CHAPTER 4

CORPORATE LEVEL STRATEGIES

LEARNING OUTCOMES

After studying this chapter, you will be able to -

- Understand and identify corporate strategies.
- Identify the various types of corporate strategies.
- Comprehend the relevance and application of various types of corporate strategies.
- Understand the reasons for adoption of various types of corporate strategies.

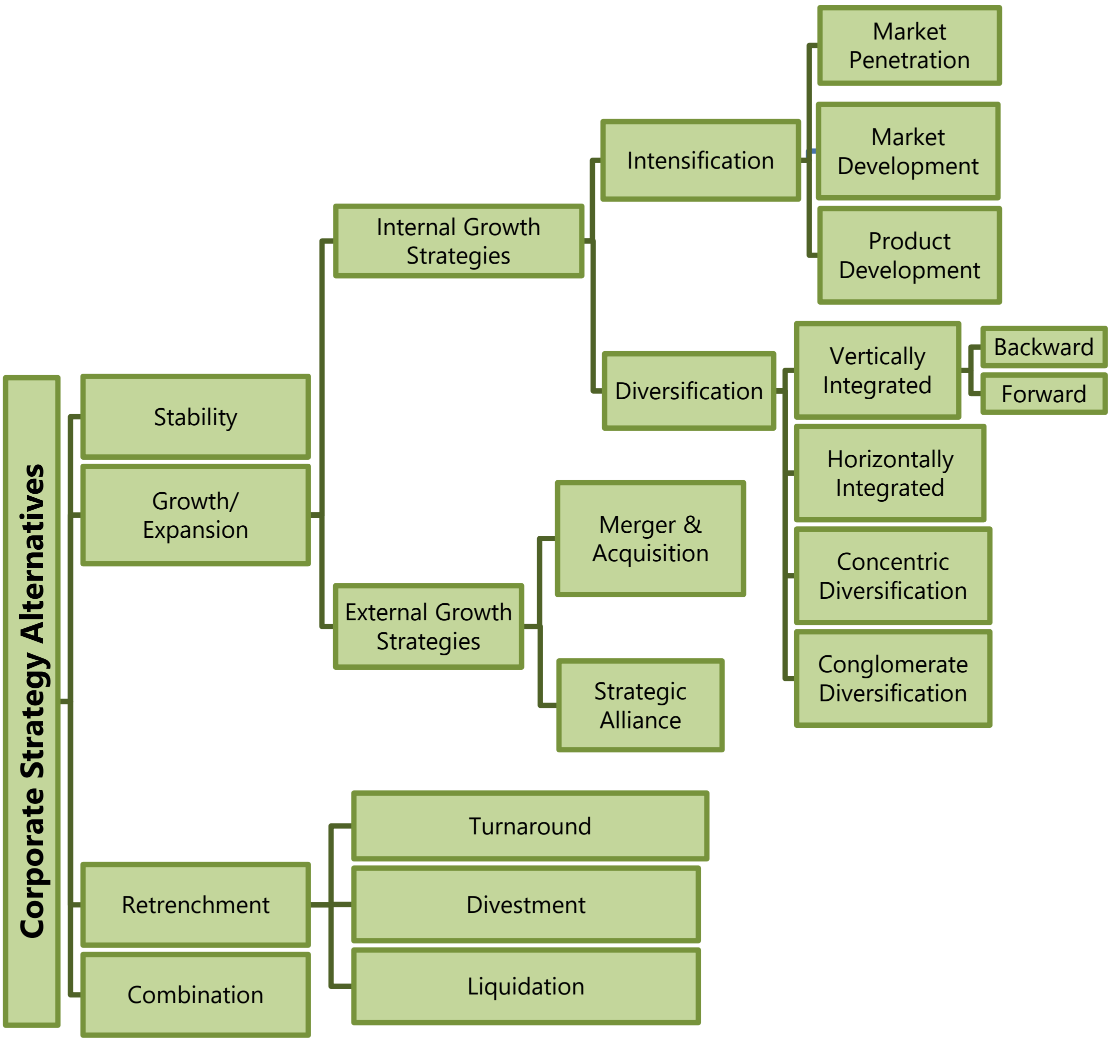
Know about combination strategies and strategic alliances.

Chance favours the prepared mind. *Louis Pasteur*

Strategy is a deliberate search for a plan of action that will develop a business competitive advantage and compound it.

Bruce D. Henderson

CHAPTER OVERVIEW



4.1 INTRODUCTION

Strategies are formulated at different levels of an organization – corporate, business and functional. Corporate level strategies occupy the highest level of strategic decision making and cover actions dealing with the objective of the firm, acquisition and allocation of resources and coordination of strategies of various Strategic Business Units for optimal performance. Top management of the organization makes strategic decisions. The nature of strategic decisions tends to be value-oriented, conceptual and less concrete than decisions at the business or functional level. This chapter deals with corporate level strategies and their various types.

4.2 TYPOLOGIES OF STRATEGIES

Businesses follow different types of strategies to enter the market and to stay and grow in the market. A large number of strategies with different nomenclatures have been employed by different businesses and also suggested by different authors on strategy. For instance, William F Glueck and Lawrence R Jauch discussed four generic strategies including stability, growth, retrenchment and combination. These strategies have also been called Grand Strategies/Directional Strategies by many other authors. Michael E. Porter suggested competitive strategies including Cost Leadership, Differentiation, Focus Cost Leadership and Focus Differentiation which could be used by the corporates for their different business units. Besides these, we come across functional strategies in the literature on Strategic Management and Business Policy. Functional Strategies are meant for strategic management of distinct functions such as Marketing, Financial, Human Resource, Logistics, Production etc.

We can classify the different types of strategies on the basis of levels of the organisation, stages of business life cycle and competition as given in the Table –1.

Table : 1- Different types of strategies on the basis of their classification

Basis of Classification	Types
Level of the organisation	Corporate Level Business Level Functional Level
Stages of Business Life Cycle	Entry/Introduction Stage - Market Penetration Strategy Growth Stage - Growth/Expansion Strategy Maturity Stage - Stability Strategy Decline Stage - Retrenchment/ Turnaround Strategy
Competition oriented	Competitive Strategies - Cost Leadership, Differentiation, Focus Collaboration Strategies - Joint Venture, Merger & Acquisition, Strategic Alliance

Above are the various types of strategies available for an organisation to adopt. The organisation adopt either of these depending upon their needs and requirements. For instance, a start-up or a new enterprise might follow either a competitive strategy i.e., entering the market where a number of rivals are already operating, or a collaborative strategy, i.e., enter into a joint venture with an established company. However, majority of startups are launched on a small scale and their main strategy is to penetrate the market and to reach the breakeven stage at the earliest and later pursue growth strategy. While a going concern can continue with the competitive strategy or resort to collaborative strategy to ensure business growth.

Reality Bite: Patanjali Ayurved adopted market penetration strategy and to be successful. It concentrated on product development and high quality at low cost. It is now at the growth stage and is following competitive strategies. It is competing with both domestic and multinational companies.

Business conglomerates having multiple product folios formulate strategies at different levels, viz., corporate, business unit and functional. Corporate level strategies are meant to provide 'direction' to the company. Business level strategies are formulated for each product/process division known as strategic business unit. While for implementation of the corporate and business strategies, functional strategies are formulated in business areas like production/operations, marketing, finance, human resources etc. In fact, big corporates follow an elaborate system of strategy formulation, implementation and control at different levels in the company to survive and grow in the turbulent business environment. In this chapter, we shall discuss the corporate level strategies.

The corporate strategies a firm can adopt may be classified into four broad categories:

1. Stability strategy
2. Expansion strategy
3. Retrenchment strategy
4. Combination strategy

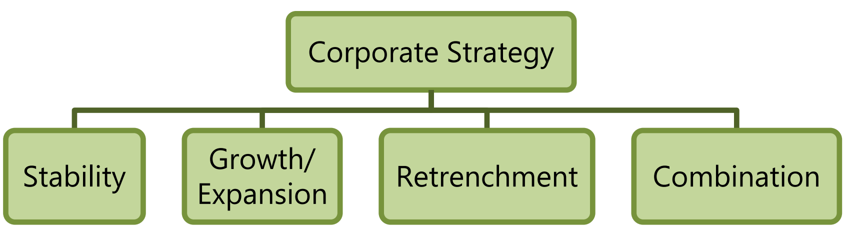


Figure:-Types of Corporate Strategies

Before proceeding further, let us discuss the basic features of all the types of corporate strategies to get the bird's eye view. The basic features of the corporate strategies are as follows:

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. Stability Strategy

One of the important goals of a business enterprise is stability strategy is to stabilise- it may be opted to safeguard its existing interests and strengths, to pursue well established and tested objectives, to continue in the chosen business path, to maintain operational efficiency on a sustained basis, to consolidate the commanding position already reached, and to optimise returns on the resources committed in the business.

A stability strategy is pursued by a firm when:

- It continues to serve in the same or similar markets and deals in same or similar products and services.
- This strategy is typical for those firms whose product have reached the maturity stage of product life cycle or those who have a sufficient market share but need to retain that. They have to remain updated and have to pace with the dynamic and volatile business world to preserve their market share. Hence, stability strategy should not be confused with 'do nothing' strategy. Small organizations may also follow stability strategy to

consolidate their market position and prepare for the launch of growth strategies. For deeper understanding of these strategies, let us delve into their characteristics:

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.

4.2.1.2 Major Reasons for Stability Strategy

- A product has reached the maturity stage of the product life cycle.
- The staff feels comfortable with the status quo as it involves less changes and less risks.
- It is opted when the environment in which an organisation is operating is relatively stable.
- Where it is not advisable to expand as it may be perceived as threatening.
- After rapid expansion, a firm might want to stabilize and consolidate itself.

4.2.2. Growth/Expansion Strategy

Growth/Expansion strategy is implemented by redefining the business by enlarging the scope of business and substantially increasing investment in the business. It is a strategy that can be equated with dynamism, vigour, promise and success. It is often characterised by significant reformulation of goals and directions, major initiatives and moves involving investments, exploration and onslaught into new products, new technology and new markets, innovative decisions and action programmes and so on. This strategy may take the enterprise along relatively unknown and risky paths, full of promises and pitfalls.

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.

4.2.2.2 Major Reasons for Growth/Expansion Strategy

- It may become imperative when environment demands increase in pace of activity.
- Strategists may feel more satisfied with the prospects of growth from expansion; chief executives may take pride in presiding over organizations perceived to be growth-oriented.
- Expansion may lead to greater control over the market vis-a-vis competitors.
- Advantages from the experience curve and scale of operations may accrue.

♦ Expansion also includes intensifying, diversifying, acquiring and merging businesses. Therefore, growth strategies can take the following forms:

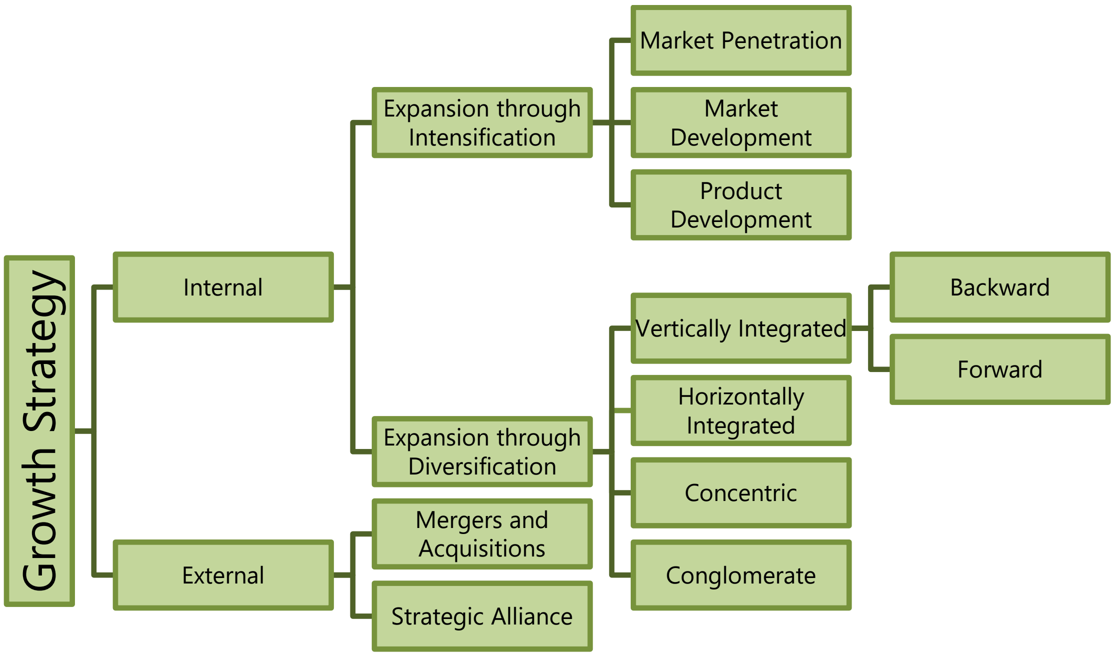


Figure: Types of Growth/Expansion Strategies

4.2.2.3 Types of Growth/ Expansion Strategy

The growth strategies can be classified into two main types:

A. Internal growth strategies

B. External growth strategies

A. Internal growth strategies

Internal growth strategies can be further divided into:

I. Expansion through Intensification

II. Expansion through diversification

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.

Igor. H. Ansoff gave a framework as shown in figure below which describes the intensification options available to a firm.

Table:3- Product-Market Expansion Grid

Market Penetration • Increase market share • Increase product usage • Increase the frequency used • Increase the quantity used • Find new application for current users	**Product Development** • Add product features, product refinement • Develop a new-generation product • Develop new product for the same market
Market Development • Expand geographically Target new segments	**Diversification involving new products and new markets** Related / Unrelated

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.

Diversification is defined as an entry into new products or product lines, new services or new markets, involving substantially different skills, technology and knowledge. When an established firm introduces a new product, which has little or no affinity with its present product line and which is meant for a new class of customers different from the firm's existing customer groups, the process is known as conglomerate diversification. Both the technology of the product and the market are different from the firm's present experience.

For some firms, diversification is a means of utilising their existing facilities and capabilities in a more effective and efficient manner. They may have excess capacity or capability in manufacturing facilities, investible funds, marketing channels, competitive standing, market prestige, managerial and other manpower, research and development, raw material sources and so forth. Another reason for diversification lies in its synergistic advantage. It may be possible to improve the sales and profits of existing products by adding suitably related or new products, because of linkages in technology and/or in markets.

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

Diversification endeavours can be related or unrelated to existing businesses of the firm.

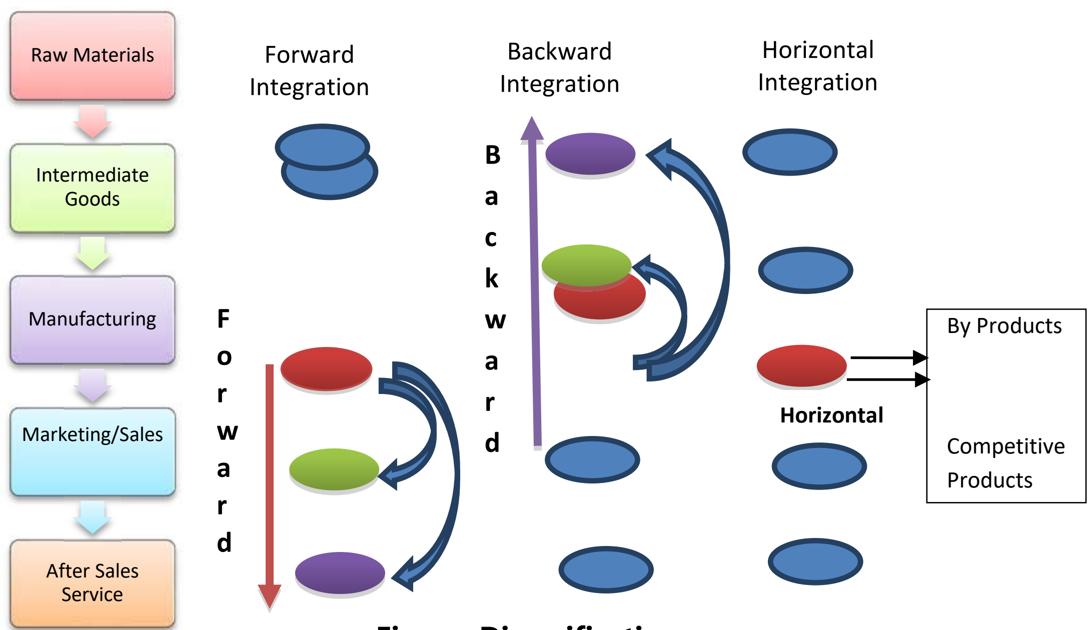


Figure: Diversification

(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.*

(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

Diversification can be related (Concentric) or unrelated (Conglomerate) to the existing businesses of the firm and hence can be either Concentric or Conglomerate.

(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.*

(iv) Conglomerate Diversification: In conglomerate diversification, no linkages related to product, market or technology exist; the new businesses/products are disjointed from the existing businesses/products in every way; it is a totally 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. **For example,** *A cement manufacturer diversifies into the manufacture of steel and rubber products.*

Table 4 : Related vs. Unrelated Diversification

RELATED DIVERSIFICATION	UNRELATED DIVERSIFICATION
Exchange or share assets or competencies by exploiting • Brand name • Marketing skills • Sales and distribution capacity • Manufacturing skills • R&D and new product capability • Economies of scale	• Investment in new product portfolios. • Employment of new technologies. • Focus on multiple products. • Reduce risk by operating in multiple product markets. • Defend against takeover bids. • Provide executive interest.

B. External Growth Strategies

When the organization instead of growing internally thinks of diversifying by making alliances with external organisations, it is called external growth diversification. It can be classified in two way.

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.

Merger and acquisition in simple words are defined as a process of combining two or more organizations together. There is a thin line of difference between the two terms but the impact of combination is completely different in both the cases. Some organizations prefer to grow through mergers. Merger is a process when two or more companies come together to expand their business operations. In such a case the deal gets finalized on friendly terms and both the organizations share profits in the newly created entity. In a merger two organizations combine to increase their strength and financial gains along with breaking of the trade barriers.

When one organization takes over the other organization and controls all its business operations, it is known as acquisition. In acquisition, one financially strong organization overpowers the weaker one. Acquisitions often happen during recession in economy or during declining profit margins. In this process, the stronger one overpowers the weaker one. The combined operations then run under the name of the powerful entity. A deal in case of an acquisition is often done in an unfriendly manner, it is more or less a forced association where the powerful organization acquires the operations of the company that is in a weaker position and is forced to sell its entity.

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.

(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 include 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 are 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.

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
- Mismanagement

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.

Characteristics of Divestment Strategy

- This strategy involves divestment of some of the activities in a given business of the firm or sell-out of some of the businesses as such.
- Divestment is to be viewed as an integral part of corporate strategy without any stigma attached.
- Like expansion strategy, divestment strategy, too, involves a redefinition of the business of the corporation.
- Compulsions for divestment can be many and varied, such as
  - (a) Obsolescence of product/process
  - (b) Business becoming unprofitable and unviable
  - (c) Inability to cope up with cut throat competition
  - (d) Industry overcapacity
  - (e) Failure of existing strategy

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.

Major Reasons for Retrenchment/Turnaround Strategy

- The management no longer wishes to remain in business either partly or wholly due to continuous losses and unviability.
- The management feels that business could be made viable by divesting some of the activities or liquidation of unprofitable activities.
- 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.
- Technological upgradation is required if the business is to survive but where it is not possible for the firm to invest in it, 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 businesses.

4.2.4. Combination Strategy

The above strategies are not mutually exclusive. It is possible to adopt a mix of the above to suit particular situations. An enterprise may seek stability in some areas of activity, expansion in some and retrenchment in the others. Retrenchment of ailing products followed by stability and capped by expansion in some situations may be thought of. For some organizations, a strategy by diversification and/or acquisition may call for a retrenchment in some obsolete product lines, production facilities and plant locations.

Example, how startup combine all the strategies to fight competition and gain advantage from other growing companies to built a niche empire.

Major Reasons for Combination Strategy

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

SUMMARY

Strategies are formulated at different levels of an organization – corporate level, business level, and functional level. The strategy changes based on the levels of strategy. Corporate level strategy occupies the highest level of strategic decision making and covers actions dealing with the objective of the firm, acquisition and allocation of resources and coordination of strategies of various SBUs for optimal performance. There are various corporate strategic alternatives available to the companies such as stability strategy, expansion strategy, retrenchment strategy, combination strategy and turnaround strategy. Expansion strategy covers expansion through intensification, diversification, acquisitions & mergers, strategic alliances etc.

TEST YOUR KNOWLEDGE

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.

Question 2

XYZ Company is facing continuous losses. There is decline in sales and product market share. The products of the company became uncompetitive and there is persistent negative cash flow. The physical facilities are deteriorating and employees have low morale. At the board meeting, the board members decided that they should continue the organization and adopt such measures such that the company functions properly. The board has decided to hire young executive Shayamli for improving the functions of the organization. What corporate strategy should Shayamli adopt for this company and what steps need to be taken to implement the corporate strategy adopted by Shayamli?

Answer

XYZ Company is facing continuous losses, decline in sales and product market share, persistent negative cash flow, uncompetitive products, declining market share, deterioration in physical facilities, low morale of employees. In such a scenario, Shayamli may choose ***turnaround strategy*** as this strategy attempts to reverse the process of decline and bring improvement in organizational health. This is also important as Board has decided to continue the company and adopt measures for its proper functioning.

For success, Shayamli needs to focus on the short and long-term financing needs as well as on strategic issues. During the turnaround, the "product mix" may be changed, requiring the organization to do some repositioning. A workable action plan for turnaround would involve:

Stage One – Assessment of current problems: In the first step, assess the current problems and get to the root causes and the extent of damage.

Stage Two – Analyze the situation and develop a strategic plan: Identify major problems and opportunities, 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.

Stage Four – Restructuring the business: If the core business is irreparably damaged, then the outlook for the entire organization may be bleak. Efforts to be made to position the organization for rapid improvement.

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.

Question 3

Arena Ltd. manufactures computers that are of low in production cost, competitive price, and quality to their competitor's product. Profits and market share are declining day by day. Shreekanth, a senior executive realizes that drastic strategies have to be created for the survival of a company. After SWOT analysis by assessing the strengths and weaknesses, they come up with the conclusion that they cannot compete in the computers with the competitors. The management directs Shreekanth to act quick and develop a suitable strategic plan.

Discuss the strategy which can be opted by Shreekanth.

Answer

Shreekant opt for turnaround strategy which is a highly-targeted effort to return Arena Ltd. to profitability and increase positive cash flows to a sufficient level. Organizations those have faced a significant crisis that has negatively affected operations require turnaround strategy. Once turnaround is successful the organization may turn to focus on growth.

Conditions for turnaround strategies

When firms are losing their grips over market, profits due to several internal and external factors, and if they have to survive under the competitive environment they have to identify danger signals as early as possible and undertake rectification steps immediately. These conditions may be, inter alia cash flow problems, lower profit margins, high employee turnover and decline in market share, capacity underutilization, low morale of employees, recessionary conditions, mismanagement, raw material supply problems and so on.

Action plan for turnaround strategy

- Stage One – Assessment of current problems
- Stage Two – Analyze the situation and develop a strategic plan
- Stage Three – Implementing an emergency action plan
- Stage Four – Restructuring the business
- Stage Five – Returning to normal

Question 4

Pizza Galleria was India's first pizza delivery chain enjoying monopoly for several years. However, after entry of Modino and Uncle Jack it is struggling to compete. Both Modino and Uncle Jack have opened several eateries and priced the product aggressively. In last four years the chain has suffered significant losses. The chain wishes to know whether they should go for turnaround strategy. List out components of action plan for turnaround strategy.

Answer

Pizza Chain may choose to have turnaround strategy if there are:

♦ Persistent negative cash flow from business.

♦ Uncompetitive products or services.

♦ Declining market share.

- Deterioration in physical facilities.
- Over-staffing, high turnover of employees, and low morale.
- Mismanagement.

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. The chain may attempt to leverage the potential Indian market by engaging a new logistics partner. It may bring innovation in food items, as well as quality and improvements in the overall dine-in and delivery experience. During the turnaround, the "product mix" may be changed, requiring the organization to do some repositioning.

A workable action plan for turnaround would involve:

Action plan for turnaround strategy

- Stage One – Assessment of current problems
- Stage Two – Analyze the situation and develop a strategic plan
- Stage Three – Implementing an emergency action plan
- Stage Four – Restructuring the business
- Stage Five – Returning to normal

Question 5

Organo is a large supermarket chain. It is considering the purchase of a number of farms that provides *Organo* with a significant amount of its fresh produce. *Organo* feels that by purchasing the farms, it will have greater control over its supply chain. Identify and explain the type of diversification opted by *Organo*?

Answer

Organo is a large supermarket chain. By opting backward integration and purchase a number of farms, it will have greater control over its supply chain. Backward integration is a step towards, creation of effective supply by entering business of input providers. Strategy employed to expand profits and gain greater control over production 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.

Question 6

Swift Insurance is a company engaged in the business of providing medical insurance maintaining a market share of 25 to 30 per cent in last five years. Recently, the company decided to enter into the business of auto insurance by having foreign collaboration. Identify the strategy being followed by the Swift Insurance with its advantages.

Answer

Overall Swift Insurance is following growth or expansion strategy as it is redefining the business and enlarging its scope. The step will also substantially increase investment in the business.

The new business is related and at the same time caters to a different segment and accordingly can be termed as related diversification. The new business falls within the scope of general insurance and horizontally related to the existing business.

In the process of expansion, the company will be able to exploit:

- Its brand name.
- The marketing skills available.
- The existing sales and distribution infrastructure.
- Research and development.
- Economies of scale

Question 7

With the global economic recession Soft Cloth Ltd. incurred significant losses in all its previous five financial years. Currently, they are into manufacturing of cloth made of cotton, silk, polyster, rayon, lycra and blends. Competition is also intense on account of cheap imports. The company is facing cash crunch and has not been able to pay the salaries to its employees in the current month.

Suggest a grand strategy that can be opted by Soft Cloth Ltd.

Answer

Soft Cloth Ltd. is facing internal as well as external challenges. The external environment is in economic recession and the organization is facing cash crunch. The company needs to work on retrenchment / turnaround strategy. The strategy is suitable in case of issues such as:

- Persistent negative cash flow.
- Uncompetitive products or services
- Declining market share
- Deterioration in physical facilities
- Overstaffing, high turnover of employees, and low morale
- Mismanagement

The company may consider to substantially reduce 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 strategy. If none of these actions work, then it may choose to abandon the activities totally, resulting in a liquidation strategy.

Question 8

Vastralok Ltd., was started as a textile company to manufacture cloth. Currently, they are in the manufacturing of silk cloth. The top management desires to expand the business in the cloth manufacturing. To expand they decided to purchase more machines to manufacture cotton cloth.

Identify and explain the strategy opted by the top management of Vastralok Ltd.

Answer

Vastralok Ltd. is currently manufacturing silk cloth and its top management has decided to expand its business by manufacturing cotton cloth. Both the products are similar in nature within the same inductry. The strategic diversification that the top management of Vastralok Ltd. has opted is concentric in nature. They were in business of manufacturing silk and now they will manufacture cotton as well. They wil be able to use existing infrastructure and distribution channel. Concentric diversification amounts to related diversification.

In concentric diversification, the new business 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.

Question 9

XYZ Co. was formed by the merger between a number of chemical companies. Since it aimed at expanding its presence in a large number of value added specialty chemical operations; within a few years the company involved in activities like bulk chemicals, explosives, fertilizers, paints and commodity plastics. But expanding the scope of business to so many businesses; little it did for the bottom line. On analyzing, the top management found that although many of the businesses were linked in some way to the chemical industry, but there were far fewer synergies among the operations that it had initially thought. The top management explored and concluded that there was little commonality between bulk chemicals and fertilizers, between plastics and paints, between explosives and advanced materials. In other words, the value created by the diversification was questionable. After reading this scenario, what do think has gone wrong in this case? How do you think this problem can be rectified?

Answer

In the present scenario, the problem is related to diversification strategy to expand and mark its presence. Diversification can be either related or unrelated. Related diversification is when the new business 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 related diversification there are benefits of synergy with the current operations as 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.

Whereas, in unrelated diversification, no such linkages exist; the new businesses/ products are disjointed from the existing businesses/products in every way. 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.

In the present case, the company tried to diversify in products like bulk chemicals, explosives, fertilizers, paints and commodity plastics thinking that the diversification is linked in some way to the chemical industry. But when the bottom line did not improve with this diversification; the top management explored and found that there were far fewer synergies among the company's operations that it had initially thought. They was little commonality between bulk chemicals and fertilizers, between plastics and paints, between explosives and advanced materials which means that the company made a dire mistake in understanding whether the diversification was related or unrelated.

The probable solution for this would be breaking up the company into constituent parts; may be two or three and put the related businesses into the relevant SBUs and consider selling off the businesses that are totally unrelated or totally get into unrelated diversification and form a structure accordingly.

Descriptive Questions

Question 10

What is Divestment strategy? When is, it adopted?

Answer

Divestment strategy involves the sale or liquidation of a portion of business, or a major division, profit centre or SBU. For a multiple product company, divestment could be a part of rehabilitating or restructuring plan called turnaround.

- A divestment strategy may be adopted due to various reasons:
- When a turnaround has been attempted but has proved to be unsuccessful.
- 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.
- Severity of competition and the inability of a firm to cope with it.
- Technological upgradation is required if the business is to survive but where it is not possible for the firm to invest in it.
- A better alternative may be available for investment.

Question 11

Write short note on expansion through acquisitions and mergers.

Answer

Acquisitions and mergers are basically combination strategies. Some organizations prefer to grow through mergers. Merger is considered to be a process when two or more companies come together to expand their business operations. In such a case the deal gets finalized on friendly terms and both the organizations share profits in the newly created entity. In a merger two organizations combine to increase their strength and financial gains along with breaking the trade barriers.

When one organization takes over the other organization and controls all its business operations, it is known as acquisition. In this process of acquisition, one financially strong organization overpowers the weaker one. Acquisitions often happen during recession in economy or during declining profit margins. In this process, one that is financially stronger and bigger establishes it power. The combined operations then run under the name of the powerful entity. A deal in case of an acquisition is often done in an unfriendly manner, it is more or less a forced association where the powerful organization either consumes the operation or a company in loss is forced to sell its entity.

Question 12

Distinguish between concentric and conglomerate diversification

Concentric diversification occurs when a firm adds related products or markets. On the other hand, conglomerate diversification occurs when a firm diversifies into areas that are unrelated to its current line of business.

In concentric diversification, the new business is linked to the existing businesses through process, technology or marketing. In conglomerate diversification, no such linkages exist; the new business/product is disjointed from the existing businesses/products.

The most common reasons for pursuing a concentric diversification are that opportunities in a firm's existing line of business are available. However, common reasons for pursuing a conglomerate growth strategy is that opportunities in a firm's current line of business are limited or opportunities outside are highly lucrative.

Question 13

Differentiate between divestment and liquidation strategy.

Answer

Divestment Strategy:	**Liquidation Strategy:**
Divestment strategy involves the sale or liquidation of a portion of business, or a major division, profit center or SBU.	It involves closing down a firm and selling its assets.
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. Option of a turnaround	Liquidation becomes only option in case of severe and critical conditions where either turnaround and divestment are not seen as solution or have been attempted but failed..

may even be ignored if it is obvious that divestment is the only answer.	
Efforts are made for the survival of organization.	Liquidation as a form of retrenchment strategy is considered as the most extreme and unattractive.
Survival of organization helps in retaining personnel, at least to some extent.	There is loss of employment with stigma of failure.

Question 14

Under what conditions would you recommend the use of Turnaround strategy in an organization? What could be a suitable work plan for this?

Answer

Rising competition, business cycles and economic volatility have created a climate where no business can take viability for granted. Turnaround strategy is a highly targeted effort to return an organization to profitability and increase positive cash flows to a sufficient level. Organizations that have faced a significant crisis that has negatively affected operations requires turnaround strategy. Turnaround strategy is used when both threats and weaknesses adversely affect the health of an organization so much that its basic survival is a question. When organization is facing both internal and external pressures making things difficult then it has to find something which is entirely new, innovative and different. Being organization's first objective is to survive and then grow in the market; turnaround strategy is used when organization's survival is under threat. Once turnaround is successful the organization may turn to focus on growth.

Conditions for turnaround strategies: When firms are losing their grips over market, profits due to several internal and external factors, and if they have to survive under the competitive environment they have to identify danger signals as early as possible and undertake rectification steps immediately. These conditions may be, inter alia, cash flow problems, lower profit margins, high employee turnover and decline in market share, capacity underutilization, low morale of employees, recessionary conditions, mismanagement, raw material supply problems and so on.

Action plan for turnaround strategy

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.

The 'people mix' is another important ingredient in the organization's competitive effectiveness. Reward and compensation systems that encourage dedication and creativity encourage employees to think 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.

Question 15

What strategic option is available to the management of a sick company dealing in an electric home appliances? Give reasons for your answer.

Answer

A sick company has huge accumulated losses that have eroded its net worth. The electric home appliance company may analyse its various products to take decisions on the viability of each.

Retrenchment becomes necessary for coping with hostile and adverse situations in the environment and when any other strategy is likely to be suicidal. The nature, extent and timing of retrenchment are matters to be carefully decided by management, depending upon each contingency.

Retrenchment strategy is adopted because:

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

Retrenchment strategy 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.

Turnaround strategy: If the organization chooses to transform itself into a leaner structure and focuses on ways and means to reverse the process of decline, it adopts a turnaround strategy. It may try to reduce costs, eliminate unprofitable outputs, generate revenue, improve coordination, better control, and so on. It may also involve changes in top management and reorienting leadership.

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.

Liquidation Strategy: In the retrenchment strategy, the most extreme and unattractive is liquidation strategy. It 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.

Liquidation strategy may be unpleasant as a strategic alternative but when a "dead business is worth more than alive", it is a good proposition.

The management of a Sick company manufacturing various electrical home appliances be explained about the each of the above three options of retrenchment strategy with their pros and cons. But the appropriate advice with respect to a particular option of retrenchment strategy will depend on the specific circumstances of each electrical home appliances and management goals of the company.

Question 16

What are acquisitions? Discuss with example of two companies resorting to this strategy?

Answer

Acquisition of 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 denote that the positive effects of the merged resources are greater than the some of the effects of the individual resources before merger or acquisition.

Some of the recent / popular instances of acquisition are listed below:

- ♦ Tata's acquisition of Anglo Dutch steelmaker Corus
- ♦ Tata's acquisition of British Jaguar Land Rover
- ♦ Mittal Steel's takeover of Arcelor
- ♦ HPCL's acquisition of Kenya Petroleum Refinery Ltd.
- ♦ Hindalco's acquisition of Canada based Novelis