Strategic Management

Lectures 2 and 3
Types of Strategies

Learning Objectives

- Identify and discuss eight characteristics of objectives and ten benefits of having clear objectives
- Define and give an example of eleven types of strategies
- Identify and discuss the three types of “Integration Strategies”
- Discuss when market penetration, market development, and product development are especially effective strategies
- Explain when diversification is an effective business strategy
- List guidelines for when retrenchment, divestiture, and liquidation are especially effective strategies
- Identify and discuss Porter’s five generic strategies
- Compare (a) cooperation among competitors, (b) joint venture and partnering, and (c) merger/acquisition as key means for achieving strategies
- Discuss tactics to facilitate strategies, such as (a) being a first mover, (b) outsourcing, and (c) reshoring
- Explain how strategic planning differs in for-profit, not-for-profit, and small firms

Topics

- Long-Term Objectives
  - Characteristics and Benefits of Objectives
  - Financial versus Strategic Objectives
  - Avoid Not Managing by Objectives
- Types of Strategies
  - Integration Strategies
  - Intensive Strategies
  - Diversification Strategies
  - Defensive Strategies
  - Michael Porter's Five Generic Strategies
- Means for Achieving Strategies
- Tactics to Facilitate Strategies
- Strategic Management in Nonprofit, Governmental, and Small Firms

Long-Term Objectives

- Long-Term Objectives represent the results expected from pursuing certain strategies
- Strategies represent the actions to be taken to accomplish long-term objectives
- The time frame for objectives and strategies should be consistent, usually from 2 to 5 years
- Long-term objectives are needed at the corporate, divisional, and functional levels of an organization
- They are an important measure of managerial performance

Long-Term Objectives …

Characteristics and Benefits of Objectives

- Quantitative
- Measurable
- Realistic
- Understandable
- Challenging
- Hierarchical
- Obtainable
- Congruent among organizational units

Long-Term Objectives …

Financial versus Strategic Objectives

- Financial examples:
  - Growth in revenues
  - Growth in earnings
  - Higher dividends
  - Larger profit margins
  - Greater return on investment
  - Higher earnings per share
  - A rising stock price
  - Improved cash flow
- Strategic examples:
  - Larger market share
  - Quicker on-time delivery than rivals
  - Shorter design-to-market times than rivals
  - Lower costs than rivals
  - Higher product quality than rivals
  - Wider geographic coverage than rivals
  - Achieving technological leadership
  - Consistently getting new or improved products to market ahead of rivals

Long-Term Objectives …

Benefits of clear objectives:

1. Provide direction by revealing expectations
2. Allow synergy
3. Assist in evaluation by serving as standards
4. Establish priorities
5. Reduce uncertainty
6. Minimize conflicts
7. Stimulate exertion
8. Aid in allocation of resources
9. Aid in design of jobs
10. Provide basis for consistent decision making

Long-Term Objectives …

Avoid Not Managing by Objectives

<u>You should avoid</u>

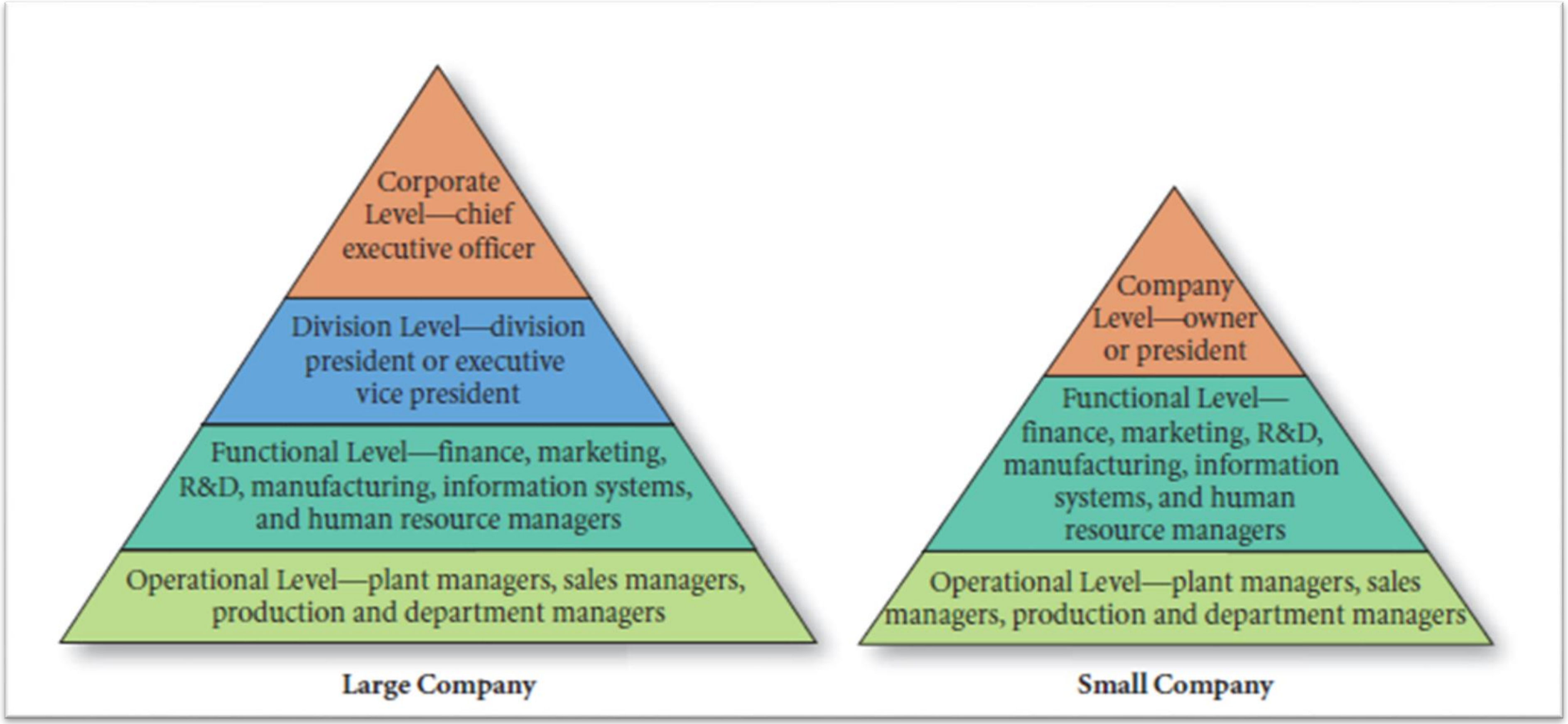
- Managing by Extrapolation
  "If it ain't broke, don't fix it"
- Managing by Crisis
  Letting events dictate the what and when of management decisions
- Managing by Subjectives
  "Do your own thing, the best way you know how"
- Managing by Hope
  Good times are just around the corner

Types of Strategies

TABLE 4-4 Alternative Strategies Defined and Recent Examples Given

Strategy	Definition	Example
Forward Integration	Gaining ownership or increased control over distributors or retailers	Amazon began rapid delivery services in some U.S. cities.
Backward Integration	Seeking ownership or increased control of a firm's suppliers	Starbucks purchased a coffee farm.
Horizontal Integration	Seeking ownership or increased control over competitors	BB&T acquired Susquehanna Bancshares.
Market Penetration	Seeking increased market share for present products or services in present markets through greater marketing efforts	Under Armour signed tennis champion Andy Murray to a 4-year, $23 million marketing deal.
Market Development	Introducing present products or services into new geographic area	Gap opened its first five stores in China.
Product Development	Seeking increased sales by improving present products or services or developing new ones	Amazon just began offering its own line of baby diapers and wipes.
Related Diversification	Adding new but related products or services	Facebook acquired the text-messaging firm WhatsApp for $19 billion.
Unrelated Diversification	Adding new, unrelated products or services	Kroger and Whole Foods Market are cooking meals, becoming restaurants.
Retrenchment	Regrouping through cost and asset reduction to reverse declining sales and profit	Staples closed 250 stores and reduced by 50% the size of other stores.
Divestiture	Selling a division or part of an organization	Sears Holdings divested its Land's End division to Sears' shareholders.
Liquidation	Selling all of a company's assets, in parts, for their tangible worth	The Trump Taj Mahal in Atlantic City, New Jersey, faces liquidation.

Types of Strategies …



Levels of Strategies

Types of Strategies ...

- Forward Integration
- Backward Integration
- Horizontal Integration

Integration Strategies

- Market Penetration
- Market Development
- Product Development

Intensive Strategies

- Related Diversification
- Unrelated Diversification

Diversification Strategies

- Retrenchment
- Divestiture
- Liquidation

Defensive Strategies

Types of Strategies …

When to Choose Forward Integration

- Present distributors are especially expensive, unreliable, or incapable of meeting the firm's distribution needs
- The availability of quality distributors is so limited
- Industry is growing and is expected to continue to grow markedly
- The organization has both the capital and human resources needed to manage the new business of distributing its own products
- The advantages of stable production are particularly high
- Present distributors or retailers have high profit margins

When to Choose Backward Integration

- Present suppliers are especially expensive, unreliable, or incapable of meeting the firm's needs for parts, components, assemblies, or raw materials
- The number of suppliers is small and the number of competitors is large
- Industry that is growing rapidly
- The organization has both the capital and human resources needed to manage the new business of supplying its own raw materials
- The advantages of stable prices are particularly important
- Present suppliers have high profit margins
- The organization needs to quickly acquire a needed resource

Types of Strategies …

When to Choose Horizontal Integration

- The organization can gain monopolistic characteristics in a particular area or region without being challenged for "tending substantially" to reduce competition
- Growing industry
- Increased economies of scale provide major competitive advantages.
- The organization has both the capital and human talent needed to successfully manage an expanded organization
- Competitors are faltering as a result of a lack of managerial expertise or a need for particular resources that an organization possesses

When to Choose Market Penetration

- Current markets are not saturated with a particular product or service
- The usage rate of present customers could be increased significantly
- The market shares of major competitors have been declining while total industry sales have been increasing
- The correlation between dollar sales and dollar marketing expenditures historically has been high
- Increased economies of scale provide major competitive advantages

Types of Strategies …

When to Choose Market Development

- New channels of distribution are available that are reliable, inexpensive, and of good quality
- The organization is successful at what it does
- New untapped or unsaturated markets exist
- The organization has the needed capital and human resources to manage expanded operations
- The organization has excess production capacity
- The organization's basic industry is rapidly becoming global in scope

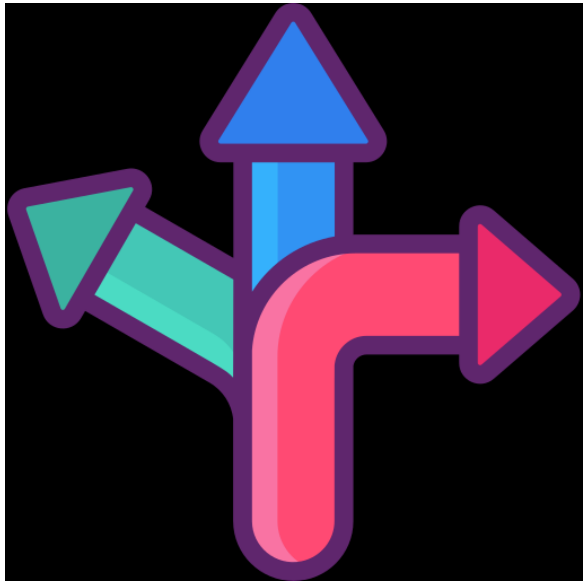
When to Choose Product Development

- The organization has successful products that are in the maturity stage of the product life cycle; the idea here is to attract satisfied customers to try new (improved) products as a result of their positive experience with the organization's present products or services
- The organization competes in an industry that is characterized by rapid technological developments
- Major competitors offer better-quality products at comparable prices
- The organization competes in a high-growth industry
- The organization has especially strong research and development capabilities

Types of Strategies …

<u>When to choose Related Diversification</u>

- The organization competes in a no-growth or a slow-growth industry
- Adding new, but related, products would significantly enhance the sales of current products
- New, but related, products could be offered at highly competitive prices
- New, but related, products have seasonal sales levels that counterbalance the organization’s existing peaks and valleys
- The organization’s products are currently in the declining stage of the product’s life cycle
- The organization has a strong management team



Types of Strategies …

When to Choose Unrelated Diversification

- Revenues derived from an organization's current products or services would increase significantly by adding the new, unrelated products
- The organization competes in a highly competitive or a no-growth industry, as indicated by low industry profit margins and returns
- The organization's present channels of distribution can be used to market the new products to current customers
- New products have countercyclical sales patterns compared to the organization's present products.
- The organization's basic industry is experiencing declining annual sales and profits
- The organization has the capital and managerial talent needed to compete successfully in a new industry
- The organization has the opportunity to purchase an unrelated business that is an attractive investment opportunity
- Financial synergy exists between the acquired and acquiring firm. (Note that a key difference between related and unrelated diversification is that the former should be based on some commonality in markets, products, or technology, whereas the latter is based more on profit considerations)
- Existing markets for an organization's present products are saturated
- Antitrust action could be charged against the organization that historically has concentrated on a single industry

Types of Strategies …

When to Choose Retrenchment

- The organization has a clearly distinctive competence but has failed consistently to meet its objectives and goals over time
- The organization is one of the weaker competitors in a given industry
- The organization is plagued by inefficiency, low profitability, poor employee morale, and pressure from stockholders to improve performance
- The organization has failed to capitalize on external opportunities, minimize external threats, take advantage of internal strengths, and overcome internal weaknesses over time; that is, when the organization's strategic managers have failed (and possibly will be replaced by more competent individuals)
- The organization has grown so large so quickly that major internal reorganization is needed

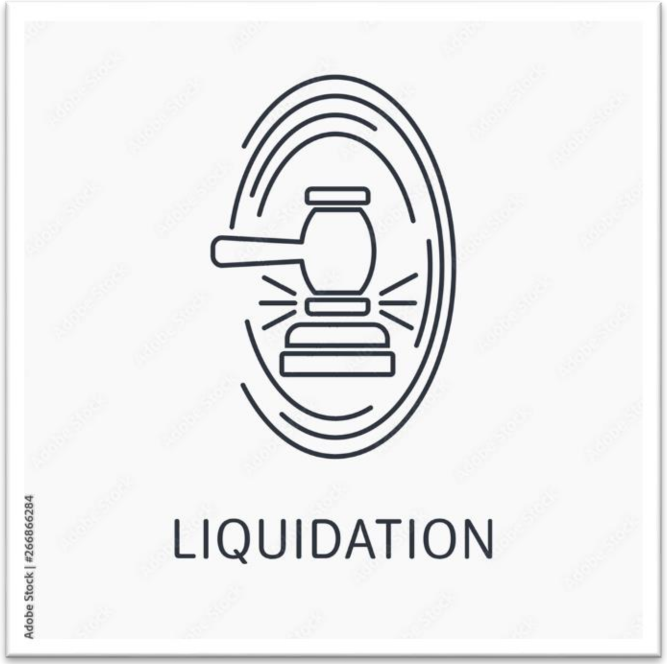
When to Choose Divestiture

- The organization has pursued a retrenchment strategy and failed to accomplish needed improvements
- To be competitive, a division needs more resources than the organization can provide
- A division is responsible for an organization's overall poor performance
- A division is a misfit with the rest of the organization; this can result from radically different markets, customers, managers, employees, values, or needs
- A large amount of cash is needed quickly and cannot be obtained reasonably from other sources
- Antitrust action threatens the organization

Types of Strategies …

<u>When to Choose Liquidation</u>

- The organization has pursued both a retrenchment strategy and a divestiture strategy, and neither has been successful
- The organization's only alternative is bankruptcy. Liquidation represents an orderly and planned means of obtaining the greatest possible amount of cash for an organization's assets. A company can legally declare bankruptcy first and then liquidate various divisions to raise needed capital
- The stockholders of a firm can minimize their losses by selling the organization's assets



Types of Strategies …

Type 1: Cost Leadership—Low Cost
Type 2: Cost Leadership—Best Value
Type 3: Differentiation
Type 4: Focus—Low Cost
Type 5: Focus—Best Value

GENERIC STRATEGIES

SIZE OF MARKET	Cost Leadership	Differentiation	Focus
Large	Type 1 Type 2	Type 3	—
Small	—	Type 3	Type 4 Type 5

FIGURE 4-3

Porter's Five Generic Strategies

Types of Strategies …

When to Choose Porter’s Type 1 or Type 2 Cost Leadership Strategy

- Price competition among rival sellers is especially vigorous
- Products of rival sellers are essentially identical and supplies are readily available from any of several eager sellers
- There are few ways to achieve product differentiation that have value to buyers
- Most buyers use the product in the same ways
- Buyers incur low costs in switching their purchases from one seller to another
- Buyers are large and have significant power to bargain down prices
- Industry newcomers use introductory low prices to attract buyers and build a customer base

When to Choose Porter’s Differentiation Strategy Type 3

- There are many ways to differentiate the product or service and many buyers perceive these differences as having value
- The buyer’s needs and uses are diverse
- Few rival firms are following a similar differentiation approach
- Technological change is fast paced and competition revolves around rapidly evolving product features

Types of Strategies …

<u>When to Choose Porter's Focus Strategy (Type 4 or Type 5)</u>

- The target market niche is large, profitable, and growing
- Industry leaders do not consider the niche to be crucial to their own success
- Industry leaders consider it too costly or difficult to meet the specialized needs of the target market niche while taking care of their mainstream customers
- The industry has many different niches and segments, thereby allowing a focuser to pick a competitively attractive niche suited to its own resources
- Few, if any, other rivals are attempting to specialize in the same target segment

Means for Achieving Strategies

- **Cooperation among Competitors**
  For collaboration between competitors to succeed, both firms must contribute something distinctive, such as technology, distribution, basic research, or manufacturing capacity
- **Joint Venture and Partnering**
  Joint venture is a popular strategy that occurs when two or more companies form a temporary partnership or consortium for the purpose of capitalizing on some opportunity
- **Merger/Acquisition**
  A merger occurs when two organizations of about equal size unite to form one enterprise whereas an acquisition occurs when a large organization purchases (acquires) a smaller firm
- **Private-Equity Acquisitions**
  Private equity firms are an integral part of the business world, especially in the United States but also in Europe, Asia, and, more recently, Latin America

Tactics to Facilitate Strategies

- **First Mover Advantages**
  First mover advantages refer to the benefits a firm may achieve by entering a new market or developing a new product or service prior to rival firms
- **Outsourcing and Reshoring**
  - Outsourcing involves companies hiring other companies to take over various parts of their functional operations, such as human resources, information systems, payroll, accounting, customer service, and even marketing
  - Reshoring is the new term that refers to U.S. companies planning to move some of their manufacturing back to the United States
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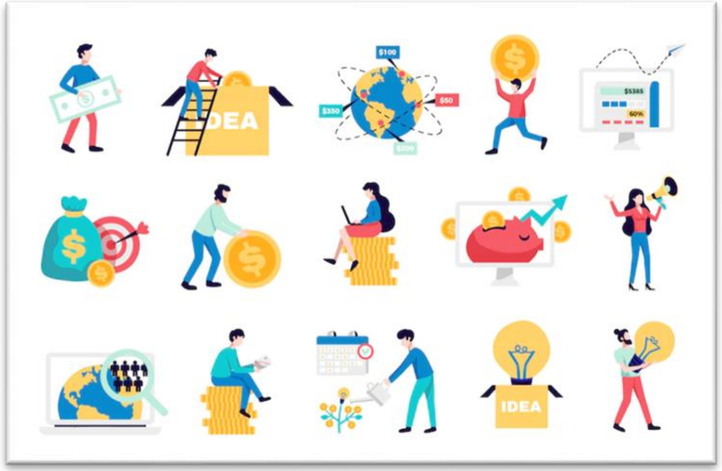
Strategic Management in Nonprofit, Governmental, and Small Firms

- Nonprofits do not pay taxes
- Nonprofits do not have shareholders to provide capital
- Nonprofit organizations embrace strategic planning just as much as for-profit firms, and perhaps even more, because equity capital is not an alternative source of financing
- Many nonprofit and governmental organizations outperform private firms and corporations on innovativeness, motivation, productivity, and strategic management
- Nonprofits and governmental organizations owe it to their constituencies to garner and use monies wisely; that requires excellent strategy formulation, implementation, and evaluation



Strategic Management in Nonprofit, Governmental, and Small Firms …

Educational Institutions

- The world of higher education is rapidly moving to online courses and degrees
- All institutions of higher learning need an excellent strategic plan to survive and prosper

Medical Organizations

- Many private and state-supported medical institutions are in financial trouble as a result of traditionally taking a reactive rather than a proactive approach in dealing with their industry
- Hospitals are beginning to bring services to the patient as much as bringing the patient to the hospital; health care is more and more being concentrated in the home and in the residential community rather than on the hospital campus

Governmental Agencies and Departments

- Strategic-management concepts are generally required and thus widely used to enable governmental organizations to be more effective and efficient
- Strategists in governmental organizations operate with less strategic autonomy than their counterparts in private firms
- Public enterprises generally cannot diversify into unrelated businesses or merge with other firms

Strategic Management in Nonprofit, Governmental, and Small Firms …

Key Attributes of Great Entrepreneurs

- They possess a high level of deliberate practice
    - ✓ Examining yourself as a person, your competition, and a wide array of factors related to the entrepreneurial endeavor at hand
- Several antecedents of deliberate practice include:
    - ✓ Strong motivation
    - ✓ Self-efficacy
    - ✓ Self-discipline
    - ✓ Delayed gratification
    - ✓ Self-control
    - ✓ Determination
    - ✓ Strong work ethic
    - ✓ Goal-oriented
    - ✓ Dedication
    - ✓ Time management
    - ✓ ”Being on a mission”
- Deliberate practice entails working “hard and smart” simultaneously; it is all about developing and utilizing a strategic mental approach to the endeavor at hand, rather than having a special innate talent or gaining 20 years of experience

THANK YOU