

- Apple initially offered computers but it later diversified into iPod and iPhone & now it also offers Apple Watch, Apple TV and many other hardware and software products.
- Walt Disney was initially into animation and children's cartoons & then come up with aggressive diversification to serve its core audience – kids & families. It now operates theme parks, hotel resorts and also has a presence in the entertainment and media industry.

Horizontal Integration Examples

Vodafone-Idea → Vodafone & Idea had a nominal market share over clients with some pricing power in India.

Marriott-Starwood → Marriott and Starwood have been two worldwide-known hotel chains.

Arcelor-Mittal → Arcelor-Mittal is the biggest steel manufacturer in the world.

Exxon-Mobil → Exxon and Mobil in the oil industry were two distinct giants.

JP Morgan Chase → A merger between Chase Manhattan Bank & JP Morgan Company resulted in JP Morgan and Chase Bank.

(iii) Concentric Diversification: Concentric diversification takes place when the products are related. In this diversification, the new business that is it diversifies into is linked to the existing businesses through process, technology or marketing. The new product is a spin-off from the existing facilities and products/processes. This means that in concentric diversification too, there are benefits of synergy with the current operations. However, concentric diversification differs from vertically integrated diversification in the nature of the linkage the new product has with the existing ones. While in vertically integrated diversification, the new product falls within the firm's current process-product chain, but in concentric diversification, there is a departure from this vertical linkage. The new product is only connected in a loop-like manner at one or more points in the firm's existing process/technology/product chain. **For example,** *a company producing clothes ventures into the manufacturing of shoes.*

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CONCENTRIC DIVERSIFICATION

CONCENTRIC DIVERSIFICATION includes adding of new but related products.

ADVANTAGES

1. Use of Existing Infrastructure

Adding a new product similar to existing products allows company to utilize the existing competencies and abilities.

2. Enables Business Synergy

It enables a company to come up with a strategic fit by coming up with similar products and services.

3. Boost Market Share

Concentric integration usually results in an increase in market share & boost a company's product presence.

Example of Concentric Diversification

- The addition of tomato ketchup and sauce to the existing "Maggi" brand processed items of Food Specialities Ltd. is an example of technological-related concentric diversification

Marketing &Technology-related concentric diversification

- When a similar type of product or service is provided with the help of related technology.

Example

- Usha International has diversified into home appliances like juicer, mixer, geyser, vacuum cleaners and washing machines and exhaust fans and tries to exploit its distribution of network of over 3,500 dealers to sell its new products. . It is an instance of **Marketing &Technology-related concentric diversification**

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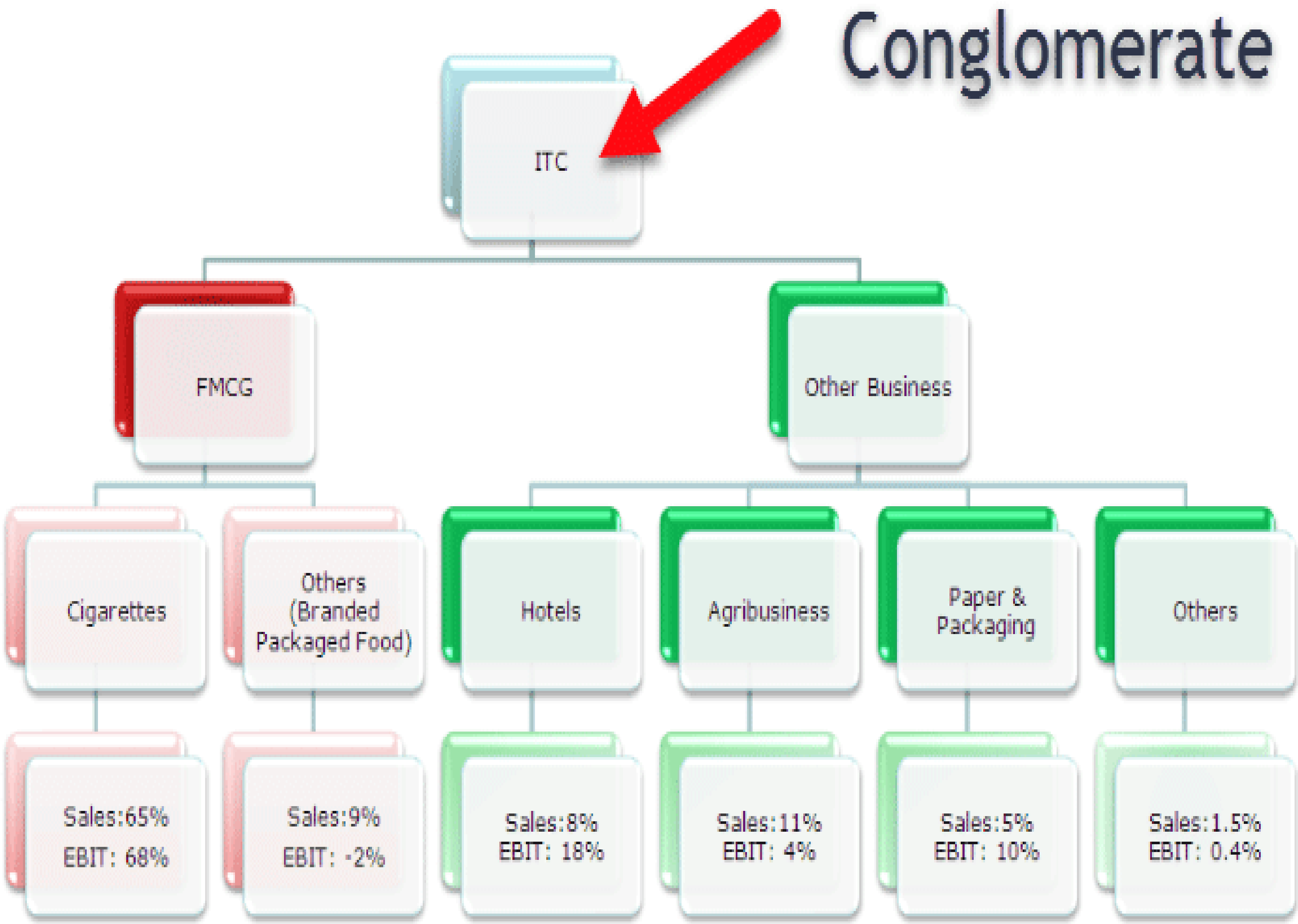
Conglomerate Diversification

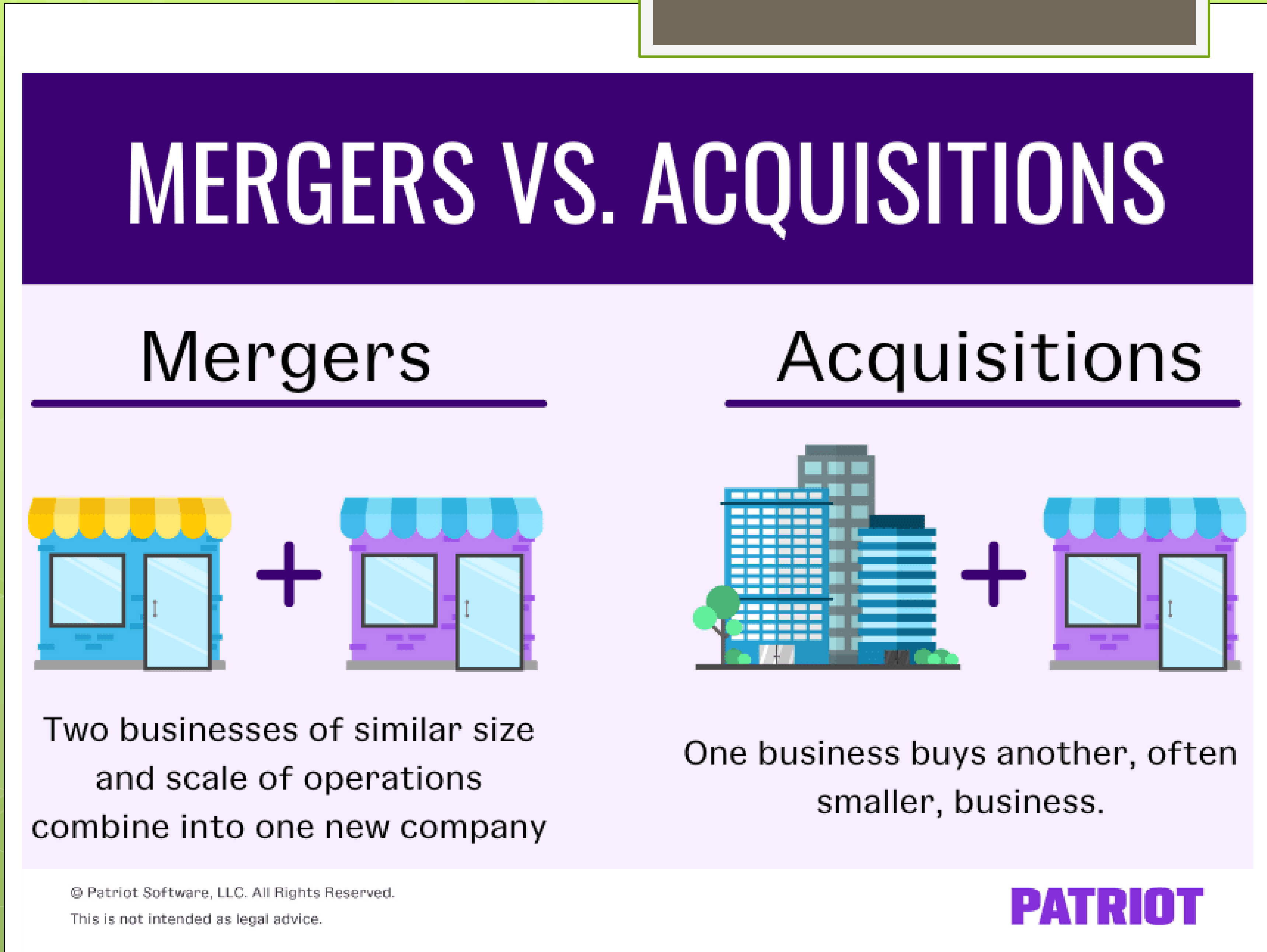
- When an organization adopts a strategy which requires taking of those activities which are unrelated to the existing businesses definition of one or more of its businesses either in terms of their respective customer groups, customer functions or alternative technologies, it is called conglomerate diversification.

General electric

General Electric (GE) is an American multinational conglomerate corporation incorporated in New York and headquartered in Fairfield, Connecticut. As of 2015, the company operates through the following segments: Power and Water, Oil and Gas, Energy Management, Aviation, Healthcare, Transportation, and Capital.

In 2011, GE ranked among the Fortune 500 as the 26th-largest firm in the U.S. by gross revenue, as well as the 14th most profitable. However, the company is listed the fourth-largest in the world among the Forbes Global 2000, further metrics being taken into account. Other rankings for 2011/2012 include No. 7 company for leaders (Fortune), No. 5 best global brand (Interbrand), No. 63 green company (Newsweek), No. 15 most admired company (Fortune), and No. 19 most innovative company (Fast Company).


Conglomerate
ITC
FMCG
Other Business
Cigarettes
Others (Branded Packaged Food)
Hotels
Agribusiness
Paper & Packaging
Others
Sales:65%
EBIT: 68%
Sales:9%
EBIT: -2%
Sales:8%
EBIT: 18%
Sales:11%
EBIT: 4%
Sales:5%
EBIT: 10%
Sales:1.5%
EBIT: 0.4%


MERGERS VS. ACQUISITIONS
Mergers
Acquisitions
Two businesses of similar size and scale of operations combine into one new company
One business buys another, often smaller, business.
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PATRIOT

I Expansion through Mergers and Acquisitions

Acquisition or merger with an existing concern is an instant means of achieving the expansion. It is an attractive and tempting proposition in the sense that it circumvents the time, risks and skills involved in screening internal growth opportunities, seizing them and building up the necessary resource base required to materialise growth. Organizations consider merger and acquisition proposals in a systematic manner, so that the marriage will be mutually beneficial, a happy and lasting affair.

Apart from the urge to grow, acquisitions and mergers are resorted to for purposes of achieving a measure of synergy between the parent and the acquired enterprises. Synergy may result from such bases as physical facilities, technical and managerial skills, distribution channels, general administration, research and development and so on. Only positive synergistic effects are relevant in this connection which denotes that the positive effects of the merged resources are greater than the effects of the individual resources before merger or acquisition.

Types of Mergers

The following are the types of mergers and are quite similar to the types of diversification.

(a) Horizontal Merger

Horizontal merger is a combination of firms engaged in the same industry. It is a merger with a direct competitor. The principal objective behind this type of merger is to achieve economies of scale in the production process by shedding duplication of installations and functions, widening the line of products, decrease in working capital and fixed assets investment, getting rid of competition and so on. **For example**, *formation of Brook Bond Lipton India Ltd. through the merger of Lipton India and Brook Bond.*

(b) Vertical Merger

It is a merger of two organizations that are operating in the same industry but at different stages of production or distribution system. This often leads to increased synergies with the merging firms. If an organization takes over its supplier/producers of raw material, then it leads to backward integration. On the other hand, forward integration happens when an organization decides to take over its buyer organizations or distribution channels. Vertical merger results in many operating and financial economies. Vertical mergers help to create an advantageous position by restricting the supply of inputs to other players, or by providing the inputs at a higher cost. **For example**, *backward integration and forward integration.*

(c) Co-generic Merger

In Co-generic merger two or more merging organizations are associated in some way or the other related to the production processes, business markets, or basic required technologies. Such merger includes the extension of the product line or acquiring components that are required in the daily operations. It offers great opportunities to businesses to diversify around a common set of resources and strategic requirements. **For example**, *an organization in the white goods category such as refrigerators can diversify by merging with another organization having business in kitchen appliances.*

(d) Conglomerate Merger

Conglomerate mergers are the combination of organizations that are unrelated to each other. There are no linkages with respect to customer groups, customer functions and technologies being used. There are no important common factors between the organizations in production, marketing, research and development and technology. In practice, however, there is some degree of overlap in one or more of these factors.

II. Expansion through Strategic Alliance

A strategic alliance is a relationship between two or more businesses that enables each to achieve certain strategic objectives which neither would be able to achieve on its own. The strategic partners maintain their status as independent and separate entities, share the benefits and control over the partnership, and continue to make contributions to the alliance until it is terminated. Strategic alliances are often formed in the global marketplace between businesses that are based in different regions of the world.

Advantages of Strategic Alliance

Strategic alliance usually is only formed if they provide an advantage to all the parties in the alliance. These advantages can be broadly categorised as follows:

1. **Organizational:** Strategic alliance helps to learn necessary skills and obtain certain capabilities from strategic partners. Strategic partners may also help to enhance productive capacity, provide a distribution system, or extend supply chain. Strategic partners may provide a good or service that complements thereby creating a synergy. Having a strategic partner who is well-known and respected also helps add legitimacy and creditability to a new venture.

2. **Economic:** There can be reduction in costs and risks by distributing them across the members of the alliance. Greater economies of scale can be obtained in an alliance, as production volume can increase, causing the cost per unit to decline. Finally, partners can take advantage of co-specialization, creating additional value, such as when a leading computer manufacturer bundles its desktop with a leading monitor manufacturer's monitor.

3. **Strategic:** Rivals can join together to cooperate instead of competing with each other. Vertical integration can be created where partners are part of supply chain. Strategic alliances may also be useful to create a competitive advantage by the pooling of resources and skills. This may also help with future business opportunities and the development of new products and technologies. Strategic alliances may also be used to get access to new technologies or to pursue joint research and development.

4. **Political:** Sometimes strategic alliances are formed with a local foreign business to gain entry into a foreign market either because of local prejudices or legal barriers to entry. Forming strategic alliances with politically influential partners may also help improve your own influence and position.

Disadvantages of Strategic Alliance

Strategic alliances do come with some disadvantages and risks. The major disadvantage is **sharing.** Strategic alliances require sharing of resources and profits, and also sharing knowledge and skills that otherwise organisations may not like to share. Sharing knowledge and skills can be problematic if they involve trade secrets. Agreements can be executed to protect trade secrets, but they are only as good as the willingness of parties to abide by the agreements or the courts willingness to enforce them. Strategic alliances may also create potential competition when an ally becomes an opponent in future when it decides to separate out.

Characteristics of a Joint Venture

- It is a temporary partnership which comes to an end after the completion of a particular venture.
- It is for a specific venture, so it is a particular partnership.
- The partnership is without the use of a firm name.
- The main purpose it to make profit and to distribute it among all co-venturers. Loss, if any, will also be borne in agreed ratio or equally if no agreement regarding ratio has been made.

8 Benefits of a

JOINT VENTURE

1. New source of investment
2. Save on more costs
3. Gain knowledge
4. Enter a new market
5. Possibility for business growth & expansion
6. Acquire intellectual property
7. Boost Credibility
8. Avoid competition

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4.2.3. Retrenchment Strategy

Retrenchment Strategy: It is followed when an organization substantially reduces the scope of its activity. This is done through an attempt to find out the problem areas and diagnose the causes of the problems. Next, steps are taken to solve the problems. These steps result in different kinds of retrenchment strategies. If the organization chooses to focus on ways and means to reverse the process of decline, it adopts at turnaround strategy. If it cuts off the loss-making units, divisions, or SBUs, curtails its product line, or reduces the functions performed, it adopts a divestment (or divestiture) strategy. If none of these actions work, then it may choose to abandon the activities totally, resulting in a liquidation strategy. We deal with each of these strategies below.

I. Turnaround Strategy

Retrenchment may be done either internally or externally. For internal retrenchment to take place, emphasis is laid on improving internal efficiency, known as turnaround strategy.

There are certain conditions or indicators which point out that a turnaround is needed if the company has to survive. These danger signals are:

- Persistent negative cash flow from business(es)
- Uncompetitive products or services
- Declining market share
- Deterioration in physical facilities
- Over-staffing, high turnover of employees, and low morale

Action Plan for Turnaround

For turnaround strategies to be successful, it is imperative to focus on the short and long-term financing needs as well as on strategic issues. A workable action plan for turnaround would involve the following stages:

- **Stage One – Assessment of current problems**: The first step is to assess the current problems and get to the root causes and the extent of damage the problem has caused. Once the problems are identified, the resources should be focused toward those areas essential to efficiently work on correcting and repairing any immediate issues.
- **Stage Two –Analyze the situation and develop a strategic plan:** Before you make any major changes; determine the chances of the business's survival. Identify appropriate strategies and develop a preliminary action plan. For this one should look for the viable core businesses, adequate bridge financing and available organizational resources. Analyze the strengths and weaknesses in the areas of competitive position. Once major problems and opportunities are identified, develop a strategic plan with specific goals and detailed functional actions.
- **Stage Three –Implementing an emergency action plan**: If the organization is in a critical stage, an appropriate action plan must be developed to stop the bleeding and enable the organization to survive. The plan typically includes human resource, financial, marketing and operations actions to restructure debts, improve working capital, reduce costs, improve budgeting practices, prune product lines and accelerate high potential products. A positive operating cash flow must be established as quickly as possible and enough funds to implement the turnaround strategies must be raised.

- **Stage Four –Restructuring the business**: The financial state of the organization's core business is particularly important. If the core business is irreparably damaged, then the outlook for the entire organization may be bleak. Prepare cash forecasts, analyze assets and debts, review profits and analyze other key financial functions to position the organization for rapid improvement.

  During the turnaround, the "product mix" may be changed, requiring the organization to do some repositioning. Core products neglected over time may require immediate attention to remain competitive. Some facilities might be closed; the organization may even withdraw from certain markets to make organization leaner or target its products toward a different niche.

  Morale building is another important ingredient in the organization's competitive effectiveness. Reward and compensation systems that encourage dedication and creativity amongst employees to think about profits and return on investments.

- **Stage Five –Returning to normal**: In the final stage of turnaround strategy process, the organization should begin to show signs of profitability, return on investments and enhancing economic value-added. Emphasis is placed on a number of strategic efforts such as carefully adding new products and improving customer service, creating alliances with other organizations, increasing the market share, etc.

The important elements of turnaround strategy are as follows:

- Changes in the top management
- Initial credibility-building actions
- Neutralising external pressures
- Identifying quick payoff activities
- Quick cost reductions
- Revenue generation
- Asset liquidation for generating cash
- Better internal coordination

II. Divestment Strategy

Divestment strategy involves the sale or liquidation of a portion of business, or a major division, profit centre or SBU. Divestment is usually a part of rehabilitation or restructuring plan and is adopted when a turnaround has been attempted but has proved to be unsuccessful. The option of a turnaround may even be ignored if it is obvious that divestment is the only answer.

A divestment strategy may be adopted due to various reasons:

- A business that had been acquired proves to be a mismatch and cannot be integrated within the company.
- Persistent negative cash flows from a particular business create financial problems for the whole company, creating the need for divestment of that business.
- Severity of competition and the inability of a firm to cope with it may cause it to divest.
- It is not possible for the business to do Technological upgradation that is required for the business to survive, a preferable option would be to divest.
- A better alternative may be available for investment, causing a firm to divest a part of its unprofitable business.

III. Liquidation Strategy

A retrenchment strategy considered as the most extreme and unattractive is liquidation strategy, which involves closing down a firm and selling its assets. It is considered as the last resort because it leads to serious consequences such as loss of employment for workers and other employees, termination of opportunities where a firm could pursue any future activities, and the stigma of failure. Many small-scale units, proprietorship firms, and partnership ventures liquidate frequently but medium-and large-sized companies rarely liquidate in India. The company management, government, banks and financial institutions, trade unions, suppliers and creditors, and other agencies are extremely reluctant to take a decision, or ask, for liquidation.

Selling assets for implementing a liquidation strategy may also be difficult as buyers are difficult to find. Moreover, the firm cannot expect adequate compensation as most assets, being unusable, are considered as scrap.

Liquidation strategy may be unpleasant as a strategic alternative but when a "dead business is worth more than alive", it is a good proposition. For instance, the real estate owned by a firm may fetch it more money than the actual returns of doing business. When liquidation is evident (though it is difficult to say exactly when), an abandonment plan is desirable. Planned liquidation would involve a systematic plan to reap the maximum benefits for the firm and its shareholders through the process of liquidation.

Scenario Based Questions

Question 1

Gautam and Siddhartha two brothers are the owners of a cloth manufacturing unit located in Faridabad. They are doing well and have substantial surplus funds available within the business. They have different approaches regarding corporate strategies to be followed to be more competitive and profitable in future.

Gautam is interested in acquiring another industrial unit located in Faridabad manufacturing stationery items such as permanent markers, notebooks, pencils and pencil sharpeners, envelopes and other office supplies. On the other hand, Siddhartha desires to start another unit to produce readymade garments.

Discuss the nature of corporate strategies being suggested by two brothers and risks involved in it.

Answer

Gautam wishes to diversify in a business that is not related to their existing line of product and can be termed as conglomerate diversification. He is interested in acquiring another industrial unit located in Faridabad manufacturing stationery items such as permanent markers, notebooks, pencils and pencil sharpeners, envelopes and other office supplies, which is not related to their existing product. In conglomerate diversification, the new businesses/ products are disjointed from the existing businesses/products in every way; it is an unrelated diversification. In process/ technology/ function, there is no connection between the new products and the existing ones. Conglomerate diversification has no common thread at all with the firm's present position.

On the other hand, Siddhartha seeks to move forward in the chain of existing product by adopting vertically integrated diversification/ forward integration. The cloth being manufactured by the existing processes can be used as raw material of garments manufacturing business. In such diversification, firms opt to engage in businesses that are related to the existing business of the firm. The firm remains vertically within the same process and moves forward or backward in the chain. It enters specific product/process steps with the intention of making them into new businesses for the firm. The characteristic feature of vertically integrated diversification is that here, the firm does not jump outside the vertically linked product-process chain.

Both types of diversifications have their own risks. In conglomerate diversification, there are no linkages with customer group, customer marketing functions and technology used, which is a risk. In the case of vertical integrated diversification, there is a risk of lack of continued focus on the original business.