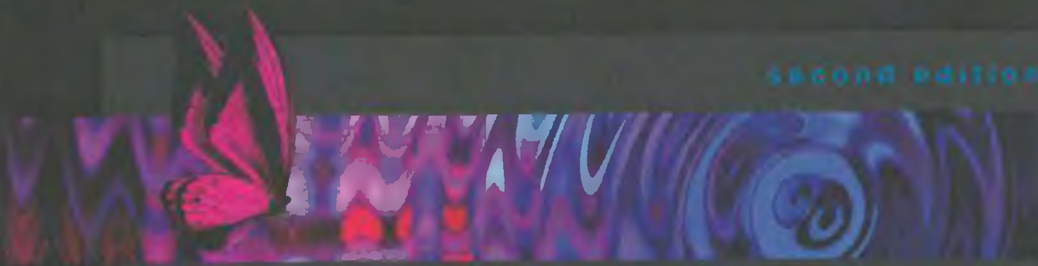
second edition



Practising Strategy

A southern African context

There are a number of strategy books, international and local, available in the South African market. Why another one? What makes this book different?

FIVE KEY APPROACHES:

- This publication focuses on **strategy implementation** and not just on the thinking and analytical aspects of strategic management.
- It explores the idea that strategy is often **emergent, messy and experimental**, unlike other strategic management books, which unrealistically portray it as a neat, analytical and rational process.
- It unpacks the recent concept that other strategists, **not only just senior management**, influence strategic direction.
- It recognises **strategy as something people do** rather than something an organisation possesses. Since people are building blocks of strategy, it is a cognitive and political activity.
- It **uses primary research** conducted among southern African top and middle managers and draws on these managerial perspectives to enrich the text with first-hand accounts of strategy experience.

The second edition of the book features a number of new chapters, focusing on strategy implementation and change management, resource allocation and responsible leadership. It also includes a more detailed coverage of managing strategic risk.

PIET VENTER is a Professor of Strategy at the University of South Africa's Graduate School of Business Leadership (the SBL). He holds an MBA from the University of Pretoria, and a Doctor of Commerce in Business Management from the University of South Africa. In addition to his more than 20 years' experience in teaching and supervising postgraduate students in management and strategy, Prof Venter has considerable practical experience in the telecommunications industry, and has worked on many strategic projects in various private and public organisations. He has published widely in the areas of strategy and strategic marketing.

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A southern African context

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Practising Strategy

A southern African context

Peet Venter & Tersia Botha (eds)

second edition

Practising Strategy

A southern African context

Second edition

Editors
Tersia Botha and Peet Venter

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Preface

A question that I was asked often when writing and compiling this book (and that, in all honesty, I had asked myself more than once) was: why another strategy book? There were, after all, quite a number of books, international and local, already available on the South African market. It became clear that we had to position this book definitively to make a unique contribution to the extant body of knowledge.

So how, then, is this book different? We believe that there are five key aspects:

- A cursory review of strategic management books shows that the focus is very strongly on the process of strategy formulation, i.e. the thinking and analytical aspects of strategic management, as opposed to the 'doing' part of strategy, which is often dealt with in one or two chapters towards the end. Given that it is the greatest challenge to managers in the 21st century and the greatest reason for strategy failure, we decided to focus on **strategy implementation** instead.
- Most strategic management books portray strategic management as a neat, analytical and rational process that flows from top to bottom in the organisation. Rather than promoting the unrealistic idea of strategy as a purely rational and deliberate outcome, we acknowledge and explore the idea that strategy is often **emergent, messy and experimental**, and above all a **human activity**.
- Top management has long been regarded as the custodians of strategy. The idea that there are **other strategists** (human and non-human actors) such as middle managers and consultants that influence the strategic direction of the organisation and distribution of resources emerged only relatively recently, and we include this factor.
- We focus on strategy as something that people 'do' rather than something that an organisation 'possesses'. Since people are the building blocks of strategy, we recognise that strategy is both a **cognitive and political activity.**
- Most South African textbooks rely on secondary sources. While we use recent secondary sources from the extant body of knowledge, we conducted **primary research** among southern African top and middle managers and drew on these managerial perspectives to enrich our material with firsthand accounts of the strategy experience.

We trust that you will find value in the contemporary and different perspectives we present in this book.

Peet Venter

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Professor Tersia Botha teaches Strategy, General Management, Finance and Entrepreneurship for the past 27 years at the University of South Africa. She authored, co-authored and acted as editor of numerous academic books in the field of Leadership, Corporate Citizenship, General Management, Strategy, Business Management by Portfolio. She published articles in accredited peer reviewed academic journals and presented papers at international and national conferences. Prof Botha has been involved in many community engagement projects for the past 25 years, most notably the partnership with Education Africa and the Davis and Dean Youth Development Programme.

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1 The relationship between general management principles and strategic management

Tersia Botha

LEARNING OUTCOMES

After studying this chapter, you should be able to:

LO 1: Explain the concepts 'manager' and 'management'.

LO 2: Explain the management process, indicating the four characteristics thereof.

LO 3: Differentiate between the various levels of management.

LO 4: Explain the various areas of management.

LO 5: Explain the hierarchy of organisational plans and depict it diagrammatically.

LO 6: Explain the composition of the management environment.

LO 7: Explain the terms 'stakeholder' and 'stakeholder relationship management'.

LO 8: Differentiate between the terms 'competitive advantage', 'sustainable competitive advantage' and 'transient competitive advantage'.

KEY WORDS

- Areas of management
- Competitive advantage
- Effectiveness
- Efficiency
- Leading
- Lower management
- External environment
- Management functions
- Management process
- Management
- Manager
- Market environment
- Micro-environment
- Middle management
- Objective
- Operational plans
- Organising
- Planning

- Remote environment
- Resources
- Stakeholder
- Strategic plan
- Sustainable competitive advantage
- Tactical plan
- Top management
- Transient competitive advantage

CHAPTER ORIENTATION

Why do business organisations exist? Take a few moments to ponder this question. Business organisations exist for various reasons. Entrepreneurs generate new business ideas, determine the feasibility and viability of these ideas and start new business ventures, in which resources are transformed into need-satisfying products and services, which are then sold to customers. The entrepreneur hopefully realises a profit, of which a part thereof is reinvested in the business organisation in order to grow and develop the business, ensure its long-term survival, create jobs, contribute to the wealth and wellbeing of society and remunerate the owners for the investment made in the organisation. As the business grows, the role of the entrepreneur changes from being the inventor of new ideas, to the manager of the business organisation. The bigger the organisation becomes, the more complicated the management process becomes, which bring us to the next fundamental question – what is the best way to manage an organisation?

When we study the evolution of management theory, this is the one recurring theme that management theorists attempt to answer. Do a quick Google search for the best way to manage an organisation. You will find thousands of views on this topic – ranging from 'tips to manage a small business' to 'how to manage a big corporate effectively and efficiently'. The reason for the numerous views on this topic is to enable us to see the proposed 'best' way to manage a business organisation in the context of the social, political, economic, technological, international, and ecological forces that affect organisations and society at a specific time. As these forces change (and they change constantly and at an accelerating pace), business managers need to change and adapt to changing circumstances in the management environment. Changing circumstances lead to great uncertainties for businesses, particularly in respect of their sustainability and management.

The opening case provides us with an example of a highly successful organisation that did extremely well on ground level – there were 88 Health and Racquet Clubs in South Africa and 22 abroad, realising a turnover in excess of R1 billion in December 1999, with after-tax profits of R100 million per annum. The company employed thousands of people and had a membership in excess of one million. In spite of its good financial performance, the company failed. Why? Firstly, the reason for the company's failure can be ascribed to a lack of strategic management. The company's board, which is mainly responsible for strategic management and leadership, became dysfunctional, resulting in a company that lacked strategic direction, a coherent strategic plan, and an effective and efficient management team to implement the strategic plans, and well-formulated action plans. Lastly, poor and ineffective communication, with little concern for corporate governance, led to the failure of the company.

The purpose of this book is to provide the reader with the necessary background and information, to be able to practise strategy successfully in the contemporary business environment. Essentially this means to:

> *develop a long-term and coherent strategic plan within the opportunities and constraints of the business environment, that leads to the development of strategic actions that need to be implemented and controlled, that will put the organisation in a position of advantage and enable it to survive over the long term and realise its long-term vision, goals and plans.*

Before we can focus on practising strategy, we first need to address the relationship between general management and strategic management. This chapter will commence with an explanation of managers, management and the management process, the various levels and areas of management, followed by an explanation of the hierarchy of organisational plans. Thereafter, we will focus on the composition of the management environment, stakeholder and stakeholder relationship management. Finally, competitive advantage, sustainable competitive advantage and transient competitive advantage will be addressed.

Case study

LeisureNet – Death of a business

For a few weeks in September and October 2000, Peter Flack was the interim chief executive officer of the ill-fated South African company LeisureNet. He had been called in as a turnaround specialist. He found that the company had deteriorated so far and so fast that all that could be done for it was to close it.

LeisureNet was a large business, but the lessons Flack draws from the LeisureNet failure need to be learned by every manager. Flack's account of one of South Africa's most spectacular corporate failures is briefly provided below.

Every organisation, whether it be a club, church, company or country, requires four basic ingredients for it to be successful. These are leadership, a strategic plan, a management team capable of implementing the strategy, and an action plan which breaks the strategic plan down into measurable bits. A business is measured against these factors.

LeisureNet, a successful and profitable company, invited one of the directors of Coronation FRM to sit on their board. A brief look at the results for the year to December 1999 showed a group with a turnover in excess of R1 billion and which made in excess of R100 million after tax per annum. As a rough rule of thumb, companies that produce after-tax profits equal to 10 per cent of gross revenue are considered healthy businesses.

The company operated 85 Health and Racquet (H&R) Clubs in South Africa and employed 4,500 people who provided an excellent service to nearly one million club members. In addition, the company expanded offshore and had built 22 H&R Clubs in Australia, Britain, Germany and Spain, with a number being in the process of construction. On the surface, LeisureNet was a company with strong leadership, a clear strategy and an obviously competent management team.

At the first board meeting that Flack attended, it was clear that the board had become dysfunctional and there was conflict between the executive and non-executive directors. The previous joint chief executive officer of LeisureNet had been transferred to Healthland International Limited (again as joint chief executive officer). Healthland International Limited was a company that operated health and fitness clubs in Australia. The previous leaders had sold almost all their interests in LeisureNet and had been awarded a substantial and meaningful stake, free of charge, in Healthland International Limited. LeisureNet's young managing director of the South African operations had been approached to take the job as CEO of LeisureNet but had not accepted the position, and the terms of his appointment had not been finalised. It was clear that there was a problem with leadership.

Part of the conflict at board level was due to the fact the LeisureNet had been used to fund, staff and train employees of Healthland. The H&R Club business had been pillaged to establish Healthland's operations and all available cash had been invested in Healthland and little, if any, in the H&R Club business. Some R370 million of this available cash had come from selling shares. The result was a lack of maintenance and refurbishment at H&R Clubs.

On closer examination, there was no strategic plan. A strategy, which is not reduced to writing, is a hope, wish or prayer, but not a plan. A strategic plan requires that its participants follow a procedure, which identifies and analyses the various internal and external issues that affect the business.

The lack of a coherent strategic plan in LeisureNet can be seen from the fact that the company had over the previous five years, when it was still in business, also established a food business, a golfing business, an education business, a casino bid, a gymnasium equipment supplier, a restaurant and the six-member Imax theatre chain. Despite the fact that LeisureNet owned only half the equity of the Imax group, the company guaranteed 100 per cent of the leases of the purpose-built facilities housing the theatres and which extended over 13–20 years.

Structure follows strategy and the lack of strategy manifested itself in the composition of the board of directors of LeisureNet. Instead of the various disciplines inherent in a company being represented on the board of directors, for example, finance, information systems, human resources and the line operations, the board consisted of two former joint chief executive officers, the managing director of the local operations and a host of non-executive directors.

Although the management information system was homegrown and, in many instances, required a duplication of effort, the accounting system, sales system, marketing and human resources procedures were well thought out. In moving offshore with Healthland International Limited, the business there had adopted the best of the local operating systems, acquired a standard management information system and had recruited the most senior of the local managers. The glaring omission, however, related to the position of chief financial officer and the treasury and cash management functions for this massively cash-hungry growth business in a state of rapid development. Ultimately, this gap in the management structure caused the downfall of Healthland as there was no action plan of any kind.

The group, with the notable exception of the H&R Club business, did not meet, let alone pass, any of the standards required by the four components for any successful business, namely, leadership, strategic planning, management and action planning. There were two other glaring omissions, namely, a lack of corporate communications and corporate governance.

The group could have been saved had it been possible to raise sufficient money to complete the building of the Healthland clubs under construction, or if the sale of these offshore clubs could have been concluded in a way that would have released LeisureNet from its obligations to the Healthland group. In the end, both attempts failed. Both of these failures can be traced back to fundamental flaws in the issues of leadership, strategy, corporate communications and corporate governance.

Source: Adapted from Flack, P. 2001. 'Death of a Business'. *Succeed Magazine*, June/July.

LO 1: Explain the concepts 'manager' and 'management'.

1.1 Managers and management

Although the term 'manager' has many meanings, for the purpose of this chapter, we will define a manager as a person who is responsible for running a part of or an entire organisation. The term 'management' refers to the interlocking functions that managers perform. For the purposes of this book, management is defined as:

> *the process of working with and through others to achieve organisational objectives in a changing environment.*

Managers experience more pressure today than at any other time in history. Changes in the world that are impacting on managers include the growing globalisation of economies, technological innovations, trends towards democratisation, increasing social imbalances and climate change, to mention only a few. In South Africa, the credit rating agency S&P Global downgraded the country's credit rating in November 2017 to full junk status, while its counterpart Moody's placed the country on review for a downgrade. The downgrading followed a similar announcement by third major rating agency Fitch, affirming South Africa's rating at sub-investment or so-called 'junk status'. The reason for the downgrade by this agency was the weak economic growth in the country that led to the deterioration of public finances beyond previous expectations. It also flagged the role that the political turmoil of the country played in hamstringing policy.[1] Having a credit rating at sub-investment level means that South Africa is not regarded as a country with good investment opportunities and investors will be hesitant to invest money in the country's private and public sectors – resulting in a slower economic growth rate, a lower gross national product, and a threat to business managers.

Business managers need to cope with diverse and far-reaching challenges such as these constantly. They have to keep pace with ever-advancing technology and find ways to incorporate the internet and e-business into their strategies and business models. They must strive to remain competitive in the face of increasingly tough global competition, uncertain environments, cutbacks in personnel and resources, and massive economic, political and social shifts. The diversity of the workforce creates other dynamics: How can managers maintain a strong corporate culture while supporting diversity, balancing work and family concerns, and coping with the conflicting demands of all employees for a fair chance at power and responsibility? The field of management is undergoing a revolution that requires managers to do more with less, to see change rather than stability as the nature of things, and to create a vision and cultural values that enable people to create a truly collaborative and enabling workplace.

Successful organisations don't just happen; they are managed to be that way. To be successful under such circumstances, every organisation needs skilled managers. In our opening case, we saw a once successful organisation that closed due to poor management and more specifically, poor strategic management.

The question that we can ask ourselves now is what should managers do to achieve organisational objectives as effectively and efficiently as possible within a changing environment? The objective of this chapter is to provide the reader with a contemporary view of general management principles and the application thereof in modern organisations, and to demonstrate the relationship between these general management principles and strategic management. This will lay the foundation for the contemporary strategic management principles that will be discussed in the remainder of the book. Everything addressed in subsequent chapters of this book relates to practising strategy in contemporary organisations and the job of the modern strategist.

LO 2: Explain the management process, indicating the four characteristics thereof.

1.2 The management process

For the purposes of this book, management is defined as:

> *the process of working with and through others to achieve organisational objectives in a changing environment.*

Although this may seem to be a very simplistic definition, we can identify four major characteristics, namely:

(1) management is a process
(2) management entails working with and through others
(3) management aims to contribute to the realisation of organisational goals and objectives, and in doing so, management needs to balance effectiveness and efficiency and makes the most of limited and scarce resources
(4) management needs to cope with a changing environment.

Each of these components will be discussed in more detail below.

1.2.1 Management is a process

In general, a process can be described as a structured, interrelated set of activities that, when executed, produce a specific output. The management function in an organisation can also be viewed as a process.

Managers need certain inputs (or resources) to deliver certain outputs (or performance). Managers need people (human resources); capital (financial resources), physical resources, raw materials, components, information, and entrepreneurial and management skills to produce products and/or services, create jobs, make a profit, achieve organisational goals and add value, and contribute to the wealth of society. The transformation of inputs to outputs requires management to perform certain activities or functions. All managers, regardless of the type of organisation, the level at which they are involved, their designated role(s) or specific skills, engage in some manner in four fundamental, interrelated activities in order to achieve some or other goal(s), also called the management functions. These functions are planning, organising, leading, and controlling.

- Planning is the management function that determines the organisation's vision, mission, strategic direction and goals. It involves identifying ways of realising the goals, adding value to the organisation and its stakeholders and finding the resources needed for the task within a complex environment. Plans are mostly made by top management and its duration varies from one to five or even ten years. These are called 'strategic plans'. Tactical plans are made by functional managers (such as financial, human resources, research and development, marketing and operations managers) to support the organisation's long-term plans. Operational plans are made by lower management (often called 'first-line' or 'supervisory' management) to plan for short periods ahead. Planning has a top-down nature in organisations, originating from top management and cascading down to lower levels of management and even at the level of the individual worker in an organisation.
- Organising is the second step in the management process. Once the goals and plans have been determined, management has to allocate the organisation's resources to relevant departments or individuals. Tasks, roles and responsibilities must be defined and policies and procedures established to achieve the goals. Thus, organising involves developing a framework or organisational structure to indicate how people and other resources should be deployed to achieve the goals. The success of an organisation lies in directing the different resources towards the achievement of a common set of goals. The better the resources are co-ordinated and organised, the more successful the organisation will be. Because organisations have different goals and resources, it stands to reason that each one should have an organisational structure that will accommodate its needs. Management must match the organisation's structure to its strategies. This process is called 'organisational design'.
- Managers are responsible for getting things done through other people – they collaborate with their superiors, peers and subordinates, with both individuals and groups, to attain the goals of the organisation. Leading the organisation entails using influence and power to motivate employees to achieve goals. Leading from the top means communicating strategic goals and motivating departments, sections and individuals to perform as well as they can.
- Controlling means that managers should constantly make sure that the organisation is on the right course to attain its goals. Control also enables management to identify and rectify any deviations from the plans, and to consider factors which might oblige them to revise their goals and plans.

It is important to realise that the functions of management do not occur in a tidy, step-by-step order. At any given time, a manager is likely to be engaged in several management functions simultaneously.

While performing the planning, organising, leading and controlling functions, managers are constantly faced with opportunities and threats that need to be addressed and decisions that need to be made. When planning, a manager needs to make decisions about goals and when, where and how they should be realised. When controlling, the manager may find out that the goals have not been realised. Thus, a problem exists that needs to be solved and the manager needs to decide on the most appropriate course of action. When organising, managers must make decisions that involve the creation of an organisational structure and the deployment of resources that will enable the organisation to attain its goals. When leading, the manager must decide how to influence and direct the behaviour of followers so that they willingly pursue the goals of the organisation. Decision-making is therefore a central aspect of all four managerial functions. In the opening case, managers (and the senior manager especially) at LeisureNet made poor decisions, resulting in the failure of the organisation.

The term 'resources' is extremely comprehensive. The following basic resources can be found in all organisations, namely, people (human resources), money (capital or financial resources), raw materials (physical resources), knowledge (information resources), technology, information and components. Management utilises these resources to achieve the goals of the organisation as efficiently and effectively as possible. Resources are scarce and management's biggest challenge is to utilise its resources as productively as possible. Managers need to make choices in terms of what programmes, projects and activities to pursue with the limited resources at their disposal. Managers also have the task of bringing resources together, deciding which resources are necessary for a specific situation or specific circumstances, and in what quantities, to achieve the organisation's goals. The success with which an organisation achieves its goals and satisfies the ever-increasing needs of society depends on the competence of its managers in utilising its scarce resources. If managers utilise resources well, the organisation will be successful. If a country's organisations are competitive and successful, the country as a whole will prosper because successful organisations satisfy needs, not only by producing products and services, but also by providing jobs and contributing to the wealth of society. The inputs or resources of an organisation are transformed to realise certain outputs, of which goal achievement, products, services, profit, job creation, efficiency and effectiveness are the most important outputs.

In the case study, we saw the detrimental effect of the poor management of LeisureNet's financial resources – LeisureNet was used to fund, staff and train employees of Healthland. The Health and Racket Club business was pillaged to establish Healthland's operations and all available cash was invested in Healthland, with very little in the Health and Racket Club business. This resulted in a lack of maintenance and refurbishment at Health and Racket Clubs.

1.2.2 Management entails working with and through others

Managers get things done by working with and through other people. Management is, above all else, a social process. Many collective purposes bring individuals together

– building houses and cars, publishing books, offering tertiary education, providing personal financial services, and so on. The activities that are needed to build a house or a car, publish a book, offer tertiary education programmes and to provide advice on personal finances, cannot happen on their own. In all cases, managers are needed to get things done by working with and through other people and other organisations.

The ability to work with and through others is therefore an important skill that managers should have in order to be successful. Problems with interpersonal relationships and failure to build and lead a team are often the reasons why managers fail, as we have already seen in the case study of this chapter.

1.2.3 Management aims to achieve organisational goals and objectives, balance effectiveness and efficiency, and make the most of limited resources

An objective can be described as a target to be strived for. A university student, for example, can set an objective for him or herself, to graduate with a specific degree by a given date. All actions taken or activities performed by the student, will be with the view to achieve this target. As with individuals, organisations formulate organisational objectives. Organisations will also be more successful when their activities are guided by challenging, yet realistic and achievable objectives. Organisational goals and objectives serve later as measuring sticks for performance. Without goals and objectives, the management process would be aimless and wasteful. In the case study, we determined that the absence of organisational goals and objectives, contributed to the failure of the company.

It is important to distinguish between the concepts of effectiveness and efficiency. Effectiveness is achieved when the organisation formulates and pursues appropriate (or stated) goals. Effectiveness, in essence, means 'doing the right things' in order to achieve the objectives of the organisation.

Given the reality of limited resources, effectiveness alone is not enough. An organisation also needs to be efficient. Efficiency enters the picture when the resources required to achieve an objective are weighed against what was accomplished. The organisation will be more efficient if the ratio between benefits (outputs or performance) and costs (inputs or resources) is more favourable. Efficiency essentially means 'doing things right'. Efficiency is achieved by using the fewest inputs (such as the number of people employed or the amount of capital utilised during the financial year) to generate a maximum amount of output (such as a number of products produced or the profit realised within a financial year).

Managers are responsible for balancing effectiveness and efficiency. Too much emphasis on either effectiveness or efficiency leads to mismanagement. On the one hand, managers must be effective by getting the job done. On the other hand, managers need to be efficient by reducing costs and not wasting resources.

Too much emphasis on effectiveness will mean that the job gets done, but limited resources are wasted. Too much emphasis on efficiency will mean that the job gets done, but available resources are underutilised. Thus, the answer lies in a balanced emphasis on effectiveness and efficiency – the job gets done and limited resources are not wasted.

In a business context, organisations have access to limited and scarce resources and managers need to make the most of these resources. In the bigger picture, we live in a world of scarcity and limited resources. Although experts and non-experts alike may quibble over exactly how long it will take to exhaust our non-renewable resources or come up with exotic new technological alternatives, one fact remains: our planet is becoming increasingly crowded and sustainability and sustainable development should be among the main concerns for managers. Organisational sustainability means to maintain, to keep being, to preserve and to support, with structures to hold on to. For an organisation to be sustainable, it must sustain its resources and the uses thereof. It also means that organisations should balance their social, environmental (ecological) and financial aspects – the so-called 'triple-bottom line' which will be further explained in Section 1.7 of this chapter. In productive organisations, managers are the custodians of limited and scarce resources and it is their job to see that the basic factors of production are used efficiently and effectively.

1.2.4. Management needs to cope with a changing environment

Successful managers are the ones who anticipate and adjust to changing circumstances rather than those who are passively swept along or caught unprepared. In Section 1.5, we will elaborate on the management environment.

We can conclude this section with *Business Week*'s amusing but challenging profile of tomorrow's managers: 'The next generation of corporate leaders will need the charm of a debutante, the flexibility of a gymnast, and the quickness of a panther. A few foreign languages and a keen understanding of technology won't hurt either'.[2]

LO 3: Differentiate between the various levels of management.

1.3 Levels of management

The management process and functions of management, explained in the previous section, merely provide us with a starting point for understanding what management and strategic management, specifically, entails. To add to the complexity of the process, management takes place at different levels and in different areas within organisations. While managers at each level and in each area must generally possess planning, organising, leading and controlling skills, certain job-specific activities and skills are more important at one level than at another.

Managers function at various levels in the organisational hierarchy. A small organisation may have only one layer of management, whereas a medium- to large-sized organisation may have several layers. In general, relatively large organisations (especially governmental organisations) have three levels of management: top-level managers, middle managers and lower-level managers.

- Top management, also referred to as senior management, represents the relatively small group of managers who control the organisation as a whole and with whom the final authority and responsibility for executing the management process rest. Top management is responsible for strategic planning that includes determining the vision, mission, strategic direction, overall goals, strategies and plans of the organisation. Top management is concerned mainly with strategic planning that has the following characteristics: first, strategic planning focuses on the entire organisation; second, it aims to reconcile the organisation's strengths and weaknesses in its internal environment, with the threats and opportunities in the external environment; third, strategic planning focuses on creating and maintaining a competitive advantage for the organisation; fourth, it considers synergy and aims to co-ordinate the efforts of departments and individuals to contribute to the attainment of competitive advantage and the long-term goals of the organisation; lastly, strategic plans filter down in the organisation to form the basis of tactical and operational plans.

  Top managers are also responsible for designing the organisation's broad organisational structure, leading the organisation (through the top executive) and controlling it. Top management also influences the corporate culture, organisational change, the allocation of resources on corporate level and determines the culture of the organisation in terms of organisational learning. Strategic managers continuously monitor the external and internal environment of the organisation to identify possible opportunities, threats, strengths and weaknesses. The annual reports of organisations usually depict their top management structure. This level of management generally comprises the board of directors, partners, the managing director, chief executive officers, management committees and other governing bodies. In this book, the focus will be on the top management of organisations and their responsibilities in terms of strategic management. Traditionally, top managers were considered the only people responsible for strategic management. The contemporary view of management suggests that top managers alone are not the only strategists and that any individual or group in an organisation that controls key actions can be regarded as a role-player in strategic management.

- Middle management, also referred to as functional management, is responsible for specific departments or functions of the organisation. Middle management primarily deals with tactical planning and implementing the policies, plans and strategies formulated by top management. It normally includes the functional heads, such as the marketing manager, the financial manager, the purchasing manager and the human resources manager. Middle management is concerned with the near future and is therefore responsible for medium-term and short-term planning, organising functional areas, leading by means of the departmental heads, and controlling the management activities of the middle managers' own departments. Middle managers also continually monitor environmental influences that may affect their own departments. The trend in recent years of corporate restructuring, delayering, downsizing and decentralisation of decision-making has been responsible for large numbers of middle managers being made redundant. Electronic technology has reduced the need for middle management in some organisations. In the area of information management, in particular, computers have replaced the information-gathering tasks of middle managers. Middle managers are, however, still essential in linking the upper and lower levels of the organisation and in implementing the strategies developed at the executive level.

- Lower-level management (also called supervisory or first-line management) is responsible for even smaller segments of the organisation, namely, the different subsections. The managerial functions of first-line managers are centred around the daily activities of their departments or sections, on short-term planning, and on implementing the plans of middle management. Their primary concern is to apply policies, procedures and rules in order to achieve a high level of productivity, to provide technical assistance, to motivate subordinates and to accomplish day-to-day goals. Typically, they spend a large portion of their time supervising the work of subordinates. Because of this, first-line management is a vital force in the organisation. These managers hold the power to increase or decrease the productivity and output of most organisations. They also maintain the crucial interface between management and the major body of employees in the organisation. This level of management usually comprises titles such as office manager, shift supervisor, advertising manager, debtors' clerk or section manager.

LO 4: Explain the various areas of management.

1.4 Areas of management

We can distinguish between various functional areas of management in organisations, namely, finance, operations, human resources, procurement, research and development, public relations and marketing.

- The financial function is responsible for obtaining the necessary finances for an organisation at the lowest cost, investing these finances in assets that would earn greater returns than the cost of capital, as well as managing the profitability, liquidity and solvency of the organisation.
- The operations function includes that group of activities concerned with the actual provision of goods and services to the organisation's clients. Operations management systematically designs, directs and controls the process that transforms inputs into products and services for both internal and external customers.

- The **human resources function** involves the appointment, development and maintenance of the human resources of the organisation. To enable the organisation to operate at optimum levels, the human resources manager must appoint the right people and provide them with the right training in order to make the best use of them.
- The **procurement function** is concerned with buying the materials and resources needed to create products and services. The manager responsible for procurement needs to balance a number of constraints. He/she needs to ensure that the right product is available, at the right time, in the right quantity and of the right quality, at the best possible price.
- The **research and development function** is responsible for developing new products and services and improving old products and services. This function is critical in organisations that operate in fast-changing environments, such as information technology, communications, and so on.
- The **public relations function** of an organisation is responsible for creating a favourable, objective image of the organisation and for establishing good relationships with those directly or indirectly concerned with the business and its products or services.
- The **marketing function** is responsible for getting the final customer and client to buy the organisation's products or services. The marketing function is concerned with new product development, promotion and distribution.

While all the functions listed above are specialised areas of management, which require more specific and specialist skills, managers in each area still plan, organise, lead and control. A financial manager, for example, is responsible for determining the financial goals of the organisation, thus performing the planning function of management. The financial manager also needs to organise financial activities by allocating financial tasks to people so that financial goals can be achieved. The financial manager takes the lead in financial activities, motivating and directing members of staff in the financial section to perform their duties in pursuit of the financial targets. Lastly, financial managers need to ensure that financial goals are accomplished through the implementation of financial control mechanisms.

LO 5: Explain the hierarchy of organisational plans and depict it diagrammatically.

1.5 The hierarchy of organisational plans

From the discussions so far, we have learned that management is a process and that managers engage in some manner in four fundamental, interrelated activities (planning, organising, leading and control) in order to realise the goals of an organisation and to add value to the organisation and society. These activities are executed on various hierarchical levels of an organisation, and the focus of strategic management and of this book, is on the highest of these levels, namely, top or senior management. The planning stage of the management process is a top-down approach, which entails top managers formulating a strategic plan, which is a document that indicates the direction of the organisation. A strategic plan consists of the following seven elements: vision; mission; analysis of the strengths, weaknesses, opportunities and threats (SWOT analysis); core organisational values; goals; objectives and strategies.

- **Strategic plans** filter down in the organisation and form the basis of tactical plans crafted on middle management levels.
- **Tactical plans** focus on the functional areas of the organisation, are more specific than strategic plans and should take synergy into account. So, in other words, it should contribute to the attainment of the overall organisational goals. Tactical plans form the basis of operational plans, developed by middle and lower levels of management.
- **Operational plans** are narrowly focused, with a relatively short time horizon. Three basic forms of operational plans exist, namely, single-use, standing, and individual plans.
- **Single-use plans** are used once to meet the needs of a particular or unique situation. Programmes, projects and budgets are examples of single-use plans. In this context, a programme refers to a set of activities designed to accomplish a specific objective over a period of time. A programme consists of various projects, with predetermined completion dates and budgets. A budget can be described as a numerical plan for allocating resources to specific predetermined activities.
- **Standing plans** provide guidance because they deal with issues or problems that occur frequently. Policies, procedures and rules are examples of standing plans.
- **Operational plans form the basis of individual plans**, which are defined as the broader organisational plans that are translated into plans for the individual worker. It is also on the individual level that the implementation and execution of strategic plans commence, from where they culminate in the realisation of operational goals, and, ultimately, in the strategic goals of the organisation. The hierarchy of plans is depicted in Figure 1.1.

For managers to formulate realistic operational and individual plans, they need clear guidance and plans from strategic and tactical managers. Only if the different kinds of plans are understood, will lower levels of management and individuals be able to develop operational and individual plans.

The execution of the fundamental managerial activities by all levels and areas of management does not happen in isolation – the organisation (as a system) is part of a bigger system that we refer to as the management environment. The composition of the management environment is described in the next section.

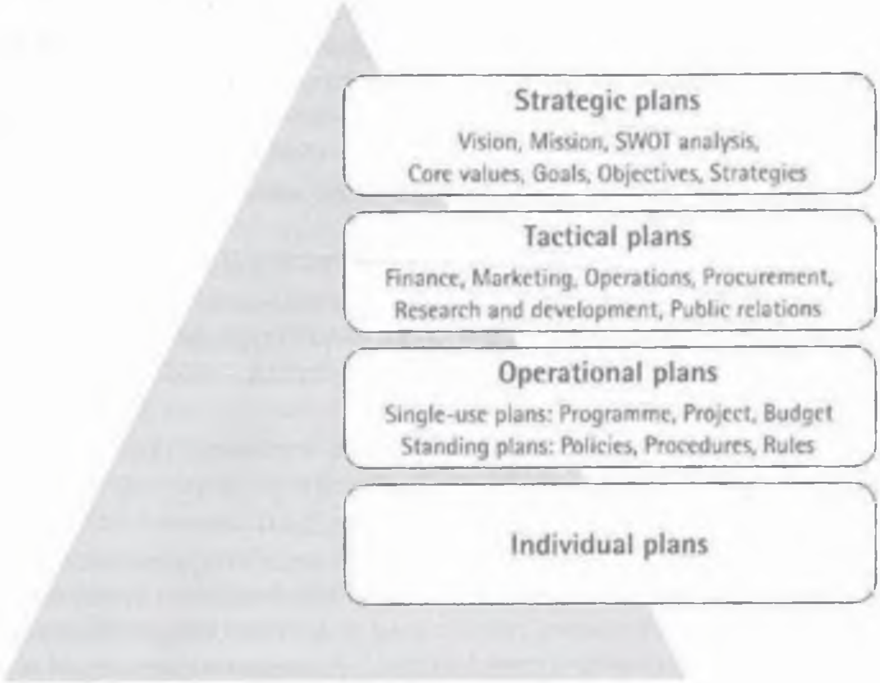

Figure 1.1 *The hierarchy of organisational plans*

LO 6: Explain the composition of the management environment.

1.6 The composition of the management environment

It is crucial to realise that organisations and their managements, source inputs from the environment, transform them into outputs, which are then returned to the environment. These are the main elements of any system: input → transformation → output. The success of the organisation as a system is largely determined by the efficiency and effectiveness illustrated by its management in performing planning, organising, leading and controlling functions. Furthermore, a system's success depends on successful interactions with its environment. In this context, the environment includes other sub-environments such as suppliers, labour unions, financial institutions, customers, and so on. The organisation is dependent on its external environment. Managements must therefore understand the structure and dynamics of the unique management environment of their organisations and, even more importantly, the unique strengths, weaknesses, opportunities and threats pertaining to the environment that impact directly or indirectly on the success of the organisation.

As the first step to a better understanding of the management environment, it is important for the manager to take account of its structure and dynamics. Without such an understanding, no realistic strategising can take place. Structurally, the management environment can be divided into the micro-environment, the market environment (industry) and the remote environment.

1.6.1 The micro- or internal environment

The micro-environment can also be referred to as the internal environment and includes the organisation's functions, policies, strategies, goals, objectives, and available resources, and also designates the area over which the manager has total or full control. Vodacom, a leading cellular network, has various features that we can identify from its micro-environment. For example, it represents a culture characterised by a winning spirit and passion for the job, progressive human resources policies, commitment to transformation, investment in social development programmes, successful staff retention programmes, competitive remuneration packages, successful skills development programmes, and commitment to ethical conduct and social development. Top or strategic managers play a profound role in the establishment of the micro-environment of the organisation. The factors in Vodacom's micro-environment are all under the direct control of its management, mainly the strategic managers of the company.

1.6.2 The external environment

The external environment comprises two major components, namely the market environment and the remote environment. The external environment also designates the area outside of the organisation over which the manager has no control.

1.6.2.1 The market environment

The market environment lies between the micro-environment and the remote environment and forms a buffer between the organisations and the remote environment. Some authors refer to it as the operating, competitive, task environment or industry. Other authors, in turn, refer to it as the 'meso-environment' or the intermediate environment. For the purpose of this book, we shall refer to it as the 'market environment'. The market environment comprises the following sub-environments: (1) customers (clients), their needs, purchasing power, behaviour and bargaining power; (2) suppliers of capital, materials and labour and the bargaining power of suppliers; (3) the population from which the organisation recruits its labour force and the unions representing it; and (4) competitors, including new entrants, existing competitors, the availability of substitute products or services and complementary products or services.

The customer

Customers can be defined as all those people or organisations that buy products or services from other people and other organisations. On the other hand, the market for the organisation's product and/or service consists of people who have needs to be satisfied and the financial means with which to satisfy their needs. The customer and the market for an organisation's product and/or service, is the main reason why an organisation exists. This is true for both private-sector and public-sector entities. For business entities in the private sector, to have no customers is to have no revenue and no profits: their survival depends on the customer. On the other hand, owing to their annual budget allocations from government, the supply of public-service entities do not depend, for their survival, on their products or services they supply to their customers, which is the community. Customers also exhibit buyer behaviour, which is influenced by variables in the macro-environment. For example, demographic trends affect the number of customers, economic trends influence the purchasing power of consumers, and cultural values can influence the buying behaviour of most customers.

Competitors

Aside from customers, competitors are the single most important day-to-day force associated with an organisation. Competition in the market environment is a situation in which different organisations with more or less the same product or service compete for the business patronage by the same consumers. Every organisation that tries to market a service and/or product in the market environment is constantly up against existing competition. In the case of business organisations, the competition is other businesses currently active in the same market sector who are competing for a share of the market. New entrants refer to potential competitors that have the resources to enter the current market in which established organisations operate.

A thorough competitor analysis, in which strategic managers should play a major role, can help an organisation to understand, interpret and predict its competitor's actions and responses. Understanding the actions of competitors is clearly an important factor contributing to the organisation's ability to compete successfully.

The labour market and labour unions

Although the labour market in economic theory equates to other markets, such as the financial market or the market for products and services, it has its own unique characteristics. The labour market comprises many different markets, such as those for various skill levels, occupations, age groups, industries, genders and geographical regions. These markets are to some extent interchangeable, yet barriers to mobility do exist. Another important difference between the labour market and other markets is the temporary nature of employment relationships. Once a purchaser buys products for consumption, it becomes the property of the buyer. This is not so with the employment relationship. Either the employer or employee may decide to terminate the relationships. This leads to greater fluidity and unpredictability in the labour market. Organisation's ability to attract and retain capable employees from the labour market is essential to its success. This ability, on the one hand, is greatly influenced by the strategic managers of an organisation. On the other hand, an organisation's personnel recruitment and selection alternatives are often influenced by the nature of both its external and its internal environments. An organisation's access to needed personnel is affected primarily by three factors, namely, the organisation's reputation as an employer, local economic conditions and subsequent employment rates, as well as the availability of people with the required skills. Organisations thus also compete for skilled and competent labour with other organisations, where labour unions play an integral role. Again, strategic managers play a profound role in determining the organisation's reputation as an employer and in its ability to attract and retain the necessary skilled human resources.

Intermediaries

In addition to consumers, competitors, the labour market and labour unions in the market environment, intermediaries also play an important role and affect the organisation directly and indirectly. Intermediaries act as middlemen between the manufacturer of products and services and the final consumer thereof. Intermediaries include wholesalers, retailers, agents and brokers, all of whom play a role in bringing a product or service from the manufacturer to the final consumer. Financial intermediaries, such as banks, insurers and other financial institutions, play a role in providing an organisation with the necessary capital to start and run a successful business.

Suppliers

Organisations need various inputs and depend on suppliers to provide regular supplies of these inputs. Most of the inputs used by the organisation form part of a value-creation process manifested in the value chain. The value chain can be described as a chain of activities that an organisation, operating in a specific industry, performs in order to deliver a valuable product or service for the market that it serves. Through the use of a value chain, value can be created for the role-players and a sustainable competitive advantage created for the organisation. The concentration of suppliers and the availability of substitutes are, on the one hand, of extreme importance to the effective functioning and survival of the organisation, and, on the other, also significant factors in determining supplier bargaining power. The terms *competitive advantage* and *sustainable competitive advantage* will further be clarified in Section 1.8.

1.6.2.2 The remote environment

The remote environment refers to the broader environment within which the organisation must function. The remote environment surrounds the market environment. It includes all PESTLE/G (explained in Chapter 5, Section 5.3.1) external influences that do not fall directly within the sphere of influence of the organisation, but which do have a bearing on its activities. When analysing the macro-environment, the emphasis falls on the changes that the uncontrollable variables at the macro-level cause and the strategic implications these hold for the organisation. For the purpose of systematic analysis, a number of sub-environments can be distinguished within the remote environment, namely, the political; economic; social, technological; legal; environmental; and international environments. Each of these sub-environments of the remote environment will be discussed below in more detail.

The political/legislative environment

The state is a major role-player in the remote environment of an organisation, because it influences the organisation primarily as a regulating force. The state enforces laws, directly affecting the way that organisations operate. Tax regulations, for instance, have a direct influence on each and every organisation and individual. Value-added taxes (VAT), for instance, was 14 per cent in South Africa. In the budget speech delivered on 21 February 2018, Malusi Gigaba the country's minister of finance at the time, announced an increase in the value-added tax rate of 1 per cent to 15 per cent, the first increase of this tax rate in 25 years. The country experienced major changes in its political environment in 2018. The major leadership changes of the ruling political party, the African National Congress, made world news. Former president Jacob Zuma resigned and was replaced with President Cyril Ramaphosa, who announced major cabinet changes and declared a country free of corruption. These adjustments led to major changes in financial markets, with an increase in the value of the country's currency, having a direct impact on organisations, especially those involved in multi-national business. With this in mind, strategic managers should be aware of changes in this environment that may require them to revisit the organisation's vision, mission statement, goals and strategies.

The economic environment

After technology, the economic environment plays a huge role in the remote environment. Organisations are influenced by factors such as business cycles, interest rates, inflation, unemployment, trends with regard to the gross national product (GNP) and the economic growth rate, monetary and fiscal policy, trends in the balance of payments, the current and provisional status of the economy in terms of recession and depression, the influence of resources, and so on. The economy, in turn, is affected by technology, politics, ecology, social trends and the international environment. These cross-influences constantly bring about fluctuations in the economy, affecting organisations, strategic managers and all other levels of management. Strategic management therefore needs to keep abreast of economic changes and trends which require them to revisit the organisation's vision, mission statement, goals and strategies.

The social environment

The social environment refers to the cultural and demographic aspects of the environment. Cultural forces, which underpin society and surround an organisation, are often not as visible as other general environmental forces. Culture refers to the unique pattern of shared characteristics, such as values, that distinguish the members of one group of people from another group. A value can be defined as the basic belief about a certain condition that has considerable importance and meaning to individuals. People's values are relatively stable over time. A value system comprises multiple beliefs that are compatible and supportive of one another. Managers need to appreciate the significance of the values and value systems of all its stakeholders – globalisation and global competition is a reality and the number of organisations that accept contracts and other assignments in other countries, is rapidly increasing. Realising the importance of cultural diversity can help strategic and other managers understand their international partners and, ultimately, to be more effective and efficient managers. The social environment also includes various demographic factors, such as, the age distribution population growth rate, emphasis on safety, career attitudes, and so on.

The technological environment

The technological environment is primarily responsible for changes in the remote environment. Technology can be defined as the knowledge, tools, actions and techniques that are used to transform ideas, information, raw materials and components into finished products and services. Furthermore, technology encapsulates the physical elements of human invention and innovation. Many new technologies are radical enough to force organisations, especially in high-tech industries, to reconsider their vision, purpose and methods of operation or face extinction. An analysis of the technological environment is crucial for strategic managers.

The most basic effect of technology and technological innovation is probably higher productivity. The ability of an organisation to produce more and better products poses a threat to competitors, compelling them to reassess their strategic plans, organisational structures, production methods, markets and other functional strategies. Effective management of technology and innovation is an extremely important source of competitive advantage for an organisation.

The environmental environment

The environmental environment (also referred to as the ecological or physical environment) relates to the limited natural resources from which an organisation obtains its raw materials. However, organisations also dispose of waste or some of their waste in the ecological environment. The ecological environment consists of the natural environment, as well as human-made infrastructure. Geography, the weather and climate, the availability and exploitation of natural resources (raw materials, water, and so on), as well as conservation agreements and conventions all form part of the natural environment. The human-made environment, in turn, refers to the roads, railways, airports, harbours, communication infrastructure and energy supplies that have an influence on all organisations.

Organisations are becoming increasingly aware of the natural environment and the interdependence between organisations and the natural environment. This interdependence presents opportunities and threats to organisations. One of the major threats is a shortage of natural resources, especially water and energy. The rising cost of energy, the cost of pollution, damage to a country's natural resources and climate changes are all threats from the natural environment. Managers should take timely steps to ensure that no actions on the part of their organisation have detrimental effects on the environment. Sustainability issues, such as green industries, buildings and transport, have become crucial for strategic management.

The global environment

Globalisation and organisations conducting business across the borders of a country is a reality. The international environment poses threats, as well as opportunities for organisations. Strategic managers need to consider these for successful strategic management in contemporary organisations.

Within the management environment discussed in this section, all managers, but strategic managers, in particular, need to be aware of the various stakeholders in the management environment. This is the focus of the following section.

LO 7: Explain the terms 'stakeholder' and 'stakeholder relationship management'.

1.7 Stakeholders and stakeholder relationship management

Various views exist in terms of who or what constitutes a stakeholder of an organisation. The so-called narrow view of stakeholder theory refers to stakeholders as a group of individuals within the boundaries of the organisation. This view only considers stakeholders who are directly linked to the organisation, such as employees, customers and financial institutions. The broader view of stakeholder theory looks beyond the stakeholders within the organisation. It includes groups within the organisation, as well, as those on the outside, such as the community, local and national government.

In this book, we will adopt Clarkson's definition of organisational stakeholders:

> *An organisation's stakeholders are the people or groups of people that have, or claim ownership, rights, or interests in an organisation and its activities, past, present and future. Such claimed rights or interests are the result of transactions with, or actions taken by the organisation, and may be legal or moral, individual or collective. Stakeholders with similar interests, claims, or rights can be classified as belonging to the same group, for example, shareholders, employees, customer and suppliers.*[3]

In general, stakeholders are classified as external or internal. External stakeholders are those individuals or groups, who do not work directly within the organisation, but who are affected by the strategies, plans and actions of the organisation. External stakeholders include the community, government, activist groups and not-for-profit organisations, competitors, the media, industry associates, organised labour, customers, suppliers, analysts, consultants and researchers.

Internal stakeholders are stakeholders who work directly within an organisation. Internal stakeholders are shareholders/business owners, investors, employees and management.

Traditionally, the primary goal of organisations was to realise a profit and thereby satisfy the needs and expectations of its owners (or shareholders). Contemporary organisations adopt the triple-bottom line – an accounting framework with three parts, comprising the social, environmental (ecological) and financial parts. By adopting this framework, organisations evaluate their performance on a broader perspective to create greater business value. The triple-bottom line not only focuses on the expectation of shareholders (profit), but simultaneously on the expectations of all stakeholders. Therefore, to be regarded as successful, an organisation needs to be (i) profitable; (ii) take responsibility for the physical environment in which it operates; and (iii) meet its social responsibilities.

Management on all hierarchical levels should acknowledge the important role that stakeholders play in organisations. Strategic managers, especially, must take into account the impact that the organisation's vision, goals, strategies, projects and plans have on all stakeholders. Organisations are responsible for considering and protecting the rights and expectations of all their stakeholders.

At the same time, the influence that stakeholders have on the organisation should also be considered. This calls for a stakeholder relationship management process, which will bear tangible and intangible long-term rewards for the organisation. For example, new products, new markets, stronger supply chains, a diverse workforce, and trusting relationships will all yield a competitive advantage for the organisation.

In our discussion so far, we have referred a number of times to the term *competitive advantage*, which is a key term in strategic management.

LO 8: Differentiate between the terms 'competitive advantage', 'sustainable competitive advantage' and 'transient competitive advantage'.

1.8 Competitive advantage, sustainable competitive advantage and transient competitive advantage

In Section 1.6, we elaborated on the management environment. The market environment was identified as the environment comprising customers, competitors, the labour market and labour unions, intermediaries and suppliers. In this environment, competition is taking place – organisations are competing for the same customers, suppliers, skilled labour and intermediaries. The most widely used framework for classifying and analysing these forces of competition in a specific industry was developed by Michael Porter of Harvard Business School.[4] His framework views the profitability or attractiveness of an industry as determined by five sources of competitive pressure in the particular industry. These five sources are (1) competition from providers of substitute, products and/or services; (2) competition from new entrants or potential competitors; (3) competition from established rivals (competitors); (4) the power of suppliers; and (5) the power of buyers.

1. **Competition from substitutes** is influenced and determined by the buyers' propensity to substitute or buy substitute products and the relative prices and performance of substitutes.
2. **Competition from new entrants** or potential competitors to the industry is influenced by various factors, such as the capital needed to enter the industry, product differentiation, and legal barriers to enter the industry.
3. **Competition from established rivals (competitors)** in the industry is influenced by factors such as the diversity of these rivals, product differentiation to be found in the industry, exit barriers and cost conditions.
4. The **power of suppliers** is also determined by various factors, for example, the price sensitivity of suppliers and their relative bargaining power.
5. Lastly, the **power of buyers** is influenced by factors such as competition between buyers, product differentiation, the information made available to buyers and the size and concentration of buyers relative to suppliers.

Once an organisation understands how the structure of the industry in which it operates drives competition in this industry, the profitability of the industry can be forecasted for the future. Determining industry structure involves the identification of the main players in the industry – the producers, customers, suppliers, and producers of substitute products. An examination of the key characteristics of each of the main players will determine the competition in the industry and bargaining power that we described in the previous paragraph. This analysis can subsequently be used to forecast industry profitability. Why? Organisations will only invest capital and other resources in an industry that meets its objectives in terms of profitability. Once an organisation understands the structure of its industry and have made forecasts of its profitability, strategies can be developed.

The next crucial question that needs to be answered is how industry profit is shared among the different organisations competing in a particular industry? To answer this question, it requires an identification of the sources of competitive advantage within the particular industry. We can use the term 'key success factors' to describe the factors in an industry that influence an organisation's ability to outperform its rivals or competitors. Once an organisation understands the drivers of industry profitability, it can identify strategies through which it can improve industry attractiveness and position itself relative to its competitive forces. In essence, this means that an organisation can earn superior financial performance either by (1) locating in an attractive industry; or by (2) establishing a competitive advantage over its rivals. Of these two, competitive advantage is the most important since competition intensifies constantly across almost all industries so that very few industries can guarantee secure investment returns. Hence, we can conclude that the primary goal of a strategy is to establish a position of competitive advantage for the organisation. Stated differently, the primary goals of strategy is to put an organisation in a superior business position – which is a requirement for sustainability and survival over the long term.

At this point, we need to provide a formal definition of the term 'competitive advantage'. The literature provides us with numerous definitions, for example:

> *Competitive advantage is what makes you better than anyone else.*[5]
>
> *Competitive advantage are conditions that allow a company or country to produce a good or service at equal value but at a lower price or in a more desirable fashion. These conditions allow the productive entity to generate more sales or superior margins compared to its market rivals.*[6]
>
> *A superiority gained by an organization when it can provide the same value as its competitors but at a lower price, or can charge higher prices by providing greater value through differentiation. Competitive advantage results from matching core competencies to the opportunities.*[7]
>
> *There is no one answer about what is competitive advantage or one way to measure it, and for the right reason. Nearly everything can be considered as competitive edge, eg higher profit margin, greater return on assets, valuable resource such as brand reputation or unique competence in producing jet engines. Every company must have at least one advantage to successfully compete in the market. If a company can't identify one or just doesn't possess it, competitors soon outperform it and force the business to leave the market.*[8]

For the purposes of this chapter, we will define competitive advantage as follows:

> *When two or more organisations compete within the same industry, one possesses a competitive advantage over its rivals when it performs (or has the potential to perform) better than its rivals.*

Common sources of competitive advantage are the following: barriers to entry, capital, cost advantage, customer satisfaction, digital maturity, distribution, know-how, market power, bargaining power, brand name, corporate governance, critical mass, design, distinctive capability, economic advantage, economies of scale, intellectual property, sustainability, trade secrets, switching costs, market position, marketability, organisational culture, product development, risk management, technology and market position.

Having a competitive advantage is the result of an organisation matching internal strengths to external key success factors. It is crucial to point out that competitive advantage is not something static and stable. In fact, competitive advantage is a disequilibrium phenomenon: it is created by change and, once established, it starts a competitive process that leads to its destruction.

The changes that create competitive advantage, can be either internal or external. Internally, some organisations may, for example, have a greater creative and innovative capability than their rivals that may lead to a competitive advantage. Externally, changes in, for example, customer demands or technology can create a competitive advantage for an organisation that is faster and more effective in exploiting change than its rivals.

Once an organisation establishes competitive advantage, it is eroded by competition. The speed of this erosion will depend on the ability of competitors to challenge, either by imitation or by innovation. For a sustainable competitive advantage, the organisation must create barriers for other organisations to imitate and innovate its advantages. We therefore define a **sustainable competitive advantage** as:

> *an organisation that has the ability to perform (or the potential to perform) better than its rivals over the long term.*

Organisations may have assets, attributes or abilities that are difficult to imitate or exceed which contribute to their competitive advantage. Competitive advantages are often short-lived and instead of building one advantage and defending it, a transient strategy focuses on innovation strategies that continually build new advantages. Therefore, we define transient competitive advantage as follows:

> *an organisation that has the ability to build up temporary (or transient) advantages where they seize opportunities, exploit it, and then move quickly when they have exhausted the opportunity.*

Some of the competitive advantage of various South African companies are highlighted below.

Practising strategy

Woolworths

Max Sonnenberg founded Woolworths in 1931. His belief that success lies in providing customers with superior quality merchandise at reasonable prices has been instrumental in establishing Woolworths as one of South Africa's leading retail chains – a benchmark for excellence and an icon of quality.[9]

South African Breweries

The South African Breweries Group, is one of the world's largest beer distributors with a market share of 98 per cent in South Africa. The company is at the forefront in addressing social inequities in its hiring, promoting, and training practices, and combating discrimination. The company's diverse workforce creates a global competitive advantage for the company.[10]

Edcon

Edgars Consolidated Stores, commonly known as Edcon, is one of the country's most successful retail operations. The company firmly believes in the power of outsourced information technology for competitive advantage. From an information technology point of view, that means that the company thoroughly analyses available technologies and options for how these are delivered to the business. A key contributor to the success of the organisation's IT strategy has been its decision to outsource substantial components of its infrastructure, data processing, systems development, security and storage capabilities. Since there is a shortage of technology skills in the country, the company believes it simply does not make sense for Edcon to develop expertise in-house. Their core focus is retail, so they look for partners that are experts in the field of IT so that the company can focus on an understanding of business principles that apply to their market and leave the technology in the hands of appropriately skilled suppliers. The company's ability to appoint appropriate expertise to take care of specialist functions is critical to achieve and sustain growth.[11]

The big picture

In this chapter, we highlighted the relationship between various general management principles and strategic management. The background and information provided lay the foundation for the successful practising of strategy, which is the focus of the remainder of the book. Strategists need to have a thorough understanding of the crucial role that strategic management plays in any business organisation. Without strategic management, the organisation is doomed for failure, as we have seen in the LeisureNet case study. Furthermore, strategists need to have a thorough understanding of the management environment in which it operates. Competition in this environment is becoming more fierce, due to various factors such as globalisation and the use of technology to conduct business, to mention only a few. Therefore, the establishment of strategies that will ensure the sustainability and long-term survival of the organisation is crucial. The study of strategic management focuses on how organisations achieve this competitive advantage, in other words how they achieve superior performance and sustainability over the long term. In Chapter 2, we will introduce you to the practice of strategy.

Summary of learning outcomes

LO 1: Explain the concepts 'manager' and 'management'.

A manager as a person that is responsible for running a part of or an entire organisation. Management is defined as the process of working with and through others to achieve organisational objectives in a changing environment. To be successful, organisations need managers performing the management process.

LO 2: Explain the management process, indicating the four characteristics thereof.

The four characteristics of management are:

(i) management is a process, consisting of four management functions namely planning, organising, leading and control;

(ii) management entails working with and through others;

(iii) management aims to contribute to the realisation of organisational goals and objectives, and in doing so management needs to balance effectiveness and efficiency and makes the most of limited and scarce resources; and

(iv) management needs to cope with a changing environment.

LO 3: Differentiate between the various levels of management.

We differentiate between the top, middle and lower levels of management. Top managers are responsible for strategic planning, implementation and control for the organisation as a whole. Middle managers are responsible for specific departments or functions of the organisation.

Lower-level managers are responsible for even smaller segments of the organisation namely the various subsections.

LO 4: Explain the various areas of management.

Seven areas of management are distinguished, namely finance, operations, procurement, marketing, human resources, public relations and research and development.

LO 5: Explain the hierarchy of organisational plans and depict it diagrammatically.

The hierarchy of organisational plans consists of strategic, tactical, operational and individual plans. The strategic plan comprises seven elements, namely the vision, mission, SWOT analysis, core values, objectives and strategies of the organisation. Tactical plans focus on the functional areas of the organisation, whereas operational plans focus on subsections of the organisation, which may be single-use plans or standing plans. Individual plans are the translation of broader organisational plans into plans for the individual worker.

LO 6: Explain the composition of the management environment.

Structurally, the management environment can be divided into the micro-, market an remote environments. The micro-environment is the organisation itself over whic management has control. It includes organisational functions, policies, strategie goals, objectives, and resources. The market environment is also referred to as th competitive environment and consists of customers, suppliers, labour and labo unions, and competitors.

LO 7: Explain the terms 'stakeholder' and 'stakeholder relationship management'.

An organisation's stakeholders are the person or groups of people that have, or claim to have ownership, rights, or interests in an organisation and its activities, past, present and future. Organisations need to manage its relationship with all stakeholders.

LO 8: Differentiate between the terms 'competitive advantage', 'sustainable competitive advantage' and 'transient competitive advantage'.

When two or more organisations compete within the same industry, one possesses a competitive advantage over its rivals when it performs (or has the potential to perform) better than its rivals. Sustainable competitive advantage refers to an organisation that has the ability to perform (or the potential to perform) better than its rivals over the long term. Organisations may have assets, attributes or abilities that are difficult to duplicate or exceed to lead to its competitive advantage. Competitive advantages are often short-lived and instead of building one advantage and defending it, a transient strategy focuses on innovation strategies that continually build new advantages. Organisations need to build up temporary or transient advantages where it seizes opportunities, exploit it, and then move quickly when it has exhausted the opportunity.

Discussion questions

1. Provide an explanation of the terms 'manager' and 'management'. Is there a difference between contemporary views of these terms, compared to more traditional views?
2. Explain the management process and highlight the most significant components of the process.
3. Discuss the various levels and areas of management and highlight the most important responsibilities of each level and area of management.
4. Explain the composition of the management environment and indicate the importance thereof in terms of strategic management.
5. Explain the hierarchy of organisational plans and highlight the most important plans pertaining to each level of the hierarchy.
6. Explain the term 'stakeholder' and defend the importance of stakeholder relationship management in organisations, as well as the important role that strategists play in this.
7. Differentiate between competitive advantage, sustainable competitive advantage and transient competitive advantage. Also, highlight the importance of these concepts in strategic management.

Learning activities

Choose a company that has been listed on a stock exchange for more than ten years and do the following:

1. Analyse the annual reports of this company and identify the following: (i) vision; (ii) mission; (iii) strategy; (iv) company values; (v) strategic goals.
2. Identify the competitive advantages of the company.
3. Identify the major stakeholders of the company.
4. What, in your opinion, is the main reason why the company has been in business for so long? Substantiate your answer.

Endnotes

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2 Introducing the practice of strategy

Peet Venter

LEARNING OUTCOMES

After studying this chapter, you should be able to:

LO1: Explain the origins of strategic management.

LO2: Identify and explain the universal principles of strategic management.

LO3: Define strategy and explain its importance to the organisation.

LO4: Identify the characteristics of strategic decision-making, and provide guidelines to strategic decision-makers to aid them in making better strategic decisions.

LO5: Explain how the success of strategy can be measured.

LO6: Discuss a contemporary strategic management framework.

KEY WORDS

- Business architecture
- Competitive advantage
- Dynamic consistency
- External consistency
- Organisational sustainability
- Strategic control
- Strategic management
- Strategic planning
- Strategic thinking
- Strategising
- Strategists
- Strategy formation
- Strategy implementation
- Strategy

CHAPTER ORIENTATION

Organisations generally have an imperative to survive and to perform above the average – as we have indicated in Chapter 1. The study of strategic management focuses on how organisations achieve this competitive advantage, in other words, how they achieve superior performance and sustainability over the long term. However, as the case study on Elon Musk suggests, the role of people in influencing strategy in the organisation cannot be underestimated.

In this chapter, we review the origins of strategic management, identify and explain the universal principles of strategic management, define strategy, explain how the success of strategy can be measured, and describe a contemporary strategic management framework.

Case study

Elon Musk – Leading with Vision

In 2006, Elon Musk announced in a blog his 'master plan' for sustainable mass transport. This entailed:

- creating a low-volume[1] car, which would necessarily be expensive.
- using that money to develop a medium-volume car at a lower price.
- using that money to create an affordable, high-volume car.
- providing solar power.

As one of the most admired technology entrepreneurs in the world, South African-born Musk is known for his vision to rid the world of fossil fuels, and Tesla's electric vehicles and solar power technologies are ways of doing just that. Musk's plan unfolded over the last decade or so first with the development of the Tesla S, an expensive, high-performing sports car, and then moving into the second phase of the plan with the development of the Tesla X and Tesla Roadster. Most recently, Tesla announced the Tesla 3, an affordable electric car, and with advance orders of more than 400,000 cars, it would seem as if the master plan is on track. In the meantime, Tesla also launched various products for residential and business solar energy production, such as the Powerwall battery system, solar panels and a 'solar roof', and their SolarCity business is now the second-largest solar provider in the US. In support of his businesses, Tesla built a Gigafactory (with Panasonic) for producing lithium-ion batteries for use in battery farms and electric cars.

When pursuing of his vision for a sustainable planet, Musk does not hesitate in sharing his ideas and technologies freely and in thinking out of the box. He made Tesla Motors' patents available to the industry for free, and has explicitly open-sourced the Hyperloop[2] train concept so that others can take the ideas and further develop them. In addition, he is striving to make travel to Mars affordable with Space-X and to establish a space colony on Mars.

Musk is often described as a transformational leader who has the following qualities:

- The capacity to think beyond what seems possible or viable today.
- The ability to make people believe in his vision, no matter how far-fetched it may seem.
- Leading by example - excellence is non-negotiable.
- A relentless (even obsessive) drive towards results – failure is not an option.

However, leaders like Musk are not always easy to work with. The amazing vision and drive that contribute to Musk's leadership style sometimes mean that 'an engineer might spend nine months working 100 hours a week on something because Musk pushed him to, and then out of nowhere, Musk will change his mind and scrap the project'.

In 2016, Musk updated his master plan to:

1. Create stunning solar roofs with seamlessly integrated battery storage.
2. Expand the electric vehicle product line to address all major [consumer] segments.
3. Develop a self-driving capability that is 10X safer than manual capability via massive fleet learning.
4. Enable your car to make money for you when you aren't using it.

With his track record up to this point, it would unwise to bet against him achieving exactly what he sets out to do.

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LO 1: Explain the origins of strategic management.

2.1 The origins of strategic management

While strategy is an ancient concept,[3] strategic management, as we know it today, originated in the late 1970s following a move away from corporate planning to a more externally focused process. Strategic management was characterised by a focus on competition as the key driving force in the business environment and profit maximisation as the primary goal of the organisation. The process of strategic management accordingly focused on the selection of markets and on the positioning of the organisation in its chosen markets relative to its competitors as a source of competitive advantage (ie superior performance over the long term). Initially, the focus of strategic management was to determine how the organisation could tap into sources of profit in an industry by virtue of its industry positioning. For example, by creating clear differentiation from its competitors, organisations could be in a position to charge higher prices for the perceived higher quality. This view, with Michael Porter[4] as its main proponent (which we discussed in Chapter 1, Section 1.8), was predominant until the 1990s and is still prominent in strategy texts to this day.

In the 1990s, the resource-based view (RBV) emerged as the dominant perspective on how organisations could achieve a competitive advantage. In accordance with the RBV, an organisation's internal resources and capabilities were the most important sources of profit and competitive advantage. The focus of strategic management accordingly shifted to understanding how organisations differed from their competitors (in terms of what capabilities they possessed) and how these differences could be leveraged for competitive advantage.[5]

Our understanding of how organisations practise strategic management and how they develop competitive advantage and organisational sustainability (the ability of the organisation to survive and outperform rivals in the long run) is shaped by our environment (which we discussed in Chapter 1, Section 1.6) and is constantly evolving. For example, in the aftermath of a string of corporate scandals internationally, as well as locally (such as Enron, Fidentia and the Steinhoff scandal), the global financial crisis of 2008 and 2009, and the current state of governance in South Africa (such as the widely publicised problems in many state-owned companies like Eskom, South African Airways (SAA) and the South African Broadcasting Corporation (SABC), there is a strong focus on responsible and ethical corporate behaviour (which we referred to in Chapter 1 as the 'triple-bottom line').

In this book, we emphasise the importance of the environment, and the resources and capabilities of the organisation. At the same time, we recognise that strategic management is a dynamic discipline and that its key influences and debates change over time. However, while our understanding of the focus of strategic management and competitive advantage has evolved, the strategic management process itself has not always enjoyed the same attention. In this book, we argue that the strategic management process is also a fluid and changing concept. While there are many different views on how strategic management should be done, there are certain common principles that underlie the various views of strategy and strategic management. In the next section, we review these common principles.

LO 2: Identify and explain the universal principles of strategic management.

2.2 The universal principles of strategic management

Most lecturers involved in teaching strategic management have experienced a situation in which students complain that the way strategic management is taught is different from the way it actually happens in their organisations. This could be seen as a sign of the theory/practice divide, and as reflective of the complexity of strategic management. More recently, the study of strategic management started to catch up to the practice of strategic management. Despite this complexity, there are some principles that are common to all views of strategic management, and we discuss these principles below, by using the example of Discovery Bank as it illustrates the application of these principles.

Practising strategy

Discovery moves into retail banking[6]

Discovery is a large, listed, financial services institution operating through Discovery Health (DH), Discovery Life (DL), Discovery Invest (DI), short-term insurer Discovery Insure, and the very popular and successful Discovery Vitality (a wellness loyalty programme). In addition, it has operations in the USA, where it licenses Vitality for use by employers and other health insurers, and in the UK, where it operated two joint ventures (JVs) with the Prudential plc – PruHealth and Prulife. Its core purpose is 'to make people healthier, and enhance and protect their lives'. Discovery is generally known for its innovativeness. For example, they are credited with the invention of the medical savings plan used widely by medical schemes today.

In 2015, Discovery received authorisation from the Registrar of Banks to establish banking operations in South Africa, and launched its banking products in 2019. This is according to Discovery CEO Adrian Gore, who said they are deep into the preparation phase of the new bank. Gore said it is a complicated process to assemble the right team, build the systems to support the bank, and develop products which banking clients need. Despite the complications, he remains upbeat about the prospects of Discovery Bank – saying it is an exciting project.

'We need to meet the needs of our customers. I think we can. We have strong ideas and convictions about that. If we can do that, the market will tell us,' said Gore.

Gore said they had tremendous success with their joint venture with FNB on the Discovery Card, which provides them with a launchpad for full banking services.

'We've got the capital, we've hired bankers, we're building substantial systems. We want to make an offering that's relevant and can win market share,' said Gore.

Discovery has an advantage over the big four traditional banks, as it does not have to maintain a country-wide network of branches and ATMs. This means Discovery Bank's costs will be lower than its competitors.

2.2.1 Principle 1: Strategy is about positive change

Strategic management is ultimately about positive change for the organisation as a whole. Positive change includes achieving superior performance, creating competitive advantage, creating shareholder wealth above the average, meeting the needs of all stakeholders (you may refer back to Chapter 1, Section 1.5 where we differentiated between shareholders and stakeholders), or, in some instances, just surviving in difficult times. It is also worth noting that it is about change, and managing such change, and not about just doing things as they have always been done (ie 'business as usual'). For example, the decision by Discovery to launch Discovery Bank[7] reflects Discovery's view that they will be able to use their expertise in the financial services industry and their loyal customer base to compete successfully in the retail banking industry and to create value for the owners of the group.

2.2.2 Principle 2: Strategy takes a long-term view

Strategy is about taking a long-term view and ultimately focusing on wealth creation and sustainability over the long term, rather than on merely creating quick wins or short-term gains.

2.2.3 Principle 3: Strategy is complex

Strategy is highly complex and is associated with high levels of uncertainty and risk. There are no easy answers, no recipes for success, and it is highly situated, meaning that it is different for every context. In other words, strategic management is about making big decisions during situations of high uncertainty and having to consider many different variables. Should strategic decisions fail, there may be very severe negative consequences for the organisation, so the risk is enormous. Discovery worked for some years on establishing Discovery Bank, and invested a lot of time and money into getting the necessary approvals and license, appointing the right personnel and establishing infrastructure. Should the bank not perform as envisaged, it could mean that this capital investment was not justified, and Discovery could end up losing a great deal of money.

2.2.4 Principle 4: Strategy has an internal and external focus

Strategy is about mobilising resources and capabilities inside the organisation t pursue opportunities outside of the organisation, or to respond to negative risk timeously. This typically means that strategic decision-makers have to understan the resources and capabilities of the organisation, and how it needs to change ov time to keep up with a changing and unpredictable external environment. In th case of Discovery Bank, the board of Discovery felt that their internal resourc and capabilities (such as their loyal customer base, their Vitality loyalty programm innovation capabilities and their experience in the insurance industry) would enal them to pursue the perceived external opportunity in the retail banking industry.

2.2.5 Principle 5: Strategy is both deliberate and emergent

Organisations have very important formal processes to create deliberate strateg Deliberate strategies are those strategies that the organisation intends to pursue order to achieve its long-term goals. Hence, we often consider strategy as someth abstract, as something that an organisation possesses, for example, 'the strat of company X is cost leadership'. However, there is increasing recognition strategising is also a human activity, something that people do in organisations e day. The acts and decisions of strategists may lead to an 'emergent' strategy th different from what the organisation intended. Robert Grant suggests that stra exists in three places: the heads of managers, in the talk and documents they prod and in their actions. Only the latter two are observable.[8] This perspective implies that, if we are to understand strategy and strategic management, we have to understand who the strategists are, and how and why they make decisions and do what they do rather than focusing only on strategy at an abstract level. In fact, the realised strategy may often end up being quite different from the intended strategy. People do not act like rational robots, but that their strategic acts (and, by implication, strategy) are fuelled by who and what they are, as well as by cognition (rationality) and politics, the quest for power. In the opening case study, it is clear that Elon Musk's way of doing things plays a considerable role in the success of Tesla.

While top managers undoubtedly play a key role in the success of strategic management, the emerging strategy perspective suggests that top managers alone are not the only strategists. Any individual or group in the organisation that controls key or precedent-setting actions[9] can be regarded as a strategist. Accordingly, we can extend our perspective of strategists to include non-executive directors, strategic planners, middle managers and consultants. Through their own interpretations of strategy, or their own actions, these role players can influence the allocation of resources. It is, therefore, important to consider their role. Certain methodologies and systems can also be used to facilitate strategising, for example, strategy workshops and projects.

2.2.6 Principle 6: Strategy involves various different thought processes

The process perspectives of strategy often present it as orderly, analytical, rational and neat, and also as deliberate – a path that is chosen and pursued efficiently. In fact, there is much evidence to the contrary. Strategy is often emergent rather than deliberate, messy rather than neat, and experimental and fraught with failure rather than efficient and effective from the start. So, while there are elements of the strategy process that are designed to be rational and cognitive (eg conducting strategy workshops), there are a myriad of social interactions inside and outside of the workplace that influence the activities and decisions of strategists. There are different thought processes at work in strategic management. In fact, strategy is often referred to as both an art and a science, suggesting that it incorporates both a rational, analytical element, as well as an element of creativity. In addition, there are often power issues at work in strategy, where individuals or groups compete for power. As alluded to earlier, strategy work is about verbal and written communication. Strategists need to be able to use persuasive language and arguments, and be able to build a coherent story of strategy from the snippets of conversation taking place all over the organisation.[10] In addition, documents such as strategic plans, operational plans and strategy presentations are important forms of discourse that can influence the strategy and strategic decision-making.

Since the term 'strategic thinking' is used so often, it is useful to consider what it means. Figure 2.1 is a comparison of some characteristics of strategic thinking with non-strategic thinking. Strategic thinking is typically focused on the future and represents a certain willingness to take calculated risks. Strategic thinkers are also generally more creative, flexible and pro-active than non-strategic thinkers.

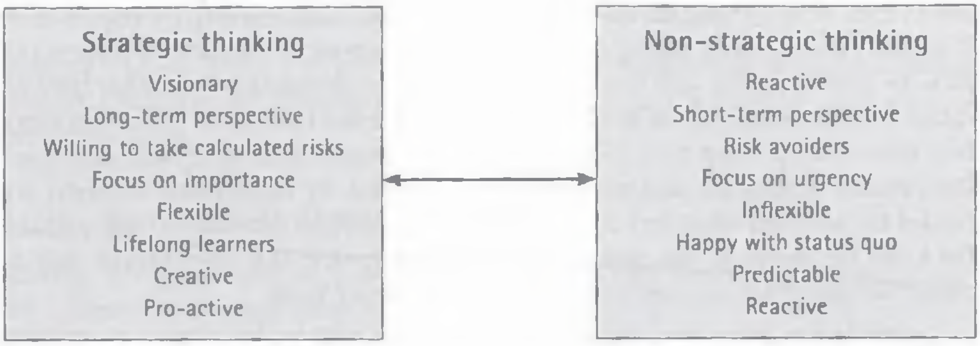


Figure 2.1 *Strategic versus non-strategic thinking*

2.2.7 Principle 7: Strategy happens at different hierarchical levels

In large multi-business organisations, strategic management and decision-making takes place at different levels. Table 2.1 compares strategic management and decision-making on corporate, business and functional levels of an organisation in terms of (1) where the decision-making takes place, (2) the scope of the decision, (3) the responsible people, and (4) the goals thereof. At the highest level, decisions about the growth path of the organisation are made by the board of directors or other governing bodies. This level of strategy is known as corporate-level strategy and the focus is on creating stakeholder value. It is at this level that decisions are made about the scope of the organisation, for example, mergers, acquisitions, divestments and globalisation. The decision by Discovery to enter the banking industry is an example of a corporate strategic decision.

Business-level strategy takes place at the level of the single business or business unit (eg a subsidiary) and the goal is for it to achieve competitive advantage within the markets in which it is competing. It supports corporate-level strategy by ensuring that it is successful in its markets, and draws on the corporate centre to provide it with the means to compete successfully. Business unit managers are responsible for attaining the overall goal of the organisation. In the case of Discovery Bank, the company will hope that with access to their existing customer base, corporate capabilities and Discovery's Vitality loyalty programme, it will be able to compete successfully in the banking industry.

Functional strategies, such as human resource or marketing strategies, ar developed by functional managers to execute the business unit strategies develope by business unit managers, and to support the implementation of business strategie For example, in setting up Discovery Bank, the human resource strategy in hiring th right talent to staff the bank is going to be crucial to its success.

Table 2.1 *Strategic management and decision-making at various hierarchical levels*

	Corporate-level strategy	Business-level strategy	Functional-level strategy
Where	Corporate centre	Business unit	Functional management
Scope	The multi-business corporation	Markets in which it is competing	Functional area (eg marketing)
Who is responsible	Board of directors	Business unit manager	Functional manager
Goal	Stakeholder value	Competitive advantage	Executing business unit strategy

Bidvest provides us with an example of the different levels of strategy that can be found in multi-business organisations.

Practising strategy: Bidvest's corporate strategy[11]

Bidvest is a South African corporation that focuses on using diversification and innovation to grow their portfolio of successful, cash-generating businesses in consumer and industrial products, electrical products, financial services, freight management, office and print solutions, outsourced hard and soft services, travel and aviation services and automotive retailing.

The company uses acquisitions to invest in a blend of defensive, cyclical and growth assets; they prefer businesses that generate cash and are not heavily invested in assets, and are aiming to internationalise in certain niche markets in services and commercial products.

The company is aiming to establish dominant positions in each of the markets they operate in with broad product offerings. Bidvest prides itself on having a highly entrepreneurial and decentralised management and operations, and a strong record of efficient capital allocation to the businesses they own.

In contrast to the Bidvest head office, where corporate strategies are identified and decisions are made in terms of the scope of the organisation, the role of Bidvest businesses is to ensure that they compete successfully in their industries. Bidvest's business goal is to achieve competitive advantage in its various markets. Within each business unit, functional managers need to execute business unit strategies so that they can compete successfully in its market. For example, Bidvest Car Rental must have business level strategies and functional strategies to ensure that they compete successfully against other car rental companies.

LO 3: Define strategy and explain its importance to the organisation.

2.3 Defining strategy

In this section, we consider some key aspects and describe what we mean by strategy, as seen from our perspective.

2.3.1 What does it mean to be 'strategic'?

Not all actions and decisions in an organisation can be considered 'strategic'.

Figure 2.2 *Strategy versus business as usual*[12]

Consider Figure 2.2. If we take point A as where we are today, and we carry on doing what we are doing (ie business as usual) and we are somewhat lucky, we may end up at point B, in a slightly better position than we are today and perhaps, if we are very lucky, in a position where we are better off than our competitors. It is also quite possible that we will end up in exactly the same or even in a worse position than where we are today. However, we can set ourselves a long-term strategic goal (point C) that, if achieved, will take us considerably beyond where we are today and possibly even beyond our competitors – in other words, it will give us a competitive advantage that will lead to long-term survival. The difference between point B and point C is 'strategy'; those actions that will help us achieve our strategic goals. Strategic goals are also known as long-term or strategic objectives. Being 'strategic' thus involves the following:

- It is not 'business as usual' – we cannot simply keep doing what we have been doing for years and years and describe it as 'strategic'.
- It reaches across all business functions, that is, it is an organisation-wid issue, and across all managerial levels.
- It is not a quick fix or a small change. It requires a large, sustained chang effort over a long period of time.
- It requires a large commitment of resources – it is not cheap or easy.

- While it may not be the domain of top management only, and it may be influenced by many other people, top management is ultimately responsible for achieving strategic goals (or for failing to achieve them) as we indicated in Chapter 1, Section 1.3.

2.3.2 The importance of strategy

Strategy is a coherent story about the future direction of the organisation. It provides members of the organisation with a framework to guide decision-making processes.

The strategic management process should combine the views and thinking of many members of the organisation and communicates the outcome back to the organisation so that everyone follows the same strategy.

Strategy is, in a sense, the verbalisation of the organisation's aspirations and accordingly provides an inspirational element that may be far removed from the realities of the present. In this sense, a good strategy can inspire, unite and motivate members of the organisation.

2.3.3 Defining strategy

Strategy has been described variously as the long-term direction of the organisation, a pattern in a stream of decisions,[13] the means by which organisations achieve their objectives and the deliberate choice of a set of activities to achieve competitive advantage.[14] These definitions make provision for both deliberate choices and for unplanned and emerging strategies. However, if we accept the idea that strategy is a conversation, we can imagine that strategy is shaped by ongoing discussions about the future of the organisation, and that strategy may simply be a believable story about the future of the organisation. What all of these definitions have in common is the notion of a direction for the future, whether it is a 'pattern' that can be recognised from the activities and decisions of the organisation, a deliberate choice of a set of activities, or the steps taken to achieve strategic goals.

Building on these definitions, and accepting that strategy is primarily a human activity, we define strategy in this book as the ***direction provided by the actions and decisions of strategists in pursuit of organisational goals.***

2.3.4 Defining strategic management

Traditionally, strategic management has been defined as setting strategic direction, setting goals, crafting a strategy, implementing and executing the strategy, and then over time and through a controlling process, initiating whatever corrective adjustments and corrections are deemed appropriate. However, more recent views have suggested that strategy is not this sequential and discrete, but is somewhat messier, overlapping and iterative. Independent of the process followed to develop and manage strategy, the purpose of strategic management is to ensure that the organisation applies the following four key elements:

1. Clear and consistent long-term strategic direction in terms of what the organisation wants to achieve in the future.
2. A profound understanding of the external environment to ensure that the organisation is able to align itself with opportunities and to deal with threats as effectively as possible.
3. An objective knowledge of the key resources and capabilities the organisation possesses, as well as its value to enable the organisation to build on these and develop a distinct competitive advantage.
4. The proper alignment of organisational structure, systems, culture, and functional and operational management (collectively referred to as organisational architecture) to ensure the effective implementation of strategic plans, portfolios, programmes, projects and initiatives.

Strategic management is ultimately about consistently aligning the organisation with its internal and external environments, as shown in Figure 2.3. In this figure, *strategic direction* refers to the long-term goals of the organisation which can be expressed as, for example, vision and mission statements. It relates to the key elements against which all strategic decisions should be measured.

- External consistency refers to the extent to which the organisation's strategy is aligned with the opportunities and threats in the external environment (refer to the components of the external environment explained in Chapter 1, Section 1.6). Significant changes in the external environment will most likely require some changes in strategy.
- Dynamic consistency measures the extent to which the strategy of the organisation is consistent with the key resources and capabilities of the organisation in its micro-environment (refer to the components of the internal environment explained in Chapter 1, Section 1.6). In other words, is the organisation making the best possible use of its resources and capabilities to benefit from opportunities and to avoid having to deal with threats.
- Internal consistency addresses the extent to which the organisational architecture (such as structure, systems, human resources, technology and processes) are aligned with the strategy. It also considers whether planning at lower levels of management in the organisation is broadly aligned with strategy. In this view of strategic management, strategising can be seen as the efforts of strategists to ensure consistency on all three levels of management and within the boundaries of the strategic goals of the organisation. Strategising will require strategic decisions to be made, and this is the focus of the next section.

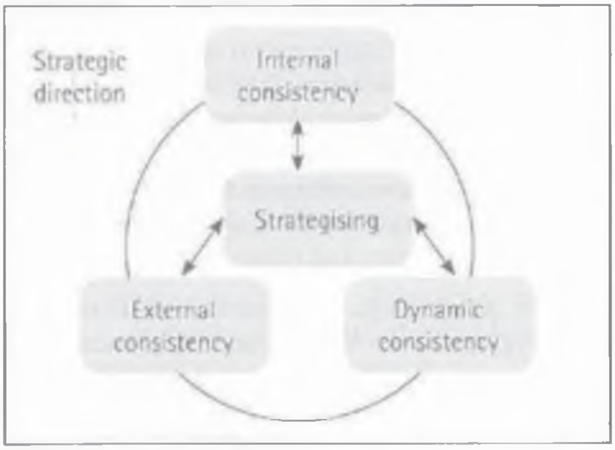


Figure 2.3 *Successful strategic management: striving for consistency*

LO 4: Identify the characteristics of strategic decision-making, and provide guidelines to strategic decision-makers to aid them in making better strategic decisions.

2.4 Strategic decisions

Strategic decisions that strategists need to make are influenced by two factors, cognitive and rational aspects, as well as political processes. These are explained below.

- **Cognitive and rational aspects.** The term 'cognitive functioning' refers to an individual's ability to perform various mental activities associated with learning, problem-solving and decision-making. Strategists, as important problem-solvers and decision-makers in an organisation, should adopt a logical approach and try to be as objective as possible when they are solving problems and making decisions. When making decisions, strategists could consider two primary decision-making models, namely the rational and the bounded-rationality model. In the case of the rational model, the strategist should select the best possible solution to the problem – known as optimising. However, while the rational view is strongly emphasised in the prevailing views of strategy, it has been recognised that managers are generally restricted by their own information-processing capabilities, which brings us to the second decision-making model, namely 'bounded rationality'. This refers to a situation in which strategists use satisficing and select the first possible solution to a problem that meets the minimal criteria. Strategists should know which model to use and when. They should optimise – apply the rational model – when making high-risk decisions in conditions of uncertainty. When they are making low-risk decisions, they should select the first option that meets the minimal criteria.[14]

- **Political processes.** Strategists will not necessarily agree on the best course of action to achieve strategic goals and may use their sphere of power and influence or persuasive (or dissuasive) language to sway others towards their preference. This is known as political behaviour in organisations. Strategists are ultimately, like all human beings, social and political beings, influenced by their backgrounds (eg education, culture and religion) and personalities in their quest for status and power. It is, therefore, almost impossible to expect strategic decisions to be entirely objective and rational.

In environments where fast strategic decision-making is required, the following guidelines can aid strategists in their decision-making processes:[15]

- **Developing more than one alternative course of action or solution to a problem.** This will help minimise the influence of politicking. Strategy simulations can be used to improve the strategists' abilities to generate and evaluate alternatives more quickly.
- **Getting real-time information.** Instead of waiting for formal reports, fast decision makers obtain the information they need from operational data and by informal discussions with other managers and members of the organisation.
- **Relying on experience and trusted advisers.** This entails not depending on junior managers and consultants for analyses, but developing a network of trusted and proven advisors.
- **Trying to reach consensus, but not at all costs.** There will be occasions when there is simply not enough time to establish consensus, and the majority should, at some point, make a decision.

In strategic decision-making, it is sometimes important to remember that it is 'better to be vaguely right than exactly wrong',[16] meaning that the time and cost associated with more accurate information will not always be of equal benefit in the decision-making process. In the next section, we will consider the question of how the success of strategy can be measured.

LO 5: Explain how the success of strategy can be measured.

2.5 How do we measure the success of strategy?

Competitive advantage and sustainability are often mentioned in the same context. However, the measure of strategic success is not always a simple matter. On the one hand, there are proponents of shareholder capitalism, who suggest that the creation of shareholder wealth through profitability is and should remain the only measure of strategic success. However, shareholder capitalism and the drive for 'profit at all cost' were heavily implicated as a leading cause of the 2008–2009 global economic crisis, with detractors suggesting that an excessive focus on profits (and especially short-term profits) was not sustainable.

On the other hand, the *stakeholder approach* (explained in Chapter 1, Section 1.7) requires a focus on balancing the often-conflicting needs of multiple stakeholders such as employees, shareholders, the environment and local communities. While we increasingly see large corporations embracing the concept and reporting, not only on their financial results, but also on their social and environmental contributions (so-called 'triple-bottom line' reporting), the stakeholder approach is criticised for vastly increasing the complexity of strategic decision-making and diluting the strategic goals of the organisation.

Michael Jensen proposes that the two approaches should meet somewhere in the middle, and that ultimately enlightened shareholder value maximisation is exactly the same as enlightened stakeholder theory.[17]

LO 6: Discuss a contemporary strategic management framework.

2.6 A contemporary strategic management framework

Although we acknowledge the contribution of traditional strategic management perspectives to our understanding of this important field, we also acknowledge that we need to incorporate newer thinking in our perspective of strategic management. To this end, we have devised the contemporary framework of strategic management (Figure 2.4) which serves as the framework for this book. This model, and the outline of the book are discussed in more detail below.

In Section 2.2, we identified various universal principles of strategic management. One of these principles was that strategy is both deliberate and emergent (as indicated in Section 2.2.5). From a deliberate strategy perspective, strategy drives organisational architecture and it is the job of managers responsible for implementing strategy to ensure that the elements of organisational architecture (such as structure and culture) are aligned with the chosen strategy. From an emergent strategy perspective, we argue that organisational architecture is so influential that it affects strategy formation profoundly. In our view, there is constant tension between strategy formation and organisational architecture, and this is depicted in Figure 2.4. We can think of this as a tug of war between strategy formation and organisational architecture. Sometimes, the strategy formation process is going to dominate and the architecture is going to follow. For example, Discovery's decision to invest in retail banking, requires them to make the necessary changes to ensure that their organisational architecture is aligned with the new direction of the organisation. At other times, the organisational architecture might lead and the strategy might follow. In the case of the South African Post Office, for example (see the practising strategy box below), we could argue that their existing national branch infrastructure, capabilities, and especially the tenacious efforts of CEO Mark Barnes, have a lot more to do with their bid to take on the Sassa business that it being a deliberate predetermined strategy.

Practising strategy: Sassa and Post Office secure social grants deal[18]

The South African Social Security Agency (Sassa) and the South African Post Office (Sapo) have reached a 'landmark' agreement to ensure social grant beneficiaries continue to receive their payments after Sassa's contract with Cash Paymaster Services (CPS) ends on 31 March 2018, Minister in the Presidency Jeff Radebe announced on Sunday morning.

In a setback to the ambitions of Sapo CEO Mark Barnes, who had hoped Sapo's Postbank would be the sole service provider, it is to be just one of four payment channels available to social grant recipients. The hybrid model the parties agreed to will also enable beneficiaries to receive their monthly payments via bank accounts at commercial banks, merchants in large retail shops, and a 'second tier' of merchants that includes village banks, general dealers, small retail outlets, and spaza shops. The hybrid model will be phased in over five years.

Sapo would provide cash disbursements through its branch network, particularly in locations close enough to replace existing cash pay points, he said. At present 2.9 million, a little less than a third (29%) of all grant beneficiaries, receive cash payments.

2.6.1 Strategy formation

In this book, we use the term strategy formation deliberately. Most textbooks refer to the formal process of developing a strategy as **strategy formulation**. However, as we take both the formal and informal elements of strategy development into account, strategy formation is a more accurate term. Strategy formation consists of three elements, namely, process, context and content.

- Process. In the first place, there are a number of processes that can be both formal and informal, involved in the development of develop strategy. They relate to the question 'how' strategy develops in the organisation, and is the focus of Chapter 3. We also examine strategists and strategising in more detail in this section (and Chapter 4), as the practices and communication of strategists at all levels ('strategising') influence how strategy is formed. Strategising can contribute towards both strategy formation and the shaping of organisational architecture. For example, middle managers, in their interactions with customers, may realise that there is an opportunity to expand the product range of the organisation and canvas top managers to affect it. Or, regional managers may realise that there is a problem with the structure of the organisation and how it supports the strategy, and may influence role-players to make the required changes.

- Context. Strategy is always context-bound. In other words, it takes place in a certain internal and external context, and this provides us with the 'why' of strategy. For example, a business in Botswana has to contend with the global context, the continental context, regional issues, country issues, the industry it is competing in, and with what is happening within the organisation. This external context and the risks it present will be explored in more depth in Chapter 5, while the internal context and the strategic resources and capabilities of the organisation will be the focus of Chapter 6.
- Content. The content of strategy refers to the actual development of strategies (the 'what', in other words) to compete in industries and to create shareholder value, and we will examine this aspect in more depth in Chapter 7.

2.6.2 Strategy implementation

Strategy implementation consists of three important elements, namely change management, organisational learning, and resource allocation.

- Change management. The alignment of organisational architecture with strategy formation does not happen naturally, and the organisation has to put in place formal processes to manage the large-scale change associated with strategy. This aspect is explored in Chapter 8.
- Organisational learning. This relates to the less formal processes of organisational learning to recognise and respond to the need for change is discussed in Chapter 9.
- Resource allocation. The allocation of resources to portfolio, programmes, projects and organisational structures responsible for giving effect to strategy is the topic of Chapter 10.

2.6.3 Strategic control

Continuous environmental scanning (both formal and informal) helps to ensure monitoring and control processes. On the one hand, environmental scanning and control need to ensure that the planned strategy is on track and to alert key decision-makers if interventions are required. This is represented by the arrow from left to right. On the other hand, leaders, strategists and other role-players in the organisation (eg market intelligence experts) may pick up signals from the environment that could affect the strategy formation process. This is represented by the arrow from right to left. This aspect is examined in more depth in Chapter 14.

2.6.4 Organisational architecture

Organisational architecture is a management tool that is used to describe the workings of an organisation, especially with regard to the alignment of strategy and the organisation.[19] It is a model of the organisation that can be shared by everyone involved in managing change and aligning strategy with structure. There are many different perspectives on organisational architecture and what it comprises, but for purposes of this book, we have focused on the four main elements, namely culture, leadership and governance, structure, and resources and capabilities.

- **Culture.** Peter Drucker once said that 'culture eats strategy for breakfast'.[20] This observation suggests that culture is so powerful that no plan will work if it is counter to the culture of the organisation. In Chapter 11, we focus on organisational culture and its vital role in aligning strategy and organisational architecture.
- **Leadership and governance.** Chapter 12 deals with the closely related issue of leadership and its role in strategy implementation and governance.
- **Structure.** The structure of the organisation refers to the physical manifestation of the organisation in terms of geographical distribution, positions, reporting and communication lines, and so on. The role of structure in the alignment of structure and strategy is the topic of Chapter 13.

Resources and capabilities

The success of organisations is dependent on them possessing unique strategic resources and valuable capabilities that form the foundation upon which the organisations are built and can grow. The role of resources and capabilities in the alignment of structure and strategy is the topic of Chapter 5.

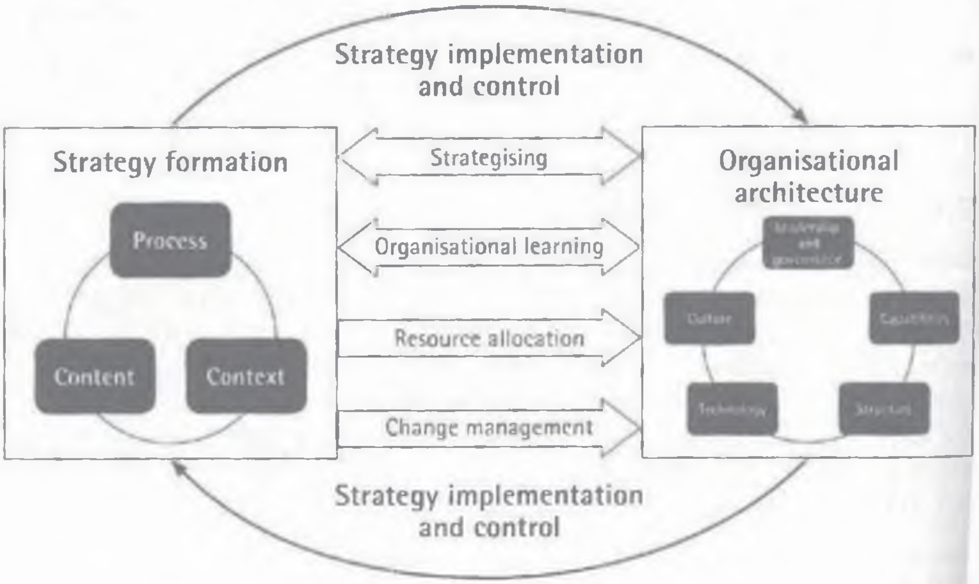


Figure 2.4 *An integrated framework of strategic management*[21]

The big picture

In this chapter, we proposed that strategy is generally a messier process with more participants than conventional perspectives of strategy, as a formal process, would suggest. In developing our perspective, we suggested that a variety of strategists contribute, through their strategising activities, to ensure that the organisation is continually aligned (through its strategic choices) with its external and internal environment. In examining strategy, we also adopted the perspective that the context of Africa is a critical influence on strategising and strategy, and suggested that organisational sustainability (the ability to sustain resources and the uses thereof) is a key goal of any organisation. Table 2.2 is a summary comparison of the conventional approach to strategic management and our approach in this book.

Summary of learning outcomes

LO 1: Explain the origins of strategic management.

In Section 2.1, we discussed the evolution of strategy as a military concept to the notion of strategic management as a concept utilised by modern businesses in the pursuit of competitive advantage.

LO 2: Identify and explain the universal principles of strategic management.

While there may be many different perspectives of what strategy is, Section 2.2 introduces seven principles of strategic management that most academics and practitioners of strategic management agree on.

LO 3: Define strategy and explain its importance to the organisation.

In Sections 2.3.1 through 2.3.4, we explain what it means to be strategic, and develop definitions for 'strategy' and 'strategic management'. We also explore the importance of strategy and the organisation's strategic management.

LO 4: Identify the characteristics of strategic decision-making, and provide guidelines to strategic decision-makers to aid them in making better strategic decisions.

Strategic decisions are complex and there are no clear 'right' answers. In Section 2.4, we outline the rational and cognitive aspects, as well as the political aspects of strategic decisions, and provide guidelines for 'good' strategic decision-making.

LO 5: Explain how the success of strategy can be measured.

The business world is filled with examples of the negative effects of pursuing short-term profits above all else. In Section 2.5, we explain that strategy should always be about the long term and creating value for stakeholders (ie sustainability), rather than about short-term profits.

LO 6: Discuss a contemporary strategic management framework.

In Section 2.6, we introduce the idea of an integrated framework for strategic management, which also serves as an outline for this book. The framework suggests that strategic management is ultimately about finding a balance between the processes of strategy formation and organisational architecture.

Table 2.2 *A comparison of a conventional approach to strategic management and our approach*

	Conventional strategic management	Our approach
Central focus	Understanding how organisations develop and maintain competitive advantage	Understanding what strategists do to achieve and maintain competitive advantage
View of strategy	Abstract – a characteristic of the organisation	The strategic acts, talk and documents that strategists produce
Responsibility	Top management formulates, middle management implements	A wide range of strategists is involved and influence the process
Process	Logical and rational	Messy, experimental and iterative
Process flow	Thinking before doing	No clear separation between thinking and doing
Key influences	Cognition, micro-economic	Cognition and politics, micro-economics and sociology
Goal	Competitive advantage and sustainability	Competitive advantage and sustainability

Discussion questions

1. Explain the origins of strategic management.
2. Identify and explain the universal principles of strategic management.
2. Explain the difference between 'strategy' and 'strategic management'.
3. Describe what 'strategic' means.
4. List the characteristics of strategic decisions.
5. What guidelines would you give to strategic decision-makers to improve strategic decision-making in their organisations?
6. Explain what success means in strategic terms.
7. Differentiate between corporate and business level strategy.

8. Explain what is meant by internal consistency, external consistency and dynamic consistency.
9. Would you describe the decision by Discovery to open Discovery Bank as a strategic decision? Substantiate your answer. (See https://mybroadband.co.za/news/banking/200968-new-discovery-bank-on-track.html for more information on the decision.)
10. Explain the contemporary framework of strategic management to your colleagues (or fellow students) with the help of practical examples.

Learning activities

1. Interview a manager in your organisation, or any organisation of your choice. Determine whether the organisation follows a deliberate approach to strategic management or an emergent approach (or perhaps a little bit of both).
2. Visit the website http://www.managementexchange.com/blog/gary-hamel-are-you-really-serious-about-innovation and watch the video 'Are you really serious about innovation?' by Gary Hamel. After watching it, what is your view on the role of innovation in strategic management?

Endnotes

1 'Low volume' in this case means high prices, and low sales volumes (such as the very expensive Tesla S).

2 For more background on the Hyperloop train concept, see https://www.youtube.com/watch?v=7A7GsAPR3J0.

3 *The Art of War by Sun Tzu* (written about 500BC) is widely regarded as one of the first known works on strategy.

4 Porter, M. 1998. *Competitive advantage: creating and sustaining superior performance.* New York, NY: The Free Press.

5 Grant, R.M. 2013. *Contemporary strategy analysis*, 8th ed. West Sussex: Blackwell.

6 For more background, see MyBroadband (online). 2 March 2017. New Discovery Bank on track. Available at: https://mybroadband.co.za/news/banking/200968-new-discovery-bank-on-track.html (accessed 19 July 2017).

7 Ibid.

8 Grant (2013: 17–18).

9 Mintzberg, H., Lampel, J., Quinn, J.B. & Ghoshal, S. 2003. *The strategy process, global* 4th ed. Upper Saddle River, N.J.: Prentice Hall.

10 Johnson, G., Whittington, R. & Scholes, K. 2011. *Exploring strategy: text and cases*, 9th ed. Essex: Pearson Education, p. 517.

11 Compiled from information available on https://www.bidvest.co.za/about.php.

12 Brevis, T. & Vrba M.J. 2014. *Contemporary management principles.* Cape Town: Juta, p. 266.

13 Mintzberg et al. (2003).

14 Porter (1998).

15 Adapted from Eisenhardt, K.M. 1990. 'Speed and strategic choice: how managers accelerate decision making'. *California Management Review*, 32(3): 39–54.

16 A quote by British philosopher Carveth Read, often wrongly attributed to economist John Maynard Keynes.

17 Grant (2013: 37).

18 Adapted from: Tamar Kahn. SASSA and Post Office secure social grants deal. Business Day Live (online). Available at: https://www.businesslive.co.za/bd/national/2017-12-10-sassa-and-post-office-secure-social-grants-deal/ (accessed 13 February 2018).

19 Lee, G.J, Venter, R. & Bates, B. 2004: 'Enterprise-based HIV/AIDS Strategies: Integration through Organisational Architecture.' South African Journal of Business Management, 35(3): 13–22.

20 This famous quotation is generally attributed to the late business management guru Peter Drucker.

21 Adapted from a framework developed by Prof Peet Venter for the module 'Managing Strategic Change, a core module of the Masters of Business Leadership (MBL)' at UNISA

3 A process perspective of strategic management

Annemarie Davis

LEARNING OUTCOMES

After studying this chapter, you should be able to:

LO1: Explain the process perspective of strategic management.

LO 2: Criticise the process perspective of strategic management.

LO 3: Identify and explain the management levels involved in strategic management.

LO 4: Explain strategy strategic planning and recognise the strategic direction and environmental analysis in organisations.

LO 5: Explain strategy implementation and recognise strategic programmes, projects, the various drivers of strategy implementation and the operationalising of strategy in organisations.

LO 6: Explain strategy review and control and identify the main strategic control mechanisms in organisations.

KEY WORDS

- Process perspective of strategic management
- Management levels
- Strategic management
- Vision (or vision statement)
- Mission (or mission statement)
- Strategy planning
- Strategy implementation
- Strategic control
- Balanced Scorecard
- Strategic goals

CHAPTER ORIENTATION

In Chapter 2, we explained that the aim of strategic management is to ensure that an organisation achieves competitive advantage, and sustains its competitive advantage over competitors. Strategic management helps organisations to achieve superior performance and sustainability over the long term. Although there are many different approaches to strategic management, the ultimate aim of any strategic management activity is survival and long-term goal achievement in a changing environment. However, strategic management is not only aimed at improving the long-term survival of profit-oriented organisations, but it also adds value to non-profit organisations, public organisations, governments, sport societies and schools. In fact, the principles of strategic management are such that it can help and guide any organisation, institution and individual towards achieving their goals despite changes in the environment.

The case study describes Capitec's success in the banking industry. The basis of Capitec's success is its commitment to its medium- and long-term strategy. The case study also highlights the fact that a clear understanding of the needs of the market informed Capitec's efforts to offer simplified and affordable banking products. The Capitec strategies are formulated through a deliberate process to evaluate strategic options in terms of the business context in which it finds itself, which is the focus if this chapter.

The process to formulate strategies can take many forms and involves the entire organisation on various levels. Table 2.1 in Chapter 2 depicted the levels of strategic decision-making and indicated the three levels of strategy (corporate level, business level and functional level). For the most part, all organisations will have strategies on each level and the implementation of these strategies cascades throughout. Yet, the approach followed is unique to each organisation and there may be vast differences between, for example, Capitec's approach and that of the Absa Banking Group. In addition, the approach followed by a smal business may be entirely different from the approach followed by a larg business which has clearly defined business levels and business units What is, however, found to be common among the different approache to formulating strategies is the involvement of senior management, focus on the long term and a commitment to the entire organisatio (and not only a business unit, department or section within). It i necessary to note here that the process of formulating strategies entai much more than strategic breakaways and glossy integrated reports. is also entirely possible that some organisations have all their strategi written down and documented while others have a less formal approac The process of formulating strategies leads to actions to implement th strategies and deliberate attempts to monitor their progress.

Strategic management and the processes associated wi strategising are not new concepts. Strategic management has be part of every organisation, albeit in a deliberate and formal approac or an emergent adaption to survive in a changing environment. T original approaches to strategic management were grounded business policies and planning approaches. Strategic manageme then evolved into a process consisting of definite stages or phas Later, and most recently, strategic management is considered fron practice perspective, wherein the impetus is on the 'doing' part.

This chapter focuses on the process perspective of strategic management, which can be described as a formal, rational approach to developing deliberate strategies for achieving strategic competitiveness and competitive advantage. It is part of strategy formation, as illustrated in Figure 3.1, focusing on the *content* part of strategy formation. The discussions in this chapter will commence with an explanation of the process perspective of strategic management, followed by an explanation of the new competitive realities and criticisms of the process perspective. The management levels involved in strategic management will then be addressed. Thereafter, each of the phases in the process perspective of strategic management will be explained with practical examples illustrating these phases.

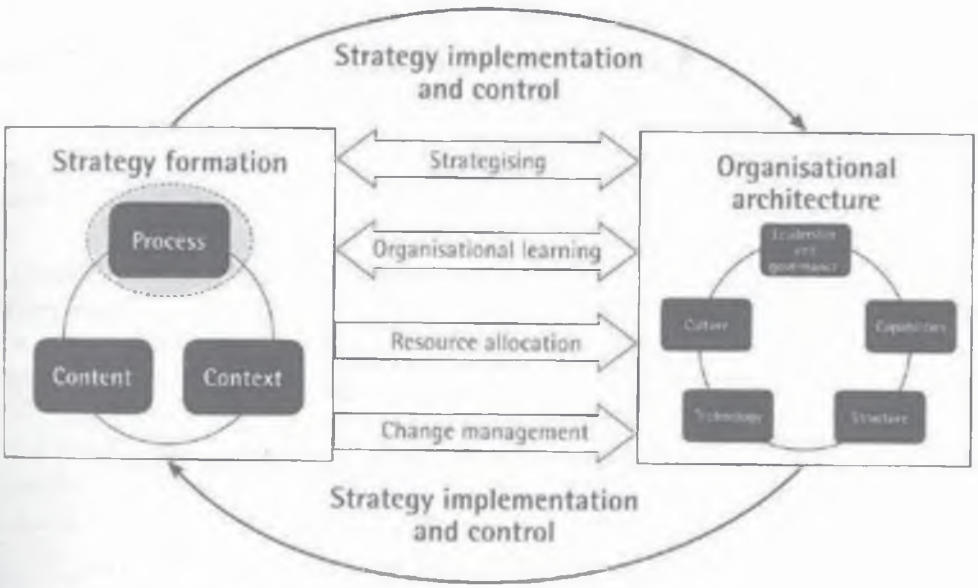


Figure 3.1 *Strategic Management as a process*

Case study

Capitec – no longer just a *new kid on the block*

The four major South African banks, Standard Bank, Absa Bank, FirstRand Bank and Nedbank, share about 80 per cent of the market. The remainder of the market belongs to a combination of other role-players in the industry. According to the South African Banking Sector Overview, the SA banking industry consists of 17 registered banks, two mutual banks, 14 local branches of foreign banks, two co-operative banks and 43 foreign banks with approved local representative offices.[1] When one looks at the latest full-year data from the retail banks, the battle to be the biggest is fierce between FirstRand and Standard Bank. What is exciting to see is the growth of Capitec. Out of nowhere in 2001, Capitec emerged with a dream to provide low-cost financial services to low-income groups. From a humble beginning, Capitec moved in and, 15 years later, celebrated an increase in headline earnings of 18 per cent to R3.8 billion for the 2016 financial year. These earnings represented a record growth of 1.3 million with 8.6 million active clients.[2] During March 2017, Capitec revealed that it was adding 120,000 new banking clients each month![3] In terms of the customer base, Capitec secured more than 15 per cent of the customers in the South African banking sector.

What is the secret to Capitec's success? How did it move from being the new kid on the block to becoming a noticeable presence and a real threat to the big four banks in South Africa?

According to the 2016 South African Customer Satisfaction Index (SAcsi) report, Capitec outcompeted all the other banks in terms of customer satisfaction – for three years in a row.[4] Capitec changed the game of banking by offering a simplified and affordable product – built on set fees and a single account over the often-complex calculations and bundled product offerings from competing groups.[5]

Capitec is led by its CEO, Gerrie Fourie, who confirms that the bank will continue its focus on the fundamentals of delivering simplified banking that is affordable and easy to access through personal service.

> *This resonates with most South Africans and is what sets us apart, especially in the current tough economic climate, giving clients a sense of value and allowing them to feel in control of their money. Through strong marketing communications, a focus on client service and positive word of mouth, the Capitec brand has grown in stature, with South Africans from all walks of life accepting Capitec as their first choice bank.*[6]

Overall, Capitec is committed to sustainable profit. This is achieved through the righ strategy, focused leadership, a healthy corporate culture based on strong values an responding to stakeholders' needs. Capitec's strategies are built on providing a uniqu service, enhancing the product offering, growing the client numbers, increasin transaction income, managing costs of credit to clients, and responsible risk managemen These strategies are crafted over the short to medium term (one to five years) withou losing focus on the long term (more than five years). The long-term view is to becom a preferred global retail bank enabled through virtual banking. The foundation of Capitec's success includes its competitive culture and its ability to achieve results through operational excellence and teamwork. These are key ingredients in Capitec's growth and its success in executing an innovative strategy.

LO 1: Explain the process perspective of strategic management.

3.1 A process perspective of strategic management

The traditional view of strategic management is that it is a process with distinct stages or phases. The approach adopted in this book is that strategic management is a complex and dynamic discipline and that a static, linear process does not consider the complexity or the environment in which the organisation operates (refer to the contemporary strategic management framework provided in Chapter 2, Figure 2.4). However, an understanding of the process perspective of strategic management is a valuable starting point and offers a sound theoretical foundation from which to work.

The three stages of the process perspective are depicted in Figure 3.2.

Figure 3.2 *The process perspective of strategic management*

The strategy planning stage is often also referred to as strategy crafting. The strategy implementation stage is also referred to as strategy execution and strategic control is also referred to as the strategy review stage or strategy review and control stage.

It is important to realise that strategic management is a continuous activity and information obtained through the strategic review or control stage feeds back into strategic planning and strategy implementation. The following section offers a more detailed explanation of each of these stages.

3.1.1 Strategic planning

The strategic planning stage is the starting point of the strategic management process. The process perspective to strategic management is often also referred to as the traditional perspective. Traditionally, it was accepted that the roles between the different levels of management were clearly defined and that the top managers were the key strategists in the organisation, while the middle and lower level of managers were mostly involved in implementing the strategies developed by the top management team. Strategic planning, according to the process perspective, is the stage in which the top management team (the strategists) decide on the strategic direction of the organisation as a whole. Typically, this stage mostly involves senior management who conduct various analyses of the organisation itself, as well as of the environment in which it operates. Part of this phase is the setting of strategic direction, in other words, deciding on the future of the organisation and setting the overarching goals of the organisation. For example, when looking at the case study about Capitec, the founder, Michiel le Roux, had a vision for a low-cost bank for low-income customers. The vision formed the centre of the founding, listing and operations of the bank. The vision set the strategic planning process in motion. During this stage, the top management team devised a vision or dream for such a bank; analysed the environment and competitors, and then devised strategies to achieve its dream. The practising strategy box below provides comments from Michiel le Roux (founder) and Gerrie Fourie (current CEO) and show how the overarching goal is still guiding Capitec's activities – 15 years down the line. The practising strategy box also includes the company slogan which exclaims that Capitec offers simple banking – aligned to the original vision of offering a simple and low-cost banking solution.

Practising strategy: Capitec

Bruce Whitfield's interview with Capitec founder, Michiel le Roux, 20 July 2016[7]

Twitter comments:

'I originally had a very basic bank in mind.'[8]

'I told our shareholders we'll either be a big success or a small failure. Not in my wildest dreams could I foresee the success we've had.'

'We'll keep it simple. In 10 years it'll still be recognisable as the bank you see today.'[9]

Comments from new Capitec CEO, Gerrie Fourie:

> When asked what the future strategy for Capitec will hold, Gerrie Fourie stated that 'more of the same, but, my tenure will have an increased focus on what is in the client's best interest. ... I need to build on this platform and drive the organisation to deliver even more value for each client. This will further differentiate us from other banks, offering greater convenience and attracting more primary bank clients'.[10]

It's banking, just simpler.

> From one banking solution and innovative tech to Sunday and paperless banking, everything we do is to make your life easier and empower you to take control of your money.[11]

In addition to a company slogan, a range of management tools can be used to set strategic direction, such as a vision statement, a purpose or mission statement, or a statement of strategic intent. Some organisations also include a value statement. Looking at Capitec again, their slogan can be translated into a mission and values statement that provides more detail about their product and service offerings, their markets, the technologies they use to make banking simpler, and their commitment to their stakeholders.

During the strategic planning stage, various analyses take place and the senior managers gather information about the operations, resources and capabilities of the organisation. The senior management team also scans the environment to identify potential opportunities and threats, as well as evaluating the market or industry in which the organisation operates and collecting information on competitors. This is referred to as an external environmental analysis. The senior management team also scans the internal environment, in other words, the organisation itself, with the purpose of identifying its own strengths and weaknesses. Once all the information from the external and internal environments has been collected and analysed, the senior management team then considers the various strategic options and chooses those strategies where the fit between what the organisation can do with the opportunities is the strongest. In addition, the senior management team formulates the strategic goals for the organisation. For example, FlySafair entered the low-cost airline industry with a vision to open the skies to many who had never flown before.[12] Their strategy is premised on their commitment to make prices sustainable and to keep them low. FlySafair aims to keep costs per seat as low as possible. Part of its actions included changing the seats on its aircraft to make it lighter and thinner, thereby reducing fuel costs.[13] Linked to its mission to provide low-fare, hassle-free and on-time travel experiences, one of FlySafair's strategic goals may, for example, be that FlySafair will achieve a 95 per cent on-time performance while offering seats at 5 per cent less than competitors will. This deliberate decision to focus on low-cost air travel is a result of an external environmental analysis that identified the opportunities in these markets.

An analysis of the organisation's internal environment identified various strengths of the organisation that enable them to make use of the opportunities identified in the external environmental analysis. Once the strategies to take the organisation towards the achievement of its objectives have been selected, the next stage of the strategic management process starts, namely strategy implementation.

3.1.2 Strategy implementation

The second stage of the strategic management process is referred to as the strategy implementation stage and is considered the most challenging stage in any strategic management process. As we explained earlier, the process perspective to strategic management offers a traditional approach in which the top management team, or senior management team, was responsible for the strategy formation and the middle and lower-level managers were seen as the implementers of the strategies devised by the senior managers.

Once the senior management team has selected the strategies of the organisation, they need to be put into action. This requires the involvement of everyone in the organisation. The corporate strategies, and the senior management team's rationale for selecting them, need to be communicated to all parties. Not only should the organisation members be told what the strategies and overarching objectives of the organisation are, but the senior management team also need to ensure that there is understanding and buy-in because the wider the organisational support, the greater the chances of successful implementation. Members must be motivated and energised towards achieving these goals on business, functional levels and even individual levels.

Operationalising strategies are an important aspect of strategy implementation. They entail translating the overarching and strategic objectives into specific programmes, projects, tasks and activities. The middle and lower management levels in the organisation are responsible for this, as well as for overseeing it, so they must be empowered to do so. By translating the strategic goals or long-term objectives into shorter term goals and activities, the organisation members become aware of their roles in the strategic success of the organisation (refer to Figure 1.1 in Chapter 1 that depicts the hierarchy of organisational plans).

At its most basic level, strategy implementation is the action ('doing') stage of the process perspective of strategic management. Actions to successfully implement strategies are ensured through certain drivers such as leadership, management, and culture. Organisational culture is commonly referred to as 'the way we do things around here' and how things are done will impact on success. For example, if the organisational culture is negative and there is little support for the strategies, then the strategy implementation process becomes more challenging and can actually fail. But when the organisational culture is positive and there is wide buy-in, the efforts to implement the strategies are more co-ordinated and have a greater chance of success. Organisational culture and strategy are discussed in detail in Chapter 11.

The middle and lower levels of managers can use rewards to drive strategy implementation. By rewarding the actions, tasks and behaviour that contribute towards successful implementation of strategies, managers enhance the chances of strategy success. Managers should thus devise reward strategies and systems that are aligned to the overall strategic direction of the organisation.

The way that the organisation is structured also impacts on the strategy implementation process. If the strategy requires quick decision-making, then a bureaucratic structure that entails time-consuming red tape may hamper efforts. The organisational structure not only indicates the lines of authority and reporting, but also the process and lines for strategy implementation. Coupled with the structure of the organisation are the inherent systems and policies inside the organisation. Organisational systems, processes and policies are used to direct the execution efforts. Again, the systems, processes and policies should be aligned with the overall strategic direction of the organisation.

Finally, leaders and managers in the organisation need to empower and enable the employees and organisation members to carry out the tasks to implement the strategies. This requires the appropriate allocation of financial, human, physical and informational resources. If the resources are lacking, the implementation efforts will surely fail.

Although monitoring the implementation of the strategies takes place continuously, in terms of the process perspective on strategic management, it is regarded as the third stage.

3.1.3 Strategy review and control

Strategy review and control involves monitoring the progress of strategy implementation, measuring actual or realised performance, comparing actual performance with planned performance, identifying problems and instituting any necessary corrective actions. Although described as the third and final stage in the strategic management process, it is a continuous process. As strategies are implemented, the strategy review takes place.

Different methods of strategy review exist. One such method is continuous environmental scanning, which can be considered a review method as it provides feedback on changes in the environment that may impact on strategic choices and their execution. Another form of strategy review is implementation control. Similar to operational control, this is where deviations from the plans are identified and addressed as they occur. This implies that corrective measures are taken during the strategy implementation process to ensure that the strategic management process continues successfully.

It is mostly senior and middle managers who are involved in the strategy review process. Most important is the feedback from the review that needs to serve as input in the amendment of existing strategies and goals, or the possible total reconsideration of the strategies and goals. Continuous feedback forms the foundation of the strategic management process.

LO 2: Criticise the process perspective of strategic management.

3.2 The new competitive realities – criticising the process perspective of strategic management

The biggest critique of the process perspective of strategic management is that, in being a linear process, the complexity of the environment is not considered and dealt with sufficiently. Also, the process perspective supports the notion that it is mainly the top management team or senior managers who craft or formulate strategies while other levels of management merely implement those strategies.

In practice, strategic management is much more complex and dynamic than is portrayed in the process perspective. Strategy is not something that an organisation *has*, but is rather something that an organisation, and the people in the organisation, *does*. The reality of strategic management in the contemporary business environment is that it is a messy and complex process, influenced by many different aspects. Strategy, in reality, is crafted through a process of conversation and input from all levels in the organisation and inputs from various stakeholders (as discussed in Chapter 1, Section 1.7).

In Chapter 4, we take a closer look at *who* does strategy in organisations.

LO 3: Identify and explain the various management levels involved in strategic management.

3.3 The management levels involved in strategic management

In a medium to large-sized organisation, there are usually three levels of management, namely top management, middle management and lower-level management. Top management comprises the CEO, the board of directors and senior managers. As described above, the top management team (or senior management team) will play a major role in setting the organisation's strategic direction and in analysing the environment. The information they gather will then be used to formulate the strategies

It is mostly the middle and lower-level managers who are responsible for the execution of the strategies through the managing of employees. The top managers rely on the middle managers to ensure that their planned strategies are implemented Top management then becomes more involved once again during the strategy review process. Chapter 4 offers a more detailed discussion of strategists.

LO 4: Explain strategic planning and recognise the strategic direction and environmental analysis in organisations.

3.4 Strategic planning

The following section discusses in more detail the process of strategic planning. The practising strategy box offers some background on Katlego Global Logistics and includes the vision and mission statement to serve as an example.

Practising strategy: Katlego Global Logistics[14]

Katlego Global Logistics (Pty) Ltd was founded in 1998 by Moses Maboi and borne out of his drive and enthusiasm for attaining efficient and dependable service in the freight logistics industry. From the onset, Moses was motivated by his passion for his country and his dream to contribute to South Africa's economic potential by partnering with stakeholders to contribute to the development and value add for black-owned and -managed companies. Given his years of experience in the industry, Moses set out, not only to render quality and professional services in all freight- and trade-related services, but also to the develop skills of employees through training and exposure.

Katlego Global Logistics offers solutions in the areas of clearing and forwarding, air freighting and car-going, supply chain and inventory management, logistics, customs broking and project shipments.

Katlego Global Logistics adds the value of time and place utility as it offers integrated services and tailored, customer-focused solutions for managing and transporting documents, goods and information. This involves the integration of information, transportation, inventory, warehousing, material handling and packaging, and occasionally, security.

The company has become recognised as a freight and courier industry expert, supply-chain innovator and a business partner. It does not use contractors within the boundaries of South Africa, assuring customers that it is tracking and keeping their precious cargo safe. With a dedicated national fleet of vehicles ranging from small, utility one-ton vans to larger eight-ton trucks, Katlego Global Logistics is well represented nationally.

The vision of Katlego Global Logistics is to be the preferred supplier in the freight logistics industry known for excellent service delivery. Their mission is:

To lead with insight and innovation, constantly strengthening the company's resilience and ensuring that our customers' needs are addressed with the utmost efficiency.

3.4.1 The strategic direction of the organisation

The organisation's management and employees need to know the reasons for the organisation's existence. The strategic direction clarifies the overarching purpose and goals of the organisation, as well as indicating to external stakeholders what the organisation is about. Several management tools are used to set the strategic direction. As an example, the practising strategy box on Katlego Global Logistics provides its vision and mission statements that offer a clear message on its purpose. The following section explains how the vision statement, the mission statement and the strategic goals are used to direct the actions and strategic efforts of the organisation over the long term.

Not only does the strategic direction provide the organisation and its members with a primary direction, but it also helps bind the organisation members as a cohesive unit. Figure 3.3 depicts the benefit of strategic direction. The diagram below indicates the multiple different directions in which the organisation and its members are working. The other one shows how the overall stated strategic direction (represented by the blue arrow) aligns the efforts of the entire organisation and its members in one direction.

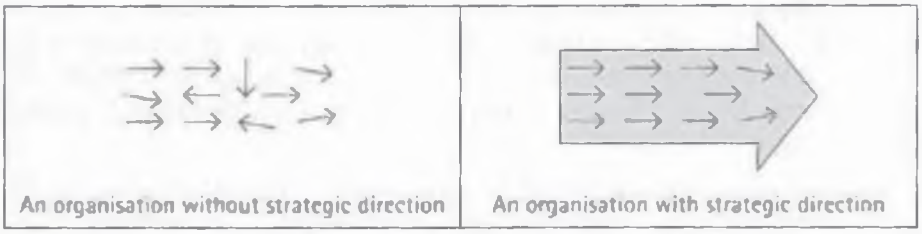


Figure 3.3 *The benefits of strategic direction*

Having sound strategic direction is a powerful contributor to strategic success as it forms the starting point for a carefully planned and implemented strategy. It also provides focus and directs all actions towards achieving the same goal.

Some organisations do not have separate vision and mission statements, while others have only mission statements. Organisations are diverse and varied, just like the people who work in them, and this creates room for a range of different practices. The strategic direction can be expressed through a vision, a mission or both. What is crucial is that the entire organisation and its members know where they are going and what they are working towards.

Table 3.1 offers a summary of the advantages of having clear strategic direction, expressed through the vision and mission statements of organisations.

Table 3.1 *Advantages of having clear strategic direction*

1.	It provides direction and a clear indication of what the organisation is aiming for.
2.	It ensures that all the organisational efforts and all the organisation members are working towards the same goals.
3.	It offers a clear message to internal and external stakeholders on what the organisation wants to achieve over the long term.
4.	It guides problem-solving and decision-making as the end goal is clear to all.
5.	It provides the organisation with a unique identity.
6.	It contributes to synergy among all managers and other employees and stakeholders.

The vision statement

The vision statement is often referred to as the dream of the organisation. It is used as an indicator of the desired future position of the organisation. It is often not realistic in literal terms. For example, the vision of Katlego Global Logistics (see the practising strategy box provided earlier) is to be 'the preferred supplier in the freight logistics industry known for excellent service delivery'. This may seem overly ambitious, but it is a powerful statement designed to motivate the entire organisation. Another example is that of the freight division of Grindrod Limited. Their vision is 'to be a dominant and profitable freight services provider focusing on infrastructural development on the African continent'. The delineation of 'African continent' clarifies their playing field. A good vision statement should identify the direction and future of the organisation. As the entire organisation and its members need to work towards reaching this future destination, it should be persuasive and credible, and easily understood.

There is no standard format for a vision statement. Some organisations may opt for short and punchy vision statements, while others may opt for more descriptive versions. However, there are certain guidelines for what a vision statement should be, namely:

- It should present a clear picture of a desirable future, something to which the organisation and its stakeholders can aspire.
- It should guide decision-making, yet be flexible enough to allow the organisation to respond to changes in the environment.
- It should be easy to communicate, to explain and to understand.

Ultimately, the vision is not just a statement on a piece of paper, but rather galvanises and directs people in the organisation.

The mission statement

The mission statement is also called the purpose statement of the organisation. In its most simplistic form, the mission statement provides an indication of what the organisation does and why it exists. The mission statement builds on the vision statement. The mission statement is not only used internally within the organisation, but often used in external communication and the media. The mission is as much an internal statement as it is an external statement. The three core components of a mission statement are *product and/or service, market* and *technology*:

- The product and/or service: A mission statement should indicate the product or service that the organisation offers and should answer the question 'what are our primary products and/or services that we offer?'
- The market: A mission statement should indicate the market that it hopes to serve and should answer the question 'who is our primary target market?'
- Technology: Lastly, a mission statement should indicate the method (technology) used to deliver this product or service to the market and should answer the question 'what technology will be used to provide the products and services to our market/s?'

In addition, a well-formulated mission statement could also contain the following:

- Often organisations give an indication of their commitment to stakeholder by including how important their customers are, or how the organisatio invests in its employees or builds relationships with business partners (se Chapter 1 for an explanation of stakeholders). A good example is City Lodg Hotels:[15]

  We will be recognised as the preferred Southern African hotel group. Through dedicated leadership, teamwork and kindness, we will demonstrate our consistent commitment to delivering caring service with style and grace. We will constantly enhance our guest experience through our passionate people, ongoing innovation and leading-edge technology. Our integrity, values and ongoing investment in our people and hotels will provide exceptional returns to stakeholders and ensure continued, sustainable growth. Through acts of kindness, we will make a positive difference to our guests, our colleagues, our communities and our environment.

- The organisation's orientation towards survival and growth is oft expressed through stating their commitment to economic objectives. I example, ADvTECH, a placement, private education and training provi listed on the JSE, specifically refers to their aim to build, grow and achie

  We aim to BUILD and grow a high-quality organisation in education, training and placement that is widely recognised for passionate commitment and success in enriching people's lives and future. We aim to GROW a reputation for our ability to make a real difference to the people we serve, for our connectedness and partnerships with African and global markets and players, for the relevance, quality and usefulness of our offerings, and for the enterprising and agile way in which we tackle our task. We will ACHIEVE this by focusing on *our customers and taking a lead from our markets, by our innovative approach, especially in harnessing the power of technology, and by striving for excellence and sustainability in all we do.*[16]

- **Organisational values** are principles that the organisation stands by; these values are held in high regard within the organisation and sets the standard of how the organisation wants to do business. An example of a mission statement that includes the organisation's values is Virgin Money, a financial services brand that entered the South African market with an aim of simplifying banking:

  Our mission is to give you: 1. A great deal, 2. Straightforward financial products, 3. Brilliant service.[17]

- The **organisational philosophy** offers an indication of how the organisation plans to do business. The organisational philosophy is often linked to ethical standards; for example, Premier Hotels and Resorts, a hospitality service provider with hotels and resorts in South Africa has the following philosophy:

  We are a professional, passionate, caring and empowering company that encourages innovation and engagement. We are a learning organisation *committed to the retention and development of our people as an essential part of building strong, respectful and* enduring guest relationships. *Our staff are motivated, friendly and obsessive about enhancing the guest experience through meeting and* exceeding expectations for quality service.[18]

The value of setting clear strategic direction, whether through a vision or mission statement or both, is an important contributor to organisational success.

The process of formulating a mission statement

Strategic direction is long term and ought to remain unchanged for an extended period. Organisations that change their strategic direction on an annual basis send a message that they are not sure where they are going. As the vision and mission statements are an expression of the strategic direction, these should also remain largely unchanged except, perhaps, for minor amendments to the wording.

Although there is no one agreed method for drafting a mission statement, most agree that it should involve as many people as possible because this contributes towards acceptance. External consultants may also be called in, but it is very important that the strategic direction be created internally.

One way to craft a mission statement is as follows:

- Orient those involved as to what constitutes a well-formulated mission statement.
- Do a brainstorming exercise to generate as many creative ideas as possible.

- Collate all the draft ideas and distribute them for comment.
- Continue this process until there is agreement on what the mission should be.

In the case of a start-up business, it is easier for a management team to compile the strategic direction. For established and multi-business organisations, however, the management team will need to maintain the business operations while the process to amend or redesign the strategic direction is underway.

Strategic goals

Flowing directly from the mission statement is the need to translate the overarching direction of the organisation into strategic goals. The strategic goals have a shorter time frame than the vision and mission statements (five to ten years as a rule of thumb) because they are determined by the nature and the level of complexity and rate of change in an organisation and within its industry.

To be of value, strategic goals need to be measurable in terms of time, money and units. Table 3.2 compares well-formulated and poorly formulated strategic goals.

Table 3.2 *A comparison of well and poorly formulated strategic goals*

Poorly formulated strategic goals	Well-formulated strategic goals
Our goal is to increase our market share.	Our goal is to increase our market share by 3% by the end of 2021.
The goal for 2021 is to expand our product range.	The goal for 2021 is to expand our product range by introducing two new products in the baby clothing division.
By 2023, we will open new stores.	By 2023, we will open one new store in Mahikeng, in the North West Province and one new store in Kimberley, Northern Cape.

The SMART principles can be used to formulate good strategic goals:

S – specific
M – measurable
A – achievable
R – realistic
T – time

Goals should be specific and measurable so that people know exactly what it is th will be expected of them. Goals must be considered attainable by those who need work towards achieving them (if, on the one hand, they seem impossible to reac people will see no point in even trying or will quickly become discouraged).

The goals should be realistic, yet aimed at a level that will motivate people (on the other hand, if they are too easy to reach, people will not be inspired to work harder). Finally, a well-formulated goal is linked to a specific time period so people have a deadline to work towards (an open-ended goal will carry no sense of urgency and could take years to complete).

Over and above meeting the SMART principles, strategic goals should also be congruent with the mission statement components, the overall strategic direction of the organisation and should focus on the key performance areas of the organisation (the next section will focus on the use of the balanced scorecard to identify these areas). Also, goals should be acceptable – people tend to pursue goals that are consistent with their preferences and perceptions. Lastly, strategic goals should be flexible. Organisations function in a turbulent business environment, which makes it necessary to allow for goals to be modified due to changing circumstances.

Using the balanced scorecard to set strategic goals

The balanced scorecard (BSC) is a strategic management tool that was developed by Kaplan and Norton.[19] When used in the strategic planning stage, it guides the organisation and management team to translate the strategic direction into strategic goals. One of the benefits of the BSC is that it offers a balanced approach to setting strategic goals. The 'balance' is grounded in its four perspectives: financial, customer, learning and growth, and business processes. At the centre of these, is the strategic direction, which will include the vision, mission and other statements.

For each perspective of the BSC, strategic goals need to be formulated that will contribute to the achievement of the strategic direction. Each perspective offers a view on what needs to be done with a focus on two internal measures (internal business processes and learning and growth) and two external measures (customers and finance). The balance between the internal and external perspectives ensure that the strategic goals are aligned with the strategic direction. The four perspectives of the BSC are explained below:

- The financial perspective, with a focus on the financial performance of the organisation. The financial perspective is linked to the expectations and needs of the shareholders, as well as to the financial performance or stewardship of the organisation.
- The customer perspective, with a focus on how the organisation's customers perceive it. The customer perspective works towards a focus on satisfying customer needs and a consideration of how customers see the organisation.
- The learning and growth perspective, with a focus on sustainable growth, value creation and innovation. This perspective is also called organisational capacity and is aimed at the employees (human capital) and the capacity to achieve its goals.
- The business process perspective, with a focus on the core capabilities at which the organisation must excel in order to be competitive. This perspective is linked to quality and efficiency in all that the organisation does.

Each of these four perspectives is linked to a specific question which guides the setting of the strategic goals. Given the foci of each of these perspectives, the BSC is a handy tool that is used to translate the strategic direction into goals and targets. These targets can be seen as the shorter term aims at the business level, which guides the activities or actions needed on the functional level. Figure 3.4 provides guiding questions for each perspective. These four questions are used to select the most important strategic goals on corporate level (refer to Table 2.1 in Chapter 2, where a distinction was made between the various levels of strategy). A successful application of the BSC may include two to five goals in each perspective and each goal should be joined by a performance target that indicates whether the goal is achieved, as part of the review process.

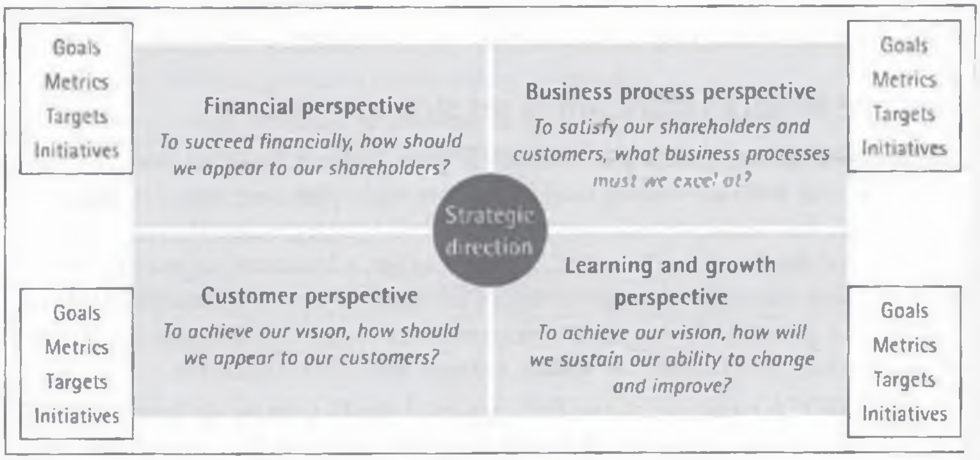


Figure 3.4 *The balanced scorecard*[20]

The scorecard is balanced in that it includes strategic goals and measures for a four perspectives. The purpose is to 'balance' the strategic goals by ensuring tha one business area (such as finance) does not dominate the strategic direction of th organisation, while, at the same time, ensuring a focus on a few key metrics tha could serve as a 'scorecard' for the whole organisation.

Table 3.3 provides examples of goals, metrics, targets and initiatives for eac of the four perspectives.

Table 3.3 *Examples of goals, metrics, targets and initiatives for a balanced scorecard*

Perspective	Goal	Metric	Target	Initiative
Financial	Consistently achieving above-average returns on shareholders' investment	Return on equity (ROE)	25% ROE per annum for the next five years	Reduce the cost of inputs to achieve higher productivity levels

Perspective	Goal	Metric	Target	Initiative
Business process	More innovative product development	New product revenue as a percentage of total revenue	Increase new product revenue to 30% of total revenue by 2022	Introduce a new product development process
Customer	Retaining valuable customers	Customer retention rate	Improve customer retention rate by 20% over the next five years	Implement a loyalty programme
Learning and growth	Reducing waste in the manufacturing process	Waste as a percentage of total manu-facturing cost	Reduce waste by 50% over the next five years	Introduce a total quality management programme

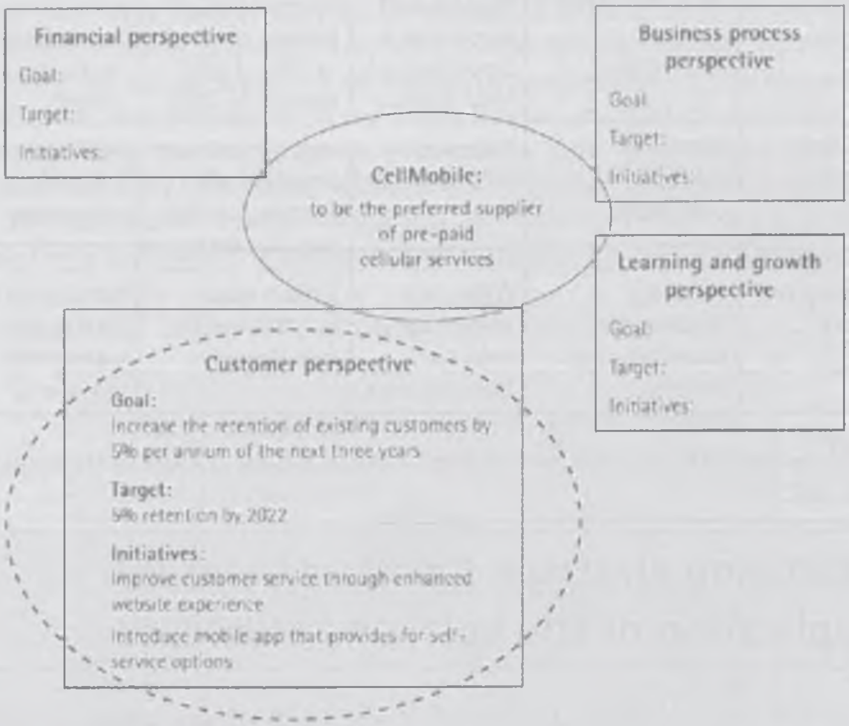
The following practising strategy box uses CellMobile as an example of the application of the BSC.

Practising strategy: An example of the application of the balanced scorecard

CellMobile is a (fictitious) organisation in the South African cellular telephone industry. Their vision is to be the preferred supplier of pre-paid cellular services. Their growth strategy is aimed at developing their market by targeting customers in rural areas where other cellular services are unreliable and often interrupted.

If CellMobile uses the balanced scorecard, their starting point will be the vision and strategy which is aimed at growth. In each of the perspectives, they will set objectives, measures, targets and initiatives that contribute to being the preferred supplier and growing their market. For example, in terms of the customer perspective, a goal might be to increase the retention of existing customers by 5 per cent per annum for the next three years. The targets to be achieved, then, would be 'five per cent retention' and 'within a three-year period'. The initiatives to achieve this could now be devised, such as improving customer service by enhancing the CellMobile website services, or by making pre-paid vouchers more readily available. In terms of the business process perspective, CellMobile could set a goal to expand the cellular phone towers to ensure better service delivery and thereby be in a position to recruit more customers and thus grow their business. The goal could be to expand by two new towers every three months over the next two years. For this goal, the targets would be 'two towers', 'every three months' and 'over the next two years', and the initiatives could then be formulated.

The diagram below depicts the customer perspective within CellMobile.



The balanced scorecard offers a valuable framework for setting strategic goals.

Once the strategic goals have been formulated, the strategy selection process starts. This is discussed in Chapter 7. In Sections 3.5 and 3.6, we provided a brief overview of the strategy implementation and strategy review processes.

3.4.2 The role of environmental analysis in the strategic management process

Continuous scanning of the external and internal environments of an organisation supports the strategic management process. The purpose of scanning the external environment is to identify **opportunities** that may be exploited, or **threats** that may prevent the organisation from attaining its strategic objectives.

Internal analysis is done for the purpose of understanding the organisation's key **strengths** and key **weaknesses**, so that it can build on key strengths and counter or mitigate key weaknesses. The role of resources and capabilities is discussed in Chapter 6.

While many organisations do environmental scanning periodically (for example, at an annual strategic planning workshop) it should really be an ongoing process that forms part of strategic evaluation and control (see Chapter 14).

LO 5: Explain strategy implementation and recognise strategic programmes, projects, the various drivers of strategy implementation and the operationalising of strategy in organisations.

3.5 Strategy implementation

The purpose of strategy implementation is to align the internal and external environments with the chosen strategy. Strategy implementation is often seen as the most challenging stage in the strategic management process. Scholars such as Jooste and Fourie,[21] Candido and Santos,[22] and Speculand[23] documented some of the challenges linked to strategy implementation. In addition to the recognition in the scholarly community, examples of strategy implementation failures often reach news headlines. Numerous studies have been conducted on strategy implementation and there is agreement amongst scholars and practitioners that strategy implementation is challenging, and it is where most strategy initiatives fail.

3.5.1 Strategic programmes and projects

Figure 1.1 in Chapter 1, depicts the hierarchy of organisational plans, which indicates that strategic plans and initiatives should be managed as special programmes and projects with a view to eventually becoming part of the day-to-day operations of the organisation.

3.5.2 Key drivers for implementing strategy

Once a strategy has been selected, it needs to be communicated to the entire organisation and those who are tasked with implementing it, need to know exactly what is required. Effective leadership and management are vital to the success of any strategy. The managers and leaders in the organisation are responsible, not only for communicating the strategy, but also for guiding the actions required to execute it. Simply informing staff and other stakeholders is not enough. A general understanding of the rationale behind the strategy and the alleviation of any uncertainties are both vital to ensure agreement and support among all who are responsible for strategy implementation.

Strategy execution and renewal is a continuous process with specific targets to be reached at specific points in time, and organisational management and leadership are responsible for keeping employees motivated. Because change goes hand-in-hand with uncertainty and resistance, leaders will need to help members come to terms with the change and empower them to guide others to do the same. Behaviour, actions and tactics will need to be adapted. Involving people in the change process and ensuring that they understand the reasons for the change will ease the transition. There should be a fine balance between driving the change and giving people time to adjust.

Strategy implementation deals with the 'doing' part of the strategy, and organisational culture plays an important role in the success or failure of an organisation. An unhealthy and negative culture can cause undue resistance to change which seriously hampers progress. This is something management and leadership will have to tackle as it can undermine the entire strategic management process. Organisational culture can help or hinder the strategy execution process. Chapters 11 and 12 deal with organisational culture and the role of strategic leaders respectively in more detail.

Resource allocation is another important driver of strategy implementation. Resources comprise human resources, physical resources, information resources and time. Coupled with the allocation of resources, is the need for structure. Organisational structure indicates the lines of authority and responsibilities in the organisation. It forms the backbone of the organisation and helps to direct the various actions required to implement the strategies. The organisational structure needs to support the implementation of the strategies. A more detailed discussion of organisational structure is included in Chapter 13.

Finally, the last driver of strategy implementation is organisational learning, which is covered in Chapter 9. Organisational learning is a process in response to change and provides for change, creating new knowledge and practices and, ultimately, the transferring of knowledge.

3.5.3 Operationalising strategy

Below is a brief explanation of the functional tactics (ie short-term goals) to explain how strategy is translated into operationalised actions. We remind you of Table 2.1 in Chapter 2 where the levels of strategic decision-making are described. This section deals with operationalising strategic goals on the business and functional levels.

It is important that the entire workforce knows, not only the overall direction of the organisation, but also what needs to be done on a daily, weekly and monthly basis in order to achieve the strategic goals. The middle management cadre will take the lead in this process by translating the strategic goals into specific, measurable, achievable, realistic goals to be achieved within a year or less. Although the strategic goals are specific and measurable, their focus is on the long term. In order to ensure that these strategic goals are operationalised, they need to be translated and adapted for the medium term. The same criteria required for setting strategic goals is important here. When the middle managers (such as the section heads, departmental leaders and site managers) involve the supervisory level in this process, the acceptance of these medium-term goals is ensured. Medium-term goals are typically set for the functional areas in the organisation, such as the marketing, operations, human resources, finance and purchasing departments. The balanced scorecard also assists in this process. As we have explained earlier, the balanced scorecard has four perspectives and the organisation's vision and strategy form the starting point. Within each perspective, the balanced scorecard is used to specify the goals, measures, targets and initiatives. Each business unit and department in the organisation will have its own focused and specifically balanced scorecard.

In addition to the medium-term goals, functional tactics also need to be developed. Functional tactics provide even more detail to ensure the daily operationalisation of the organisation's strategies. A functional tactic is developed in support of the short-term goals. Functional tactics are even more specific and require wider participation. The focus of the functional tactics is the tasks and activities required to operationalise the strategy and indicate what needs to be done immediately and on a daily basis.

Finally, the organisational actions to operationalise the strategy are guided by the organisational policies. Policies are often referred to as 'red tape' but form an important part of the fair and justified actions of the organisation and its workers. Policies provide detailed and specific guidelines and rules that direct the organisational activities – the framework and specific 'do's and don'ts'. Policies are often referred to as standard operating procedures. It is important that the organisational policies be documented and recorded in written format and made available to all the organisational members. In line with fair business practices, the policies should also be made available to the customers and other stakeholders. Policies guide the organisational managers in the control and co-ordination of organisational activities.

LO6: Explain strategy review and control and identify the main strategic control mechanisms in organisations.

3.6 Strategy review and control

This chapter started with an explanation of the strategic management process. We indicated earlier that the process begins with the development of the organisation's strategies, followed by their implementation. The third phase is the review and control phase. In this phase, the management uses a range of different measures and processes to check on the progress of the implementation process and monitors the need for changes to some of the previously developed strategies and goals. As organisations operate in changing environments, the need for regular and continuous monitoring and review is important. Different methods to review the strategy implementation process exist and although the focus of each methodology is different, the aims remain the same: review and control.

Our focus is on the four main strategic control mechanisms, namely, premise control, strategic surveillance, special alert control and implementation/execution control. Typically, all four of these methodologies will be employed, but at different stages of the implementation process. When the strategies are devised, a number of assumptions or premises are made. Premise control is aimed at reviewing these assumptions in a focused way. If any of the assumptions are no longer valid, a change in the strategy is required. This type of control is very specific. With its exclusive focus, it is possible that other factors, that may also bear an impact on the success of the strategy, are overlooked. Hence the need for the strategic surveillance type of control.

Strategic surveillance is also referred to as environmental scanning and is not focused, but rather opens the opportunity for managers to consider a whole range of internal and external environmental factors. As organisations operate in a changing environment, some changes may occur that were not predicted. Despite the proactiv nature of the strategic management process, it is impossible to predict and plan fo all changes, especially unexpected changes that lead to a total reconsideration o the strategies. This type of control is often referred to as implementation control o execution control. It takes place during the strategy execution process and comprise four steps: setting the standard, measuring the actual, identifying deviations an taking corrective measures. The functional managers are responsible for this type c control, with inputs from the supervisory level. Special alert control is linked to largely unpredicted and unexpected event that warrants a total review of the strateg Chapter 14 provides a detailed discussion of the different types of strategic revie and control methodologies.

The big picture

The process perspective of strategic management advocates that strategic manageme comprise three stages, namely, strategic planning, strategy implementation ar strategy review and control. The process perspective supports a linear approa to managing organisations strategically and is also referred to as the tradition approach. Yet, as organisations and management thinking evolve, new perspectiv and approaches to strategic management have emerged. These perspectives do n replace the traditional perspective, but rather open opportunities for managi organisations in new competitive realities.

The focus of this chapter was to introduce different perspectives and to provi specific details on the process perspective of strategic management.

Summary of learning outcomes

LO1: Explain the process perspective of strategic management.

The process perspective is a traditional approach to strategic management that follo a mostly linear process that is driven by the top management team and divided ir three distinct stages or phases.

LO 2: Criticise the process perspective of strategic management.

The process perspective is a linear process that does not consider the complexity the environment in which the organisation operates. The process perspective also s strategy as a top-down function – with strategic decisions made by top managem and middle managers tasked with implementing it.

LO 3: Identify and explain the management levels involved in strategic management.

The different management levels involved in strategic management fall within three main categories: top management, middle management and lower-level management. For the most part top management is responsible for setting the strategic direction and middle and lower-level managers are responsible for the execution of the strategies.

LO 4: Explain strategy strategic planning and recognise the strategic direction and environmental analysis in organisations.

With the process perspective of strategic management, the first stage is strategic planning that starts with the setting of the strategic direction. By having strategic direction, organisations and its members form a cohesive unit. Strategic direction is expressed through a vision and mission statement. Organisations operate as open systems in changing environments which require environmental analysis. Environmental analysis includes and analysis of both the internal and the external environment. The purpose of scanning the external environment is to identify opportunities that may be exploited, or threats that may prevent the organisation from attaining its strategic objectives. Internal analysis is done for the purpose of understanding the organisation's key strengths and key weaknesses, so that it can build on key strengths and counter or mitigate key weaknesses.

LO 5: Explain strategy implementation and recognise strategic programmes, projects, the various drivers of strategy implementation and the operationalising of strategy in organisations.

The purpose of strategy implementation is to align the internal and external environments with the chosen strategy. Strategy implementation is often seen as the most challenging stage in the strategic management process. A number of drivers exist for strategy implementation. These include leadership, organisational culture, resource allocation, organisational structure and organisational learning.

LO 6: Explain strategy review and control and identify the main strategic control mechanisms in organisations.

Strategy review and control develop during this stage of the strategic management process. In this phase, the management uses a range of different measures and processes to check on the progress of the implementation process and monitors the need for changes to some of the previously developed strategies and goals. The four main strategic control mechanisms are premise control, strategic surveillance, special alert control and implementation/execution control.

Discussion questions

1. Depict the process perspective of strategic management diagrammatically.
2. Explain what vision, mission, and value statements entail.
3. Critique the process perspective of strategic management.
4. Explain the role of environmental analysis in strategic management.
5. Explain strategic programmes and projects.
6. Identify and explain key drivers of strategy implementation and identify these in organisations.
7. Explain strategy review and control and recognise various control mechanisms in organisations.

Learning activities

1. Interview two managers in any two organisations of your choice about their perception of the value of the strategic management process. What did you learn about strategic management from these interviews?
2. Visit the website of strategist Tony Manning and read the blog at http://www.tonymanning.com/stratblog/. What are the implications of this perspective for strategic management as a process?
3. Read some of the work by scenario planner Clem Sunter (or visit the website http://www.clemsunter.co.za/). What role does scenario planning and environmental scanning play in the development of strategies?

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5 The external context of strategy

Clifton Singh

LEARNING OUTCOMES

After studying this chapter, you should be able to:

LO 1: Explain the external environment in the context of strategic management.

LO 2: Explain the importance of strategic context in strategic planning and decision making.

LO 3: Analyse the remote environment to identify opportunities and threats facing an organisation.

LO 4: Analyse the market environment to identify threats and opportunities facing an organisation.

LO 5: Discuss strategic responses to changes in the external environment.

KEY WORDS

- Economic environment
- External (or macro-) environment
- External Factor Evaluation Matrix
- Global environment
- Industry
- Legal environment
- Market environment
- Opportunity
- Political environment
- Social-cultural environment
- Strategic agility
- Strategic ambidexterity
- Strength
- Technological environment
- Threat
- Weakness

CHAPTER ORIENTATION

The environment is what gives organisations their means of survival. In Chapter 1 (Section 1.6) we indicated that organisations source inputs from the environment, transform that into outputs, which is then given back to the environment. The success of an organisation as a system is largely determined by its successful interactions with the environment. Structurally, the management environment can be divided into the micro-, market and remote environments. This chapter focus on the market and remote environments.

Our case study 'Uber comes to Africa', paints a picture of the traditional metered taxi industry that faces new competition since Uber entered the market. The world of business is characterised by competition and unpredictability, and it is essential for strategists, organisations and industries to adapt and be responsive to changes in its environment and not to depend on their successes of the past. A dependence of successes of the past will be devastating with far-reaching implications.

The effect of the environment on organisations and their strategic choices should not be underestimated or considered lightly. Instead, organisations and industries must be able to respond quickly to changing circumstances posing as threats and opportunities, and alter their strategies accordingly as they strive for a strategic fit between their organisation and the environment.

Strategy is thus context-specific and while each organisation has unique internal and external contexts, the primary focus of this chapter will be on the external context, in other words, the environment outside the boundaries of the organisation, called the external (or macro-) environment. The external environment comprises two sub-environments, namely, the market and remote environments, which were explained in Chapter 1 (Section 1.6). Understanding these environments and their strategic context is vital to making strategic choices that will guide and direct the organisation. While the previous chapters focused more on how strategy is crafted, this chapter provides important tools that strategists can use to gain insight into the strategic context of their organisations and develop a strategic perspective of the organisation and its environment. Figure 5.1 depicts the focus of this chapter in relation to the broader strategic management process.

In this chapter, we will first explain the external environment in the context of strategic management. Second, an explanation will be provided for the importance of strategic context in strategic planning and decision-making. Third, an analysis of the remote environment for the purposes of identifying the opportunities and threats facing an organisation will be addressed. Then, attention will be given to the analysis of the market environment, in order to identify opportunities and threats to an organisation. Lastly, strategic responses to a changing external environment will be explained.

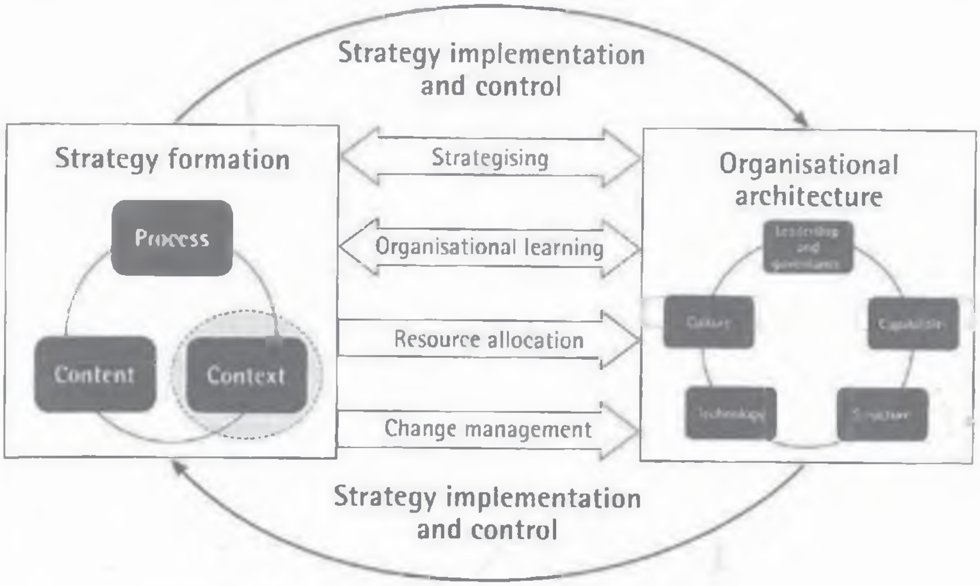

Figure 5.1 *The external context of strategy*

Case study

Uber comes to South Africa

There was a time, in the early days of motorised transport, when cars were not allowed to drive faster than 6.4km per hour and commercial motor vehicles were not allowed on public roads unless someone carrying a red flag walked in front of it. These were among a series of draconian laws enacted in Britain and parts of the USA from the mid-1860s, reportedly backed by railroad barons who were scared of the competition posed by the new founded 'road locomotives'.[1]

Some 120 years later, a similar battle is playing itself out on the streets of cities in South Africa. This time, the disruptor is the ride-hailing smartphone application, Uber, and the part of the rail barons is being played by the traditional metered-taxi industry.[2] Uber launched in South Africa in 2012 and has since redefined the traditional industry model for taxi operators. The Table 5.1 lists various consumer and competitor dimensions of the taxi industry and compares the traditional metered taxi and the Uber taxi in terms of these dimensions.

Table 5.1 *Traditional metered taxis versus Uber taxis*

Consumer and competitor dimensions of the taxi industry	Traditional metered South African taxis	Uber taxis
Reserving a taxi	Customers wander the streets looking for a cab or wait at a depot or call a central office and wait.	Customers connect to the Uber application on smartphones and reserve a taxi.
The taxi ride	The main aim of the taxi driver is to get the customer to his or her destination.	Taxi drivers perform their best since they are aware that services are rated and poor service rendered will influence future business.
Payment method	The taxi meter or the route travelled, determines the price charged by the metered taxi. Customers pay metered taxi drivers in cash.	The cost of using Uber is debited from the customer's bank account and no cash payments are necessary. Uber calculates the price by taking the following into account:[3] (i) base fare: the price for pick up; (ii) time: from start to the end of the trip; (iii) distance: kilometres of the route travelled; (iv) surge price (if applicable); and (v) tolls and other fees (if applicable). The base fare, time and distance rates will differ depending on the vehicle option chosen by the customer and the city.
After the taxi ride	Services rendered are not rated.	The customer rates the driver and the driver can improve his or her reputation for future customers.

Uber (a software development organisation) has experienced explosive growth around the world since it was founded in San Francisco in the USA in 2009 with just a single car. A valuation of Uber in February 2018 estimated it at a staggering US$72 billion (approximately R850 billion at the average US$/Rand exchange rate of R11.80 at the time of the valuation).

Hostility to Uber

Mention the word *Uber* and it is bound to set off a range of comments. Despite consumer willingness to try out and adopt Uber, it has run into obstacles in a number of its markets, both in developed and developing countries. The South African metered taxi companies and taxi operators are fighting back, co-ordinating protest marches and calling on the government to clamp down on Uber, which they accuse of flouting the laws that regulate public transport. Uber drivers are also intimidated by other metered taxi drivers claiming that Uber is stealing their business and operating illegally. However, more often than not, people who make use of Uber did not previously use metered cab taxis[4] and Uber flourishes globally.

LO 1: Explain the external environment in the context of strategic management.

5.1 The external environment in the context of strategic management

No organisation exists within a vacuum, and organisations should always be viewed as open systems – influenced by changes in its environment. For example, new trends in technology, nature and society are slowly revolutionising the business environment on a global and unprecedented scale[5] – no organisation can escape these changes as was also illustrated in the case study. This 'globality' is characterised by greater interconnectedness and interdependencies between countries and organisations. These forces emanating from the external environment exert an enormous amount of influence on organisations. Strategists in organisations are therefore required to respond appropriately to changes in their remote environments. Furthermore, as industry players, they should be able to adapt or actively change their market environments to enhance their competitive positions and survive.[6]

'Going green', 'eco-friendly' and 'sustainable practices' are now commonly accepted and are more than just buzz words or jargon. One of the aims of Uber, as discussed in the case study, is to improve the transportation ecosystem, proving itself as an organisation concerned about the natural environment. A growing number of customers, employees, investors and other stakeholders are demanding that organisations behave 'responsibly' in terms of the natural environment (where the natural environment is only one of the variables in the external environment). As such, a new compact between business and society is being advocated where 'business as usual' is no longer an option. The term 'compact' refers to an *agreement between various parties*. The agreement is the decision, approval and acceptance of a new arrangement/relationship (whether formal or informal) which is being advocated between business and society in general. The United Nations Global Compact (UNGC), for example, is a call to organisations around the world to align their strategies and operations with ten universal principles. These principles are human rights, labour, the environment and anti-corruption. Three specific principles were formulated for the environment theme, where the 'environment' refers to the physical or natural environment (as a variable in the remote environment of organisations). First, organisations should support a precautionary approach to environmental challenges. Second, organisations should undertake initiatives to promote greater environmental responsibility. Lastly, organisations should encourage the development and diffusion of environmentally friendly technologies.[7]

Historically, the business world has primarily always considered internal stakeholde (such as business owners, investors, employees and management) in developin strategy. Business is now increasingly under pressure to deal comprehensivel with external stakeholders (such as the community, government, activist group: competitors, the media, and so on) as well (you may refer back to the explanatio of the classification of stakeholders in Chapter 1, Section 1.7). Therefore, a profoun understanding of the external environment gained through knowledge of the interest and influence of key external stakeholders is paramount to strategic decision-makin and planning, and is recognised as a source of strategic value.[8]

The context within which organisations exist is defined by their market and remote environments. Figure 5.2 depicts the organisation and its environment consisting of the micro-environment (over which management has control) and its market- and remote environments (over which management has no control).

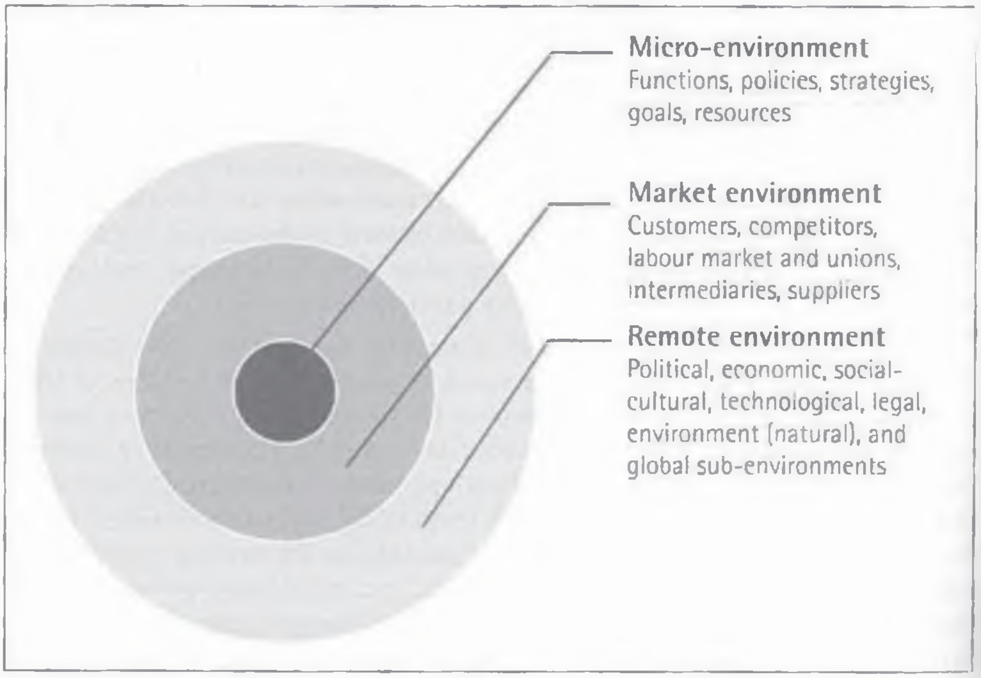

Figure 5.2 *The organisation and its environment*

Two levels of the analysis of the macro-/external environment, that will influence the organisation's strategic direction and strategic actions, can be identified, namely:

1. Analysis of the remote environment. This analysis focuses on the identification and forecasting of trends pertaining to political, economic, socio-cultural, technological, legal, environmental (or natural) and global variables.

2. Analysis of the market environment. This analysis focuses on the key role-players in this environment (such as customers, competitors, the labour market and unions, intermediaries and suppliers), along with the factors and conditions influencing an industry's profit potential.

Although these analyses will be discussed separately in this chapter, performance is likely to improve when the organisation integrates the results of both analyses.[9] The analysis of the remote and market environments will be explained in more detail in Sections 5.3 and 5.4 of this chapter.

LO 2: Explain the importance of strategic context in strategic planning and decision-making.

5.2 The importance of strategic context in strategic planning and decision-making

The boundaries and interfaces that exist between organisations and the external environment are relatively fluid and cannot be defined easily or clearly. As a result, unexpected changes in the external environment may occur from time to time, and strategists need to be prepared to react to these changes. Under such conditions, timely and accurate information about the environment is critical for strategic decision-making and planning. For example, if organisations know very little about the preferences of their customers and their future trends, they will have difficulty designing new products and/or services, setting up a production schedule, or developing strategic and marketing plans.

However, the reality is that strategists often do not have enough information about the external environment readily available. They are operating in turbulent industries and can be challenged even further when they have to operate under conditions of rapid change and uncertainty. Strategists are not only constrained by a lack of information about the environment, but also by a limited ability to understand and predict the future.

Ideally, for strategic decision-making and planning to be effective, strategists must not only understand the context of their current management environments, but also the context of their future management environments.

An organisation's success is, to a certain extent, determined by the characteristics of the industry in which it exists and the market for which it competes. Furthermore, different industries are characterised by different competitive conditions and dynamics. Hence, when viewed in relation to competitors, as well as to competitive *threats* and *opportunities* existing in the external environment, all organisations have inherent *strengths* and *weaknesses* and are exposed to external *threats* and *opportunities*:[10]

- Strengths are internal organisational resources and capabilities that can lead to a competitive advantage (Chapter 1, Section 1.8 provides an explanation of competitive advantage).
- Weaknesses are internal resources and capabilities that an organisation may not possess yet but are necessary, resulting in competitive disadvantage until the organisation acquires them.
- Opportunities are conditions in the external environment that allow an organisation to take advantage of organisational strengths, overcome weaknesses, and/or neutralise environmental threats.
- Threats are conditions in the external environment that may stand in the way of organisational competitiveness or the achievement of stakeholder satisfaction.

If strategists do not understand the strategic context, in other words, how the external environment affects their organisations, their ability to make decisions, formulate and execute plans will be severely limited.[11] When studying the organisation in relation to its external environment and key role-players in this environment, strategists should:

- take advantage of inherent or internal strengths and the identified opportunities arising from the external environment
- overcome inherent weaknesses, or neutralise identified threats found in the external environment in order to ensure the strategic 'fit' or consistency between the opportunities and threats in the external environment and the strengths and weaknesses in the internal environment.

Strategic direction is an outcome of melding the desires and expectations of key organisational stakeholders with environmental realities.[12] Therefore, a profound understanding of the external environment, coupled with an understanding of its key role-players, is paramount to charting an organisation's road to success. Understanding the external strategic context should lead to the identification of strategic alternatives and provide a basis for crafting strategies, as well as providing the organisation with a foundation for all other tasks of strategic management. The next section focuses on the remote environment, as a sub-environment of the external (or macro-) environment.

LO 3: Analyse the remote environment to identify opportunities and threats facing an organisation.

5.3 Analysing the remote environment

To a large extent, organisations can only respond to the fundamental forces arising from the remote environment. While individual organisations can exert some influence over their market environments, they can rarely influence the remote environment (except, for example, through radical technological innovation, as in the case of organisations such as Intel or Microsoft in the microprocessor, microcomputer and software industries).

In the discussion that follows, we will first identify the remote environmental forces, and will then discuss the remote environment in an African and regional context. Lastly, we will address the evaluation of an organisation's strategic response to factors in the remote environment.

5.3.1 The identification of remote environmental forces

The most important elements of the remote environment can be identified using the traditional PEST framework. They comprise the following factors:[13] *political (P), economic (E), socio-cultural (S)* and *technological (T) factors*. The traditional PEST model can be extended to include a consideration of *legal* (L), *environmental* (E) and *global* (G) factors, (where (E) refers to the natural environment) to yield the acronym PESTLE/G. You may also refer to Chapter 1 (Section 1.6) in which the management environment is explained.

Analysing the environmental forces and trends at a global, a regional and a domestic level, respectively, is important because it can have an impact on an organisation and its internal/micro- and market environments. Below are just a few examples of the implications that external environmental forces hold for markets and organisations:[14]

- Political factors. Political factors include aspects such as the government and its political policy and economic interventions and policies. The government of a country is a major role player in the remote environment of all organisations. An example of political forces in South Africa is the change of leadership in the ruling party, namely the African National Congress (ANC). On 14 February 2018, the former president Jacob Zuma resigned and was replaced by President Cyril Ramaphosa. This had an enormous effect on various indicators, for example, the value of the country's currency and business confidence. Business confidence can be measured in terms of the Business Confidence Index, which is the weighted mean of five sectoral indices, namely, that of manufacturers, building contractors, retailers, wholesalers and new vehicle dealers. Business confidence can vary between 0 and 100, where 0 indicates an extreme lack of confidence, 50 indicates neutrality and 100 indicates extreme confidence.[15] Index Points in South Africa increased to 45 Index Points in the first quarter of 2018 from 34 Index Points in the fourth quarter of 2017 – an increase of 11 points.[16] As a result of these influences, business organisations are also affected. For example, an increase in business confidence may result in organisations investing more in new machinery, equipment or buildings in order to increase their productive capacity in lieu of an expected increase in the demand for their products. Also, consumers will spend more, and foreign investors will be more willing to invest in South African organisations due to higher business confidence levels. South Africa has seen many key economic policy changes by government, especially for the period 1994 to 2013. The Reconstruction and Development Programme (RDF), as part of the election platform of the ANC in the 1994 elections, was chosen as the primary socio-economic programme with the aim to establish a more equal society through reconstruction and development, as well as strengthening democracy for all South Africans. Due to various constraints, the government replaces this policy in 1996 by a new macro-economic policy framework called the Growth, Employment and Redistribution (GEAR) strategy, with the aim to stimulate faster economic growth, which was required to provide resources to meet social investment needs. In 2005, GEAR was replaced by the Accelerated and Shared Growth Initiative for South Africa (ASGISA) as further development on the first two developmental strategies. ASGISA had the following aims: to reduce poverty by 2010, and to halve unemployment by 2014 from the 28 per cent in 2004 to 14 per cent by 2012. It also recognised that the policies implemented to address these issues needed to be at the forefront of economic policy decision-making. ASGISA was replaced in 2010 with the New Growth Path (NGP), envisioned to accelerate growth in the South African economy, and to do so in ways that rapidly reduces poverty, unemployment and inequality. In 2013, government introduced the National Development Plan (NDP) 2030 as South Africa's socio-economic development roadmap. This policy was adopted as the blueprint for a future economic and socio-economic development strategy for the country. The NDP is viewed as a policy blueprint for eliminating poverty and reducing inequality in South Africa by 2030. In order to address the country's socio-economic imbalances, the NDP identifies the key constraints to faster growth, among other things, and presents a roadmap to a more inclusive economy.[17]

- Economic factors. These include factors such as the economic growth rate, the inflation rate, interest rates and exchange rates. Economic forces influence the demand for products and services, so it is important for strategists to monitor and forecast events in the domestic and global economies. Economic forces are often interdependent with socio-cultural forces. For instance, an ageing population can influence unemployment figures and salaries of a younger workforce significantly.
- Socio-cultural factors. These include factors such as social values, culture, lifestyles and demographics. Stakeholder groups are products of society. Their values, morals, beliefs and subsequent behaviours and lifestyles are therefore influenced by society at large. Developing social trends may also offer organisations various opportunities. For example, health and fitness lifestyle trends have created opportunities in the home fitness, nutritional supplement, low carbohydrate food and even bicycle industries. Organisations therefore stand to gain if strategists can identify and assess the effects and opportunities presented by socio-cultural forces, as well as manage and sustain their relations and reputation with stakeholder groups.

- Technological factors. These include factors such as research and development, new products and processes, and new technologies. The innovation and technology fields have grown exponentially in recent years. They are continuously driving the development of new products and services, thereby creating new industries. They also have the power to transform society and revolutionise the way business is conducted. This is evidenced by the rise of the internet, as well as by the communication and computing industries. Innovation and technology can spill over from one industry to another, especially if they are closely related. The opening case study indicated that technology is responsible for changes in the metered taxi industry. Uber became a major role-player in this industry, which reinforces the statement that organisations should also monitor developments in innovation and technology in neighbouring, related and even unrelated industries. Strategists need to evaluate the consequences for their own products and services, creating strategies that could take advantage of these changes.
- Legal factors. These include factors such as regulations and laws with which organisations must comply. No organisation is fully exempt from government legislation and regulations. However, not all laws and regulations apply equally to all organisations. Some (such as smoking laws) pertain to specific industries, whereas other legislation (such as occupational health and safety, labour relations, and employment equity in South Africa) cuts across entire industries. In our case study, it was indicated that the South African government finds it difficult to regulate the new industry created by Uber. Once regulated, it will have an influence on Uber, as well as on the metered taxi industry.
- Environmental factors. These include ecological and environmental forces of nature such as weather, climate, climate change and associated factors such as water shortages. The Western Cape water crises in 2017/2018, as a result of prolonged drought, is affecting all industries in South Africa, especially the agricultural, hospitality and tourism industries. Even households and individuals are affected. For example, in 2018 Cape Town households were faced with water and sanitation tariff increases of approximately 27 per cent. An increase in these tariffs will have a negative effect on consumer behaviour and spending patterns, influencing all industries. The principles of the UNGC, alluded to earlier in Section 5.1, calls on organisations to align their strategies to their environmental principles.
- Global factors. Organisations are operating in an increasingly global economy. Examples of global trends[18] which have the potential to significantly affect and challenge strategists and leaders in the next 30 years are briefly discussed in Table 5.2.

Table 5.2 *Global trends*

Global trends	Explanation	Examples of implications for strategists
Increasing population	The world's population is increasing fast from 7.6 billion in June 2018 to an expected 9.7 billion by 2050.[19] The South African population, as on 4 June 2018, based on the latest United Nations estimates, is 57,348,015[20] and is expected to grow to 72,754,583 by 2050.[21]	The need for basic necessities, such as food, water and housing, will increase as the population increases, while, at the same time, water and food sources will come increasingly under pressure due to diminishing farmland and pollution.
Increasing urbanisation	Megacities with 10 million or more inhabitants will become commonplace. In South Africa, Johannesburg is set to be classified as a megacity by 2030, with its population exceeding 10 million people[22], while Lagos, Cairo and Kinshasa will each have to cater for over 20 million people.[23]	Due to the high urbanisation rate, the need for various products and services (such as the need for education, water, electricity, housing and medical services) to mention only a few, increases.
The spread of infectious disease	Migration and cross-border flow of labour and goods are increasing, causing the likelihood of epidemics and the spread of infectious diseases such as hepatitis A, typhoid fever, and malaria. An outbreak of listeriosis (a serious foodborne disease) has been ongoing in South Africa since the start of 2017. There were 978 laboratory-confirmed cases and 183 fatalities reported over the period 1 January 2017 to 14 March 2018.	Infectious diseases (such as malaria and meningitis) cause a growing demand for preventative measures (such as insect repellents and inoculations) and treatment options. Outbreaks of foodborne diseases may require strategists to place more emphasis on preventative quality controls, and to act quickly in the case of an outbreak. The food processing company and three of its retailers export to 15 countries in the African region. All of the affected countries had to recall the implicated products.[24]

Global trends	Explanation	Examples of implications for strategists
Natural resource crises	The global natural resource crises are worse than its financial crises. The 2016 Living Planet Report[25] calculates that humans are using 30 per cent more natural resources than the Earth can replenish each year, which is leading to deforestation, degraded soils, polluted air and water, and dramatic declines in the number of fish and other species. The problem is also getting worse as populations and consumption keep growing faster than technology can find new ways of expanding what can be produced from the natural environment. This has led to the prediction that by 2030, if nothing changes, humankind will need two planets to sustain its lifestyle.[26] In Africa and South Africa specifically, the need for and conflict over water resources are prominent.[27] Since 2014, the City of Cape Town has been experiencing a record drought for three consecutive years (the worst in more than a century). The drought, exacerbated by climate change and population growth, has sparked a water crisis in Cape Town. In March 2018, municipal leaders warned that residents are increasingly likely to face a 'Day Zero' scenario. Day zero is defined as the day when the supplying dams are depleted, and residents are expected to live on less than 25 litres per day. If the city is unable to deal with the crisis, then four million people may have to stand in line surrounded by armed guards to collect rations for drinking water.[28]	Organisations will increasingly be required to operate in ways that are environmentally sustainable by reducing their carbon footprint, reducing waste and reducing their water usage.

Global trends	Explanation	Examples of implications for strategists
Environmental degradation	Biodiversity is often used as an indicator of the state of the natural environment since it refers to the diversity of micro-organisms, plants and animal species, as well as to the ecosystems within which they interact and live. The 2016 Living Planet Report indicates the Living Planet Index (LPI), which measures biodiversity by gathering population data of various vertebrate species and calculating an average change in abundance over time. The LPI can therefore be regarded as an important indicator of the planet's ecological conditions. From 1970 to 2012, the LPI shows a 58 per cent overall decline in vertebrate species (mammals, birds, fishes, amphibians and reptiles). The most common threat to declining populations is the loss and degradation of habitat. This refers to the modification of the environment where species lives, by either complete removal, fragmentation or reduction in quality of key habitat characteristics. Common causes are unsustainable agriculture, logging, transportation, residential or commercial development, energy production and mining. For freshwater habitats, fragmentation of rivers and streams and abstraction of water are common threats. Species over-exploitation, pollution, invasive species, disease and climate change are further threats and contribute to environmental degradation.[29] The decline in species populations is inextricably linked to the state of the ecosystems that sustain them. Destruction of these ecosystems represents a risk, not just to plants and animals, but to humans as well – ecosystems provide us with food, fresh water, clean air, energy, medicine and recreation. Human life depends upon healthy and diverse natural systems for the regulation and purification of water and air, climate conditions, pollination and seed dispersal, and control of pests and diseases.	Organisations will increasingly have to understand the impact that its current and future operations will have on biodiversity and the ecological systems that they operate in. This is already becoming part of the legal environment. For example, in South Africa Environmental Management Inspectors (also known as the 'Green Scorpions') specifically police for transgressions of environmental laws and regulations.

Global trends	Explanation	Examples of implications for strategists
Economic integration	Economic integration refers to an agreement between countries in a geographic region to reduce and ultimately remove, tariff and non-tariff barriers to the free flow of products or services and factors of production among each other.[30] Economic integration is a phenomenon of the second half of the 20th century that has been experienced on a varying scale and intensity throughout the world. Countries from all continents seem eager to join economic alliances that range from customs unions to areas of full economic integration, such as the European Union. Strong and weak economies participate in such groups, aiming at stability and growth.	Inevitably, participating in these alliances conveys important changes in the domestic business environments of organisations. For example, the competition in the market environment of organisations may change completely as a result of economic integration. Changes in the quantity and quality of demand may also appear, requiring strategists to reconsider and change organisational strategies based on these changes. South African President Cyril Ramaphosa on 20 March 2018 punted the idea of a single currency for African countries in a bid to attract infrastructure investment and enable intra-African trade, a decision that will have an influence on all participating countries and organisations within these countries.
Advances in technology and information technology	Advances in technology create new processes, systems, material, equipment and components. New technology enables organisations to develop new and innovative products and/or services. Advanced information systems can disseminate essential, timely and accurate information faster and more efficiently. New processes can increase the productivity of organisations. New technology and information technology results in increased competition and forces organisations to use the latest technology to sustain their competitive advantage.	Organisations need to be aware of technological changes and how they affect their businesses. While organisations can use technology to improve their own efficiency, they can also be the victims of technology. There is the obvious threat of hacking, which means that organisations have to pay very close attention to cybersecurity. On a more fundamental level, technology can enable new breeds of competitors and change the business landscape, as we saw in the Uber case study earlier in this chapter.

Global trends	Explanation	Examples of implications for strategists
Biotechnology	Biotechnology is defined as the use of biological processes, organisms, or systems to manufacture products intended to improve the quality of human life. The earliest biotechnologists were farmers who developed improved species of plants and animals by cross-pollination or cross-breeding. In recent years, biotechnology has expanded in sophistication, scope and applicability. The science of biotechnology can be broken down into subdisciplines called red, white, green, and blue. Red biotechnology involves medical processes such as getting organisms to produce new drugs or using stem cells to regenerate damaged human tissues and perhaps re-grow entire organs. White (also called grey) biotechnology involves industrial processes such as the production of new chemicals or the development of new fuels for vehicles. Green biotechnology applies to agriculture and involves processes such as the development of pest-resistant grains or the accelerated evolution of disease-resistant animals. Blue biotechnology, rarely mentioned, encompasses processes in marine and aquatic environments, such as controlling the proliferation of noxious water-borne organisms.[31] Many organisations have begun investigating the application possibilities of biotechnology in their industries. Companies such as Motorola have begun investigating the potential of genetic engineering in computing as a first step toward a DNA-based computer.	While biotechnology offers many potential opportunities to organisations to increase their production and reduce their carbon footprint (for example, by using biofuel), it also has created heated debates around issues such as genetic manipulation of food, the use of stem cells from embryos in providing health services, and cloning. Biotechnology is an area in which organisations need to be very aware of the ethical risks they face.

Global trends	Explanation	Examples of implications for strategists
Governance	The business dictionary defines *governance* as the establishment of policies, and the continuous monitoring of their proper implementation, by the members of the governing body of an organisation. It includes the mechanisms required to balance the powers of the members (with the associated accountability), and their primary duty of enhancing the prosperity and viability of the organisation.[32] *Corporate governance* is defined as the framework of rules and practices by which boards of directors ensures accountability, fairness and transparency in an organisation's relationship with all stakeholders,[33] in order to improve the accountability of an organisation and to prevent massive disasters before they occur.	Corporate governance is an inevitable topic of discussion in corporate boardrooms, academic roundtables and among policymakers worldwide. Several events are responsible for this. First, corporate implosions over the last ten years and the subsequent increased demand for continuous improvement and transparency in the boardroom have heightened the pace of change for boards worldwide. Second, the wave of financial crises in Russia, Asia and Brazil in 1998, affected their entire economies and deficiencies in corporate governance endangered the stability of the global financial system. Third, corporate governance failures in the United States and Europe caused some of the largest insolvencies in history. In the aftermath of these events, economists, the corporate sector and the policymakers worldwide recognised the potential long-term consequences of weak corporate governance systems. In the wake of more recent corporate scandals relating to KPMG and Steinhoff, for example, it is likely that we will see an increased focus on corporate governance, and an increasing focus on the role of supposed 'watchdogs' such as auditing firms.

The implications of these global trends for strategists and their organisations are far-reaching. They have the potential to change individual organisations, entire industries or even entire economies. In this context, the change can be drastic or a radical re-organisation caused by trigger events and processes requiring change in order to improve the situation. As an example, environmental degradation caused by motor vehicle carbon dioxide (CO_2) emissions (above a certain threshold) has seen the introduction of an environmental levy on new motor vehicles manufactured or imported into South Africa. The objective of the levy is to ensure that the composition of South Africa's motor vehicle fleet becomes more energy-efficient and environmentally friendly. However, the implication is greater for motor vehicle manufacturing industries and local automotive clusters or economic hubs (existing in countries such as Mexico and Thailand). The industry is expected, not only to reconfigure fuel consumption in motor vehicle design, but is also mandated to show CO_2 emission standards as part of vehicle certification.

The preceding example intends to illustrate how a global factor such as environmental degradation (caused by global warming due to the production of a greenhouse gas from motor vehicle CO_2 emissions) affects, not only driving behaviour, but also all motor vehicle manufacturers in all countries. Organisations attuned to similar challenges, which prepare for them and respond appropriately, will likely thrive; those that ignore them, will do so at their own peril.

The practising strategy box below, provides an example of another change in regulation that has a huge impact on all South African business organisations, namely Black Economic Empowerment.

Practising strategy: Black Economic Empowerment

The South African government launched the Black Economic Empowerment (BEE) programme as a racially selective programme to address the inequalities of apartheid. The programme gives Black, Coloured and Indian South African citizens economic privileges that were previously not available to them. In 2003, a strategy for BEE was released which defined the programme as:

- 'an integrated and coherent socio-economic process that directly contributes to the economic transformation of South Africa and brings about significant increases in the numbers of black people that manage, own and control the country's economy, as well as significant decreases in income inequalities.
- Thus, the BEE process will include elements of human resource development, employment equity, enterprise development, preferential procurement, as well as investment, ownership and the control of enterprises and economic assets.'[34]

The initial programme was criticised for benefiting only a few of the previously disadvantaged groups, which led to the development of the modified programme in 2007, called the Broad-based Black Economic Empowerment or B-BBEE. In this year, the new Codes of Good Practice of the B-BBEE and sector scorecards were gazetted by the government. In 2008, Chinese people were also added to the programme. In 2013, the Codes of Good Practice was again updated and gazetted by government. The new codes provided organisations with elements that it needed to prioritise, namely, ownership, skills development and enterprise development. In the context of strategic management, these elements should then become strategic priorities for South African organisations to be BEE-certified. A points allocation system, that accompanies the Codes of Good Practice, includes sub-minimum target thresholds of 40 per cent for these priority elements. Failing to achieve these thresholds results in penalties whereby an organisation's compliance level could be dropped.

The B-BBEE programme has a significant impact on the strategic priorities of all South African business organisations. Business organisations are encouraged to procure the products and/or services they need from other businesses that are B-BBEE-compliant. Organisations that are not BEE-certified will therefore find it difficult to retain their positions in the marketplace.

The next section focuses on the analysis of the remote environment in an African context.

5.3.2 The remote environment in an African context[35]

The 'sleeping giant' called Africa awakens – with great, but unrealised emerging power. While the continent presents significant business opportunities, the need to become a region with strong technological and innovative competitiveness is yet to be realised. Strategists, however, should be mindful of the following strategic issues plaguing Africa as a whole, and sub-Saharan Africa, in particular:[36]

- **Lack of infrastructure.** The lack of roads, harbours, electricity, ICT networks and railroads may, for example, seriously affect an organisation's supply chain and distribution system or even its ability to implement a cross-border strategy.
- **Lack of industrial development.** Most countries in Africa apply primary resource development in mining and agriculture but fail to develop, for example, industries for beneficiation or further processing, resulting in dependence on imports for local consumption and lower country productivity.
- **Political instability.** From a business perspective, this may take the form of erratic and unpredictable government decisions or national and regional conflicts that may lead to uncertainty and volatility in markets, and making strategic decisions riskier.

- **High levels of poverty.** In most developing Southern African countries (South Africa, Botswana, Namibia, Zambia and Lesotho), as well as the Comoros and the Central African Republic, there is a wide income inequality gap between rich and the poor.[37] In addition, poverty eradication remains one of the greatest challenges in the region. A Southern African Development Community (SADC) Regional Vulnerability Assessment and Analysis Synthesis Report in 2016 indicated that 40 per cent of all SADC citizens were living in abject poverty.[38] The high levels of poverty and living conditions of the poor make high-quality nutrition, education and healthcare inaccessible and unaffordable.
- **Corruption.** While levels of corruption may be a global phenomenon, not solely confined to Africa, it significantly differs between countries according to the Corruption Perceptions Index 2017.[39] The index, which ranks 180 countries and territories by their perceived levels of public sector corruption according to experts and business people, uses a scale of 0 to 100, where 0 is highly corrupt and 100 is very clean. New Zealand and Denmark rank highest with scores of 89 and 88, respectively. South Sudan and Somalia rank lowest with scores of 12 and 9, respectively. South Africa is ranked 71 with a score of 43. The best performing region is Western Europe, with an average score of 66, and the worst-performing region is Sub-Saharan Africa, with an average score of 32. With the potential to generate anger and destabilise societies, the cumulative effect of corruption on organisations and economies could be massive.
- **An inefficient public sector.** Sluggish and even negative economic growth that contributes to failure in alleviating poverty in sub-Saharan Africa is at least partly attributed to an inefficient and unproductive public sector.[40] Public sector reform involves effectiveness, efficiency, accountability, performance management and, ultimately, service delivery to society. Studies on public sector inefficiencies have shown that public sector management tends to prioritise the interests of the government (who is also the provider of public resources), even when the government's interests are contrary to the needs of the people.[41] South African studies have shown that progress has remained slow and limited because of political interference, unaccountable civil servants, non-compliance to reforms and the overall decline in governance.[42]
- **Lack of key human resource skills.** Limited access to education at various levels often results in an over-supply of unskilled and semi-skilled labour and a lack of people with the requisite skills to drive economic growth and development.[43] Key findings of the World Economic Forum Report on the Future of Jobs and Skills in Africa 2017 indicates that 9 per cent of employers surveyed in South Africa identified inadequately skilled workforces as a major constraint to their business and expects the pattern to worsen in the future. The report further states that in South Africa alone, 39 per cent of core skills required across occupations will be wholly different by 2020.[44]

On the positive side, there are many African countries (such as Côte d'Ivoire, Ethiopia, Kenya, Mali, Rwanda, Senegal, and Tanzania) with stable economies and political dispensations. These countries promote economic growth, and realised annual gross domestic product growth rates above 5.4 per cent from 2015 to 2017.[45] Within the African context, organisations are encouraged and often required to work together with governments to achieve strategic objectives and attain competitiveness at national, regional and Pan-African levels.[46]

5.3.3 The remote environment in a regional context[47]

Of particular interest to South African strategists and decision-makers is an understanding of the remote environment in a regional context. This comprises the sub-Saharan region and specifically, the Southern African Development Community (SADC) group of countries. The SADC comprises 15 member states, namely Angola, Botswana, the Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, the Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.[48] The main objectives of the SADC are 'to achieve development, peace, security, and economic growth, to alleviate poverty, enhance the standard and quality of life of the peoples of Southern Africa, and support the socially disadvantaged through regional integration, built on democratic principles and equitable and sustainable development'.[49]

While it is certain that Africa and the sub-Saharan region are developing strategies for its own future, organisations need to consider not only the challenges, but also the opportunities for organisations outside its region, to conduct business in Africa. Strategists should accommodate the continental strategic approach and factor a country's disposition in terms of its local conditions and customer preferences. Strategic decision-making should also acknowledge the role that government, as an economic enabler, plays in strategy development. Africa presents an opportunity for addressing the needs of the majority poor at the 'Bottom of the Pyramid' (BOP) market.[50] Broadly stated, the BOP is a socio-economic concept that allows us to categorise the poorest socio-economic group in a country or society. This segment of people represents an invisible and unserved market confronted by challenging barriers that prevent them from realising potential benefits for them, their families and society.[51]

Members of the BOP are those households who live with an annual disposable income of less than US$2 500. This group is excluded from the modernity of our globalised societies and has no access to organised financial services. The three largest BOP markets (Nigeria, Kenya, and South Africa) are home to over 16 million households.[52] Given the high percentage of the population living on less than US$2 a day, organisations with an entrepreneurial mindset and a willingness to invest over the long term and contribute to Africa, are more inclined to be successful than those who invest in these countries with a short-term financial goal.

The practising strategy box below provides an example of the exploitation of an opportunity identified in the remote environment that could develop into a viable business idea and profitable organisation.

Practising strategy: The *Lightie*[53]

Approximately 600 million people in Africa and 2 billion worldwide do not have access to electricity and are forced to use candles or paraffin lamps to provide light. The cumulative burden of these sources of energy in developing countries is enormous:

1. This costs 2 billion people in developing countries 25 per cent of their income for just one hour of light per night – amounting to a total of R380 billion per year.
2. Two million people in developing countries die annually from the use of these energy sources.
3. This 'dirty fuel' releases a total of 190 million tons of carbon dioxide (CO_2) pollution into the atmosphere annually.

In response to this problem, 27-year-old Michael Suttner invented the *Lightie*, a solar-powered lamp that screws into the top of a standard two-litre soda bottle. It provides 12 times lighter than a paraffin lamp, and uses a long-life lithium battery that will last for four to five years.

At less than US$10 per unit, the *Lightie* is a product that will provide an ideal energy solution for the BOP market.

In the bigger context, what is evidently clear is that with increasing globalisation and regionalisation, the interconnectedness and interdependencies between countries are increasing and global competition is intensifying. Two phenomena have already created seismic shifts in global economic activity:[54]

1. The centre of gravity of economic activity is shifting with global business growth originating from the developing world. The emergence of the BRIC countries (Brazil, Russia, India, and China) has already significantly changed global competition. These countries are all deemed to be at a similar stage of newly advanced economic development. It is estimated that China and India will, by 2050, become the world's dominant suppliers of manufactured goods and services, respectively. In addition, it is estimated that Brazil and Russia will become dominant suppliers of raw material. Due to lower labour and production costs in these countries (now including a fifth nation, South Africa), many organisations have cited BRICS as a source of foreign expansion opportunity, in other words, becoming promising economies in which to invest.[55] The MINT nations of Mexico, Indonesia, Nigeria and Turkey, share many of the characteristics of the BRICS countries, namely, strong economic growth and the potential to provide high returns for investors in these countries over the coming decade.[56]
2. The economic winners are not the organisations that control natural resources and physical capital, but rather those organisations that have mastered ideas and technology – resources that are not bound by ownership or geography, or governed by traditional rules of scarcity and scale economics.

'Globality' and regionalisation are creating opportunities as well as threats for developed-world multi-nationals and new champions from developing countries alike.

5.3.4 Evaluating an organisation's strategic response to factors in the remote environment

The list of factors that constitute a remote environment is almost endless. While changes in the remote environment may affect a cross-section of industries, some variables are more important than others as drivers of change in different industries. Factors are context-specific and vary from industry to industry, even from organisation to organisation, and can be operating at a national, regional or even a global level. Therefore, when analysing the remote environment, strategists are required to go beyond a mere description of change in the environment to an assessment of the forces driving it in order to prioritise these forces and thereby enable the organisation to focus its resources on the most strategically important issues. How organisations respond to these influences can have important competitive implications, as well as implications for their long-term survival and sustainability.[57]

An organisation can buffer itself against threats and take advantage of opportunities by firstly identifying and evaluating these influences. A useful tool for summarising and evaluating the strategic significance of PESTLE/G factors in the remote environment is the External Factor Evaluation (EFE) Matrix. This tool is illustrated in the practising strategy box below by making use of a holiday resort for illustrative purposes.

Practising strategy: External Factor Evaluation (EFE) Matrix for a holiday resort[58]

Column A Key opportunities and threats	Column B Weight	Column C Rating	Column D Weighted score	Column E Priority
Opportunities				
1. New water park being developed within 4 km	0.2	1	0.2	5
2. Number of foreign tourists growing 8% annually	0.1	3	0.3	4
3. A major competitor in the province ceased operations	0.3	3	0.9	1

Column A Key opportunities and threats	Column B Weight	Column C Rating	Column D Weighted score	Column E Priority
Threats				
4. *New health and safety regulations*	0.1	4	0.4	3
5. *Technology infrastructure*	0.1	2	0.2	6
6. *Customer base changing (golf, deep-sea diving)*	0.2	3	0.6	2
Total	1.0		2.5	

Notes

1. Column A lists the most important opportunities and threats originating from the remote and market environments. The opportunities and threats are numerous and not all are equally important. Key opportunities and threats are those considered to be the most strategically relevant to the organisation.
2. The strategic significance of the key opportunities and threats to the organisation is based on priority as determined by the weighted score, indicated in Column B. The sum of the weights equals 1.0.
3. In the example of the holiday resort, the six identified opportunities and threats are prioritised, where the priorities are provided in Column E. Priority 1 (*major competitor in province ceased operations*) is the factor with the highest priority and priority 6 (*technology infrastructure*) is the factor with the lowest priority to the organisation. Therefore, the most strategically significant factors for the organisation would be *a major competitor in province ceasing operations*, a *changing customer base*, and *new health and safety regulations*. Accordingly, the least strategically significant factors would be the *number of foreign tourists growing 8% annually, the new water park developed within 4 km, and technology infrastructure*.
4. Column C provides a rating of each of the identified key opportunities and threats, indicating how effectively the organisation's current strategies are responding to the factors, where 1 = response is poor, 2 = response is average, 3 = response is above average, and 4 = the response is superior. Bear in mind that ratings are organisation-based whereas weights are market-based and that both threats and opportunities can attract a 1, 2, 3, or 4 rating.

Column D provides the weighted score, which is determined by multiplying the weight in Column B by the rating in Column C, in order to calculate a weighted score for each of the identified opportunities and threats. The sum of the weighted scores of all factors is calculated to determine the total weighted score for the organisation. Regardless of the number of key opportunities or threats, the highest possible total weighted score for an organisation is 4.0 and the lowest possible weighted score is 1.0. A total weighted score of 4 indicates that the company is responding in an outstanding way to the existing opportunities and threats. In the example of the holiday resort, the weighted score for the company is 2.5 indicating that the organisation's strategic response to the key environmental factors is average. The six key external factors in this example have been randomly selected for illustrative purposes and have not been subjected.

The EFE Matrix is useful in enabling strategists to visualise and prioritise the opportunities and threats that an organisation is facing, and in assessing organisation's strategic response to the identified factors in the environment and as a whole. It also reveals whether the organisation's current strategy is seizing external opportunities and minimising the potential effects of external threats. Such an analysis can inform strategists on how to devise alternate strategies.

While this section focused on the analysis of the remote environment, the next section focuses on the analysis of the market environment.

LO 4: Analyse the market environment to identify threats and opportunities facing an organisation.

5.4 Analysing the market environment

In seeking to devise a strategy, we have to progress from the remote environmental analysis to the analysis of the market environment and its constituent stakeholders with whom the organisation interacts regularly, as illustrated in Figure 5.2. A good point of departure in industry analysis is firstly to understand what an industry is and to differentiate between the terms 'sector', 'industry', and 'market'. We then move on from understanding the industry to developing an understanding of its attractiveness. Lastly, we conclude the chapter by investigating the drivers of change.

5.4.1 Defining an industry

A *sector* is a group of closely related industries. For example, the computer sector comprises the computer component industries (for example, the disk drive, semi-conductor, and modem industries), the computer hardware industries (for example the personal computer, hand-held computer and mainframe computer industries), and the computer software industries (for example, the word processing and spreadsheet industries). Industries within a specific sector may connect with one another in many different ways. For example, organisations in the computer software industry may provide important complements to the computer hardware industries.

An industry is not merely defined as a market or composed of organisations competing with one another. A distinction should be made between the *industry and organisations it belongs* to and a *market that it serves*.[59] A market is defined as a group of customers with similar needs. For example, an organisation could exist in the automobile industry, but may choose to compete in the commercial vehicle market. Another example is Uber (refer to the opening case study). As an organisation, Uber exists in the software development industry, but its target market is that of metered taxi operator. An industry is therefore defined as *a group of organisations offering products and services that are close substitutes for one another, ie products or services that satisfy the same basic customer needs*.[60] The basic customer needs that are served by a market define an industry's boundary. For instance, Coca-Cola long saw itself as part of the soda (carbonated soft drinks) industry, whereas it was actually part of the soft drinks industry (which includes non-carbonated soft drinks). In the mid-1990s, the rise of customer demand for bottled water and fruit drinks began to cut into the demand for sodas, which caught Coca-Cola by surprise. Coca-Cola moved quickly to respond to these threats by introducing its own brand of water and acquired orange juice maker Minute Maid. By defining its industry too narrowly, Coke almost missed the rapid rise of non-carbonated soft drinks within the soft drinks market.

5.4.2 Analysing industry attractiveness[61]

According to Michael Porter, *customers*, *suppliers* and *competitors* are the primary determinants of industry competition. Competitors are comprised of *existing competitors* (incumbent rivals), *potential competitors* (new entrants to the industry) and *substitute providers* (providers of alternate products and services from other industries). This results in five forces that are primarily responsible for industry attractiveness (in terms of both the nature of competition in an industry and its profitability). These forces are listed below:

1. Customers
2. Suppliers
3. Existing competitors
4. Potential competitors
5. Substitute providers.

Porter argues that the greater the collective strength of these five forces, the less profitable and less attractive the industry is likely to be. Porter's model of industry stakeholders and competitive forces is depicted in Figure 5.3.

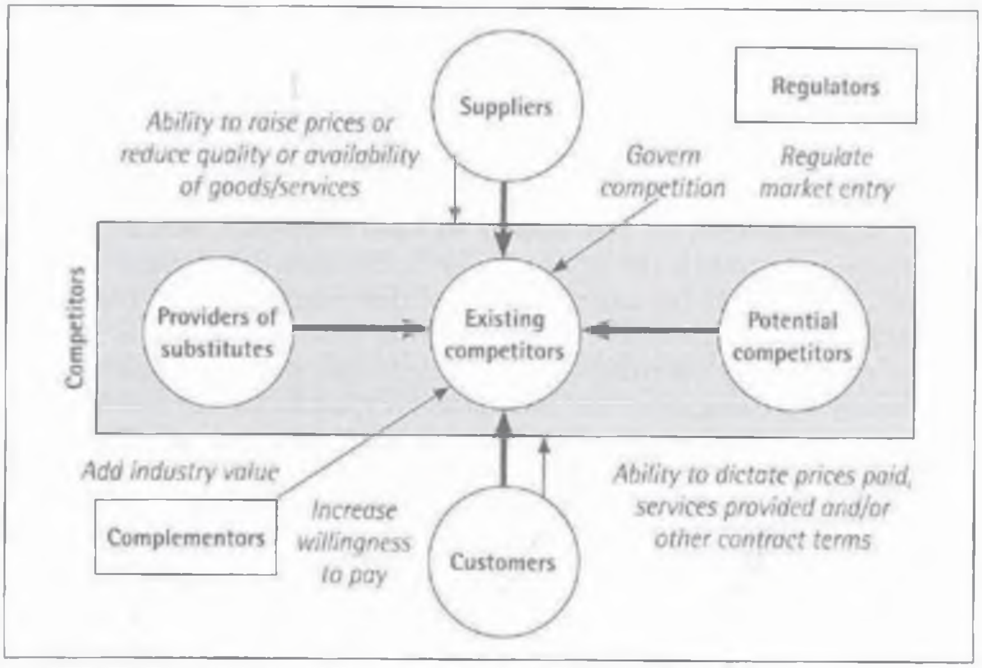

Figure 5.3 *A model of industry stakeholders and competitive forces*[52]

A brief explanation of Porter's competitive forces is provided below.

1. **Customers (power of buyers).** Customers have the ability to dictate prices paid, services rendered and/or other contract terms. Some customers exert greater economic power than others and have a greater ability to dictate prices and other contract terms as they negotiate with sellers. As a result, powerful customers and buyers may actually reduce the profitability levels of industries from which they buy. The power of buyers is high under the following conditions: (a) buyers are few in number and/or have the ability to buy in bulk; (b) the product or service being offered is similar to others offered, making it easier to switch to alternative suppliers; (c) the value of the buyers' purchases is a significant portion of the sellers' total income; and (d) the buyers can move backwards into the value chain by acquiring or developing the ability to produce the products or services themselves.
2. **Suppliers (power of suppliers).** Since suppliers provide all the required inputs to the organisation, including materials, capital and labour, they have the power to influence pricing and profitability, reduce quality and/or the availability of products and services, thereby creating uncertainty in the buying industry. Supplier power is high under the following conditions: (a) there are only a few major suppliers and they are highly concentrated in relation to the industry they serve; (b) supplies to the industry are not similar, making it difficult for incumbents to switch to alternative suppliers; (c) few or no alternative or substitute products or services exist; (d) the suppliers can move forward into the

value chain by acquiring the ability to use their products and/or services as inputs to the following product and/or service in the value chain; and (e) the value of the industry's purchases represents a small portion of the suppliers' total income (ie the suppliers' income is derived from serving other or multiple industries).

3. **Existing competitors (rivalry among organisations).** Competitive rivalry is characterised by strategic manoeuvring and retaliatory countermoves on the part of industry incumbents. This leads to increased competitive pressure, thereby affecting profitability. The degree of rivalry is dependent on the industry growth rate, as well as on the number of players, their relative size and competitive abilities. Competitive rivalry is high under the following conditions: (a) there are a large number of rivals who are relatively equal in size and power; (b) the industry is growing slower and incumbents are vying for the support of existing customers, rather than seeking new customers; (c) incumbents carry huge fixed costs; (d) rivals have excess capacity; and (e) existing players are unable to exit the industry, either due to the high costs associated with ceasing operations or high exit barriers.
4. **Potential competitors (threat of entry).** Existing industry players want to retain their market share and positions and are wary of new entrants because they can increase the level of competition, leading to reduced profits. Organisations therefore create entry barriers, which are forces intent on keeping potential competitors out while offering protection to existing industry incumbents. There are six barriers to entry, namely:
   i. *Capital required to enter the industry* – if capital requirements related to manufacturing facilities and equipment, working capital and other start-up costs are high, potential entrants will be deterred.
   ii. *Access to distribution of products and/or services* – where difficulty in building a network of distributors and/or securing retail shelf space is experienced, potential entrants will be deterred.
   iii. *Cost disadvantages not related to size* – where incumbents enjoy experience, relational, technological and learning-based cost advantages that are hard for newcomers to replicate and overcome, a barrier to entry will be created.
   vi. *Economies of scale* – when the cost advantages derived by incumbents due to their scale of operations in production, distribution and advertising, afford them cost advantages over potential entrants, a barrier to entry will be created.
   v. *Government legislation and regulation* – where restrictive regulatory policies limit or control new entrants by requiring licences and permits to operate in some markets such as telecommunications, cable TV and broadcasting, a barrier to entry will be created.
   vi. *High switching costs* – where customers have a strong brand preference and a high degree of loyalty to established brands, making it harder for a newcomer to break into the marketplace, a barrier to entry will be created.

5. Substitute providers (of substitute products or services). Organisations providing products that serve as replacements for alternatives or substitutes to the products of an organisation in a specific industry could be regarded as indirect competitors. For example, sucralose contained in artificial sweeteners is a substitute for sucrose in cane sugar. Substitute goods and services pose enormous threats to most industries and often place a cap on a particular industry's pricing, thus affecting profitability. However, a large part of what constitutes a substitute is a matter of personal judgement. Strategists should be vigilant and closely monitor neighbouring sectors, industries and markets for any changes in technology or cost structures. From a strategic perspective, substitutes that show improvements in price-performance relative to industry averages should be closely scrutinised, especially if produced by substitute providers who have huge financial resources.
6. A sixth force?[63] Since the business environment is not static and continuously changes, it is easy to see why the five forces model has come under criticism in recent times. One of the most frequent suggestions is that industry regulation is growing and should be added as a sixth force, since it regulates market entry and governs competition. There is ample evidence that *regulators* or government intervention can have a significant impact on industry structure (see the practising strategy box on companies guilty of anti-competitive behaviour below). Another contender for the sixth force is that of *complementors*. Products and services are becoming increasingly more complex and a wider range of organisations are involved in making and delivering them. Organisations develop relationships, not just with suppliers and competitors, but with other organisations whose products enhance their own. For example, applications on a smart cellular telephone could be seen as a complementary product because customers value their device more with applications than without it. Complementors add industry value and also increase customer's willingness to pay for products and services.

The basic steps to follow when using the competitive forces model to analyse industry attractiveness are as follows:[64]

- For each of the identified forces, identify the different parties involved, and the specific factors that bring about competitive pressures.
- Evaluate how strong the pressures stemming from each of the forces are (strong, moderate to normal, or weak).
- Determine whether the collective strength of the competitive forces (overall), is conducive to earning attractive profits in the industry.

However, for the purposes of strategic analysis, the central challenge is not applying the model and assessing the strength of the forces, but in extracting the strategic implications for the organisation concerned. Strategists should not only consider the influence of the forces but should seek out ways of manipulating these forces to the advantage of the organisation. An example is demonstrated by the symbiotic relationship between McDonald's and Coca-Cola, both giants in their respective markets. McDonald's has exclusively stocked and sold Coca-Cola beverages since 1955 and is Coca-Cola's biggest single client. The two companies helped each other grow throughout the globe[65]. This illustrates that organisations may alter the nature of competition in their market environment by creating partnerships with powerful stakeholders. Finally, the results of such analyses should not only guide organisations in making strategic decisions pertaining to industry (un)attractiveness and (un)profitability, but could also assist in identifying forces relevant to opportunities and threats.[66]

The practising strategy box below is a news extract that provides an example of competitive forces in the stolen-vehicle recovery industry in South Africa.

Practising strategy: Tracking companies guilty of anti-competitive behaviour[67]

In 2010, the Competition Tribunal found three vehicle-tracking companies and the industry body guilty of anti-competitive behaviour. The tribunal found that Netstar, Matrix Vehicle Tracking, and Tracker Network (representing over 90 per cent of the industry) and the Vehicle Security Association of SA (Vesa) had contravened the Competition Act by setting standards which created barriers to entry. This prevented competitors from entering or expanding in the market and denied consumers the benefit of lower prices, greater choice, and technological development. The tribunal found the standards had an exclusionary effect and were self-serving and irrational.

This case was brought by both the Competition Commission and the complainant and intervenor in the matter, an organisation called Tracetec. Tracetec wanted to enter the stolen-vehicle recovery (SVR) market because it believed that radio transmitter technology could be successfully applied in the SVR market. However, based on the standards, Tracetec was prevented from being admitted to the SVR category.

Vesa was an industry association for organisations engaged in the vehicle security industry that, at that particular time, had a sub-committee that set standards for admission to membership of its SVR category. The tribunal concluded, based on evidence, that it was not possible for an organisation to expand in the SVR market at the time without having its product approved by Vesa in the SVR category. This was because all the major short-term insurance companies, represented through their industry association, would not approve a customer installing a system that did not have Vesa approval. The tribunal also noted, in its reasons, that the South African Insurance Industry Association (SAIA), representing all the large insurers and a large part of the rest of the industry, who had organised Vesa to set standards for the industry, did so, not because of concerns for the consumer, but for its own business interests.

The relief sought by both the commission and Tracetec was limited to a declaration that the conduct constituted a prohibited practice, ie that the conduct was anti-competitive. This declaration would enable a rival organisation to institute civil action for damages against the respondents.

5.4.3 Industry drivers of change[68]

All industries are affected by new developments and ongoing trends that alter industry conditions, some more speedily than others. Many of these changes are important enough to require a strategic response. Since the five competitive forces (with the added sixth force) have such significance for an industry's profit potential, strategists must remain alert to the changes most likely to affect the strength of these forces. It is important to focus on the most powerful agents of change – those with the biggest influence in reshaping the industry landscape and altering competitive conditions.

Some of the most common industry drivers of change listed below:

- **Changes in the industry's long-term growth rate.** This refers to a situation in which a fluctuation in industry growth (negative or positive) over an extended period affects the supply and demand of an industry's products or services. This change in growth will subsequently influence the potential entry of new competitors (if growth is positive), as well as the exit of existing competitors (if growth is negative). The resultant change in the number of industry incumbents ultimately influences the degree of competition and the industry's overall attractiveness.
- **Changes in demand and customer preferences.** In the opening case study, it was mentioned that research indicates that people that never made use of metered taxis before, are using Uber. Changes in terms of customer demand and customer preference may also occur. For example, cellphone addiction and electronic device dependency is a growing trend among students and the youth. Studies have highlighted, not only psychological and social health-related issues as concerns, but also the major distractions caused by this dependency, often leading to motor vehicle accidents and other related medical emergencies.[69]
- **New business models.** The opening case study illustrates a new business model that developed in the taxi industry, enabled by technology. Organisations need to be aware of new business models in their industries that affect the way in which they do business and which can actually 'displace' their existing industry entirely. Other examples are cellular technology, digital cameras and video-on-demand television in their respective industries.
- **Product and marketing innovation.** This refers to the implementation of new marketing methods involving significant changes in product design or packaging, the placement of products, product promotion or product pricing. New marketing methods can be applied to new and existing products, which will attract new customers, offer differentiation and new value, thereby altering the nature of competition, especially in technology-based industries. Nokia is an example of an organisation that defined the mobile telecommunications industry at one time. Although it was the world leader in the mobile phone market for many years, the launching of the iPhone 3G, with its innovative touchscreen and enhanced multi-media

capability, by Apple in 2007, displaced Nokia as the industry leader. Apple's competitive advantage over Nokia was its ability to develop new, innovative products that share the same operating system, software and applications. This innovation allowed for the speedy introduction of a stream of new products, enabling the organisation to stay ahead of its competitors.

- **Entry or exit of major organisations.** This refers to a situation in which new industry players enter the market, or in which a reduction of industry players allows for new competition. An example can be found in the South African textile and clothing industry. Trade liberalisation during 1995 and 2002 left this industry vulnerable to penetration by Chinese and Indian competitors. South African organisations were unable to compete against the surge of low-cost substitutes, resulting in steady job losses over the following 15 years to the point where government intervention was required.
- **Changing social concerns of customers.** The social concerns of customers may change over time. In South Africa, #FeesMustFall is a student-led protest movement that began on October 2015 at the University of the Witwatersrand in response to an increase in fees at South African universities. The protest soon spread to other South African universities as well and was repeated year after year, with various consequences for government and all universities.

Many more potential drivers of change can be added to the list above. However, the key questions are: (i) *what factors are driving industry change;* and (ii) *what impact will they have on the organisation*? The true analytical task is to evaluate the forces of industry and competitive change carefully enough to separate the major factors from the minor factors. Merely identifying the drivers of industry change is not sufficient for strategic management and planning; a more important step in dynamic industry analysis is to determine whether the prevailing change drivers, overall, are acting to make the industry environment more or less attractive.

It is important to remember that in practice, industry changes do not follow or mimic the pattern of product or service life cycles exactly. A product or service life cycle refers to the stages that it goes through from when it was first thought of until it is finally removed from the market. (These stages are introduction, growth, maturity and decline). Some industries are able to re-invent themselves, one such example is the music recording industry illustrated in the strategy practice box that follows.

Practising strategy: How the music recording industry keeps re-inventing itself[70]

1877: First recording of the human voice. While experimenting with a new telegraph device, Thomas Edison noticed a speech-like noise as he accidentally ran indented tin foil under the telegraph stylus. He went on to invent the first working phonograph using a tinfoil cylinder that could both record and playback audio instantly.

1888: Invention of the gramophone. Emile Berliner invented the gramophone using a flat 7-inch disc as the recording medium that could hold up to 2 minutes of recorded sound.

1901: The '78 debuts. Named for its rotational speed of 78 rotations per minute (rpm), the '78 disc, along with the 'Victrola' (the best-selling record player of its time), signalled the end of cylinder playback technology. The '78 recording format survived well into the 1970s.

1948: 'Battle of the speeds'. Columbia Records introduced the first 12-inch, ($33\frac{1}{3}$ rpm) micro-groove long-playing vinyl called the LP, but RCA Records retaliated with its own format, a 7-inch disc called the 7-single that went on to become the standard for the popular jukebox.

1964: The cassette tape. Although the technology was already invented as early as 1930, the cassette tape could not penetrate the market because of the Great Depression and World War Two. The cassette tape, however, made a commercial breakthrough, when Philips introduced its own 30-minute format of the tape cartridge and allowed other manufacturers to duplicate the specifications. Piracy became an issue for the first time in the music recording industry.

1980: Death of vinyl. Philips and Sony co-operated to come up with a uniform standard for a compact disc (CD) in 1978. In 1988, the CD surpassed the LP in sales and the 80s became the most explosive boom period in recorded audio history as consumers replaced their vinyl collections.

1990: Birth of the MP3. Advances in computing technology during the 1980s introduced the combination of MP3 digital audio invention and the Internet. The MP3 compressed digital audio file size by a factor of 12, allowing digital transmission from computer to computer without compromising quality. Subsequently, in 1999, Napster introduced its online portal, marking the removal of geographical restriction on the publication and distribution of recorded music. Since there is no longer a tangible product separating production, publication and distribution, intellectual property ownership became the issue and still remains an issue in the industry.

2003: iTunes. Following tough negotiations with music record executives, Steve Jobs of Apple Computer subsequently launched iTunes that allows customers selective purchasing of the tracks they love. iTunes went on to become the most successful online music store to date. In its first year, Apple sold 70 million songs at US$0.99 per song, creating nearly US$70 million in legal Internet music sales, thus leading the way for online music and media e-commerce. New generation music recording includes music streaming platforms for cellular phones such as Apple Music and Google Play.

The time span involved in industry change varies significantly from industry to industry. Furthermore, some industries, such as the motor vehicle industry, stay in the maturity phase if their products become basic necessities of life. Other industries skip the mature stage and go straight into decline. The real pay-off for strategising comes when strategists draw some conclusions about what strategy adjustments will be needed to deal with the impacts of the changes in industry conditions. Therefore, a dynamic industry perspective is not to be taken lightly. It has practical value and is fundamental to the task of identifying potential opportunities and threats, and thinking strategically about where the industry is headed and how to prepare for the changes ahead. The last section in this chapter focuses on strategic responses to changes in the external environment of organisations.

LO 5: Discuss strategic responses to changes in the external environment.

5.5 Strategic responses to changes in the external environment

It is essential for strategists and organisations operating in an unpredictable world to be able to respond quickly to changing circumstances and to alter their strategies accordingly. The dramatic rise of Google with its new business model is a good example.[71] Google's business model is based on revenues earned from advertising links associated with search results, the so-called pay-per-click (PPC) business model. PPC is also known as paid search, which refers to an Internet search result that provides links to content. If these links are clicked on, a cost is paid to the advertiser. In response to search requests, search engines display PPC ads in the space allocated to advertising on the page displaying the search results. When introduced, the impact was disruptive to the business models of other companies that made money from online advertising. Companies like Yahoo.com and Microsoft's MSN network with strong online advertising had to rapidly change their strategies to adapt to the threat Google posed. Few people had seen this development coming and therefore could not plan for it. Nevertheless, companies had to respond to it, and rapidly.

In the section that follows, the limitations of the process approach to strategic management will be explained, followed by a discussion of the concepts of strategic agility and ambidexterity as mechanisms for responding to changes from the external environment.

5.5.1 Limitations of the process perspective of strategic management

In Chapter 3, the process perspective of strategic management was explained as a traditional view that comprises distinct stages or phases (ie strategic planning, implementation and control), which incorporates a linear view. This perspective rests on an implicit assumption that an organisation's strategies need only be reviewed during the strategic planning exercise.[72] However, according to critics of formal planning systems, a flexible approach to strategy making is not possible within such a framework. The argument is that we live in a world in which small change events can have a large and unpredictable impact on outcomes. In such circumstances, even the most carefully thought out strategic plans are prone to being rendered useless by rapid unforeseen change. Therefore, today's successful organisations cannot afford to stand still and rest on previous accomplishments. If they do, they can easily become vulnerable to a competitor's new product, shifts in customer preferences or other changes in the environment. Instead, they should focus on building sustainable competitive advantage for the future by seeking out new ways to remain flexible, innovative, efficient and responsive. Strategic agility and strategic ambidexterity became more important than ever. These two concepts are explained below.

5.5.2 Strategic agility

Strategic agility can be defined as the ability of organisations to stay competitive in their industry and markets, by adjusting and adapting to new ideas and using these ideas to create new products and services, as well as new business models.[73] Organisations, like organisms, must be 'adept at adapting' or they will not survive.[74] While the formal processes and structures of organisations are designed to control people, resources, decisions and actions, successful agile organisations do not follow these rigid models. They are effective at managing change, continuously adapting their organisational bureaucracies, systems, products and cultures to survive the shocks and to prosper from the forces that often decimate the competition. *Agility* (quickness, responsiveness, the ability to adapt to changing demands) is therefore more vital than ever to an organisation's survival. Every organisation exists in an environment and interacts with it to some degree. Strategists and organisations have a number of options they can follow in order to respond to the external environment. These include:[75]

- Adapting to the environment. This refers to organisational change in response to a significant environmental factor or variable through a process of corresponding adaptation. There is usually a time lag involved, but if the organisation fails to adapt to the change in the environment, it will gradually become irrelevant or even extinct. The South African Post Office is an example of an organisation that failed to keep pace with the development and proliferation of the Internet and smartphone usage. As such, it could not offer its digital customers a digital post or email solution and therefore failed to stay relevant to its customers. An example of an organisation that managed to adapt to the South African economic environment is First National Bank (FNB). It was estimated in 2017 that there were over 820,000 *stokvels* in the country with a combined membership of 11.4 million people, handling over R44 billion per annum.[76] FNB was the first to introduce a stokvel account aimed specifically at savings as a group.[77] Other banks such as Nedbank also entered the stokvel market after FNB.

- Influencing the environment. This refers to an organisation (as one of many competitive players in its respective market) that proactively changes the environment through the leveraging of technology or leveraging of its business model, creating new value for the market, thereby wrong-footing competitors and often making the opposition redundant. Organisations such as Uber (referred to in the opening case study to this chapter) and Napster (explained in the reinvention of the recording music industry practising strategy box) are examples of organisations that actively influence the dynamics and nature of competition in their market environments. While it is a very rare occurrence for organisations to influence even the remote environment, it is possible. Intel Corporation, for example, through research and development, invented the Intel 4004 micro-processor or computer chip in 1971. This revolutionary micro-processor (the size of a little fingernail and slimmer than human hair) delivered the same computing power as the first electronic computer built in 1946 (which filled an entire room).[78] Computer engineers could purchase this 'building block' and then customise it with software to perform different functions in a wide variety of electronic devices. This first general-purpose programmable processor is an example of a technological force stemming from the remote environment that ushered in the era of integrated electronics in all technology-based industries.
- Selecting a new environment. This refers to an organisation that decides to divest or exit a market because of industry unattractiveness due to high levels of competition and low-profit potential and/or that selects a different or new market that is more attractive with greater profit potential. Examples of South African companies for whom this response has worked are Woolworths and Mr Price. Woolworths was initially known for selling homeware and clothing, but has been very successful as a food and grocery outlet. Mr Price's initial offering was fashion apparel. However, the organisation has since successfully moved into sporting apparel and homewares such as textiles and furniture.

5.5.3 Strategic ambidexterity

Early in the development of the strategic management field, the external environment was considered the primary determinant of which strategies would likely be successful.[79] This idea of *environmental determinism* suggested that good management is associated with determining which strategy will best fit environmental forces at a particular point in time, and then executing it. From a *deterministic* perspective, the most successful organisation will be the one that best adapts to existing forces in the external environment (*adapters*). However, environmental determinism is no longer accepted as an absolute or the primary guide for crafting strategies. The notion of adaptation has been supplemented by the principle of enactment, which assumes that organisations do not have to submit to existing forces in the environment and can, to a certain extent, actively shape their environments through strategic actions (*shapers*). In reality, the most successful organisations will not opt for adaptation *or* enactment. They will engage in processes of adaptation and enactment simultaneously.

Strategic ambidexterity can be defined as the ability to exploit existing competencies while simultaneously exploring new opportunities in the organisational environment. Stated differently, it involves a balance between explorations and exploitation – and so achieves the 'best of both worlds'. Strategic ambidexterity will position the organisation, giving it the ability to influence those parts of the environment over which it can exercise some control, while adapting to environmental circumstances that are beyond control or too costly to influence.

Animals have used this mechanism for millions of years to forage for food effectively, and they must consider the same essential trade-off that companies do, and this is whether or not to *exploit* the current environment or to go beyond the current environment and *explore* the unknown.

Giraffes, for example, employ clear and distinct approaches for balancing this trade-off. When food is abundant, as it usually is in the wet season, they don't need a targeted strategy – there's plenty of low-hanging fruit. In the dry season, giraffes need, on the one hand, an explicit strategy for how frequently and how far away they should search for food sources, since staying too long at one grove will reduce yield and leave them too hungry to find the next food source. On the other hand, spending too much time wandering around looking for food will also make them vulnerable to starvation. Businesses, too, need to balance exploiting and renewing their advantage, especially when their current source of advantage is threatened by changes, such as technological, social, economic, cultural, political, environmental, competitive or natural changes. 'Low-hanging fruit' for businesses is scarcer than ever, and they need deliberate approaches to achieving ambidexterity.[80]

The big picture

When considering the context of strategy, a profound understanding of the business environment is a prerequisite for successfully managing and practising strategy. This is particularly important when viewing strategic decision-making at domestic, regional and African contexts. In order for organisations to survive, strategists need to know how to assess the market and remote environments in relation to key stakeholders and, more specifically, to identify and evaluate the extent to which key factors provide an opportunity or a threat for the organisation concerned.

However, the main objective of external environmental analysis is not only to determine opportunities and threats, but also to provide strategists with an understanding of the strategic context and a solid foundation for decision-making and planning. A major shortcoming is often the inability to move beyond mere *accurate identification* and *description* of forces driving change. What is required, is an appropriate interpretation and assessment of what important strategic and competitive implications these forces hold for organisations charting a future direction.

Summary of learning outcomes

LO 1: Explain the external environment in the context of strategic management.

Organisations are open systems that are influenced by the environment in which they operate. The environment consists of the micro- (or internal) environment, and the macro- (or external) environment, where the latter consists of the market and remote environments. Variables in the micro-environment are organisational functions, policies, strategies, goals and resources. Variables in the market environment are customers, competitors, the labour market and labour unions, intermediaries and suppliers. Sub-environments of the remote environment are the political, economic, socio-cultural, technological, legal, environment (natural) and global environments. Two levels of analysis of the macro-environment, that will influence the organisation's strategic direction and strategic actions, can be identified, as (i) an analysis of the remote environment; and (ii) an analysis of the market environment.

LO 2: Explain the importance of strategic context in strategic planning and decision-making.

For strategic planning and decision-making to be effective, it is important to identify opportunities and threats in the external environment, as well as strengths and weaknesses in the internal environment. Strategists should take advantage of inherent or internal strengths and the identified opportunities arising from the external environment; overcome inherent weaknesses, or neutralise identified threats found in the external environment; to ensure the strategic 'fit' or consistency between the opportunities and threats in the internal environment.

LO 3: Analyse the remote environment to identify opportunities and threats facing an organisation.

The analysis of the remote environment firstly involves the identification of remote environmental forces. The most important elements of this environment are the political, economic, socio-cultural, technological, legal, environmental and global factors (PESTL/G). For South African business organisations, it is important to also analyse the remote environment in an African and regional context. Lastly, strategists also need to evaluate an organisation's strategic response to factors in the remote environment. The external Factor Evaluation Matrix is one of the tools that can be used for this purpose.

LO 4: Analyse the market environment to identify threats and opportunities facing an organisation.

The terms 'sector', 'market' and 'industry' are differentiated. A sector is a group of closely related industries. A market is a group of customers with similar needs, while an industry is a group of organisations offering products and services that are close substitutes for one another. Various forces are responsible for the attractiveness of an industry (in terms of competition in an industry and the profitability of the industry), namely, customers, suppliers, existing competitors, potential competitors, substitute providers, industry regulation and complementors.

LO 5: Discuss strategic responses to changes in the external environment.

Organisations should be able to respond quickly to a constantly and rapidly changing environment and alter their strategies accordingly. Strategic agility and strategic ambidexterity are two important abilities in this regard, where strategic agility is defined as the ability of organisations to stay competitive in their industry and markets, by adjusting and adapting to new ideas and using these ideas to create new products and services, as well as new business models. Strategic ambidexterity can be defined as the ability to exploit existing competencies while simultaneously exploring new opportunities in the organisational environment.

Discussion questions

1. Explain how an understanding of the external environment of an organisation can provide strategists with a foundation for crafting strategies.
2. Explain the composition of the management environment and discuss how this framework aids in your understanding of the context of strategy.
3. Differentiate between the terms 'sector', 'industry' and 'market'.
4. Explain the various forces that shape the attractiveness of an industry, both in terms of competition and profitability.
5. Differentiate between the terms 'strategic agility' and 'strategic ambidexterity'.

Learning activities

1. Visit the web page https://www.howwemadeitinafrica.com/business-africa-12-profit-making-ideas/60141/. Select any one idea that interests you, and conduct an environmental analysis to determine if the idea could work.
2. Visit the SABMiller website and download the annual report for 2017 at http://www.sabmiller.com/investors/reports. Read the chairman's report in the annual report and identify three opportunities and three threats from the perspective of SABMiller.

3. Visit the SABMiller website https://sabcms.blob.core.windows.net/wp-content/2017/05/The-South-African-Breweries-BEE-Certificate-2017-2018-Final.pdf. Comment on the implications of this certificate for the strategic planning and implementation of the company.

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6 Strategic resources and capabilities

Cecile Nieuwenhuizen

LEARNING OUTCOMES

After studying this chapter, you should be able to:

LO 1: Explain the importance of resources, capabilities and core competencies in strategic management.

LO 2: Explain the appraisal of the value of resources and capabilities.

LO 3: Explain the resource-based view of an organisation's internal analysis .

LO 4: Explain the identification of capabilities and core competencies to create value according to the functional area and value chain analyses.

LO 5: Discuss the contribution of resources, capabilities and core competencies towards competitive advantage and sustainable competitive advantage of an organisation.

LO 6: Explain the importance of capturing the value generated by resources, capabilities and core competencies.

KEY WORDS

- Appropriability
- Capabilities
- Competitive advantage
- Core competencies (also known as distinctive capabilities)
- Dynamic capabilities
- Exploitable
- Inimitable
- Knowledge; explicit knowledge; tacit knowledge
- Explicit knowledge
- Tacit knowledge
- Non-substitutable
- Rare
- Resources
- Resource-based view (or resource-based theory)
- Sustainable competitive advantage
- Value chain

CHAPTER ORIENTATION

Strategy is the link between the organisation and its environment. This means that there should be consistency between the external environment of the organisation (including the market and remote environments) with its opportunities and threats, and its internal environment (including its mission, goals, values, resources, capabilities, structure and systems) with its strengths and weaknesses.[1]

Matching resources and capabilities within the organisation, with opportunities in the external environment is essential for successful strategy. Resources and capabilities have been identified as the primary source of competitive advantage and also as a basis for the formulation of a strategy for an organisation. Resources and capabilities enable organisations to differentiate themselves from competitors and develop strategies from which they can benefit.

In this chapter, the focus is on the role of the organisation's resources and capabilities in the development and implementation of strategy to achieve the goals of the organisation. First, we differentiate between resources, capabilities and core competencies and focus on their importance in strategic management. Second, we focus on appraising the value of resources and capabilities addressed, and then on the resource-based view relating to internal environmental analysis. Subsequently, we identify the capabilities and core competencies for creating value in line with the functional area and value chain analyses. Then, the contribution of resources, capabilities and core competencies towards the competitive advantage and sustainable competitive advantage of organisations are addressed. Lastly, the importance of capturing the value generated by resources, capabilities and core competencies is addressed.

Figure 6.1 demonstrates the focus of this chapter within the broader context of strategic management. This figure also demonstrates the uniqueness of strategic resources and capabilities, in the sense that they underpin both strategy formation and organisational architecture. They form part of the internal context of organisations, because organisations need to understand their strategic resources and capabilities and their strengths and weaknesses in this regard.

Current development and/or the development of new resources and capabilities can also be the content of strategic decisions. For example, in the Discovery Bank case study, Discovery used its strategic resources (such as the Vitality customer base) and capabilities for innovation and managing financial services organisations as a basis for entering the retail banking industry. They are also a vital part of organisational architecture, and have to be aligned, not only to the strategy, but also to other components of the organisational architecture, such as leadership. They also need to be aligned with the needs of key stakeholders.

In the opening case study, Adrian Gore explains how Discovery's ability to create unique new value propositions for customers will be brought to bear on the banking sector.

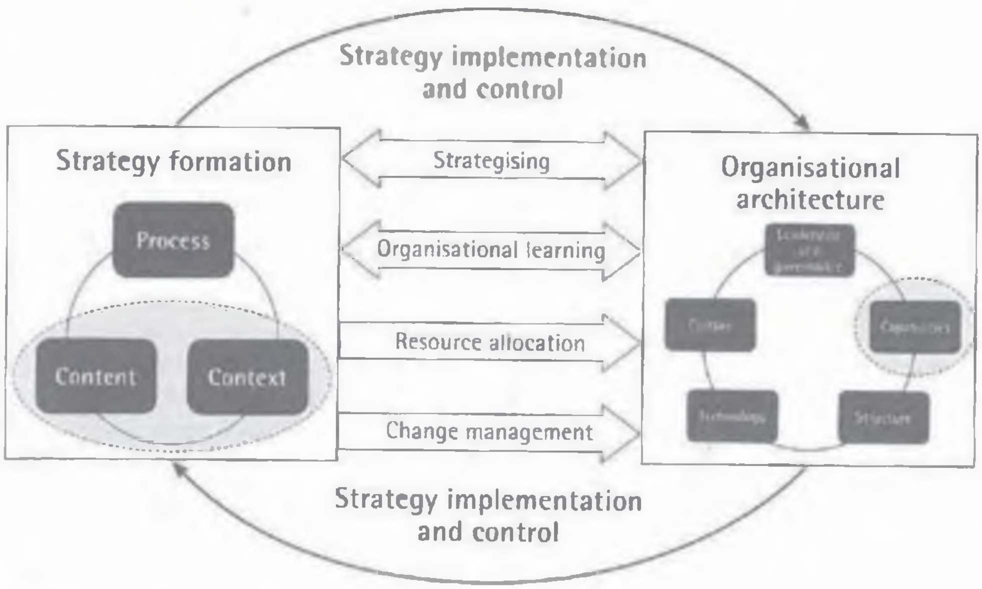

Figure 6.1 *Strategic resources and capabilities*

Case study

Discovery Bank[2]

Discovery, one of South Africa's leading insurance companies, is entering the retail banking market with Discovery Bank in 2018. Discovery built its success on its leading medical insurance business, Discovery Health, and its highly successful Discovery Vitality loyalty programme.

Discovery has been working on its bank for two years, and according to CEO Adrian Gore, it has made good progress. They now have a strong team of people on the project and the company is already interacting in the payment space. Discovery Bank is being built from the ground up, and around R1.5 billion has already been invested in the project to ensure that the best platform to serve customers is built, without taking any shortcuts. 'The value proposition itself will be good for customers. I mean, that is what we do,' said Gore.

Discovery Bank will essentially target the same market as its health and insurance businesses, namely, the 'mass affluent market' in South Africa. As they had shown with the Vitality programme, using incentives to change behaviour where people are often irrational works well, and Discovery feels that they can add value with their model of sharing value and creating behavioural change. What Discovery brings to the banking industry is the ability to innovate and a lot of experience in disrupting other industries – they were, after all, the company that revolutionised health insurance in South Africa – and millions of loyal Vitality customers. What they do not have is extensive experience of operating a bank successfully, and only time will tell if they are able to master this requirement to compete successfully in the very competitive South African banking industry.

LO 1: Explain the importance of resources, capabilities and core competencies in strategic management.

6.1 The importance of resources, capabilities and core competencies in strategic management

6.1.1 Resources

Resources are the productive assets owned by organisations[3] used to transform inputs to marketable outputs (you may also refer to Chapter 1, Section 1.2.1, where resources were first introduced). Resources can be grouped into five primary categories:

1. **Financial resources.** Financial resources refer to any economic resource that an organisation has, measured in terms of the money utilised in the organisation to buy what is needed to offer products and/or services to the market. An organisation can generate financial resources internally from own funds or externally from third parties (or non-owners) such as banks, financial institutions and creditors.
2. **Physical resources.** Physical resources refer to an input in the production process, for example, operational and manufacturing equipment, raw materials and components.
3. **Human resources.** Human resources refer to the skills, knowledge and experience possessed by an individual or group of individuals, which is viewed in terms of their value to the organisation. Human resources also include aspects such as employee insight, intellect, relationships, training and judgement.
4. **Organisational resources.** Organisational resources are often referred to as the prime intangible asset of an organisation. It relates to resources such as patents, brands and human capital, that are used to transform inputs to marketable outputs and be productive. Organisational resources also include the reporting structure and management, including planning, co-ordinating, controlling and networks in organisations.
5. **Technological resources.** The technological resources of an organisation can be the sum of two components, namely, the tangible component (which includes the active part of the organisation's tangible fixed assets such as computers and information technology systems) and the intangible component (which includes intangible assets related to intellectual properties, accumulated skills and experience, software licences and patents).

Resources can be used as a basis for the formulation and implementation of strategies, but not all are strategically relevant. Some have little or even a negative impact on the performance of an organisation. Resources that can contribute positively to an organisation's strategy and lead to sustained competitive advantage need to be identified.

Although resources of organisations in the same industry are typically similar, organisations themselves are never identical. They will therefore possess some resources that are differentiating, valuable, rare and inimitable (cannot be imitated) and will accordingly pursue different strategies and achieve different levels of success. This heterogeneity in resources can be acquired and sustained over a longer period within an industry as it may not be perfectly mobile across organisations.[4]

To determine the resources of an organisation, a comprehensive inventory (according to the various categories thereof as explained previously) should be developed. The inventory should differentiate between tangible and intangible resources and capabilities, and human resources (or tacit knowledge). The practising strategy box below illustrates an example of the value of resources and capabilities of Discovery.

Practising strategy: Discovery Medical Aid Insurance

Discovery Medical Aid Insurance started as a corporate entrepreneurial venture within First National Bank (FNB). This means that it was started as a business within a business. Through FNB, resources, including financial, physical, human, organisational and technological resources, were available to commercialise a new business opportunity identified by the bank. Examples of available resources to establish Discovery Medical Aid Insurance were:

- *Financial resources*: start-up capital was provided, salaries were paid to existing and new employees and funds were made available to market the new venture;
- *Physical resources*: office space, equipment and infrastructure for those involved in setting up the new venture were made available;
- *Human resources*: existing employees in FNB who had the knowledge, experience, training and relationships relevant to the new business and who had the necessary experience to appoint the required new employees, were made available; organisational resources such as a related knowledge and experience in the financial services market and a tested management structure that was also relevant to the new business;
- *Technological resources*: existing technology, such as computers and an established information technology system that could be used and adapted according to the needs of Discovery Medical Aid, were made available.

The resources at the disposal of an organisation can also be categorised as tangible and intangible resources.

Tangible resources

Tangible resources are physical, observable and quantifiable assets of the organisation and include physical things such as equipment, money, structures, the sophistication and location of a plant, formal reporting structures, technology used and patents. Tangible resources can fall into any of the five categories of resources identified above: financial (ie loan capital raised), physical (ie equipment and machinery), human (ie employees), organisational (ie brands) and technological (ie computers) resources. However, some of these resources can also be intangible, for example, intellectual capital as a human resource and networks as an organisational resource.

Intangible resources

Intangible resources are a subset of an organisation's strategic resources and can be categorised into three types, namely, human resources, innovation resources and reputational resources.[5]

Kristandl and Bontis define intangible resources as follows:[6]

> *Intangibles are strategic firm resources that enable an organisation to create sustainable value, but are not available to a large number of firms (rarity). They lead to potential future benefits which cannot be taken by others (appropriability), and are not imitable by competitors, or substitutable using other resources. They are not tradeable or transferable on factor markets (immobility) due to corporate control. Because of their intangible nature, they are non-physical, non-financial, are not included in financial statements, and have a finite life. In order to become an intangible asset included in financial statements, these resources need to be clearly linked to a company's products and services, identifiable from other resources, and become traceable results of past transactions.*

Intangible resources are not so easy to identify, but are usually much more valuable and superior to tangible resources. Intangible resources include the reputation of an organisation and that of its product, employee know-how, perception of quality, ability to manage change, ability to innovate, team-working ability and participative management style.

Competitors find it difficult to understand, acquire, substitute and imitate intangible resources. Therefore, organisations often rely on intangible resources for their core competencies and capabilities. Consequently, more intangible and unobservable resources will lead to more sustainable competitive advantage.[7]

The three types of intangible resources, (human resources, innovation and reputation) are discussed in more detail below.

1. **Human resources.** Human resources refer to people that own, manage or work in an organisation, that have knowledge, trust and managerial capabilities. Having these capabilities can be valuable and even primary contributors to competitive advantage as these can contribute to the uniqueness of an organisation.
2. **Innovation resources.** Innovation resources include ideas, scientific capabilities and the capacity to innovate. Innovation resources refer to the capacity of an organisation to innovate through the acceptance and implementation of new ideas, processes, products or services. It involves the ability of an organisation to understand the needs of customers and develop innovative solutions that will ensure customer satisfaction. The practising strategic box, focusing on Discovery Medical Aid Insurance, highlighted the fact that Discovery started as a corporate entrepreneurial venture within FNB. Corporate entrepreneurs (also referred to as 'intrapreneurs)' have the vision and ability to develop new ideas and opportunities (in this case, new approach to medical aid insurance) within an existing business (in this case, FNB).
3. **Reputational resources.** Reputational resources include the brand name, reputation with customers, perceptions of product quality and reliability. Corporate reputation can be defined as the collective assessments of an organisation's past actions and the ability of the organisation to deliver improving business results to multiple stakeholders over time. Financial results, management efficiency and effectiveness, the quality of products and services and market competitiveness are examples of factors that can be used as criteria for ranking. A good corporate reputation is vital for an organisation. Organisational reputation and image, as well as brand reputation and image, are reputational resources. These resources ensure the credibility, trust and confidence of current and future employees, shareholders, customers, service providers and the public in general, within an organisation.

6.1.2 Capabilities

Capabilities are the capacity of an organisation to deploy resources for a unique end result. Capabilities are organisation-specific clusters of activities developed through complex interactions between tangible and intangible resources over time and reflect what an organisation excels at compared to other organisations. They can also be information-based.[8]

Key characteristics of capabilities are that they are valuable across various products and markets, embedded in routines and are tacit. Capabilities are what the organisation can do exceptionally well.[9] While resources are static and will generally deplete over time, capabilities increase with use and become more valuable. Figure 6.2 illustrates an example of how resources combine to become marketing and branding capabilities within an organisation.

Figure 6.2 *The link between resources and capabilities*

Capabilities can be within business functions, can be linked to technologies or product design, can involve the ability of the organisation to manage linkages between elements of the value chain or can refer to the capacity of the organisation to deploy resources through processes.[10]

Capabilities are 'high-level routine[s] that, together with its implementing input flows, confers upon an organization's management a set of decision options for producing significant outputs of a particular type'.[11] A capability is reflected in high-level activities (routines) that produce important outputs of significant value that contribute to the organisation's competitive advantage.

The practising strategy box below provides an example of an organisation that develops and continuously improves its capability to develop strong brands.

Practising strategy: Discovery brands

Discovery is an example of an organisation that develops and continuously improves its capability to develop strong brands. This is possible through the combination of financial resources (Discovery Medical Aid was initially funded by First National Bank as a corporate entrepreneurial venture), human resources (experts in the financial services and insurance sector and experts in marketing) and organisational resources (knowledge of brand development and management expertise) as the bases for the development of excellent business development, marketing and branding capabilities. The first venture was with Discovery Medical Aid, that started in the 1990s and is now the best-known brand, as well as the largest and most successful medical aid fund in South Africa. This was followed by the Discovery Vitality reward programme that was developed for Discovery Medical Aid clients. Discovery Vitality rewards Discovery Medical Aid members by encouraging them to exercise regularly, eat well and do relevant and regular health checks. Subsequently, Discovery Insure was added to the Discovery portfolio and includes Discovery Life Insurance and Discovery Car and Home Insurance. Discovery Car Insurance is combined with Discovery Vitality

Drive that is a unique driver behaviour programme that rewards members for driving well. Another service developed by Discovery is Discovery Credit Card, a unique credit card that gives cardholders access to Discovery Miles rewards. Members earn up to 10 times the number of kilometres when they shop with Discovery's wide range of in-store and online partners.[12]

The business development, branding and marketing capabilities improve and strengthen with each new service and brand added. It is difficult for competitors to imitate (inimitable) Discovery as their capabilities improve continuously and form the basis of its competitive advantage in the financial services and related industries.

Carefully developed capabilities form the basis of competitive advantage and are therefore the primary differentiators of organisations from their competitors. Building difficult-to-imitate capabilities, as seen from the Discovery examples, is of great importance to an organisation as this ensures differentiation.

6.1.3 Core competencies

According to Grant and Jordan[13] and other authors,[14] capabilities or competencies are the same thing. However, core competencies (also referred to as distinctive capabilities) are those capabilities or competencies that distinguish an organisation from others in an industry and form the basis of its competitive advantage, strategy and performance. In Figure 6.3, the link between resources (tangible and intangible), capabilities, core competencies, strategy, competitive advantage, value creation and organisational performance, is illustrated.

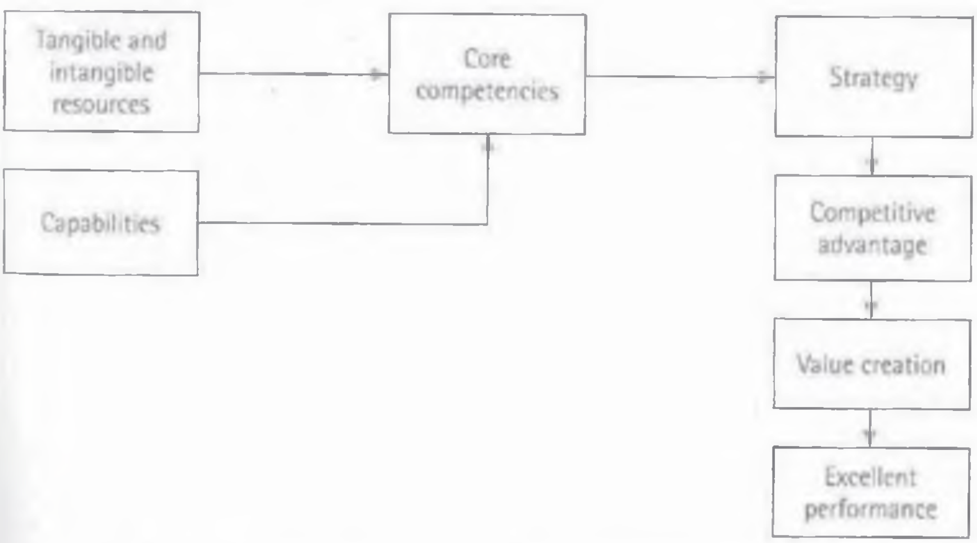

Figure 6.3 *The link between resources, capabilities, core competencies, strategy and competitive advantage and organisational performance*[15]

Core competencies make a disproportionate contribution to customer value and the efficiency of its delivery, and serve as a basis for market entry.[16] Core competencies that are internal strengths of an organisation enable it to capitalise on opportunities that are identified in the environment.

Core competencies involve the combination of various resources and capabilities. The development of core competencies usually takes place over a period of time and is a process of accumulation and learning how to use a unique combination of resources and capabilities. It also often involves communication and an intensive commitment to working across organisational boundaries. It can entail the co-ordination of diverse production skills and the integration of multiple streams of technology.

Their complex co-ordination, integration and harmonisation across production skills, technologies and capabilities make core competencies difficult to imitate. They enable access to a variety of markets and significantly contribute to perceived customer benefits from products and services.[17] Most successful organisations will have only one or two core competencies, while many average organisations will have no distinguishing core competencies at all. From the Discovery example (see the practising strategy box), we can see that their capabilities and core competencies are their strategic priorities, meaning that the organisation requires a lot of resources to develop and expand those important strategic resources.

Practising strategy: Discovery's core competencies

Discovery's capabilities to develop new businesses, branding and marketing have become so specialised and distinctive that it distinguishes Discovery from others in the insurance and financial services industries. Therefore, new business development, branding and marketing are the basis of its competitive advantage and strategy.

Creating a balanced and attractive spread of businesses

The range of Discovery businesses is differentiated yet related, ranging from medical aid, insurance, reward programmes and banking services. All are based on their core competencies of new business development in insurance and financial services and rewards programmes, branding and marketing. Their next project, Discovery Bank is proof that they are continuously looking for new business opportunities.

Developing strong, relevant brand portfolios that win in the local market

Discovery developed a variety of brand portfolios that meet different insurance and finance needs of the same target market, the mass affluence market These services are complemented by rewards programmes with equally strong brands, ie Vitality linked to Discovery Medical Aid and Vitality Drive linked to Discover Car Insurance.

Through the varied services, Discovery attracts clients that then often also migrate to other services. For instance, a Discovery Medical Aid and Vitality member will also acquire the Discovery Credit Card due to the integrated benefits (ie additional rewards and Discovery miles) between the services.

Constantly raising the profitability of their businesses

Discovery's aim is to keep on developing new businesses and to improve their operational performance through top-line growth and continuous improvement in services and products.

Our focus now turns to the appraisal of the value of organisational resources and capabilities.

LO 2: Explain the appraisal of the value of resources and capabilities.

6.2 Appraising the value of resources and capabilities

Capabilities and resources have the potential to become core competencies and these core competencies can result in competitive advantage, but only if they meet certain conditions. A resource-based framework for the analysis of an organisation will determine the resources and capabilities that will result in core competencies.

For resources and capabilities to become the core competencies, they should be valuable (V), rare (R), inimitable and non-substitutable (I), and exploitable by the organisation (O), creating (VRIO). Each of these measures can be used to test the strategic value of resources and capabilities and are discussed in more detail below.

6.2.1 Value (V)

Valuable (V) resources imply that the organisation has the ability to transform a resource into a product or service at a lower cost or with a higher value to the consumer. Capabilities are valuable when they enable an organisation to implement a strategy that improves efficiency and effectiveness (refer to Chapter 1, Section 1.2.3, where these concepts were explained). To be valuable, the capability must increase efficiency by using fewer resources to generate maximum outputs, or by using the same resources to generate more outputs. For example, an information system could reduce the number of customer service agents required or increase the number of calls that the same number of agents can answer. To be valuable, the capability must increase the effectiveness of the organisation, meaning that the organisation should increasingly be 'doing the right things' – formulating and pursuing appropriate organisational goals. Value is dependent on the type of strategy implemented, for example a low-cost strategy of a specialist South African airline, such as Kulula.com, that offers flights at a lower cost than conventional airlines. Thus, Kulula.com attracts more customers, which is valuable as this contributes to higher profitability for the company. Another example is value created by a differentiating strategy. For example, the African Pride hotels, the luxury hotels in the Protea Group of hotels, generate additional income for the group from customers who require specialist services and who are prepared to pay for such services. African Pride hotels transform a resource into a service (hotel accommodation) with a higher value to its customers. An organisation decides on a strategy for a specific business unit that will add value to the organisation. In business, this value can be a measure such as profitability

6.2.2 Rarity (R)

A valuable resource and/or capability that an organisation owns that other organisations do not have, and that is not generally available in the open market, is considered rare (R). The situation that arises when a few organisations have the same resource and/or capability, creates competitive parity. This is because organisations can use identical resources to implement the same strategies and no organisation.

6.2.3 Inimitability and non-substitutability (I)

Inimitable capabilities (I) and core competencies are valuable, unique and complex resources, and include intangible resources (such as organisational reputation, networks employed, client trust and the intellectual property that an organisation might have) and capabilities (such as knowledge, the culture of the organisation, skills and experience)[18] that make it difficult for competitors to copy what an organisation is doing, resulting in sustained competitive advantage. If it is easy to copy something valuable that an organisation started doing first, its competitors will soon follow, and in the process, erode any competitive advantage.

Imitation by competitors is prevented if:

- they do not understand the reason for the organisation's success.
- they do not have the same unique historical conditions.
- the cause of effectiveness is uncertain due to social complexity (for example, trust between the organisation and its stakeholders, teamwork and informal relationships such as networks).

Non-substitutability is also part of the inimitability of resources and capabilities and means that there are no equivalent resources, duplicates, substitutes or imitations that can be exploited to implement the same strategies. The strategic value of a capability or core competency of an organisation increases when it is difficult for competitors to substitute it and also when it is difficult for them to identify, discern or observe it. Specific knowledge of the organisation and trust relationships are not easily observable and therefore difficult to copy.[19]

6.2.4 Exploitable by the organisation (O)

The organisation's structure and systems (O) should be suitable for a specific competitive advantage. If an organisation cannot exploit a resource or capability, it will have little value. Managerial awareness, of both the potential competitive advantage and the action required to realise it, is essential.[20] The practising strategy box below provides an example of the importance of an organisation's structure and systems that should be suitable for a specific competitive advantage.

Practising strategy: The Joule electric car runs out of current[21]

In 2008, the Joule, an electric car developed in South Africa, was launched with great fanfare in Paris. The car, a first for South Africa, was designed by South African-born automotive designer Keith Helfet, chief stylist at Jaguar, and it certainly seemed set to shake up the motoring world.

However, the dream was not to be. In 2012, Optimal Energy, the company behind the Joule, announced that it was shutting down, with the loss of 60 jobs and the R300 million, largely funded by the government through the Industrial Development Corporation (IDC) that was invested to develop the vehicle.

The reason for winding down Optimal Energy was that it could not attract the R7 billion required to industrialise the Joule, and the IDC and other investors decided against providing further funding for the project. Efforts to find manufacturing partners or facilities had also been fruitless, with Optimal Energy exploring the options of taking over the then-defunct Hummer production line at the General Motors plant in Port Elizabeth or joining forces with other manufacturers. Another option was to develop an electric bus using the intellectual property developed by Optimal Energy for the Joule.

While one could argue that the Joule was a good design and idea, the company simply could not meet the requirement of organisation, meaning that it could not attract the required funding and manufacturing expertise to commercialise its idea. However, the intellectual property is still a valuable resource that could be used to generate revenues for its owners.

In the next section, our focus shifts to the analysis of the internal strengths and weaknesses of the organisation in terms of its resources. We focus on one specific model that can be used for this purpose, namely, the resource-based view.

LO 3: Explain the resource-based view of an organisation's internal analysis.

6.3 The resource-based view of internal analysis

Strategy formulation originally included a market-focused mission statement addressing what the organisation was about, its business, the market and needs it served, and its customers. In a volatile and ever-changing environment, this external focus became risky and in the 1990s, attention shifted towards the internal strengths, resources and capabilities of organisations.

The resource-based view (RBV) is a model for analysing the internal strengths and weaknesses of the organisation with respect to its resources and linking them to opportunities in the external environment. It determines where the organisation can build competitive advantage, superior performance and customer value.

A model of the RBV is presented in Figure 6.4. It indicates an assessment of the organisation that starts with a general internal evaluation to determine its strengths, specifically as related to the industry in which it operates. Important considerations for this assessment are the following:

- Management's strategic role and the strategic direction. This should reflect what is conveyed in the vision, mission, purpose and values to determine whether the organisation is clear about what it wants to achieve and how it wants to achieve it.
- Core competencies. Core competencies, as identified, developed and protected by management that contribute to the competitive advantage of the organisation, should be considered.
- Resources. The value, barriers to duplication, inimitability and rarity of the tangible and intangible resources of the organisation should be considered.
- Capabilities. The value, barriers to duplication, inimitability and rarity of the capabilities of the organisation as determined by the culture of the organisation, the knowledge, skills and tacitness of employees and the ownership structure of the organisation should be considered.
- Appropriability. This refers to the ability of the organisation to retain the value it creates for its own benefit. The organisation also needs to determine who benefits from this added value. It needs to ensure the retention of key employees, the inimitability of intangible assets and an ownership structure that reinforces inimitability contribute to the core competencies of the organisation.
- Managers. This relates to determining whether the experience, strengths and management style are aligned with the strategy of the organisation.
- Business owners and investors. This entails determining whether they are aware of and in possession of the resources, capabilities and core competencies required for success in their organisation.

- **Operational issues.** Aspects such as sales, assets and location should be considered in order to determine whether the management thereof are appropriate for the specific organisation.
- **Employees.** The type and level of employees should be considered to determine whether the employees have the relevant skills, knowledge and experience required for the organisation.
- **Organisational culture.** The culture of the organisation should be considered to determine whether the shared values and beliefs of the people in the organisation are conducive to the improved performance of all stakeholders.

A positive assessment of the organisation (management's strategic role and core competencies) will lead to sustainable competitive advantage that ensures value to the client and, subsequently, superior performance in terms of profitability of the organisation, sustainability and the attainment of organisational goals.

Figure 6.4 depicts a model of the resource-based view of an organisation's internal analysis.

As mentioned previously, the RBV is a model that is used for analysing the internal strengths and weaknesses of the organisation in terms of its resources and linking them to opportunities in the external environment. It determines where the organisation can build competitive advantage, superior performance and customer value. Although the RBV is a widely accepted and invaluable framework for strategy formulation, some limitations have been identified. These limitations are listed below:

- It has not yet been tested and proven empirically.[23] Daellenbach and Rouse suggest that an important requirement is that the RBV be measured and analysed at the resource level, implying the need for longitudinal studies. A longitudinal study is a research design that involves repeated observations of the same variables over different points in time. Reviewing and testing of longitudinal data will make it possible to measure the performance of an organisation over a period of time, with a start and end date.[24]
- It does not address how to increase profitability and/or how to develop further competitive advantages or create new ones.[25]
- The lack of future orientation and the inability to differentiate between valuable and less valuable resources and capabilities result in a lack of predictability.[26]

The next section focuses on the identification of capabilities and core competencies in an organisation.

Management's strategic role
- Core competency identification
- Core competency development and protection

Core competencies

	Tangible resources	Intangible resources	Capabilities
Value	Value recognised in the balance sheet	Value results from reputation and client trust	Value is embodied in the culture of the organisation and the knowledge and skills of employees
Barriers associated with duplication	Easy for rivals to identify and duplicate	Unique and complex resources create inimitability	Tacitness and casual ambiguity create inimitability
Appropriability	Fully appropriate for the organisation	Value remains within the organisation due to resource inimitability and success in retaining key personnel	Ownership structure reinforces inimitability enabling the organisation to appreciate value

Sustainable competitive advantage
Value to client – consistently high performance

Superior performance
Constantly outperform competitors - rate of return relative to competitors

Figure 6.4 *An adapted model of the resource-based view*[22]

LO 4: Explain the identification of capabilities and core competencies to create value according to the functional area and value chain analyses.

6.4 The identification of capabilities and core competencies to create value

Through the exploitation of capabilities and core competencies, organisations create products and services with value which customers are willing to acquire. Those that are superior to what is being offered by competitors contribute to competitive advantage. Value is determined by lower production cost and/or differentiation between products and services of competitors.

The identification and assessment of capabilities and core competencies are challenging but essential as it forms the basis of an effective organisational strategy.[27] A value-chain analysis or a resource-based approach can be used. Both models involve determining the strengths and weaknesses of an organisation and how the strengths contribute to its competitive advantage. The performance of an organisation can also be evaluated and compared to the performance of competitors.

Identifying and assessing capabilities and core competencies will enable the organisation to determine the following:

- how the components of its value chain add worth to its performance.
- how resources and capabilities contribute to competitive advantage.
- how good its financial performance is compared to competitors.
- how customers and employees benefit from the organisation's capabilities and core competencies.

As discussed in the previous section, the resource-based view of strategy focuses on the internal environment with analysis of the internal strengths and weaknesses of the organisation in terms of its resources and capabilities and links it with opportunities in the external environment. Internal resources and capabilities determine strategic decision-making as these are key factors that determine the performance of an organisation. The five stages of strategy formulation according to Grant and Jordan[28] based on the resource-based view of strategy are as follows:

1. The identification and classification of the organisations' resources.
2. The identification of the capabilities of the organisation.
3. Appraisal of the rent-generating potential (the value) of resources and capabilities.
4. The selection of a strategy that optimally exploits the resources and capabilities of the organisation relative to the opportunities in the external environment.
5. The identification of resource gaps, that is the difference in the resources available and the resources needed for the organisation's strategy.

An organisation's resources, capabilities and core competencies can be identified, classified and analysed either (1) according to its functional areas, or (2) by means of an analysis of its value chain. These two approaches are explained below.

6.4.1 Classification of capabilities and core competencies according to the functional areas of an organisation

A functional analysis identifies capabilities that can become core competencies of an organisation in line with its functional areas. Below, examples in terms of the finance, operations, human resources, procurement, research and development, marketing and public relations functions are provided:

- **Financial function.** This chapter's opening case study on Discovery Bank provided an example of a profitable organisation which had access to internally generated funds, as well as external funds, due to their reputation for excellent performance. Their access to funds enables them to implement research initiatives, be innovative and continuously expand the organisation.
- **Operations function.** Toyota Motor East Japan, Inc. has been at the core of the Toyota group, serving as a key base for development and production. It excels in its operations function due to its culture and tacit knowledge that cannot be imitated by Toyota plants in other countries.
- **Human resources function.** For six consecutive years, the Massachusetts Institute of Technology (MIT), has been rated the world's top university. At the heart of this incredible ranking is their extremely strong reputation among both fellow academics and employers, as well as the fact that MIT is responsible for an impressive number of academic citations per faculty.
- **Procurement function.** Mr Price Home identifies trends and products that they imitate, order and buy directly from producers and wholesalers. Due to this procurement capability of bringing desirable, yet affordable products in high volumes to the low- and medium-income mass market, Mr Price Home has a competitive advantage in the home and décor market.
- **Research and development function.** Apple Inc. is an example of a company in which research and development in its high-technology products is a core competency. Apple's strategy is to always be ahead of its competitors in new products, applications, functions and the look of their Mac computer range, iPods, iPhones, iPads, Apple watch and complementary products and services.
- **Marketing function.** In the opening case of this chapter, the marketing function of Discovery is identified as a core competency. The database of existing customers using one service, ie the medical aid, are exposed to Discovery's other and new services, such as their new banking services.
- **Public relations function.** Building relations with strategic markets is, in effect, the management of relationships with the public relevant to the organisation. Upmarket restaurants are organisations that have developed public relations as a core competency. For example, the very successful chef and restauranteur Chantel Dartnall whose Mosaic restaurant has twice been named as one of the top ten restaurants in the country, present culinary programmes on prominent television stations, participates in chef competitions in South Africa and internationally, and was named the best female chef in the world in 2017. Besides distributing a quarterly newsletter to customers, regular articles and snippets about Dartnall and the restaurant appear in magazines. She also personally presents her menu of the day to all patrons of the restaurant, and even meets and greets customers informally in public places. Effective public relations is a core competency of this organisation.

6.4.2 Classification of capabilities and core competencies through value chain analysis

The main function of an organisation is to add value successfully in the process of producing products and/or delivering services. In other words, this means that the main activities of an organisation are effectively combined to create customer value. Michael Porter developed the value chain, which can be defined as a set of activities that an organisation performs to create value for its customers. These activities are divided into five primary and four support categories.[29] Figure 6.5 depicts the value chain.

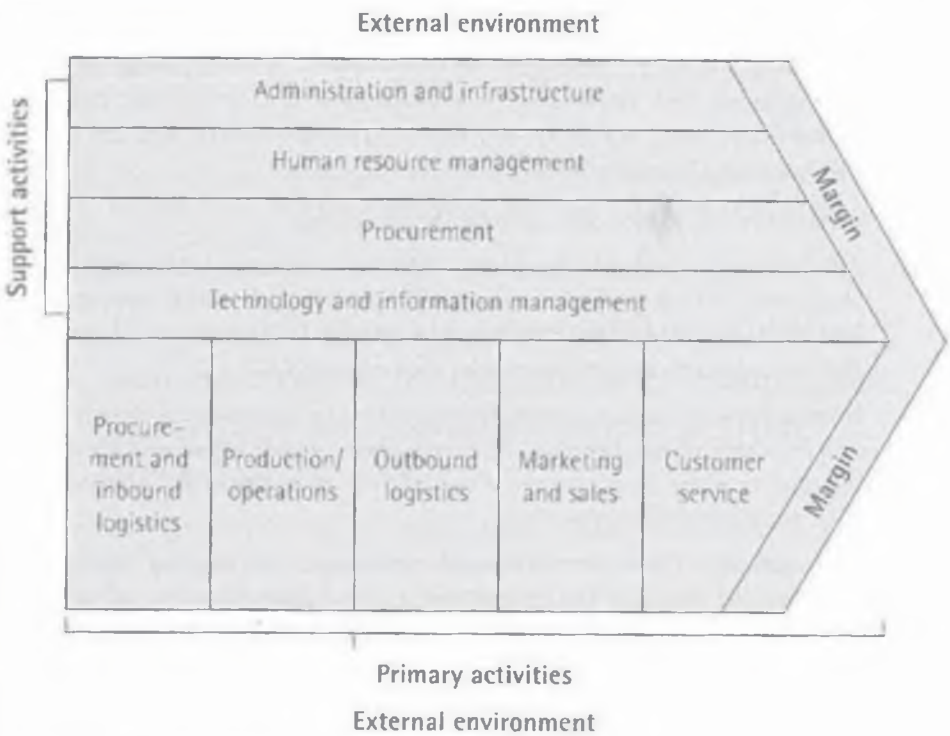

Figure 6.5 *The value chain*[30]

As previously stated, capabilities or competencies are the same things. However, core competencies (also referred to as distinctive capabilities) are those capabilities or competencies that distinguish an organisation from others in an industry and form the basis of its competitive advantage, strategy and performance. Thus, capabilities can become an organisation's core competencies.

A distinction is made between primary and support activities. Primary activities and related capabilities in the value chain include the following:

- **Procurement and inbound logistics.** These activities relate to receiving, storing and distributing inputs for the manufacturing of products by the organisation. *Capabilities:* purchasing, material and inventory control systems.

- **Production/operations.** Production/operations activities refer to those activities that transform inputs into final products, ie facility operations, machines and assembly. *Capabilities:* design and product development, quality control, component manufacture and assembly.
- **Outbound logistics.** Outbound logistics refers to activities related to collecting, storing and distributing products and services to customers. *Capabilities:* distribution co-ordination, processes related to warehousing of products and dealer relationships.
- **Marketing and sales.** These refer to marketing, sales and purchasing of an organisation's products and services. *Capabilities:* innovative promotion and advertising, and a motivated sales force.
- **Customer services.** Customer services refers to everything involved in improving and maintaining the value of a product for the customer. *Capabilities:* parts, warranty and servicing arrangements, and the quality and training of employees.

Support activities in the value chain include the following:[31]

- **Administration and infrastructure.** These activities support the entire value chain and include general management, planning, financial management, information systems, legal issues and quality management. *Capabilities:* risk management and integration of the value chain.
- **Human resource management.** This involves the appointment, development and retention of employees at all levels, their compensation and all matters relating to their employment. *Capabilities:* training, skills development, staff recruitment and retention.
- **Procurement.** Procurement is also referred to as the purchasing function and involves the selection and development of suppliers, sourcing of supplies, evaluating price, cost control, paperwork and accounting and inventory control. *Capabilities:* inventory and database management.
- **Technology development.** This involves all technology related to the operations and management of the organisation. *Capabilities:* integrated management information systems and technology-managed design and manufacturing.

The internal environment of the organisation, including the primary and support activities, determines an organisation's strengths and weaknesses. This has to be aligned with the opportunities and threats in the external environments (as indicated in Figure 6.5). Therefore, knowledge and understanding of the external environment are essential to determine opportunities and threats. The external environments that impact on organisations are the market environment and the macro-environment. The market environment comprises consumer behaviour, needs, purchasing power, suppliers, intermediaries and competitors. The macro-environment includes the political, technological, physical and international environments, as well as broad economic and social issues.

The margin (which is also indicated in Figure 6.5) is the economic value that the organisation retains for corporate and operational purposes and includes profits and funding other projects, such as research and development projects, corporate social responsibility projects, mergers and acquisitions.

The objective of successful organisations is to build difficult-to-imitate core competencies that distinguish an organisation from its competitors. Capabilities and core competencies are valuable when they enable an organisation to implement strategies that improve efficiency and effectiveness. The type of strategy also determines the value, ie low cost or differentiation strategies.

The following section focuses on the contribution of organisational resources towards the competitive advantage and sustainable competitive advantage of organisations.

LO 5: Discuss the contribution of resources, capabilities and core competencies towards the competitive advantage and sustainable competitive advantage of an organisation.

6.5 The contribution of resources, capabilities and core competencies towards competitive advantage and sustainable competitive advantage

When two or more organisations compete within the same industry, one organisation possesses a competitive advantage over its rivals when it performs (or has the potential to perform) better than its rivals (refer to Chapter 1, Section 1.8, where the term 'competitive advantage' was introduced). Organisations can achieve competitive advantage, in two ways:

1. **Differentiation.** It can produce products and services that are superior in value to those of competitors, and that allows it to charge premium prices or to retain customers for a longer period of time. The differentiation approach can be focused, meaning, that the organisation can concentrate on offering its products or services to a specific segment of a market or niche market. Alternatively, if it is a product or service with a wider appeal, it can target broad segments of a market or industry.
2. **Cost leadership.** It can produce products or services at a significantly lower cost than its competitors (cost leadership), enabling it to leverage higher profit margins. The cost leadership strategy can also be aimed at a focused or broader market.

The practising strategy box that follows provides examples of companies achieving competitive advantage through various strategies (differentiation and cost-leadership).

Practising strategy

Apple: Competitive advantage through a broad differentiating strategy

As introduced in Section 6.4.1, Apple Inc. is the producer of the Macintosh computer and laptop range, iPods, iPhones, and iPads, Apple watch and complementary products and services. The products are also developed to integrate and synchronise with one another. Many people who make up Apple's loyal customer base owns various Apple products, such as a Mac Air laptop, an iPhone, an Apple watch, an iPad and all the complementary products such as smartphone and iPad covers, docking stations, various applications such as iTunes and more. The design of Apple products is sleek and sophisticated and the Apple brand is a core competence of the organisation. Apple Inc. is an example of a company that is a differentiator, as it spends a lot on research and development and charges a premium price for its products. Despite this, Apple products have a broad international appeal in the high-income market.

Singita: Competitive advantage through a focused differentiating strategy

Singita is an example of a focused differentiating strategy, offering a range of exclusive game lodges in private African game reserves. Tourists stay at Singita to experience the expansive space and beauty of their reserves. Limited guests paying a premium ensures that guests experience exceptional care. These lodges are accessible only to highly affluent, mostly international tourists, as the cost per person per night is around R24,000 (in 2018). This includes luxury accommodation, all meals and refreshments, exclusive safari experiences and other five-star services.

Mr Price Sport: Competitive advantage through cost leadership

The establishment of Mr Price Sport has followed Mr Price's success in bringing fashion clothing at affordable prices to the mass market in South Africa. Mr Price Sport has identified the extensive market for sports clothes and equipment at affordable prices. By offering a wide range of good quality sports clothes and equipment at unbeatable prices, Mr Price Sport has gained a large market share of all income groups, including the vast market for children. In many cases, the same producers and suppliers of fashion clothing are also able to supply the new venture with sports clothing. Due to its large market share, Mr Price is in the position to negotiate excellent prices, often directly with producers of clothes and equipment, as well as with international wholesalers. The benefit of the low prices paid for stock can then be transferred to customers to whom pricing is of utmost importance. Mr Price is an example of an organisation with a competitive advantage based on a broad cost leadership strategy.

Road Lodge Hotels as a focused cost leadership strategy

As part of the City Lodge Hotel Group, the Road Lodge Hotels offers accommodation at very affordable rates to a focused market, namely, the public that want to or have to travel, but within a limited budget. Accommodation at these hotels is focused on providing low-cost accommodation to those niche markets who want to travel for leisure or are entry-level employees who have to travel for work, but have limited funds available.

For differentiators, competitive advantage is achieved by combining resources, capabilities and core competencies to produce products and services of superior quality. For cost leaders, production efficiency is important. Either a differentiating or cost leadership strategy can be achieved through different capabilities, as follows:

- **The ability to produce high-quality products.** Products are perceived as superior to those of competitors when they have a high brand value or are more reliable and durable.
- **The ability to innovate.** Innovation involves experimentation and creative processes aimed at developing new products, services or processes for commercialisation and introduction to the market or potential users. In order to innovate, organisations will typically have to spend more than their competitors on research and development. This can involve technological improvements to products, services or processes; the design of new products; new marketing strategies, or improved administrative and organisational systems and techniques. By ensuring uniqueness through innovation and the ownership of patents, trademarks or brands that cannot be imitated by competitors, organisations can achieve competitive advantage.
- **Responsiveness to customers.** This is the ability of an organisation to identify and satisfy the needs and wants of customers. To contribute to competitive advantage, customer responsiveness should be superior to that of competitors. By providing unique and innovative services, organisations may be in a position to charge premium prices or to retain customers.
- **Efficiency.** Efficiency is achieved by using the fewest inputs (raw materials, production methods, labour, knowledge, expertise, technology) to generate a maximum amount of outputs (products and services produced). The level of efficiency is determined by the quantity of inputs needed to produce output, therefore:

  Efficiency = output/input

  An efficient organisation will require less input to produce a desired output. Efficiency is often determined by the productivity of the employees of an organisation. The ability to produce products or services at a cost significantly lower than competitors rests on the ability of the organisation to leverage production efficiencies. Production efficiencies can be achieved through various means, for example:

- **Economies of scale.** Economies of scale is an economics term that describes a competitive advantage that large organisations have over smaller ones. It means that the larger the organisation, the lower its costs and such an organisation will be able to produce larger quantities of a product at lower prices.
- **Economies of learning.** A learning economy can be defined as an economy in which knowledge is the crucial resource and learning is the most important process. Just like economies of scale, economies of learning will enable an organisation to develop a competitive advantage by gaining more experience, which will lead to a decrease in production costs.
- **Designing products for more economical production or using new technologies to reduce costs.** Organisations can gain competitive advantage by designing products which require fewer inputs, and which will lead to higher levels of efficiency.
- **Reducing unnecessary costs.**
- **Leveraging location advantages.** Organisations can gain a competitive advantage by locating productive assets in areas where the costs are lower.

Practising strategy

Differentiating or cost leadership strategy can be achieved through different capabilities:

- **The ability to produce high-quality products.** Harley-Davidson motorcycles deliver high-quality products. There are various Harley-Davidson models, but all have the distinctive Harley-Davidson look, sound and branding and are regarded as status symbols in some motorcycle circles. To many, the appeal lies specifically in the American heritage of these motorcycles, and customers are willing to pay a premium for these symbols to reflect their status as motorcycle connoisseurs. There are also many complementary Harley-Davidson accessories such as jackets, helmets and other items that further enhance the experience of belonging to a group of people who own products with high brand value.
- **The ability to innovate.** As explained previously (Section 6.4.1), Apple Inc. has built a large loyal customer base by producing innovative products and stylish product designs, with the result that from 2013 to 2017, Apple was recognised as the most valued brand in the world, with a brand value worth of $184,15 billion in 2018.[32]

- **Responsiveness to customers.** Discovery Medical Aid's Vitality programme rewards members for healthy living. Discovery's unique approach is in identifying rewards that are valuable to their customers, ie discounted gym membership, movies, national and international flights and hotel accommodation; cash back when buying healthy foods; rewards such as smoothies for reaching activity goals and many more. By constantly researching and identifying what would add value to customer experience Discovery responds to their needs, often before customers realise their own needs. This capability of Discovery is very difficult, if not impossible to imitate, thus inimitable. Therefore, Discovery is a good example of an organisation that is responsive to its customers.
- **Efficiency.** Mr Price is an example of a very efficient organisation. Through its network of suppliers and high-volume purchasing, Mr Price offers fashion, sport and home goods at excellent prices at its three extensive specialist store ranges, Mr Price Clothing, Mr Price Sport and Mr Price Home. Due to economies of scale, goods at Mr Price stores can often be purchased at lower prices than through wholesalers that seldom have the purchasing capacity of Mr Price. Mr Price reduces cost by identifying fashion trends in clothing, interior décor and home goods and having it reproduced in large numbers at very good prices.

An organisation that has the ability to perform (or the potential to perform) better than its rivals over the long term, has a sustainable competitive advantage (refer to Chapter 1, Section 1.8, where we differentiated between competitive advantage, sustainable competitive advantage and transient competitive advantage). Sustainable competitive advantage is determined by the durability of the relevant resources, capabilities and core competencies and how inimitable they are. *Durability* refers to the length of time over which a capability is relevant and can contribute to the competitive advantage of the organisation. For example, a strongly ingrained culture is extremely durable and long-lasting, while a technical competence is of much shorter duration. *Imitability* refers to how easy or difficult it is for competitors to copy the competitive advantage and is determined by transferability and how replicable a capability is. *Transferability* is how easy or difficult it is to acquire or buy a resource. For example, raw materials, components, machines and human resources are all easily transferable, while immobile and intangible resources, such as organisational culture, are not easy to transfer. The latter is more valuable because it may be specific to the organisation or lose worth when transferred. *Replicability* refers to the ability to use the resource in other settings. For example, Curro Private schools were established in 1998 as a leading independent school provider in southern Africa. It was able to replicate its ability to start up and manage more than 100 private schools since its establishment in South Africa.

In the last section of this chapter, our focus turns to capturing the value generated by resources, capabilities and core competencies.

LO 6: Explain the importance of capturing the value generated by resources, capabilities and core competencies.

6.6 Capturing the value generated by resources, capabilities and core competencies

Even when resources are inherently valuable and comply with the value, rarity, inimitability and organisation (VRIO) principles explained in Section 6.2, it does not necessarily mean that the organisation will have the capacity to take advantage of them, nor benefit from them. If the organisation cannot capture sufficient value to justify its investment in developing unique resources and capabilities, it will not be able to achieve competitive advantage. This is known as *appropriability*.

As explained in Section 6.1.2, dynamic capabilities are strategic in nature and are those capabilities that help organisations to learn new capabilities that enable them to adapt to environmental changes. Dynamic capabilities involve the ability to integrate, build and reconfigure internal and external processes and competencies to address a rapidly changing environment. It is the ability to adapt capabilities that is the ultimate basis of sustainable competitive advantage.

Resources and capabilities are valuable when they enable organisations to deliver products and services to customers at a price they are willing to pay. The value of resources and capabilities is indirectly determined by the following:

- the external environment, including demand and the potential of the market.
- changes in the external environment, for example, changes in technology, the structure of an industry and preferences of customers.
- differences between the resources utilised by different organisations.
- value as determined by either lower production cost than rivals or increased revenues, or a combination of the two.

Although competitive advantage is important to an organisation, on its own it does not necessarily lead to superior organisational performance. For resources and capabilities to be the basis of competitive advantage, as well as ensuring superior profitability, the following are important:

- The resources and capabilities should be inherently valuable, as determined by the VRIO framework.
- The resources and capabilities should enable the organisation to address market segments that are large enough (L) to allow the organisation to generate sufficient financial returns.
- The resources and capabilities should enable the organisation to identify and address an unmet (U) needs of customers. Unmet needs are defined as those needs of customers that are high in importance and insufficiently satisfied.[33]

These additions extend the VRIO framework of resources and capabilities to VRIOLU. The extended framework involves the evaluation of resources and capabilities along three important dimensions:[34]

1. From the organisational perspective, it evaluates the value (V) to the organisation and the ability of the organisation (O) to exploit the resources and capabilities.
2. From the perspective of competitiveness, it considers the rareness (R) and inimitability (I) and the availability of resources and capabilities to competitors.
3. From the perspective of customers, it evaluates the size of the market and determines whether it is large (L) enough to cover the fixed costs of the organisation. It also evaluates the extent to which resources and capabilities allow the organisation to address unmet (U) customer needs.

The development of capabilities is highly dependent on human beings and their store of knowledge. As Robert Grant explains, organisational capability is a function of knowledge integration.[35] In other words, competitive advantage begins with individual knowledge, but individual knowledge on its own is not worth very much. It is really in the extent to which it is shared, assimilated and transformed that its true value will be realised, and this will ultimately determine the development of capabilities and core competencies. For that reason, this section should be read in conjunction with Chapter 9, which explores the learning organisation, and the individual and organisational learning process.

The big picture

In this chapter, we introduced four key concepts. First, we explored the idea of strategic resources, as the tangible and intangible assets of the organisation. On their own, resources are valuable, but will reduce in value over time. It is only when resources are combined to develop **capabilities** that they become a revenue-generating asset. Unlike resources, capabilities will become more valuable with use and over time, they will lead to the generation and accumulation of more resources.

We also explored the importance of **dynamic capabilities**, those capabilities that allow the organisation to sense opportunities for renewing itself and developing new capabilities.

Core competencies (also known as distinctive capabilities) are the few very important capabilities that the organisation does differently and better than its competitors and provides the organisation with a competitive advantage.

In the resource-based view, history matters, and the more resources an organisation begins with, the more likely it is to succeed and to add to its resources, increasing the foundations of its success. For this reason, it is important for organisations to think about their strengths and weaknesses in terms of resources and capabilities, and to find ways of developing dynamic capabilities.

Summary of learning outcomes

LO 1: Explain the importance of resources, capabilities and core competencies in strategic management.

Resources are the productive assets owned by organisations. Resources are grouped into five primary categories, namely, financial, physical, human, organisational, and technological resources. Resources at the disposal of an organisation can also be tangible or intangible. Capabilities are the capacity of an organisation to deploy resources for a unique result. Core competencies are those capabilities that distinguish an organisation from others in that industry and form the basis of its competitive advantage, strategy and performance.

LO 2: Explain the appraisal of the value of resources and capabilities.

Capabilities and resources have the potential to become core competencies and these core competencies can result in competitive advantage, but only if they meet certain conditions. A resource-based framework for analysis of an organisation can be used to determine the resources and capabilities that will result in core competencies. For resources and capabilities to become core competencies, they should be valuable, rare, inimitable and non-substitutable, and exploitable by the organisation.

LO 3: Explain the resource-based view of internal analysis.

The resource-based view (RBV) model for analysing the internal strengths and weaknesses of the organisation in terms of its resources and linking them to opportunities in the external environment was elucidated. The RBV determines where the organisation can build competitive advantage, superior performance and customer value.

LO 4: Explain the identification of resources, capabilities and core competencies to create value according to the functional area and value chain analysis.

An organisation's resources, capabilities and core competencies are identified, classified and analysed according to its functional areas, or through an analysis of its value chain.

LO 5: Discuss the contribution of resources, capabilities and core competencies towards competitive advantage and sustainable competitive advantage of an organisation.

This learning objective explained how organisations achieve competitive advantage over competitors through differentiation or cost leadership based on their resources, capabilities and core competencies.

LO 6: Explain the importance of capturing the value generated by resources, capabilities and core competencies.

Appropriability or the ability of the organisation to capture sufficient value to justify its investment in developing unique resources and capabilities, to ensure the achievement of competitive advantage, is explained.

Discussion questions

1. Differentiate between resources, capabilities and core competencies of an organisation and explain the importance thereof to strategic management.
2. Distinguish between tangible and intangible resources of an organisation.
3. Explain why it is important for an organisation to ensure that its resources and capabilities become core competencies.
4. Explain the VRIO analysis.
5. Explain the resource-based view of an organisation's internal analysis.
6. Explain the identification of capabilities and core competencies to create value in terms of their functional area analysis.
7. Explain the identification of capabilities and core competencies to create value in terms of the value chain analysis.
8. Identify an example of how organisations gained competitive advantage through a differentiation and cost leadership strategy respectively.
9. Explain, and illustrate with the aid of an example, your understanding of the 'appropriability' of an organisation.
10. Consider the opening case study in this chapter. What are the core competencies of Discovery? How valuable will these core competencies be in the insurance and financial services industry? Substantiate your answer.
11. Read the story on Apple Inc. by Gary Hamel on Management Innovation Exchange (http://www.managementexchange.com/blog/what-makes-apple-apple) and identify the core capabilities of Apple that led to their success.

Learning activities

1. Watch the video on the resource-based view by Jay Barney on YouTube (http://www.youtube.com/watch?v=-KN81_oY11s). What did you learn about the notion of differential resources in this video?
2. Interview a manager in any organisation of your choice about his or her organisation's key strengths and weaknesses. What did you learn about the idea of resources and capabilities in this interview?

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7 Developing and choosing appropriate strategies

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LEARNING OUTCOMES

After reading this chapter, you should be able to:

LO 1: Understand the nature and use of strategic goals and strategic choices in providing strategic direction.

LO 2: Differentiate between various corporate-level strategies that create corporate value and synergy.

LO 3: Discuss the management of the multi-business organisation.

LO 4: Differentiate between the various business-level strategies for creating and sustaining competitive advantage.

LO 5: Explain the evaluation of strategic choices.

KEY WORDS

- Acceptability
- Cooperative strategy
- Cost leadership strategy
- Differentiation strategy
- External growth strategy
- Feasibility
- Internal growth strategy
- Strategic business units
- Suitability
- Turnaround strategy

CHAPTER ORIENTATION

Becoming a leading multi-national group starts with one strategic decision. In the case of Bidvest, it was through buying businesses that others were eager to sell, followed by a process to turn under-performing operations around. On the surface, this process seems quite basic, but success only follows well-considered strategic choices in anticipation or response to market conditions. Good strategic decisions follow a clear strategic direction, insight to the external environment (as explained in Chapter 5), understanding of the organisations' own strengths and weaknesses (as explained in Chapter 6), as well as the ability to anticipate and respond to customers' needs.

This chapter deals with developing and choosing appropriate strategies. First, the nature and use of strategic goals and strategic choices to provide strategic direction to an organisation are explained. Second, we differentiate between the various corporate-level strategies, and follow this with a discussion of the management of multi-business organisations. Third, we differentiate between the various business-level strategic options. Lastly, we explain the evaluation of strategic choices. Figure 7.1 illustrates how to develop and choose appropriate strategies in the context of this book.

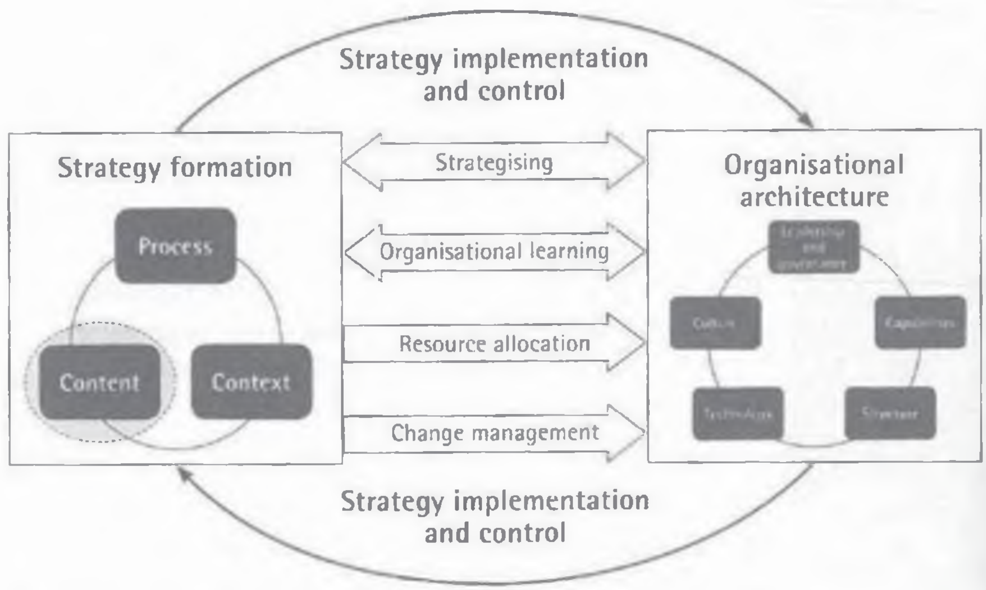

Figure 7.1. *The development and selection of appropriate strategies*

Case study

Bidvest: From humble beginnings to a leading multi-national group[1, 2, 3]

The JSE-listed Bidvest Group is one of the leading corporations in South Africa with a turnover of over R70.1 billion, employing more than 130,000 people.[4] Brian Joffe launched the organisation in 1988. Joffe built the organisation by buying businesses that others were eager to sell. He followed a uniquely empowered business model driven by autonomous entrepreneurs, each responsible for growing their own operations. Following the acquisition by Bidvest, under-performing operations were often transformed into industry leaders. Rather than focus on one market, the group offers a diverse range of products and services across industries. Key corporate strategies, since the inception of the organisation, are listed in Table 7.1:[5]

Table 7.1: *Corporate strategy*

Year	Corporate strategy	Year	Corporate strategy
1988	Start of Bidvest Food Services Acquisition of: • Chipkins • Sea World	2005	Acquisition of: • G Fox
1989	Start of Bidvest Commercial Products Acquisition of: • Afcom Group	2006	Acquisition of: • Deli XL • Top Turf • Execuflora • Versalec Buy the controlling stake in HORECA Trade
1990	Bid Corporation becomes holding company of Bidvest	2007	Acquisition of: • Anglis Rennies Bank became Bidvest Bank
1991	Start of Bidvest Hygiene Services Business and start of Bidvest Business Services Division Acquisition of: • Steiner Services	2008	Viamax acquisition concluded
1992	Acquisition of: • Crown Food Holdings Crown Food Holdings merged with National Spice to establish Crown National	2010	Acquisition of: • Nowaco Group • Purgeau • Bidtrack Bidvest Namibia lists on the Namibian Stock Exchange (Bidvest owns 52%)
1993	Start of Bidvest Freight Acquisition of: • Safcor • Prestige Cleaning Services Prestige Cleaning Services merged with Steiner	2011	Acquisition of: • Seafood Holdings • Nowaco Baltics • Rotolabel
1995	Acquisition of: • Manettas Manettas renamed Bidvest Australia	2012	Acquisition of: • Deli Meals

Year	Corporate strategy	Year	Corporate strategy
1997	Start of Bidvest Office Acquisition of: • Waltons (including the Konica Minolta operations)	2013	Acquisition of: • Home of Living Brands
1999	Acquisition of: • Booker Foodservice • Rennies Group • Lithotech	2014	Acquisition of: • Mvelaserve • Academy Brushware
2000	Acquisition of: • Crean • Island View Storage Banking licence granted to Rennies Bank, to form Bidvest Financial Services	2015	Acquisition of: • DAC (Italy) • PLC Transport 24/7 (UK) • Compendium and Bush Breaks acquisitions concluded.
2001	Acquisition of: • John Lewis Foodservice • mymarket.com, Bidvest's e-commerce initiative launched	2016	Acquisition of: • Plumblink • Glassock Foodservices unbundles to unlock shareholder value
2002	Start of Bidvest Electrical • Remaining 68% of Voltex acquired Acquisition of: • Paragon Paragon merged with Lichotech	2017	Acquisition of: • Brandcorp • Technilamp • Eagle Lightning
2003	The Bidvest Academy, a group training and development programme launched. BEE initiative with Dinatla Investment Holdings announced	2018	Acquisition of: • Noonan
2004	Start of Bidvest Automotive Acquisition of: • Mc Carthy South Africa (South Africa's second-largest motor retailer)		

The Bidvest Group strategy focuses on strategic diversification, across industries and geographies. This strategy creates built-in stability, for example, when the South African economy faces challenges and the Rand comes under pressure, offshore businesses generally provide a strong counterweight. Representation across numerous industries ensures that a degree of growth is achieved overall, even in difficult trading conditions.

The first step that Bidvest follows when implementing the strategy, is to identify an underperforming organisation, to acquire such an organisation and to turn its performance around by the redefinition of the market and expansion into related areas. For example, in 1995, Bidvest acquired Manetta Australia (now Bidvest Australia). In the first two years following the acquisition, Bidvest made a loss of AU$6m. However, after the two years, the company contributed to the organisation's profit. Once an organisation has been acquired, it is followed by the redefinition of the market and expansion into related areas. For example, Walton's, a stationery supplier, created an entry-point into the business retail industry (supplying stationery to businesses). However, the market was widened by adding office furniture and office technology.

The organisation is of the opinion that critical mass enables greater efficiency that drives further growth and helps secure the jobs of employees. In most cases, efficiency results in less wasted resources and further cost advantages due to scaling. Lower costs can either improve margins or enable the organisation to lower selling prices, which in turn could increase market share. Reinvention and a wider vision are critical. For example, the Rennies acquisition created potential for strategic expansion into banking, freight, shipping services and the travel industry. The acquisition of the McCarthy automotive retailing business created a base for financial services such as car financing, leasing and insurance. These services were added to Bidvest Bank (originally Rennies Bank, a bank that specialised in foreign exchange business targeting a niche (specialised) segment.

The creation of critical mass ahead of renewed growth was also evident in 2014 when Bidvest acquired the Mvelaserve group of corporate service businesses. Bidvest was, at the time, of the opinion that the acquisition would enable Mvelaserve to continue its customers more efficiently once it became a subsidiary of Bidvest. Services would be enhanced as Mvelaserve could use products supplied by Bidvest Hygiene Services, thereby bulking up its own services and rental and products. Mvelaserve also benefited from being able to offer its products to the wider customer base of Bidvest. Bidvest simultaneously responded to the growing importance of consumer spending on the economy by purchasing the Home of Living Brands. The Home of Living Brands is a supplier of a wide range of consumer products to major retailers. This acquisition therefore expanded Bidvest's market to enter the retail industry that service consumers. Entry into another important industry that serves consumers was then achieved with the purchase of 35 per cent of the shares in the pharmaceutical organisation, Adcock Ingram.

Bidvest has grown from its humble beginning to a multi-national organisation. During the last 30 years, the company had to consider its own resources and capabilities as well as the opportunities in the external environment to make the best strategic choices. The current portfolio of the organisation is strategically diversified and the result of a number of strategic choices responding to market conditions.

LO 1: Understand the nature and use of strategic goals and strategic choices in providing strategic direction.

7.1 Strategic goals and strategic choices

In Chapter 3, we explained strategic planning as the responsibility of strategists to determine and communicate the strategic direction of the organisation. In Chapter 3, we also highlighted the formulation of the vision, mission and strategic goals that provide an indication of strategic direction. We also considered how value statements can be used to keep the behaviour of all staff members in line with organisational expectations. We established that every organisation is part of a larger system and that interactions within this system are determined by various role-players, referred to as stakeholders, present in the organisation's business environment as well as the composition of the business environment. The first part of any strategy formulation process is thus to assess the current situation. The findings of such an assessment will inform the goals of the organisation with the overall goal of creating a strategic fit between the organisational resources and capabilities (which are explained in Chapter 6) and the opportunities present in the external environment (explained in Chapter 5). We note that strategic goals are statements that express specific outcomes to be achieved. We also acknowledge that goals form the basis of a common language for understanding the wider context as it contains realistic measures of progress and achievement.[6]

These measures of progress are set to support and achieve the strategic direction of the organisation. However, the primary objective of business strategy is to achieve a sustainable competitive advantage that leads to above-average performance and returns. To achieve this objective, managers and key employees need to make decisions on three levels:

1. **Organisational or corporate level.** Decisions are taken about the overall purpose, scope, range and diversity of the organisation. These decisions are typically orchestrated by senior management, such as the Chief Executive Officer (CEO) or Managing Director (MD), the board of directors and other senior executives. The outcome of these decisions is corporate strategies, and the purpose of corporate strategy should be to maximise stakeholder value in the long term by managing a portfolio of businesses.
2. **Business level.** General managers of each line of business or strategic business unit (eg a subsidiary) determine which business (or competitive) strategies would be most suitable to achieving sustainable competitive advantage. These decisions constitute business-level strategies.
3. **Functional level.** Managers lower down make decisions about how to best support business-level strategies by performing strategy-critical activities. These functional strategies include decisions, such as optimal staffing (the responsibility of the HR manager), marketing strategies (the responsibility of the marketing manager) or research and development initiatives.

In this chapter, we focus on corporate and business-level strategies. The corporate centre is typically the head office of a multi-business organisation (see Figure 7.2) and manages a portfolio of businesses with a view to maximising the value of the portfolio for the benefit of stakeholders. The corporate head office will typically add value to strategic business units (SBUs) by means of specific capabilities or shared corporate services. SBUs are organisational units that exercise control over most of the resources they require to be successful (ie they are autonomous). Consider, for example, the Bidvest Group. The group operates through seven SBUs (also referred to as divisions), namely Automotive, Commercial Products, Electrical, Financial Services, Freight, Office and Print and Services. In this case, the corporate centre adds value by 'identifying strategic investment opportunities while promoting experience sharing across SBUs and fostering synergies and savings'. Specific examples of value added to SBUs include:[7]

- access to corporate finance
- Bidvest brand support
- compliance
- executive training, oversight and management of organisation-wide financial management
- investor relations and corporate communications
- risk and sustainability issues
- strategic direction.

Each SBU is required to compete in their respective markets and industries with a view to establishing competitive advantage as a means of creating competitive advantage for their corporate owners.

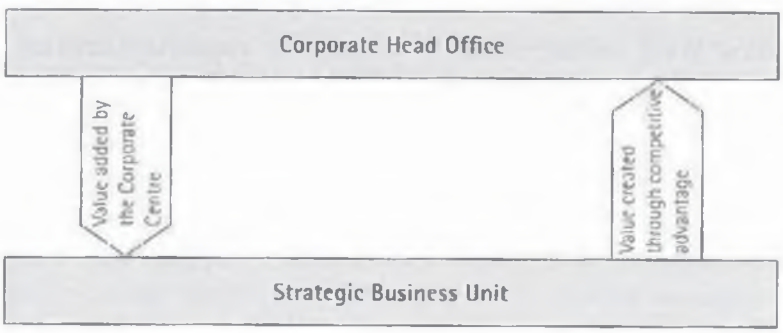

Figure 7.2 *The relationship between the corporate centre and strategic business units*

In this chapter, we will review different corporate and business strategic options that could be implemented to create strategic success based on an organisation's proposed strategic direction, its strengths and weaknesses, as well as the opportunities and threats presented in the environment in which it operates. The complexity of strategic choice lies in the alignment between choices and the realities found in the operating environment. In addition, strategy is developed over time and often involves choices.

LO 2: Differentiate between the various corporate-level strategies that create corporate value and synergy.

7.2 Corporate level strategic options: creating corporate value and synergy

In order to create value for the organisation as a whole, executives need to make decisions about the growth path of the organisation. On a corporate level, executives on the highest level need to make decisions about the overall purpose, scope, range and diversity of the organisation. In short, the corporate-level strategies deal with the number of products and services that the organisation will offer and the markets which will be pursued.

In the case study on The Bidvest Group, we see how the organisation grew from its humble beginning in 1988 to become a leading multi-national organisation. The Bidvest Group strategy is based on strategic diversification, across industries and geographies. Note how this position was built over three decades as a result of a number of strategic decisions.

Whether an organisation operates as a multi-business or not, organisations have the option to pursue any, or a combination of, corporate strategies. We can broadly classify these strategies into the following categories:

- Internal growth strategies
- External growth strategies
- Co-operative or corporate combination strategies
- Turnaround and exit strategies.

Each of these broad categories can be achieved by employing different strategic options. The choice of the most appropriate strategy is dependent on the strategic fit between the organisation's internal strengths, capabilities and resources, and the opportunities available and threats facing the organisation in the external environment. Table 7.2 provides a summary of the corporate strategic options that will be discussed in this chapter.

Table 7.2 *Corporate level strategic options*

Internal growth strategies	External growth strategies	Co-operative or corporate combination strategies	Turn around and exit strategies
• Market penetration • Market development • Product development • Innovation	• Diversification (related or unrelated) • Inegration (horizontal or vertical)	• Strategic alliance • Joint venture • Merger • Acquisition	• Retrenchment • Recovery • Revenue growth • Divestiture • Liquidation

7.2.1 Internal growth strategies

Often the least risky option for organisations is to grow from within. This type of strategy aims to leverage the organisation's current range of products (or services) and the markets it serves and propose growth strategies that combine new and/or existing products and markets. Depending on whether products and markets are new or not, four internal growth strategies are possible, namely, market penetration, market development, product development and innovation.

We will use Woolworths Holdings Limited (WHL) as an example to illustrate how it successfully employed each of these strategies. WHL is one of the top 40 companies listed on the JSE Limited Securities Exchange (JSE). The organisation opened its first Woolworths clothing store in Adderley Street in Cape Town more than 80 years ago. Today the organisation is a leading retail group with operations across the southern hemisphere.[8]

Market penetration strategies

Market penetration strategies aim to increase market share by selling more of the organisation's existing products and/or services to its existing markets. One of the strategic focus areas of Woolworth's, for example, is to 'build stronger and more profitable customer relationships'.

To achieve this objective, the organisation relies on customer insights and data obtained through the WRewards loyalty programme to inform business decisions. At present, approximately 75 per cent of the 3.3 million Woolworths[9] customers participate in this programme, which enables the organisation to track customer-spending patterns. In turn, customers earn rewards based on a tiered system determined by their annual spend at the retailer. In order to participate in and benefit from this programme, customers need to accept marketing material. This offers the organisation the opportunity to direct carefully selected promotions to market segments based on customer history. In addition, customers are encouraged to apply for a Woolworths Store Card or Credit Card. This allows them to buy on credit and enjoy an additional 5 per cent savings. The organisation realised that through effective database marketing campaigns, they can successfully increase spend per customer.[10]

Market development strategies

The aim of market development strategies is to grow turnover by selling the organisation's existing products and/or services into new markets. For example, Woolworths expanded its footprint in areas where it had a low density of stores, or no stores, by opening stores at petrol station forecourts. This strategy is so successful that the organisation now trades out of 72 Engen petrol forecourts selling food products across South Africa.[11]

Product development strategies

The aim of product development strategies is to grow turnover by selling new products or services to the organisation's existing market. Moving beyond retailing of quality food and fashion, Woolworths Financial Services was launched in 1993 in order to provide Woolworths' customers with an in-store card and access to credit facilities. Over the years, its product range has grown and today it offers a suite of financial products, including in-store credit, credit cards, personal loans and a range of insurance products.

Innovation strategies

The aim of innovation strategies is to introduce advancements in technology and/or services. These advancements are developed through research and development. Woolworths products and services are continuously advanced to create superior value. Consider, for example, Woolworths school shirts. These shirts have built-in ultra-violet protection and block out more than 98 per cent of harmful ultraviolet rays.[12]

As can be observed from the Woolworths example, choices made on the basis of products and markets have successfully contributed to the organisation achieving its growth objectives. Read more about the organisation's growth objectives in the practising strategy box below.

Practising strategy: Insight into Woolworths strategic focus[13]

According to Ian Moir, Woolworth's CEO, the future of retailers lies in the creation of amazing experiences for consumers and the combination of food and fashion. Retailers need to consider changing consumer behaviour and face the possibilities offered through online platforms. Moir says customers want to interact differently with retailers and want more personalised services.[14]

Woolworths has six strategic focus areas that are driven at a group level. This organisation understands that their long-term success depends on their ability to use their resources to implement the group's strategy. Table 7.3 reviews the performance indicators against various targets of Woolworths South Africa. The first column lists the six strategic focus areas of Woolworths South Africa. The second column lists the performance measures used to evaluate the performance of each strategic focus. Finally, the third column reports the actual performance of Woolworths South Africa as reported in the WHS 2017 integrated report. These targets revolve around improved customer relationships, an increase in online sales of the organisation, an increase in sales as a leading fashion designer, an increase in food sales, improved synergies within the organisation and the organisation's targets in terms of sustainability. Specifically, note that each organisation determines its own performance measures in line with the organisational objectives. These objectives should include clear targets, as well as timelines in which the targets should be achieved. It is beyond the scope of this chapter to review performance measures and the measures listed below merely illustrate how Woolworths measures the performance of each strategic area.

Table 7.3 *Targets of Woolworths South Africa*

Strategic focus area	Performance measures	2016/7 Performance
Customer relationships	Number of active customers	3.3m
	% revenue tracked on loyalty cards	75%
Connected retail	Growth in online sales	33.1%
	% online sales	0.7%
	Net new space	3.8%
Leading fashion designer	Sales	R13.9bn
	Comparable sales growth	(1.1%)
	Gross profit margin	47.9%
	Return on sales %	15.6%
	Customer perceptions of fashion and quality	Improved
Big food business	Sales	R27.7bn
	Comparable sales growth	4.6%
	Gross profit margin	25.1%
	Return on sales %	7.3%
	Market share	Increased
	Customer perceptions on price	Improved
Drive synergies	Cost to sell %	22.7%
Embed good business journey	% targets achieved on sustainability scorecards	85%

7.2.2 External growth strategies

Some organisations choose to grow by adding new businesses to their current portfolio, which is referred to as external growth strategies. These strategies create diversification by means of new products or markets or integration when organisations acquire an organisation similar to the current business.[15] Strategic options to achieve external growth can be broadly classified as diversification and integration.

Diversification strategies

Diversification strategies are driven by two key objectives, namely, growth and risk reduction. However, diversification that only seeks growth or risk reduction is likely to destroy value. Conversely, if these objectives are supplemented by an intention to exploit economies of scope (in cases where it is cheaper to manufacture a variety of products together, rather than separately) in resources and capabilities, it has the potential to create stakeholder value.[16] Once an organisation decides to diversify, it faces the choice of whether to diversify into related or unrelated businesses.

Businesses are said to be related when there is a close resemblance between how they perform key value chain activities. Pursuing this strategic option allows the organisation to build stakeholder value by leveraging synergies between the two organisations, enabling the organisation to perform better as a whole than just the sum of its individual businesses.[17] An example of an organisation that employed this strategy successfully is VJO Attorneys. This boutique South African legal firm expanded their legal services and conveyance practice in 2011 to include a debt counselling practice, taking advantage of the opportunities created by the downturn in the economy.[18] Debt counselling requires a strong legal background and there were many synergies between the resources and capabilities required by both the legal practice and debt counselling practice.

An unrelated diversification strategy discounts the merits of pursuing a cross-business strategic fit. Instead, it focuses on entering and operating businesses in industries with opportunities to realise consistently good financial results.[19] An example of an organisation that achieved growth through unrelated diversification is the Bidvest Group, as illustrated in the case study. Today the group operates in the areas of consumer and industrial products, electrical products, financial services, freight management, office and print solutions, outsourced hard and soft services, travel and aviation services and automotive retailing.[20]

Integration strategies

Organisations often acquire other organisations similar to their own. The operative word here is *similar*, meaning that the operations of these organisations are incorporated within the current operations of organisations pursuing this strategic option. These organisations aim to achieve growth through acquisitions of and/or mergers with competitors (horizontal integration) or suppliers or distributors (vertical integration).[21] Mergers and acquisitions are discussed in more detail below.

7.2.3 Co-operative or corporate combination strategies

Co-operative or corporate combination strategies allow different organisations to form partnerships to share resources, capabilities or technical know-how (ie to 'combine') to build a competitive advantage.[22] We will briefly review four popular strategic options in this category, namely, strategic alliances, joint ventures, acquisitions and mergers.

Strategic alliance strategies

A strategic alliance is a formal agreement between two or more separate organisations in which they agree to work collaboratively toward some strategically relevant goal.[23] Such agreements typically entail organisations sharing financial responsibilities and require joint contributions of capabilities and resources. Furthermore, organisations entering these agreements, share risks and control. The duration of such agreements is determined by the desired outcome thereof. Some agreements may include long-term arrangements while others are designed to accomplish short-term objectives. In these agreements, there is no formal ownership, but the relationship is guided by contractual arrangements.[24] An accepted practice in the aviation industry, for example, is code-share agreements, where two or more airlines share the same flight. A seat can be purchased on one airline, but is actually operated by a co-operative airline under a different flight number. This agreement allows greater access to more destinations through a given airline's network without having to offer extra flights. It also makes connections simpler by allowing single bookings across multiple planes.[25]

Joint venture strategies

When a strategic alliance involves ownership ties, it is called a joint venture. In this agreement, a new corporate entity is formed and is jointly owned by two or more companies that agree to share in the revenues, expenses and control of the newly formed entity.[26] In 2013, South Africa's Imperial Logistics announced that they entered into a joint venture with international advisory and procurement firm, The Beijing Axis. The partnership enabled Imperial to improve its international supply chain management in Asia, and its clients to benefit from increasing trade between Africa and Asia.[27]

Acquisition strategies

An acquisition occurs when one entity targets and buys another to become the sole owner of both. Consider the Noonan acquisition reported on in the opening case study. Bidvest bought Noonan in 2018 for approximately R2.7 billion ($208 million). Noonan is a leading provider of strategic outsourcing and operates in the United Kingdom and Ireland. Noonan design and deliver services and solutions for many of the world's largest and most prestigious organisations and are highly experienced in delivering large and complex facilities management outsourcing projects. They are recognised experts in first-generation outsourcing and provision of services to quality critical environments and sectors with unique challenges. Examples of areas in which they operate are life sciences, retail, healthcare, education and police and justice. This acquisition supported Bidvest's overall growth strategy and the purchase allowed the organisation to diversify geographically. According to the CEO of Bidvest, Lindsay Ralphs, Noonan's business model complements Bidvest and the acquisition helps the organisation to improve its services, increase its client base, and support international growth.[28]

Merger strategies

A merger occurs when two separate entities combine forces to create a new organisation. An example of a merger was when two medium-sized South African audit, tax and financial and legal advisory service organisations merged in 2018. BDO South Africa merged with the Cape Town and Port Elizabeth offices of Grant Thornton. Both these offices then operated under the BDO brand. The merged organisation benefits from a scale-up of professional services and can now offer the full spectrum of professional services, including audit, company secretarial, business services and advisory services, corporate finance, cyber lab, economic incentives, and HR advisory service, internal audit and forensics services, legal services, risk advisory, tax, tech advisory, and wealth advisory services. The merger furthermore allowed the organisation to leverage the opportunities created by the changes in the auditing profession, including the introduction of mandatory audit firm rotation. BDO is now in a far stronger position to take advantage of opportunities in the market and to provide the market with a significant alternative to competition.[29]

7.2.4 Turnaround and exit strategies

Operational realities and fierce competition often result in companies performing poorly over an extended time. These organisations are not in a position to grow and for them, survival becomes the core objective. In order to affect a turnaround, executives need to acknowledge problems and consider strategic options that could yield immediate returns. Unfortunately, sometimes there is no other option than to cut losses and exit the industry.

In this section, we will review a few strategic options available to organisations facing this scenario. The practising strategy box on South African Airways' turnaround strategy below reviews key considerations for the new CEO to turnaround the performance of the national carrier.

Practising strategy: South African Airlines: We live in hope[30, 31]

On August 2017, South African Airways (SAA) appointed yet another CEO, Vuyani Jarana, whose responsibility it was to attempt implementing the organisation's ninth turnaround strategy in a little over a decade, inheriting a massive debt and maturing loans of almost R20bn over the next five years. In August 2019, Jarana resigned and SAA will need new leadership again.

Key considerations for the new CEO include the following:

1. **Implement staff reductions.** An audit needs to be conducted on the entire staff complement and benchmarks be done to determine the worker/aircraft personnel ratio. International best practice reported a ratio between 120 and 140 employees per aircraft. The current SAA ratio is 190 employees per aircraft, which is approximately 46 per cent higher than the average. To be competitive, it would require SAA to retrench 3,000 employees, but this might not be realistic from a political standpoint.
2. **Update fleet.** SAA's fleet does not match that of international competitors. The procurement of new aircraft seemed to be done without any larger strategy. For example, the five new A330-300 aircraft acquired, have a range of 6,350 nautical miles, which can limit their usage in key European or Asian markets. The fleet of older Airbus aircraft was known for high fuel consumption. If SAA wants to compete internationally in terms of cost efficiency in a comfort-driven long-haul market, they need to consider updating their fleet with the prevailing best sellers of the A350-900 or B787 variant. This would, however, require huge capital investments.
3. **Servicing sensible routes.** SAA faces a chicken and egg situation when it comes to routes. To service routes, airlines compete on extremely tight margins and often uncontrollable extraneous factors. SAA will require the right equipment and rigorous internal controls to contain operational costs. It would help if SAA operated a lean and profitable route network and entered into code-sharing partnerships to cover destinations that it could not be serve profitably previously. Over the longer term, a more city-to-city direct approach to connectivity needs to be established.
4. **Implementing international services from Cape Town.** Cape Town is one of South Africa's main tourism destinations and is considered an important business hub, with a population of 4 million. Therefore, Cape Town should be regarded as a core component of the airline's global route network.

5. **Liaison more efficiently with South African tourism.** As the South African national airline, SAA should partner with South African Tourism, the country's national tourism board. The partners could then work together to develop travel packages to popular South African tourist destinations.
6. **Providing some extras.** Many airlines allow greater weight allowances for travellers and SAA needs to consider providing travellers with some extras that would distinguish them from their rivals.
7. **Improving service levels.** SAA needs to develop a commitment to outstanding service. Given the intensity of international rivals, any turnaround strategy could fail (again) as a result of lacklustre or uninspiring service. When evaluating services, customer satisfaction surveys should be complemented with staff morale surveys to determine the relationship between staff morale and customer satisfaction.
8. **De-politicising the airline.** An independent assessment of all business linkages needs to be established to rid the airline of the bad habits of graft and patronage. The 2015 Ernst & Young forensic investigation into 48 tenders at SAA indicated that 28 of these did not comply with tender requirements.

At the time of writing this chapter, the public and media were speculating whether South Africa could really afford a national carrier, or whether some degree of part-privatisation is necessary. This follows the request from the airline for yet another cash injection by the Finance Minister to keep the airline flying by providing salaries and urgent debt repayment. The nation lives in hope that SAA will stabilise.

In the shorter term, the most successful turnaround strategies focus on reducing direct operational costs and improving productivity gains. Three strategic options that can be used to achieve these objectives are retrenchment, recovery and revenue growth.

Retrenchment strategies

Retrenchment strategies are typically used to reduce the size or diversity (in terms of the number of product offerings or strategic business units) of the organisation. This strategy takes two forms, namely, cost-cutting and reducing non-core assets. In the SAA example above, overwhelming evidence suggests that a combination of systematic weaknesses are the result of a lack of internal control. Suggestions are, for example, that the SAA board approved wasteful and irregular expenditure. Cost-cutting will only incur when internal controls are in place to ensure operational efficiency, reliable financial reporting and compliance with laws and regulations. Cost-cutting would also result if staff are reduced in line with international best practice and if mechanisms are put in place to ensure optimum performance.[32]

Recovery strategies

Recovery strategies are used to stabilise the business. This strategy is often employed in response to externally induced problems and a recovery strategy aims to introduce new entrepreneurial blood in the form of turnaround specialists or a new leadership team. The appointment of Mr Vuyani Jarana on 1 November 2017 as new CEO of SAA was part of the recovery strategy of the airline. Following his resignation, it needs a new recovery strategy.

Revenue growth strategies

Revenue growth strategies aim to grow sales in various ways, for example, decreasing selling prices, increasing promotions, implementing product modifications, appointing more sales staff and improving customer service.

Divestiture strategies

Turnaround can also be achieved through divestiture. A divestiture is the partial or full disposal of assets or SBUs through sale, exchange or closure. Divestiture results from a management decision to cease operations in a particular area because it is no longer part of a core competency or when it is no longer profitable.[33] SAA, for example, should reconsider its current routes, suspend some routes, and minimise loss-making international networks.

Liquidation strategies

If none of the options above (retrenchment, recovery, revenue growth or divestiture strategies) are viable, the organisation would have no other choice but to exit the industry. In order to exit, executives may sell the organisation, liquidate the organisation or declare bankruptcy.[34] A liquidation strategy implies that the entire organisation be sold-off, either as a whole or in parts of it. Liquidation can be voluntary or, in the case of bankruptcy (where the organisation can no longer pay its debts), can be directed by the court.

In summary, this section provided an overview of the various options for corporate-level strategies. In the following section, our attention shifts to the management of the multi-business organisation.

LO 3: Discuss the management of the multi-business organisation

7.3 Managing the multi-business organisation

Managing a sometimes diverse group of business units in an organisation, requires action that is tailored to the circumstances confronting each business unit with due consideration to the resultant impact on the entire organisation. A useful management tool to provide a snapshot view of an organisation's investments is two-dimensional matrices. Executives can use various adaptations of well-established portfolio matrices, such as the Boston Consulting Group (BCG) matrix, the directional policy matrix (General Electric-McKinsey matrix), the SPACE or the parenting matrix.[35] For purposes of this chapter, we will focus on the directional policy matrix as illustrated in Figure 7.3.

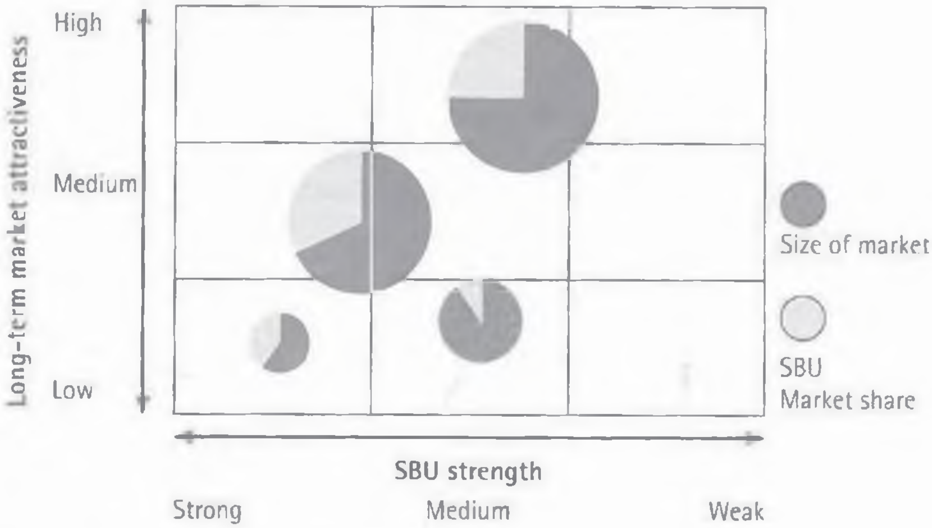

Figure 7.3 *Directional policy matrix*[36]

The directional policy matrix positions the various strategic business units (SBUs) of an organisation according to (1) the long-term attractiveness of the relevant market in which they operate, ranging from low to high (depicted on the vertical axis of this matrix), and (2) the competitive strength of the SBU in the market, ranging from strong to weak (depicted on the horizontal axis of the matrix). The matrix further allows analysts to illustrate the relative size of the market, as well as the market share of the SBU. In Figure 7.3, the size of the market is indicated in blue, whereas the market share is indicated in grey. This snapshot serves to inform portfolio strategies to guide corporate decision-making in terms of financial investment and divestment. Investment would be appropriate in instances in which the market is attractive and the SBU displays a relative strength in that industry. Divestment would be considered in unattractive markets where the SBU display a competitive weakness. If we look at Figure 7.3, the smallest circle indicates a strong SBU in terms of market share, but the long-term market attractiveness is very low. The biggest circle indicted in Figure 7.3 indicates an SBU with a medium to weak market share, with high long-term market attractiveness. The organisation might decide to rather invest most of its resources indicated in the SBU with the biggest market share, with medium long-term market attractiveness. These decisions also need to consider the organisation's strategic direction, potential for growth elsewhere and possible synergies among SBUs.

With this in mind, it is clear that matrices such as these, only provide a simplistic view and should be supported by sound business intelligence. Each matrix gives more or less attention to one of three criteria:[37]

- the balance of the portfolio, for example, in relation to its markets and the needs of the organisation
- the attractiveness of the business units in terms of their individual competitive positioning and how profitable their markets or industries are likely to be in future
- the 'fit' that the business units have with one another in terms of potential synergies or the extent to which the corporate parent will be good at managing them and assisting them in creating value in the corporate portfolio.

An understanding of where the organisation want to go should be followed by an agreement on how to compete in order to get there. The next section focuses on the various business-level strategic options.

LO 4:	Differentiate between the various business-level strategies for creating and sustaining competitive advantage.

7.4 Business-level strategic options: creating and sustaining competitive advantage

Corporate-level strategies essentially deal with the number of products and services that the organisation will offer and the markets which they will pursue. Business-level, or competitive, strategies consider how to compete successfully in these markets. In other words, these strategies focus on how to position an organisation within an industry in such a way that it has competitive advantage.

There are many variations in business-level strategies, but if we strip away the details to get to the real substance, the biggest and most significant differences among competitive strategies are reduced to the following:

- whether an organisation's target market is broad or narrow
- whether the organisation is pursuing a competitive advantage linked to low cost or product differentiation
- a combination of the above.[38]

When you ask customers why they buy a specific product or service, they will tell you that it is because the product is cheaper than, different from or provides a better value proposition than alternative competing choices. Although these are broad generalisations, important implications which represent the generic strategic options for achieving competitive advantage flow from them. Four distinct generic competitive strategy approaches stand out:[39, 40]

Cost leadership strategies

A cost leadership strategy involves becoming the lowest cost organisation (with regard to production cost) in a domain of activity by a significant margin. This strategy will typically target a broad spectrum of buyers. It is important to note that cost leadership does not necessarily imply low price – in fact, having low production costs and a low price will result in average returns and no real competitive advantage.

Differentiation strategies

A differentiation strategy involves uniqueness along some dimension that is sufficiently valued by customers to allow a price premium. This strategy may focus on either a broad section of buyers or a narrow buyer segment.

Focus strategies

A focus strategy involves targeting a narrow segment or domain of activity and tailoring its products or services to the needs of that specific segment, to the exclusion of others.

Best cost provider strategies

A best cost provider strategy is a hybrid strategy that involves giving customers more value for their money by offering upscale product attributes at a lower production cost than rivals.

Each of these four generic competitive approaches stakes out a different market position, as illustrated in Figure 7.4.

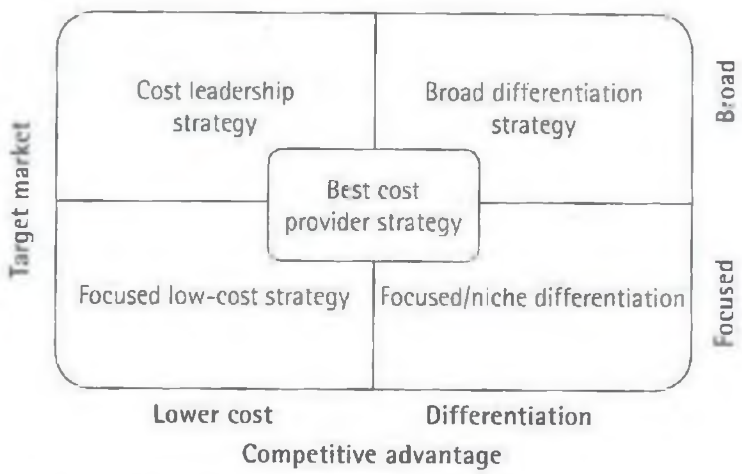

Figure 7.4 *Business-level strategies*[41]

Figure 7.4 illustrates that the type of business-level strategy is determined by two factors. The first factor is the type of competitive advantage offered by the organisation (either lower cost, differentiation, or a combination of lower cost and differentiation), which is depicted on the horizontal axis of Figure 7.4. The second factor is the target market pursued by the organisation (either broad or focused), which is depicted on the vertical axis of Figure 7.4. A best cost provider strategy is depicted in the middle of Figure 7.4 – indicating a strategy positioned between the extremes of a lower cost and differentiation on the horizontal axis and between the extremes of a broad and focused strategy on the vertical axis. These strategies relate to the organisation's deliberate decisions on how to meet its customers' needs, how to counter the competitive efforts of its rivals, how to cope with the existing market conditions and how to sustain or build its competitive advantage. Some companies choose to focus their strategic efforts to build leadership in one type of competitive advantage. A good example of such an organisation is PEP Stores which is known for overall cost leadership in all the product categories they offer. Other companies, such as Unilever, aim to serve several market segments by offering different products to different markets. Consider the information in the practising strategy box that follows, which is based on Unilever's position strategies and then reflect on the different business-level strategies employed by this organisation in the washing powder product range.

Practising strategy: Unilever: Position strategies

Brand	Positioning[42]
Skip Competitive strategy: broad differentiation strategy Price:* R64.99 Weight: 1 kg Product: SKIP Auto Regular Autowashing Powder * Price obtained from Pick 'n Pay Online on 6 August 2019	We at SKIP believe that you get the cleanest wash with our product through technology that makes the laundry process simpler and faster for you. SKIP washing powder was the first automatic washing powder in South Africa. It was launched in the 1960s – when the first washing machines were introduced in South Africa. SKIP is the leading garment care expert and as such, consumers have not only come to trust SKIP and be loyal consumers, they also expect SKIP to continually offer them the most up-to-date, technologically advanced products on the market, to care for their clothes. SKIP is a premium brand with a premium offering. Not only does SKIP offer cleaning power, but it also specialises in caring for clothes. SKIP is the technology expert that prides itself on its ability to help clothes last longer.

Brand	Positioning[43]
OMO **Competitive strategy: best cost provider strategy** **Price:* R69.99** Weight: 3 kg Product: OMO Multi-active Flexi Washing Powder * Price obtained from Pick 'n Pay Online on 6 August 2019	Remember when you were a child? How you were free to explore, returning home covered in dirt and other stains that you wore like the badges of an intrepid discoverer? 'Dirt is good!' More significantly, the idea that dirt is good isn't simply a catchphrase for OMO. It lies at the core of our brand, supported by patent-protected technology that gives your kids the freedom to get dirty, safe in the knowledge that OMO will remove those awkward stains. Omo's superior formulation offers South Africa's best-ever stain removal, which cleans deep inside pockets, where kids often store their little discoveries. To ensure that everyone, everywhere, can share in this initiative, we're investing heavily in developing a range of products that suits the pockets of all income groups.
Brand	**Positioning[44]**
Surf **Competitive strategy: overall low-cost provider strategy** **Price:* R37.99** Weight: 2 kg Product: Surf Regular Washing Powder * Price obtained from Pick 'n Pay Online on 6 August 2019	Surf washing powder is known for its super whitening power. Surf washing powder is one of the oldest washing powders on the market in South Africa. It was launched in 1959. Surf washing powder is known for its super whitening power. It has been used and trusted by many people over the years, because of its reputation for maintaining the whiteness of white garments. Surf is a handwashing powder. Because of high foaming, it is not suitable for washing machines – twin tubs, top loaders and front loaders.

Although consolidated market positions are achieved over time, organisations often need to review different strategic choices more frequently. Once an organisation has selected potential business-level strategies, it needs to evaluate these options to choose the most appropriate business-level strategy or combination of strategies. The next section focuses on the evaluation of strategic choices.

LO 5: Explain the evaluation of strategic choices.

7.5 Evaluating strategic choices

Strategies can be evaluated against three key evaluation criteria, namely, suitability, acceptability and feasibility. *Suitability* considers whether the proposed strategies address the key issues related to the strengths, weaknesses, opportunities and threats the organisation faces. Suitable strategies need to take advantage of external opportunities and internal strengths while, at the same time, overcoming external threats and internal weaknesses. In order to identify whether a strategy is suitable, the strategist should have a good understanding of the internal environment of the organisation (the focus of Chapter 6), as well as of the external environment (the focus of Chapter 5), in which the organisation operates. In practice, it often happens that more than one strategy may be suitable, but that limited resources necessitate the screening of options so that the most appropriate strategy can be selected.

Strategies are acceptable if their expected performance outcomes meet the expectations of all stakeholders. Since the *acceptability* of a strategy option is determined by expected performance outcomes, this criterion requires strategists to consider risk, return and stakeholder reaction. We find that organisations, regardless of the industry in which they operate, mostly engage in formal risk assessment if strategic options require substantial investments. Tools such as sensitivity analysis, financial ratios, and break-even analysis are useful to evaluate risks. These aspects are dealt with in Chapter 14. The second consideration is return, which refers to the financial benefits which stakeholders are expected to receive from a strategy. To assess return, strategists can use different measurements such as financial analysis, shareholder value analysis, cost-benefit evaluations and the real option approach. To assess the final consideration, which is the reaction of stakeholders, strategists can make use of stakeholder mapping.

Finally, a strategy is feasible when the organisation has, or can obtain, the capabilities required to deliver a strategy. To assess *feasibility*, strategists need to address two key questions:

1. Do the resources and competencies currently exist to implement a strategy effectively?
2. If not, can they be obtained?

The answers should be informed by considering financial and human resource requirements, as well as resource integration.[45]

Although the criteria seem to be quite straight forward, the reality is that each criterion can only be assessed if key strategic issues dealing with it are identified by means of a comprehensive internal and external environmental analysis.

The big picture

Choosing appropriate strategies is not possible unless they are aligned with organisational resources and capabilities and the opportunities available in the external environment. As a result, strategy selection is a dynamic process that is subject to change. We need to realise that there is not a 'one size fits all' option. Organisations are different in terms of their overall purpose, scope, range and diversity of products and/or services, as well as in terms of the markets they serve. On a corporate level, portfolios need to be managed in such a way that the corporate parent creates value for the SBUs. Each SBU needs to be positioned within an industry in which it has a competitive advantage (see Figure 7.5). There are various strategic options available to companies to achieve this, but each organisation has unique needs and the application of options will differ accordingly. Finally, strategic options need to be evaluated to determine their suitability, acceptability and feasibility. The outcome of this evaluation will indicate whether the strategy selected has a strategic fit within the operating environment.

Corporate level strategy

How do we create value and synergy for the organisation as a whole?

- Internal growth strategies
- External growth strategies
- Co-operative or corporate combination strategies
- Turnaround and exit strategies

Business-level strategy

How do we create competitive advantage in each strategic business unit?

- Overall cost leadership
- Differentiation
- Focus
- Combination strategies

Figure 7.5 *Corporate- and business-level strategy*

Summary of learning outcomes

LO 1: Understand the nature and use of strategic goals and strategic choices to provide strategic direction.

Strategic goals are statements that express specific outcomes to be achieved. These goals are set to support and achieve the strategic direction of the organisation. To achieve strategic goals, managers and key employees need to make strategic choices on three levels. First, decisions are taken about the overall purpose, scope, range and diversity of the organisation. The outcome of these choices is corporate strategies that aim to maximise stakeholder value in the long term by managing a portfolio of businesses. Second, decisions are taken about how to differentiate each strategic business unit. The outcome of these choices is business-level strategies that determine competitive advantage. Third, decisions are required on a functional level about how to best support business-level strategies by performing strategy-critical activities.

LO 2: Differentiate between the various corporate-level strategies that create corporate value and synergy.

Corporate-level strategies determine the overall purpose, scope, range and diversity of the organisation. In this chapter, we discussed internal growth strategies, external growth strategies, corporate combination strategies, turnaround and exit strategies. We also reviewed strategic options that can be followed in support of the strategy types listed above.

LO 3: Discuss the management of the multi-business organisation.

To manage multi-business organisations, strategic decisions should be tailored to the circumstances confronting each business unit, with due consideration to the resultant impact on the entire organisation. In this chapter, we propose that executives would benefit from depicting SBUs on portfolio matrices to get a snapshot of the entire organisation. This snapshot would then serve to inform portfolio strategies to guide corporate decision-making with regards to financial investment and divestment. These decisions also need to take into consideration the organisation's strategic direction, potential for growth elsewhere, and possible synergies among SBUs. Matrices should further be supported by sound business intelligence.

LO 4: Differentiate between the various business-level strategies for creating and sustaining competitive advantage.

Business-level strategies take into consideration to compete successfully in these markets. In this chapter, we reviewed four different strategic options, namely, cost leadership, differentiation, focused and best cost provider strategies.

LO 5: Explain the evaluation of strategic choices.

Strategies can be evaluated against three key evaluation criteria, namely, suitability, acceptability and feasibility. *Suitability* considers strategic fit between the organisation's capabilities and resources and the opportunities present in the external environment. Strategies are acceptable if the expected performance outcome of the strategy meets the expectation of all stakeholders. Finally, a strategy is feasible when the organisation has, or can obtain, the capabilities required to deliver a strategy.

Discussion questions

1. Distinguish between corporate- and business-level strategies.
2. Explain why the Bidvest Group followed a successful diversification strategy. Substantiate your answer.
3. Explain how an organisation can build a competitive advantage.

4. Discuss three strategic options that companies can employ to grow from within.
5. Evaluate South African Airlines' turnaround strategy.

Learning activities

1. Watch the interview with Michael Porter on YouTube (http://www.youtube.com/watch?v=mYF2_FBCvXw) on the five competitive forces. How do these forces shape strategy?
2. Read the article available on http://www.whatifyourstrategy.com/wp-content/uploads/ 2008/08/with-all-this-intelligence1.pdf. What are the implications, in your view, for strategists?

Endnotes

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